INTERNATIONAL MEDIATION AND ARBITRATION CONFERENCE

2nd South Pacific International Arbitration Conference

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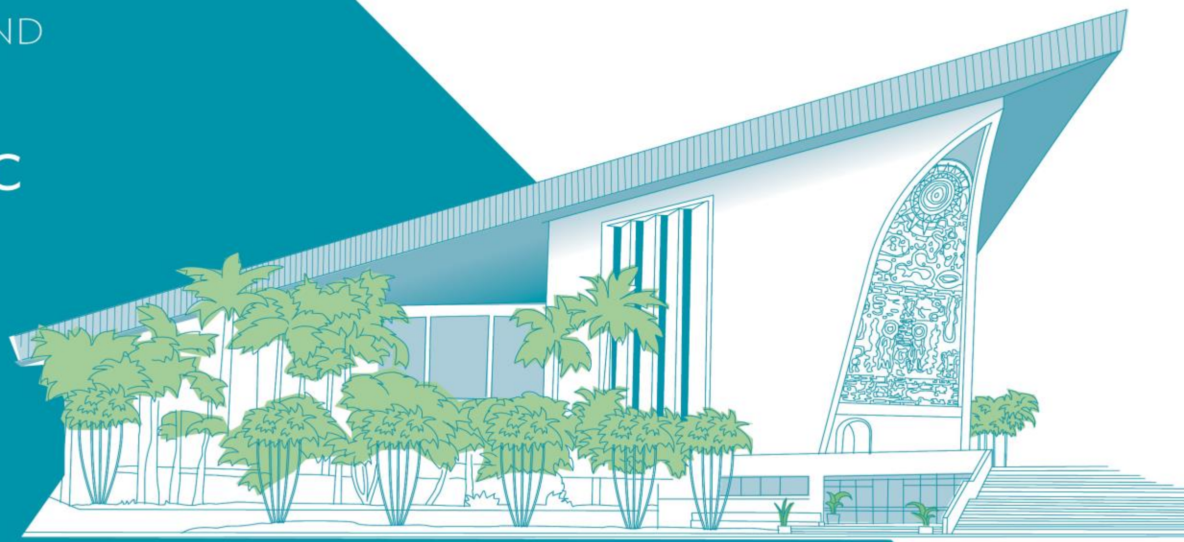
Stanley Hotel, Port Moresby
Papua New Guinea



International Commercial Arbitration in Upstream Oil and Gas Vector

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KEY STAGES OF OIL AND GAS PRODUCTION

Upstream	• Exploration of reserves • Drilling & evaluation of the commercial viability of wells • Recovery & production from fields
Midstream	• Transportation • Storage
Downstream	• Refining and processing • Distribution

UPSTREAM KEY COMMERCIAL CONTRACTS:

- **Concession agreement**: venturers are granted rights by the host state to develop a specified area and are granted title to hydrocarbons in exchange for royalties and taxes. Agreement may also cover royalties for indigenous communities and a percentage offtake for use in the host state.
- **Production sharing agreement**: venturers granted rights to develop the field but host state retains title to the extracted product. Venturers bears exploration, production and development costs in exchange for a share of profit.

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UPSTREAM KEY COMMERCIAL CONTRACTS:

- **Joint operating agreement (JoA)**: Typical structure involves several SPVs (special purpose vehicles) participating in an unincorporated JV.
  JOA will cover:
  - participant contributions including funding, equipment and personnel /expertise
  - decision making processes on development and expenditure (e.g. through an operating committee)
  - equity funding / cash calls, including timing for cash calls and the consequences of not responding
  - lifting rights to a proportionate share of production
- **Operating or management agreement**: in some cases a separate operating or management agreement will define the rights and obligations of the operating entity (whether the operator is either a JV participant or SPV). This will include obligations to adhere to international and local environmental, health and safety obligations.

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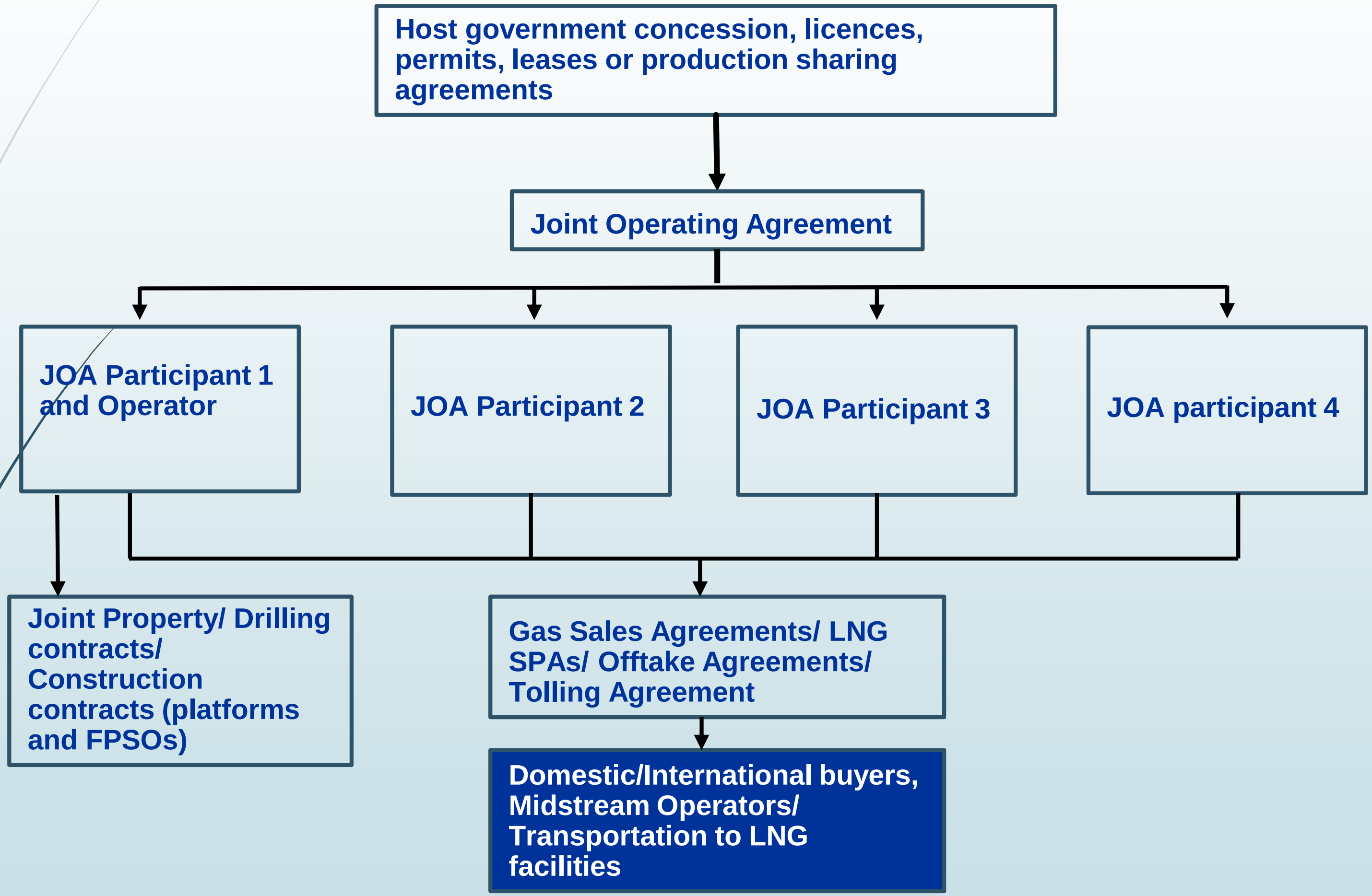
KEY COMMERCIAL CONTRACTS: UPSTREAM PHASE

- Other commercial contracts govern:
  - **Procurement and contractors**: e.g. drilling contracts, vessel and equipment hire, including period of use, maintenance and technical support
  - **Intellectual property and confidential information**: e.g. licenses to use proprietary technology, rights and obligations in relation to new IP created by the JV
  - **Insurance** covering e.g. operational risks, third party liability, D&O insurance (incorporated JVs), pollution risks and clean up costs, workers compensation and political/security risks
  - **Leases** with local landholders

UPSTREAM CONTRACTING STRUCTURE : UNINCORPORATED JV



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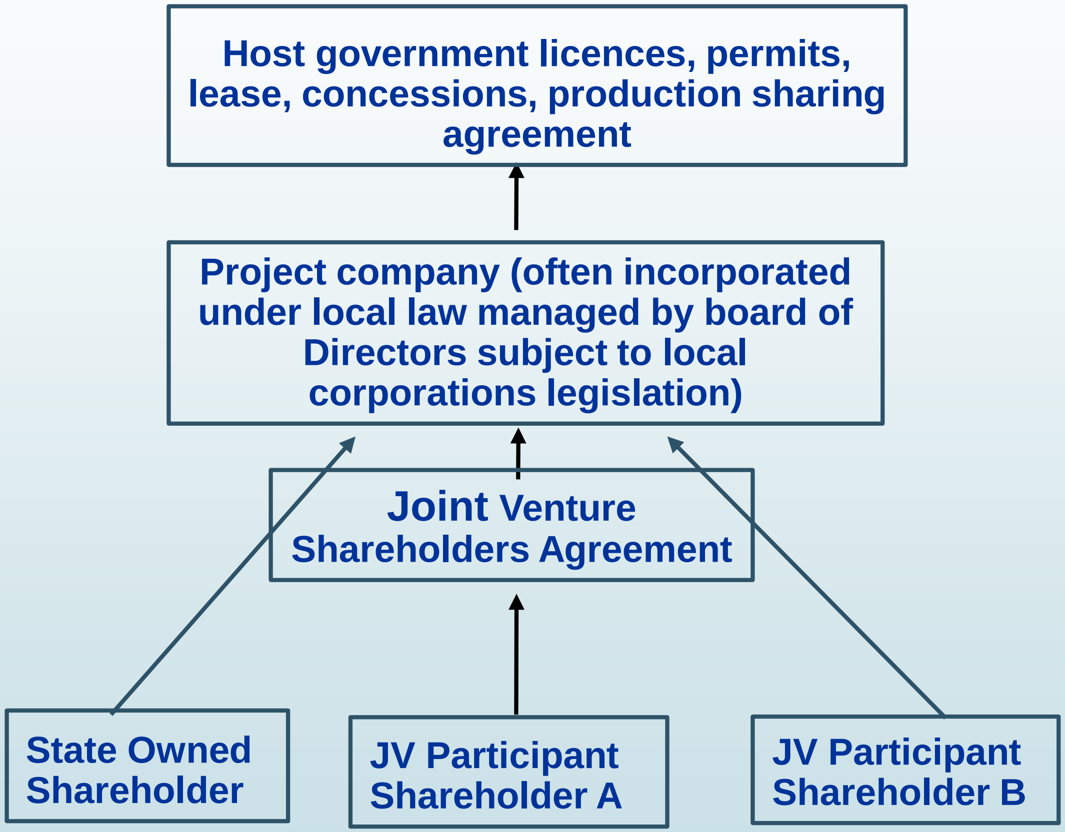

Disputes under concession & production sharing agreements – between host and venturers

- Calculation of taxes and royalties
- Allocation of geological risks
- Claims by investors to invoke stability / stabilization provisions
- Access to infrastructure and resources including water

In production sharing contracts:

- What costs are recoverable before profit is allocated
- Allocation of profit petroleum

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Inter-investor disputes

- Disputes between the operator and non-operators
- Commercial consent / authorization of expenditure
- Compliance with management agreements, JV processes, authority
- Consequences of meeting payment obligations
- Rights of pre-emption (i.e. option to buy out interest on terms being offered by third party), first refusal or consent in relation to disposal of interests
- Breach of warranties / allocation of risk / calculation of loss related to inherent uncertainties (i.e. seismic data, price prediction or reserve prediction)
- Disputes over tax liabilities (i.e. interpretation of indemnities and warranties)

Inter-investor disputes: incorporated Joint ventures

- Disputes may arise under the relevant company law e.g.
  - oppression of minority interests
  - claims of breach of directors' fiduciary interests.

  N.B. directors may find themselves torn between their obligations as employees of an investor, and fiduciary duties owed to the company of which they are a director.

Disputes with third parties

- Disputes with service providers e.g.
  - geophysical prospecting
  - equipment failures and breach of supply
  - ancillary services e.g. labour hire, catering, accommodation.
- Disputes with other JVs:
  - utilization agreements over abutting blocks
  - equipment sharing and cost-splitting arrangements.
- Disputes with insurers.

Benefits of arbitration in upstream disputes

- **Neutrality**: disputes resolved by an independent panel of international experts, usually lawyers.
- **Confidentiality and privacy**: typically, significant elements of proceedings with be confidential which is beneficial to preserving relationships on multi-decade ventures. Hearings are conducted in private reducing external scrutiny of individual witnesses and experts.
- **Enforceability**: upstream ventures are typically operated on an international basis with business partners and joint ventures located in different countries. Arbitral awards are generally readily enforceable under the New York Convention 1958 (ratification by 159 signatory states).

Arbitration: key considerations for upstream ventures

- **Management of long term relationships**: ventures are long term and represent significant capital investment. The preservation of relationships must feature in any arbitration strategy e.g.:
  - optimise opportunities to settle and avoid formal proceedings
  - avoid incendiary pleadings e.g. allegations of bad faith or misrepresentations.
- **Parties to the arbitration agreement**: careful drafting, taking account of interlocking and related agreements, is required to mitigate the risk of a parties' interests being impacted by related entities which are not party to the arbitration agreement.
- **Relevant laws:** relevant agreements sometimes reflect a compromise between local law and international legal standards.

Arbitration: key considerations for upstream ventures

- **Consistency of dispute resolution arrangements:** careful planning is required to manage disputes where arrangements across the suit of upstream contracts are not completely complimentary.

  i.e. risk of parallel proceedings, and asymmetries in relation to specific parties being bound to a particular award.

- **Multiple parties; multiple arbitrations**: ideally, careful consideration will be given at the drafting stage to manage this risk. Otherwise, this needs to be considered in the early stages of any disputes.