Standardisation of Oil and Gas Law: The Emergence of Transnational Layers of Governance

Djakkhongir Saidov
Diamond, timber, construction and other industries/commercial sectors:

- In a globalised environment, with its drive towards harmonisation/uniformity, all these sectors manifest tendency towards increased standardisation of governance
- Extensive use of and reliance on model contracts
- ‘Self-regulation’: governance by sources, that are not rooted in or based on national/state law
In parallel, a long-standing debate about the existence and content of global law merchant (\textit{lex mercatoria}):

- Does the law governing business transactions that is autonomous from state-made law really exist?

- If so, what are its constituent sources?

- Can non-state made sources be regarded as ‘law’?
Introduction: *lex petrolea*

- These Qs already directed at the oil and gas (O&G) industry:
  - proliferation of non-state made rules and norms = a truly autonomous transnational petroleum legal order (*lex petrolea*)
  - There is an international petroleum community:
    - 'whenever there is a social body that meets a certain degree of autonomy and organization there is manifestation of the law'
  - Transn’l c–ts function best in a legal order which is transn’l
  - *Lex petrolea* = self–sufficient
  - Sources: various international arbitral awards, industry model c–ts and the alleged existence of customary law, industry standards and practices relating to petroleum E&P
Introduction: Questions to explore

- To what extent is the O&G industry self-governed?
- To what extent are the petroleum operations and transactions governed by state-made law?
- What is the actual content of some of the key (potential) sources of ‘non-state made law’?
- What is the interaction between them all?
- Has transn’l petroleum law/lex petrolea emerged?
Introduction: practical consequences

- If exists, *lex petrolea* can be used as an applicable law, governing petroleum c–ts

- Even where c–ts are governed by domestic law, its content/meaning and that of the relevant c–ts/licences is likely to depend on ‘transn’l petroleum law’

- Given how widely certain generic clauses/standards are used, more clarity and certainty needed with respect to the meaning of such clauses/standards
Cycles of operations:

- Upstream (exploration, development, production (E&P))
- Midstream (processing, storage, transportation up to the point of sale)
- Downstream (refining, marketing, distribution, sale)

Key players:

- International oil and gas companies (IOCs) (majors, other integrated companies, independents)
- Host countries/governments and their national oil companies (NOCs)
State-to-IOC (vertical) relationship:

- Petroleum and related legislation:
  - Constitution
  - Petroleum Code/Law/Statute
  - Petroleum Regulations
  - Instruments, granting E&P rights: c-ts or licences
Company-to-Company (horizontal) relationship:

- Area of Mutual Interest (AMI)
- Joint Bidding Agreements (JBAs)
- Joint operating agreements (JOAs)
- Unitisation agreements
- Lifting agreements
- Service contracts
- Confidentiality agreements
- Sale and acquisition of petroleum assets (eg, farm-outs, exchange of assets, asset sale, share sale)
- Decommissioning security agreements
- Gas Sales
In the vast majority of countries: state ownership of natural resources (permanent sovereignty over natural resources)

Hence, an instrument, granting E&P rights to an IOC(s), is required

A granting instrument and legislation on which it is based = main source of regulating E&P operations
These regimes are structured differently:

- Licences/Modern Concession Contracts
- Production Sharing Contracts
- Risk Service/Iranian Buy–Back Contracts
- Joint Ventures/Hybrid Arrangements

That’s it! A menu of options is limited.

The meaning of all these arrangements is thus internationally standardised.
All petroleum legal regimes have much in common: ‘common core’

Methods of awarding E&P rights:
- Negotiations or Bidding (Competitive and Discretionary)

Exploration phase:
- Division onto sub-phases
- IOC’s submission of plans/programmes for state approval (minimum expenditure, work obligations)
- Relinquishment provisions (mandatory and voluntary)
- Ring-fencing
Other examples of ‘common core’:

- **Development and Production:**
  - Dev–t/Prod–n plans, programmes, budgets for state approvals

- **Payments:**
  - Area rentals
  - Signature or information bonuses
  - Royalties (fixed or sliding scale; in cash or in kind)
  - Production bonuses

- **General standards of performance:**
  - Good Oil Field Practices (GOP) or Practices recognised in International Petroleum Industry
  - Prudent and Workmanlike Manner
National regulatory frameworks are thus much standardised (80% of content is standard (?)) – **why?**

- States borrow ideas from one another

- Industry is global and IOCs carry their experiences/cts/commercial practices with them

- States adopt recommendations of int’l organisations (eg, World Bank)

- Much knowledge/expertise disseminated by int’l law firms, private consultancy, int’l organisations, increasingly global legal academia and education
What does the internationalisation of nat’l regulatory regimes mean for the debate on *lex petrolea*?

- **Legal thinking/language/concepts** standardised even if a c–t is subject to domestic law

- Common frames of references are created for states, making each other’s experiences relevant to one another

- Possibility of one **jurisdiction’s experience influencing another** (dispute resolution or legislative reform)
Stand–n of nat’l regulatory regimes can generate common standards, which will influence everyone (including IOCs) and everything (including industry standards) w/in the industry.

This creates harmonisation and convergence in governance; harmonisation is not too far from universality on which the ideas of *lex mercatoria/ petrolea* are based.

BUT, ultimately, law and regulation are about specific rules and terms – these are not universal and will be specific to a particular state/its granting instrument.
Since 1950s, the industry has been producing model/standard c–ts (SCs)

Examples of SC producing bodies:

- Association of International Petroleum Negotiators (AIPN)
- American Association of Petroleum Landmen (AAPL)
- Canadian Association of Petroleum Landmen (CAPL)

Extensive use of SCs: stand–n in governance of the sector
Benefits of standardisation of c–t terms

- Increased speed of negotiations/drafting

- Saving time and reducing transactions costs, maximising efficiency

- Increased consistency in understanding of terms and standards = fewer disputes

- Better quality of c–ts

- Better commercial relationships (?)
Do SCs create a transn’l petroleum order?

- Extensive use of SCs: an autonomous legal order, a form of industry self-regulation that is alternative to the state-made law (?)

- In a cross-border context, extensive self-regulation creates a form of transn’l law (?)

  ◦ SCs provide a ‘framework...of routine and custom, that establishes a social context in which the parties can understand their business relation and their mutual expectations’
  ◦ by providing detailed regulation, SCs function as ‘a system of default rules, like the implied terms of the common law and the supplementary laws of codified legal systems’
Caution needed:

- SC = a starting point in drafting a c–t

- Associations such as AIPN do attempt to ensure that SCs reflect the existing industry practices

- BUT ultimately they reflect the views and experience of the representatives of those sectors and parts of the industry who draft them SCs.

- Not every SC necessarily contains an industry practice
Do SCs create a transn’l petroleum order? (cont)

- Which provision reflects a global std/practice/benchmark?
  - No systematic and detailed study carried out

- Without such data, can it be definitively claimed that SCs are sources of much of the transn’l petroleum law?

- SC and practices constantly evolve

- BUT, with time, a wide usage of SC can generate a wider industry practice, standard or usage
Still, an extensive usage of SCs in practice produced much harmonisation:

- CA of New Zealand in respect of the 1995 AIPN Model Joint Operating Agreement (JOA): this model c–t is ‘widely used as a starting point for such contracts’ Todd Pohokura Ltd v Shell Exploration NZ Ltd; OMV New Zealand Ltd [2015] NZCA 71, para. [9]

- In some cases, a prominent standing of a SC w/in the industry and its ability to reflect an int’l industry practice/standard can be asserted w/ confidence.
ICC Case No 11663, 2003, Final Award:

- A provision, based on the AIPN model JOA, whereby a 
cp, failing to make its financial contribution in 
response to a cash call w/in 60 days, is required to 
forfeit and assign its participating interest to a non-
defaulting CP upon the receipt from the latter of a 
default notice.

- The tribunal appears to have treated this provision as 
‘standard practice in the oil and gas industry’.
SCs: concluding observations

- Just like HG c-ts, SCs have harmonised governance of commercial (horizontal) transactions:
  - The same ways for conceptualising commercial arrangements
  - Common structures, similar legal language and concepts, all used and understood worldwide
  - Stand–d solutions to common problems

- A number of SCs/or some of their provisions reflect/evidence industry st–ds:
  - BUT which ones exactly? A systematic investigation is required
  - The power of SC to evidence an industry practice/st–d must always be verified
Push towards the creation, use and promotion of various technical industry (and also non-industry) standards

International Association of Oil & Gas Producers (OGP):

‘Standards are like DNA. They are the basic building blocks for all technology and economic systems’
An industry st-d: the definition

- ‘a benchmark or a level of quality or attainment with reference to which something is evaluated or the compliance with which is desirable or expected’

- often created by non-state bodies, organisations or associations: usually voluntary and have been described as ‘pieces of general advice offered to large numbers of potential adopters’

- The ISO definition: ‘a document that provides requirements, specifications, guidelines or characteristics that can be used consistently to ensure that materials, products, processes and services are fit for their purpose’
Benefits of standardisation

• Improved quality of goods, services, processes
• Compatibility and efficiency
• Reduction in cost and time
• Better environmental protection and people health/safety
• Sharing and dissemination of knowledge
• Technology transfer to developing countries
• Help in capacity building
• Reduced government regulations
Several thousands st–ds in the O&G industry today

Many standards developing bodies, eg:

- American Petroleum Institute (API) (O&G industry)
- Energy Institute (EI) (O&G industry)
- International Organisation for Standardization (ISO) (for many industries, including oil and gas)
- International Maritime Organization (the UN’s specialised agency: maritime safety and preventing pollutions from ships)
- International Electrotechnical Commission (IEC) (non-governmental; electrical, electronic and related technologies)
What do these ‘int’l standards’ deal with?

An extremely selective list of examples:

- Equipment and materials
- Planning, design, construction, installation, operation and maintenance of equipment, facilities, offshore platforms, cranes
- Petroleum measurement
- Health & safety
- Environmental protection
- Professional conduct and certifications
Which standards are ‘global’?

- Only widespread recognition of a standard can make it a source of transnational petroleum law.

- Possibly: API Spec 6A Wellhead and Christmas Tree Equipment (a similar ISO 10423), or IMO’s Code for the construction and equipment of mobile offshore drilling units.

- Many challenges to overcome before this question can be answered:
  - What criteria are to determine a truly ‘global’ standard?
    - Arguably, universality cannot be required.
Other challenges arise from multiplicity of st–ds and st–d setting bodies:

- What if there are several incompatible st–ds?

- Should the highest or lowest st–d be selected (the latter so far recommended)?


i. Do the different designations reflect their ranking in terms of significance, levels of recognition?

ii. Should they lead to different legal consequences?

iii. What legal order/source provides basis/framework for answering these questions (i and ii)?
• Research needed into a ‘methodology’ for dealing w/the proliferation of industry st–ds

• In the absence of ‘methodology’: meaningful answers to be found w/in the contract law framework

• See, eg, the UNIDROIT Principles of International Commercial Contracts (UPICC) (Art 4.3):
  – if a st–d amounts to a ‘usage’, it is binding on CPs
  – if not, it is a ‘factor’ to be taken into account in interpreting the c–t
If a st-d is not a ‘usage’, it cannot be binding on CPs

It is ‘soft law’ at most; BUT still influential as part of a commercial background against which c-ts/legislation are to be interpreted

However, ‘soft law’ can turn into ‘hard law’ (!):

- HG Petroleum regimes (laws/regulations/c-ts/licences) not infrequently incorporate industry st-ds
- Generic clauses to be interpreted w/ reference to industry st-ds: ‘good oilfield practices’ (GOP), ‘performance in a prudent or workmanlike manner’
Nearly universal use of these clauses
Arguably, an international standard in itself
Legal framework for upstream operations, is dependent and premised on the existence of such clauses (!)
Industry players recognise their existence

But still mysterious and uncertain
How to ascertain its meaning in precise circumstances?
- HG legal framework
- SCs
- Industry standards
- Int’l arbitration and domestic body of cases
A JV between a state organisation and IOC
IOC effectively acting as the operator (OP)
State party: OP failed to act as ‘prudent’ OP in making exploratory drillings; operations incompetent and negligent

Tribunal:
- proceeding w/ the gas flow test ‘without the use of a packer’ and w/out calculating the salt pressure in complex and dangerous wells – an imprudent action
- the use of lost circulation materials (LCMs) – ‘prudent under the prevailing circumstances where [OP] experienced lost circulation.'
Another potential source of *lex petrolea*

Sources that can potentially evidence an industry usage:

- HG framework and the experience/case law of a domestic jurisdiction
- SCs
- Industry standards
- Findings as to GOPs and the like
Art 1.9(2) UPICC (UPICC claim to be part of *lex mercatoria*):

A usage is one ‘that is widely known to and regularly observed in international trade by parties in the particular trade concerned except where the application of such a usage would be unreasonable’

Difficulties: how ‘widely known’? what is meant by ‘regularly observed’?
Usages and customs: the reality

- Little evidence that they have been used actively, at least at the dispute resolution stage

- May still be important in governing operations, c–t negotiations, day–to–day commercial dealings

- US case law – confined to the domestic industry context?
Lex petrolea and state-made law: The relationship

- No need to counterpose the two
- Complex synergy
- State-made law exerts influence on lex petrolea and vice versa:
  - SCs revised in the light of case law and experience in various states of dealing with SCs
  - Experience of state regimes can itself generate global standards, producing ‘transnational law’
  - State regimes rely extensively on industry standards and generic clauses (GOP), impliedly incorporating industry standards
  - State regimes are often dependent and premised on the existence of industry standards
  - State legislative practice/drafting looks at the industry experience
O&G industry: Entirely self-regulated?

- NO

- The basic regulatory framework is set by the state-made regulatory regimes

- ALL other commercial arrangements must be compliant w/ the state regulatory regime

- BUT much of governance/regulation is carried out via industry sources
A great deal of harmonisation/convergence, but caution required

No more than ‘transnational layers of governance’ have emerged

- *Lex petrolea* = NOT a mature legal order, workable in practice:
  - No reasonable degree of order, clarity and certainty regarding its sources and relationship between them
  - Not self-sufficient: non-state sources part of a larger legal framework
  - No methodology of dealing w/ non-state made sources
Further research:

- Which SCs/provisions reflect industry standards?

- Methodology for determining and ‘ranking’ the legal significance and consequences of constantly proliferating industry st–ds

- A systematic effort into injecting meaning into GOPs and the like

- The role and meaning of usages/customs
Need for major international initiatives: conventions, global industry codes?

- No need for inter-state international efforts

- O&G – a politically sensitive sector. States want to preserve ‘sovereign’ control over/ways of running it

- An even greater industry co-operation into developing answers to Qs, such as those posed here would help produce commercial and legal certainty

- The constantly proliferating standards may over time converge and lead to global industry codes
Thank you