

ClientAlert

Oil & Gas

January 2015

Amendment to the Kazakhstan Legal Regime for the Oil & Gas Industry

The Law of the Republic of Kazakhstan "On introduction of amendments and additions to certain legislative acts on subsoil use matters" No. 271-V 3PK was adopted on 29 December 2014 and, save for the specified provisions, became effective from 11 January 2015.

Affecting the Subsoil Use Law, the Land Code, the Tax Code, the Code on Administrative Offenses and the Environmental Code, the amendments are primarily aimed at attracting more investments in the industry by liberalizing and simplifying the rules (the "**Amendments**").

Overview of key Amendments

The key Amendments to the Subsoil Use Law (the "**Law**") include:

Limited state pre-emption right

Pursuant to the Amendments, the state's pre-emptive right to acquire exploration and production rights as well as associated interests (when disposed) will be limited to the so-called "strategic" deposits and areas. It should be noted that the general requirement to obtain the consent of the competent authority (Ministry of Energy (the "**MoE**")) for transactions involving exploration and production rights and associated interests has been preserved.

It is important to note that the minimum mandatory term for the consideration of applications for the MoE's consent now has been shortened to 20 business days, while the time frame for the consideration of applications covering the matters of the state's pre-emptive right and the MoE's consent remains 70 business days.

The Amendments also limit the ability to withdraw or revise already filed applications requesting the waiver of the state's pre-emptive right within three months from the submission date. Nevertheless, this new rule does not require sellers to sell subsoil use rights and associated interests to the state.

"Strategic deposit" definition

The Government is authorized to approve list of strategic deposits and areas. Previously, the Government used its discretionary powers to designate deposits and areas as strategic and include them on a list. Under the Amendments, such list must further be compiled based on "strategic" criteria which, in turn, must be developed by the Government as well.



If you have questions or comments regarding this Alert, please contact one of the lawyers listed below:

Maxim Telemtayev
Partner, Astana
+ 7 717 258 26 50
mtelemtayev@whitecase.com

Timur Odilov
Associate, Astana
+ 7 717 258 26 50
todilov@whitecase.com

White & Case Kazakhstan LLP
3rd Floor Block A Business Center Q
Kabanbai Batyr Street, 15a
Astana 010000, Kazakhstan
+ 7 717 255 28 68
+ 7 717 258 26 50

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Termination of contracts

Before enactment of the Amendments, the Law provided that the MoE may unilaterally terminate a subsoil use contract if a subsoil user fails to cure more than two previously committed breaches of the obligations under a subsoil use contract or project documents within the time period specified in the MoE's breach notification. Pursuant to the Amendments, breaching obligations stipulated by only project documents are no longer a sufficient ground for the MoE to terminate a subsoil use contract. At the same time, the Amendments introduced a new, additional ground for the MoE to unilaterally terminate a subsoil use contract – breaching financial obligations under a subsoil use contract by more than 70% for 2 consecutive years.

As regards the time limits for curing breaches, such periods, previously determined by the MOE at its discretion on a case-by-case basis, are now contemplated in the Law as follows:

- physical obligations – up to six months;
- financial obligations – up to three months; and
- other contractual obligations – up to one month.

Thus, the MoE must establish a specific cure period within these time limits. At the same time, in certain cases, a cure period exceeding the established time limits may be extended upon a subsoil user's request.

Timing for preparing project documents

The Amendments have also extended the maximum time for the development and approval of project documents: (i) from six to eight months for prospecting; (ii) from five to eight months for appraisal; and (iii) from 18 to 21 months for commercial development. In addition, all these periods can be further extended for up to an additional six months if the project documents were not developed and approved in time due to circumstances beyond the subsoil user's control.

Feasibility studies

Feasibility studies are no longer considered as project documents and, hence, as a prerequisite for entering into production contracts.

Expert review of draft subsoil use contracts

The Amendments abolish certain mandatory expert reviews of draft contracts. From now on, draft production contracts will be subject to economic and legal expert reviews, while draft contracts of other types will be subject only to legal expert review. The environmental expert review has been abolished entirely.

Expert review of project documents

Industrial safety, sanitation and epidemiological expert reviews of certain project documents at the exploration stage have been abolished. In particular, prospecting project documents and appraisal project documents that do not include trial production are subject to only environmental expert review. Thus, appraisal project documents that do include trial production are still subject to all types of expert review: environmental, industrial safety, sanitation and epidemiological.

Contract by application

The Amendments also introduce a simplified legal regime for exploration for, among other things, oil and gas located in "understudied areas" (to be determined by the Committee of Geology and Subsoil Use of the Ministry of Investment and Development (the "**Geology Committee**")). First, all such areas will be subject to a graticular boundary (or block) system. Second, the maximum size of an exploration area granted under the simplified regime is ten blocks. Third and most importantly, exploration rights in respect of understudied areas may be granted to any applicant as a result of direct negotiations with the MoE. Exploration rights will be granted in proforma contracts. Finally, a holder of exploration rights is exempted from the local content requirements.

Auction as a new method

As an alternative to the existing tendering process, the MoE may now grant exploration and production rights through conducting English type auctions based on signing bonus bids.

Extension of contract area boundaries

The Amendments have eliminated contradictions between different provisions of the Law that did not allow subsoil users to extend contract area boundaries. Following enactment of the Amendments, subsoil users may extend the boundaries of a contract area upon prior permission from the MoE. However, a contract area may not be extended by more than 50 percent of the existing size.

Oil spills

The Amendments introduce a new article to the Law specifying requirements for subsoil users in respect of oil spills. Pursuant to the Amendments, oil spills are divided into three categories depending on the scope of the spill and resources required to clean it up. All subsoil users must be able to clean up first and second categories spills. However, only specialized oil spill response companies hired by subsoil users may clean up spills of the third category. Any oil spill must be cleaned up pursuant to the oil spill prevention and response plan to be developed by subsoil users in compliance with the regional oil spill prevention and response plan approved by the relevant local authorities.

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Oil inventory information system

From 1 January 2017, oil producers and other entities engaged in oil sales will be required to equip their facilities (the list will be determined by the MoE) with meters to measure volumes of oil production, processing, transportation, storage, shipment, export and import, etc., in real-time mode.

Re-injection of drill cutting waste

A definition of "construction and/or operation of underground facilities associated with exploration and/or production" has been introduced, clarifying that no separate subsoil use contract for underground facilities is required for the disposal and storage of drill cutting waste in underground facilities while implementing contracts for exploration and/or the production of hydrocarbons.

Surrender of a contract area

Before the enactment of the Amendments, the terms of surrender of a contract area were regulated by individual subsoil use contracts. The Amendments require the Geology Committee to develop and approve the general rules for the surrender of contract areas.

General comment

We note that as of the date of this Client Alert the relevant secondary legislation has yet to be developed or brought in line with the Amendments. Therefore, there might be a certain transition period prior to the practical implementation of the Amendments. The statutory period for the adjustment of secondary legislation is one month from the date of enactment of the Amendments; however, in practice, it may take longer.