



Cuba Natural Gas

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Past performance for investors in the Cuban energy space might suggest otherwise. Serious efforts by foreign energy companies over the past 20+ years to build refineries, upgrade oil import terminals and install new pipelines have generally floundered, and millions of dollars have reportedly been spent by oil giants, such as Repsol and Petronas, on investments that failed to yield meaningful results.¹ Moreover, notwithstanding the apparent turning point in U.S.-Cuba relations, the Cuban government appears generally committed to ensuring, for now, that energy project development remains under significant control of the Cuban government.

But the energy industry is accustomed to operating in difficult markets. And given the current general problem of weak global energy product demand, including in the LNG markets, at a time of an abundance of global energy product supply, particularly natural gas, opening a new market that has the potential to soak up some of this excess supply, now or in the not-too-distant future, might not be such an extreme risk for an industry accustomed to taking calculated risks.

Sources of New LNG Demand

It is no secret that low oil prices are affecting the global LNG market. For example, spot LNG prices in Asia have fallen from more than \$20 per mmbtu in 2014 to less than \$5 per mmbtu today.² At such low prices, after taking into consideration shipping and gas liquefaction costs, it may be difficult for LNG sourced from the United States to be competitive outside of the Americas. It is also no secret that some energy companies with firm commitments to purchase LNG in the United States are exploring options to sell down some of their excess

LNG supply.³ While likely off the radar of many, Cuba might be one strategic option to consider to mitigate some of this exposure.

For example, if an import terminal (perhaps an onshore LNG import terminal or offshore floating LNG storage and regasification unit or, given the size of the Cuban economy today, a CNG (compressed natural gas) terminal) were to exist on the island or offshore Cuba today, on pure availability of supply analysis, such terminal could easily be supplied with gas from the United States, and it is hard to imagine the project participants being unable to obtain gas supply at very attractive pricing. Indeed, one area of optimism in an otherwise stagnant global LNG market is the growth potential for natural gas in the Caribbean basin.

AES Corporation, which developed an LNG import terminal in the Dominican Republic in 2003 (AES Andres), billed as the first LNG import facility in an emerging market, has indicated its desire to use such facility as an LNG transshipment and bunkering hub for the Caribbean and Central and South America.⁴ In addition to AES Andres, LNG terminals exist on Mexico's Gulf Coast, as well as in Puerto Rico and Trinidad. Further, in addition to two LNG import projects under consideration in Panama, one of which would be developed by AES, LNG projects have been proposed, or are under consideration, in the Bahamas, Guadeloupe, Honduras, Jamaica, Martinique and along Colombia's Caribbean coast. Even if some of these projects never make it to FID (final investment decision), it is likely that a Caribbean LNG market will develop. And developing an LNG import infrastructure in Cuba, the Caribbean's largest and most populous island, would be a logical next step in this process as the region makes the inevitable switch from diesel to cheaper and cleaner natural gas. Such developments could be viewed as a "win-win" solution, allowing energy companies with excess LNG supplies access to new markets and these markets to access cleaner and cheaper fuels.

Cuba Energy Markets Today

From the time of the Cuban revolution until the collapse of the Soviet regime, the Cuban-sugar-for-Soviet-crude oil trade helped ensure that Cuba had a steady supply of hydrocarbons. In more recent times, Venezuela provided Cuba with a lifeline through its export program, PetroCaribe, in the Cuban-doctors-for-Venezuelan-crude oil trade, but, today, with Venezuela experiencing deep economic distress, Cuba is again in need of an energy lifeline. But more than just supply, the country needs substantial investment in energy infrastructure. Cuban power plants run on either untreated refined Venezuelan crude or the

country's domestic crude oil, a relatively low grade that results in its plants running at only a fraction of their potential.⁵

Indeed, almost all of Cuba's domestic oil production goes directly into running its own power plants, without first passing through a refinery, contributing to a significant amount of carbon emissions, given Cuba's relative size.⁶ Certainly, converting Cuba's power plants that run on oil to natural gas will be expensive, but, with greater efficiency, the cost of power generation should decline.⁷ Since natural gas has a significantly lower level of carbon emissions than crude oil, these plants would also be cleaner.⁸

America's Interest

The United States Geological Survey estimates that the Cuban portion of the Straits of Florida contains 5.5 billion barrels of undiscovered petroleum liquids and 9.8 trillion cubic feet of natural gas, with much of these resources in waters only 60 miles off the United States' coastline.⁹ The Cuban government's own estimates are purportedly larger. However, developing these deepwater resources involves inherent risks and substantial challenges. To the extent the development of such deepwater resources is not properly managed, the consequences of potential well incidents or other environmental crises for the United States and, in particular, the economy of Florida, could be substantial.¹⁰ Models plotting the trajectory of "virtual particles" from an oil exploration site 22 miles north of Havana have shown that, due to the strong current of the Gulf Stream, oil would reach the aquamarine waters and coral reefs off the South Florida coastline within five to six days of any leak or spill.¹¹ If a major spill were long-lasting or to the extent of continuous leakage, it could have a significant impact on Florida's economy. On average, 100 million tourists visit Florida each year, contributing more than \$80 billion per year to Florida's economy.¹² If Florida's waters were adversely impacted by offshore Cuban oil and gas exploration and production activities, these numbers would be negatively impacted.

Thus, to the extent that U.S.-Cuban relations continue on the path of more dialogue and regulatory change, the U.S. government should consider policy changes that promote greater engagement in the energy sector and that are supportive of effective energy development, with special emphasis on supporting the LNG/CNG trade on the island. Presently, the United States has a policy of general approval for export and re-exports to Cuba of items related to renewable energy or energy efficiency. Additionally, the U.S. government has adopted a case-

by-case review policy for exports and re-exports of certain items to meet the needs of the Cuban people, including facilities for supplying electricity and other energy to the Cuban people. This established platform of U.S. policy provides a basis to expand and build upon as a matter of common bilateral interests.

Existing U.S. Sanctions Against Cuba

Clearly, the U.S. embargo against Cuba remains a substantial impediment to energy projects involving Cuba at the present time. The sanctions generally prohibit U.S. persons – including U.S. companies and their foreign subsidiaries, as well as other non-U.S. entities that are owned or controlled by U.S. persons – from engaging in transactions with, or involving, Cuba or Cuban nationals (including entities), except where specific transactions are exempt from the regulations or otherwise licensed. Nonetheless, President Obama’s recent policy initiative to re-engage with Cuba, diplomatically and economically, creates significant opportunities for U.S. businesses to enter the Cuban market and potentially to expand economic engagement in the energy sector.

The Department of the Treasury’s Office of Foreign Asset Controls (OFAC) and the Department of Commerce’s Bureau of Industry and Security (BIS) have implemented the administration’s policy initiative through changes to the Cuban Assets Control Regulations (CACR), Part 515 of Title 31 of the Code of Federal Regulations, and the Export Administration Regulations (EAR), Parts 730 through 772 of Title 15 of the Code of Federal Regulations, respectively, which ease many of the embargo’s restrictions on doing business with Cuba. Specifically, OFAC has issued and expanded general licenses that authorize activities otherwise prohibited by the CACR. In addition, BIS has issued, and expanded, a number of license exceptions allowing persons to export or re-export items subject to the EAR to Cuba for certain authorized purposes. BIS has also established licensing policy changes that are largely focused on supporting the needs of, and empowering, the Cuban people and creating increased opportunities for U.S. companies to trade with Cuba. Among other changes, these reforms include the recent general authorization of disaster mitigation and relief services, including potential exports necessary for rapid response to offshore well events in the energy sector that pose a common threat to parallel U.S. and Cuban environmental and national interests.

Cuba Tomorrow

Whether the Cuban market today (or in the not-too-distant future) can help soak up some of the world's excess LNG remains to be seen, but recent political developments make clear that the time for first-movers to begin to advance projects on the island is likely now.

Akin Gump Today

Akin Gump Strauss Hauer & Feld LLP has had an involvement with Cuba for more than 15 years. Our Cuba practice consists of more than 30 lawyers and advisors, including international trade and sanctions advisors, lobbyists and industry leaders, with extensive experience developing compliance policies and procedures, voluntary disclosures, license applications, reports and other submissions to the U.S. Congress, the White House and relevant U.S. government agencies with respect to Cuba. We are the only law firm on the board of directors for the U.S. Chamber of Commerce's U.S.-Cuba Business Council, which has unparalleled access to key U.S. and Cuban government officials. Our experience assisting clients with issues involving Cuba, including market access, dates back to the earliest renewal of commercial relations with the country, and members of our team remain deeply engaged in the process of commercial diplomacy, on the ground in Havana and in Washington D.C., that is defining the renewal of U.S. relations with Cuba at this time.

¹ Jeff Franks, Drilling rig leaves Cuba, taking oil hopes with it, *Reuters* (Nov. 14, 2012), at <http://www.reuters.com/article/cuba-oil-rig-idUSL1E8MEHET20121114>.

² Platts: spot LNG prices to Asia lowest since 2009, *LNG World News* (April 25, 2016), at <http://www.lngworldnews.com/platts-spot-lng-prices-to-asia-lowest-since-2009>.

³ Toshiba Shedding Freeport LNG Capacity, *LNG World News* (November 6, 2015), at <http://www.lngworldnews.com/report-toshiba-shedding-freeport-lng-capacity>.

⁴ Statement of Andres Gluski, President and CEO of the AES Corporation, United States Cong. House Committee on Foreign Affairs Subcommittee on Western Hemisphere: "U.S. Dominican Republic Relations: Bolstering Economic Growth and Independence" (July 23, 2014), at <http://docs.house.gov/meetings/FA/FA07/20140723/102535/HHRG-113-FA07-Wstate-GluskiA-20140723.pdf>.

⁵ David Ferris and Nathaniel Gronewold, Energy Policy: The U.S. opportunity in Cuba, *EnergyWire* (April 10, 2015), at <http://www.eenews.net/stories/1060016531>.

⁶ Id.

⁷ Id.

⁸ Id.

⁹ Assessment of Undiscovered Oil and Gas Resources of the North Cuba Basin, Cuba, 2004, *US Geological Survey*, World Assessment of Oil and Gas Fact Sheet, at https://pubs.usgs.gov/fs/2005/3009/pdf/fs2005_3009.pdf.

¹⁰ Leo Oppenheimer, The Environmental Threat of Cuba's Deep Water Exploratory Drilling Under the Embargo, *Columbia Journal of Environmental Law* (2016), at <http://www.columbiaenvironmentallaw.org/assets/FR2014/Oppenheimer-MACRO-final-12-20-2014.pdf>.

¹¹ Robert H. Weisberg, Tracking a potential Cuba oil spill, *Tampa Bay Times* (February 4, 2012), at <http://www.tampabay.com/opinion/columns/tracking-a-potential-cuba-oil-spill/1213878>.

¹² <http://www.visitflorida.org/about-us/what-we-do/tourism-fast-facts/>.

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