

General overview on the oil and gas environment in Mozambique

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In 2012, Mozambique has emerged as a new giant in natural gas with the discoveries of more than 100 Tcf mainly in the offshore Rovuma Basin.

Due to these major discoveries made by the operators leading the exploration activities in Areas 1 and 4 of the Rovuma Basin (Anadarko and ENI, respectively), it was understood that the volume of proven gas reserves justifies construction of a liquefied natural gas (LNG) facility on the northern coast of Mozambique. These two companies are already making efforts to develop a LNG project that will receive gas from the offshore fields and pre-treat and process it in preparation for storage and export. Although, it has been made public that most of the gas from the Rovuma Basin will be sold on the international market preferentially at the Asian countries, the Government of Mozambique (GoM) is also concerned and keen to supply the national market. Example of this concern is the Natural Gas Master Plan for Mozambique, enacted by the GoM and that outlines scenarios for utilisation of the natural gas once production starts in 2018.

The existing petroleum legislation

Under the existing petroleum legal regime, the state reserves the right to participate in petroleum operations in which any legal entity is involved and is, even up to its decision to participate in a commercial discovery, exempt from payment of any costs of the said operations (carried-forward interest scheme). The decision on the participation of the state in any given project may be made at any stage under the terms to be established by contract between the state and the holder of the rights. The company Empresa Nacional de Hidrocarbonetos (ENH) is the state owned oil company charged with the mission to convert itself into a competent company with a profitable portfolio of business activities covering oil and gas exploration and production, gas transmission, distribution and gas utilisation and to optimise the value that can be generated for Mozambique through commercial participation in exploration and production as well as in the total petroleum value chain. Currently, ENH participates in exploration activities, with carried interest, in association with oil companies, and is currently a stakeholder in the LNG Project.

Petroleum operations covered by the law are subject to a prior concession contract with the State and are divided into exploration, appraisal and production and oil and gas pipelines. The concession is awarded, as a rule, through public tender and by simultaneous or direct negotiation, in certain cases exclusively provided for in the Petroleum Operations Regulation.

Concession contracts for petroleum operations are awarded through a public tender process, pursuant to which applications for concession rights must be addressed to the Ministry of Mineral Resources and filed at the INP, however, the GoM can negotiate the

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grant of such concession contracts directly with interested parties:

- if a public tender process has been unsuccessful;
- to find a replacement concession holder in case of early termination of a petroleum concession contract; or
- if it is necessary to connect two adjacent concession areas for technical or economic reasons.

Applications must contain the following information:

- the name, address and nationality of the applicant. In the event the applicant is a foreign entity, the identification of its representative in Mozambique will be required;
- a description of the applicant's nature, including identification of and the relationship with any parent company or other affiliates, location of incorporation and registration, identification of the members of the applicant's board of directors, and the location of their residence and respective citizenship;
- the relevant experience of the applicant in the oil and gas industry, and in particular in the areas of drilling, production and transportation of oil and gas in similar circumstances to those in which the applicant intends to undertake its activity in the applied-for area, as well as its experience in oil and gas production, refinery and trading activities;
- a description of the applicant's technical and operational capacity, including its abilities for research and development;
- a description of the organisation and the technical resources that the applicant will have available in Mozambique or in any other location for performing the activities; and
- the financial situation of the applicant, including its share capital, shareholding structure and financial documentation (including the applicant's last three annual financial reports and accounts, as well as those of the parent company, if applicable).

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Revision of petroleum legislation

The above context also led the GoM to start a process of reviewing the existing petroleum legislation in order to make it appropriate to the international standards of the oil and gas regime.

In fact, the Council of Ministries has already approved the proposal of the revised draft of the revised Petroleum Law, and has submitted it to Parliament for further ratification (that is expected to occur during the parliamentary session that is currently taking place, which is due to last until July 2014).

Since no further material amendments to the revised draft submitted to Parliament are expected, some of the most relevant changes to the Petroleum Law deal with the following matters:

(i) the creation of a new type of concession contract – construction and operation of infra-structures, which grants its holder with the right to build and operate infra-structures for petroleum operations, such as processing and conversion, which are not covered by an approved exploration and production development plan, and that allows to accommodate the implementation of future LNG projects;

(ii) the stabilisation and respect of acquired rights under already approved exploration and production concession contracts (EPCCs);

(iii) the total or partial transmission of rights and obligations granted under a concession contract, to an affiliate or third party, which must be done accordingly with the Mozambican legal system and subject to a GoM approval, also applicable to other direct and indirect transmissions of participating interests in concession contracts, including the transfer of shares or other modalities of participations which may determine the decisive control of the entity which holds the rights under a concession contract. The rationale of this legal provision, in line with the recently approved Regulations of the Mega Projects Law, which establishes the guiding rules for the process of contracting, implementing and monitoring undertakings of public-private partnerships (PPP), large-scale projects and business concessions, refers to a recent trend in which the GoM is seeking to guarantee that the sale of shares in oil, gas and mining companies whose assets are in Mozambique should bring financial benefits to the country, trying to avoid situations where such sales often take place outside Mozambique and sometimes the GoM is not even informed about it, although the company shares have become valuable precisely because of the Mozambican assets;

(iv) the obligation imposed to the holders of rights to conduct petroleum operations to inform the GoM of any discovery in the concession area within 24 hours, as of the date of discovery, and constitute a fund for the closing and decommissioning of the infra-structures;

(v) the possibility for the National Oil Company (Empresa Nacional de Hidrocarbonetos) to enter into international arbitration;

(vi) the necessary institutional and inter-sectorial articulation between the governmental entities of the sector.

A final discussion with the Parliament with the stakeholders is expected to take place before the end of May and the draft Law shall be submitted to approval during this legislative session.

LNG project

As mentioned above, a project for the construction of LNG facilities in the northern Mozambican province of Cabo Delgado is currently being discussed which, if implemented, in principle, will allow the first exports of LNG to take place in 2018.

The LNG project will require an investment of between \$25-30 billion, which represents by far the largest investment made in Mozambique soil. It is expected that the onshore processing units of the LNG project will produce between 3,000 and 5,000 barrels of LNG/day, during the projected 30 year life span of the project. Anadarko and ENI are working together to develop the processing facilities and eventually to export the gas. The main markets are expected to be Japan, India, China and potential consumers in the Far East. Production wells must be drilled, and pipelines laid on the bed of the sea to carry the gas to land. In addition to the treatment and liquefaction plant, a port must be built for use by the cryogenic vessels that will move the LNG to the export markets. An airport and housing for the work force are also among the infrastructures that are to be built. The Anadarko/ENI plans will turn Mozambique into one of the world's main producers of LNG. The 30 year life span of the project is said to be a conservative estimate and the discovery of further reserves of natural gas could extend it.

One of the major points of discussion in Mozambique is the nature of the LNG activities and their qualification as a petroleum operation in order to evaluate what type of instrument should govern the project, i.e. whether the project can be developed under the existing Exploration and Production Concession Contracts (EPCC) or whether it requires a separate instrument that awards and regulates the activities to be undertaken.

The applicable Mozambican law is silent in respect of the regulation of LNG facilities, namely in relation to the legal instrument that is to be used to govern LNG underlying activities either onshore or offshore. At present, the Government's opinion is that the offshore liquefaction (floating LNG) is still covered by the existent EPCCs, opinion that we in fact share. However, the onshore liquefaction activities are more complex from a local content perspective and the Government of Mozambique is been consistent in having a separate legal regime from the EPCCs, to be established through a competent legal instrument.

Our understanding is that, notwithstanding the legal instrument selected, the same principles, which are applicable to the administrative nature of the EPCC are also applicable to the LNG project, notably:

a) The undertaking of activities of liquefaction of gas requires the exploration of natural resources that belong to the public domain; and

b) Consequently, such activities can only be granted for exploration to private entities by means of a concession agreement or a license. The authority vested with powers to administer or regulate the exploration and development of oil and gas in accordance with the Petroleum Law is the Ministry of Mineral Resources. The National Institute of Petroleum (INP) is considered to be the regulatory authority for the petroleum operations of exploration, production and transport of hydrocarbons.

The discussions towards the approval of the legal instrument that will suit better the interests of the Government of Mozambique and of the operators of Area 1 and 4 are still ongoing. From the Government's perspective the LNG project will create the possibility to significantly and materially reduce the absolute poverty Mozambican indexes.

On the other hand, the Government of Mozambique is aware of the potential and added value that will arise from the implementation of the LNG project from a local content perspective.

One of the GoM's strategic objectives is to encourage the involvement of Mozambican private enterprises in petroleum operations. As part of this policy, the GoM will give preference to Mozambican legal persons (being Mozambican registered companies whose capital is more than 50% owned by Mozambican persons) and to foreign legal persons associated with Mozambican legal persons.

The existing Petroleum Law states that companies must "give preference to Mozambican products and services whenever they are competitive in terms of price and comparable in terms of quality and supply", while the Petroleum Operations Regulations provides that "the procurement of goods and services is made by means of public tender" and "the operator shall give preferential treatment to the purchase of local goods and services when such goods and services are internationally comparable in terms of quality, availability, quantity required, and are offered at prices inclusive of taxes not higher than 10% of the available imported goods".

Examples of local content provisions can also be found in the Mega Projects legislation, which stipulates that the PPP investment must benefit the Mozambican economy, create jobs for Mozambicans, offer opportunities for technology transfer to locals and help build local small and medium enterprises.

The Public Procurement Law contains nationality criteria to favour local firms, since it requires tenders to either restrict participation based on nationality or provide a preferential margin to national bidders or nationally produced goods.

As one can see, the applicable legislation is somehow vague and in general only contains general principles on local content, notwithstanding, we may advance that, based on our experience and to the best of our knowledge, the GoM's stance has been to promote and encourage the involvement of Mozambican companies in these projects (notably local suppliers) and, for this purpose, it has been understood that a Mozambican company is the one that has the majority of its shareholding structure owned by Mozambican natural/legal persons.

Regarding the terms of specific fees or taxes levied by the GoM on a transfer or change of control, the Mozambican parliament recently passed an amendment to the Corporate Income Tax Code, stipulating that sales of Mozambican assets held by non-resident entities will be taxed at 32% without consideration for the period they were held. This amendment provides that, regardless of the place where the transaction took place, the proceeds obtained from the assignment, directly or indirectly, paid or free of charge, between non-resident entities, of shares or other participating interests or rights, involving assets located in Mozambican territory, are considered to be obtained in Mozambique and, hence, are subject to the tax rate above mentioned.

Employment of foreign citizens

From a labour perspective, the regime applicable to the employment of foreign citizens under the Petroleum Law and Mining Law is the quota regime that establishes limitations for the hiring of foreign citizens in favour of the local workforce. The failure to observe this quota regime is punishable by suspension of the foreign employee and a fine equivalent to five to ten times the monthly wage of the employee. Unlike other jurisdictions, the Mozambican legal system does not require a mandatory training fund for the local workforce.

This legal regime is applicable to all domestic and foreign employers, and all foreign employees working in these sectors, and provides a regime of quotas for the employment of foreign citizens under which employers may employ foreign citizens by simply giving notice of the employment to the Ministry of Labour, or an entity to whom the minister has delegated this competency, within 15 days after the admission of the employee, subject to the following quotas:

- 5% of the total number of employees in large enterprises (an enterprise employing more than 100 employees);
- 8% of the total number of employees in medium-sized enterprises (an enterprise employing more than 10 but not more than 100 employees); and
- 10% of the total number of employees in small enterprises (an enterprise employing up to 10 employees).

If the enterprise has already fulfilled the quotas, it is possible to employ foreign citizens by means of requesting a work authorisation from the Ministry of Labour. In these cases, the admission of the foreign citizen shall only proceed if the employee has the required academic and professional qualifications, and it is proved that there are no nationals with such qualifications.

In petroleum or mining investment projects approved by the GoM (through the Investment Promotion Centre) that contemplate the employment of foreign citizens in a greater or smaller percentage than those foreseen above, work permits shall not be required, and it shall be sufficient for notice to be given to the Ministry of Labour within 15 days after the foreign citizen enters into Mozambique.

Finally, the law also provides for short-term work, which is considered to be work performed by a foreign citizen that does not exceed 180 days a year, continuous or interrupted.

Short-term work does not require any work authorisation, it being only necessary to remit, within 15 days following the arrival of the foreign citizen to the country, a communication to the Ministry of Labour mentioning, inter alia, the identity of the employee, his or her qualifications, a reason for hiring him or her, the activities that will be performed, and dates when he or she will be in the country.

Recent trends

With reference to recent trends in the Mozambican jurisdiction, the bill revising the current Petroleum Law was approved by the GoM in April 2013 and has been submitted to the Mozambique Parliament. It is expected that the Parliament will give its approval during the course of the present parliamentary session, which is due to take place until July 2014, hence the new Petroleum Law may enter into force still this year. In place is also the review of the Labour Law for the Petroleum and Mining Sectors. This is expected to be followed by a revision of the fiscal regime applicable to the oil industry, since the intention of the GoM is to compile in a single document, as much as possible, the main fiscal terms for use in future oil projects, notably regarding matters such as royalties and corporate income tax. Furthermore, the INP announced that, in principle, it will launch its fifth oil and gas bidding round in 2014, which will mostly consist of offshore blocks. INP is only waiting for the approval by the Parliament of the new Petroleum Law and subsequent entry into force, in order to proceed with the above said bidding round.

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Taciana Peão Lopes has 16 years of experience providing legal and regulatory advice to private companies, government agencies and state owned corporations throughout Mozambique. She has a solid understanding of PPP (public-private partnership) laws in Mozambique, which includes experience of initiatives such as BOT (build-operate-transfer), BOOT (build-own-operate-transfer), DBOOT (design-build-own-operate-transfer), foreign investment, project financing and public tenders in areas of mining, energy, oil and gas, transport, port, rail, tourism and commercial infrastructures.

Her main areas of work are oil and gas, energy, mining and infrastructure legislation and she is an expert on concession matters related to this sectors.

Taciana has been actively involved in the the LNG project in northern Mozambique and all other major infrastructure projects in Mozambique, namely public-infrastructure projects and other forms of public-private collaboration and private finance initiatives (PFI).

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Márcio Paulo joined the energy, natural resources and infrastructure where he has been advising in the areas of infrastructures, energy, gas and oil and mining, in 2011.

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Gisela's experience includes:

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- Negotiation, structuring of the transaction, drafting of legal instruments and agreements of Renewable Wind Energy Project;
- Negotiation, structuring of the transaction, drafting of legal instruments and agreements of the Ressano Garcia Power Plant Project, in Ressano Garcia (II), a 200 MW natural gas fired power station;
- Negotiation, structuring of the transaction, drafting of legal instruments and agreements of the Búzi Power Plant Project, in Sofala, a 350MW natural gas fired power station.