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L A W F I R M

Developing Israel's Offshore Natural Gas Discoveries – Lessons from the Start-Up Nation

The Yam Tethys offshore gas field was first discovered in 1999 and was the spark which ignited Israel's newly founded natural gas industry. This initial discovery provided a limited amount of natural gas to the Israeli market and primarily to the Israeli Electric Company, its main customer. Today, this field is virtually depleted but, fortunately, other sizable discoveries like the Tamar and Leviathan fields have been made offshore Israel. The Tamar field is operational and is currently selling gas to the domestic market in Israel since April 2013. The Leviathan field is expected to be operational by 2017; however, due to the tremendous amounts of capital required to finance this project, its development is dependent on many external and regulatory factors such as export quotas and markets which will determine the financial model for this project and consequently, its timeline.

The developmental costs associated with these types of offshore projects are enormous and it is critical that the State of Israel fosters and nurtures an investor friendly environment in order to attract the massive amounts of foreign capital that is required for this endeavor. To date, most of the financing raised for these offshore projects (Yam Tethy, Tamar and Leviathan) has been obtained from foreign banks and institutional investors although the Israeli public has also funded considerable portions of these projects. Most recently, Delek Drilling and Avner Oil completed a successful \$2 billion bond offering but much more funds are still needed if we are to develop this industry and become a global player .

In the arena of high-tech, Israel is known globally as the "Start-Up Nation" and its model for success has been and continues to be copied by other nations around the globe. While there have been some extremely successful public sector initiatives in the high tech industry such as the Office of the Chief Scientist of the Israeli Ministry of Finance and Trade, for the most part, the Israeli high tech industry flourishes with minimal governmental intervention and is supported by a robust Israeli and foreign venture capital industry. To allow its energy industry to blossom, the government of Israel will need to take a similar view in the parallel world of natural gas, despite the inherent and natural tendency of the State to be extremely cautious in protecting these important national assets. For example, the recently instituted tax and royalties' collection regimes and export quotas' system should remain static, if investors are to feel confident that this market is stable and will not be subject to change. Since petroleum assets typically serve as the main collateral in financing these projects, it is also critical that clear guidelines regulating their transfer be put in place, giving investors certainly that they will be able to realize their collateral, following an event of default. Lastly, many of the financing transactions could be simplified if the Israeli tax authorities find a way to exempt the borrower from its obligation to withhold tax at source when making an interest payment.

Currently, this obligation exists when making an interest payment to a foreign lender, where a payment to an Israeli lender would usually be exempt .

To summarize, these are just a few examples of where the State of Israel needs to focus and channel its energy on being investor friendly and in opening the floodgates of our natural gas industry to the world at large. Israel is already on the international map with respect to its high tech abilities and entrepreneurship and there is no reason that Israel cannot be a world leader in energy exploration as well. For this to occur we will need to create the correct environment and hopefully the State of Israel will take lessons from the "Start-up Nation".

The writer, Simon Weintraub, is a partner in the international department at Yigal Arnon & Co. Simon has been involved in most of the financing transactions relating to the development of the Tamar and Leviathan gas fields to date. Most recently, he represented the Joint Book-Running Managers JP Morgan, CitiGroup and HSBC as the lead underwriters of a private placement to Israeli and foreign institutional investors of senior secured notes in the aggregate amount of \$2 billion and also acted for Barclays Bank Plc, as arranger, Bank Mizrahi Tefahot, as facility agent and a number of Israeli institutional lenders in a \$225 million credit facility and re-financing transaction with Dor Gas Explorations Partnership, a partner in the Tamar field.

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