

## Obtaining hydrocarbon licences in the Republic of Cyprus

In recent years the Republic of Cyprus (“Cyprus”) has taken great strides in its attempt to develop its hydrocarbon resources. In particular it has concluded a number of bilateral agreements with Egypt, Lebanon and Israel in order to delimit its Exclusive Economic Zone (“EEZ”). The Ministry of Commerce, Industry and Tourism of Cyprus (the “Ministry”) has also held its first hydrocarbon licensing round, which closed on 16 August 2007, with Noble Energy International Ltd (“Noble”) receiving an exploration licence for block 12 (there are 13 blocks in the Cyprus EEZ, however only 11 of the 13 blocks were contested in the first licensing round).

Noble has estimated that block 12 contains a mean range of seven trillion cubic feet of gas, however further rounds of exploratory drilling will be needed in order to confirm these estimates. In light of this and in order to keep the momentum going, the Cyprus Council of Ministers has now authorised the Ministry to proceed with all the necessary steps for the launching of the second hydrocarbons’ licensing round for the remainder of the blocks.

This article aims to explain the hydrocarbon licensing regime in Cyprus and assist companies which may be interested in obtaining a hydrocarbon licence from the Ministry.

### The Applicable Legislation

The hydrocarbon exploration and exploitation activities in Cyprus are governed by the Hydrocarbons (Prospection, Exploration and Exploitation) Law No.4(1) of 2007 (the “Law”) and the Hydrocarbons (Prospection, Exploration and Exploitation) Regulations of 2007 (the “Regulations”). The Law is in line with the EU Directive 94/22/EC, which amongst others provides that member states retain the right to determine the areas within their territory to be made available for the exercise of the activities of prospecting, exploring for and producing hydrocarbons.

The Law allows the Council of Ministers to make regulations in order to allow better implementation of the legislation. As such the Regulations serve as a practical guide for applicants who, for example, wish to find out the duration of a prospection, exploration and/or exploitation licence and how for example to deal with abandonment or with their drilling operations (although these should be outlined in greater detail in a contract between the Ministry and the contractor).

## Obtaining a Hydrocarbon Licence

The process begins either with the initiative of the Council of Ministers, through the Ministry, which will publish a notice inviting applicants in the Official Gazette of Cyprus and/or the Official Journal of the EU (the “Journals”), at least 90 days before the closing of the application process, or by a notice by the Ministry, with the approval of the Council of Ministers, being published in the respective Journals following submission of an application by a contractor. Any other interested contractor will have at least 90 days after the publication to submit their application.

The invitation to submit applications will amongst others specify the type of licence, the geographical area, the proposed date or time-limit for granting a licence and any conditions and/or requirements that an interested contractor has to satisfy in order to obtain a licence.

Applications are to be submitted to the Ministry with an application fee (the fee of EUR1,500 per application was levied during the first licensing round).

The applications will then be evaluated based on criteria that may relate to the following:

- national security or public interest;
- the technical and financial ability of the applicant;
- the ways in which the applicant proposes to carry out the activities specified in the licence;
- when the licence is put up for sale, the price which the applicant is prepared to pay in order to obtain the licence;
- any lack of efficiency and responsibility displayed by the applicant in operations under a previous licence.

If following the evaluation two or more applicants have equal merit, the proposals of the applicants in relation to the protection of public safety, public health, security of transport, protection of environment, protection of biological resources and of national treasures possessing artistic, historic or archaeological value, safety of installations and workers and planned management of hydrocarbon resources will be taken into account.

## The Licence

Depending on the licence sought by the contractor, a company will have to enter into a contract (most likely a model production sharing contract) with the Ministry, which will flesh out the conditions and requirements provided in the licence. A contractor may be awarded one of the following licences:

1. **Prospection Licence:** this licence will be granted for a maximum period of 1 year and gives the contractor the permission for prospection using various geophysical techniques in order to evaluate the offshore hydrocarbon potential of Cyprus. This licence will not permit the contractor to carry out any drilling operations;
2. **Exploration Licence:** this licence is granted for an initial period of 3 years and may be renewed for up to 2 terms, each term not exceeding 2 years, provided that the contractor has fulfilled all their obligations under their current licence. Upon each renewal of the term of the exploration period, the contractor relinquishes 25% of the initial surface area of the licensed area. The contractor is required to apply for an extension 2 months prior to the expiry of its current licence. A contractor may also be able to extend its final renewal period where an appraisal work programme with respect to a discovery is in progress and has not been completed. In these circumstances the exploration licence will be extended for another 6 months in case of crude oil discovery and 24 months in case of natural gas discovery. If during its exploration period a contractor makes a commercial discovery it may apply for an exploitation licence after the approval of their development and production plan;
3. **Exploitation Licence:** this licence is granted for a period not exceeding 25 years and may be renewed for a maximum of 10 years. The contractor must submit an application for renewal 1 year prior to the expiry of its current licence.

Contractors will not be able to transfer or assign rights under their licenses without obtaining the prior consent of the Council of Ministers. Contractors will also need to maintain the same ownership structure throughout the duration of the licence. If the ownership structure were to change consent from the Council of Ministers would be required if the licensee were for example to come under the direct or indirect control of a third country or third country national.

## Analysis

The discoveries made in the Cyprus EEZ are estimates for now; however, there are good indications from the surrounding areas that the gas discoveries will be viable for commercial extraction. In particular in the Israeli EEZ where gas exploration has taken place there have already been gas extractions on the Mari-B field which was discovered in 2000 and the Tamar field, which will come on stream in 2013.

In general, in the Mediterranean basin around Cyprus, there has been a lot of activity and it may be regarded as the next hotbed for hydrocarbon extraction. Lebanon has scheduled a first licensing round for early 2012, Syria opened a

bidding round in March 2011 for three blocks totaling 9,000 km<sup>2</sup> and Egypt is offering 15 blocks covering over 18,000 km<sup>2</sup>.

However, Cyprus should be a contractors' destination of choice due to its membership of the EU, stable political system and modern hydrocarbon legislation which makes the application process for obtaining a hydrocarbon licence relatively straightforward. However, contractors may still wish to seek assistance during the negotiation stage with the Ministry especially if they are looking to vary any of the terms contained in the model production sharing contract.

With the second hydrocarbons' licensing round looming, companies should be looking to finalise their applications as the Cyprus EEZ appears to contain lucrative hydrocarbon exploitation potential.

## Further Information

*The foregoing is for general information purposes only and not intended to be relied upon for legal advice in any specific or individual situation.*

*For more information on the subject please contact Kirill Vahonin (kirill.vahonin@harneys.com) or your usual Harneys contact.*

*February 2012*