UDO UDOMA & BELO-OSAGIE

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BALANCING FX LIQUIDITY WITH SUSTAINABILITY: HOW NIGERIA'S CASH POOLING POLICIES ARE SHAPING ITS PETROLEUM INDUSTRY

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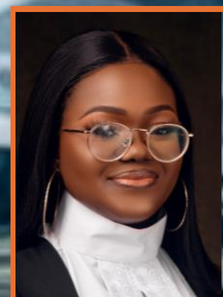
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Overview

In H1 2024, through a series of circulars issued on February 14th, May 6th, and May 31st, the Central Bank of Nigeria (CBN) introduced significant cash pooling policies affecting International Oil Companies (IOCs) operating in Nigeria's upstream petroleum sector.

Cash pooling, a common financial arrangement used by IOCs, centralises the management of bank accounts by consolidating the daily assets and liabilities of group subsidiaries. The parent company allocates liquidity according to each subsidiary's needs, resulting in automatic inter-company loans. This system optimises the group's overall financial position by maintaining a unified balance managed by a designated cash pooling bank. Subsidiaries with excess cash can lend to those in need through centralised accounts, providing benefits such as optimised liquidity, reduced financing costs, improved risk management, enhanced strategic planning, streamlined financial operations, and mitigation of currency risk.

Initially, the CBN's February 2024 circular restricted IOCs to repatriating only 50% of their export proceeds immediately, with the balance available after 90 days, with the balance available for repatriation after 90 days. Following feedback from stakeholders and to improve liquidity in the domestic FX market, the CBN adjusted its measures in May 2024. The 50% balance of export proceeds required to be held within Nigeria for a 90-day period IOCs may be used to settle eligible financial obligations in Nigeria at any time during the retention period.

These changes aim to balance liquidity needs and operational flexibility for IOCs. The CBN emphasises that these measures are designed to stabilise the Nigerian Naira and improve foreign currency availability. Retaining a portion of the export proceeds locally is expected to increase local investments and economic activity, particularly in infrastructure and local services.

The Regulatory Framework

In addition to the 2024 Circulars, Nigeria's regulatory landscape for cash pooling is principally shaped by the CBN Foreign Exchange Manual, the Pre-Shipment Inspection of Export Act, and the Nigerian Oil and Gas Industry Content Development Act 2010 (Local Content Act). This framework aims to enhance the availability of foreign exchange (FX) and to regulate the inflow and utilisation of export proceeds from the petroleum sector.

The CBN mandates that exporters, particularly those dealing in petroleum products, must open and maintain foreign currency domiciliary accounts in Nigeria. According to Memorandum 10 of the CBN Foreign Exchange Manual and Section 10 of the Pre-Shipment Inspection of Export Act, all export proceeds must be deposited into these domiciliary accounts. This ensures that export proceeds are fully accounted for within the Nigerian banking system, thereby enhancing the availability and liquidity of foreign exchange.

In addition, the CBN's guidelines for cash pooling require its prior approval for the repatriation of funds under a cash pooling agreement. Entities must provide evidence of such agreements, submit detailed statements of expenditures, and demonstrate the sources of FX inflows. These measures facilitate effective management of FX resources while maintaining oversight and control over cross-border financial transactions.

Notably, since 2010, Section 52 of the Local Content Act has required operators, contractors, and sub-contractors in the petroleum industry to maintain bank accounts in Nigeria, retaining at least 10% of total revenues from local operations. For industry stakeholders, especially IOCs, understanding and adapting to the new cash pooling policies, alongside the existing Section 52 requirements, necessitates a strategic approach to financial management, compliance, and investment. This approach optimises the benefits of cash pooling while ensuring adherence to regulatory requirements.

2024 Regulatory Timeline

- **Before February 14, 2024**:

  Multinational oil companies could repatriate all proceeds from crude oil exports to offshore parent accounts, subject to the 10% retention requirements of section 52 of the Local Content Act.

- **February 14, 2024 (Circular TED/FEM/PUB/FPC/001/004)**:

  CBN limited the transfer to parent companies' offshore accounts to 50% of export proceeds initially, with the remaining 50% eligible for repatriation after 90 days.

- **May 6, 2024 (Circular TED/FEM/PUB/FPC/001/005)**:

  Allowed IOCs to sell the retained 50% of their export proceeds immediately in the Nigerian FX market during the 90-day retention period, in addition to the settlement of eligible financial obligations at any time during the retention period.

- **May 31, 2024 (Circular TED/FEM/PUB/FPC/001/006)**:

  Reinforced the May 6 changes and clarified procedural requirements for IOCs to ensure compliance.

Potential Implications for the Nigerian Petroleum Industry

- The CBN's new policies aim to balance and improve FX market liquidity, support operational demands, and stimulate the local economy. Implementing them will necessitate strategic adjustments by IOCs, which must also adhere to the documentation requirements outlined by the CBN, including obtaining prior approval, maintaining cash pooling agreements, and providing detailed expenditure statements. IOCs may also need to adjust their cash flow strategies to align with the new requirements, ensuring sufficient funds are available to meet local obligations before repatriating profits.

- The CBN's policies give IOCs the flexibility to either sell 50% of their repatriated export proceeds to CBN-authorised FX dealers, or to apply retained funds to certain domestic financial obligations, including petroleum profit tax, royalties, payments to domestic contractors, cash calls, transaction taxes (including the Nigerian Contenet Development (NCD) Levy, and education taxes.

- The new policies enable banks to submit requests for cash pooling prior to the receipt of the expected proceeds, provided they supply the necessary documentation. This measure is intended to improve the management and oversight of pooling arrangements, ensuring a more efficient and streamlined process.

- Retaining a portion of export proceeds locally should also support increased spending on domestic services and projects by IOCs. The influx of funds should help to stimulate local businesses and create economic growth opportunities. In addition, the increased local availability of funds should help to facilitate investments in critical infrastructure, addressing certain long-standing constraints in the sector and enhancing overall efficiency and productivity.

- IOCs will need to incorporate these regulatory changes into their long-term strategic planning, considering how prolonged retention of funds in Nigeria affects their global financial operations and capital allocation.

  OCs might also, conceivably, seek strategic partnerships with local companies to enhancing commitments to local content and optimise their Nigerian operations.

Conclusion

The Central Bank of Nigeria's (CBN) directive on cash pooling marks a significant shift in the country's regulatory framework, aimed at balancing the operational needs of International Oil Companies (IOCs) with Nigeria's broader economic objectives. While these restrictions introduce immediate challenges in liquidity management and may increase compliance and strategic planning costs, they also offer potential opportunities for local investment and economic growth.
By mandating the retention of a portion of export proceeds within Nigeria, the directives are likely to encourage local spending, stimulate domestic industries, and enhance the stability of the FX market. These measures are anticipated to contribute to a more diversified and resilient Nigerian economy, fostering sustainable development and reducing economic volatility.

Disclaimer: This update is authored by Folake Elias-Adebowale, Godson Iwuozo, Noble Chinwendu, Josephine Ukpong, and Anjolaoluwa Shittu of Udo Udoma & Belo-Osagie. It is intended for information purposes only and shall not be construed as legal advice on any subject matter in any circumstances. It does not and shall not be construed as creating any relationship, including a client/attorney relationship, between readers and our firm or any author or serve as legal advice. The opinions expressed in this publication are the opinions of the individual authors and may not reflect the opinions of the firm or of any individual attorney. You should contact your attorney to obtain advice with respect to any particular issue or problem. For more information about our oil and gas and other practice group offerings, please visit our website at www.uubo.org or email us atogteam@uubo.org and at uubo@uubo.org.