China’s Regulations, Status & Challenges for Attracting Foreign Investment in Petroleum Exploration and Production

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Outline

◆ Regulations for Investment Promotion Campaigns
◆ Current Status of Domestic Sino-foreign Cooperation for Petroleum Exploration & Production
◆ Development Prospects and Challenges
In order to promote international cooperation and technology exchange in petroleum industry, Chinese government promulgated the following regulations and rules:

- Based on the rules of WTO, the two regulations mentioned above were revised in Sept. 2001.
- The new version of “Rules of Instruction of Foreign Investment Orientation” was issued in Feb. 2002;
- “Catalog of Instruction of Foreign Investment” was jointly issued by State Development and Planning Commission (SDPC), State Economy and Trade Commission (SETC) and Ministry of Foreign Trade and Economic Cooperation (MOFTEC) in Mar. 2002.

According to the two cooperation regulations mentioned above, there are four oil companies have rights to cooperative exploitation of petroleum resources with foreign companies in China.

- The China National Petroleum Corporation (CNPC) and the China Petrochemical Corporation (SINOPEC GROUP) are designated as the parties in charge of the exclusive rights to all cooperative exploration, development, production and sale of onshore petroleum resources with foreign parties.

- The China National Offshore Oil Corporation (CNOOC) has exclusive and overall responsibility for the work of exploiting offshore petroleum resources in China in cooperation with foreign enterprises.

- The China United Coalbed Methane Corporation (CUCBM) is designated as the Chinese party in charge of the exclusive rights to all cooperative exploration, development, production and sale of coalbed methane with foreign parties.
China’s National Oil Companies

**CNPC** is a national integrated energy corporation, engaging in both upstream and downstream operations, oil and gas field engineering and technical services, and petroleum materials and equipment manufacture and supply, being the largest producer and supplier of crude oil and natural gas in China.

**Sinopec Group** is one of the largest integrated energy and chemical companies in China, engaging in oil and gas exploration, development, production and marketing, oil refining, production and sales of petrochemicals, chemical fibers, chemical fertilizers and other chemical products; storage and pipeline transportation of crude oil and natural gas and import, export and import/export agency business of crude oil, natural gas, refined oil products, petrochemicals, chemicals, other commodities, being China’s largest producer, distributor and supplier of oil products and major petrochemical products.

**CNOOC** is a national oil company incorporated in 1982. It has established six business sectors ranging from offshore oil and gas exploration and development, technical services, chemicals and fertilizer production, natural gas power generation to financial services.

**CUCBM**, as a China’s sole backbone CBM enterprise, was established in March 1996. Its business scope covers CBM exploration, development, production, transportation sales and utilization.

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**Regulations for Foreign Petroleum Investment**

- According to the “Catalog of Instruction of Foreign Investment” for foreign investors joining in the China’s oil and gas business, there are two kinds of ways for foreign investment in oil and gas E&P field:
  - Sino-foreign jointly-invested projects in terms of oil and gas risk exploration and development, low permeability reservoirs (oil fields) development, development and application of new technologies to enhance oil recovery (EOR), and development and application of new E&P technologies, e.g. geophysical exploration, drilling, well logging and down-hole operation, etc.
  - Projects allowed sole investment by foreign companies in terms of coalbed methane E&P, design and manufacture of new instruments and equipments in oil E&P operation, special automobiles manufacture in petroleum industry, such as dune buggy, construction and operation of oil and gas pipelines, storages and terminals and energy-saving technology, etc.
Licensing & Contracts

• Licensing Method----international bidding/negotiation
• Contract Mode ----Production Sharing Contract
  According to the two above cooperation regulations, China’s oil companies usually award foreign enterprises the licenses of cooperation blocks through the way of bidding/ negotiation, and sign the production sharing contracts with foreign companies.

RIGHTS AND OBLIGATIONS OF FOREIGN CONTRACTORS

• According to the two cooperation regulations mentioned above, the foreign contractor has the following rights and obligations.
  • the foreign contractor shall provide the investment to carry out prospecting, be responsible for prospecting operations and bear all prospecting risks; after a commercial oil (gas) field is discovered, both the foreign contractor and China’s oil company shall provide the investment for its cooperative development, and the foreign contractor shall be responsible for the development and production operations until China’s oil company takes over the production operations when conditions permit as provided in the petroleum contract.
  • The foreign contractor, in accordance with the provisions of the petroleum contract, recovers its investment and expenses and receives remuneration out of the petroleum produced.
RIGHTS AND OBLIGATIONS OF FOREIGN CONTRACTORS

- The foreign contractor may export the petroleum due to it and the petroleum it purchases, and may also, in accordance with the law, remit abroad the investment it recovers, its profits and its other legitimate income.
- All foreign enterprises participating in the cooperative exploitation of petroleum resources shall pay taxes in accordance with the law and shall pay mining royalties.
- All the employees of the enterprises mentioned above shall pay individual income tax in accordance with the law.

RIGHTS AND OBLIGATIONS OF FOREIGN CONTRACTORS

- The equipment and materials imported for carrying out the petroleum contract shall be subject to tax at a reduced rate, or be exempted from tax, or be given other preferential-tax treatment in accordance with relevant provisions.
- The foreign contractor shall open a bank account and deal with other foreign exchange affairs in accordance with the provisions of the Regulations on Foreign Exchange Control of the People’s Republic of China and other regulations on foreign exchange control.
RIGHTS AND OBLIGATIONS OF FOREIGN CONTRACTORS

• In carrying out the petroleum contract, the foreign contractor must
  —promptly and accurately report to China’s party on the situation of
  petroleum operations;
  —acquire complete and accurate data, records, samples, vouchers and
  other original data with respect to the various aspects of the petroleum
  operations,
  —regularly submit to China’s party the required data and samples as well
  as various technological, economic, financial and accounting, and
  administrative reports.

• In carrying out the petroleum contract, the foreign contractor shall
  establish a branch or subsidiary or representative office within the territory
  of the People’s Republic of China and fulfil registration formalities in
  accordance with the law.

• The location of the branch, subsidiary or office shall be determined
  through consultation with China’s party.

• The assets purchased and/or constructed by foreign contractor according to the project and budget for the purpose of contract shall belong to the property of Chinese party after the recovery of contractor’s investment pursuant to the contract or termination of the production phase.

• The contractor may use these assets in accordance with the provision of contract during the term of the contract.
Outline

- Regulations for Investment Promotions Campaigns
- Current Status of Domestic Sino-foreign Cooperation for Petroleum Exploration & Production
- Development Prospects and Challenges

Current Status of Domestic Sino-foreign Cooperation for Petroleum E&P

- In Feb. 1982, CNOOC began the first international bidding round of offshore exploration blocks.

- In 1985, the State Council of China made a decision to open the ten provinces/regions in southern China to foreign companies for cooperative exploitation of onshore petroleum resources.

- In Jan. 1993, some provinces/regions in northern China also opened to foreign companies for cooperative exploitation of onshore petroleum resources.

- By the end of 2004, four China’s state-owned oil corporations (CNPC, SINOPEC, CNOOC, CUCBM) had signed more than 220 contracts of petroleum resources exploitation with foreign companies.
Current Status of Domestic Sino-foreign Cooperation for Petroleum E&P

- All the contract blocks covered the area of more than 1.0 million sq.km in offshore and onshore China.

- All the cooperation projects engaged in risk exploration, enhanced oil recovery, individual well servicing, and geophysical prospecting, etc.

- The total foreign investment reached nearly US$10 billion.

CNPC Domestic Sino-foreign Cooperation for Petroleum E&P

- Since 1985, CNPC has pursued Sino-foreign cooperation in onshore operations within China.
- By the end of 2004, the company had signed 53 petroleum contracts and 24 agreements with 46 foreign companies from 10 countries and regions with the foreign investment of US$1.386 billion.

- At present, there are 15 Sino-foreign cooperation contracts under execution.
- The contract blocks are distributed in Songliao, Bohai bay, Sichuan, Ordos, Qaidam and Junggar basins, covering the area of 11,000 sq.km.
**Sinopec Domestic Sino-foreign Cooperation for Petroleum Production**

Due to historical reason, Sinopec Group was authorized to cooperate with foreign enterprises to exploit the onshore petroleum resources by the State Council of China until 2001.

At the present, 4 cooperative contracts of oil production are being executed in Shengli oilfield.

1. West Chengdao block, oil production project, American Energy Development Company (EDC).
2. Zhuangxi buried-hill reservoir, IOR, Malaysia Company.
3. Oil well stimulating project, American BJ company.
4. Yi64 block, oil production project, American Microbe Company.

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**CNOOC Domestic Sino-foreign Cooperation for Petroleum E&P**

- CNOOC began the first international bidding round of exploration blocks in 1982.
- By the May of 2005, it has signed 167 petroleum contracts and agreements with 72 foreign enterprises from 19 countries and regions.
- There are 27 contracts under execution now, the contract areas cover 12,000 sq.km.

- In 2005, 10 blocks covering the area of 66,666 sq.km was available for cooperation between CNOOC and foreign companies.
  1. One block in Bohai Bay Area
  2. One block in South Yellow Sea Area
  3. One block in East China Sea Area
  4. Four blocks in the East of South China Sea Area
  5. Three blocks in West of South China Sea Area
CUCBM Domestic Sino-foreign Cooperation for CBM E&P

- CUCBM has achieved fruitful results in CBM exploration with foreign companies.
- By the end of 2004, the company had signed 21 production sharing contracts with 10 foreign companies from USA, Canada, France etc..

- The total contract area covers about 33,800 sq.km.
- The foreign investment had reached US$ 119 million, 127 CBM wells of different types had been drilled.

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According to the new round of China’s petroleum resources assessment, the oil resources in place are 102.1 billion tons, the natural gas resources 47 trillion cubic meters.

Many researches show that there are 14-17 billion tons of recoverable oil resources, 10-15 trillion cubic meters of recoverable natural gas resources.

By the end of 2004, the discovery rate of recoverable oil resources (accumulative recoverable reserves / total recoverable resources) is about 40%; the discovery rate of recoverable natural gas resources is about 20%, showing the great potential of petroleum exploration in China.

China is rich in unconventional oil and gas resources, such as coalbed methane (CBM), oil shale, oil sand, tar sand, tight sandstone natural gas, and gas hydrate.

It is estimated that the CBM resources in place to the depth of 2000 m below the surface is about 30 trillion cubic meters in China. China is one of the richest CBM countries in the world.
China have made rapid development in Crude oil and gas pipelines.

The construction of the major infrastructures (e.g. west-east gas pipeline, Shaanxi-Beijing gas pipeline, Southwest oil pipeline, etc.) will offer good opportunities to petroleum resources development and utilization.

In order to develop petroleum industry, Chinese government has been made many policies to encourage the production and utilization of petroleum resources, including:

- Establishing the sustainable development strategy of petroleum industry
- Increasing the supply of natural gas.
- Encouraging international trade and cooperation for petroleum exploration, production and utilization.
- Quickening the development of petrochemical industry and the efficient utilization of petroleum resources.
- Setting up the petroleum reserve system and anti-risk measures.
- Perfecting the laws and regulations for the development and efficient utilization of petroleum resources.
The Chinese government will continue to encourage, support and promote the open of petroleum industry to the outside world, and try to create many investment opportunities for foreign investors.

The main investment fields of petroleum industry in recent years will be as follows:

- Oil and gas exploration and development
- Unconventional oil and gas resources exploration and development, e.g. coalbed methane.
- Infrastructure construction, e.g. natural gas pipeline.
- Natural gas power generation.

Main Challenges for Attracting Foreign Investment

- China is still facing many challenges for attracting foreign investment in petroleum E&P fields, including laws and regulations, management, information services and human resources. We need to do the following works in order to create better investment environment for foreign investors.
  - to perfect relevant laws and regulations.
  - to strengthen management
  - to improve information services.
  - to do personnel training.
  - to learn advanced experiences.
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