LEX PETROLEA IN INTERNATIONAL LAW

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1. Introduction

The term *Lex Petrolea* entered the lexicon of legal literature and the international oil & gas industry more than a quarter century ago.[1] The term first emerged in a landmark international arbitration case in 1982, where it was argued that the international petroleum industry in its disputes had "generated a customary rule valid for the oil industry - a *lex petrolea* that was in some sort a particular branch of a general universal *lex mercatoria".*[2] In a seminal article in 1998, the thesis was put forth that in the prior twenty-five years" an increasing number of international arbitral awards relating to the petroleum industry have been published… [which] created the beginnings of a real *lex petrolea* that is instructive for the international petroleum industry."[3] A more recent article on the subject updated" all arbitral awards published since 1998 that relate to the international oil and gas exploration and production industry", while furthering the argument that "… the published awards relating to the international exploration and production industry have created a *lex petrolea* or customary law comprising legal rules adapted to the industry's nature and specificities."[4] Those two articles primarily relied upon a number of published awards from state investment disputes, along with a couple of commercial arbitration awards, to draw their conclusions on the meaning of *Lex Petrolea*.

This article supports the thesis that a *Lex Petrolea* has developed over the years*,* but widens the scope of inquiry to the full range of disputes encountered in the international petroleum sector. *Lex Petrolea* primarily arises from international arbitration and court cases. However, it has also developed in a number of other forums, from governments' petroleum legislation & contracts to the industry's business practices, which are found in its model contracts.

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[1]However, one will still not find it in a legal dictionary. The closest sounding term to be found is *Lex Petronia*, which is an ancient Roman law forbidding masters from sending their slaves to fight wild beasts in the arena without a magistrate's authorization. *See* BLACK'S LAW DICTIONARY, 995 (Bryan A. Garner ed., 9th Edition, West 2009).

[2] Government of the State of Kuwait v. American Independent Oil Co. (AMINOIL), Award of 24 May 1982, 21 International Legal Materials (ILM) at 976 (1982). Yearbook IX at 71 (1984). Note that in an article entitled "L'Intervention de L'Etat en Matiere d'Hydrocarbures en France" or "The Intervention of the State in the Hydrocarbons Sector in France" published by Professor Claude-Albert Colliard in the Annals of the Faculty of Law and Economic Sciences of Aix-en-Provence (Novelle Serie No. 52, Annees 1960-1961), Professor Colliard used the term "petro-droit" or "petroleum law" indicating an emerging concept of *Lex Petrolea* in the international petroleum sector.

[3]R. Doak Bishop, *International Arbitration of Petroleum Disputes: The Development of a Lex Petrolea*, XXIII Y.B. COM. ARB. 1131 (1998).

[4]Thomas C. Childs, *Update on Lex Petrolea: The Continuing Development of Customary Law Relating to International Oil and Gas Exploration and Production*, 4:3 J WORLD ENERGY LAW & BUSINESS, (September 2011)at 214.

Unlike courts, the world of international arbitration is not bound by precedent,[5] i.e., decisions of arbitration tribunals are not binding on other tribunals. However, arbitrators make their decisions in context and not in a vacuum. Counsel use precedent in arguing their cases and arbitrators refer to precedent in writing their awards. The practical result is that precedent is relied upon in international arbitration and a *Lex Petrolea* has developed accordingly.

The worlds of commerce and investment seek out consistency and predictability in making their decisions. So clarifying what *Lex Petrolea* means and how it is applied is helpful both to the world of international arbitration and to the world of international oil and gas, which generates the largest percentage of disputes both in the investment state world[6] and in international commercial disputes.[7] Arbitrators attempt to rely upon credible sources in determining their arbitral awards. This article helps to explain where they can find such sources in deciding international oil & gas arbitration cases.

Lex Petrolea is most often established from the decisions arising from disputes within the international oil & gas sector. That is where the contracts, legislation and treaties that impact the petroleum sector are tested and interpreted. In order to determine the full extent of *Lex Petrolea*, one has to therefore look to the full range of disputes in the international oil & gas business.

2. Types Of Disputes In The International Oil And Gas Business

There are essentially four types or categories of disputes found in the international oil and gas sector.[8] They are:

2.1 State vs. State Disputes

These are primarily boundary disputes concerning oil and gas fields that cross international borders, most of which are located in maritime waters. They involve governments since only they are able to claim sovereign title and resolve boundaries with their neighboring states. However, oil and gas companies sometimes get indirectly involved in these disputes when they are granted concessions that straddle disputed boundary lines.

2.2 Company vs. State Disputes

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[5] REDFERN & HUNTER ON INTERNATIONAL ARBITRATION, Nigel Blackaby & Constantine Partasides (Oxford, 5th Edition, 2009) at paragraphs 1.113, 8.58, 9.195, and 9.212. Note that courts of first instance in some jurisdictions are not bound by decisions of higher/appellate courts.

[6] *See* ICSID data on state investment disputes *at*http://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=CaseLoadStatistics

[7] See ICC data on international commercial disputes *at*: http://www.iccwbo.org/court/arbitration/index.html?id=34704

[8] This categorization was first used by the author in a PRIMER ON INTERNATIONAL DISPUTE RESOLUTION written for the Independent Petroleum Association of America and the Association of International Petroleum Negotiators in 2011, which was subsequently published as: A. Timothy Martin, *Dispute Resolution in the International Energy Sector: an Overview*, 4:4 J WORLD ENERGY LAW & BUSINESS, pp. 332-368 (December 2011).

These are state investment disputes (sometimes called investor-state disputes). They occur when governments significantly change the terms of the original deal or nationalize (or as sometimes referred to, “expropriate”) an investment. The investor (in this case an oil and gas company or a consortium of oil and gas companies) can base its claim on its investment contract (either a production sharing contract or risk service agreement) or an investment treaty, or possibly both. Most treaty claims are now made under bilateral investment treaties (BITs) and some under a multilateral treaty such as the Energy Charter. These are the disputes on which the two *Lex Petrolea* articles primarily based their analysis.

2.3 Company vs. Company Disputes

These are international commercial disputes arising out of oil & gas contracts. There are two subcategories of disputes occurring between energy companies. The first subcategory is amongst holders of interests in oil & gas concessions such as joint venture participants or buyers & sellers of such interests or the production from such interests. They are found in such agreements as:

- Confidentiality Agreements
- Joint Operating Agreements
- Unitization Agreements
- Farmout Agreements
- Area of Mutual Interest Agreements
- Study and Bid Agreements
- Sale and Purchase Agreements

The second subcategory of disputes is between operators and service contractors for providing services or equipment in the following kinds of agreements:

- Drilling and Well Service Agreements
- Seismic Contracts
- Construction Contracts
- Equipment and Facilities Contracts
- Transportation and Processing Contracts

They make up the majority of disputes in which oil and gas companies find themselves. They are primarily resolved in arbitration rather than in courts in the international oil & gas business.

2.4 Individual vs. Company Disputes

There are a number of situations where individuals initiate claims against oil and gas companies. The first is when an individual suffers a personal injury and begins a tort claim against a company. This is common in U.S. jurisdictions but is increasingly happening in other countries. A second area of individual claims arises from human rights or environmental claims. They are sometimes filed in U.S. courts using the Alien

Tort Statute or other jurisdictions using a variety of innovative legal mechanisms[9]. The third group of claims by individuals arise when promoters of oil & gas deals claim they have an interest in a host government contract and the accompanying joint operating agreement as a result of a third party tortious action or by way of agreement. The final group of claims concerns agents or consultants who demand payment under their agent agreements for winning a government contract for a company. There are a series of arbitrations that have happened over the last 50 years where companies have refused to pay their agent based upon corruption allegations after securing the host government contract.[10]

3. Boundary Disputes

"Because of the many undelimited maritime boundaries across the globe, international oil and gas exploration and production companies will often encounter boundary-related uncertainty as they enter new exploration areas."[11]As a result, boundary disputes between sovereign states form part of the body of *Lex Petrolea* that impact the world of international oil & gas. Boundary disputes clearly fall within the area of international public law. But it "… is a somewhat esoteric activity and the number of true experts in the field is quite small."[12]That activity and that expertise often revolve around oil & gas operations.

There are both land and maritime boundary disputes in the world that involve control over natural resources, but the greatest number of them are located in the world's oceans and seas. The primary source of law for delimiting maritime boundaries is the United Nations Convention on the Law of the Sea (UNCLOS). Most of the world's states have ratified it and many of its provisions are now considered to be customary international law.

The primary forums for the binding resolution of international boundary disputes are the International Court of Justice (ICJ) in the Hague that was established under the Charter of the United Nations in 1945, the International Tribunal for the Law of the Sea (ITLOS) in Hamburg that was established under UNCLOS in 1996, and *ad hoc* arbitration tribunals. The ICJ has issued more than a dozen boundary awards and ITLOS presently has one boundary case pending. States involved in *ad hoc* arbitrations usually keep the results confidential. The awards from these cases interpret the customary international law around the delimitation of sovereign boundaries.

There is now sufficient jurisprudence in this area to provide some certainty around delimiting a boundary. But both states and tribunals have sometimes been creative in

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[9]*See* Jonathan Drimmer, *Human Rights and the Extractive Industries: Litigation and Compliance Trends*, 3:2 J WORLD ENERGY LAW & BUSINESS (July 2010) for more details on these claims worldwide.

[10]*See* A. Timothy Martin, *International Arbitration and Corruption: An Evolving Standard*, 20th Annual Institute for Transnational Arbitration (June, 2009). Available at: http://www.timmartin.ca/qualifications/publications

[11]Derek Smith and Martin Pratt, HOW TO DEAL WITH MARITIME BOUNDARY UNCERTAINTY IN OIL AND GAS EXPLORATION AND PRODUCTION AREAS, 25 (AIPN, 2007) available at: www.aipn.org

[12]*Id.* at 31.

establishing boundaries, so boundary delimitation can still be regarded as much an art as a science.[13]

There is an extensive body of boundaries literature. The most comprehensive study of international maritime boundaries and its law is the American Society of International Law's INTERNATIONAL MARITIME BOUNDARIES.[14] An excellent introduction to understanding how international boundaries are established and their impact on oil & gas companies is HOW TO DEAL WITH MARITIME BOUNDARY UNCERTAINTY IN OIL AND GAS EXPLORATION AND PRODUCTION AREAS, published by the Association of International Petroleum Negotiators (AIPN).[15]

4. State Investment Disputes

Most of the published arbitration awards that have established a *Lex Petrolea* arise out of state investment disputes. Given their public nature and the rules of institutions such as the International Centre for Settlement & Investment Disputes (ICSID), those awards are usually published and made available in the public domain. These are the cases that the two articles on *Lex Petrolea* by Doak Bishop and Tom Childs rely upon. What is striking about those cases is that not only have they established a *Lex Petrolea*, but on a larger scale they have established the customary international law for dealings between states and private investors. This is because the oil and gas business has historically been one of the largest and most active global industries. The industry invests in very large, complex, and capital-intensive projects with long life spans. People, companies, governments and circumstances invariably change in such projects and misunderstandings arise that often result in disputes. Hence the significant impact of *Lex Petrolea* on state investment disputes.

The impact of the early cases described in the first *Lex Petrolea* article has influenced the behavior of both investors and governments in the post 1998 cases described in the second article. Most of the post-1998 awards arose from BIT claims. There were none prior to 1998. Only one award since 1998 deals with the nationalization or expropriation of assets, whereas many of the pre-1998 awards are about this issue. Many of the post-1998 awards deal with claims relating to changes in the host State's fiscal regime; i.e., creeping expropriation. Whereas, none of the pre-1998 awards addressed such claims.[16]Some of the highlights and observations on *Lex Petrolea* that flow from these state investment disputes follow.

4.1 Expropriation

States have the right to expropriate investments. However in doing so, states must compensate the investor. It is only unlawful "if it is discriminatory, it is not motivated by the public interest of the expropriating country, it breaches stabilization clauses of the parties' contract, or if no compensation is paid, offered or other provision for it made. The modern effect of such illegality, however, is merely to permit an award of additional

[13] *Id.* at 15.
[14] INTERNATIONAL MARITIME BOUNDARIES Vols. I-V, Martinus Nijhoff.
[15] Available at: www.aipn.org
[16] Childs, *supra* note 4, at 215.

compensation."[17] The result under *Lex Petrolea* and customary international law is that once expropriation has been established, the only issue remaining is how to properly calculate the compensation to the investor.

4.2 Duress

The defense of duress is not effective in most creeping expropriation cases. "In the absence of a written record of reservations of rights, protests or a lack of consent, this claim is seldom given much credence."[18]Therefore the best legal course for an investor who is suffering creeping expropriation is to establish a clear written trail of protests that it can point to in its arbitration with the state. Unfortunately as a practical matter, this is often not a viable formula for working successfully on an ongoing basis with a government and its officials.

4.3 Force Majeure

Force majeure clauses in an investment contract can be effective. Tribunals have held that "*force majeure* is a general principle of law that may be applied even if the contract is silent on the point."[19] These clauses cannot however be taken for granted. Much will turn on the wording of the *force majeure* clause and the circumstances in which *force majeure* is invoked. Negotiators of host government contracts (HGCs) therefore need to pay a lot of attention to what is included (or not included) in a *force majeure* clause.

4.4 Transfer of Interest

Failure to obtain required government approvals on transfers of interest can result in termination of a host government contract. This risk can occur even when an oil company attempts to bifurcate the title and claim that no "legal" title was transferred and thus did not require prior government approval.[20] This may be an acceptable practice in some domestic jurisdictions, but not in many international operations.

> *Even though bifurcation of title is regularly used in farmout agreements in North America where it is legally recognized and valid, that is not always the case in international farmout agreements in other parts of the world. If the HGC or hydrocarbon law does not recognize the bifurcation of title and requires prior government approval of a title transfer in the HGC to a third party, there is significant risk in not obtaining prior written government approval to a farmout agreement and the bifurcation and transfer of title*.[21]

There are policy reasons around this risk. The control and development of natural resources is important to petroleum producing countries. One of the primary means such countries control how their natural resources are developed is by approving which international oil companies (IOCs) are allowed to acquire an interest in their host

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[17] Bishop, *supra* note 3, at 1156 & 1158.
[18] *Id.*at 1164.
[19] *Id.*at 1168.
[20] *Occidental Petroleum Corporation v. Republic of Ecuador*, ICSID Case No. ARB/06/11, Decision on Provisional Measures, Aug. 17, 2007, paragraphs 9-24, 62-97.
[21] A. Timothy Martin, *Bifurcation of Title in International Oil & Gas Agreements*, A LIBER AMICORUM: THOMAS WÄLDE, 182 (J Werner & A Ali eds., Cameron May, 2009).

government contracts. As a result, failure to obtain the prior authorization of the designated ministry to the transfer of any interest in the host government contract may result in its termination and a potential state investment dispute with significant downside for the investor.

4.5 Remedies – Specific Performance

Investors should not count on the remedy of specific performance in seeking to enforce their host government contracts. With one notable exception, international arbitration tribunals have consistently awarded damages rather than specific performance after determining that there has been an expropriation. That exception is the *TOPCO v. Libya* case.[22]The sole arbitrator in that case "found that *restitutio in integrum* is an appropriate remedy under the Libyan Civil Code and Muslim law, and cited the *Chorzow Factory* case as applying the rule of *restitutio in integrum*."[23] Unfortunately for TOPCO, Colonel Qaddafi and his regime ignored the arbitrator's award that granted it specific performance and never did allow the company back into the country to perform its contract.

International tribunals have continued to take this approach as shown in recent cases. In *Al-Bahloul v. Tajikistan*, the tribunal denied the claimant's request that it order specific performance of Tajikistan's obligation under the Energy Charter Treaty's umbrella clause to issue exclusive exploration licenses to the claimant because it would be materially impossible to implement a remedy of specific performance.[24]A tribunal denied Occidental Petroleum's request for provisional measures for specific performance of its contract, which Ecuador had terminated by declaring a "*caducidad*" on the ground that Occidental did not have a right to specific performance under international law.[25]In another case, Bridas Petroleum, an Argentine company, requested specific performance of its joint venture agreement with Turkmengeologia, a Turkmenian state company, but subsequently withdrew it.[26] The tribunal stated that they considered this a "wise" decision because it was unrealistic to assume either that Turkmengeologia would obey the tribunal's order of specific performance or that a national court having personal jurisdiction over it would enforce the order.

4.6 Remedies - Damages

There are a number of approaches to calculate damages in any dispute, including asset based, income based and market based approaches. Tribunals have considered and used many of them, such as net book value, discounted cash flow (DCF), going concern value and liquidation value. The more speculative the assumptions used in the calculations, tribunals become less comfortable with and unwilling to consider. Tribunals are comfortable with awarding out-of-pocket costs and losses to investors. They are not

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[22] Texaco Overseas Petroleum Co. (TOPCO) & California Asiatic Oil Co. v. Government of the Libyan Arab Republic, Award of 19 January 1977, 17 ILM (1978) p. 3, Yearbook IV (1979) p. 177.
[23]Bishop, *supra* note 3, at 1173.
[24]*Mohammad Ammar Al-Bahloul v. Republic of Tajikistan,* SCC Case No. V (064/2008), Final Award, June 8, 2010, paragraphs 35, 45-63.
[25]*Occidental supra* note 20, at, paragraphs 20-32, 75-94.
[26]*Joint Venture Yashlar v. Government of Turkmenistan,* ICC Arbitration Case No. 9151, Interim Award, June 8, 1999, paragraphs 538-40.

so comfortable in awarding lost profits, even when the claimant cloaks them in creative ways.[27]

The DCF method is probably the most controversial valuation methodology. Investors rely upon it in their preliminary investment decisions and their subsequent investment claims since they expect growth and profits in their investment. States often reject it because they consider the valuation method to be speculative and that any potential gains should stay with the ultimate owner of the resource, i.e., the state. Some tribunals have accepted the DCF method of calculating value "provided that the claimant could establish a likelihood of future lost profits with sufficient certainty."[28] Claims made on assets that are expropriated at the exploration stage where there is uncertain geology, questionable financing, no proven reserves, no production and no established revenue stream will have difficulty convincing a tribunal to apply the DCF methodology. Despite the uncertainty in the upstream petroleum sector, at least one tribunal has been willing to use a "risk economics" methodology and awarded some value to an exploratory concession based upon a dry well that provided information about the potential of the subsurface geology.[29]

5. Commercial Disputes

The sources for determining the *Lex Petrolea* arising from commercial disputes in the international oil & gas business are different than those arising from state investment disputes. Most of the publicly available case law that interpret commercial oil & gas agreements comes from U.S. (primarily Texas), Canadian (primarily Alberta) and English courts. Those cases deal with disputes arising from oil & gas operations in their own domestic jurisdictions. Oil & gas domestic operations and their agreements can vary quite significantly from the international industry's business practices and their agreements, which are illustrated in the analysis provided below on Joint Operating Agreements (JOAs) and Farmout (F/O) Agreements. Therefore, domestic oil & gas case law often falls short in establishing a relevant *Lex Petrolea* for the international oil & gas business.

Disputes that arise from international oil & gas agreements are mostly decided by international arbitration tribunals, which reflect the dispute resolution forums chosen in those agreements.[30]Those decisions are usually not publicly available because of the confidentiality requirements under the applicable dispute resolution clauses. Since international commercial arbitration awards are invariably not publicly available and

[27]Bishop, *supra* note 3, at 1175 & 1176.
[28]Childs, *supra* note 4, at 253.
[29]*Bettis Group Inc. v. Profco Resources Ltd., AAA Case No. 77-T-168-00228-98, Award, Sept. 9, 2000, at* 13-14 *available at* LEXIS, 18-3 MEALEY'S INT'L ARB. REP. 3 (2003).
[30] The 2002 AIPN Model JOA drafting committee sent a list of questions to all AIPN members asking them how they used the existing JOA and what revisions would be most beneficial. The survey confirmed that few disputes arose under the 1995 model JOA, that international arbitration was the preferred forum and that English law was widely chosen (with Texas and New York law being chosen less often than once thought). *See* Philip Weems and Michael Bolton, *Highlights of Key Revisions – 2002 AIPN Model Form International Operating Agreement* 6 Int'l Energy L & Tax'n Rev (2003) 169, 171. The result was that the 2002 AIPN Model JOA did not provide for courts as a binding mechanism in its dispute resolution clause, only international arbitration. This approach was continued in the 2012 AIPN Model JOA.

domestic oil & gas cases usually deal with very different kinds of operations and agreements, the best way of determining the *Lex Petrolea* of international oil & gas commercial agreements is by referencing the industry's business practices, which are captured in their model contracts.

The international petroleum industry uses model contracts extensively in its transactions and operations.[31] They are developed and published by petroleum industry associations. Parties regularly use and accept model contracts in the negotiation and drafting of their agreements. Model contracts that are widely used contain clauses that reflect industry practice and commonly accepted terms.[32]Model contracts standardise the terms governing certain common types of agreements used in the petroleum business.[33]They are drafted to be flexible enough to allow the parties to pick and choose the alternatives and options that work best for them.

> *With the acceptance of a particular model contract, it becomes widely used as the industry standard. The result is that transactions are drafted and handled more consistently and it is easier for parties to understand how they have addressed key issues in their contracts. With increased consistency and understanding, parties inherently reduce potential grounds for dispute and, therefore, their litigation risk.*[34]

5.1 Joint Operating Agreements

The most significant and long term contract used amongst oil and gas companies in the upstream oil and gas business is the JOA. It sets out the fundamental and overarching relationships in a joint venture consortium from the initial exploration to the ultimate production of hydrocarbons. A leading textbook on international petroleum transactions describes the primary purposes of an international JOA:

> *Each international JOA has two main functions. The first is to establish the basis for sharing rights and liabilities among the parties. In most cases, these will be shared in proportion to the interests of the participants in an operation. The second is to provide for the manner in which operations will be conducted by a designated operator subject to the supervision of an operating committee comprised of one representative from each party to the JOA*.[35]

The evolution of JOAs in North America has been different from those in the international oil and gas business for a number of fundamental reasons:

> *The oil and gas operating agreement has evolved as an industry-wide document over several decades. The widespread need for it in United States onshore*

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[31] A. Timothy Martin & J. Jay Park, *Global Petroleum Industry Model Contracts Revisited: Higher, Faster, Stronger,* 3:1 J WORLD ENERGY LAW & BUSINESS 6 (March 2010).
[32] A. Timothy Martin, *Model Contracts: a Survey of the Global Petroleum Industry,* 22:3 J. ENERGY & NAT. RESOURCES L. 284 (2004).
[33]Martin & Park, *supra* note 31, at 4.
[34]Martin, *supra* note 32, at 284.
[35]Bruce M Kramer & Gary B Conine, *Joint Development and Operations* in INTERNATIONAL PETROLEUM TRANSACTIONS 561 (2nd edn, Ernest E Smith *et al* eds, Rocky Mountain Mineral Law Foundation 2000).

> *operations has resulted in the development of a relatively uniform agreement for domestic activities. However, as the complexity and size of the operation increases, as in the case of offshore and international exploration and production, modifications in standard terms of the onshore agreement become necessary. Domestic offshore and international joint operating agreements (JOAs) are not only more detailed and significantly different from onshore counterparts but exhibit important variations from transaction to transaction*.[36]

Onshore domestic operations are relatively simple and straightforward. It is a less diverse and complicated operating environment. Operators usually conduct one operation at a time, e.g., shooting seismic or drilling a well, by issuing an Authority for Expenditure (AFE) that non-operators sign allowing the operator to carry out that particular operation without further adieu. Parties delegate broad authority to an operator in onshore North American operations. The result is a relatively simple and uniform agreement for domestic activities.[37]

International projects are larger in scale and more technically difficult than most domestic operations. Located in places where there may be very little infrastructure and long logistical chains, operators of international JOAs do not have broad discretion and do not make unilateral decisions on their own that bind non-operators. Instead, international JOAs provide for a management committee that exercises authority and control over operations. Management committees review and approve each item. The result is a more diverse and complex agreement.[38]

As a result, international oil and gas operations & their agreements are very different than agreements in domestic oil and gas operations.[39]Domestic US and Canadian onshore model JOAs[40] contain a limited number of elections, whereas the AIPN international model operating agreement[41] has many.

There have been a limited number of published arbitration awards dealing with international JOAs or similar agreements. *ICC Case No. 11663*[42] was about three parties that had a shared management agreement ("SMA") and participation agreement for a production sharing agreement. The SMA provided for the sharing of costs and expenses and required that if a party was in default for more than 60 days after receiving a default notice, it had to forfeit and assign its participating interest to the non-defaulting party

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[36] Kramer & Conine, *supra* note 35, at 561-2.
[37] Andrew B Derman & James Barnes, Inst on Oil and Gas Agreements, *Autonomy versus Alliance: An Examination of the Management and Control Provisions of Joint Operating Agreements* (Rocky Mt Min L Fdn, 1996), § 4.03 at 10.
[38] Kramer & Conine, *supra* note 34, at 564.
[39] Michael D Josephson, *How Far Does the CAPL Travel? A Comparative Overview of the CAPL Model Form Operating Procedure and the AIPN Model Form International Operating Agreement,* (2003) 41(1) ALTA L REV 1, 3.
[40] *See* The American Association of Petroleum Landmen (AAPL) at http://www.landman.org for its Onshore Joint Operating Agreement 610 and its Offshore Joint Operating Agreements (Shelf 710 and Deep 810) that are the standards for the U.S. oil & gas industry and the Canadian Association of Petroleum Landmen (CAPL) at http://www.landman.ca for its CAPL Operating Procedure., which is the Canadian oil & gas standard.
[41] *See* Model International Operating Agreement published by the AIPN at www.aipn.org, which is the standard used in the international oil & gas industry.
[42] *ICC Case No. 11663 of 2003,* Final Award on Jurisdiction, *in* XXXII Y.B. COM. ARB. 60 (2007).

upon the request of that party. One of the parties consistently failed to pay its share of cash calls. The other two parties served it with a default notice and demanded that it assign its interest to them. The Tribunal found that it was a "fundamental principle" of the SMA that each party must pay its share of cost and expenses under such an agreement and issued a declaration that the non-paying party had forfeited its participating interest in the project.[43]They found that this was consistent with standard practice in the oil and gas industry, as demonstrated by the AIPN model international JOA, which contained an alternative clause similar to what was in the SMA.

In addition, the Tribunal found that the management committee had the right to remove the operator and replace it with another party if it was in material breach of any of the parties' agreements. In this case, the non-paying party was also the operator and failed to provide a timely letter of credit to the ministry.[44] This case supports the ability of management committees to carry out their responsibilities under industry operating agreements. It also illustrates that tribunals are prepared to grant requests for specific performance (in this case, forfeiture and assignment of a JOA interest) in commercial disputes where damages are an inadequate remedy.[45]Based upon this case, one can conclude that a party that fails to pay its share of project costs and expenses can result in its default of a JOA and an obligation to forfeit and assign its participating interest to the other party(s) that pay the defaulting party's share.

5.2 Farmout Agreements

IOCs will often raise capital for exploration work programs by finding joint venturers through a farmout. This helps them spread both the risk and cost associated with exploration. Farmouts are usually structured in one of two ways with regards to when a farmor assigns a part of its interest to the farmee:

> *Farmout agreements traditionally have taken the form either of an agreement to convey or a conditional assignment. The essential difference in the two is the point in time when the farmee acquires an interest in the farmed-out property. When the farmout is in the form of an agreement to convey, the farmee obtains its rights only if it performs the conditions made prerequisite by the contract. When the farmout is in the form of a conditional assignment, the farmee obtains an interest in the farmed out property when the agreement is made, subject to an obligation to reconvey or to automatic termination if the conditions subsequent are not performed*.[46]

The traditional use of the term 'farmout' is normally applied to a 'drill to earn' arrangement. What normally happens in the North American oil and gas industry is that the farmee in its own capacity undertakes to either shoot seismic or drill a well or several wells (or both) on the farmor's oil and gas lease. Once the farmee completes that undertaking, it has earned its interest in that oil and gas lease. The farmee usually continues to operate that lease; rather than the farmor re-assuming its former operator role. These types of arrangements are relatively straightforward in North American operations where the land registry systems are efficient and government approval is not

[43]*Id.* paragraphs 7-15.
[44]*Id.* paragraphs 48-56.
[45]*Id.* paragraphs 69-72.
[46]John S Lowe, *Analyzing Oil and Gas Farmout Agreements,* 41 Sw. L.J. 759, 796 (1987).

required for the transfer of mineral rights. The international oil and gas industry also uses the term 'farmout', but the mechanics of the transaction are handled differently. Quite often, the farmee agrees to provide the funds to the farmor so that the farmor can carry out the agreed upon operations; while the farmee retains the ability to approve or not approve what the operator (i.e., the farmor) does. This reflects the legal, political and operational challenges encountered in the international oil and gas business. Failure to take these differences into account can result in the kinds of disputes described in the *Occidental* case referenced above.

5.3 Lex Petrolea in International Oil and Gas Commercial Disputes

There are only a few jurisdictions (most of which are listed above) that have a developed and sophisticated oil & gas jurisprudence. Most jurisdictions in which international oil & gas operations are conducted have no or very little such jurisprudence. As shown in the above examples of JOAs and farmout agreements, the agreements used in the international oil & gas business are quite different than those used in the domestic oil & gas business. This makes any reference to domestic oil & gas cases (even from well developed oil and gas law jurisdictions) quite limited in understanding how international commercial oil & gas agreements work and what they mean. International commercial arbitration awards are often not much help either in establishing a *Lex Petrolea* given the scarcity of such published awards. Therefore, the determination of the *Lex Petrolea* of international oil & gas agreements and the disputes arising from them are primarily found in the industry's business practices, which are recorded in their model contracts and the guidance notes, commentary and research arising from such models. The manner in which the industry develops its model contracts is the most thorough, documented and peer reviewed process for international oil & gas agreements and thus the most credible source of *Lex Petrolea* for such agreements.[47]

There are a series of steps (as appropriate) that arbitrators can take in determining the correct interpretation of international commercial oil & gas agreements being disputed and its *Lex Petrolea*. Similar to any contractual dispute, arbitrators need to first look to the contract itself and what it has to say. However, disputing parties usually have different interpretations of the same language because of some ambiguity, unexpected event or unique circumstance, which often leaves this initial inquiry short in definitive conclusions.

Arbitrators can then consider the choice of law in the contract and its general principles of contract interpretation. The common law usually requires that the contract is honoured as written and that adjudicators keep their inquiry within the "four corners of the contract" even if there is an unfair result. The civil law is generally concerned that the contract is fair to all parties and is performed in good faith. The Shari'a law, similar to the common law, uses precedent and strictly interprets contracts as written. But as required by the Koran, Shari'a prohibits practices such as ribat (interest/usury) and gharar (speculation on uncertainty). While common law, civil law and Shari'a law jurisdictions share many similarities within their respective systems, due to the possibility of varying solutions to the same issue found in different countries, one has to consider the specific governing law in an oil & gas contract to determine if there are any relevant precedents or principles.

[47] Martin, *supra* note 32, at 284.

Arbitrators need to next look at the facts of each particular case, which is where many of these cases are determined. Consideration needs to be given to relevant case law, keeping in mind the limitations of domestic oil & gas case law and the dearth of published international commercial arbitration awards. Arbitrators then need to turn to industry practice to confirm how these agreements are used and interpreted. The primary source of determining such business practices in the oil & gas industry is its model contracts. The model contracts developed and published by the AIPN are the main source for confirming business practices in the international oil & gas business.

6. Individual and NGO Disputes

There is a body of *Lex Petrolea* that has developed over the last two decades where individuals and groups, including non-governmental organizations (NGOs) and plaintiff lawyers who represent them, have pursued international oil & gas companies in U.S and other courts around the world on charges of human rights and environmental violations. One of the largest and most spectacular cases is the *Lago Agrio* case against Chevron. It is a long running case that has been fought in multiple forums, including international arbitration tribunals, U.S., European and Ecuadorian courts. It arose from the operations of Texaco (which was acquired by Chevron in 2001) in the Lago Agrio area of the Oriente region of Ecuador between 1964 and 1990. The plaintiffs, who are native Indians, allege that Texaco dumped toxins into the water supply that resulted in the destruction of the local rainforest and physical harm and cancer to the indigenous people. In February 2011, a judge in Sucumbios province, Ecuador, delivered a judgment of US$ 18.2 billion against Chevron. The native Indians are represented by a group of U.S. plaintiff lawyers who are financed by publicly traded investment funds.[48] There have been subsequent legal actions by Chevron in U.S. and European courts against the lead plaintiffs' lawyers alleging fraud, intimidation of judges, fabricated evidence and criminal collusion. The case is still unresolved as of the writing of this article, even though Chevron has been recently successful on several claims dating back to 1991 in an UNCITRAL dispute administered by the Permanent Court of Arbitration in the Hague.[49]

The majority of human rights cases have been brought in the United States under the Alien Tort Statute. There is, however, an increasing trend of such cases being brought in other domestic courts around the world, such as Ecuador, Colombia, and Australia; and international bodies, such as the committees responsible for the following U.N. Conventions: the Torture Convention, the Optional Protocol to the International Covenant on Civil and Political Rights, and the Convention on the Elimination of All Forms of Discrimination Against Women. There are other tribunals responsible for regional conventions that are getting involved in similar human rights charges, such as: The Convention for the Protection of Human Rights and Fundamental Freedoms, enforced by the European Court of Human Rights; the American Convention on Human

[48] Roger Parloff, *Have You Got a Piece of this Lawsuit? The Bitter Environmental Suit Against Chevron in Ecuador Opens a Window on a Troubling New Business: Speculating in Court Cases*, 163:8 FORTUNE (June 13, 2011) 69.

[49] http://www.chevron.com/chevron/pressreleases/article/08312011_chevronawarded96millioninarbitrationclaimagainstthegovernmentofecuador.news

Rights, enforced by the Inter-American Commission; and the African Charter on Human and Peoples' Rights, enforced by the African Commission.[50]

Oil and gas companies will likely see a continuing increase in these cases in multiple forums. They therefore need to be aware of developments in this particular area of *Lex Petrolea* in order to properly manage their risks.

CONCLUSION

Lex Petrolea covers a wide area of international law, given the size and significance of the industry. It can be viewed as either the application of international law to the petroleum sector or as a specific legal regime that has evolved to meet the particular needs of the international oil and gas sector. Or it can be viewed as both.

The growing development of *Lex Petrolea* in areas such as disputes about boundaries, human rights and environmental claims is more akin to the former, i.e., the application of international law to the petroleum sector. Whereas the areas of international commercial disputes and state investment disputes are more the latter ,i.e., a customary law of the international petroleum sector that has been adapted to the industry's nature and specificities. No matter what the view adopted, *Lex Petrolea* is clearly a law that has impacted a great deal of international public and private law as we know it today.

[50] Drimmer, *supra* note 9, at 133.