

General overview on the regulatory framework for the petroleum industry in Mozambique

Couto Graça & Associados in Maputo provide an introduction to oil and gas regulation in Mozambique

All petroleum resources located in the soil, subsoil, inland waters, territorial sea and continental shelf and in the exclusive economic zone are the property of the State. The State controls the prospection, exploration, production, transport, commercialization, refining and transformation of liquid and gas hydrocarbons and their derivatives, including petro-chemical and LNG and Gas for Liquids (GFL) activities.

Control of the country's upstream oil industry rests with the state owned oil company Empresa Nacional de Hidrocarbonetos de Moçambique (ENH), which has exclusive rights to explore for and develop petroleum in Mozambique and is permitted to exercise these rights in association with foreign investors.

As per the recently enacted Petroleum Law (which entered into force in August 18 2014), ENH is responsible to participate in all petroleum operations and the respective stages of the activities, from prospecting, exploration, production, refining, transport, storing and commercialisation of oil and gas and their derivatives, including LNG and GTL inside the country or abroad, and is also responsible to manage the oil and gas quotas destined for the development of the national market and the country's industrialisation. Any investor interested in the exploration of petroleum resources in Mozambique shall enter into a partnership with ENH.

The Petroleum Law also provides that the State shall ensure that no less than 25% of petroleum produced in the country be dedicated to the national market.

The two key regulatory and oversight bodies responsible for regulating petroleum activities are the Ministry of Mineral Resources and Energy and the National Institute of Petroleum (INP).

In addition, the Petroleum Law provides that a new authority was created to oversee extracting industries (High Authority for the Extractive Industry), nevertheless the Petroleum Law is silent as to what the powers of such authority shall be. In particular, it is uncertain whether it will be a regulatory authority or just an ombudsman, as well as to what extent its role and powers will not conflict or overlap with those of the National Petroleum Institute.

Applying for petroleum rights

Petroleum operations shall be carried out via a concession contract following a public tender, nonetheless it shall arguably be possible to have competitive award or direct award following a failed public tender, the early termination of prior concession agreement or a unitization.

The conduct of petroleum operations is subject to the prior execution of a concession contract or other form of contract in accordance with the Petroleum Law, which grants rights of:

- a) Reconnaissance;
- b) Exploration and production;

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c) Construction and operation of oil pipeline or gas pipelines systems;

d) Construction and operation of infrastructure.

A reconnaissance concession contract grants the non-exclusive right to carry out preliminary exploration work and assessment operations in the concession contract area, through airborne, terrestrial and other surveys, including geophysical, geo-chemical, paleontological, geological and topographical studies. A reconnaissance concession contract is executed for a maximum period of two years, non-renewable, and permits the drilling of wells to a depth of 100 meters below the surface or the bottom of the sea.

An exploration and production concession contract grants an exclusive right to carry out petroleum exploration and production, as well as a non-exclusive right to construct and operate oil pipelines or gas pipelines systems for transportation of crude oil or natural gas or infrastructure for liquefaction of gas produced from the concession contract area, except where access to an existing oil pipeline or gas pipeline system or other existing infrastructure is available on reasonable commercial terms. The contracts entered into between legal entities with the purpose to submit a request for rights or for carrying out petroleum operations are subject to the approval of the Government. The exclusive right to petroleum exploration, under an exploration and production concession contract, will not exceed 8 years and shall be subject to the provisions regarding abandonment of areas. In the event of a discovery, the holder of an exploration and production right may maintain the exclusive right

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to complete the operations initiated within a specified area, in relation to the exploration period, for completion of the work schedule and commercial value assessment or determination and to allow the petroleum development and production.

The holder of an exploration and production right may maintain, in accordance with the development plan approved by the Government, the exclusive right to develop and produce oil and gas in the development production area, subject to renewal for equal or shorter periods, as it is more beneficial for the national interest.

An oil pipeline or a gas pipeline system concession contract grants the right to construct and operate oil pipeline or gas pipeline systems for the purpose of transporting crude oil or natural gas, in those cases that such operations are not covered by an exploration and production concession contract. An oil pipeline or a gas pipeline system concession contract shall be accompanied by the relevant development plan, which is an integral part of the concession contract.

The concession contract for the construction and operation of petroleum infrastructure grants the right to construct and operate infrastructure for petroleum operations, such as processing and conversion, which are not covered by an approved exploration and production development plan.

The construction and operation of an oil pipeline and gas pipeline system, as well as the concession and operation of infrastructure, are enabled through a concession contract following a public tender.

Entities entitled to perform exploration and production activities

Mozambican or foreign legal entities that are registered in Mozambique and who demonstrate that they have the technical capability and adequate financial resources for the effective conduction of petroleum operations may be holders of the right to carry out petroleum operations.

Foreign legal entities which directly or indirectly hold or control legal entities that own rights under a concession contract, shall be established, registered and administered under a transparent jurisdiction.

The applicants for rights regarding petroleum operations, in the form of a commercial company, shall, together with the application, deposit a document showing evidence of the incorporation of the company, including the identification of the shareholders and the value of their participations.

Mozambican legal entities as well as foreign legal entities that associate with Mozambican legal entities shall have a pre-emption right in the granting of concession contracts.

The State reserves the right to participate in petroleum operations in which any legal entity is involved. The participation of the State may

occur during any phase of the petroleum operations in accordance with the terms and conditions to be established by contract.

Although the Petroleum Law does not establish a maximum participating interest, the Mega Projects Law establishes a maximum 20% interest in the share capital of the entity that has been awarded with the concession. The government is further entitled to negotiate a free carry of its participating interest in such entities in at least 5% of the share capital, at any stage of the process.

Local content provisions

The state typically participates in petroleum operations through the state-owned national oil company ENH and usually holds a minority stake (usually 10-15% in petroleum concessions), typically granted to ENH on a free carry basis.

The Petroleum Law states that the acquisition of goods or services by the petroleum operations right holders, above a set amount, must be made through public tender and this must be published in the means of communication of greater incidence in the main newspapers of the country and on the internet page of the respective right holders. Natural or legal foreign entities that provide services to the petroleum operations must associate to single or collective Mozambican entities. In the evaluation of tender, the quality of the services, the price, delivery date and offered guarantees must be taken into account. The petroleum operations right holders must give preference to local products and services when comparable, in terms of quality, to the international materials and services that are available in time and in the quantities required and when the price, including taxes, is not over by 10% to the price of the available imported goods.

Moreover, the Petroleum Operations Regulations also 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 other local content provisions can also be found in the Mega Projects legislation, which stipulates that PPP (public-private partnership) 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 new Petroleum Law seeks to remedy certain loopholes in the previous legal regime, in particular, concerning the restrictions on transfers of interests in oil and gas concessions.

Under the previous legal regime, the Government of Mozambique's consent was only required for transfers of interests in petroleum concessions by the concession holder and not in case of a change of control of the concession holder. The new Petroleum Law now clearly states that any change of control of a concession holder also requires the Government's prior consent. In the context of a project financing, the lenders may wish to have the Government agree in a direct agreement to certain objective criteria relating to the identity of a transferee which, if satisfied, would constitute consent of the Government. Such objective criteria could relate to technical competence, financial capability, upstream and/or LNG ownership and/or operations.

From our experience, normally concession contracts contain a clause stipulating that every person who constitutes the concessionaire may assign to another person its rights and obligations or an undivided proportionate part, including direct and indirect transfers of interest or participation under a concession contract, such as assignment of shareholdings or any legal instrument that provides or may provide decisive control over a person constituting the concessionaire or its participating interest under a concession contract.

Such an assignment shall require the prior written consent of the Minister of Mineral Resources, as per the provisions of the petroleum legislation.



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CGA–Couto, Graça & Associados is a leading Mozambican Law Firm, highly regarded both within and outside Mozambique, due to the quality and value of the legal services it renders to clients.

The Firm has legal expertise in the various fields of law, public and private, and has rendered services to companies and institutions, both profit and non-profit oriented, which are operating in the country's multiple sectors of activity. Organizations that have benefited from such services and others specialized in the legal market research, considered CGA a highly recommended law firm, whose legal services have been relevant and valuable in supporting their businesses, business strategy and operations. The Firm is renowned for having a nun matched experience in liaising Government owned institutions and private companies in relation to investment projects.

CGA is keen to pursue its vision, mission and values: a long-standing, leading and highly recommended legal service provider in the Mozambique market, rendering state-of-the art legal assistance with conduct inspired on professional ethics, innovation and quality for the benefit of clients. A firm that values and rewards good performance of its working professionals. A firm that is responsive and acts in accordance with public policy, relevant social values and the law.

Inherited from legal service providers lasting more than a decade, CGA values are foundational, having a bearing on the day-to-day work of its lawyers.

CGA professionals perform their duties to the best of their professional knowledge and experience and ensure confidentiality with any information related to the client and its businesses.

The Firm, with seven partners a team of lawyer's associates, and some of the most are established leading lawyers for corporate, finance and commercial transactions.

Chairman Pedro Couto, who focuses on projects finance, banking, company restructuration, PPP's, oil and gas, and Managing Partner Jorge Graça, who has a strong track record in regulatory, compliance, concessions and legislative issues, are leading a team of experienced partners, among whom, Telmo Ferreira, Faizal Jusob and Rita Furtado are in charge of areas such as contracts, corporate, capital markets, foreign investment, natural resources, energy and infrastructures.

CGA also has an association with a top tier Iberian firm Cuatrecasas Gonçalves Pereira and is member of Lex Africa, the largest and long lasting pan African leading law firms.

Areas of practice & sectors:

The firm's core business includes the following main areas:

- Contracts, concessions, "project finance", investment, tax and exchange control;
- Corporate – private and public;
- Banking, finance and insurance;
- Energy, Natural Resources & Infrastructure;
- Legislative research and drafting; law development and implementation review;
- Land and Environment;
- Labour and Social Insurance;
- Litigation – courts and arbitration;
- Intellectual Property.

The firm's main focus sectors are the following:

- Bank, credit, finance, insurance and stock market.
- Energy: Oil, Gas; Renewable Energies and Power.
- Mining Industry.
- Infrastructures (Airports, Ports, Railways, Roads and Construction Works).
- Transports (Aviation, Maritime and Land).
- Agro-Industry and Forestry.
- Industry and Trade.
- Tourism and Conservation.
- Public Sector.
- International Institutions.

Although the petroleum legislation is silent in respect of a change in control, from our experience, any direct disposition of greater than 50% of the legal or beneficial ownership of voting securities of a concessionaire, by way of a sale, voting trust or otherwise, that results in a transfer of the effective control of the concessionaire in question, would be deemed a transfer, and, thus, would require the prior approval of the Minister of Mineral Resources.

The law is silent with respect to time frames to obtain the required approval for the above-mentioned transactions; nevertheless, in our experience the approval process tends to be quite simple and rapid as long as all requirements are fulfilled (e.g., evidence of the technical and financial capacity of the transferee).

Stock exchange

The new Petroleum Law requires all petroleum companies operating in Mozambique to be listed on the Mozambican Stock Exchange.

The law does not provide any further details of the time frames for the listing or how much of the share capital is to be listed.

This will need to be understood more fully by investors so they can take it into consideration in structuring their investments. For instance, investors looking to develop projects on a project finance basis will need to understand the impact of this requirement on the share security and completion support available to lenders.

Although the Petroleum Law does not expand on this matter and the new regulations are still to be approved, we may refer to the Mega Projects Law that states that the financial benefits for Mozambique of a Business Concession undertaking shall include the participation reserved for sale, through the stock market, in favour of the economic inclusion on commercial market terms, preferably of Mozambican natural persons, in the share capital of the undertaking or in the joint venture equity, whether or not foreign investment is involved, guaranteed by:

- a) the State or other public entity appointed thereby, in a percentage not less than 5% nor greater than 20% of the referred capital; or
- b) the entity implementing the undertaking, of the same level of participation, for unconditional sale.

Hence, we understand that the Mega Projects Law provides some answers, although we expect that the regulations to come will expand on this requirement.

Oil and gas for internal consumption

The Petroleum Law now provides that the Government must ensure that at least 25% of the oil and gas produced in the country is channelled into the domestic market for consumption.

The terms under which the acquisition of such a quota of oil in gas shall take place will be regulated by the Government.

Labour

Decree 63/2011 of December 7 2014, provides the legal regime and the mechanisms and procedures for the employment of foreign citizens under the Petroleum Law and Mining Law. 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 em-

ploy 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 government (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.

In summary, the quota regime 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.

Recent Trends

The Ministry of Mineral Resources and Energy has developed an EITI Compliant Mining Cadastre Portal to improve transparency and promote investment in the Mozambican mining and oil sector (<http://portals.flexicadastre.com/mozambique/en/>). At present, all mineral tenure and state mining contracts are available for viewing. Access to this portal is not subject to the payment of any fees.

Through Law 27/2014 of September 23 2014, which establishes the specific regime of fiscal benefits and taxation for petroleum operations and entered into force on the January 1 2015, the Government operated a revision of the fiscal regime applicable to the petroleum industry aiming to compile, in a single document and as much as possible, the main fiscal terms for use in future petroleum projects, notably regarding matters such as royalties and corporate income tax.

In the meantime, the INP launched, on October 23 2014, its fifth oil and gas bidding round. A total of fifteen blocks are included comprising some 76,800 square kms of acreage in the offshore Rovuma, offshore Zambezi, offshore Angoche, onshore around the Pande-Temane concession and onshore Palmeira areas. The 5th Licensing Round is scheduled to close on April 30 2015.

The Petroleum Law entered into force on the August 18 2014 and contains a clause stating that the Government was responsible for regulating all matters in the Petroleum Law within 60 days, as of the day of its publication at the Government Official Gazette. However, the sixty days have already passed and the Government has not yet approved the regulations over the Petroleum Law. It is expected that this will take place within the coming weeks and that a new Petroleum Operations Regulation will enter into force shortly after.

- Lastly, through Decree Law 2/2014, which entered into force on December 2 2014, the Government of Mozambique approved a special legal and contractual regime to be applied to the Rovuma Basin Project.

This Decree Law was much anticipated and clarifies many issues raised in respect to the activities to be undertaken within the Offshore Areas 1 and 4 of the Rovuma Basin, such as LNG sales, procurement of goods and services, financing structures, exchange control, stabilisation and land rights, among others.



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Chairman and the head of the Department of Energy, Natural Resources and Infrastructures at Couto Graça & Associados (CGA).

Pedro has 21 years of experience as a general counsel for private companies, state organisations and corporations throughout Mozambique and is involved in initiatives such as BOT, BOOT, corporate restructuring of companies, foreign investment, financing, privatization, and public procurement (transport, mining, aviation, energy, oil, gas, port, rail, and commercial infrastructure). He is an expert in project finance and finance structuring having participated in most of the key power and Infrastructure projects in recent years in Mozambique.



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Paulo Ferreira has six years of litigation experience in civil, commercial, labour and administrative matters, including in cases submitted to judicial and arbitration tribunals in which he acted as an advocate. He joined the energy, natural resources and infrastructure practice in 2011 and has been advising in the areas of infrastructure, energy, mining and natural resources.

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- Negotiation, structuring of the transaction, drafting of legal instruments and agreements of the Chokué Power Plant Project, in Chokué, a 40MW natural gas fired power station.



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Márcio Paulo has five years of experience in general corporate and commercial law and banking and finance fields.

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- Negotiation, structuring of the transaction, drafting of legal instruments and agreements of the Chokué Power Plant Project, in Chokué, a 40MW natural gas fired power station.



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Gisela Graça has experience in civil, commercial, labour, administrative matters and academic research. She joined the energy, natural resources and infrastructure practice in August 2013 and has been advising in the areas of infrastructure, energy, mining and natural resources.

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- Negotiation, structuring of the transaction, drafting of legal instruments and agreements of a Photovoltaic Energy Project in Nampula;
- 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;