SITUATION
ANALYSIS

# The State of Oil and Gas in East Africa

For African oil and gas markets, the last few years have been turbulent. Traditional players and long term oil dependent countries such as Nigeria and Algeria have seen the price of oil plummet from an average of $90 - $100 a barrel to half of that (and less) and as a result, their economies have slumped. New players, such as Kenya, Uganda and Tanzania, who had hoped to benefit from the rush of oil and gas discoveries in their countries, have been put in an uneasy position. Firms that could once rely on ever increasing oil prices to take on riskier projects with long term pay-outs are beginning to focus on more reliable oil fields in more established jurisdictions. With the above in mind, EALS teamed up with the team at the Africa Legal Network to develop a brief on the State of Oil and Gas in East Africa.

EAST AFRICA LAW SOCIETY

# The State of Oil and Gas in Kenya

*(By Sonal Sejpal, Njeri Wagacha and Edwin Baru of Anjarwalla & Khanna)*

The exploration of oil in Kenya begun in the 1950s and according to the National Oil Corporation of Kenya, of the 30 wells sunk between 1960 and 1992, only 5 encountered signs of oil staining or oil shows. In 2012 however, Tullow[1] announced commercial finds in blocks 10BB and 13T in the arid northern county of Turkana. In total, Kenya is currently estimated to have recoverable reserves of up to 750 million barrels but it is thought that the recoverable estimates could be in excess of 1 billion barrels. In addition, a number of gas and liquid hydrocarbon deposits finds have been made off the Kenyan coast but none have so far proven to be commercially viable[2].

To actualise the full benefits of the oil finds, Kenya will have to overcome a number of challenges. One of these challenges is that Kenya plans to export all its crude. The oil producing fields are located in a remote and marginalised area of the country with limited infrastructure. This is further complicated by the fact that Kenya's crude is waxy and requires heating during transportation and storage which limits its yield and increases investment costs in relation to transport and storage.

As demonstrated by the well documented slump in the price of oil, producers cannot continue assuming that the price of oil will continue rising. The solution for oil producers will therefore be to focus on efficiency and cost cutting. In this regard, it has been reported that Kenya intends to build an 865 kilometre pipeline at a cost of approximately US$ 2.1 billion, linking the production fields to Lamu Port. The country was forced into building the pipeline on its own after Uganda abandoned initial plans for a joint pipeline with Kenya and opted for a pipeline through Tanzania. Uganda cited cost and security concerns as the reason.

## Oil and Gas Framework in Kenya

The oil and gas industry in Kenya is governed by the Petroleum (Exploration and Production) Act, Chapter 308 of the Laws of Kenya (PEPA) and the Petroleum (Exploration and Production) Regulations, 1984 promulgated under the PEPA. The PEPA which was enacted in 1984 is generally considered as outdated and the country is in the process of undertaking extensive policy, legal, and institutional reforms of its extractive and energy industries in line with the Constitution of Kenya 2010. This review has seen Parliament debate the Petroleum Bill 2015 and the Energy Bill 2015. Once passed, the Petroleum Bill, 2015 will usher a new and hopefully more attractive regulatory regime for oil and gas activities in Kenya

## Current Production

Kenya has signed a Production Agreement with Tullow which will trigger the commencement of the early oil scheme. Through the early oil scheme, Kenya intends to move between 2,000 and 4,000 barrels of oil per day from the production fields to the coast for export using trucks and rail. The crude will be stockpiled at the Changamwe Oil refinery, or elsewhere at the Coast, which has been converted into a storage facility until there are sufficient quantities for export. The Government has stated that though the early oil scheme is expected to be loss making, the scheme shall help build infrastructure and provide well data for planning for full field development. Many have however questioned the wisdom in pursuing the early oil scheme arguing that the state should focus on constructing a pipeline before exporting crude given the costs associated with road and rail transport.



1 http://www.tullowoil.com/operations/east-africa
2 https://www.standardmedia.co.ke/business/article/2000164436/australian-oil-explorer-withdraws-from-lamu-basin

## Local Content

Another concern relates to local content and the sharing of benefits with local governments and communities. As mentioned earlier, the discoveries have been made in the northern county of Turkana which has historically been marginalised. In a devolved Government, profit sharing therefore becomes a critical issue between the local government and the national Government. While there have been various legislative attempts to deal with this matter[3], a harmonised local content and benefit sharing regime is required to provide certainty.

## Maritime Border Dispute with Somalia

Another issue likely to affect the industry is the maritime border dispute between Kenya and Somalia. In 2014, Somalia filed a case at the International Court of Justice (ICJ) for the determination of the suit. The disputed area is a triangle off the coast which purportedly has a large deposit of oil and gas. Kenya's position is that the boundary lies on the line parallel to the line of latitude. Somalia wants the boundary as an extension of the land border. The outcome of this dispute could potentially affect a number of licences in the disputed region[4].

## Conclusion

As Kenya works towards becoming an oil producing nation, it is hoped that the price of oil shall remain high enough to enable the profitable development of its oil fields. Tullow and the Government estimate Kenya's breakeven oil price to be USD 39 per barrel which is substantive given the current price of around USD 59, provided the price remains stable and so the future success of Kenya's nascent industry will be in the hands of the international market.

# State of Oil and Gas in Tanzania

*(By Aggrey Ernest and Geofrey Haule of ATZ Law Chambers)*

As with Kenya, the exploration of oil and gas in Tanzania begun in the 1950's, with the first natural gas discovery made in early 1974 in Songo Songo and a second discovery in Mtwara Region (Mnazi Bay) in 1982. These early discoveries make Tanzania the most mature of East Africa's oil and gas producers as it has been producing gas from on and nearshore fields since 2004. In 2010 Tanzania's growth projections were boosted substantially following significant natural gas discoveries currently confirmed at 55 trillion cubic feet (tcf)[5], potentially making the country a significant exporter of gas. Additionally there have been other significant discoveries in Mkuranga, Kiliwani North and Ntorya.

With its wealth of hydrocarbons, Tanzania has embarked on a number of projects to monetise the current 47 tcf[6] in deep-sea gas resources. In 2015 the US$ 1.3 billion National Natural Gas Infrastructure Project , possibly the biggest infrastructure project undertaken in the country whereby a pipeline from Mtwara in the gas-producing southern part of the country to its industrial centre Dar es Salaam, was completed, opening the way for a further expansion of production for domestic consumption. Further, Tanzania has embarked on a project to export Liquified Natural Gas . It is anticipated that the project will cost between US$ 20–30 billion, likely to make it the continent's most capital-intensive infrastructure project ever.

3 including under the Community Land Act, 2015, the Natural Resources (Benefit Sharing) Bill, 2014, the Local Content Bill 2015, the Petroleum Bill, 2015 and its draft Petroleum Exploration, Development And Production (Local Content) Regulations, 2014, these efforts have all been disjointed resulting in conflicts in various laws and confusion.

4 http://www.dw.com/en/kenya-or-somalia-who-owns-the-sea-and-what-lies-beneath/a-19557277

5 https://mem.go.tz/sera-ya-ushirikishaji-wazawa-sekta-ndogo-mafuta-na-gesi-kusisitiza-ajira-kwa-watanzania/

6 https://mem.go.tz/sera-ya-ushirikishaji-wazawa-sekta-ndogo-mafuta-na-gesi-kusisitiza-ajira-kwa-watanzania/

In relation to oil, the Tanzania and Uganda Government have agreed upon the construction of the East Africa Crude Oil Pipeline the proposed export pipeline from Hoima in Uganda for the export of crude from Uganda and other inland fields. It is estimated that the pipeline will be 1,443 kms in length making this a significant project costing over US$ 3.5 billion. But according to an IMF report, once infrastructure is in place and production is under way, annual revenue collections could range between US$3 billion and US$6 billion[7].

## Oil and Gas Legal Framework in Tanzania

The legal framework for petroleum and gas exploration and development in Tanzania was until recently governed by two key laws, the Petroleum (Exploration and Production) Act [Cap. 328 R.E. 2002] (the PEPA) and the Petroleum Act 2008 (the PA 2008). The PEPA governed the upstream petroleum sector, as it related to any naturally occurring hydrocarbon, whether in gaseous, liquid or solid state or mixture while the PA 2008 dealt with the downstream petroleum sector.

From June 2015 the two laws were amalgamated to form one new consolidated legislation; the Petroleum Act, 2015 (the PA 2015). The PA 2015 came into force on 25 September 2015.

The PA 2015 seeks to consolidate and put in place a single, effective and comprehensive legal framework for regulating the oil and gas industry in the country including midstream and downstream gas activities. The PA 2015 also sets up a number of regulatory bodies including an Oil and Gas Bureau and the Petroleum Upstream Regulatory Authority (PURA) which replaces the Tanzania Petroleum Development Corporation (the TPDC). When operationalised, the PURA will be the body responsible for the monitoring and regulation of the upstream segment in Tanzania mainland.

Legislation and regulations supplementary to the PA 2015 have not yet been published. However, once PURA has been established, we understand that the remaining legislation should follow fairly quickly. Until this has happened, the old law and transitional provisions from the PA 2015 remain in place.

## Taxation Regime in Tanzania

The Government, through Finance Act, 2016 (the FA) amended the Income Tax Act, 2004 (the ITA) to introduce a new taxing regime for petroleum operations. The FA's provisions serve as a harmonisation of the provisions set out in the PA 2015 and the relevant provisions set out in the ITA. The introduced regime is more strict than it was prior to the changes and it is geared towards increasing tax collections from the sector.

This tax regime is fairly new; as such it is too early to establish the impact it has had on investment in the sector.

## Local Content

Local content in the Tanzanian oil and gas context refers to the added value brought to Tanzanians through activities of the natural gas industry. These may be measured and undertaken through employment and training of local workforce; investments in developing supplies and services locally; and procuring supplies of services locally. The Government is currently putting in place regulations that will govern local content in the sector, the first draft of the Petroleum (local Content) Regulations, 2016 was published at the end of 2016 for comments from stakeholders.



7 International Monetary Fund, United Republic of Tanzania, Selected Issue, Report IMF Country Report No. 14/121

## Oil and Gas Operations in Zanzibar

Under the Tanzanian constitution, petroleum activities are a union matter and the TPDC is therefore responsible for Production Sharing Agreements (PSA) in Zanzibar. Zanzibar has been resisting this which has created uncertainty in the sector in Zanzibar.

The PA 2015 applies to Mainland Tanzania and Zanzibar[8]. TPDC will still be the National Oil Company for Zanzibar where operations are undertaken within Zanzibar due to petroleum being a union matter, however, PURA will be the regulator in Mainland Tanzania.

Currently we understand that Zanzibar has taken its own concessions and on 14 March 2017 exploration activities kicked off in Zanzibar with a UK firm conducting operations on behalf of United Arab Emirates Company (RAK Gas Company). As, constitutionally, petroleum is a union matter, unless and until the constitution is amended, there is a risk that any PSA granted by the Zanzibar Government is unconstitutional and therefore void.

Tanzania has demonstrated its ability to take on large scale projects with huge financial returns. What it is now seeking to do is ensure that its legislation in this area has the multiple aims of increasing investment, protecting local content and being enforceable not only on the mainland but in Zanzibar as well. The Government of Tanzania has now included in its future plans a revision of the terms and conditions under which oil companies operate to ensure that they benefit Tanzanians.

# State of Oil and Gas in Uganda

*(By Marion Angom and Fiona Magona of MMAKS)*

Uganda is currently described by the World Bank as the hottest inland exploration frontier in the world and the country to watch in the oil and gas space, due to the commercial discovery of an estimated 6.5 billion barrels of oil, 1.4 billion of which are recoverable. Against this backdrop, the major players in the Oil and Gas market are Total E & P Uganda, Tullow Uganda Operations Pty Limited and China National Offshore Oil Corporation (CNOOC) who are all holders of production licences issued in respect of six (6) exploration blocks (the Blocks) in Albertine Graben (located in the western arm of the Great East African Rift, which they operate under the terms of a joint venture in accordance with a Joint Operating Agreement.

With oil production expected to begin in 2020, there has been a hive of activity in the oil and gas sector. Some of the notable developments are discussed below:

## Local Content

The Petroleum (Exploration, Development and Production) (National Content) Regulations 2016 came into force on 6th May 2016 and are intended to ensure participation of indigenous Ugandan entities in the oil and gas sector. In brief, the regulations require any licensee, contractor and sub-contractor to give priority to goods and services that are produced and available in Uganda and which are rendered by Ugandan citizens and companies during procurement. In addition, they are required to reserve the contracts for ring fenced goods and services like security, foods and beverages, hotel accommodation for supply by Ugandan citizens and companies.

8 Although the regulation of operations of the PA 2015 in Zanzibar are to governed and administered by institutions in accordance with the laws of Zanzibar where operations are undertaken within Zanzibar

A Ugandan company is defined as a company incorporated under the Companies Act No. 1 of 2012 and which provides value addition in Uganda, uses available local materials, employs at least 70% Ugandans and is approved by the Petroleum Authority of Uganda. Several concerns have been raised regarding this definition of a Ugandan company as it does not guarantee that indigenous Ugandan companies will benefit from the sector. In effect, the definition seeks to suggest that a fully owned foreign owned entity incorporated in Uganda but employing 70% Ugandans would qualify as a Ugandan entity. This may mean that locally owned companies could be outcompeted by the foreign owned entities when it comes to bidding for contracts and confirming capacity and experience.

The regulations were recently discussed at the 4th National Content Conference on Oil and Gas held in Kampala. The major sentiment at this conference was the need to amend the regulations and ring fence more goods and services for local contractors.

## Issuance of exploration licenses

In February 2015, the Government of Uganda (the GoU) announced the first open competitive licensing round for the Blocks. Armour Energy Limited of Australia, WalterSmith Petroman Oil Limited, Niger Delta Petroleum Resources Limited of Nigeria and Oranto Petroleum International Limited were the 4 shortlisted firms with whom the GoU will negotiate and sign other production sharing agreements.

## Issuance of production licenses

A total of 9 production licenses have been issued so far in Uganda. The first one was issued to CNOOC in 2013. Tullow Uganda Operations Pty Limited and Total were issued with 5 and 3 licenses respectively in August 2016. The issuance of these production licenses was a huge milestone and is expected to fast-track the foreign investment decision of the 3 joint venture companies which is expected by the end of 2017.

In February 2017, Technip, Fluor and Chicago Bridge and Iron Company were awarded a contract for the first phase of the Front End Engineering Design (the FEED) on 2 of the exploration areas. This is intended to continue for a period of 6 months and aims to determine the technical aspects, cost estimates and implementation schedules for the production phase. Upon successful completion, the 2 successful companies will be required to compete for the Engineering, Procurement and Construction contract.

## Oil refinery

The GoU previously entered into negotiations with RT Global Resources for the establishment of a local oil refinery. Negotiations with RT Global Resources failed and the GoU turned to SK Engineering Limited, the alternate bidder. These negotiations also yielded no results. The GoU is currently back to the drawing board in search of a new partner for the oil refinery project. Approximately forty (40) unsolicited bids were received and evaluated last year. Currently they are shortlisted to 4 consortia and the winner is to be announced soon. The project structure has since changed with the GoU now favoring a public led as opposed to a private led partnership. Once completed, the refinery is expected to produce 60,000 barrels of oil per day.

## Crude oil pipeline

The much anticipated crude oil pipeline is now set to run from Hoima in Uganda to Tanga in Tanzania. This was a shift from the agreed position in the Memorandum of Understanding signed between the GoU and the Government of Kenya which preferred the route from Hoima to Lokichar to Lamu in Kenya. The revised decision was taken after feasibility studies showed that the Hoima to Lokichar to Lamu route was more costly and insecure due to potential exposure to Somali Al Shabab terrorist activities along that route.

A FEED study on the pipeline was launched in January 2017. Gulf Interstate, the contractor is required to map out the actual route, technical designs and cost for the pipeline which is currently estimated to cost about $ 3.55 billion. The MEMD received several bids for the crude oil pipeline project that are currently under evaluation.

### The Future

While Uganda waits with bated breath for its first drop of oil in 2020, it is under scrutiny over how it will handle a natural resource that is both considered a blessing and a curse. The question whether Uganda will use its" black gold" to propel her economy to a much desired middle income status by 2020 depends largely on GoU's commitment to among other things prioritize national participation, promote environmental sustainability especially in ecologically sensitive exploration areas and the strategies in place to avert the oil curses that has struck other oil rich nations.

## State of Oil and Gas in Rwanda

*(By Emmanuel Muragijimana and Eric Cyaga of K-Solutions and Partners)*

The potential economic benefits of the discovery of petroleum in Rwanda are becoming more of a reality due to recent preliminary geophysical data that has been generated in the Kivu basin[9]. The prospect of a Kenya–Uganda–Rwanda Petroleum Products Pipeline[10] in the near future to transport oil between these three countries will boost the petroleum industry even further once it has been built.

### Oil and Gas Framework

To take advantage of the tremendous potential of this sector in Rwanda, the Government of Rwanda (GOR) is working to provide the framework for the development of Rwanda's petroleum industry through mutually beneficial cooperation between the GOR and various petroleum exploration and development companies. So far the GOR has implemented the fundamentals of the fiscal and legal framework and has set about establishing how the relationships among actors in the petroleum sector will work vis a vis the institutional frameworks in an environment where there is a need to protect national participation.

The GOR has found it necessary to strengthen the institutional arrangement mandated to promote and regulate the oil and gas sector in Rwanda. The institutional framework takes into consideration the different critical roles of the Government ministries and agencies involved in the implementation of upstream petroleum policy activities. The Rwanda Geology and Mines Authority (OGMR) that was created in 2007 later transformed into the Rwanda Natural Resources Authority (RNRA) has now morphed with the Rwanda Mines, Petroleum and Gas Board (the Board) in order to establish, among others, a government institution with a separate legal personality, financial and administrative autonomy that will focus on Mines, Oil and Gas the country. It is hoped that the Board will build on the progress that had been made previously in the areas of exploration, licensing, inspection and regulation. So far, together with the Rwanda Utilities Regulatory Authority (RURA) it has emphasized the close

9 http://www.theeastafrican.co.ke/business/Ngali-Mining-Rwanda-oil-search-Lake-Kivu/2560-3804790-e28xngz/index.html
10 http://af.reuters.com/article/kenyaNews/idAFL5N0RB08320140910

supervision of companies and persons participating in petroleum activities to ensure that the environment is protected and all legal standards observed.

The complete petroleum value chain starts from the promotion of oil blocks for exploration up to consumption of the extracted oil and has been brought together by the National Upstream Petroleum Policy for Rwanda[11]. It covers promotion, licensing, exploration, development, production of petroleum, transportation, refining and conversion of gas, distribution, marketing and sale of petroleum products.

It is in this context that Rwanda has passed legislation relating to the regulation of petroleum and petroleum products[12] and the governing petroleum exploration and production activities[13]. Pursuant to this legislation, parties are permitted to apply for licenses for the exploration and production of oil and gas as well as trading licenses such as in the construction oil and gas infrastructure, transportation, distribution and retail of oil and gas products. Within this legislative framework, parties may choose to enter in PSC's the GOR under the terms of a concession agreement, a joint-venture, a service contract or an equity participation contract.

Rwanda seeks to attract investment in the petroleum exploration sector and recognizes that private sector investors need to be able to operate profitably and be internationally competitive while petroleum endowment concerns the exploitation of the country's non-renewable resources in the interest of Rwandan people.

Rwanda envisions a secure energy supply by diversifying into new sources including locally produced petroleum. So far, the GOR's key achievements lie in its development of institutional framework and legislation and regulate this burgeoning sector.

## Conclusion – State of Oil and Gas in East Africa

As detailed above, East African countries hoping for investment must offer up attractive and competitive environments through their regulatory, fiscal and licensing provisions.

Despite wide interest from investors, the East African region has a number of drawbacks which could become barriers to investment into the oil and gas sector. For example, the discoveries made in Kenya, Uganda and South Sudan have all been in remote areas, far from the coast and therefore reliable transportation from the oil fields to the export point on the coast becomes a key factor. Although regional and bilateral cooperation would solve such issues, there is a general lack of harmony between the East African countries as signified by the back and forth as Uganda tried to decide whether to strike a pipeline deal with Kenya, or with Tanzania. It will be important for East African countries to seek to work together in order to ensure that all countries in the region benefit from their potentially lucrative natural resource.

That said, oil and gas is East Africa is an exciting area to be in. New discoveries are regularly being made and the future of the industry looks bright – provided that the various governments continue to engage in a predictable and stable way with the industry and its investors.

11 http://www.mininfra.gov.rw/fileadmin/user_upload/new_tender/REP_17th_March_2015.pdf
12 Laws include: Law no 85/2013 of 11/9/2013
13 Law n°13/2016 of 02/05/2016

No. 6 Corridor Area, Off Jandu Road
P.O. Box 6240, Arusha, Tanzania
Tel: (+255 27) 254 3226 /7 (+255 786) 821010
E-mail: info@ealawsociety.org
Website: www.ealawsociety.org
EAST AFRICA LAW SOCIETY