

The new 2005 Algerian Hydrocarbons Law

By Francois Krotoff and Nicolas Bonnefoy, Gide Loyrette Nouel, Paris and Samy Laghouaty and Abdelhamid Ghezali, Gide Loyrette Nouel, Algiers

A new hydrocarbon law was adopted in Algeria on April 28, 2005 (*loi n 05-07 du 28 avril 2005 relative aux hydrocarbures*, the '2005 Hydrocarbons Law'). Published in the *Journal Officiel de la République Algérienne* on July 19, 2005, the 2005 Hydrocarbons Law replaces the former hydrocarbons law (*loi n 86-14 du 19 août 1986 relative aux activités de prospection, de recherche, d'exploitation et de transport, par canalisation des hydrocarbures*, the '1986 Hydrocarbons Law'). The aim of the 2005 Hydrocarbons Law is to improve transparency in contract awards, establish a competitive and liberalised market as well as to establish a simplified legal and tax regime. The 1986 Hydrocarbons Law and 2005 Hydrocarbons Law are so different that the implementation of the 2005 Hydrocarbons Law may well lead to an actual revolution in the petroleum industry in Algeria. However, for the time being, implementation regulations have still not been passed and many issues remain outstanding, so the long-awaited implementation regulations will be critical.

1986 Hydrocarbons Law

The 1986 Hydrocarbons Law established the monopoly of the State over hydrocarbons exploration, exploitation and transportation activities. The State could only entrust these activities to national companies such as Sonatrach, therefore, international oil & gas companies, i.e. foreign companies in Algeria (hereinafter referred to as 'IOCs') could not carry out hydrocarbons exploration

and exploitation activities except through a partnership with Sonatrach.

The following basic rules applied to those partnerships:

1. Only partnerships pertaining to hydrocarbons exploration and production activities were authorised. Hydrocarbons pipeline transportation was the monopoly of Sonatrach.
2. Partnerships pertaining to hydrocarbons pipeline transportation were not authorised. However, foreign entities could finance, build and operate hydrocarbons pipeline transportation on behalf of Sonatrach, in cases where there was a lack of spare transportation capacity. Though Sonatrach always remained the owner of said transportation infrastructures.
3. As far as hydrocarbons exploration and production activities were concerned, the mining titles and licences (prospecting authorisation, research permit, provisional exploitation authorisation and exploitation permit) were exclusively granted to Sonatrach.
4. Natural gas production was required to be marketed through a joint marketing company, in which Sonatrach had the majority of voting rights.
5. The IOC was allocated a share of crude oil and oil products FOB Algeria and/or a share of the revenues generated by the sale of natural gas, as a lump sum for cost oil and profit oil, free from any tax, duties whatsoever, as well as from any obligation to repatriate the funds and proceeds of the marketing of its share of those products.
6. The IOC profit share (net of tax) in the relevant project could not exceed 49% of the total production each year.

7. Sonatrach was allocated two shares of crude oil, oil products and/or revenues generated by the sale of natural gas: one share pertaining to its capacity as mining title holder (51%) and another share pertaining to its capacity as private investor.
8. Sonatrach's share, pertaining to its capacity as mining title holder, was allocated to the payment of royalty, income tax and transportation costs.

2005 Hydrocarbons Law

The 2005 Hydrocarbons Law establishes two new agencies and relieves Sonatrach of its public regulatory capacities and responsibilities; liberalises upstream, midstream and downstream activities; and simplifies the hydrocarbons legal and tax regime.

New bodies

The 2005 Hydrocarbons Law creates:

- *L'Agence Nationale de Contrôle et de Régulation des Activités dans le domaine des Hydrocarbures* (hereinafter referred to as 'ARH'); and
- *L'Agence Nationale pour la Valorisation des Ressources en Hydrocarbures* (hereinafter referred to as 'ANALFT').

ARH will implement and enforce the regulations pertaining to hydrocarbons exploration and production activities in Algeria, including technical regulations as well as regulations pertaining to transportation tariffs, third party access to transportation infrastructures, health, safety and environmental standards. ARH is also responsible for considering applications for pipeline transportation concessions.

ANALFT will promote the Hydrocarbons industry, manage Algeria Hydrocarbons database, evaluate competitive bids and award exploration and exploitation areas, as well as exploration and exploitation contracts, and approve development plans.

Therefore, Sonatrach is relieved of all the public responsibilities it was assigned under the 1986 Hydrocarbons Law and becomes a regular commercial company, able to compete with other IOCs investing in Algeria.

Liberalisation of hydrocarbons upstream activities

Upstream activities are entirely liberalised:

- IOCs are not required to enter into a partnership with Sonatrach;
- IOCs profit share (net of tax) is not limited to 49%; and

- IOCs are not required to market natural gas through a joint marketing company, in which Sonatrach has the majority of voting rights.

In addition, title to ownership of hydrocarbons is not transferred FOB Algeria but at the measurement point directly. Investors may also enjoy the right to own all the facilities set up for the purposes of hydrocarbons production, extraction and separation, and any other real assets that they may have developed within the contractual perimeter area. These new property rules should ease financing by allowing the grant of mortgages over these facilities as loan security.

However, Sonatrach is given the right to participate in the two following cases:

1. Following the approval of a development plan, Sonatrach has an option to acquire a participation of between 20% and 30%. Should Sonatrach exercise this option, it would then pay development and exploitation costs and exploration costs pertaining to the discovery well and related appraisal costs, and the natural gas must be marketed jointly. However, Sonatrach is restricted from assigning the participation acquired for a period of five years.
2. Upon any assignment of participation, Sonatrach has a pre-emptive right, similar to that of the 1986 Hydrocarbons Law. However, the 2005 Hydrocarbons Law does not provide any further details regarding the exercise of the pre-emptive right and it is hoped that the implementation regulations will clarify this issue.

Liberalisation of hydrocarbons midstream activities

Midstream activities are entirely liberalised. Indeed, transportation activities in Algeria are no longer the monopoly of Sonatrach. Therefore, any IOC now has the right to build and operate its own transportation pipelines in accordance with its hydrocarbons transportation concession. We should emphasize that the hydrocarbons transportation concessions may be granted to any IOC, whether operating in Algeria under an exploration and exploitation contract or not, so we can anticipate the birth of a new hydrocarbons transportation market in Algeria.

The 2005 Hydrocarbons Law establishes a third party equal access principle to any transportation system in situations of spare capacity. Third party access is granted on the basis of a regulated transportation tariff calculated per geographical zone. This tariff must be non-

segregating and the lowest possible. However, implementation of a third party equal access principle requires clarification and the transportation tariff calculation mechanism still remains unclear.

Liberalisation of hydrocarbons downstream activities

Downstream activities are also entirely liberalised. Indeed, the 2005 Hydrocarbons Law allows IOCs to freely invest in refining and liquefaction activities as well as in storage and distribution of oil products.

Simplified legal and tax regime

Exploration and production agreements provided by the 1986 Hydrocarbons Law included joint ventures, partnerships, production sharing, and risk service contracts. The 2005 Hydrocarbons Law only includes two main instruments: The Exploration and/or Exploitation Contract; and the Pipeline Transportation Licence.

The Exploration and/or Exploitation Contract is

entered into between the IOC and ANALFT, which is the mining title holder, further to a competitive, fair and transparent bid process. Similar to the 1986 Hydrocarbons Law, the contract is approved by decree and published in the *Journal Officiel de la République Algérienne*. ANALFT manages the entire bid process, approves the development plan and any assignment of participation. The Pipeline Transportation Licence is granted by the Minister in charge of hydrocarbons further to a competitive, fair and transparent bid process. It covers transportation and storage of hydrocarbons but excludes gas networks supplying the domestic market. Indeed, natural gas public distribution remains under the monopoly of SONEGAS, the State owned electricity and natural gas distribution company.

However, the most significant changes are related to the tax regime governing the Exploration and/or Exploitation Contract, as follows:

1. There is no participation allocated to the State



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Oil & Gas Practice Group

Algiers

Tel. +213 (0)21 23 94 94
Fax +213 (0)21 23 92 73

Contacts

Samy Laghouati
laghouati@gide.com
Abdelhamid Ghezali
ghezali@gide.com

London

Tel. +44 (0)20 7826 9700
Fax +44 (0)20 7826 9701

Contacts

Michael Doran
mdoran@gide.com
Christopher Czarnocki
cczarnocki@gide.com

Paris

Tel. +33 (0)1 40 75 60 00
Fax +33 (0)1 43 59 37 79

Contacts

François Krotoff
krotoff@gide.com
Nicolas Bonnefoy
bonnefoy@gide.com

anymore, such as the former participation allocated to Sonatrach in its capacity as private investor.

2. There is no production sharing mechanism anymore. The Exploration and/or Exploitation Contract is a regular tax and royalty agreement and is not a production sharing contract.
3. The IOC pays its share of taxes directly.

Under the new tax regime governing the Exploration and/or Exploitation Contract, IOCs will be subject to the following main taxes:

- a monthly proportional royalty (*redevance*), based on the location of the field and the level of hydrocarbon production, to be paid to ANALFT in its capacity of mining title holder;
- an annual surface tax (*taxe superficière*), based on the surface area covered by the Contract, to be paid to Public Treasury;
- a monthly petroleum income tax (*taxe sur le revenu pétrolier*), based on a sliding scale, which increases as and when the cumulative value of hydrocarbons production increases, to be paid to Public Treasury; and
- an annual additional income tax (*Impôt complémentaire sur les résultats*), calculated at the same rate as the prevailing rate of the regular corporate profit tax.

Exploration and production activities are exempt from value added tax, customs taxes and importation fees, royalties and duties, and any other tax or duty on production revenues.

Finally, in accordance with the 2005 Hydrocarbons Law, assignments of participation are subject to a 1% transfer tax, based on the value of the transaction. However, it is still unclear whether assignments of

participation related to contracts executed before the 2005 Hydrocarbons Law enters into force, will be subject to the transfer tax.

Conclusion

The 2005 Hydrocarbons Law will lead to a much improved image for the hydrocarbons industry in Algeria: competitive, fair, simplified and, in particular, liberalised. However, many issues still need to be clarified before they are implemented, and therefore, the success of the 2005 Hydrocarbons Law will now depend on the forthcoming implementation regulations. For instance, this is especially important for contracts concluded before the 2005 Hydrocarbons Law was published as there is some uncertainty as to when a contract is 'concluded'. The answer to this question is critical for the sixth licensing round - and the next round under the 2005 Hydrocarbons Law - the success of which will depend on the interest of the international petroleum industry in Algeria.

It may well be that a new day has dawned for the Algerian hydrocarbons industry.

**Francois Krotoff and Nicolas Bonnefoy,
Gide Loyrette Nouel,
26, cours Albert 1er, 75008, Paris, France.
Emails: krotoff@gide.com /
bonnefoy@gide.com
and
Samy Laghouaty, and Abdelhamid Ghezali,
Gide Loyrette Nouel, Algiers.
Emails: laghouaty@gide.com /
ghezali@gide.com
www.gide.com**