

April 2018

GAS ENERGY LATIN AMERICA (GELA) Specialized Consultant



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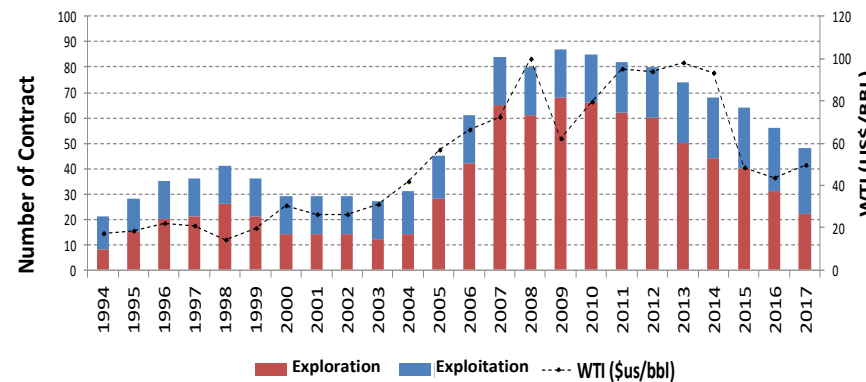
1. Exploration Contracts in Peru

Until recently, Peru was one of the most attractive countries in the region for investors. Today the situation is becoming increasingly uncertain, especially in the hydrocarbon sector

The balance between new and returned contracts is negative. In the last 2 years, 26 blocks were returned, mostly exploratory, and there are other 20 blocks declared in force majeure due to social conflicts or environmental impediments.

Unlike its neighboring countries that compete to attract investments in the sector, Peru has not adopted stimulus measures for the oil sector since the fall in oil prices in 2014.

Record of existing E & P contracts



Source: Perupetro

2. Social conflicts, environmental demands and lack of authority

Social conflicts and the lack of authority is the main problem affecting the Peruvian hydrocarbon sector. Although these problems are common to all extractive activities, in the case of the hydrocarbon sector, there is interest from environmental and other NGOs to prevent oil activity from being carried out in the Amazon rainforest or at sea. If we add to this a State without authority that does not enforce the laws and does not promote a serious policy for the development of the sector, what end up happening is an environment of conflict that makes the development of new exploratory projects unfeasible.

There is a divorce between the State, the communities and the companies, even if all of them have as a common objective to value the natural resources available in the area. The pending task of the current administration is to lead the process for the unification criteria that will allow the development of an effective plan to address this issue. The goal should be to promote harmony between investors and local communities under the tutelage of the State, which is responsible for seeking that all stakeholders benefit.

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Another issue of equal concern, is the obligation that exists to conduct citizen participation workshops as part of the Environmental Impact Studies.

In all the countries of the region, environmental approval processes and social licensing processes occur through separate channels given that environmental issues are technical and those of pertaining to social license require a search for consensus and agreements between communities and the investors.

This obligation for citizens to participate in environmental impact talks generates an atmosphere of doubt and fear among the population regarding the activity, mainly due to ignorance and unleashes in actions of rejection towards the projects.

Social Conflicts – a Constant

El Comercio El lote 192: un crudo panorama [INFORME]

Block 192: A harsh picture (REPORT)

Two weeks ago, indigenous people occupied facilities to demand Pacific oil Company to pay land use compensation



3. Perupetro, Offshore Rounds and Direct Negotiation

Perupetro is the entity in charge of promoting investments in the oil sector in Peru.

Perupetro, according to the organic hydrocarbons law, has the role of promoting, negotiating, bidding, subscribing and supervising oil contracts, as well as the collection of royalties in favor of the State. However, its role at improving the competitiveness of Peru and attract new investments in exploration has been scarce in recent years.

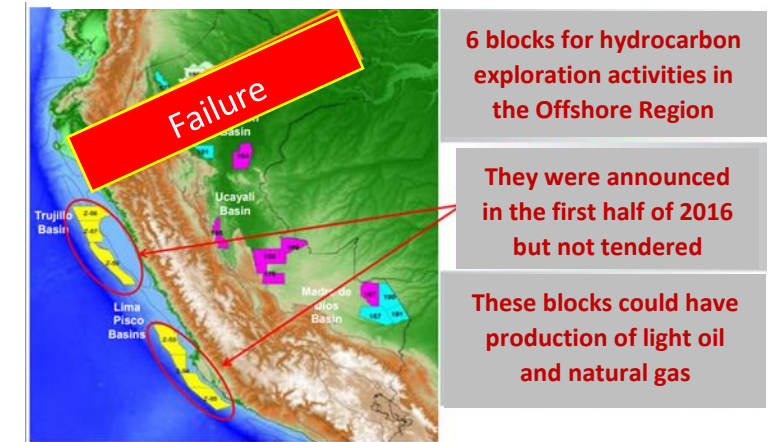
Since the fall of oil prices in 2014, investment in exploration has been reduced globally. Peru, does not have a geology as favorable as those of Mexico, Brazil or Argentina. If we add to that social, environmental and of procedure issues mentioned above, the result is obvious: Peru has failed in its latest bidding rounds to secure takers for the offshore blocks. No companies expressed interest in participating.

In 2017 and as a reaction to those disappointing outcomes Perupetro resume the system of awarding blocks via direct negotiation.

Perupetro also targeted companies interested in offshore exploration, particularly those focused on deepwater. Contrary to the blocks in the amazon jungle, offshore blocks do not require prior consultation, facilitating the award process.

Under this scheme, in 2017 Perupetro signed a contract with Anadarko for exploration work in 3 deepwater blocks and recently 5 additional blocks also deepwater with with Tullow Oil.

Last failures of Bidding by rounds of parcels



- 6 Blocks in the Offshore zone (2013)
- Blocks III and IV in the Peruvian northwest (2014)
- Block 192 in the north Peruvian jungle (2015)
- 7 blocks in the north Peruvian jungle (2015)

Source: Perupetro

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4. Suspicion exceeds reason

Currently Peru has just gone through one of its most serious political crisis in its history, the President of the Republic was forced to resign, and the vice president took office, in an atmosphere of suspicion about corruption issues. The approval of the signature of exploration contracts by the resigning president, the day of his resignation, generated doubts among political opponents, questioning the validity of the contracts.

Although the negotiation of the contracts is the responsibility of Perupetro, the formal process requires that the contracts are only signed after they are reviewed and approved by the Ministries of Energy and Economy. Then the President issues a Supreme Decree authorizing Perupetro to sign it. That is, the President only validates a negotiation conducted by Perupetro and reviewed by two Ministries.

By approving these contracts the day he resigned is broadly view as another act of corruption for the embattled former President.

Awarding blocks through direct negotiation is recognized by Peruvian legislation. There is also a long precedent since of the current 43 exploration and exploitation contracts (17 and 26 respectively) only 8 were signed after a bidding process.

Peru has entered a situation where not only must confront the problems of the sector, but also and even more now, it most address the suspicions expressed by a sector of Congress.

Press cuttings referring to the current uncertainty of the contracts



Perupetro statement following the questioning of signed contracts



NOTICE

Approval of Licensing Contracts by direct negotiation

Lotes Z-64, Z-65, Z-66, Z-67 and Z-68

2 En el desarrollo de los procesos de negociación de los Contratos de Licencia de los Lotes Z-64, Z-65, Z-66, Z-67 y Z-68, PERUPETRO S.A. ha observado estrictamente las normas de la Ley Orgánica de Hidrocarburos y los Reglamentos respectivos, incluyendo el de Participación Ciudadana.

El 18.10.2017, PERUPETRO S.A. otorgó calificación a la empresa TULLOW OIL, PLC. La negociación de los Contratos de Licencia se desarrolló entre el 03.11.2017 y el 01.12.2017. Los proyectos de Contrato de Licencia fueron aprobados por el Directorio de PERUPETRO S.A. el 20.12.2017 y remitidos al Ministerio de Energía y Minas para su trámite de aprobación con fecha 27.12.2017, concluyendo dicho trámite con la publicación de los Decretos Supremos N° 006-2018-EM, N° 007-2018-EM, N° 008-2018-EM, N° 009-2018-EM, N° 010-2018-EM, con fecha 24.03.2018.

Cabe indicar que, a la fecha, los referidos Contratos de Licencia se encuentran pendientes de suscripción.

3 Los Contratos de Licencia de los Lotes Z-64, Z-65, Z-66, Z-67 y Z-68 están en fase de determinación de la regala Metodología por Escalas de Producción y la Metodología por Resultado Económico - RRE, así como los porcentajes de regala, establecidos en el Decreto Supremo N° 017-2003-EM.

Al respecto, del total de 17 contratos de hidrocarburos vigentes en fase de exploración, 11 contratos contemplan las mismas metodologías y porcentajes de regala establecidos en el Decreto Supremo N° 017-2003-EM.

4 Los Contratos de Licencia de los Lotes Z-64, Z-65, Z-66, Z-67 y Z-68 corresponden a áreas de exploración, en las que no existe descubrimiento de hidrocarburos y, en consecuencia, no cuentan con reservas ni gases productivos. Los Contratos establecen una fase de exploración de 7 años, con programas mínimos de trabajo cuyas inversiones estimadas superan los 200 MM.USD, a ser asumidos por el Contratista.

El Contratista, luego de la suscripción de los Contratos de Licencia, deberá remitir los respectivos Estudios Ambientales e Instrumentos de Gestión Ambiental Complementarios, según las actividades a desarrollar, de acuerdo con la normatividad vigente.

5. PERUPETRO S.A. reaffirms the legality and transparency of the negotiation processes in the Licensing Contracts of the Lotes Z-64, Z-65, Z-66, Z-67 and Z-68, complying with its role of promoting investments in exploration and exploitation activities of hydrocarbons in the country.

Lima, April 02, 2018
PERUPETRO S.A.

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5.- Conclusions

The continuous political ups and downs have affected the sector. It hinders decision making by the authorities to attract investments in exploration. When decisions are made they are immediately questioned often without technical or legal support, but purely based on political reasons.

It is now urgent to adopt fiscal and regulatory policy changes to reactivate the hydrocarbons sector. But more urgent is to convince different sectors of the political class often ignorant the oil business in Peru that oil exploration is actually a good activity for the country.

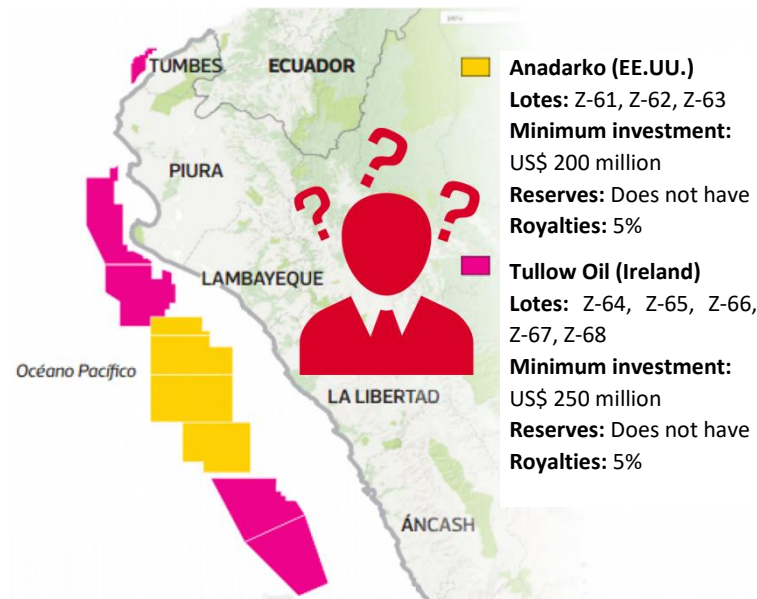
Now opposition to oil activity has emerged from a new group fishermen, who have been led to believe that exploration activities will harm the bio diversity of the area. This assertion is questionable since, artisanal fishing occurs within 5 miles of the coast and the assigned blocks are located more than 40 miles from the coast.

Offshore exploration is an activity where Peru encounters heavy competition from neighboring countries. Neighbors have adopted policies aimed at encouraging oil companies to explore. Sadly, Peru does not offer sufficient guarantees for investments for the country in this area.

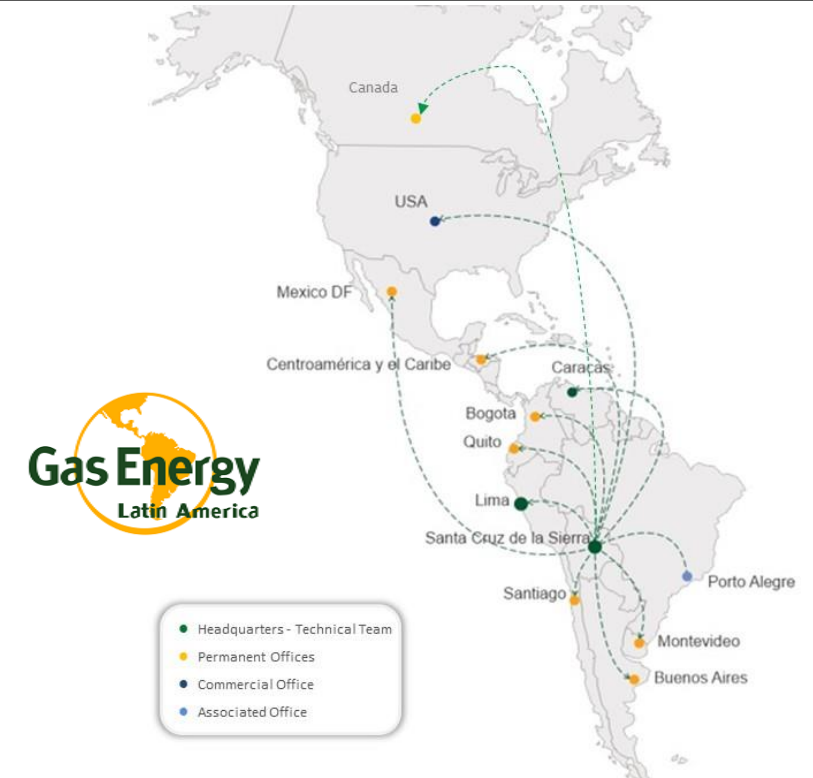
This situation is critical, mainly in a country with low oil production, depends on imports, and has a huge oil potential that has not been developed by 30%.

If the Supreme Decrees approving the signing of the exploration contracts with Tullow oil are repealed, Peru will send a very negative signal to private investors all over the world.

Offshore blocks in questionings



Source: infographics - El Comercio



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