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OIL & GAS ALERT



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PART 3

Draft Upstream Petroleum Resources Development Bill, 2019: Ways in which to apply for petroleum exploration and production permits or rights and consultation with interested and affected parties regarding acceptance of applications

In part three in our series of articles on the draft Upstream Petroleum Resources Development Bill, 2019 (the Petroleum Bill) we unpack certain provisions set out in chapter 4 of the Petroleum Bill, specifically sections 26 to 28.

A Crude-Awakening: The Covid-19 Oil Price War

A drop in global demand as the world came to grips with the extent of the COVID-19 virus, coupled with a price war between two oil producing giants, Saudi Arabia and Russia, has caused oil prices to plummet. By 8 March 2020, oil prices had fallen by 30% sending shock waves through already spooked financial markets.

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Draft Upstream Petroleum Resources Development Bill, 2019: Ways in which to apply for petroleum exploration and production permits or rights and consultation with interested and affected parties regarding acceptance of applications

Section 26 of the Petroleum Bill provides that the Minister may, by notice in the Government Gazette, invite applications for reconnaissance permits, technical co-operation permits, exploration rights and production rights in respect of blocks designated by the Petroleum Agency of South Africa.

In part three in our series of articles on the draft Upstream Petroleum Resources Development Bill, 2019 (the Petroleum Bill) we unpack certain provisions set out in chapter 4 of the Petroleum Bill, specifically sections 26 to 28. Chapter 4 contains what is referred to under the Petroleum Bill as “*Petroleum Regulations*” and covers various aspects of the upstream petroleum sector, including provisions on the application for permits or rights, the processing of applications for permits or rights and consultation with interested and affected parties.

Section 26 of the Petroleum Bill provides that the Minister of Mineral Resources and Energy (the Minister) may, by notice in the Government Gazette, invite applications for reconnaissance permits, technical co-operation permits, exploration rights and production rights in respect of blocks designated by the Petroleum Agency of South Africa (the Petroleum Agency).

This “*application-by-invitation*” regime proposed by the Petroleum Bill is a notable shift from the open licensing regime contained in the Mineral and Petroleum Resources Development Act 28 of 2002 (the MPRDA). The Petroleum Bill proposes three types of by-invitations applications, which consist of (1) a by-invitation bid round; (2) a by-invitation first come first served and (3) by-invitation reconnaissance permits.

(1) By-invitation bid rounds

The implementation of a by-invitation bid round system which is introduced in section 26(1), allows the Minister to invite multiple bids for designated block/s, evaluate each compliant application on its merits and then select the best bid which is then awarded the permit or right. The Minister’s invitation may prescribe (a) the period within which the application must be lodged with the Petroleum Agency; (b) the procedure for lodgement of the application; and (c) the basic terms and conditions on which such applications

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may be granted or refused. These terms and conditions may include, for example, that only applications for an exploration right will be accepted in relation to the designated block to which the Minister’s invitation relates.

The Petroleum Agency will accept an application submitted in terms of section 26(1), if it complies with the requirements of section 27(3), and must reject an application if it does not meet these requirements. The requirements set out in section 27(3) of the Petroleum Bill include, inter alia, the applicant having to prove (i) technical and financial ability, (ii) that the estimated expenditure is compatible with the intended work programme, and (iii) compliance with the requirements stipulated in the invitation notice published by the Minister.

Insofar as the proof of financial ability is concerned, the applicant is required to provide a “*form financial guarantee*”. We note that section 27(3)(a) is unclear on whether this requirement refers to a parent company guarantee, bank guarantee or the like. It is also unclear whether the requirement to submit a “*form financial guarantee*”, at application phase, contemplates a signed or unsigned “*form*” guarantee. This is a significant distinction, as securing a signed guarantee, from a

third-party guarantor in particular, may be impractical and considered unfeasible at application phase, and this requirement would benefit from clarification by the drafters.

The Petroleum Agency must acknowledge receipt of each application received in terms of section 26(1), in writing and within 14 days of receiving each application. Once processed, the Petroleum Agency must, within 60 days from the date of the initial acknowledgment of receipt, inform applicants in writing of the decision to accept or reject their application. Should an application be rejected by the Petroleum Agency because it does not meet the requirements of section 27(3), then the Petroleum Agency is required to provide written reasons to the applicant on its decision to reject an application. This aligns with the constitutional right which entitles an applicant to written reasons for any adverse decisions taken by an administrative body, provided for under the Promotion of Administrative Justice Act 3 of 2000.

(2) By-invitation first come first served

Section 26(7) of the Petroleum Bill also makes provision for the Minister to invite applications for exploration rights and production rights in respect of

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Section 26(7) of the Petroleum Bill also makes provision for the Minister to invite applications for exploration rights and production rights in respect of blocks identified by the Minister.

blocks identified by the Minister. Unlike section 26(1), these applications are processed on a "first come, first served" basis. This means that applications are dealt with in accordance with the date of receipt, as opposed to being dealt with on its merits. The Minister thus has to finalise the processing of the application which was lodged first; and the Petroleum Agency is not allowed to accept receipt of a subsequent application until the first application has been rejected.

Applications for exploration rights lodged in terms of section 26(7) of the Petroleum Bill are processed in accordance with section 46 and applications for production rights lodged in terms of section 26(7) are processed in accordance with section 51. These processes are not dissimilar to the application processing employed under the current regulatory regime. We will be reviewing applications processed in accordance with section 46 and section 51 in an upcoming article.

Once an application has been accepted, section 28(1) of the Petroleum Bill requires that the Petroleum Agency (a) notify interested and affected persons that an application for an exploration right or production right has been accepted for consideration and (b) call on such interested and affected

persons to submit their comments and objections. If an objection is received, the Petroleum Agency must refer the objection to the Petroleum Development and Environmental Committee, a newly introduced committee which will be established by the Petroleum Bill, which will inter alia consider the objection and advise the Minister thereon. The Petroleum Agency may also require the applicant to consult with the person who lodged the objection.

Under the National Environment Management Act, 107 of 1998 (NEMA), public consultation is compulsory as part of the environmental impact assessment process. The consultation with interested and affected parties is in addition to the public consultation process provided for under NEMA. As the nature of objections has not been defined, an applicant may be prematurely compelled to address objections which would otherwise be addressed during the public participation process provided for under NEMA. This may result in a duplication of the public consultation process and a delay in the granting of the exploration or production right. Importantly, consultation with interested and affected persons in terms of section 28 of the Petroleum Bill is only a requirement for applications lodged

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in terms of section 46 (exploration right applications) and section 51 (production right applications), and therefore not a requirement for applications submitted pursuant to the Minister's invitation under section 26(1).

(3) By-invitation reconnaissance permits

Another new feature proposed by the Petroleum Bill is the introduction of section 26(4), which grants the Minister the power to invite seismic survey operators to lodge applications for reconnaissance permits to conduct seismic surveys over multiple blocks, including blocks which are the subject of existing exploration or production rights. However, this provision seems to contradict section 41(2)(b) of the Petroleum Bill which stipulates that an application for a reconnaissance permit must be accepted if no other person holds a permit or right over the same block. This contradiction in section 26(4) might be removed by requiring the applicant to seek the consent of the existing exploration right or production right, as required under section 41(3) of the Petroleum Bill. Section 41(3) also states that such consent cannot be unreasonably withheld.

Applications for reconnaissance permits lodged in terms of section 26(4) are processed in accordance with

section 27(3). The Petroleum Bill does not expressly clarify whether reconnaissance permit invitations are issued by the Minister on a bid round or first come first serve basis. However, given the processing of these applications in accordance with section 27, it is likely that the drafters intended that the Minister be empowered to invite multiple bids for reconnaissance permits.

The proposed hybrid "*application-by-invitation*" regime, which allows for bid rounds and for applications to be dealt with on a "*first come, first served*" basis, is a welcomed addition to the upstream petroleum sector. We are eager to see the implementation of the by-invitation system once the Petroleum Bill is enacted. Although bid rounds generally are more effective in producing jurisdictions, they can be an effective tool to maximize and expediate exploration activities for petroleum resources in frontier basins.

In our next article in this series we will be dissecting inter alia the establishment and role of the Petroleum Development and Environmental Committee under the Petroleum Bill.

Megan Rodgers and Shameegh Allen

A Crude-Awakening: The COVID-19 Oil Price War

Saudi Arabia's push for steeper and longer production cuts than had been expected by OPEC members, and Russia's refusal to decrease its production to this extent, resulted in a deadlock.

A drop in global demand as the world came to grips with the extent of the COVID-19 virus, coupled with a price war between two oil producing giants, Saudi Arabia and Russia, has caused oil prices to plummet. By 8 March 2020, oil prices had fallen by 30% sending shock waves through already spooked financial markets.

Ironically, the rapid price decline followed from a meeting of the Organisation of Petroleum Exporting Countries (OPEC) where the goal was to reduce oil production so as to offset the collapse in demand, due to the COVID-19 outbreak, and in doing so stabilize and support the oil price. Saudi Arabia's push for steeper and longer production cuts than had been expected by OPEC members, and Russia's refusal to decrease its production to this extent, resulted in a deadlock. Analysts reported that Russia had become increasingly frustrated with OPEC's policy of supply restraint. Russia views this as facilitating the growth of shale oil producers in the United States. Recently sanctioned Russian state-owned oil company, Rosneft, stated that *"by yielding [their] own markets, [they] remove cheap Arab and Russian oil to clear a place for expensive US shale oil and ensure the effectiveness of its production"*. Immediately after the failed OPEC meeting, Saudi Arabia, ramped up its oil production, slashed crude oil prices for its preferred customers and plummeted the oil price.

By launching an oil price war, Russia and Saudi Arabia engaged in a high-stakes game of *"who blinks first"*. In the meantime, the oil market would re-balance itself largely at the expense of the United States shale oil producers.

This of course did not sit well with the United States, which is regarded as the *"most important ally to Saudi Arabia"*. Senators in the United States called on the Trump Administration to implement the No Oil Producing and Exporting Cartels Bill (NOPEC Bill). In summary the NOPEC Bill, in its current form, makes it illegal to artificially cap oil and gas production or to set prices, as OPEC currently does. The NOPEC Bill was last threatened by the United States in October 2018 but Saudi Arabia enabled the oil price to remain above the key US\$70 per barrel level. Any sustained oil price above US\$70 per barrel is regarded as beneficial to shale producers in the United States. Analysts predicted that the oil price war was likely to last until the end of 2020. The current OPEC production cut deal expired on 31 March 2020 and this would either see a fierce battle for market share, as OPEC members would then be able to produce as much as they please or, optimistically, sanity would prevail between the oil producing giants and a production cut deal would be re-visited.

Ultimately neither Russia nor Saudi Arabia could afford to burn their cash reserves at the rate they were, coupled with the downturn in global financial markets due to the COVID-19 virus. In basic oil economics terms, Russia has a budget breakeven price of US\$40 per barrel and Saudi's is US\$84 per barrel. The oil price currently hovers around US\$26-US\$29 per barrel so this was not sustainable in the long term. It would have been an unwinnable war for both countries, if protracted.

Following days of discussions, OPEC and its oil producing allies finalised a historic agreement to cut production by 9,7 million barrels per day, starting on 1 May 2020.

A Crude-Awakening: The COVID-19 Oil Price War...continued

Oil is a resilient commodity and global reliance on it has not tired since the oil economy emerged in the 19th century.

This is the single largest output cut in history. The agreement ends the Saudi Arabian-Russian oil price war that broke out at the beginning of March. However, despite the record size of the production cut, some fear it's still not large enough to combat the drop in demand but the agreement will at least offer a temporary relief for the energy industry and the global economy. OPEC will meet again on 10 June 2020, via videoconference, to determine further actions which may be necessary to balance the market.

It is not the first time the oil price has fallen as dramatically as it did, and it certainly will not be the last. Oil is a resilient commodity and global reliance on it has not tired since the oil economy emerged in the 19th century. Manufacturing of well over six thousand products are derived from crude oil production and its refining process and on a global scale the primary energy consumption derived from oil and gas is approximately 373% more than global energy consumption from wind, solar and other renewables combined.

In frontier jurisdictions in sub-Saharan Africa, such as Namibia and South Africa, upstream regulatory authorities will need to work closely with oil companies so as to ensure that these investors are able to continue their investment in these non-producing jurisdictions, notwithstanding the drop in global demand caused by the COVID-19 virus and crippling oil price. To this extent regulatory authorities may need to consider allowing oil companies the opportunity to defer work program activities until such time as time as the world has come to grips with the COVID-19 virus and the oil price settles.

The CDH oil and gas team have an abundance of experience in the upstream oil and gas sector in both Namibia and South Africa and with upcoming wells planned in both these jurisdictions regulatory certainty and a good fiscal package for upstream investors is now more important than it has ever been.

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