

Barrisford Petersen, Managing Director, BBP Law



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Set out below are the responses to questions put to Attorney Barrisford Petersen by the Oil Council in a recent interview. Barrisford Petersen has been working as a lawyer in the African oil and gas industry for the more than 20 years and is also the Managing Director of BBP Law Inc, a South African specialist oil and gas legal practice based in Cape Town.

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SOUTH AFRICAN OIL AND GAS INDUSTRY REMAINS IN FLUX



Clearly history has taught us that if you create an enabling framework, then investment will follow. What are you seeing on the ground at the moment and where are we with the Mineral and Petroleum Resources Development Act Amendment Bill?

Currently the MPRDA Amendment Bill (MPRDA Amendment) has been referred back to the South African National Assembly by President Jacob Zuma. The Amendment Bill has been sitting on President Jacob Zuma's desk for almost 2 years after being approved by the National Council of Provinces in March 2014 and sent to him in final form for his assent.

For the South African oil and gas industry, this referral back to Parliament is potentially both a blessing and a curse. A blessing because the Amendment Bill as currently drafted, and if implemented, will be a precursor to the final demise of foreign investment in South African's oil and gas industry and a curse because the legislative uncertainty that has prevailed since the Amendment Bill was first introduced in December 2012 will continue.

Our research at BBP Law makes it clear that South Africa does not, from a best practice point of view, have the right enabling legislative environment in place for the establishment and continued growth of the upstream oil and gas industry. Existing legislation, with regard to the oil and gas industry was inflexible, failed to address important socio economic changes taking place in South Africa and most importantly failed to recognize the differing natures between the oil and gas industry and the mining industry. Balanced against the aforesaid, it has to be stated that prior to the MPRDA Amendment Bill's introduction, the legislation governing South Africa's oil and gas industry, while not perfect was adequate, remained manageable and there was sufficient legislative certainty that investment was not discouraged.

Many of the amendments proposed by the Amendment Bill are commendable and worthy of implementation within South Africa's established mining industry, but not for the oil and gas industry. The South African legislature has and continues to miss the opportunity for creating the right legislative framework that encourages investment in the South Africa's oil and gas industry. While the South African legislature should be pushing forward with legislation that encourages foreign investment, we find ourselves in a vacuum of uncertainty that has now lasted for more than three years and can be expected to continue for at least the remainder of this year.

It would seem the South African legislature has not only failed in appreciating the devastating impact the proposed MPRDA Amendments will have on the South African oil and gas industry but also the negative impact in having a protracted period of uncertainty as to whether the MPRDA Amendment in its latest form will indeed be passed into law. In our 2013 submissions to DMR and the parliamentary portfolio committee, we severely criticised the Amendment Bill. The main criticisms were not separating the oil and gas industry from the mining industry and not taking the opportunity to put in place a separate oil and gas act that conforms to best practice but also recognises that the South African oil and gas industry is in its infancy and will be subject to future changes that have to be correctly managed without losing investor confidence.

The future of South Africa's oil and gas industry is not only dependent on the oil and gas exploration companies that are currently exploring but more so with the many other International Oil Companies ("IOC") that are evaluating South Africa as an oil and gas investment destination. Policy makers and the legislature must create a stable fiscal environment that mitigates and deals appropriately with investment risk, investment stability and the social and economic changes taking place in South Africa. For so long as policy makers and the legislature fail to separate the oil and gas industry legislation from the mining industry legislation, each having differing investment requirements, this confusion will remain and one industry will always suffer at the expense of the other.

In all probability the MPRDA Amendment will find its way back onto the desk of the Parliamentary Committee for Mineral Resources. From that point on we are unsure of what exactly will happen to the Amendment Bill. We are certain that further amendments to the MPRDA Amendment will be made however we are doubtful that separating the oil and gas industry from the mining industry will be an issue high on the agenda.



The other area that is confusing to many from outside RSA is the relative roles of different departments in the current climate, DPR, DOE, Petroleum Agency, PetroSA and the now Draft African Exploration Mining and Finance Corporation Bill, 2015. What light can you spread on these relationships and who holds power?

In South Africa there is a central designated licensing agency called the Petroleum Agency SA (Petroleum Agency), Under the MPRDA, IOC's applications for an oil and gas rights gets lodged with the Petroleum Agency. The Petroleum Agency then evaluates the application, makes a recommendation to Department of Mineral Resources (DMR), which then goes onto the Minister's desk for consideration and approval. It has been our experience that DMR and the Petroleum Agency do not work well together, hence the proposal in the MPRDA

Amendments to dissolve the Petroleum Agency. The power therefore remains with DMR. The current proposal under the MPRDA Amendment is to disband the Petroleum Agency and decentralise oil and gas regulatory control regionally under DMR. This in our opinion does not make sense. Decentralising regulatory regionally lends itself to numerous inefficiencies and the maladministration of oil and gas rights.

Complicating matters further is the involvement of the Council of Geoscience, which perceives itself now as having an enhanced role as a consequence of most of the onshore data required for unconventional oil and gas exploration, being held by them. We also have PetroSA, the South African national oil and gas company, which reports to the Department of Energy (DOE) not DMR or the Department of Public Enterprises (DPE). Clearly in South Africa we have a situation ripe for confusion, uncertainty and inefficiency.

The African Exploration Mining and Finance Corporation Bill of 2015 that has been recently proposed seeks to create a new State owned enterprise that will hold State interests in resources which includes oil and gas resources. Where does that leave PetroSA for now, we are not sure.



A lot is spoken about South Africa in terms of unconvensionals. Can you spread some insight as to where we currently are with the conventional and unconventional drilling programs?

Certainly with the advent of significant interest in South Africa's unconventional oil and gas resources, and here we mean shale gas and coal bed methane (also referred to as coal seam gas), South Africa has a potential game changer that can only enhance the more costly and riskier offshore conventional oil and gas exploration industry within South Africa as more skills, resources and infrastructure is made available and created. The South African Oil and Gas Alliance is doing a sterling job in encouraging the growth of industry and businesses that provide essential support services to the oil and gas industry whether conventional or unconventional.

At present, there has been a number of coal bed methane exploration wells drilled with discoveries made and one coal bed methane production right granted. The production right is however in respect of an extremely small coal bed methane project. As far as shale gas drilling is concerned there remains a State imposed moratorium in place over a significant part of South Africa's onshore blocks which precludes the Petroleum Agency from receiving and processing shale gas applications. Existing shale gas rights holders have for some time been precluded from all shale gas drilling until appropriate shale gas drilling regulations are put in place. It would seem that these regulations will be promulgated shortly. As far as we are aware certain existing shale gas rights holders have recently been given permission to commence with shale gas exploration drilling on the understanding that no hydraulic fracturing will take place. We suspect that limited hydraulic fracturing will only be permitted once the regulations have been finalised.

South Africa remains underexplored for conventional oil and gas resources. Approximately 250 exploration wells have been drilled offshore the entire coastline of South Africa with not more than two wells drilled in depths greater than 1500 meters of water. South Africa, despite its oil and gas potential remains underexplored.

Legislative and fiscal uncertainty, despite plenty of IOC interest, has done a lot of damage in discouraging IOC's from investing in South Africa. Offshore exploration wells drilled in the Southern hemisphere continue to exceed budgeted costs and in a cost sensitive environment, this remains a huge hindrance. Another key problem area is local content or rather the lack thereof. Locally we do not have the necessary drilling infrastructure to support drilling at the depths required. A significant amount of skills and resources must still be imported. We often forget that offshore exploration drilling is dangerous, high risk and very expensive.

In terms of conventional oil and gas drilling, which primarily takes place off-shore in the Republic of South Africa we have recently had the drilling of the Total well offshore in Blocks 11B/12B last quarter 2014. With many IOC's cutting exploration budgets as a consequence of low oil prices and with the continued legislative uncertainty in South Africa, it is expected that IOC's will defer expensive offshore drilling obligations in South Africa for as long as they can within the foreseeable future.



Much of South African acreage is owned by independents. Apart from the great success of Impact Oil and Gas many independents seem to be struggling to farm down their interests/source financing. Does BBEE have an effect here?

For so long as the legislative uncertainty exists in South Africa, investment into South Africa's oil and gas industry will suffer. IOCs are reluctant to spend money and those that already hold exploration blocks will find it extremely difficult to mitigate exploration risk through focused divestment.

Having met with a number of oil and gas divestment specialists in London over the last 3 years, all express the same views namely, general lack of appetite for exploration risk world-wide and with regard to South Africa the existing legislative uncertainty. IOC's and oil and gas investment and divestment houses are unable to properly model economic investment decisions with the degree of certainty and accuracy required to justify a positive investment decision in South Africa's oil and gas industry. The uncertainty created by the MPRDA Amendments preclude long term investment decisions from being made.

Matters regarding the MPRDA Amendments have been further complicated by the recently proposed draft new Amended Broad Base Socio Economic Empowerment Charter Mining Charter (Mining Charter Amendments) published for comments. Since the MPRDA Amendment intends ensuring compliance by the oil and gas industry with the Mining Charter, the impact of the proposed Mining Charter Amendments on the oil and gas industry and the MPRDA Amendment will most certainly have to be reconsidered.

At present provision is made in both the exploration right and the production right granting instruments for black economic empowerment in line with the Liquid Fuels Charter, considered to be more appropriate for the oil and gas industry. It is inconceivable that the legislature in terms of the MPRDA Amendments would now seek the implementation of the black economic empowerment based on the Amended Broad Base Socio Economic Empowerment Charter (Mining Charter) as it has been drafted specifically for an established mining industry in South Africa. The impact of imposing the objectives of the Mining Charter on foreign investment in the oil and gas industry at this crucial stage of its growth could be in our opinion prohibitive,

especially when considering how limited sources of funding are for established oil and gas companies.

At present a 10% equity interest is reserved for State participation with IOC's having to carry the State's expenditure interest through exploration only and a 10% equity interest is reserved for black economic empowerment participation but only required for the grant of a production right. During exploration, IOC's must use best endeavors to find a black economic empowerment joint venture partner. The MPRDA Amendments together with the Mining Charter Amendments would significantly restructure the ownership of oil and gas rights in South Africa to the detriment of IOC's investment decision making economic models, consequently discouraging investment. Under the Mining Charter, black economic empowerment interests would have to be at the 26% equity interest level and State participation (with a free carried interest) could conceivably be anything from an equity interest of 10% as currently exists upwards as the MPRDA Amendments places no limitation thereon.



The Gas Utilisation Master Plan (GUMP) is a strategy geared towards increasing energy diversity and security for South Africa. What role does government have to play in creating a “gas economy”? The Department of Energy currently has its IPP office reviewing gas options to provide over 3000MW power to the RSA grid possibly utilizing LNG. What do you make of this?

Anything that is done by the State to create and put in place infrastructure to support the demand for energy within South Africa can only be regarded as positive for oil and gas exploration. A lot of positive feedback has been received with regard to South Africa's renewables IPP projects. But for the intervention of the State in not only creating the necessary supporting infrastructure but most importantly putting in place the necessary guarantees to support the Eskom power purchase agreements, it is doubtful the renewable IPP projects would have been as successful. Ultimately the question that has to be asked is if the same State support was given to other forms of power generation projects would the normalized cost of electricity for the very same power generated by the renewable projects have been cheaper or more expensive.

Since perceptions of success are present it would seem natural that a gas IPP is considered and as a precursor to that gas IPP, GUMP considering the shale gas potential within the Republic of South Africa, the world being in oversupply of LNG generation capacity and the significant gas discoveries that have been made on the east coast of Africa. It should however be noted that all the aforesaid potential gas supply projects for power generation within South Africa will not to meet South Africa's short term energy needs. South Africa for the foreseeable future will remain dependent on coal and petroleum products for the generation of power with renewables having a small impact albeit costly.

Having due regard to the aforesaid, we, as are many IOC's, of the opinion that oil and gas exploration within South Africa has the potential to make South Africa, energy independent. Many IOC's have identified South Africa as an oil and gas investment destination if only the right legislative and investment framework was created and maintained. For this reason we believe that the effort and cost invested in GUMP and the gas IPP, while being an important part of our future, may be a bit premature. In our opinion, it would be better for the State and

the legislature to focus their attention on doing what is necessary to encourage foreign investment in South Africa's upstream oil and gas industry, remove IOC's causes of concern and not sacrifice our upstream oil and gas industry in pursuit of more expensive alternatives.



 **OIL & GAS COUNCIL**

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