INTRODUCTION

The potential for disputes occurring in the oil and gas industry remains high. This is not surprising having regard to the myriad contractual relationships and the immense costs of hydrocarbon exploration and exploitation.

This paper will examine the rudiments of the nature of the International Commercial Arbitral process, the relevance of arbitration to the petroleum industry and the use of arbitration in the different relationships and contractual arrangements in the oil and gas industry. I will then look at the developing forms of alternative dispute resolution, known by its acronym 'ADR', and its application as a tool of dispute resolution in the petroleum industry. Finally I will discuss some dispute minimisation and avoidance measures currently in use in the industry and conclude by assessing the challenges facing the Lagos Regional Centre in its objective of becoming the Regional Centre for International Commercial Arbitration in Sub-Sahara Africa.

It is perhaps necessary to say two things about this paper at the outset. First, I have deliberately adopted a broad brush approach to the subject of arbitration in the oil and gas industry. I am aware of the diverse professional disciplines and interests of those interested in the subject of arbitration, many of whom may not work in the petroleum industry, but who may perhaps be interested nevertheless to know something of the manner in which disputes are resolved in the industry.

Second, I have tended to have a 'Petroleum Upstream' bias in this paper, mainly due to the fact that this is the area in which I mostly render professional legal advice and also because to do otherwise would result in an inordinately lengthy paper.

For those who work in the oil and gas industry, I hope to have provided enough material to stimulate debate and encourage you to delve further into the areas treated.

WHAT IS INTERNATIONAL COMMERCIAL ARBITRATION?

Arbitration has been described as 'a private process which commences with the agreement of parties to an existing, or potential, dispute to submit that dispute for decision by a tribunal of one or more arbitrators.'

Arbitrations are regarded as **International** by UNCITRAL (the United Nations Commission for International Trade Law) in the Model Law on International Commercial Arbitration if:

" (a) the parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of businesses in different States; or

(b) one of the following places is situated outside the State in which the parties have their places of business:

(i) the place of arbitration if determined in, or pursuant to, the arbitration agreement;

(ii) any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject-matter of the dispute is most closely connected; or

(c) the parties have expressly agreed that the subject matter of the arbitration agreement relates to more than one country."[2]

International arbitrations are of course in contrasts to **domestic** arbitrations which involve a country's own nationals.

An arbitration is **commercial** in nature which covers matters arising from all relationships of a commercial nature, whether contractual or not.

The significance of the fact that an arbitration is **international** in nature lies in the fact that a number of legal systems may be relevant in the dispute. For example, where a *Ghanaian* company has a contract with a *German* company, expressed to be governed by *English* law and disputes arising out

1. Pg. 3, *International Commercial Arbitration - A Handbook* by Mark Huleatt-James and Nicholas Gould (1996) published by LLP.
2. Article 1(3) of the Model Law adopted by the UNCITRAL on June 21, 1985.

of which are to be submitted to arbitration in *Nigeria* pursuant to the arbitration rules of the Lagos Regional Centre for Commercial Arbitration. In such a case, it will be necessary to decide:

1) the law applicable to determine **the capacity** to enter into the arbitration agreement - in the case of a corporate entity it is usually the law of the place of incorporation.

2) the law applicable to the **arbitration agreement** itself - the concept of the 'autonomy' or 'severability' of the arbitration agreement means that it is a separate agreement and survives termination of the contract in which it is contained. The law applicable to the **arbitration agreement** itself can therefore be different from that applicable to the principal contract.

3) the law applicable to the **arbitration proceedings** (*lex arbitri*) - usually the law of the country in which the arbitration is taking place.

4) the law applicable to **the dispute** itself (*the lex causae*) - the parties often choose the applicable law, failing which, the relevant International Arbitration Rules or the conflict of laws rules of the seat of arbitration should resolve the point.

5) the law applicable to the **enforcement of the award** - the law of the country in which enforcement is sought.

ARBITRATION IN THE INTERNATIONAL PETROLEUM INDUSTRY

Arbitration is widely used in the oil and gas industry, and in particular, the UNCITRAL Rules are being adopted more often in oil industry arbitrations.

Several factors contribute to the use of arbitration for dispute resolution in international agreements in the petroleum industry including:

1) The technical nature of the industry which requires an arbitrator with specialist knowledge.

2) The high degree of use of sophisticated contracts drafted by professional advisers means that dispute are anticipated and resolution procedures put in place.

3) The international nature of the operations of multinational oil and gas companies and cross border oil and gas fields, favour arbitration as a mode of dispute resolution.

4) Overlapping commercial interests and long term contractual relationships between oil and gas companies militate against litigation which is often expensive, time consuming, adversarial and destructive of good relationships.

ARBITRATION IN OIL AND GAS ARRANGEMENTS/AGREEMENTS

The oil and gas industry routinely employs arbitration agreements in contractual arrangements. I will highlight some of the more common types of contracts and relationships:

1. **Governments and Oil Companies**

Typical examples are the grant of an Oil Exploration Licence, Oil Prospecting Licence or Oil Mining Licence by the State to a Lessee and the grant of fiscal incentives by the Government in the form of a Memorandum of Understanding or Side Letter.

Traditionally, Governments did not like entering into Arbitration, assuming the position that any attempt to diminish its powers in dealing with interests conferred in the oil industry amounts to a derogation of its sovereignty. However, the Washington Convention of 1965 which provides for the establishment of the International Centre for the Settlement of Investment Disputes (the *ICSID Convention*) is gradually removing this barrier.

The ICSID, an autonomous international organisation and a member of the family of World Bank Institutions, provides facilities for the arbitration of investment disputes between host Governments and foreign investors. ICSID jurisdiction is limited to disputes occurring between a Contracting State and a national of another Contracting State. Although parties must consent in writing to submit disputes to the ICSID, such consent may be expressed in bi-lateral treaties and foreign investment laws as well as in contracts.

Host States wishing to attract foreign investment often advertise their willingness to resolve foreign investment disputes using the ICSID, in domestic investment laws.[3] Foreigners are encouraged to invest taking comfort from the fact that they will not be compelled to submit disputes to an unfamiliar panel.

A local example of contemporary host Government's enthusiasm for inclusion of arbitration clauses is the Nigerian LNG (Fiscal Incentives' Guaranties and Assurances) Decree No. 39 of 1990, as amended. Paragraph 22, Schedule 2 of that legislation provides that, in the event of failure to amicably resolve any dispute within 90 days of issue of the letter of notification of the dispute to the Government, such dispute may be submitted to arbitration before the ICSID.

It may nevertheless be prudent where the other party to the arbitration agreement is a State, to ask for waiver of both its immunity to the jurisdiction of the Courts of the place of arbitration and its immunity from execution in respect of any award made against it.

2. **Joint Concession Holders (Joint Ventures, Production Sharing Contracts and Farm Out Agreements)**

Contractual arrangements may be made between an oil company and a designated State enterprise to create a joint interest or to grant a general exclusive authorisation to the oil company in respect of a certain area (the licence area). Similarly joint ownership arrangements may exist between oil companies. Examples are Joint Venture Arrangements, Joint Operating Agreements and Production Sharing Contracts. Arbitration Agreements are commonly found in these contracts, although the applicable law is generally that of the State enterprise, if any, reflecting the stronger bargaining power of the State.

3. *The International Centre for Settlement of Investment Disputes: Responses to Problems and Changing Reqiurements* by Carolyn B. Lamm & Abby Cohen Smutny in The Journal of the Chartered Institute of Arbitrators, Vol. 64, No. 1, February, 1998.

It has been said with regard to parties to a **Joint Operating Agreement** (JOA) that their relationship is akin to that of a marriage. The partners agree

"to have and to hold in accordance with the terms of the JOA until termination, withdrawal, assignment or default do us part."[4] Consequently a long relationship is envisaged in that type of arrangement.

Issues which may likely lead to disputes in this type of arrangement include (i) cash call requirements (ii) supplies made to the Joint Venture Operations (iii) control of the Operator and (iv) approvals by the Joint Operating Committee.

In a **Production Sharing Contract**, the contractual arrangement is between a foreign oil company (Contractor) and a designated State enterprise (State party) authorising the Contractor to conduct petroleum explorations and exploitation within a certain area (contract area) in accordance with the rules of the agreement. Further, it is the Contractor that is responsible for funding the exploration and exploitation work. Whilst the State party owns the resources, it lacks the required manpower, funds and technology to exploit it. Further as the sums involved are usually substantial, in the event of a dispute, parties are likely to opt for arbitration.

A Farm Out Agreement is "an agreement whereby a third party agrees to acquire from one or more of the existing licensees an interest in a production license and in the operating agreement relating to it, for a consideration which in oil industry practice will normally consist of the carrying out of a specified work obligation, known as the earning obligation, used in the drilling of one or more wells."[5] In simpler terms, they refer to 'deals where a company not at present a licensee on a particular licensed area, can acquire an interest from one of the existing licensees".[6]

3. Contracts between Oil and Gas Companies

Common types of contracts between Oil and Gas are Unitisation Agreements and contracts granting Third Party Access to oil field facilities.

4. *Joint Operating Agreements* by Sandy Shaw, Upstream Oil and Gas Agreements (1996), Sweet & Maxwell.
5. Daintith & Willoughby, United Kingdom Oil and Gas Law (2nd Ed.) See also A. Akinjide, "*Why Oil Companies do Farm-Out and Farm-Ins* (1 & 2)" the Guardian (Lagos) 4 March, 1997, 35, 11 March, 1997, 30.
6. United Kingdom Department of Energy Press Release, 27 Nov. 1990, titled *"New Statement on Guidelines for Oil and Gas Farm-In Deals"*.

The Unitisation Agreement is an agreement by the owners of a single oil field which extends into more than one license area to develop that field as a single unit.[7] Otherwise referred to as 'Unit Operating Agreement', the Unitisation Agreement normally includes all the provisions of an ordinary JOA, together with additional ones which are intended to establish the rights of the respective parties to production from the field. A typical clause of such an agreement runs as follows:

"All rights and interest of the parties under the licenses are hereby unitised in accordance with the provisions of this Agreement in so far as such rights and interest pertain to the Unitised Zone and each of the parties shall own all unit property and unitised petroleum in undivided shares in proportion to its Unit Equity."

It is therefore evident that from wherever in the reservoir unitised petroleum actually comes, and in whichever licence block the platforms are located, the owners will own them in their unitised proportions.

This arrangement makes economic sense and is also environmentally attractive. However, a party though signatory to the agreement, who observes that much of the 'Unitised Petroleum' comes from his licence area may attempt to renege on the agreement. A pre-emptive measure might be to include in the Unitisation Agreement a reward system which takes into consideration the situation just described. Arbitration proceedings where adopted should also reflect this fragile arrangement. Institutional arbitration may be advisable. That is because of the experience and expertise of those institutions.

Invariably, Unitisation Agreements provide for the appointment of an expert, for binding expert determination in the event of dispute during the equity determinations. This is known as the 'Guided Owners' process in which an expert is appointed from the beginning of the process, before any dispute arises. The expert is invited to all discussions of the unit owners and as such will be aware of all the issues and positions of the parties as the process evolves. The advantage of this process is that disputes are resolved promptly as they arise, saving the parties the huge costs attendant on delays. The use of Expert Determination will be further examined in this paper.

7. *Unitisation Agreements* by Warwick English, Upstream Oil and Gas Agreements, (1996) Published by Sweet & Maxwell.

4. Oil and Gas Operators and Service Contractors

The list of services provided by Contractors to Operators in the oil and gas industry is endless, ranging from major construction and rig leasing contracts to minor supply contracts. Arbitration clauses are a common feature of contracts in this category, with the Operator often providing standard forms of contract.

However where the Contractor is providing highly specialised services or plant and equipment, there is likely to be intense negotiation between the parties on the content of the Arbitration Agreement, for instance in Mobile Production Unit Agreements. Mobile Production Units (MPUs) i.e. Jackup Rigs, Semisubmersible Drilling Rigs and Floating, Production, Storage and Offtake facilities, are facilities which can be rapidly mobilised and demobilised at low cost.

These MPUs are often the subject of leasing arrangements between the Contractor/Owner and oil companies. Against this background, as the parties are likely to be in business together for a long time and considering the huge amounts at stake, an arbitral process is often carefully negotiated to resolve any disputes arising during the life of the contract.

ALTERNATIVE DISPUTE RESOLUTION - THE APPROACH IN THE COMING MILLENNIUM

The development of ADR methods is a reflection of the general belief that Arbitration is an expensive imitation of litigation and that Arbitration has failed to deliver the much heralded benefits of speed, cost savings and procedural flexibility.

ADR procedures are varied and include

1) mediation,
2) concililation
3) mini-trial
4) non-binding Expert Finding
5) binding Expert Determination
6) Final Offer Arbitration.

The ADR procedures stated in 1 - 4 above are non-binding while procedures 5 and 6 are binding.

The growing acceptance and importance of non-curial dispute resolution cannot be overstated. In the UK, the Woolf Report on '*Access to Civil Justice*' and the resulting promulgation of The New Civil Procedure Rules which came into effect yesterday i.e. Monday, 26 April 1999, is testimony to the tremendous importance that even the Court system attaches to ADR methods. The new UK Civil Procedure Rules 1999 enjoin the Court to actively manage cases and take steps for "*encouraging the parties to use an alternative dispute resolution procedure if the Court considers that appropriate and facilitating the use of such procedure*".

The enlightened view today tends towards bringing ADR into the mainstream of dispute resolution. Because ADR can lead to early resolution of disputes, it might be said that a lawyer who did ***not*** provide in the parties' contract for ADR to take place prior to the commencement of legal proceedings or litigation, has done his client a disservice.

In line with this approach, arbitration institutions such as the American Arbitration Association (AAA), the International Court of Arbitration of the International Chambers of Commerce (the ICC), ICSID and UNCITRAL have all embraced ADR procedure and published Conciliation Rules.

Non Binding ADR

Mediation - The mediator (chosen by the parties) is a person of integrity who is impartial, and who possesses the necessary skills to assist the parties to a dispute to negotiate a settlement. This entails a process of managing conflict and constructively facilitating a settlement.

Conciliation - Conciliation is similar to mediation, except that the conciliator will take a view on a fair settlement and recommend it to the parties.

Mini-trial - This involves the presentation by both sides of their case to a panel made up of senior executives from each party together with a neutral chairman. The aim is to narrow the areas of contention and open negotiations for a settlement.

Non-binding Expert Finding - the parties engage an expert to make an appraisal of the dispute, especially where the issues are highly technical, who suggests an outcome, which is non-binding.

The perceived advantages of non-binding ADR procedures are:

- the possibility of creative 'win/win' settlements
- speed
- reduced costs
- maintenance of relationships
- confidentiality
- ADR often takes places concurrently with arbitration or litigation.

The disadvantage of non-binding ADR procedures is that the procedure may **not** result in a resolution of the dispute. Where parties fail to agree then they have to fall back to litigation or arbitration or other forms of binding ADR.

Also, non-binding ADR can be viewed as ineffective as it is unenforceable. A party to an agreement can change his mind and renege on the deal. In such a case, the only way to enforce the agreement is to initiate a Court action in contract based on the settlement agreement, obtained judgement and levy execution process. On the other hand, voluntary compliance with mediated settlement is very high, as the parties see themselves as owners of the mediation process. Where ADR is used as complementary to litigation or arbitration it may be possible to record the terms of the settlement as a consent judgement or consent award.

Binding ADR

Expert Determination - The parties agree to refer their disputes to an expert, whose decision is 'final and binding on the parties.' Like arbitration, expert determination is rooted in contract.

However unlike arbitration:

- it is an inquisitorial process and the expert may reject both partiesí views in favour of his own views

- an expert need not give reasons for his decisions

- an expert has no immunity from suit where he does not exercise reasonable skill and care

- the Courts have no supervisory or coercive jurisdiction over experts

- there is no automatic recognition and enforcement of an expert's decision[8].

Expert determination is particularly useful in the oil industry because of the enormous sums involved, the technical nature of many disputes and the need to preserve long term relationships.

Final Offer Arbitration - Involves each party submitting their final offer to an arbitrator who must choose one of the two alternatives. A variant of this procedure is *not* to disclose the final offers to the arbitrator until *after* he has made a decision and then choose the offer which comes closest to the arbitratorís decision. The benefit of this procedure is that it forces the parties to moderate their claims and in so doing can lead to a settlement before the arbitrator's decision is made. Additionally, the parties know the 'worst case' outcome and it eliminates the surprise element inherent in an expert determination.

Clearly, binding ADR procedures, like non-binding ones, are cheaper, quicker and less formal than arbitration.

PARTNERING AND ALLIANCING

It is worth mentioning very briefly here recent use of Partnering or Alliancing agreements between oil companies and service companies, where attempts are made to reconcile strict business relationships with the conduct and will of the parties. Partnering agreements recognise the principle that

"Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement"[9].

8. *Expert Determination and Final Offer Arbitration* by Caroline Kehoe and Ted Greeno, Institute of Petroleum Conference Proceedings, December, 1998.
9. (1981) Restatement (Second) of Contracts, American Law Institute.

The goal of these Partnering contracts is to save costs by minimizing disputes, using gain sharing and risk sharing mechanisms, reducing adversarial contract clauses and forging close working relationships and teamwork.

Alliancing agreements will often contain 'Motherhood Statements' stating "the aim and purpose of the venture, articulating the joint aspirations, targets and ideas and philosophies of the parties."[10]

This "new culture of co-operation and even collaboration instead of confrontation"[11] if clearly followed through in the contract documents should produce the effect of avoiding disputes and, at the very least, minimise the negative consequences of disagreements.

CHALLENGES FACING THE LAGOS REGIONAL CENTRE

The scope for the Lagos Regional Centre to facilitate arbitration and ADR procedures in international commercial disputes arising in the oil and gas industry in West Africa is vast. The West African oil industry encompasses such mature and maturing markets as Cameroon, Cote D' Ivoire, Equitorial Guinea, Gabon, Ghana, Mozambique, Namibia and the Republic of the Congo. There is every reason to believe that the Lagos Regional Centre is up to the challenges ahead.

The Arbitration Rules of the Lagos Centre are the UNCITRAL Arbitration Rules, which enjoy widespread international acceptance.

The *lex arbitri*, where the arbitration takes place in Nigeria, is based on the UNCITRAL model law and most importantly, the Nigerian judiciary increasingly supports arbitration by recognising one of the principal objectives of UNCITRAL in the preparation of the Model Law i.e.

"to limit the role of national Courts and to give primacy to the will of the parties in establishing the procedure for the settlement of the disputes." [12]

10. *Dispute Minimisation and Avoidance in the International Oil and Gas Industries* by Stephen Hallam, Robert Palmer and Belinda Schofield, Institute of Petroleum Conference Proceedings, Dec., 1998.
11. *Partnering - Think it Through* by John B. Dorter, The Journal of the Chartered Institute of Arbitrators, Volume 63, No. 3, August, 1997
12. Pg. 23, International Commercial Arbitration - a Handbook, Ibid.

AUTHOR'S PROFILE

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Mrs. Jumoke Akinjide-Balogun is the Managing Partner of AKINJIDE & CO. She holds an LL.B (Hons) Degree from Kings College London and a Masters Degree (LL.M) from Harvard Law School, USA. She qualified both in Nigeria and as a Solicitor of England and Wales, achieving first class honours in the English Solicitors Final Examinations. She worked with Simmons & Simmons, one of the top ten firms in the city of London.

Mrs. Akinjide-Balogun is a member of the Chartered Institute of Arbitrators (UK), Nigerian Bar Association, the International Bar Association, the Harvard Business School Alumni Association and the Institute of Petroleum.

She is also a member of the Continuing Legal Education Association of Nigeria, the Nigerian Maritime Law Association and the Women's International Shipping and Trading Association (WISTA).

Mrs. Akinjide-Balogun is the author of several articles on Nigerian company law and oil & gas law.

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This is a core strength of the firm. The energy team acts for international oil companies, service companies, small producers/indigenous oil companies and the Nigerian National Petroleum Corporation. We have extensive experience of advising on all aspects of the oil and gas industry including joint ventures, production sharing contracts, operating and technical services agreements, farm-in agreements, exploration, drilling and production contracts and other contracts for services, project finance, interpreting and advising on the Nigerian petroleum laws and regulations.

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