This briefing discusses issues surrounding the declaration of force majeure by Tullow oil on behalf of its joint venture partners Africa Oil and Total. Interestingly, Tullow is yet to make the announcement and Africa Oil has made the announcement available here. The update indicates;

*These declarations are the result of impact of the COVID-19 pandemic on the operations, including Kenyan government's restrictions on domestic and international travel, and recent tax changes that adversely impact the project economics. These are exacerbated by the recent unprecedented crash in global crude oil prices.*

In this update we intend to review the key arguments on the reasons behind the invoking of force majeure or clause by the companies involved.

**Force Majeure**

It is sometimes referred to as the “act of god” clause. Usually to indicate an incident that was not reasonably foreseen by two parties to a contract. The incident would greatly impede the ability of one or both parties to successfully perform their obligations under a contract and is beyond the control of both parties. It is therefore, why the companies are not relying on the global crash of crude oil prices as a reason, merely adding it as an additional factor. The volatility of the price of crude is reasonably foreseen and indeed since the discovery of crude in Kenya the price has oscillated from a high of USD $100 to as low as 20.

It is also not unprecedented, in illustration Tullow in 2016 temporarily invoked Force Majeure in its Ghana operations due to challenges with its offshore production facility.

The Kenyan clause reads as below;

50. Force Majeure

(1) In this clause, force majeure means an occurrence beyond the reasonable control of the Cabinet Secretary or the Government or the contractor which prevents any of them from performing their obligations under this contract.

(2) Where the Cabinet Secretary, the Government or the contractor is prevented from complying with this contract by force majeure, the person affected shall promptly give written notice to the other and the obligations of the affected person shall be suspended, provided that that person shall do all things reasonably within its power to remove such cause of force majeure. Upon cessation of the force majeure event, the person no longer affected shall promptly notify the other persons.

(3) Where the person not affected disputes the existence of force majeure, that dispute shall be referred to arbitration in accordance with clause 53.

(4) Where an obligation is suspended by force majeure for more than one (1) year, the parties may agree to terminate this contract by notice in writing without further obligations.

(5) Subject to sub-clause 50(4), the term of the contract shall be automatically extended for the period of the force majeure.
Covid-19 and restrictions on domestic and international travel

On the domestic front it would be upon the companies to prove that government restrictions have limited their movement and ability to carry out works. Currently, companies have applied and gained exemptions to the travel for essential services. It is likely a business case would have been made for services including drilling which involve limited social contact.

International travel is different in that it is beyond control of both parties. However, Tullow had already reduced its footprint and centralised a majority of its operations either centrally in Nairobi or HQ. It would be upon them to prove that staff undertaking crucial functions are currently unable due to travel restrictions. The pending issues were related to the Full field development programme and not necessarily ground related.

Tax changes adversely impact the project economics.

Recent measures introduced in the Finance proposed the removal of VAT exemption on taxable supplies, imported or purchased for direct and exclusive use in geothermal, oil or mining prospecting or exploration. At the committee stage of the bill presentations argued that this provision would impede prospecting and exploration in the Oil and Gas areas. Treasury in a rare response indicated; In 2018 alone tax revenue foregone by Government was almost 30% of revenue. The tax incentives have limited government capability, while improving profit margins at the expense of service to Kenyan citizens.

While the VAT changes could be argued as a change in project economics as the Swahili say “msema kweli” is the series of contracts that remain unreleased. A good start would be the original contract signed by Africa Oil, the Heads of Terms agreements signed last year by the joint venture partners. Once the contracts are released coupled with the project economics we can then ascertain whether the project becomes unviable as the company would claim. Additionally, most resource contracts contain stabilisation contracts and may therefore not be impacted by changes in legislation.

The challenge remains attempts by the oil companies to benefit from incentives offered to different sector of the company by understating the viability of the project. It is likely going to be a drawn-out process of negotiation which is likely to lead to further delays towards Kenya’s first oil.

The big question?

Can Tullow prove that they still have the technical and commercial capacity to undertake their responsibilities?