

# Risks, Security of Investment and Dispute Resolution Under Upstream Petroleum Regimes

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## ABSTRACT

There is more worldwide commerce, and foreign investment, occurring today than ever before in history. There is undeniable evidence that the world is proceeding toward a more globalized economy.

As part of this commercial globalization process there have also been changes in dispute resolution where foreign investment is involved. There has been a move from the national court system of the host country to international arbitration. This change has given the foreign investor international petroleum company ("IOC") a greater degree of assurance that dispute resolution in connection with its foreign investment will be fair, impartial, and with effective enforcement.

The international energy industry has also changed accordingly. International arbitration is now also the norm for dispute resolution in the context of Host Government ("HG") Upstream Petroleum Regimes ("UPR"s), inclusive of Host Government Contracts ("HGCs") such as PSCs. HGCs vary greatly, however, in regard to the elements of the international arbitration provision, and to the extent fairness, impartiality and effective enforcement are promoted.

HGCs also vary greatly regarding: (i) the degree of contract stability offered to the IOC (in regard to both fiscal and non-fiscal contract elements); (ii) the standards applicable to HG approval of operations (objective or subjective); and (iii) recourse to third party experts in the event of disputes over approvals and technical/factual matters.

"Political risk": IOCs can buy various kinds of "political risk insurance", including policies insuring against war and insurrection. But perhaps the primary risk that this sort of policy insures against is the risk that the Host Government will breach the contract. Example: the well-publicized international arbitration between Turkmenistan and Bidas.

But that is just one risk for the IOC. What about contractual risks that do not involve a breach by the HG? Many UPRs are unclear on whether or not the IOC has the right to develop ("monetize") any discovery that it might make. Under some UPRs the HG may be able to prevent the IOC from "monetizing" a discovery without breaching the UPR. Consider the well-publicized disputes over offshore discoveries in the 1990s between Equatorial Guinea and various IOCs. In cases where the HG does breach the UPR, then enforcement of the IOC's rights may become a question of the efficacy of the HGC dispute resolution provision – as well as whether there are applicable enforcement treaties.

The following considerations are pertinent:

- HGC due diligence-it begins with the host country's constitution
- Stability of contract and the hierarchy of laws – which kinds of approaches to stability work best under the circumstances of a given UPR?
- Fiscal stability vs. non-fiscal contract stability
- HGC approval standards for annual work program and budget, appraisal plans, development plans and assignment – applicability of determination by either special expert or arbitration in the event of a dispute – or a moratorium over development pending HG/IOC agreement
- Litigation in the national court system of the host country vs. international arbitration
- Why the place of arbitration is among the most important elements of the arbitration provision
- When the law of the place of arbitration will override the arbitration provision

- Significance of arbitral rules such as UNCITRAL, ICC, LCIA and ICSID
- Significance of a waiver of sovereign immunity from execution
- HGCs that permit international arbitration for some issues, but at the same time require some of the most important issues to be determined by the national court system of the host country
- Stability provisions contained in HGCs between the IOC and the HG vs. stability provisions contained in HGCs between the IOC and an "instrumentality" of the HG. Contracts between the IOC and an NOC (example-Egypt).
- Legal significance of HGC being enacted as a law (Egypt, Syria).
- Enforceability of arbitral awards – applicability of multilateral treaties such as the New York Convention, ICSID and the Energy Charter Treaty, as well as bilateral investment treaties
- Why ICSID is the preferred choice of many IOCs for purposes of security of investment
- Inapplicability of ICSID to subdivisions, instrumentalities or subdivisions of HG (such as national oil companies) unless specific requirements of ICSID are met.
- How to avoid international arbitration in the first place – including regular communication meetings and ADR.