



Ministry of Foreign Affairs and Trade

Faroese Parliament

Date: 28 February 2017
File No.: 16/00932
Caseworker: TP

Parliamentary Bill No. 72/2016: Proposed legislation governing the fourth licensing round for the exploration and exploitation of hydrocarbons.

**Proposed Bill
for an
Act of Parliament
Governing the Fourth Licensing Round
for the Exploration and Exploitation of Hydrocarbons**

§ 1. Pursuant to § 7, Clause 2 of Parliamentary Act No. 31, dated 16 March 1998, governing hydrocarbon activities, this Act stipulates the areas to be offered for licensing and the standard terms and conditions governing the granting of a license in the fourth licensing round for exploration and exploitation of hydrocarbons.

§ 2. The areas to be offered for licensing in the fourth licensing round are the following blocks and partial-blocks of the Faroese continental shelf:

- 1) 6004/1-9, 11-13, 16-17;
- 2) 6005/1-25;
- 3) 6103/1-9, 11-13, 16-17, 21, 25;
- 4) 6104/1-30;
- 5) 6105/3-5, 8-10, 13-15, 17-20, 21-30;
- 6) 6201/1-2, 6;

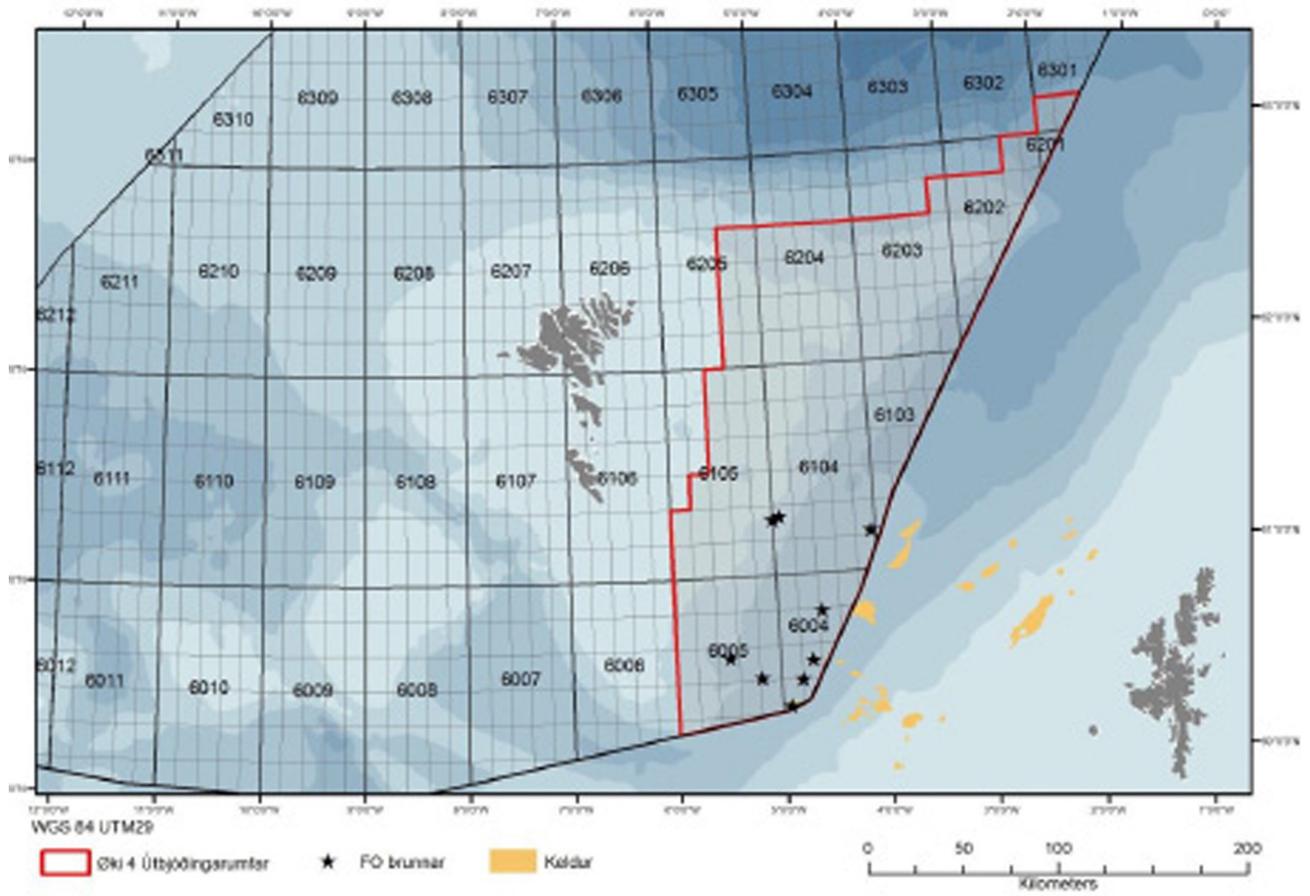
- 7) 6202/4-18, 21-22, 26;
- 8) 6203/10-30;
- 9) 6204/11-30;
- 10) 6205/14-15, 19-20, 24-25, 29-30;
- 11) 6301/26-28;

Stk. 2. Licensing area can be seen on the map, attached as Annex A.

§ 3. Pursuant to § 6 of the Hydrocarbon Activities Act, the Minister awards the licenses for the exploration and exploitation of hydrocarbons. The standard terms and conditions governing the granting of a license are stipulated in the Model License attached as Annex B.

§ 4. This Act shall enter into force the day after it is promulgated.

Fourth Licensing Round Licensing area



**MODEL LICENSE
FOR THE
EXPLORATION AND EXPLOITATION OF HYDROCARBONS
FOURTH LICENSING ROUND**

Jarðfeingi
Faroese Geological Survey

Pursuant to § 6 of Parliamentary Act No. 31, dated 16 March 1998, governing hydrocarbon activities [hereinafter, “the Hydrocarbon Activities Act”] and based on the information provided in the application of the Company, dated _____ and other information, the Minister (hereinafter, “the Minister”) hereby grants a license to engage in the exploration and exploitation of hydrocarbons in the area stipulated in § 2 hereof (hereinafter, “the License”) to the Company or Companies indicated below (hereinafter, “the Licensee”):

Company:

Business Registration No:

Registered Business Domicile:

Share: %

Company:

Business Registration No:

Registered Business Domicile:

Share: %

Company:

Business Registration No:

Registered Business Domicile:

Share: %

The License is subject to the following terms and conditions:

§ 1

In this License, the following terms shall mean:

“Hydrocarbons” – crude oil, condensate, natural gas and other hydrocarbons found naturally in the subsoil that can be extracted in a gaseous or liquid form.

“Hydrocarbon deposit” or *“deposit”* – a contiguous accumulation of hydrocarbons in the subsoil. The Minister shall resolve any question regarding what shall constitute a hydrocarbon deposit.

§ 2

The License is valid for the area(s) indicated on the attached map with relevant corner coordinates and block(s) set forth in Annex I.

2. The mapping and coordinate system implemented herein is based on the geographic latitude and longitude coordinates of the European Terrestrial Reference System 1989 (ETRS89). Each quadrant is labelled according to the south-eastern corner coordinates, e.g. 6105 (N 61°, W 05°). Each individual quadrant is subdivided into 30 blocks of 12 longitudinal minutes and 10 latitudinal minutes each. The blocks are labelled from 1 to 30, beginning in the north-western corner of each quadrant, e.g. 6103/1.

§ 3

The License grants to Licensee in the area(s) referenced in § 2 the sole and exclusive right to explore for and exploit any hydrocarbons, as defined in § 1. Hydrocarbons derived from, inter alia, the destructive distillation of coal, bituminous shale or other subsoil deposits are not included in this License.

2. The License granted herein shall not restrict the Minister, within the area governed by this License, from granting permission to a third-party (i) to undertake prospecting for hydrocarbons in the subsoil, (ii) to explore for and exploit any natural resources not covered by this License, (iii) to establish and operate pipeline facilities intended for activities falling within the scope of the Hydrocarbon Activities Act, (iv) to use the subsoil for storage or for purposes other than production, and (v) to conduct scientific investigations. The Licensee shall endeavour to ensure that the activities permitted under this License do not impede unnecessarily the third-party activities enumerated in the previous sentence, as well as any other hydrocarbon exploration and exploitation activities carried out under other licenses. Jarðfeingi (The Faroese Geological Survey) [hereinafter, “Jarðfeingi”] shall endeavour to ensure that the activities enumerated in the first sentence of this clause and the activities of other licensees provided for under other

licenses do not impede unnecessarily the activities granted to the Licensee under this License.

3. The Licensee shall endeavour to organise its activities and if necessary revise its operations to accommodate the fishing effort that normally occurs in the area. To comply with this requirement, the Licensee, prior to conducting any seismic or other investigations, shall submit to Jarðfeingi in a timely manner a detailed Work Programme for approval.

4. If the Licensee discovers any natural resources not within the scope of this License, the Licensee shall notify Jarðfeingi thereof.

5. In the event that other natural resources may be exploited at the same time as a necessary extension of hydrocarbon exploitation activity, the Licensee shall be entitled to said natural resources unless owned by a third party. The Minister reserves the right to impose upon the Licensee specific terms and conditions with respect thereto, including payment of a special surcharge in the event said additional exploitation is commercially viable.

§ 4

The License Term and Work Programme are stipulated in Annex II. The Licensee shall carry out the exploration programme and the other activities specified in Annex II during the License Term.

2. In the event of any discovery of hydrocarbons, the Licensee shall immediately communicate this fact to Jarðfeingi. No later than eight (8) months after the completion of the well in which the discovery is made, the Licensee shall submit a report on the discovery and a field appraisal programme detailing the work required to ascertain whether exploitation of the hydrocarbon deposit is technically feasible under the conditions present and that the discovery is commercially significant, consistent with best practices within the North Sea oil industry. The field appraisal programme shall include a time schedule and an outline of the work required to support the declaration to be submitted pursuant to § 5, Clause 2 herein no later than four (4) months before the expiry of the Exploration Term stipulated in § 4, Clause 1, (confer Annex II, § 1), or within any extension of the Exploration Term granted by the Minister pursuant to § 8, Clause 1 of the Hydrocarbon Activities Act. Jarðfeingi shall approve the appraisal programme.

§ 5

An extension of the License Term, pursuant to § 8, Clause 2 of the Hydrocarbon Activities Act, for production purposes shall be granted by the Minister for the area delimited pursuant to Clause 3 below for a period of thirty (30) years from the date the extension is granted. Extensions may be granted for one or more areas individually.

2. The extension of a license term, as referenced in § 5, Clause 1 above, is conditioned on that the Licensee (i) has fulfilled all its obligations, (ii) has verified a commercially exploitable hydrocarbon deposit, and (iii) has submitted an application for an extension of the license term no later than four (4) months before the expiry of the term specified in § 4, Clause 1 (confer Annex II, § 1). The application shall certify that a hydrocarbon deposit(s) has been demonstrated under such conditions that exploitation is deemed technically and commercially feasible, and that the Licensee intends to initiate such exploitation. The application shall further stipulate the specific area(s) for which the Licensee requests the extension. The Licensee shall designate the area(s) within the region stipulated in the application that the Licensee believes contains the hydrocarbon reservoir(s). The application shall be accompanied by a report that documents the appraisal of the deposit(s) on which the declaration is based. The report shall contain a description and an evaluation of the deposit(s) with respect to its geology and the technical aspects of the reservoir(s), plus a statement regarding the production technology and the economic assumptions upon which the Licensee's declaration is based.

3. The Minister shall delimit the area(s) for which an extended license term is granted for exploitation purposes, designated by geographical coordinates and depth. The specific hydrocarbon deposit(s) that the Minister deems to have been verified by the Licensee in connection with its request for a license term extension shall be further designated within said area(s). The depth of the delimited area(s) is deemed to extend to at least the end point of drilling and shall include without exception all hydrocarbon deposit(s) for which the extension is granted. If deemed necessary, the delimited area(s) may encompass several deposits. If it is not possible to delimit the size of the deposit(s) with reasonable certainty, the Minister shall take this fact into consideration when determining the extent of any additional area(s) to be covered under the license and their associated depth(s).

4. The area(s) for which the Licensee relinquishes the right in which to explore for and exploit hydrocarbons and the area(s) for which this right is preserved pursuant to § 4 Clause 1, as well as the area(s) for which a license term is extended pursuant to § 5, Clause 1 above shall be contiguous and shall be delimited by longitude and latitude, expressed in whole minutes.

§ 6

Any extension of the license term to be granted pursuant to § 5 above is subject to the following conditions, (i) that, prior to the deadline stipulated by the Minister with respect to the extension of the License, the Licensee shall submit a Field Development Plan for the designated hydrocarbon deposit(s) for approval by the Minister pursuant to § 15, Clause 2 of the Hydrocarbon Activities Act; and (ii) that the Licensee shall initiate production within the time stipulated in the approval.

2. The Minister may promulgate specific directives and regulations governing the content and form of an application, pursuant to § 15 of the Hydrocarbon Activities Act, as well as the information that shall be submitted with or subsequent to said application.

§ 7

On each License Date, the Licensee shall pay an annual fee (see Clause 3 below), based on the size of the licensed area(s). This Area and Environmental Impact Fee shall not be assessed on producing hydrocarbon deposit(s) delimited pursuant with § 5, Clause 3 above. In calculating the size of the area(s), the number shall be rounded up to the nearest whole square kilometre.

2. The Area and Environmental Impact Fee is:

Payment 1 – 6 (i.e., payments for license years 1 - 6)	DKK 750 pr. km ²
Payment 7	DKK 1.250 pr. km ²
Payment 8	DKK 1.750 pr. km ²
Payment 9	DKK 2.500 pr. km ²
Payment 10	DKK 3.750 pr. km ²
Payment 11	DKK 5.250 pr. km ²
Payment 12	DKK 7.750 pr. km ²
Payment 13	DKK 11.250 pr. km ²
Payment 14	DKK 17.250 pr. km ²
Payment 15	DKK 26.250 pr. km ²
Payment 16 and subsequent payments	DKK 39.250 pr. km ²

3. The Area and Environmental Impact Fee for each license year for the area(s) covered by the License shall be paid in advance on each License Date, which is defined as the calendar date on which this License was dated and issued (the “License Date”). If a payment is late, the Licensee shall pay interest at an annualized rate equal to the then current official discount rate set by the National Bank of Denmark (Danmarks Nationalbank), plus 6% from the date the payment is due and payable to the date of actual payment.

4. Of said Fee, 250 DKK per square kilometre shall be set aside for the required environmental impact assessment regarding hydrocarbon-related activities. Jarðfeingi shall administer these funds and shall consult with the relevant governmental authorities and the oil industry on how the funds may best be used.

§ 8

The Licensee shall pay a Hydrocarbon Production Royalty (hereinafter, “HP Royalty”) to be

calculated and paid pursuant to § 8, Clause 2 – 4 and §§ 9 and 10. The HP Royalty shall be paid in Danish Krone (DKK).

2. The amount of the HP Royalty shall be based on the quantity of hydrocarbons produced each quarter (1 January – 31 March; 1 April – 30 June; 1 July – 30 September; and 1 October - 31 December) of each calendar year. All produced hydrocarbons, including the hydrocarbons consumed during production activities, shall be included when calculating the quantities of hydrocarbons subject to the HP Royalty. Small quantities of hydrocarbons that are lost during production or any hydrocarbons reinjected back into the reservoir(s) prior to the measurement point shall not be included in the calculation of the HP Royalty, but such quantities shall be noted in the calculation report submitted to Jarðfeingi.

3. The HP Royalty is two percent (2%) of the value of the production, which is calculated pursuant to the provisions of this License.

4. As and when the Minister determines that the HP Royalty, wholly or partially, shall be paid in-kind, the Minister shall provide written notice to the Licensee of said decision. Within sixty (60) days following the date of said notice, the Minister and the Licensee shall agree on the basis, the location, the measurement procedures (pursuant to provisions governing similar in-kind payments), and the conditions of transfer. Said agreement shall be consistent with the governing principles stipulated in this License and such other usual and customary principles governing the payment of in-kind HP Royalty as the Minister may adopt. In no event shall the decision by the Minister to accept an in-kind HP Royalty payment affect then current HP Royalty payments until payment of the in-kind HP Royalty shall commence. Jarðfeingi shall not incur any costs relevant to the payment of the in-kind HP Royalty, except those that may occur subsequent to the transfer of the in-kind HP Royalty.

§ 9

Said HP Royalty, referenced in § 8, Clause 3, is levied on the value of the quantities of hydrocarbons on which each quarterly royalty is based. The value of the hydrocarbons subject to the HP Royalty shall be established based on the rules in the following Clauses 2 - 6.

2. The valuation of the hydrocarbons produced shall be based on the value at the following Transaction Points:

a) Produced hydrocarbons landed by ship: The value at the shore-based terminal, port or other off-loading point where the hydrocarbons are first landed, without any deduction for transport, handling or other costs incurred prior to such landing point.

b) Produced hydrocarbons landed via pipeline: The value at the point where the hydrocarbons are landed at a shore-based terminal or other land-based facility via a pipeline, without any deduction for transport costs prior to such landing point.

c) In the event that produced hydrocarbons are not landed as set forth in a) or b) above, the Minister, in approving the Field Development Plan, shall determine the relevant Transaction Point at which valuation shall be calculated.

3. If, prior to the date specified in § 10, Clause 1 for submission of the quarterly production statement, the quantity of hydrocarbons recovered during said quarter is sold to a third party pursuant to a binding sales agreement without any prior refining or other substantial processing, said quantity of hydrocarbons shall be valued at the sales price stipulated in the sales contract, if delivery is to be made to the purchaser at a Transaction Point that is governed by the valuation share under Clause 2 above.

4. If the Minister determines that the sales price of the hydrocarbons agreed to by the Licensee does not correspond to the price the Licensee could have obtained through a sale to a third party on the open market, the Minister shall stipulate the value of said hydrocarbons. In his valuation, the Minister shall apply the values assessed for the applicable quarter pursuant to Clause 3 above for similar hydrocarbon sales to third parties, provided that the Minister is able to conclude that such sales can be considered representative of the price level. Otherwise, the valuation shall be based on the prices obtained during the relevant period for the delivery of a similar grade and quality of hydrocarbons via third-party sales on the European open market.

5. The value of that portion of the hydrocarbons not sold to a third party within the date stipulated in Clause 3 above shall be stipulated by the Minister consistent with the provisions in Clause 4 above.

6. In the event that the nominal price for produced hydrocarbons is stipulated pursuant to the provisions of Parliamentary Act No. 26 of 21 April, 1999 on the taxation of income derived from hydrocarbon activities, the valuation of said produced hydrocarbons shall always be based on said representative nominal price, notwithstanding the provisions of this License.

7. If any information required for the calculation of the HP Royalty is not fully known at the time the production statement is to be submitted, a provisional production statement shall be issued pursuant to the provisions set forth under § 10 below. The provisional production statement shall be prepared in such a manner as to state, as closely as possible, the final HP Royalty obligation for the respective quarter. The Minister may promulgate specific rules regarding the basic principles to be followed in the preparation of a provisional production statement.

§ 10

The HP Royalty shall be calculated every quarter. No later than thirty (30) days after the end of each quarter, the Licensee shall submit to the Minister a Production Statement declaring the HP Royalty for the relevant quarter. In those situations governed by § 9, Clause 7, a provisional calculation of the HP Royalty shall be prepared, consistent with the rules in this section.

2. Along with the Production Statement, the Licensee shall submit to Jarðfeingi all information relevant to the calculation of the HP Royalty. The information provided shall include, but not be limited to, the quantities, quality, and grade of the hydrocarbons produced; the density of all liquids, the calorific value and the chromatographic analysis for all gaseous hydrocarbons; the disposition of the quantities produced, including the terms relating to prices, delivery and all other conditions agreed upon with the individual purchaser for a particular sale, and any other special circumstances that might have influenced said terms and conditions. The Minister may promulgate specific rules and regulations governing the submission of information, and may require supplementary information in individual cases.

3. In the event a final or provisional Production Statement is not timely submitted pursuant to Clause 1 above, or the information to be submitted pursuant to Clause 2 above is not furnished by the deadline stipulated by the Minister, the Minister shall determine the HP Royalty. In the event the Production Statement is not made in conformity with the then current rules and regulations, and is not revised by the deadline stipulated by the Minister, the Minister shall determine the HP Royalty. If the Minister determines the HP Royalty, the Minister shall further decide if the HP Royalty shall be considered final or provisional.

4. If a quarterly HP Royalty is deemed provisional, the final Production Statement shall be submitted with the Production Statement for the next subsequent quarter. In the event that any information deemed necessary for the final Production Statement is unavailable, the Minister shall stipulate the final HP Royalty, if said information is not produced prior to the deadline established by the Minister.

5. Provisional HP Royalties and HP Royalties due and payable pursuant to final Production Statements shall be paid to Jarðfeingi by the deadline for submission of the Production Statement stipulated in Clause 1 above. If the HP Royalty is fixed by the Minister pursuant to Clause 3 or 4 above, the HP Royalty deemed due and payable shall be paid no later than seven (7) days after the Licensee receives notice from the Minister of the amount of the HP Royalty.

6. If payment of the HP Royalty is made after the deadline stipulated in the second sentence of Clause 1 above for submission of the Production Statement, interest shall be charged at an

annual rate equal to the then current official discount rate set by the Danish National Bank (Danmarks Nationalbank), plus 6% from the date the payment is due and payable to the actual date of payment. If the Minister stipulates the amount of the Production Royalty pursuant to Clause 3 or 4 above, interest shall be charged at the same rate from the deadline in the second sentence of Clause 1 above. 7. The following rules shall apply if a provisional HP Royalty is paid and it is finally determined in the final Production Statement that the provisional Production Statement resulted in a calculation of an overpayment or an underpayment: In the event of an underpayment, interest shall be charged on the difference between the provisional HP Royalty and the final HP Royalty for each quarterly period from the date of payment of the provisional quarterly HP Royalty until payment is made pursuant to the final Production Statement. The rate of interest shall be an annual rate equal to the then current official discount rate set by the Danish National Bank (Danmarks Nationalbank), plus 2% from the date the payment is due and payable to the actual date of payment. If the final Production Statement demonstrates that an overpayment has been made and that the Licensee is due a refund, the Licensee may deduct said overpayment from the next subsequent payment of the HP Royalty.

§ 11

The Licensee hereby acknowledges and agrees to set aside and distribute 300,000 DKK at the beginning of each License Year as stipulated in Annex II toward meaningful projects related to future hydrocarbon exploration in the territory of the Faroe Islands. This provision is also applicable in the event that the License is extended.

§ 12

The Licensee acknowledges and agrees to provide Faroese companies genuine opportunities, in free and open competition with others, to obtain primary contracts or subcontracts to provide goods and services in connection with the performance of the activities stipulated by this License. In this connection, the Licensee shall comply with the procedures stipulated by the Minister regarding the reporting of initiatives intended by this License to be undertaken by the Licensee related to the tendering of work regarding the performance of the activities stipulated under the License, as well as on the reporting of the terms and conditions governing the contracts to provide said goods and services.

2. The Licensee has the responsibility to ensure that the provisions of § 12, Clause 1 above are followed by its employees, as well as its contractors, subcontractors or other third parties that provide services to the Licensee in connection with the performance of the activities stipulated in this License.

§ 13

The Licensee acknowledges and agrees to provide employment opportunities in the Faroes and

to endeavour to offer Faroese educational and research institutions and the Faroese business community in general the opportunity to participate in such research and development projects that may be undertaken in performance of the activities stipulated in this License. In this connection, the Licensee shall comply with such reporting procedures as may be specified by the Minister.

2. The Licensee acknowledges and agrees to encourage, promote and facilitate the execution of contractual agreements between Faroese companies and foreign contractors engaged in the provision of goods and services to the Licensee in order to augment the competence and technological know-how of Faroese companies in the delivery of said goods and services. In this connection, the Licensee shall comply with the directives and regulations on the submission of reports stipulated under § 33 of the Hydrocarbon Activities Act.

§ 14

The Licensee shall endeavour to develop Faroese competence in the industry and shall bear the costs of such efforts in compliance with the guiding principles that the Minister has promulgated or shall promulgate in the future. The Licensee hereby acknowledges and agrees to set aside and distribute 300,000 DKK at the beginning of each License Year as stipulated in Annex II of this License. This provision is also applicable in the event that said License is extended.

§ 15

Pursuant to § 11, Clause 1 of the Hydrocarbon Activities Act, the Licensee shall transport any and all equipment and passengers via a Faroese quay or a Faroese airport. In special cases, the Minister may issue an exception to this requirement.

§ 16

The Licensee's exploration and production activities shall be carried out from the Faroe Islands to the extent specified, consistent with Clause 2 and 3 below.

2. Within three (3) months after the License has been granted, the Licensee shall submit a plan to the Minister for approval on how and where the land-based activities of the Licensee shall be organized during the exploration phase.

3. A similar plan for the production phase shall be submitted for approval by the Minister along with the application for approval of the Field Development Plan, pursuant to § 15, Clause 2 of the Hydrocarbon Activities Act.

§ 17

If the License is granted to a consortium, said License is granted upon the condition that a Joint

Operating Agreement is prepared regarding the permitted activities within ninety (90) days of the granting of the License. Within thirty (30) days of the execution of the Joint Operating Agreement, said Agreement shall be submitted to the Minister, who may, within ninety (90) days of submission, require the Agreement to be amended to reflect certain obligatory changes and resubmitted prior to the deadline stipulated by the Minister.

2. Any amendment to, deviation from or supplement to said Joint Operating Agreement, including, but not limited to, the designation of a new operator, shall be submitted to the Minister in accordance with the rules stipulated in § 17, Clause 1 above.

§ 18

Pursuant to § 33, Clause 5 of the Hydrocarbon Activities Act, the representative of Jarðfeingi has the right to participate as an observer in the Joint Operating Committee created pursuant to the Joint Operating Agreement referenced in § 17 above.

2. Jarðfeingi shall be provided notice of said meetings with the same advance notice and shall receive the same documents and materials, including, but not limited to, the minutes of the meetings, as provided to the individual Licensees.

§ 19

Pursuant to § 33, Clause 4 of the Hydrocarbon Activities Act, the owner or user of an offshore installation, as well as any party acting on its behalf, shall be required to grant the staff of a governmental supervisory authority all the assistance required for their investigations. Moreover, when said supervisory authority so requests, the Licensee shall assume responsibility for the transportation of the representatives of said public authority from their place of work to and from the location of the relevant activities, and shall also provide accommodation. All associated expenses shall be borne by the Licensee.

§ 20

To ensure in-depth knowledge and oversight of the activities of the Licensee under this License, the Licensee(s) shall submit all information required about its prospecting, exploration and exploitation activities, as well as information about its financial condition, pursuant to the then current rules and regulatory schemes promulgated under § 30 of the Hydrocarbon Activities Act.

§ 21

Jarðfeingi staff, other public officials and individuals under contract with the aforementioned

governmental authorities have a duty of confidentiality pursuant to § 26 of the Faroese Public Administration Act and §§ 152 through 152 (f) of the Civil Penal Code regarding disclosure of confidential information and test samples, etc., as may be received from time to time from the Licensee pursuant to the Hydrocarbon Activities Act and this License.

2. Test samples and/or other confidential information or data covered under § 31 of the Hydrocarbon Activities Act are deemed to be the property of the Faroese people. The Licensee that has submitted said test samples and/or confidential information or data has no right to demand any payment for said test samples and/or confidential information or data that the Faroese governmental authorities may distribute subsequent to the expiry of the duty of confidentiality.

3. Test samples and/or other confidential information or data covered under § 31 of the Hydrocarbon Activities Act may be distributed to entities other than Faroese governmental agencies five (5) years after said confidential information becomes known and available to the Licensee. In the event that the License expires, or the Licensee abandons the License, or the License is totally or partially rescinded, said five-year period shall be reduced to two (2) years, relevant to the area for which the License is rescinded.

4. The provisions of Clause 1 above shall not prevent the disclosure of said confidential information or other data under the following conditions:

a) the dissemination of general information about circumstances surrounding the exploration and/or exploitation provided in due course by public statements, annual reports or the like, or

b) the distribution of confidential information pursuant to collaboration with governmental authorities in other countries, on condition that said country has a similar duty of confidentiality for said confidential information. Proprietary and/or confidential information or information that could reasonably be deemed to be proprietary or confidential received from the governmental authorities in other countries shall be subject to the provisions of Clause 1 above.

§ 22

1. In communications to individuals or to the public, the Licensee shall not, without the prior consent of the Minister, directly or indirectly quote or refer to any statements or communications from the Minister, the supervisory authorities, other public authorities or any person employed by or performing duties for these entities that specifically concern, but not limited to, the probability of discoveries, the size of hydrocarbon deposit(s), or the timing and nature of any hydrocarbon exploitation.

§ 23

Any equipment, procedures and/or measurement tools designed for the qualitative and quantitative measurement and analysis of recovered hydrocarbons shall be approved by the Minister. Measurements shall be taken consistent with usual and customary methods, and under the oversight of the Minister.

2. If it is determined that the methods or equipment used have provided too low a measurement, the shortfall shall be deemed to have existed since the previous inspection review took place, unless it can be documented that the shortfall has existed for a shorter or a longer period of time.

§ 24

If the License is granted to a consortium, each member of said consortium shall be jointly and severally liable for any compensation payable pursuant to Article 7 of the Hydrocarbon Activities Act and for any of the obligations held under this License towards the Faroese Government.

§ 25

To ensure that the Licensee complies with all the obligations under this License, including, but not limited to, any compensation for damages, the Licensee shall provide evidence of sufficient security within thirty (30) days from the issuance of said License in an amount and of a kind that is acceptable to the Minister, including a comfort letter guarantee from the parent company, unless the Minister exempts the Licensee of this requirement. The Minister may subsequently require upon 30-days' notice that such security be amended or supplemented.

§ 26

This License or any part thereof shall not be assigned or otherwise transferred, directly or indirectly, in whole or in part, to any third party or from one co-Licensee to another, without the prior written approval of the Minister. The same restrictions are applicable to the sale of company stock or other ownership interests that may have a direct consequence to the company or other entity that is a Licensee or co-Licensee, or to any agreements entered into by the Licensee or co-Licensee.

§ 27

In the event that the rights granted under this License are relinquished during the exploration phase, said abandonment shall extend to the entire license area, unless the Minister consents to partial abandonment of the area.

2. In the event that the Term of the License is extended for one or more areas for the purpose of production, the Licensee may relinquish the right to similar areas subject to a one-year notice.

§ 28

In the event that the License expires, is abandoned or is rescinded, the Licensee shall not be relieved of its obligations under any relevant legislation, this License or other applicable rules and regulations, conditions or directives.

2. In the event that any part of the Work Programme set forth in Annex II hereto is not performed, the Licensee shall, unless the Minister grants an exemption, pay Jarðfeingi an amount equal to the estimated cost of performing that relevant part of the Work Programme. Such cost shall be calculated in light of the expenses that would have been incurred if a third party were to perform the work on behalf of the Minister upon the expiry of the License.

3. Payment of the amount referenced in Clause 2 above is not conditioned upon the Minister arranging for the completion of the abandoned work.

4. Payment shall be made no later than 30 days after the Minister has submitted a demand for payment.

5. In the event of overdue payments, the Licensee shall pay interest at an annual rate equal to the then current official discount rate set by the Danish National Bank (Danmarks Nationalbank) plus 6% from the date the payment is due and payable to the actual date of payment.

§ 29

The Licensee shall indemnify and hold harmless the Government of the Faroe Islands, Jarðfeingi and all related and collateral parties from any and all disputes, actions, claims or causes of action (including attorneys' fee and costs) brought by a third party arising out of or in connection with the activities of the Licensee or co-Licensee undertaken pursuant to this License.

2. The Minister shall notify the Licensee of any claim falling within the scope of Clause 1 above. In the event that the Minister considers any such claim unjustified, the Minister shall reject the claim, if necessary by bringing the matter before the courts. The Licensee may join any action brought in respect of such claim in accordance with the applicable provisions of the Administration of Justice Act.

§ 30

This License and any activities undertaken pursuant to this License shall be subject to the then current laws in force in the Faroe Islands, including, but not limited to, subsequent amendments

to the Hydrocarbon Activities Act, or relevant regulations or directives. This License shall not be construed in any manner as to restrict the right of the Faroese Government to levy taxes or its authority to issue specific directives or regulations governing how exploration and production activities shall be carried out.

2. This License shall not exempt the Licensee from obtaining any other required licenses and/or approvals pursuant to the Hydrocarbon Activities Act or any other legislation.

§ 31

Licensees that do not have a subsidiary company or a branch registered in the Faroe Islands shall establish a subsidiary company or a branch no later than three (3) months after the License is granted.

§ 32

Any disputes or controversies arising out of or in connection with this License or with the activities of the Licensee undertaken pursuant to this License shall be resolved pursuant to the then current legislation in force in the Faroe Islands, and shall be brought before a Faroese or a Danish court.

2. The venue shall be Tórshavn.

3. Clause 1 and 2 above shall not prejudice the right of the Minister and the Licensee to decide, in any particular case, that a dispute or controversy referenced in Clause 1 shall be resolved by arbitration.

ANNEX I

MODEL LICENSE FOR THE EXPLORATION AND EXPLOITATION OF HYDROCARBONS FOURTH LICENSING ROUND

NOTE: Annex I is provided for illustration purposes only. Based on the offer of the applicant and the determination of the Minister, each individual License Area shall be specifically stipulated.

Area covered by the License (Confer § 2, Clause 1 of the License).

The License encompasses the area represented in block(s) _____,
as shown on the attached map, with the following coordinates

European Coordinate System: ETRS89

LATITUDE

LONGITUDE

Stig Min Sek

Stig Min Sek

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ANNEX II

MODEL LICENSE FOR THE EXPLORATION AND EXPLOITATION OF HYDROCARBONS FOURTH LICENSING ROUND

NOTE: Annex II is provided for illustration purposes only. Based on the offer of the applicant and the determination of the Minister, each individual Work Programme shall be specifically stipulated.

License Term and the Stipulated Work Programme of the License (Confer § 4, Clause 1 of the License).

The following License Term and Work Programme cover the exploration activities that the Licensee shall undertake pursuant to § 4, Clause 1 of License No. for Exploration and Exploitation of Hydrocarbons, dated, which is effective for the License Area represented by block(s) See Annex I.

1. The License Term is years, divided into two parts: (i) an Initial License Term of years with a Fixed Work Programme, and (ii) a Secondary License Term of years with a Conditional Work Programme. In the event that the Licensee does not intend to undertake the Conditional Work Programme, the License shall terminate at the expiry of the Initial License Term.
2. No later than two (2) years after the License is issued, the Licensee shall have acquired km of its own 2D seismic data. Of this data, a minimum of km shall lie within the Licensee's block(s).
3. No later than years after the License is issued, the Licensee shall have drilled one exploration well, pursuant to the following conditions:
4. The exploration well(s) shall be drilled through/to (geological description) or to a maximum depth of metres, whichever is gained first. The decision to drill or to abandon the License shall be taken no later than
5. The acquisition of seismic data and the drilling of the well(s) shall be carried out in a manner consistent with industry best practices and pursuant to relevant governmental directives.
6. Prior to the commencement of the Work Programme, the Licensee may request the Minister to take a decision as to whether the work planned fully complies with the approved Work Programme. In the event that the Licensee relinquishes the license area, in whole or in part, the Licensee shall submit a final report to the Minister on the hydrocarbon potential of the area that the Licensee has abandoned.

Chapter 1. General Comments

1.1 Reasons for the bill

In order to maintain steady exploration activities, licensing rounds are commonly held with regular intervals. Based on previous work conducted on the Faroese continental shelf and the potential that exists to make significant discoveries, in addition to the experiences gained by the authorities from previous exploration activities, the Faroese Geological Survey [hereinafter, “Jarðfeingi”] finds the time appropriate to initiate a 4th licensing round. A draft bill on the fourth Exploration Round is consequently being presented to the Parliament.

1.2 Current legislation

Article 7(1) of Parliamentary Act No. 31 of 16 March 1998 on hydrocarbon activities [hereinafter, “the Hydrocarbon Activities Act”] stipulates that permission to explore and exploit hydrocarbons shall be granted pursuant to publically announced tenders. Pursuant to Article 7(2), the area on offer and the standard terms and conditions shall be set out in a separate Parliamentary act.

The Hydrocarbon Activities Act also stipulates that the comments to the separate bill shall include an assessment of the possible impact of the hydrocarbon activities on navigation, fishing and other commercial activities, and on nature, environment and any other effects on the community, as well as an assessment of the contributions of the activities to stimulating the economy and employment opportunities.

1.3 Objective with the bill

The objective of the Bill is to define the areas to be offered for licensing and to establish the general terms and conditions on which licenses will be granted in the fourth Licensing Round.

Once the act on the Licensing Round is approved, it is the Minister who issues the licenses. The applicants who are granted a license shall comply with the terms and conditions regarding requisite expertise, experience, resources and financial capacity. Moreover, emphasis will be placed on the work programme, which the applicant is willing to undertake.

In addition to initiating the fourth Licensing Round, the hydrocarbon authorities intend to start the preparation for the fifth and sixth Licensing Round in the Faroese region. Jarðfeingi’s experience, including its interaction with the oil companies to be expected to participate in the hydrocarbon exploration and potential exploitation in the Faroese area, indicate that the possibilities for organized long-term hydrocarbon exploration can improve if the authorities and the oil companies work in tandem toward this common goal.

1.4 Review of the re-arranged exploration regime

1.4.1 Background

Three licensing rounds have been held to date. The first was in 2000, the second in 2004/2005, and the third licensing round was held in 2008. Moreover, licenses were granted in 2013 according to an open door system, which allows the offshore installation to issue licenses in areas included in previous licensing rounds and pursuant to the previous terms and conditions.

The oil companies showed substantial interest for the first licensing round. Considerable amounts of hydrocarbons were already discovered in the British sector adjacent to the Faroese region, and seismic data indicated similar presence of hydrocarbons in the Faroese sector. The interest was concentrated at the Judd Basin whereas it was considerably less elsewhere on the Faroese continental shelf. It was accordingly decided to issue two types of licenses, lasting for 6 and 3+6 years, respectively. The six years licenses were intended for the Judd Basin and presumed the inclusion of one or several well commitments, whereas licensees elsewhere had the option of spending the first 3 years on preliminary studies prior to committing to exploration drilling. The outcome was four 6-years licenses in the Judd Basin and three 3+6 years licenses outside the Judd Basin.

With the view to diversify the exploration activities with respect to geographical regions, exploration concepts and oil companies on the Faroese continental shelf, the second licensing round was initiated in 2004. However, modest drilling results from the first licensing round reduced the interest among the oil companies considerably for the second round albeit some encouragement resulted from the discovery of hydrocarbons in reservoir rocks within the volcanic section in the adjacent British sector.

Due to the great diversity of the Faroese region, it was decided to allow for increased flexibility in the licensing terms in the second licensing round. This resulted in seven new licenses with 4 to 8 years terms. The exploration models were partly similar to previous models but the round also included some new models and two new operators entered the area. Due to reduced expectations, the work programs only included data acquisition and processing although license 008 was subsequently extended to include a well commitment.

In 2008 and 2009, most licenses reached the stage where decision was to be taken as to potential extension with additional terms or, alternatively, they had to be relinquished. Despite the reduced exploration interest in the Faroese region, it was decided to proceed with the third licensing round in order to ensure continuous exploration. The result was three new licenses which included data acquisition and processing.

At this stage, large parts of the overall region considered suitable for hydrocarbon exploration were covered by licenses and, consequently, it was decided to introduce an open door system in order to facilitate the promotion of individual exploration prospects and to accommodate potential sudden interest from oil companies. Two such licenses were issued in the Judd Basin in 2013.

1.4.2 Summary of main terms

The area proposed to be included in the fourth licensing round is 31,888 km² wide. It is a continuous area extending from the Faroe-Shetland Channel in the east, to the region south-west of the Faroe Islands – see Annex A.

The intent behind offering this area for exploration is to create the foundation for on-going exploration undertakings, the purpose of which is to map out the extent of the hydrocarbon resources and to fully explore the potential for commercial hydrocarbon production in the Faroes. Continuous exploration activities in this area will also create the foundation for the preparation of the fifth and sixth licensing rounds.

During the preparation of the fourth licensing round and while administrating the Work Programmes stipulated in the existing licenses, Jarðfeingi will keep the purpose of the Hydrocarbon Activities Act fully in mind, namely to provide for prudent and appropriate exploration and exploitation of hydrocarbon resources for the benefit of the Faroese economy and employment opportunities. The activities shall be planned with due consideration given to fishing, navigation, the environment, nature and other interests of society.

Not all the terms and conditions for the oil companies' activities are included in this bill. Tax issues are governed by Parliament Act No 26, dated 21 April 1999 on taxation of revenue relating to hydrocarbon activities, as amended (special taxes), and by Parliament Act No. 16 of 14 February 2000 on assessment, collection, audit, etc. in connection with taxation of income derived from hydrocarbon activities.

Simultaneously with the presentation of the bill on the fourth licensing round, some amendments in the taxation legislation are being prepared. Jarðfeingi has prepared a draft bill proposing that ship crews working in the Faroese area will not be eligible for taxation until the individual person has been present in Faroese territory more than 30 days within a period of 12 months or in time intervals, which sum up to more than 30 days within a 12 months period. This proposal accommodates enquiries from these ship crews, in order to facilitate the companies' administration. The reading of the mentioned amendments of the taxation legislation is not part of the reading of the present bill.

It is also proposed to make a slight amendment to the Act on Hydrocarbon Activities. It is proposed to amend Article 8(1) in a way to facilitate the extension of existing licenses by four years rather than only two years as in the current text. No intention is though to extend the maximum total licensing term of 16 years.

All other Faroese legislation remains in force.

It is recommended that the same licensing regime for the first, second and third licensing round be used, wherein the Minister stipulates in the exploration license how the license term shall be organized and what exploration obligations are binding under the license. The exploration obligations that shall be imposed on each licensee should mirror the assumed exploration potential for each license area.

The purpose is to ensure that the terms and conditions reflect the competitiveness of the Faroese region in terms of exploration activities as well as the potential of discovering hydrocarbons in the individual license blocks. An additional purpose is to ensure a stable regime for hydrocarbon exploration and exploitation in Faroese waters, which is considered more important for the oil industry than introducing convenient yet more variable terms.

Pursuant to the Hydrocarbon Activities Act and the Model License (Annex B of the Licensing Act), the licensees are bound to ensure that Faroese businesses are offered actual opportunities, in free and open competition with others, to provide goods and services to the licensee(s) as either the principle contractor or the subcontractor. At the same time, the licensees have the responsibility to diligently strive to encourage an environment in which Faroese and foreign companies and governmental agencies enter into agreements that foster the development of Faroese competencies within and technical

knowledge of the oil industry. This shall be done with the intent of making Faroese companies more competitive and encouraging them to enter into new markets.

The license applicants shall pay an application fee of 50,000 DKK upon applying for a license to explore and exploit hydrocarbons. In addition, upon being granted a license to a certain part of the continental shelf, the licensees shall pay an annual area fee and a fee for the environmental impact assessment. The fee shall be based on the size of the area covered by the license.

A production fee (royalty) of 2% shall be paid on the hydrocarbon extracted, pursuant to the following provisions in section 5.3 of this Annex . In addition, a business tax of 27% is levied on production, as well as a special tax. Under this tax regime, the total taxes/duties due the national treasury equates to less than 57%.

1.4.3 Summary of the first, second and third Licensing Rounds, and the Open Door licenses

On 17 August 2000, seven licenses for exploration and exploitation of hydrocarbons were issued in the first licensing round, four of which were 6-year licenses located in the Faroese part of the sedimentary Judd Basin in the south-easternmost portion of the continental shelf, adjacent to the British sector, where there is very limited basalt occurrence that would hinder oil exploration. Furthermore, this area is near producing oil reserves in the British sector. Oil companies had sufficient seismic data available in the Judd basin well before the licensing round was initiated. Thus, it was well known prior to the first licensing round that there would be competition for these blocks. The combined work programmes for the licenses that were granted encompassed eight wells, as well as seismic studies.

Three 9-year licenses were issued outside the Judd Basin in regions where the expected prospective sediments are covered by basalt. The work programmes agreed upon for these licenses covered a three-year period, wherein the licensees should undertake various geophysical surveys and studies that could assist in the determination of whether to undertake exploration drilling in these areas.

As mentioned, four of the wells agreed upon for the 6-year license areas were exchanged for two exploration wells in the basalt covered 9-year license areas L006 and 007 outside the Judd Basin. In the remaining 9-year license, L005, the first 3-year period was succeeded by six years on the basis of a well commitment. As part of the work programmes, it was also agreed that the licensees should set aside a total of nearly 40 million DKK towards research projects with a view to future hydrocarbon exploration.

The Hydrocarbon Activities Act stipulates as well that the licensees should strive to develop the local oil industry competence not only of individuals, but also the for Faroese business community as a whole. It was agreed that the oil companies should dedicate around 84 million DKK for this purpose.

On 17 January 2005, seven other licenses were granted in addition to the first seven licenses granted for the exploration and exploitation of hydrocarbons. The areas that were licensed extended more to the north and west along the boundary with the United Kingdom, compared with the first licenses. The license areas offered in this subsequent round, most prospects are covered by basalt. In spite of the basalt, it is possible in these areas to map out interesting structures that could serve as reservoirs of oil and gas. The work programmes that were agreed upon for the second licensing round were combined into an initial phase with the focus on the acquisition and interpretation of seismic and

other data before a decision would be taken on whether to proceed with the next phase of the work programme that would focus on more detailed surveys or an exploration well. The result was that the licensees in L008 committed to drill a well.

It was also agreed to support Sindri with about 10 million DKK and to spend 13 million DKK on advancing the local competence within the oil industry.

Three additional licenses were issued on 8 December 2008. The area on offer extends along the entire Faroe-Shetland Channel, the Faroe Bank Channel, the Wyville Thomson Ridge and a little further to the west from here. All the applied license areas were covered by basalt. In the licenses, which lasted between 3 and 6 years, the companies committed to reprocess and/or acquire new seismic and other data before potentially deciding to drill an exploration well. DKK 2.4 mio. were allocated for local industrial competence building and research with a view to future hydrocarbon exploration.

On 25 June 2013, two licenses were issued in the Judd Basin where the first four wells were previously drilled. This was part of an 'open door' system. The prospects covered by these licenses included the Marjun discovery and the region where the two wells, Svínoy and Marima, are located. The licensee committed to reprocess seismic data and perform other investigations during the three year term of these licenses, before potentially deciding to drill an exploration well. DKK 1.2 mio. were allocated for local industrial competence building and research with a view to future hydrocarbon exploration.

All committed work programs have by now been completed and all licenses relinquished.

1.4.4 Results of the exploration drilling

To date, four exploration wells have been drilled on the Faroese continental shelf in the Judd Basin. Three wells were drilled in 2001 and one in 2003. The results from the exploratory drilling varied. All the wells targeted sandy sediments corresponding with those in the Foinaven and Schiehallion fields east of the boundary with the United Kingdom. Such comparisons proved to be unreliable, because the play models failed. These strata contained high-quality sandstone sediment, which generally can hold hydrocarbons, but in this case, in the main, they were filled with water and only small amounts or traces of hydrocarbons.

A large quantity of sand, compared to shale, was one reason why the play types failed. The third well, Marjun, which was drilled by Amerada Hess in 2001, was drilled deeper than the commitment depth. The borehole went through around 170 m of hydrocarbon bearing sandstone and clay sediment from the lower Palaeocene period. The production potential of the reservoir rock in this stratum is modest because of the large depth. However, there is still insufficient data available to determine if commercial production is possible, given the technical possibilities for exploitation and access to existing infrastructure for transport of the produced hydrocarbons.

After verification of the results from the drilling in the Judd Basin, exploration is now focused on the so-called "structural" play types in areas outside the Judd Basin, e.g. on and around the East Faroe High, which is very similar to the Corona Ridge within a UK region where significant deposits have been found in recent years.

In 2006, an exploration well was drilled in license area L006 through thick basalt layers to determine if hydrocarbon bearing sediments were present at a deeper level. Even though only traces of gas were measured in the well, the drilling was successful in the sense that: (i) the drilling operation went well, (ii) the thickness of the basalt in the region was established, and (iii) there were indications of a working hydrocarbon system below the borehole's termination depth. This is useful information that can support further exploration.

In October 2007, BP undertook the overall sixth exploration well in the Faroese region, named William, in license area L007. This well was also in an area where the anticipated thickness of the basalt was more than that encountered in the first four exploration wells. After affirmation that the main prospect in this well only contained volcanic rocks, it was terminated without encountering any trace of hydrocarbons.

The William well was drilled in the winter period and due to poor weather, more than half of the time was spent on stand-by. Together with a decision to somewhat moderate the original obligations of BP, this was the reason why the well did not reach a deeper target, which apparently is located near the base of the basalts, based on current knowledge.

In the third of the 9-year licenses from the first licensing round, L005, operated by ENI, a well was drilled in 2008. Technically, the drilling went well and substantial amounts of gas was encountered in the basaltic section. Due to poor reservoir quality, the prospect was however not deemed of interest. ENI terminated the well at the committed depth after having confirmed that it had penetrated the basaltic column without encountering reservoir rocks of the deeded quality.

In the autumn of 2012, Statoil, as the operator, initiated a new exploration well in license area 006 to test if gas could be found at larger depths than the termination depth of the previous Brugdan well. After a successful start of the well, technical problems and poor weather conditions caused the suspension of the well during the winter. 2013 was spent to assess how to organize the further drilling to larger depths, and the well was re-entered in 2014. It confirmed that still more volcanic strata were present at depths, and it was consequently decided to terminate the well without having encountered any reservoir rocks or hydrocarbons.

Statoil, as the operator, also drilled a well in license area 008 in 2014. The aim was to find hydrocarbons in the strata above as well as in between the basaltic sections. The former prospect proved to hold good quality reservoir rocks although without any hydrocarbons, while neither hydrocarbons nor any reservoir rock were found in the latter prospect.

1.4.5 Main aspects of the fourth licensing round

The main aspects of the fourth licensing round are outlined below. They deal with e.g. the area intended to be put on offer in the round together with the terms and conditions in relation to exploration (work programme) as well as financial and industrial aspects. Section 5.6 touches briefly upon some additional general obligations.

Three licensing rounds have been performed to date, where the Faroese authorities have offered interested oil companies to explore for hydrocarbons in some particular areas. Moreover, two licenses have been issued pursuant to the 'Open Door' system where one oil company on its own initiative

applied for a license to further investigate the hydrocarbon potential in an area which previously had been covered by a separate license.

In all three previous licensing rounds, oil companies have showed interest and willingness to make offers in certain areas, and additional licenses have been issued to an oil company applying on its own initiative for permission to explore in areas that it deemed interesting. Considerable amount of work has been performed pursuant to these licenses and in cooperation with the oil companies, the Faroese authorities have got a thorough overview and understanding of large parts of the Faroese continental shelf. In this respect, it is deemed crucial that the authorities cooperate closely with the oil companies where the authorities issue licenses to explore for and exploit hydrocarbons in certain areas, while the companies in turn use their resources and expertise to investigate if hydrocarbons may be present in the licensing areas.

The Faroese region is still juvenile with respect to exploration with only nine wells drilled to date, although it has been confirmed to hold hydrocarbons in the subsoil. Moreover, large structures are known, which may contain considerable amounts of hydrocarbons, both in previous licensing areas and west of the islands.

Hydrocarbon exploration is a time consuming undertaking needing very large financial resources as well as know-how and ability to analyze the acquired information from the investigated areas. The long-term aspect relates to the exploration activities and not least to potential production, in the event that recoverable amounts of hydrocarbons are discovered.

In order for both the authorities and the oil companies to plan their long-term strategies for future exploration activities in the Faroese region, it is proposed to initiate the preparations of the fifth and sixth licensing round in continuation of the fourth licensing round. Jarðfeingi believes this will facilitate continuous exploration activities... and create the basis for investigating the hydrocarbon potential in the Faroese region at large.

In the event that the preparatory work towards the fifth and sixth licensing rounds show an actual basis for the initiation of these rounds, respective draft bills for these rounds are to be prepared and presented to the Parliament for approval. It will thus be the parliament that, ultimately, decides if, when and on which conditions each of the licensing rounds are to be implemented.

1.4.6 Motivation for the implementation of the fourth licensing round

When Statoil initiated their last drilling operations in 2014, the time seemed right for starting to prepare one more licensing round. In case Statoil discovered substantial amount of hydrocarbons, such a round would accommodate the expected reaction of the industry. In the opposite case, most of the existing licenses would most likely be relinquished. In the latter case, which actually materialized, all existing data would have to be re-interpreted in order to promote the area based on the new information, with a view to interest as well as geological challenges.

The knowledge of the Faroe-Shetland Channel is considerable compared to the remaining part of the Faroese continental shelf and due to the general situation in the oil industry, the companies are reluctant to explore new regions. The fourth licensing round is consequently focused on the Faroe-Shetland Channel while existing data and knowledge from the remaining part of the shelf is investigated with a

view to future licensing rounds. This way, Jarðfeingi can focus its resources to promote this particular area and optimize the chances for a successful outcome.

The area on offer includes previous license blocks, which has been relinquished, in addition to non-licensed regions (see Annex 1).

In terms of exploration, the area on offer is three-fold:

- The Judd Basin, which is part of the Faroe-Shetland Channel where the first four exploration wells were drilled. The knowledge base is relatively good in this basin and the technical risk correspondingly low although the results from the first wells destroyed the so-called Foinaven play model, which was the basis for those wells, lost its relevance. Jarðfeingi has however developed a new play model, which has caught the oil companies' attention.
- The Faroe-Shetland Channel at large where new mapping by Jarðfeingi gives a better understanding of the region including its most promising structures.
- The Fugloy Ridge, which is a large structure although little is known about its exploration potential. The technical and financial risk is correspondingly high, though its mere size creates attention among the oil companies.

1.4.7 Arguments for the preparation of the fifth licensing round

The purpose of the fifth licensing round is to provide the prerequisite for investigating the possibilities for the presence and recoverability of hydrocarbons in the region to the west of the Munkagrannur Ridge, including the Wyville Thomson Ridge, Faroe Bank Channel, Bill Baily Bank and Lousy Bank, with intermediate basins.

These regions differ in character:

- Faroe Bank Channel, Wyville Thomson Ridge and Ymir Ridge appear to have undergone considerable volcanic activity. The Wyville Thomson and Ymir ridges are, however, very large structures with the potential to hold large quantities of hydrocarbon, in case these have not been too negatively affected by the volcanic activities.
- Very little data exists from the Bill Baily and Lousy banks and thus, the knowledge of this region is limited. Efforts are currently being made to initiate data acquisition in the area in order to improve the knowledge base and assess the likelihood of an active hydrocarbon system to be present.

The region of Bill Baily and Lousy banks have not previously been on offer for hydrocarbon exploration and the potential impact on the environment and fishing industry needs to be assessed before a final decision can be taken as to which parts of this region can become subject for the fifth licensing round.

The oil industry shows limited interest for these regions at present, the reason however being mainly due to the current state of this industry and the limited knowledge of the area. The British authorities, nonetheless, have spent quite some money on data collection in their adjacent part of this region and subsequently put it on offer for hydrocarbon exploration.

1.4.8 Arguments for the preparation of the sixth licensing round

The Faroe Platform, Munkagrannur Ridge and Faroe-Iceland Ridge constitute an overall area of very limited knowledge as to the deeper substrata. Different models have been proposed although discrepancies between them just seem to reflect the lack of knowledge.

The different sub-regions in this area differ in character:

- Munkagrannur Ridge is an extensive, elongated structure extending southward from Suđuroy which, in geological terms, can be included. Existing data from this area indicate a limited depth to substrata, which may be subject to hydrocarbon exploration.
- Faroe Platform seems to be covered by thick volcanic layers. Different models, however, emphasize the need for further investigation before making any conclusion in this respect.
- Faroe-Iceland Ridge is a region of controversy as to its ‘continental’ or ‘oceanic’ nature. In the former case, but not in the latter, this very large structure will be of interest for hydrocarbon exploration. This necessitates further knowledge before a decision be made to potentially include this ridge in a licensing round.

All areas subject to investigation with a view to future licensing rounds are environmentally sensitive and need to be assessed with respect to potential impact on fishing activities before any final decision can be made as to which particular regions should be included in future licensing rounds.

1.4.9 Exploration conditions

It is recommended that the same simple and flexible license regime used in the third licensing round be used, wherein the Minister grants licenses that stipulate how the license term shall be organised, and what obligatory work programmes are to be undertaken under the license. Pursuant to the Hydrocarbon Activities Act, licenses for hydrocarbon exploration can be granted for a period of up to 12 years, which may be extended for up to two years at a time for a total of 16 years at most.

As mentioned in section 3 above, an amendment to this clause is proposed in order to allow for extension of the licenses of up to four years at the time. A corresponding proposal to amend the Act on Hydrocarbon Activities will be presented to the parliament simultaneously with the present proposal. The offshore installation expects such a possibility for extending the licenses for more than two additional years to be advantageous in relation to the negotiations with the oil companies with a view to establish reasonable terms and conditions for their exploration activities. It will likewise facilitate the authorities’ administration.

1.4.10 Taxes and Fees

Matters related to taxes and fees are set forth in the Hydrocarbon Taxation Act, in the licenses and in regulations and directives promulgated under authority of the Hydrocarbon Taxation Act.

The Hydrocarbon Taxation Act stipulates what activities are covered by that Act. Briefly, the Act imposes on oil companies and their subcontractors the requirement to pay tax on its activities and for individuals to pay personal income tax. Faroese companies acting as subcontractors for the oil industry do not have to prepare a special tax report regarding their participation in these activities because their commercial activities are covered by the income tax report normally prepared by the company.

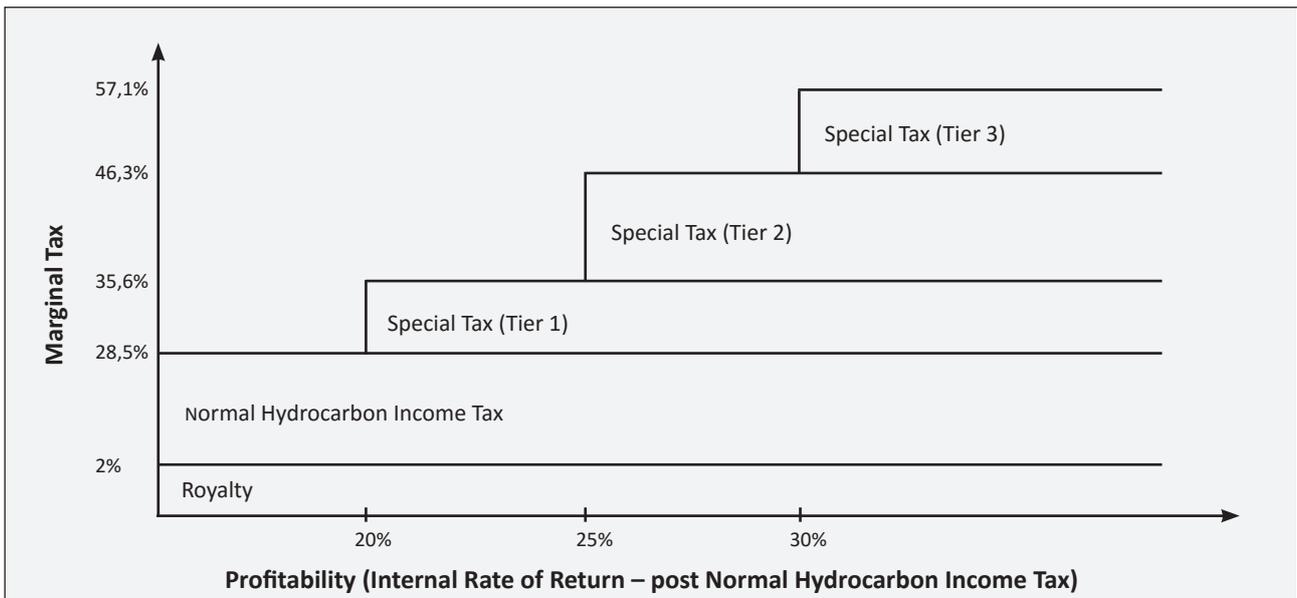
As mentioned, a proposal is being prepared to ensure that ship crews working in the Faroese area will not be eligible for taxation until the individual person has been present in Faroese territory more than 30 days within a period of 12 months or in time intervals, which sum up to more than 30 days within a 12 months period. This proposal accommodates enquiries from these ship crews, in order to facilitate the companies' administration. The reading of the mentioned amendments of the taxation legislation is not part of the reading of the present bill.

One goal of the hydrocarbon tax regime is that it shall ensure the Faroese community its financial share. Another goal was to design a tax regime that would be consistent and predictable, meaning that it should be so structured that it would be unnecessary to repeatedly amend it, even though circumstances to a certain extent might change. The hydrocarbon tax regime is therefore two-fold: one part is corporate tax, which levies taxes on "ordinary" income; the other aspect of the tax regime relates to a special tax, which is triggered by especially high earnings from oil production. The corporate tax for oil companies is 27%. In the event that an oil company earns a high income, it shall also pay a special tax. This special tax is in three stages, dependent on the rate of profitability. If the rate of return on investment and operations is less than 20%, there is no special tax levied. If the rate is between 20% and 25%, a special tax of 10% is levied, etc. If the rate is 30% or greater, the special tax is 40%, which is the highest rate in effect.

In addition to taxes, pursuant to §§ 8 – 10 of the Model License, the intent is to levy a Hydrocarbon Production Royalty (HP Royalty) on the income of the oil companies. In the first and second licensing round, the HP Royalty was 2% and it is recommended that the HP Royalty remains unchanged in the fourth, fifth and sixth licensing round. The production royalty shall be calculated on the gross value of hydrocarbons sold. This means that when the first barrel is sold, the production royalty shall be paid into the national treasury. This is not the case with taxable income because a company is not subject to taxation as income is earned. Current and carried forward costs shall be recouped first.

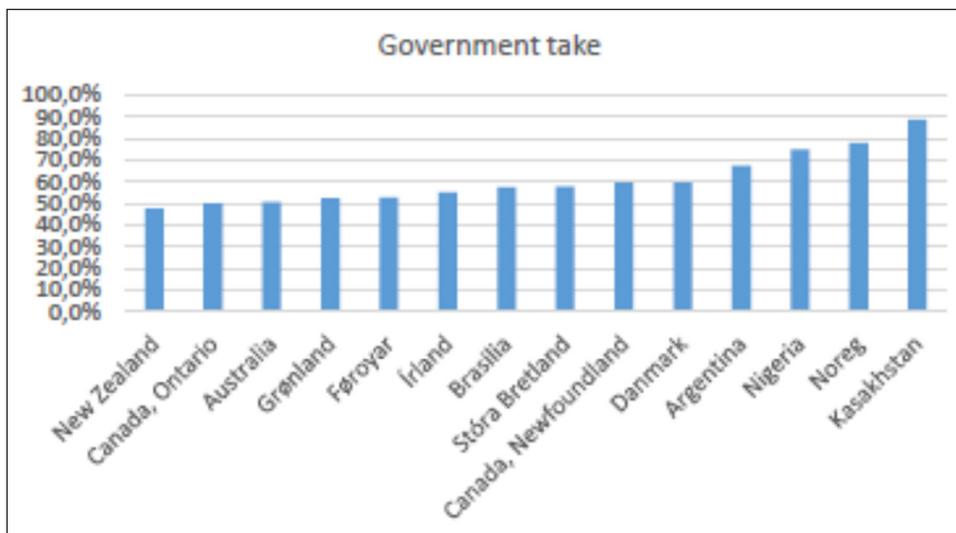
The levying of a production royalty was the normal practice in many countries, but it is not so today. The reason is that to a certain extent such a royalty dampens the exploration interest of the oil companies because, as production from a field decreases or becomes marginal, the operational costs thus become proportionally higher. Thus, a gross production royalty could be one reason why production would be discontinued sooner than otherwise may have been the case. One should therefore be cautious with the application of this method of ensuring the national treasury gains a share of the wealth earned by the oil companies. A production royalty of 2% is, nevertheless, not believed to have any significant impact on oil company interests.

The production royalty can be deducted as an expense from taxable income in calculating the corporate as well as the special tax. An oil company's corporate tax can be deducted from the taxable income for purposes of calculating the special tax. For purposes of clarity, the total tax burden for oil companies is set forth in the Table below.



If the oil companies have a profit margin of less than 20% of investment and operational costs, they would pay around 28.5% in taxes and production royalty. If they come to the highest tax threshold, they would pay around 57% in taxes and production royalty, but this is conditioned on a profitable rate of return of more than 30% of their investment and operational costs.

Compared with some of the oil producing countries, including countries in our region of the world, the Faroese taxation level is below average – as demonstrated in the figure below.



In addition to taxes and the HP Royalty, the oil companies, pursuant to § 7 of the Model License, are obligated to pay an Area and Environment Fee for the areas they are allocated. The fee is 750 DKK for each square kilometre for the first six years and increases to 39,250 DKK at year 16 and possible subsequent years. If hydrocarbons are produced in an area, this fee is not required for that area.

The national treasury has derived some income from the exploration activities that have taken place to date. The paid-in taxes from companies and individuals that are not domiciled in the Faroes have amounted to around 63 million DKK through and including 2007. In addition, the area fee has been some 32 million DKK. Income from the fees for the collection of seismic data has been 15 million

DKK. Altogether, hydrocarbon-related activities generated around 110 million DKK. Taxes and fees from companies and individuals domiciled in the Faroes levied on income from hydrocarbon-related activities have not been calculated separately, thus it is not possible to state how large this revenue has been for the national treasury.

1.4.11 Double taxation agreements

For oil companies and their employees who work in a variety of countries, taxation issues are a significant determinant in the evaluation of how attractive a particular country might be to work in. Aside from the tax burden, etc. in the various countries, the oil companies also focus on the tax agreements that exist between countries. This is where double taxation treaties are very important. These agreements ensure that a company does not pay tax on the same income in several countries. We have long had double taxation agreements in place with e.g. the other Nordic countries and the United Kingdom.

1.4.12 Faroese participation in oil industry activities

It is self-evident that we in the Faroes should attempt to gain as much as possible from the oil industry undertakings, first with regard to exploration, and subsequently from development and production initiatives. The terms and conditions of the exploration licenses were constructed in such a way that the Faroese business community should have the possibility to effectively participate in the oil industry:

(i) funds would be set aside for the development of the requisite competencies; (ii) the licenses stipulated specific conditions wherein Faroese companies could effectively participate in tenders for services in competition with others; (iii) the oil companies should facilitate linkages between Faroese and foreign companies; (iv) there should be focused efforts to ensure that the Faroese could obtain work and that Faroese researchers should have the possibility to participate in research that the licensees would be initiating relevant to their exploration undertakings in the Faroese region.

Experience has shown that it is not easy to effectively promote and implement Faroese participation in the oil industry. This is due partly to the fact that drilling activities are so sporadic. When many years pass with no drilling, and different licensees undertake drilling operations, it would appear not an easy task for the oil industry and local industry to cooperate. Faroese companies have, however, developed and strengthened considerably in this field and are now offering multiple services to the international oil industry.

1.4.13 Faroese supplies

§ 11 of the Hydrocarbon Activities Act stipulates that all transport to and from the Faroese region shall take place via Faroese ports or the Faroese international airport. In addition, § 12 in the Model License stipulates that Faroese companies in free and open competition with others should be afforded genuine opportunities to tender the goods and services needed by the licensees in connection with their activities in the Faroese region.

These provisions should ensure that Faroese companies could participate in hydrocarbon exploration activities, and they have actually resulted in certain activities. Most of the current oil industry related activities within Faroese companies does however not directly relate to these stipulations but results from determined efforts among these companies to themselves as providers of services to the oil industry in several countries, and not only in relation to the sporadic exploration activities in Faroese waters.

The oil companies consider the obligation to have all their goods and staff transported via a Faroese port or airport, and to change their providers during their usually single well operation in Faroese waters, as a burden. They can neither see how this stipulation by any actual means helps to improve Faroese expertise.

The offshore installation and Jarðfeingi find these stipulations worth to continue, although it should be evaluated how they can help providing Faroese companies with durable assignments.

1.4.14 Linkages with foreign companies, employment options and research

Pursuant to § 13, Clause 1 in the Model License, the licensees should strive to facilitate agreements between Faroese and foreign companies with the goal of enhancing competency and technical knowledge. As part of this competency development, Faroese companies have also been assisted in the forging of linkages with foreign companies through which they could gain the skills necessary to participate in the international marketplace.

If the results are to be more widely disseminated, it is necessary to steadily work on this goal. To bring about such agreements is especially demanding and time consuming. It is difficult to say whether this is one reason why companies that have worked toward this goal nevertheless give up. One reason for this is possibility that the licensees have not placed sufficient emphasis on this requirement. The offshore installation and Jarðfeingi therefore will strive specifically to ensure that the licensees pay strict attention to this provision.

Pursuant to § 13 in the Model License, the licensees shall also strive to offer employment opportunities to Faroese workers. In the main, what has spun out of this stipulation to date is that Faroese workers have been employed in the offices maintained by some oil companies in the Faroes. There have also been some individual jobs on the offshore installations. Some Faroese have offered their services to the oil companies, but not in connection with the license provision.

§ 13 as well stipulates that the licensees should strive to give Faroese governmental agencies and companies the possibility to participate in research and development projects, if undertaken in connection with the work programme of the license. As part of this requirement, the licensees have agreed to set aside funds for such R&D projects as described elsewhere in these comments, which have importance for future oil exploration in the Faroese region. As a consequence, Faroese research facilities are participating in research and development projects that are focused on geological issues.

In addition, the licensees have supported Faroese PhD studies and the training at the University of the Faroe Islands and the Faroese Business School, as part of their obligation to support competency development.

1.4.15 Competency Development

As part of their overall license obligations, the licensees in the previous licensing round agreed to facilitate industry-related business development. In the first licensing round, some 85 million DKK was allocated for this purpose, in the second licensing round around 13 million DKK was allocated,

in the third round the amount was 2.4 million DKK, and the Open Door licenses gave 1.2 million DKK for this purpose.

Each licensed consortium adoffshore installations its own funds set aside for this purpose. If there is any doubt as to whether or not a particular project could be deemed an industry-related business development, the relevant companies shall decide, in consultation with Jarðfeingi. Once a year, the various consortia shall submit a report to Jarðfeingi on how these funds have been used.

In order to ensure a flexible process, the acceptance criteria were structured as simple as deemed advisable. Simple rules made it possible to easily judge whether or not a project was related to business development and thus could be undertaken with oil company support. Although opinions might differ on just how “business-related” a funded project might be, there has never been any disagreement on just how beneficial these projects have been to Faroese society in general. The alternative to this flexible regime is a more rigid scheme, but there is no indication that a more rigid scheme would be better.

Business development projects have been used to support training of staff, innovation in equipment and production, development of quality control processes, management skills and research, etc. Education support is especially intended for higher education. The University of the Faroe Islands and the Faroese Business School have received funding. Support is especially provided to the University for the training of PhD candidates and education in oil engineering. PhD coursework is focused on, e.g., subjects related to the oil industry, wave modelling and fish farming in open waters. The Faroese Business School has offered, inter alia, management training in association with Robert Gordon University in Aberdeen.

The scheme has on the whole worked well. It has been suggested, however, that some changes should be introduced. One suggestion is that the a specific amount should be stipulated for competency development, rather than competency development being just another parameter of drilling that is subject to negotiation. The other suggested change relates to who should adoffshore installation the funds.

The amount that is dedicated to business competency development will never equal what was allocated during the first licensing round, but will more resemble that which was allocated during the second licensing round. That such funds should be negotiated as part of the drilling parameters, is therefore believed to be unnecessary. It is simpler to stipulate a specific amount and then let the negotiations focus on the content of a specific work programme, i.e., the geophysical work to be undertaken.

It is suggested that the fee for business competency development (§ 14 in the Model License) be set at 300,000 for each license to be paid at the beginning of each license year. If a license were granted for five years, for example, the total fee for the license would be 1.5 million DKK.

The licensees are not in complete unity as to what is the best way to administer these funds: whether they themselves should undertake this or whether it should be handled by someone else. Some feel that it would be advantageous that the oil companies themselves administer the funds, while others see it as an administrative burden. Jarðfeingi is of the opinion that it does not matter who administers the funds, if the funding principles are clear and actionable. Therefore, it should not be a problem if some

licensees wish to administer their competency development funds themselves, as long as the Minister has the authority to stipulate who shall administer said development funds if certain licensees have no interest in administering these funds. For example, one could envision that such funds could be turned over to one or another of the existing business development initiatives for which the Faroese Government is responsible.

The fee in accordance with § 14 in the Model License should equal the fee according to § 11, i.e. DKK 300,000.

1.4.16 Other standard license terms and conditions

§ 18 of the Model License stipulates that the government agency responsible for hydrocarbon activity has the right to participate in meetings of the Joint Operating Committee of the respective Licensees. §§ 19 and 20 sets forth the obligations the licensees have to offer assistance to the employees of the various governmental oversight authorities in their investigation efforts. These provisions further stipulate that the government may promulgate specific regulations governing the information that the licensees are required to provide to the various oversight authorities.

§§ 21 and 22 set forth matters related to confidentiality, how long confidentiality must be maintained, etc.

§ 24 stipulates that the licensees in a consortium are jointly and severally liable for the damages and compensation due to fishermen that shall be paid pursuant to Article 7 of the Hydrocarbon Activities Act and that all obligations towards the Faroese government pursuant to this license be fulfilled. § 25 requires that the licensees provide guarantees regarding said indemnification.

Pursuant to § 26, a license may not be transferred or assigned without the approval of the Minister.

1.4.17 Health, safety and the environment, etc.

The Hydrocarbon Activities Act stipulates that only well-qualified applicants will be granted exploration and exploitation licenses. It is the task of the governmental authorities to ensure that the applicants have the necessary industry knowledge, experience, competence and financial strength within the oil exploration and production business.

With regard to health, safety and the environment, the following prequalification criteria are decisive in determining whether an applicant can be adjudged as being sufficiently qualified to be granted a license:

- the applicant's guidelines vis-à-vis drilling operations
- the special challenges addressed by the applicant regarding drilling in deep water
- risk management tools in place, and
- the applicant's internal standards and requirements regarding competency development and the training of its employees

Moreover, the application for an exploration and exploitation license shall describe the requirements that the applicant itself sets with regard to health, safety and the environment, etc. These requirements should be designed to reflect the conditions found in Faroese waters, and the intended work programme outlined in the respective application.

When the license is granted, the regulations in the directives on health, safety and the environment during the exploration period, etc. enter into effect. The Hydrocarbon Activities Act stipulates that the “exploration and production shall be carried on in a safe and appropriate manner”. The licensees bear the responsibility that said activities are organised and undertaken in a safe and secure manner. The governmental authorities meanwhile shall ensure compliance with the respective regulations and directives.

The regulations and directives on health, safety and the environment enforce during the exploration phase stipulates the necessary requirements regarding how drilling operations shall be carried out. The licensees shall have an emergency response plan in place that shall be implemented in the event of accident or if hazardous conditions arise. In this regard, until now it has been required of the licensees to have a SAR helicopter on stand-by in the Faroes while drilling was taking place. After evaluating this requirement, the offshore installation and Jarðfeingi have concluded that, given a publicly-owned search and rescue helicopter is now available in the Faroes, it is reasonable to assume that the Faroese public emergency response system would also cover oil activities and that the licensees themselves do not need to ensure that a search and rescue helicopter is available in the Faroes.

In the event that the licensees, on the other hand, determine that the public emergency response system is not sufficient, the licensees, of course, can themselves arrange to augment the emergency response system and pay the associated costs. When the licensees apply for a license to engage in drilling operations, Jarðfeingi will determine if the emergency response system in place for all areas is sufficient and shall stipulate additional requirements should that prove necessary. The emergency response plan shall also cover the actions and equipment necessary to address intermittent pollution of the ocean environment. Suitable oil spill recovery equipment is required to be available on site, in the Faroes, or obtained internationally within an acceptable time frame.

1.4.18 Consequences for the fishing industry, the environment, etc.

Pursuant to the second sentence in § 7, Clause 2, in the Hydrocarbon Activities Act, the explanatory notes to the Act shall include an assessment of the possible impact of the hydrocarbon activities on navigation, fishing and other commercial activities, and on nature, environment and any other effects on the community, as well as an assessment of the contributions of the activities to stimulating the economy and employment opportunities.

Jarðfeingi has discussed the licensing round with representatives from the Faroe Marine Research Institute (Havstovan) and the Environment Agency (Umhværvisstovan).

Havstovan was of the view that the inclusion of the Munkagrinnur Ridge and the Faroe Bank would hardly harm fish spawning and the fish stock at large. Neither of these regions are included in the fourth licensing round, so the issue will be dealt with separately in connection with the fifth and sixth licensing rounds where these areas may become relevant.

Jarðfeingi is of the view that the general knowledge is satisfactory in relation to the area on offer.

Jarðfeingi has in addition discussed the terms and general conditions for hydrocarbon exploration in the Faroes with representatives from oil companies, the Faroe Oil Industries Association, and with other knowledgeable persons within this field. Jarðfrøðisavnið concludes from this interaction that

the existing regime is satisfactory in general, and that steadiness of the terms is preferable rather than temporary improvements with a view to encouraging oil companies to explore in the Faroese region.

Below is an assessment on potential impact from the fourth licensing round activities on fishery, navigation, nature and environment in addition to other industries, economy, etc. The assessment is based on the expected level of activity during the exploration phase.

1.4.19 Consequences for navigation

Exploration activities on the Faroese continental shelf can impact navigation for, inter alia, the fishing fleet in two ways:

- Offshore installations are moored in specific offshore areas and as a consequence, they may interfere with the ease of navigation in Faroese waters. Pursuant to the Hydrocarbon Activities Act, safety zones shall be established around offshore installations. The width of the safety zone is 500 m around the offshore installation.
- Exploration activities on the continental shelf include ship traffic in Faroese waters with regard to both transport and seismic acquisition, and thus can impact other navigation and the conditions under which the fishing fleet must operate.

Exactly how the offshore installations might impede navigation and to what extent ship traffic may increase is dependent on how extensive the exploration activities are and how many offshore installations will be present over time.

Ships engaged in the acquisition of seismic data need to hold their designated course and speed within the designated area to ensure proper collection of data. Therefore, this activity should be arranged in such a way as to ensure that the seismic vessels do not have to alter course because of fishing vessels. Thus, it is necessary to coordinate with the Faroese Maritime Rescue and Coordination Centre (MRCC) to provide notice of these activities. Moreover, it is imperative that Faroese communication liaisons are onboard to facilitate expedient and appropriate communications with other vessels in the area.

The conclusion is that the exploration activities and the associated navigation will not pose any appreciable hazard to other navigation.

1.4.20 Consequences for Faroese fisheries

Whether considering one or many wells, an offshore installation, as noted above, must maintain a 500-meter safety zone in all directions. Fishing is not permitted within this area. If an offshore installation is maintained in place with anchors, the anchoring area will be wider than the safety zone.

As a rule of thumb, the distance from the offshore installation to the anchor equates to 2-3 times the water depth. When estimating the consequences this has for fishery, it is necessary to distinguish between the various types of fisheries and the equipment used. The consequences are varied and depend on the type of equipment: bottom trawl, pelagic trawl, seine nets, lines or small nets, and whether the fishing effort seeks bottom fish or pelagic.

As a general rule, seismic shooting is not permitted from 1 November to 15 April. For certain areas, the restriction against seismic activity is extended to 31 May and 31 July, respectively. Since 1998, the Faroese Sea Fisheries Inspectorate has operated a notice regime that provides information about seismic activity on the continental shelf.

Even though exploration to the east and south of the Faroes can impact the potential of fully exploiting the fish stocks present in these areas, the conclusion of Jarðfeingi is that exploration in the licensing area will not seriously disturb the fisheries. This decision is based first and foremost on the fact that the licensing area by and large lies in waters deeper than most fishing effort for benthic fish occurs.

Exploration well operations normally last only 70 – 100 days. Thus, there is really very little competition for the ocean during the overall exploration phase, which in most instances stretches over six years or more. Therefore, the catch potential of the fishing fleet will be reduced but little.

Pursuant to the licenses intended to be awarded as part of the fourth licensing round, the initial activities, in the main, will be seismic acquisition. During the period that this seismic activity takes place, fishery activities could be impeded, if they take place in the same area. The vessels engaged in seismic acquisition need to hold their prescribed course and speed in the area being studied to ensure satisfactory results. Therefore, this activity needs be arranged in a way as to ensure that the seismic vessels do not have to alter course because of fishing vessels. It is consequently necessary to coordinate with the MRCC to provide adequate notice of these activities, and a Faroese communication liaisons needs to be onboard to facilitate expedient and appropriate communications with other ships in the area. For an exploration license that is in effect for three or more years, seismic studies generally last from 1 – 3 months. Thus, it is believed that seismic activity does not pose any severe threat to the fisheries.

In addition, it is recommended that a requirement be stipulated in the license for exploration and exploitation of hydrocarbons that the activities of the licensees and the fisheries in the area be organized in such a manner as to ensure that neither party is unnecessarily disturbed.

1.4.21 Impact on other industries – competition within the labour market

Given that activities in the exploration phase are generally minimal and limited to specific periods, experience to date indicates that activities on the offshore installation and the supply bases have very limited impact on the demand for Faroese labour. Generally, the operator leases the offshore installation with crew and equipment. On any given supply base, there is only a few person-years of work available. This is also the case when there are several offshore installations operating in succession.

Based on the anticipated exploration activities and the expected demand for labour, there is little basis upon which to believe that the exploration activities connected with the fourth licensing round in the first years will impact other industries to any notable degree. In the discussions that have taken place with the oil companies regarding exploration and the legislation as a whole, some have pointed out that the requirement that equipment shall first be transhipped to the Faroes, off-loaded here and subsequently transported to the offshore installation, makes exploration more costly.

1.4.22 Consequences for the natural environment

Hydrocarbon activities on the whole are believed to be a polluting enterprise in which pollution, first and foremost, stems from discharge from the offshore installation into the sea and the atmosphere. Pollution can also stem from accidents.

The extent of the impact on the environment is dependent on the safety protocols in place, the emergency response structure, the comprehensiveness of the actions taken to protect the environment, the attitude toward the environment manifested by the licensees and contractors, etc. On the whole, the oil industry has adopted a new perspective in recent years with regard to carefully organising its activities to protect the environment. However, it is still very important to maintain oversight of the activities undertaken by the oil companies to ensure that they are carried out with the appropriate care and concern for the environment. It is important to continue to require that only companies/consortia that can demonstrate an environmental protection programme that meets the requirements of such internationally recognised standards as ISO 14001 or EMAS can be granted a license for exploration purposes in the Faroes in which drilling is a part of the work programme.

During exploration drilling, these discharges especially are anticipated to occur:

- drill bits and mud
- concrete residue
- waste water and sewage
- overflow from the drilling deck
- cooling water
- fumes and vapours
- accidental leakage

Unless the proper prevention measures are in place to prevent such discharges, there is a risk that the environment could be polluted with untoward ecological consequences for the animal life in the area. Most substances that are discharged cause little or no damage in and of themselves, while others could have a negative impact on the environment. Discharge permits specifically stipulate that toxic substances and compounds that bioaccumulate, as well as persistent synthetic substances, may not be discharged. The discharge into the atmosphere increases the overall Faroese discharge of greenhouse gasses, especially carbon dioxide and nitrous oxides.

The Hydrocarbon Activities Act expressly states that “licenses may only be granted to applicants that are deemed to have the requisite expertise, experience, resources and financial strength”. Therefore, when applications for licenses are reviewed, careful attention must be paid to determine whether an applicant’s competence regarding environmental issues is satisfactory. Prior to undertaking drilling operations, other more specific requirements regarding the environment are stipulated. The regime stipulated in the Hydrocarbon Activities Act requires that a licensee shall obtain a special permit or approval for each and every activity it wishes to undertake. For example, the licensees may not drill an exploration well without prior approval for this activity. In addition, it is required that the licensees submit an assessment of the impact that drilling can have on the environment – a so-called environmental impact assessment. Each of the terms and conditions regarding the environment required of the licensee in connection with its exploration well operations are dependent, inter alia, on the conclusions stated in this environmental impact assessment.

The drilling agent that the licensees intend to use must be approved. The regulations on this are stipulated in Directive No. 37, dated 8 March 2001, on the use and removal of substances and materials from an offshore offshore installation.

Pursuant to this directive, a so-called discharge permit from the Environmental Directorate is required for the use and removal of all materials that are used in connection with drilling operations. This permit stipulates as well the conditions for the treatment of waste, notice requirements, etc. In the application for such a permit, the licensee must delineate all the information necessary to assess the impact of the discharge on the environment. In addition to this information, the licensee shall provide detailed information on the environmentally related characteristics of each of the substances that the licensee intends to use. Furthermore, the licensees are required to investigate the ocean floor environment at and around the drilling site. The conditions stipulated in said permit and the requirement for an environmental assessment are based on OSPAR1 Convention regulations and principles.

One direct consequence of exploration is that the animal life in the area around the exploration operations is disturbed to a certain extent, especially small creatures on the bottom and in the ocean, fish, seabirds and marine mammals in general that are attracted to the offshore installation. Fish, seabirds and marine mammals to a certain extent can move away from the area and, when the exploration activities are concluded, can freely move back into the area. This is not the case for animals inhabiting the ocean floor, which for the most part are bound to a certain area.

Seabirds are especially vulnerable to oil slicks that are created from oil spillage and leaks. The previous drilling efforts experienced hardly any problems, aside from 50 litres of diesel oil leaking into the sea during a bunkering incident in 2001.

Our legislation requires an assessment of the potential impact of a drilling operation or a development project. The oil companies shall conduct a survey of the area in order to suitably describe the area so that once drilling operations are concluded it is possible to confirm whether or not the drilling activities impacted the area and to what extent.

For the fourth licensing round, it is recommended that the terms and conditions from the third licensing round be maintained that requires the licensees to pay a sum certain to finance surveys to describe the natural environment of Faroese territorial waters. In this manner, we can build upon those previous studies that were conducted specifically to gain a better understanding of the ocean environment before oilrelated activities got underway. Specifically, these studies include the GEM survey carried out in connection with the 1st licensing round. Therefore, it is recommended that, as part of the licensing fee, the area lease fee be restructured as an “area and environment fee”, wherein a part of this amount shall be allocated for the environmental assessment study referenced above (250 DKK per square kilometre per year). The area lease fee shall otherwise be transferred to the national treasury, while it is recommended that Jarðfeingi shall administer the environmental fee and arrange, in collaboration with other governmental authorities, research institutes and the oil industry, which studies should be undertaken. Moreover, it is recommended that the guiding principles and structure of the previously mentioned Strategic Environmental Assessment be followed as much as possible.

1.4.23 Consequences for other societal interests

To date, we have experienced some exploratory operations and we can confirm that the impact on

the Faroese community as a whole has been limited. The impact on our society of a discovery of a commercially significant quantity of hydrocarbons is, on the other hand, difficult to predict. People have different opinions on how best to prepare our community for such a turn of events. Some would argue that it is difficult to prepare a society because the consequences could be quite varied, depending on how large the find or finds might be. This is very true. On the other hand, one could well ask whether it might not be reasonable to have a wideranging discussion to form a consensus on what issues need to be addressed relatively quickly and which ones could be postponed.

1.4.24 Assessment on what contribution hydrocarbon activities could offer the Faroese economy and business community

The contribution that hydrocarbon activities undertaken pursuant to this licensing round can make to the Faroese economy and the local business community is dependent upon the exploration commitments to which the oil companies agree.

Experience has shown that, if only seismic and other geological activities are carried out, the effect on the Faroese economy and local business community will be but little. Not until commercial quantities of hydrocarbons are confirmed, followed by development of the field(s) and subsequent production, can one expect any appreciable impact on the Faroese business community and the economy. The economic impact is dependent upon how the Faroese themselves wish this development to occur and the level of activity that is desired to actually occur within the Faroes. The Hydrocarbon Activities Act stipulates that before any field development takes place, said development must be approved by the relevant governmental authorities. Through such an approval process, the Faroese people can themselves ultimately control how development shall take place.

1.4.25 Implementation of the 3rd licensing round

This section briefly discusses the implementation of the licensing round subsequent to the adoption by the Parliament of the fourth licensing round legislation.

Subsequent to the adoption of the licensing law by the Parliament, the fourth licensing round shall commence upon public notice in relevant Faroese and international media. The Minister intends that this will take place at a conference in the Nordic House in May 2017. The application deadline will be nine months after the date of public notice.

The invitation shall describe the main criteria that the applicants must comply with in order to be granted an exploration license, as well as the requirements for any substantiation documentation, etc. In addition, the invitation shall describe the area to be licensed and the standard terms and conditions of the Model License.

An individual company as well as a consortium of companies may apply for a license.

1.4.26 Prerequisites for the granting of a license

Pursuant to § 6 of the Hydrocarbon Activities Act, a license for exploration and exploitation of hydrocarbons may only be granted to an applicant that is deemed to have the necessary expertise, experience, competence and financial strength to undertake such activities.

The designated operator shall comply with the technical specifications, while the consortium shall jointly and severally be held accountable for the financial requirements. The Model License stipulates that the licensees, joint and severally, are responsible for the payment of any damages assessed, etc.

One other prerequisite that is much emphasized in connection with the granting of a license is the competency of the applicants with regard to safety, health, work environment, and environmental issues, as well as emergency preparedness and disaster response protocols. See §§ 7 and 8.4 above.

The Minister shall moreover consider the extent to which the government is able to gain insight into and benefit from the activities related to the license.

1.4.27 Evaluation criteria when assessing the final licensees

When selecting the final licensees from among the applicants that meet the general prerequisites to be granted a license, considerable emphasis is placed first and foremost on an applicant's proposed work programme, including the documentation provided that demonstrates the applicant's competence and determination to undertake reasonable hydrocarbon exploration activities in the licensed area.

1.4.28 Administration, etc.

The work of Jarðfeingi is anticipated to increase somewhat as a result of new licenses being awarded pursuant to this licensing round. However, it is believed that the tasks and duties of Jarðfeingi will not increase very much immediately after the granting of the licenses. The current number of staff is believed to be sufficient to take on these new duties.

It is difficult to estimate the income that could be derived from the proposed licensing law. The income directly linked to the licensing round stems from the application fee. In addition, the area and environmental fee will provide some income. In connection with the processing of the application, an application fee of 50,000 DKK is levied for each application. This is the same amount stipulated in the second and third licensing rounds. This fee shall finance the costs incurred by the Faroese authorities to prepare the licensing round and to process the applications.

The proposed legislation on the fourth licensing round for the exploration and exploitation of hydrocarbons will also have an impact on the activities of other governmental authorities and institutions, e.g. those involved with the administration of the ocean environment laws, the law on hydrocarbon taxation, etc.

1.4.29 Recommendations and recommendation sheets

Aloang with a proposal to amend the Parliamentary Act on Hydrocarbon Activities, the draft bill was submitted for hearing to the Ministry of Finance, the Ministry of Fisheries, the Faroese Oil Industry Group (FOIB), and the Faroe Oil Industries Association. Replies were received from to the Ministry of Finance, FOIB, and the Faroe Oil Industries Association. They can be summarized as follows:

The reply from the Ministry of Finance was very brief and positive (see Annex 1). The Ministry considers the draft well prepared and just adds a comment on a misplaced footnote regarding an international treaty – which is now corrected.

The reply from FOIB was likewise positive as to procedure and content although the Group proposed several general as well as more specific amendments (see Annex 2). FOIB aired a general view that despite the importance of stable procedures, this should not prevent rational amendments aimed at facilitating flexibility of the license terms.

The Ministry of Foreign Affairs and Trade considers such flexibility to already be taken care of in the draft bill.

More specifically, FOIB suggests abolishing royalty, reducing the oil companies' corporate tax from 27% to 18%, in line with other limited companies.

To this end, the Ministry of Foreign Affairs and Trade considers the overall terms and conditions for the oil industry's activities in the Faroese region to be competitive with neighboring countries and it does not find reasons for amendments at this stage.

FOIB finally points to the view of the industry that the obligation to transport equipment and passengers to and fro Faroese territory via Faroese quay or Faroese airport generates extra costs.

The Ministry of Foreign Affairs and Trade recommends to not make any amendments in this respect.

The Faroe Oil Industries Association supports the draft bill on the fourth licensing round although making some comments on specific matters (see Annex 3) regarding increase of particular fees, the administration of competence-building fees, and Faroese participation in the exploration activities.

The Ministry of Foreign Affairs and Trade recommends to accommodate these suggestions.

The Association also highlights the obligation to transport equipment and passengers to and fro Faroese territory via Faroese quay or Faroese airport.

In this respect, the Ministry of Foreign Affairs and Trade points out that this obligation is engrained in the Act on Hydrocarbon Activities, § 11.

The Association points out that the industry should participate in the organization of onshore activities during the exploration phase.

The Ministry of Foreign Affairs and Trade supports this view.

It is also suggested that representatives from Jarðfeingi should be present onboard the offshore installations.

In this respect, the Ministry of Foreign Affairs and Trade points out that, according to the current promulgation, the authorities have the prerogative of visiting offshore installations, as needed.

The Association is of the view that supply places and subcontractors should be mentioned in Annex B to the bill with a view to provide them with a share of the fees that Jarðfeingi achieves for the purpose of obtaining equipment for services.

Finally, the Association points out that the obligation to transport equipment and passengers to and fro Faroese territory via Faroese quay or Faroese airport not always generates extra costs for the hydrocarbon exploration activities; rather contrary in some cases.

The replies are attached as Annexes to the draft bill – as follows:

Annex 1: Consultation Document from the ministry of Finance;

Annex 2: Consultation Document from FOIB (Faroese Oil Industry Group);

Annex 3: Consultation Document from the Faroe Oil Industries Association.

Chapter 2. Overall consequences of the proposed legislation

2.1 Financial Impact for the country and its municipalities

A. For the country

Initially, the only oil-related activities being considered are feasibility studies and possibly some exploration efforts. These will have but little financial consequence for the country. However, some revenue could be derived from the area lease fees, and, if drilling takes place, some additional revenue could be derived.

If hydrocarbons are discovered, considerable revenue could be expected to flow into the national treasury as a result of the Hydrocarbon Tax Act.

See also section 1.4.21 and 1.4.24.

B. For the municipalities

During the exploration phase, there will be little if any financial consequences for the municipalities. If hydrocarbon production is undertaken and such operations are conducted from the Faroes as the Hydrocarbon Activities Act so stipulates, those individual municipalities involved with such operations will derive some revenue.

See also section 1.4.21 and 1.4.24.

2.2 Administrative consequences for the country and the municipalities

The exploration phase is not expected to create any substantial administrative consequences for the country, and none for the municipalities. In the event of hydrocarbon production, Jarðfeingi and the Hydrocarbon Tax Department will need to be upgraded, among others.

2.3 Consequences for the business community

During the exploration phase, it is possible that certain companies will derive some income, but for most companies there will be but little revenue to be derived from activities during this period. If production is undertaken, it can be expected that there will be much activity onshore.

The draft bill does not suggest any administrative changes for the industry.

See also section 1.4.21 and 1.4.24.

2.4 Environmental Impact

The exploration phase is not expected to have any special consequences for the environment, however, this is dependent on the size of the operations undertaken. If there is development of one or several fields, it will be necessary to undertake this development cautiously and with due respect for the natural environment.

If hydrocarbon production is undertaken, one can expect increased discharge of greenhouse gases.

See also section 1.4.22.

2.5 Consequences for certain areas of the country

In the event that field development and production takes place, one can expect there to be repercussions for the business community in the Faroes, but it is difficult to assess which parts of the country will be most affected. One could anticipate that second-tier consequences will more than likely impact the entire country.

2.6 Consequences for certain social groups or associations

The bill does not have consequences for certain social groups or associations.

2.7 Consequences with regard to international conventions and directives

There are no consequences vis-à-vis existing agreements or directives. However, if the Faroes accedes to reduce its discharge of greenhouse gases, the challenge of reducing such discharge will be greater if there is hydrocarbon production.

The so-called Hoyvíkssáttmáli on the abolishment of all obstacles to economic relations between Iceland and the Faroe Islands stipulates, however, non-discrimination toward Icelandic concerns established in the Faroe Islands, or against Icelandic citizens in the Faroes.

2.8 International conventions and directives

There are no consequences vis-à-vis existing agreements or directives. However, if the Faroes accedes to reduce its discharge of greenhouse gases, the challenge of reducing such discharge will be greater if there is hydrocarbon production.

2.9 Border impediments

No known border impediments exist.

2.10 Taxes and duties

As a part of the general terms and conditions, the bill stipulates that companies initiating hydrocarbon production are due to pay royalty – see section 1.4.10

2.11 Fees

According to the bill, companies applying for a license are to pay an application fee, and those who obtain a license are to pay are subject to area rentals.

2.12 Does the draft bill impose any personal duties?

The draft bill does not in itself impose any duties on personnel or companies.

In the event licenses for exploration and exploitation of hydrocarbons are issued, obligations will follow as part of the license conditions, including obligation to perform the agreed work programme and duty to submit to the relevant authorities information on the activities pursuant to the license.

2.13. Does the draft bill give the necessary powers to the Minister of Foreign affairs and Trade, another Minister or the local district authority?

The draft bill appoints, which areas are licenses out for exploration and production of hydrocarbons in the fourth licensing round, and which terms shall be valid for the given licenses. The minister does in agreement with the draft bill have the authority to grant the licenses after the Faroese parliament in a special bill has marked the areas open for licensing, and the public terms for the licenses.

2.14 Does the bill give public authorities access to private properties?

An exploration license, see above, authorizes the Ministry of Foreign Affairs and Trade / Jarðfeingi insight into results, etc., from the exploration activities, and to enter offshore installations, as needed.

2.15 Are there any additional consequences attached to the bill?

The draft bill does not cause additional consequences other than what is mentioned above.

2.16 Outline of the consequences of the proposed legislation

	For country or authority	For local district authorities	For certain areas of the country	For certain social groups or associations	For business community
Financial or economic consequences	Yes	No	No	No	No
Administrative consequences	Yes	No	No	No	No
Environmental consequences	Yes	No	No	No	No
Consequences with regard to international conventions and directives	Yes	No	No	No	No
Social consequences			No	No	

Chapter 3. Comments to specific sections of the law

To § 1

Pursuant to § 7, Clause 2 in the Hydrocarbon Activities Act, the Parliament shall decide which areas shall be offered for hydrocarbon exploration and exploitation and which standard terms and conditions shall be required in this regard.

Following the passage of the licensing law, the Minister shall take the necessary steps to implement the licensing round and grant licenses to those applicants who are deemed to have met the prerequisites to be granted a license and who have committed themselves to the best work programme for their respective blocks.

To § 2

Pursuant to § 7, Clause 2 of the Hydrocarbon Activities Act, the proposed legislation stipulates the area to offered for the fourth licensing round.

Reference is made to the map attached herein as Annex A and made a part of this report by reference herein, and the General Comments above.

To § 3

Pursuant to § 7, Clause 2 of the Hydrocarbon Activities Act, the proposed legislation stipulates the standard terms and conditions for the licenses granted under the fourth licensing round. The standard terms and conditions are set forth in the Model License, which is attached as Annex B and is made a part of this report by reference herein.

The licenses be issued in accordance with the Act on Hydrocarbon Activities, which regulates the issuance of licenses as well as all the phases of the hydrocarbon activities, i.e. preliminary surveys, exploration and appraisal, development and production, as well as decommissioning.

The standard terms and conditions are the same for all licenses and are not subject to negotiation prior to the granting of a license during the licensing round. If, during the licensing round, it becomes apparent that certain minor adjustments should to be made to the standard terms and conditions, the Minister is authorised to so amend the standard terms and conditions as required.

In addition to the standard terms and conditions, exploration and production licenses shall incorporate specific terms and conditions relative to the individual licenses. Unlike the standard terms and conditions, the individual terms and conditions cannot be stipulated before the applications have been submitted and negotiations have occurred with the individual applicants. Specific terms and conditions to be negotiated under the fourth, fifth and sixth licensing rounds pertain to the areas covered and the proposed work programme for the individual licenses.

Some of the provisions of the Model License authorise the Minister to promulgate specific regulations and directives under various circumstances. For example, § 12 of the Model License stipulates that the Minister may establish the procedures as to how the licensees shall report on their activities, which work is to be subcontracted, etc. The Minister shall ensure that said procedures comply with existing legislation governing commercial undertakings, trade agreements, etc.

To § 4

It is stipulated that the act enters into force on the following day after its promulgation.

Minister of foreign Affairs and Trade

Poul Michelsen

Minister

/ Herálvur Joensen