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Lebanon's hydrocarbon licensing regime takes off

CMS Cameron McKenna
Stephen Millar and **Malek Takieddine**

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C'M'S' Cameron McKenna

Major natural gas reserves recently discovered off the coast of Israel have ignited considerable interest in the hydrocarbon potential of the East Mediterranean basin.

Recent discoveries include Tamar near the port city of Haifa (240 billion cubic metres of natural gas) discovered in January 2009; Dalit near the northern city of Hadera (14 BCM) in April 2009; and Leviathan off the coast of Haifa in June 2010, the largest gas discovery in the world within the last decade (approximately 460 BCM of natural gas). In 2010, the US Geographical Survey estimated that the entire Levant basin, encompassing parts of Israel, Lebanon, Syria and Cyprus, may contain as much as 1.7 billion barrels of recoverable oil and 3.45 trillion cubic meters (122 trillion cubic feet) of recoverable natural gas. For comparison, Iraq, ranked as the 11th country worldwide in terms of proven gas reserves, has 3.1 trillion cubic meters of gas.

Lebanon is a small country but it is strategically positioned at the centre of the Levant basin. Unlike other Middle Eastern countries that possess valuable hydrocarbon reserves, Lebanon's earliest attempts in the 1960s and early 1970s to explore for onshore oil and gas did not result in any discoveries. Lebanon today remains a non-hydrocarbon producing country with an economy suffering from the weight of a US$52 billion public debt representing a debt-to-GDP ratio of approximately 130%; among the highest in the world. In an effort to revive hopes of discovering hydrocarbon reserves, Lebanon contracted Norwegian company, PGS Geophysical AS, to conduct offshore 3D seismic surveys. The resulting data was described as showing promising signs.

The new Hydrocarbon Law

In August 2010, Lebanon passed Hydrocarbon (Offshore) Law number 132/2010 (the "Hydrocarbon Law") creating a production sharing system under which oil companies will be granted Exploration and Production Agreements (EPAs). The Government is granted the authority to determine State royalties, area rental fees, cost oil and profit sharing percentages. The exploration and the production phases will be specified in the EPA but may not exceed 10 years and 30 years respectively. Should the EPA set shorter periods, application for extension of the periods may be made provided that the total duration of each of the two phases remains within the above limits. Any such extension will also require relinquishment of 50% of the relevant area. Further, any area not included in any approved development plan must also be relinquished at the end of the exploration phase.

The Hydrocarbon Law provides that each EPA must be entered with no less than three interest holders. It is not clear why the Lebanese legislature chose to make this a requirement of law rather

than leaving the issue to the discretion of the Government as is the case with most EPAs.

Other important provisions of the Hydrocarbon Law include:

▸ A new agency, the 'Petroleum Administration' is to be created to advise the Minister of Energy on, inter alia, marketing the hydrocarbon resources of Lebanon, evaluating applications of oil companies bidding for EPAs, assisting the Minister in negotiating with oil companies and evaluating field development plans. At the time of writing this article, the Petroleum Administration had yet to be established.
▸ The Lebanese State retains the right, once commercial viability is proven, to establish a national oil company with the right to be involved in all petroleum activities. EPAs will likely preserve the right for State participation at a later stage.
▸ All State hydrocarbon revenues will be deposited into a sovereign wealth fund to be regulated by an as yet to be enacted law.

Implementing Legislation

The Hydrocarbon Law will be implemented through the issuance of Government Decrees, 14 of which are currently being drafted by the Ministry of Energy. The decrees are expected to be detailed and comprehensive allowing minimal flexibility in the negotiation of EPA provisions. It is also expected that Cost Oil will be capped and that no signature bonus will be required in the first licensing round.

The Ministry of Energy expects that the decrees will be finalised no later than the end of 2011 and that IOCs will be invited to submit their applications during the first six months of 2012. However, the process of passing laws and decrees in Lebanon, especially those of strategic importance, is often the subject of lengthy and heated debate among various local political parties. An additional factor in Lebanon's progress towards the holding of a first offshore licensing round is the existence of competing claims between Lebanon and Israel in relation to several maritime areas. Israel and Lebanon have been in a state of war for over half a century and recent violent confrontations suggest that the risk of conflict over maritime boundaries and/or hydrocarbon resources remains high. Although these contentious areas constitute approximately only about 2% of offshore Lebanon, maritime border disputes may have a disproportionate effect on the stable progress of petroleum operations in the region.

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