



Review of the Petroleum Exploration, Development and Production Bill 2014

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National Policy on Upstream Operations & National Upstream Strategic Plan

- a national policy on upstream operations and National Upstream Strategic Plan. Policy to be reviewed every 5 years
- Note: A review does not necessarily connote policy change.
- Where it leads to changes in policy, it could send disturbing signals about investor perception of policy consistency.
- Long-term policy consistency is important for building investor confidence
- Compensating changes with stability clauses. But this has cost & can undermine future developments.
- Kazakhstan now excludes environmental issues. Ghana has limited it to economic equilibrium
- National Upstream Strategic Plan can change frequently without problems

State participation

- For the purpose of accelerating beneficiation, state participation is encouraged. The state can participate through the National Oil Company (NOC) or a Contractor.
- However, it is important to examine the type of NOC the country wants and the role it has to play.
- NOC have sometimes over-stepped their boundaries and became tin gods and beyond government control as is the case in Angola.
- At this stage of petroleum development in Kenya, the definition of the NOC should be clear, with responsibilities well defined through legislation.
- The NOC should have right over all acreages unless the area is under a Petroleum Agreement.
- The NOC should be a party to all Petroleum Agreements, holding the state interests and indemnified against all losses and damages in petroleum operations.

Investment attraction

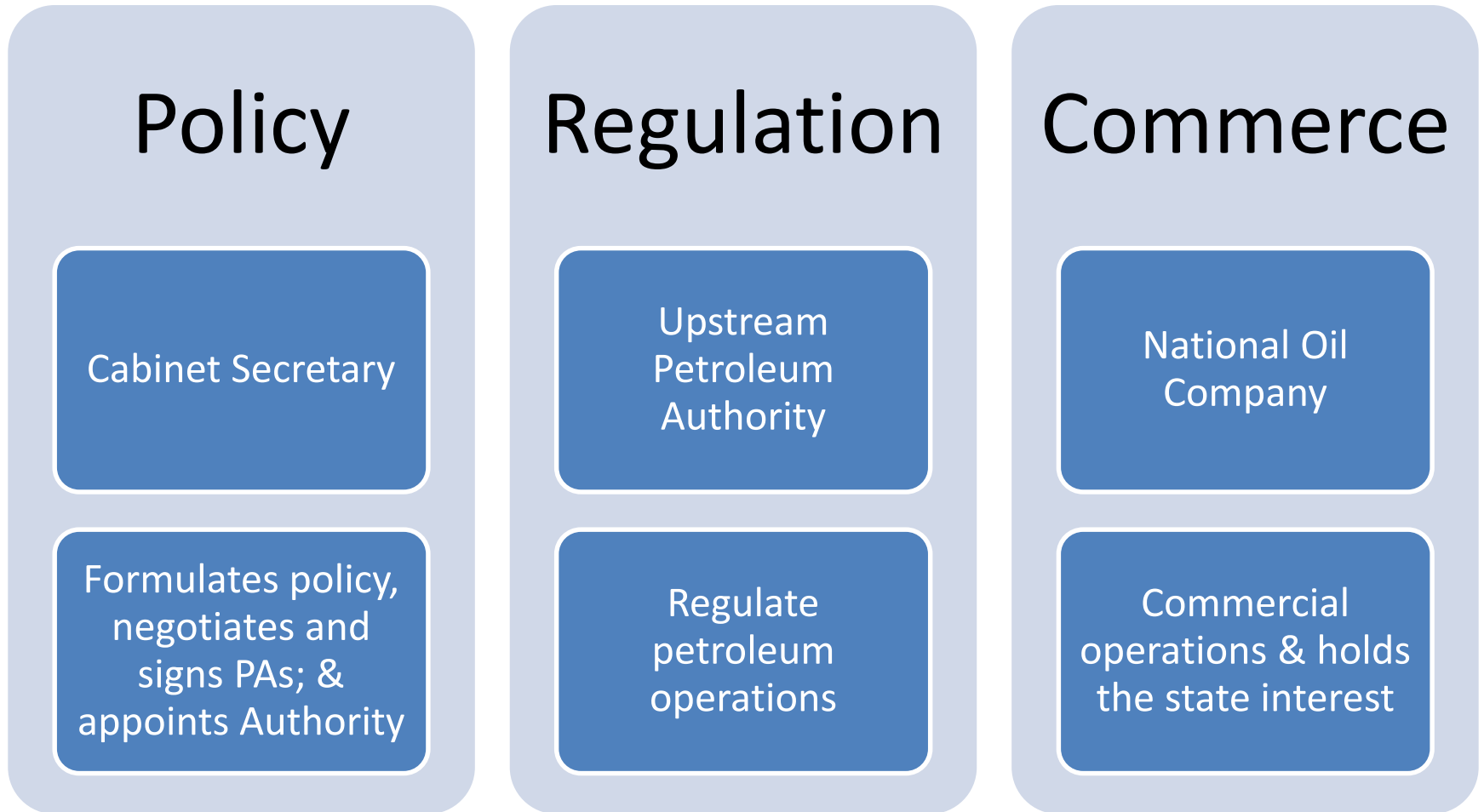
- Government shall promote a conducive environment for investments in upstream petroleum infrastructure development
- Clearly, the objective of the government is to attract upstream investments.
- The Petroleum Bill must therefore be forward looking and investment friendly.
- A law can be investment friendly with the following provisions
 - Lower fiscal terms
 - Stability clauses
 - Long exploration period and production periods
 - Lesser penalties
 - Tax incentives
 - Unlimited cost recovery. Etc.

Investment Attraction

As at February 2014, only 86,300 squared kilometres constituting only about 18% of the total basin area of 491,396 has data.

| Basin | Area (km²) | Wells drilled | Average Sediment thickness (m) |
|---------------|------------------------------|----------------------|---------------------------------------|
| Lamu | 261,000 | 19 | 12,000 |
| Mandera | 43,404 | 2 | 10,000 |
| Anza | 81,319 | 11 | 10,000 |
| Tertiary Rift | 105,673 | 7 | 4,000 |
| Total | 491,396 | 39 | 36,000 |

Institutional framework in the Bill



Others

**Upstream Advisory
Committee**

Parliament

County Gov.

Comments on Institutions

- The cabinet Secretary has so much powers which may undermine the Petroleum Authority
 - Power to negotiate petroleum agreements
 - Power to sign petroleum agreements & terminate
 - Power to appoint & dismiss Director General + Board of the Petroleum Authority
 - Power to appoint members of the Upstream Advisory Committee
- Power to perform regulatory functions
 - 10(d) to supervise petroleum operations carried out under a petroleum agreement;
 - 10(f) review and approve any proposed exploration activity contained in the annual work programme, appraisal programme and production forecasts submitted by a Contractor
 - 10(g) review and approve budgets submitted by a Contractor

Comments on Institutions

- Upstream Advisory Committee also performs regulatory functions
 - 10(2)(d) participate in the evaluation of the bids and applications for awarding petroleum blocks;
 - 10(2)(e) conduct all due diligence and investigate all the affairs of contractors prior to entering into petroleum agreements.
- The role of the Cabinet Secretary & Advisory Committee conflicts with the Petroleum Authority's regulatory role in licensing blocks
- The Bill therefore limits the role of the Authority to post licensing operations.
- There are no checks and balances in the licensing process. The Minister has absolute power in this process which is not consistent with best practice.

Protecting the Independence of the Authority

- How to protect the independence of the Authority – Some good examples
- The operational independence can be protected by introducing the ff. clauses:
 - *“The Authority shall implement the policies, regulations and decisions made by the Cabinet Secretary”*
 - *“The Cabinet Secretary shall not interfere in the operational functions of the Authority”*
- Appointment of the Director General and the Board should be made by the Cabinet Secretary. Rather by a higher appointing authority.
 - In Ghana, the President appoints the CEO of the Petroleum Commission and the Board
 - In Sierra Leone, the President appoints the Director General of the Petroleum Directorate, and approved by Parliament.
- The Petroleum Authority should present an annual report on all petroleum activities to Parliament and publish it, to ensure transparency + accountability.

Zoning of blocks

- The role of Cabinet Secretary in zoning oil blocks (standard).
- It is important to recognize the right of communities to prior and informed consent at this stage.
- When an area is earmarked for zoning, it is good practice for people or communities to be given hearing by the Cabinet Secretary if their interest is affected.
- The Cabinet Secretary must publish the concerns of the communities as well as his decision within specified number of days.
- This ensures that community conflicts are pre-empted and proactively resolved before the area is open for award.
- In some countries, aggrieved persons can seek redress in court. However, in order to ensure that petroleum related matters are not subject to litigations; litigation is usually limited to compensation decision and this has been well addressed in the sections on land use.

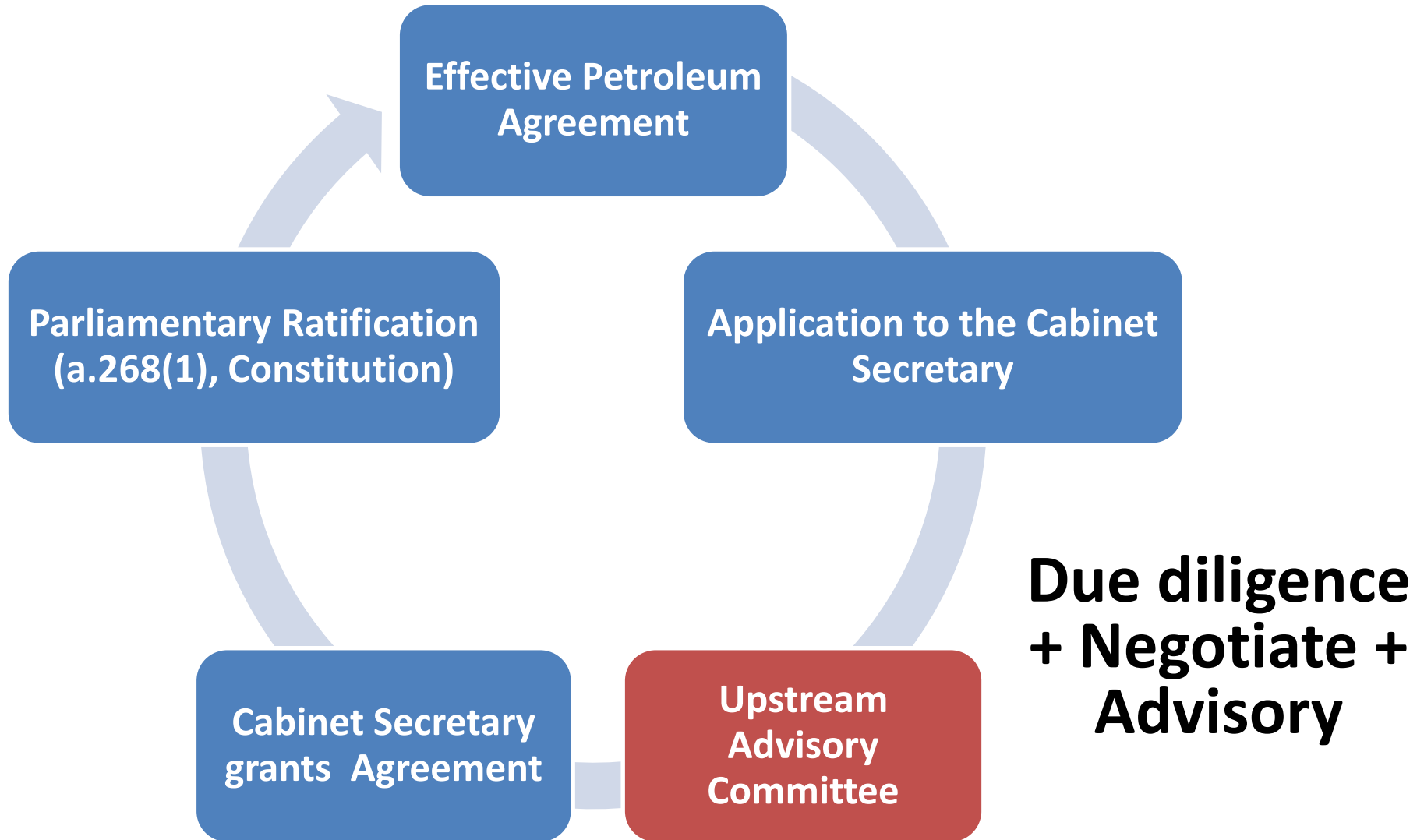
Licensing of Petroleum Rights

- Two types
 - Exploration license
 - Petroleum Agreement
- Exploration licence
- Exploration license has a unique objective of promoting investment in data acquisition.
- A significant advantage of exploration license is that, once significant data is acquired, the state can do any of the following:
 - Negotiate better terms
 - Undertake open and competitive public tender
 - Raise financing to develop the blocks on its own exploration

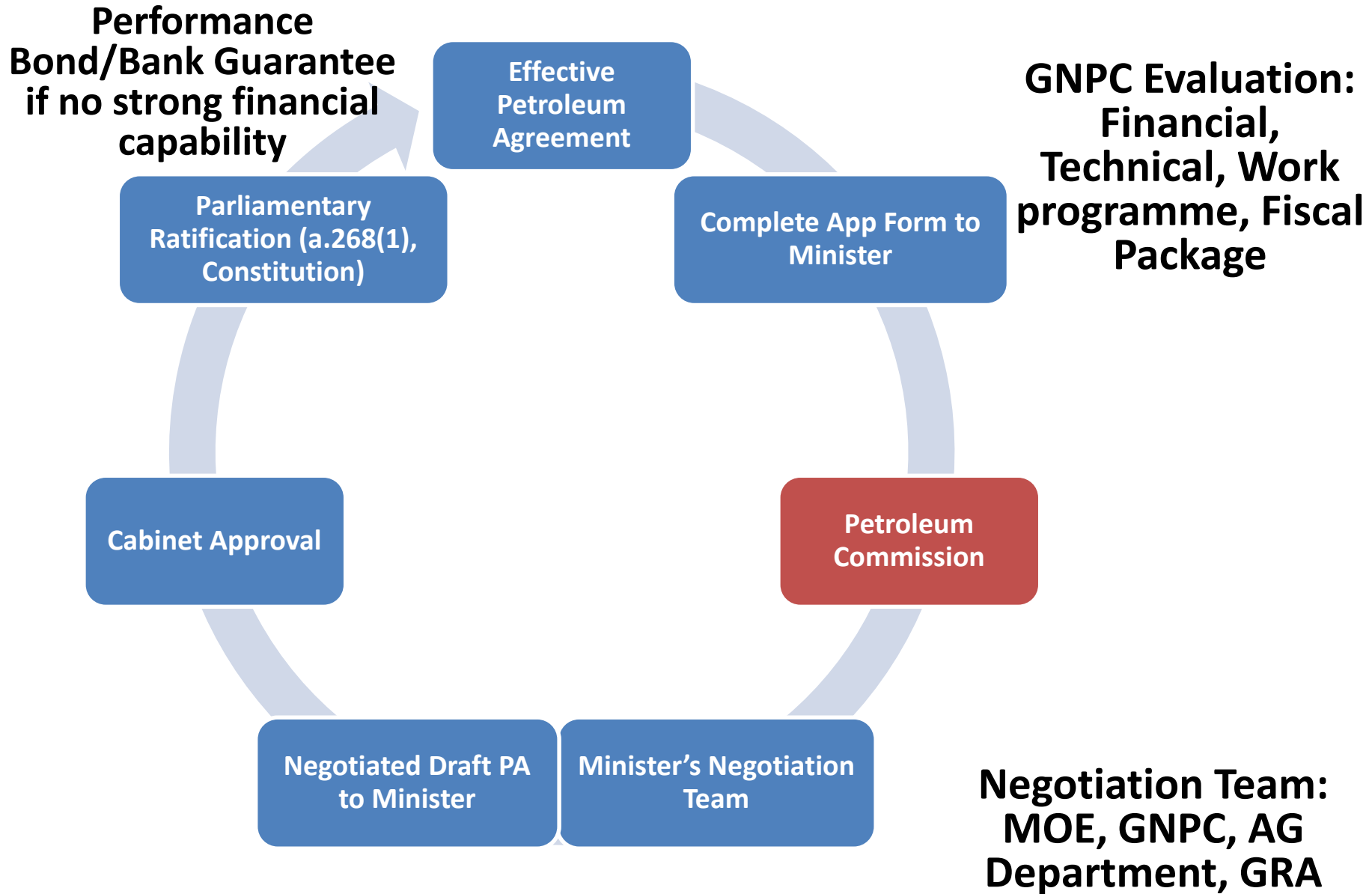
Licensing of Petroleum Rights

- Petroleum Agreement
- Petroleum Agreement is awarded by Public tender or direct negotiation
- **Direct negotiations**
- Direct negotiation and award shall only be, upon the advice of the Advisory Committee in the following circumstances:
 - Where there are no bids received following a public tender;
 - Where the bids received do not satisfy the criteria for award; and/or
 - Due to low quality data or inadequate data.
- In order to improve transparency in the licensing process through direct negotiation, the Bill requires the Cabinet Secretary to inform the public of its decision to apply direct negotiations.

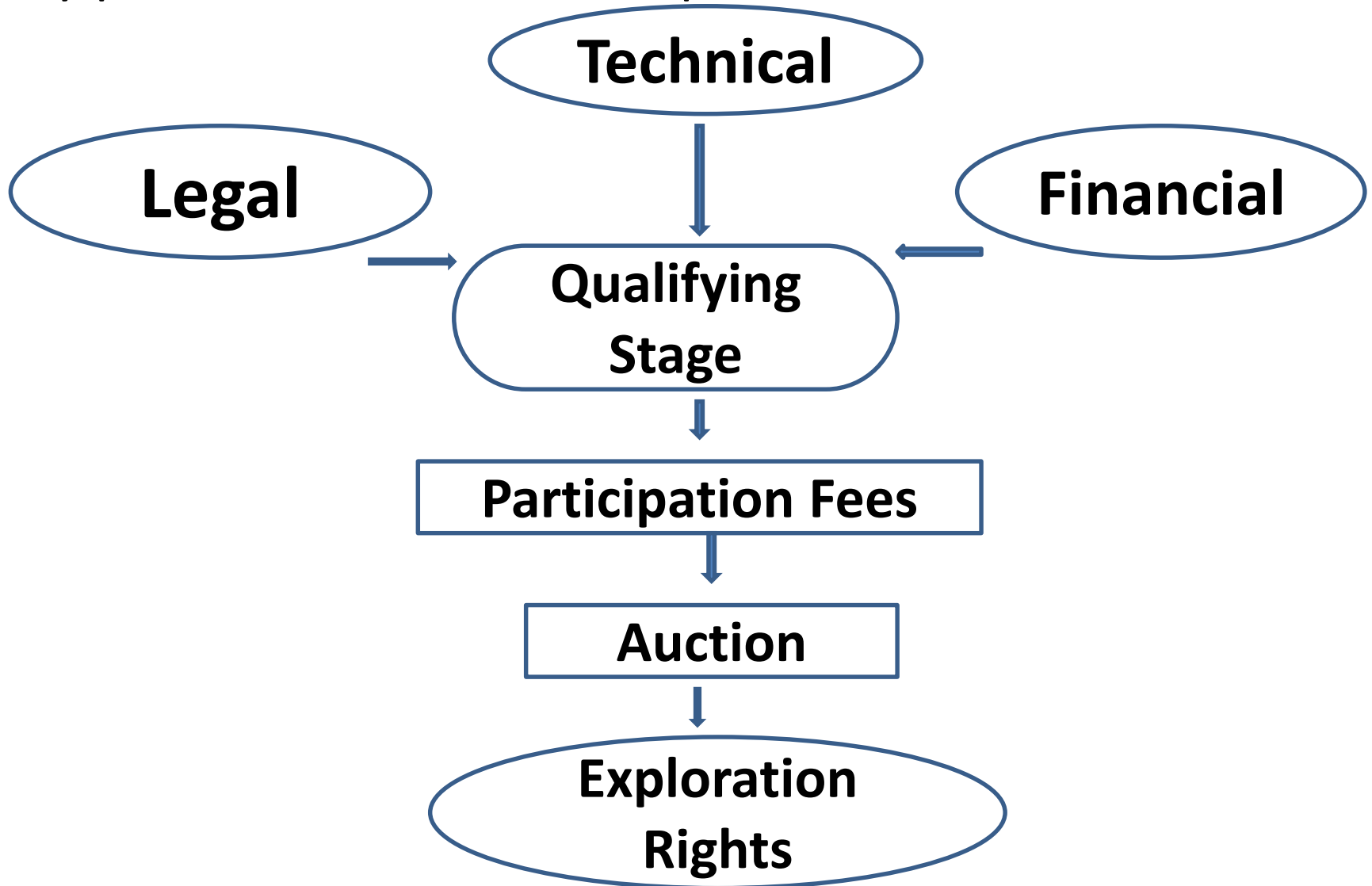
Procedure for Obtaining Petroleum Block in Bill through Direct Negotiation



Ghana Procedure for Obtaining Petroleum Block –



Procedure for granting petroleum agreement by public tender – An Example



Where Direct negotiation is the only option

- *“Should the Cabinet Secretary receive a proposal for direct negotiations under subsection (4), and opts to proceed with the direct award of the production sharing contract, the Cabinet Secretary shall issue a public notice of intent to enter into direct negotiations, and may commence direct negotiations with the entity proposing direct negotiations if within thirty days from the date of publication of notice, no entity declares an interest in the contract area in question. If another entity declares interest, the Cabinet Secretary shall conduct the prescribed tender procedure, limited to the interested entities”.*
- This provision is same as in Angola’s 2004 Petroleum Act. The only difference is the waiting time for commencement of negotiation. In Angola, the waiting time is 15 days.

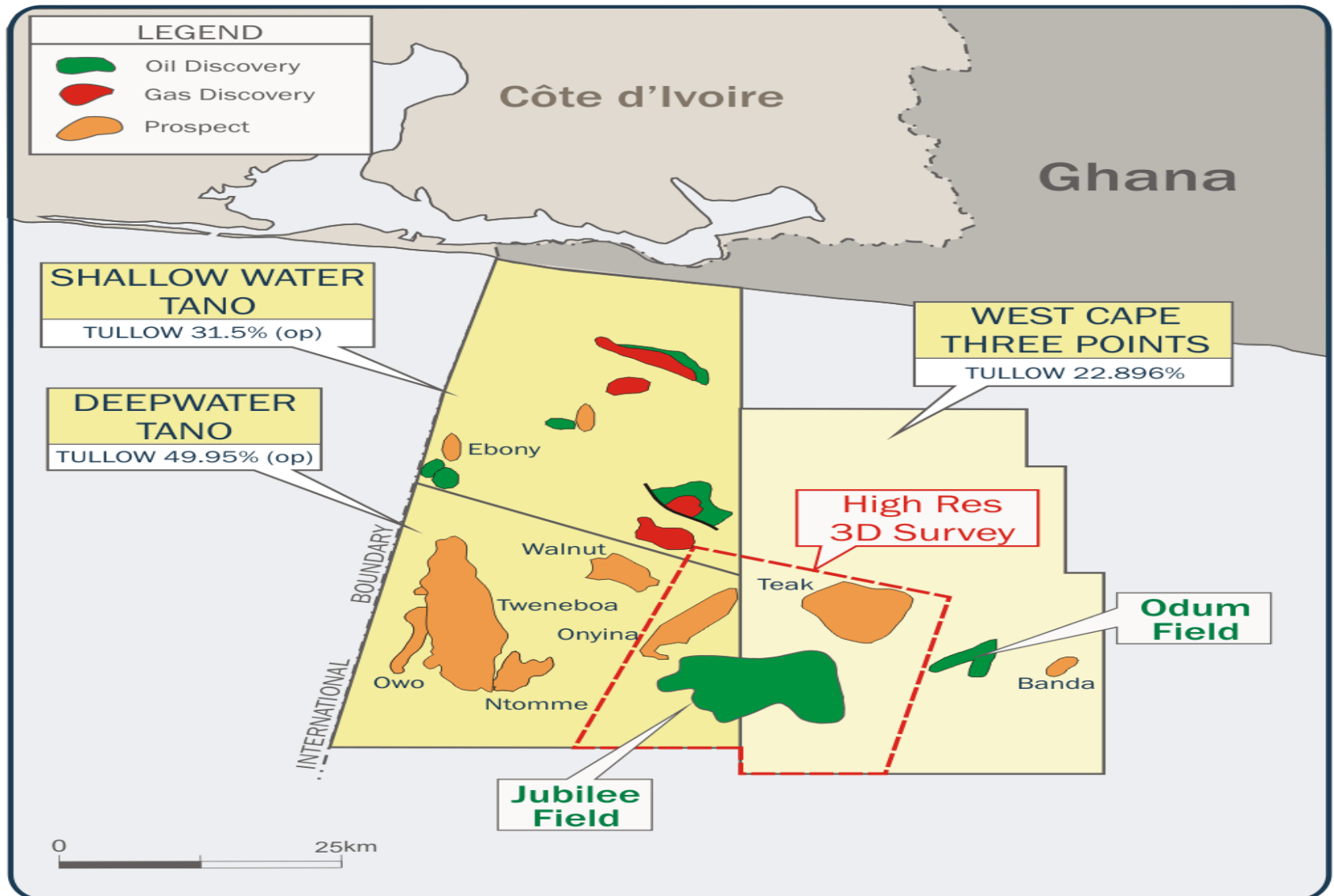
Development and Production

- Field Development Plan
 - (a) the contractors' proposals for the development and production of the reservoir;
 - (b) assessment of the possibility of unitization
 - (c) assessment of how to coordinate upstream petroleum operations with other Contractors, including the joint use of facilities subject to this Act and any other applicable law;
 - (d) proposals relating to the spacing, drilling and completion of wells and the facilities required for the production of petroleum including;
 - (e) the estimated number, size and production capacity of production platforms, if any;
 - (f) the estimated number of production wells;
 - (g) the particulars of production equipment and facilities;
 - (h) the particulars of feasible alternatives for transportation of petroleum including pipelines;

Development and Production

- The contents that have implications for communities are not included in the Bill, which is a serious omission:
 - Security plan
 - Health and safety assessment report
 - Emergency preparedness plan
 - Local content plan
- Contents that have financial implications for the state are also not included:
 - Description of fiscal metering
 - A financial plan
 - Decommissioning plan
 - Transfer of technology plan

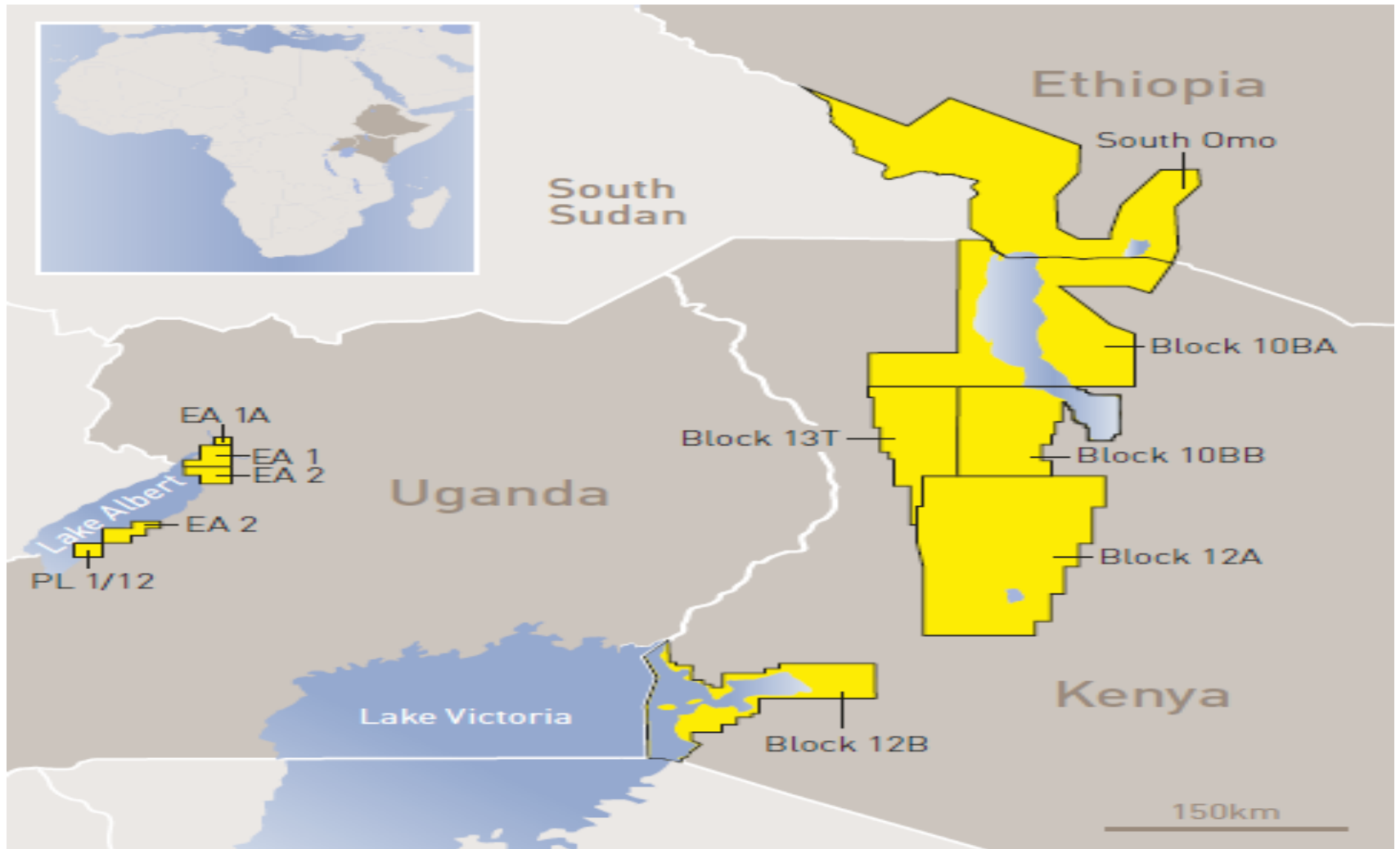
Unitization - The Jubilee Fields



What about Joint Development Zone? Nigeria-Sao Tomme Joint Development Zone



What about Joint Development Zones?



Infrastructure use

- Third Party Open Access
- The Bill provides for this.
- In view of the land situation in areas where exploration is active in Kenya, open access to infrastructure is relevant to prevent overlapping infrastructure facilities.

Decommissioning and Decommission Fund

- The Bill provides for decommissioning (Standard) .
- It also proposes a Decommissioning Fund.
- Contributions to the Decommissioning Fund as provided in the Bill starts:
 - When 50% of the recoverable reserves has been recovered
 - When it is left with 10 years before the expiry of the production permit
- This is an improvement as many countries allow contributions from the commencement of production.
- However, the success of the model in the Bill depends on the size of the contributions to the Fund.
- The Bill also makes contributions to the Fund a recoverable cost (Standard).
- Management of the Fund shall be by a committee of representatives from the country and the contractor. This is good for transparency.

Decommissioning and Decommission Fund

- A significant proposal in the Bill on decommissioning Fund is that when the fund is not enough for the decommissioning cost, the contractor shall take the remaining cost and expenses.
- This indemnifies the state of any responsibility.
- However, contractors may experience liquidity problem which may delay decommissioning under this circumstance, putting the area at environmental risks.
- The best practice is to request the Contractor to post a performance bond which will guarantee cash for decommissioning if the decommissioning fund proves insufficient.

Local content

- Local Content Requirements
- The Bill proposes that all operators must comply with local content requirements.
- They must prepare and submit annual local content plans for approval by the Upstream Petroleum Authority.

- Unique rules
 - The uniqueness of the Bill is its recognition of the importance of “local local content”.
 - *Clause 85, sub-section 3a of the Bill gives first consideration to the Counties in the use of services, but generalizes the use of goods to the country.*
 - Kenyan standards versus the so-called international standards. In most jurisdictions, the term “international standards” has been over-glorified, yet there is no common standards for the international community since different countries have different standards.

Local Content

- Monitoring of Local Content
- Monitoring of local content is the role of the Upstream Petroleum Authority.
- Training Fund
- Financing the training fund is based on annual training fees to be paid by the oil companies. This is to be negotiated between the state and the companies.
- In both Nigeria and Ghana, 1% of every contract awarded to an operator, contractor, sub-contractor, alliance partner or any other entity engaged in oil projects, operations, activity or transactions in the upstream sector shall be paid to the Fund.
- Use of the Fund limited to training and capacity building
- It should be expanded to cover R&D and financing local county initiatives such as small – medium scale firms.

Payments and Revenues

- Revenues to the state are dictated by the fiscal terms negotiated in petroleum agreements.
- In this Bill, specific fiscal terms that constitute revenue streams are provided to include:
 - i. Annual fees
 - a. Surface fees
 - b. Training fees
 - c. Such other fees as may be prescribed
 - ii. Signature bonus
- Share of petroleum which is based on Production Sharing Model

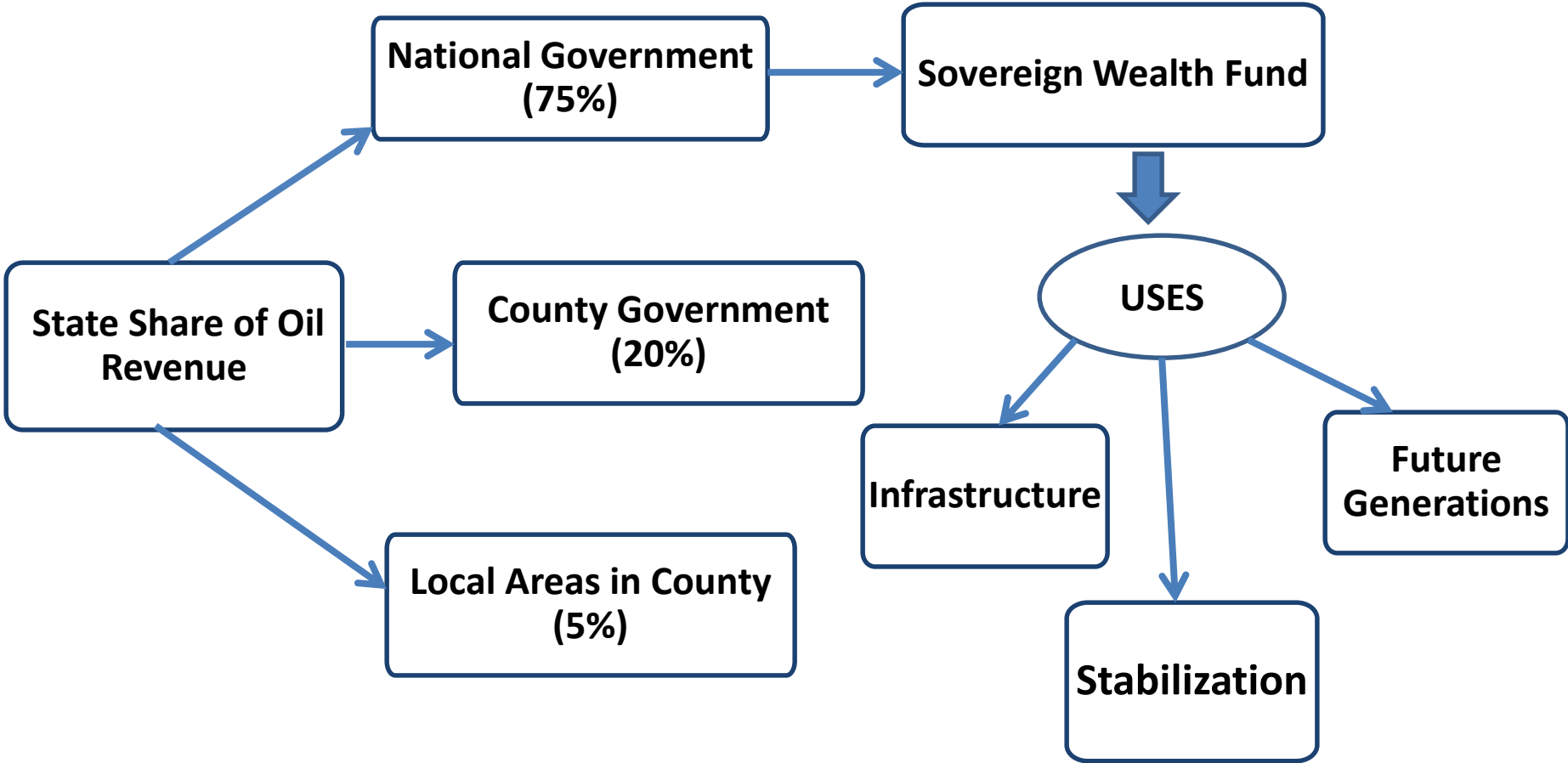
Petroleum Revenues and Distribution of Revenues

- The Bill proposes that the government share of revenues from oil shall be apportioned between the national government, the county government and the local community.
- County government share shall be 20% of government share whilst the local community share shall be 5% of government share paid through the county government.
- Two significant provisions in the Bill which communities must hail are:
 - Sub-section (4) – This does not want to make the share of the county government a substitute for revenues allocated to the counties by Commission for Revenue Allocation in the financial year.
 - Sub-section (6) – This requires each county government to legislate on the prudent utilisation of the funds received for the benefit of present and future generations.

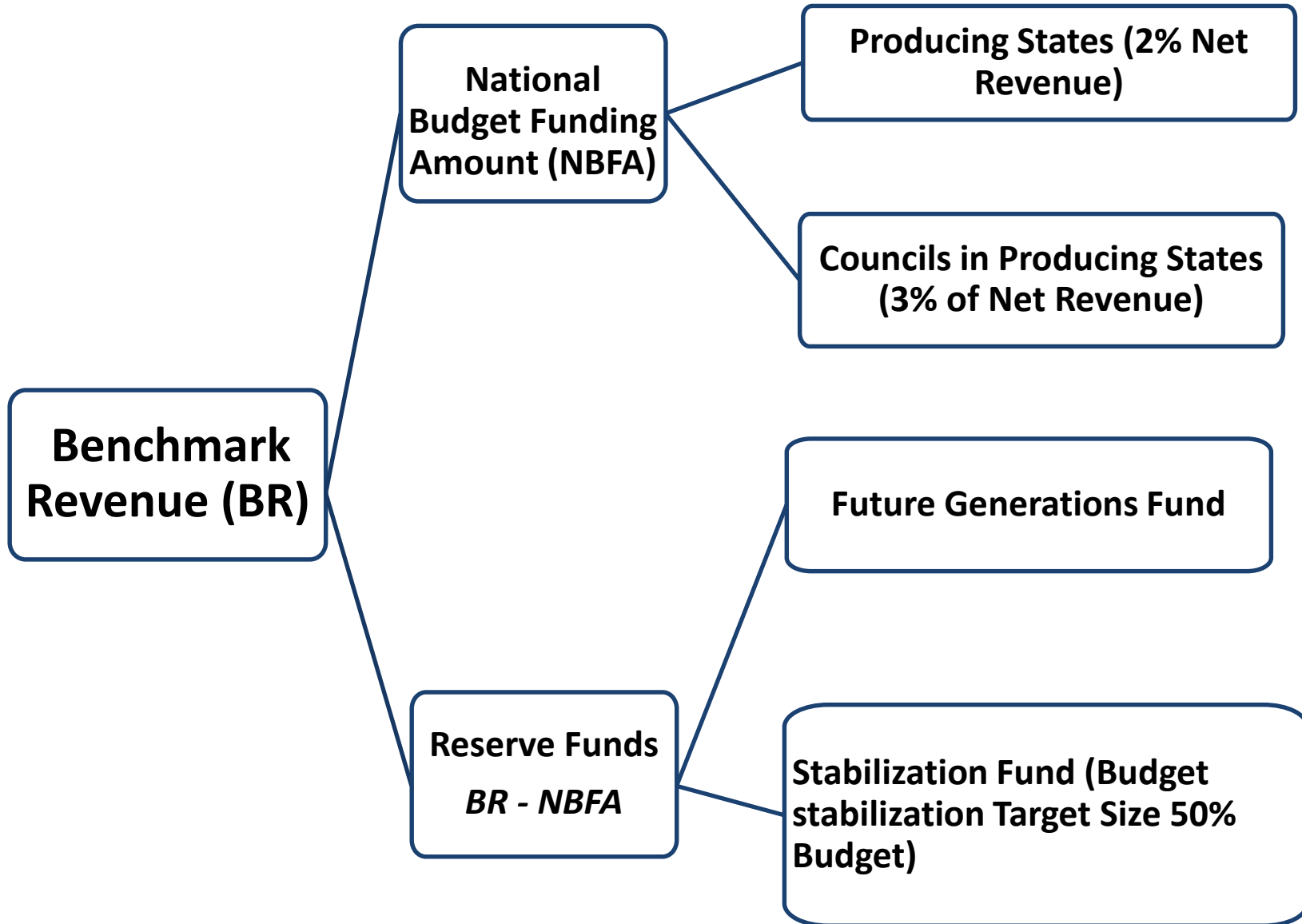
Sovereign Wealth Fund.

- The Bill also proposes a Sovereign Wealth Fund.
- In this Bill, the model of the Sovereign Wealth Fund follows the Norwegian model in which all revenues are put in a pool and applied to different uses including for:
 - infrastructure development,
 - expenditure smoothing (stabilization) and
 - inter-generational equity (savings for future generations)
- However, the Bill does not provide clear rules on petroleum receipts and withdrawals.
- It does not also provided investment and savings rules
- In most jurisdiction, there different funds with specific uses:
 - Budget Support
 - Stabilization Fund
 - Future Generations Fund
- Generally the provisions on revenue management are not adequate

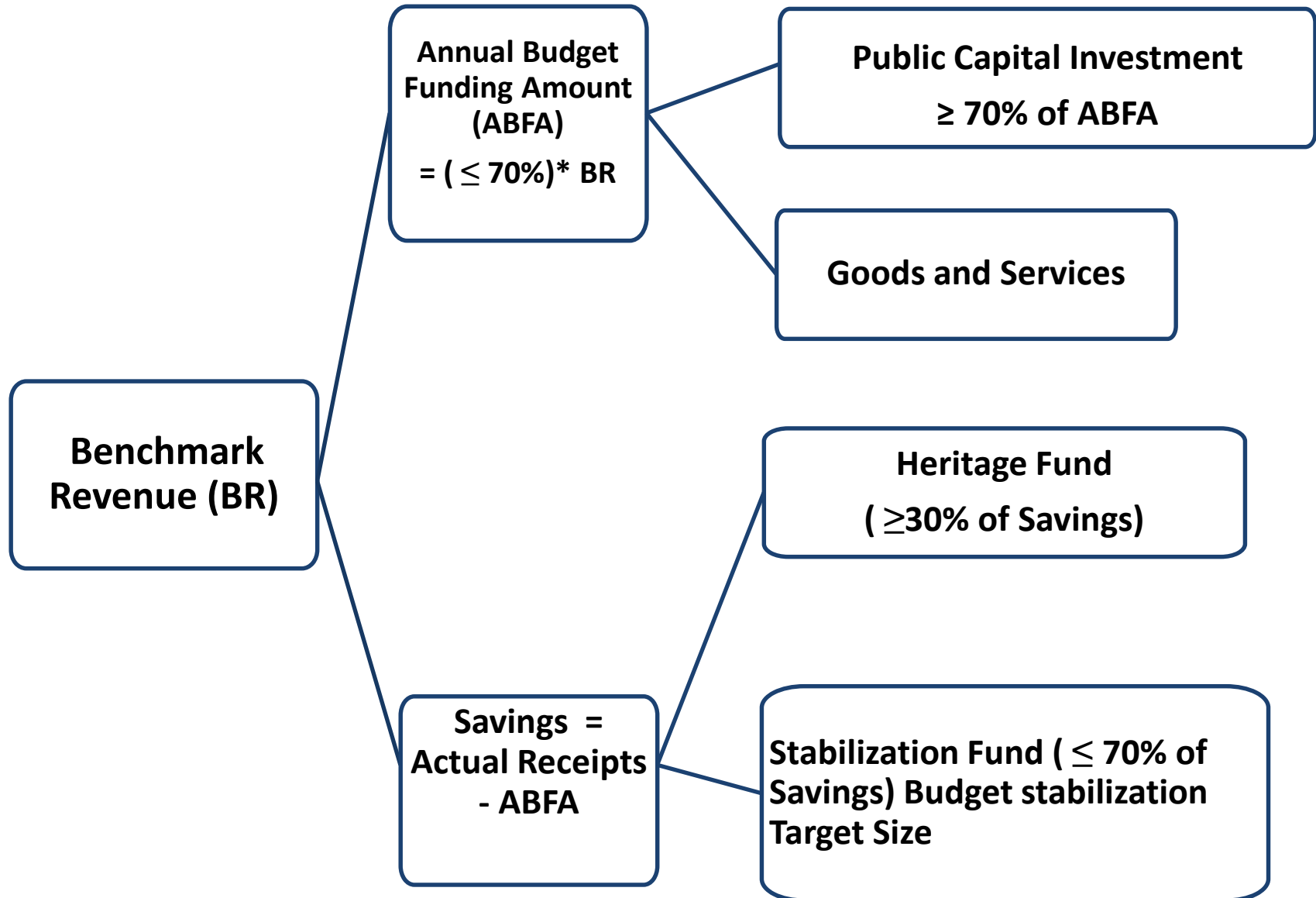
Revenue Distribution – Kenya Proposals



Revenue Distribution – South Sudan has a Decentralized Policy



Revenue Distribution – Ghana has a Centralized Policy



Framework for Transparency and Accountability

- Transparency and accountability
- The Bill provides that the Cabinet Secretary shall:
- Develop a framework for transparency and accountability in the upstream petroleum sector, which includes the annual publication of all records, accounts, and reports of:
 - revenues (royalties, fees, taxes and other charges), as well as,
 - any other relevant data and information that support payments received by the Government of Kenya, county governments, and local communities.
- It is highly encouraging that the Bill proposed sub-national reporting covering counties and communities as only a few countries undertake this type of public reporting

Transparency and Accountability

- The transparent and accountable framework for the upstream petroleum sector shall be disaggregated into each petroleum agreement, non-exclusive permit, drilling permit, production permit, and plug and abandonment permit in the following categories:
 - Payment type by each contractor (i.e., royalties, taxes, fees and other charges);
 - Production volumes by each contractor measured at the delivery point of sale;
 - Transfers of all petroleum sector revenues from national government to county governments and communities, including royalties;
 - All contractor contributions (in cash or in kind) to county governments and local communities.

Transparency and Accountability

- However, the provisions on transparency and accountability emphasize revenue transparency.
- It does not cover the new standards of the Extractive Industries Transparency Initiative. The new reporting standards include the following:
 - Mandatory disclosure of petroleum agreements, permits and authorizations through a public register
 - Explanation of how licenses are awarded or transferred during the year covered, and details on applicants and criteria used in any license auctions.
 - Mandatory disclosure of beneficial ownership information
 - Reporting on expenditure from petroleum revenues at national, county and community level to facilitate budget tracking

Community Rights

- The Bill provides that subject to the provisions of The Constitution of Kenya, 2010 and any other written law the community shall have the right to—
 - be informed prior of any activities to be carried out within their county and sub-county
 - put forward any inquiries, interrogation planned activities which directly or indirectly affect their interaction with the ecosystem during the preliminary phase of awarding of petroleum licenses for consideration
 - adequate compensation for land taken over for upstream petroleum operations as per the relevant land laws and the constitution
 - be compensated by any Contractor who causes environmental damage and/or pollution
 - be compensated for any injury, illness directly or indirectly related to the petroleum operations if the Contractor was in a position to take measures to prevent occurrence of the same.
 - compensation for damage to property and lost source of revenue or livelihood as a result of petroleum operations taking place in their immediate surroundings.

Community Rights

- The community rights outlined above are comprehensive. However, the problem is usually with enforcement.
- This has resulted in some jurisdictions providing mechanism by law to ensure compliance and minimize community resentment which are likely to disrupt oil operations.
- Two mechanisms are common:
 - The establishment of a Fund for community compensations
 - Community Development Agreement
 - In some jurisdictions, these agreements are admissible in court when there are breaches.

Thanks