CITO

ENERGY GROUP

Going International

A Guide to International Expansion for Canadian Energy Companies

CITO.ENERGY

Anthony Cioni

Pat Cunningham+

Nick Bryanskiy

Heather Lilles

Tony Vacca++

Renee Matthews

+ a geologist providing commercial, not legal, advice to CITO Energy Group clients via CITO Acumen Inc.

++ a tax lawyer working in association with CITO Energy Law LLP

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1. Introduction – A Framework for International Practice

The aim of this paper is to provide a guideline for the identification, assessment, and mitigation of high-level risks in international petroleum transactions. In recent years, the Canadian oil and gas industry, including upstream oil and gas explorationists, oil and gas service providers and midstream and downstream entities, has recognized the need to diversify away from the predominant Canadian market to ameliorate the risk of a region-specific slowdown. Yet venturing into an international commercial arena can expose new participants to significantly greater risks in addition to the usual spectrum of risk faced in their domestic projects.

This paper is not intended to be a scholarly undertaking or comprehensive review of international petroleum transactions, but rather we hope to assist the international petroleum venturer to identify, assess and mitigate international risks. In doing so, we have considered the upstream, midstream and downstream sectors, as well as the petroleum service sector.

International petroleum transactions are predominantly commercial animals – far more so than any other area of practice we have encountered. There is wide variance in the type of risks and risk mitigants present from country to country; even within a given region.

Relying solely on legal techniques that have been developed and refined to reduce and mitigate risks in common law jurisdictions can be a narrow, and sometimes even a naïve approach, to deal-making in non-rule-of-law countries. In jurisdictions where the arbitrary exercise of power is common and generally accepted principles of the rule of law are circumvented or are absent altogether, the leading risks are most often financial, technical, and operational. Legal risk mitigation techniques so vital and heavily negotiated in common law jurisdictions can quickly lose their strategic and practical value outside the rule of law. For example, the legal niceties of an indemnity in a Chinese joint venture contract are irrelevant compared to the credit risk of payment under that indemnity. If there is no mitigation of the credit risk, not even the most carefully drafted and reasoned indemnity clause will effectively mitigate the financial risk.

This situation is further compounded by the effect of cultural nuances in international transactions. In Western culture, a signed contract represents the culmination of a successful negotiation. In many other cultures, the execution of an agreement is merely the creation of a commercial relationship – starting with the negotiation process and evolving over time. In non-rule-of-law countries, these types of cultural imperatives are logical consequences of the unreliability of legal protection. Without prospective, stable, and certain laws, applied equally and consistently to both State and individual entities, there is no rule of law. Without the re-

liable certainty that contracts will be legally enforced, either by the State, the courts, or some other quasi-judicial body, those laws have little value, or even present risk by dint of selective enforcement against foreign investors.

It is critical to remember these factors when advising on international transactions. Many Canadian lawyers too narrowly define their task by only considering legal risks and mitigants of a project or transaction, while impractically leaving the rest to the client to assess and manage. Canadian lawyers are acculturated by the sanctity of contract and trained to practice in the 'lawyer box'. While understandable, this approach is not practical or helpful. In our view, thinking outside of the 'lawyer box' is simply part of the job of competent international counsel.

How does a lawyer think outside of that box? A few techniques are useful:

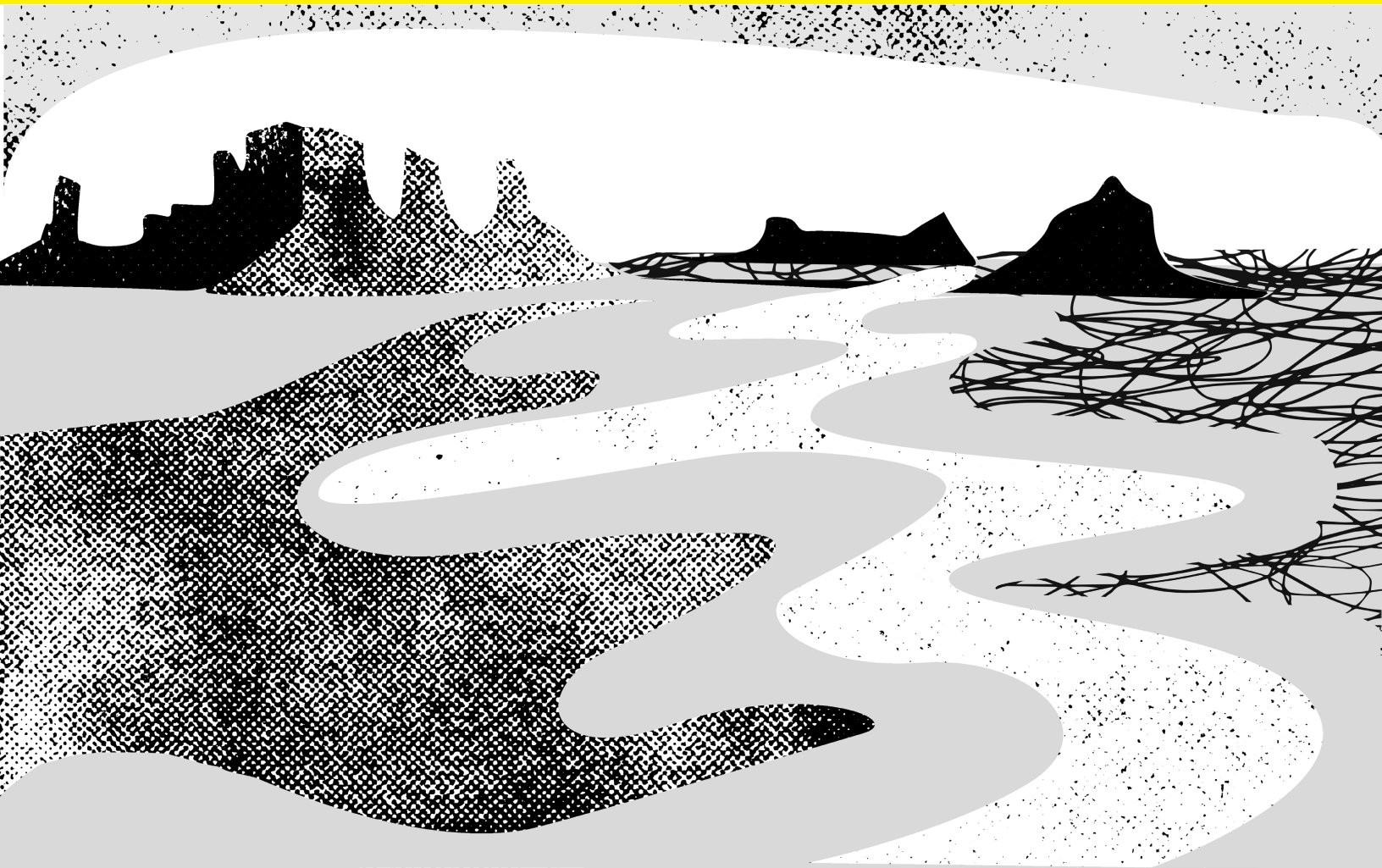
- Lawyers should help their clients engage in strenuous risk-reward diligence for all known risk factors relating to the deal or the project, not just legal risks. This does not mean that a lawyer needs to be expert on non-legal matters. Practical benefits can arise from simply identifying the issue or mitigant to be considered by the client's expert. Clients will not necessarily identify those risks or mitigants on their own.
- Ideally, this risk-reward diligence should occur before the commencement of negotiations or project development. While managing the cultural nuances inherent in effectively communicating with a foreign counterpart is challenging in its own right, changing tack mid-negotiation to address an overlooked risk item may not be practically possible.
- Problem solving should always focus on practical outcomes. Per the example above, a lengthy research memorandum on the enforceability of an indemnity in a Chinese joint venture contract will not likely assist the client. As a value for service proposition, it is unlikely to assist your professional reputation either. Consider instead which commercial structures are available to mitigate the risk. In our example, the indemnitor could issue additional security or suffer financial set-off or the loss of key contractual rights where the indemnity has not been paid.
- In many jurisdictions, it would be prudent to begin with a number of presumptions that would not typically apply where rule of law is valued and respected. For example, it may be judicious to start negotiations fully cognisant that the terms of the contract may be ignored, or perhaps not even reviewed and considered, by the counterparty. Along similar lines, if the execution of a contract in some countries is customarily seen as the start of a much longer, negotiated commercial relationship, then your client should be prepared for some erosion of its benefits. The risk/reward diligence process should help you determine

which erosion points are likely to arise. Think of a contract as a stack of poker chips to be played over a long series of poker games. Your aim is to create the highest stack of chips possible to ensure the maintenance of your client's extra-contractual leverage.

- It is vital to retain the right local counsel. At a very minimum, local counsel must be competent to assess both legal and commercial risks in-country also while being trustworthy. Just because local counsel works at a large, international firm in-country does not necessarily mean that these basic attributes are met. More optimally, identify local counsel who are known for remaining unintimidated in the face of State pressure. This requires a degree of courage and professional integrity that many Canadian lawyers can scarcely appreciate, and it is a privilege to work with these advocates. Ideally, local counsel will also have sufficient social standing and professional reputation in-country to effectively dissuade counter parties from deviating from the contract.

Part 2

Assessing Country Risk



2. Assessing Country Risk

2.1. The Country-Specific Risk/Reward Analysis

As mentioned, at the heart of every successful international petroleum transaction is a strenuous due diligence review - a risk/reward analysis to identify those issues of material significance to the success of the potential transaction before the commencement of negotiations. Most, if not all, of the factors listed below will be considered in each case, but in every transaction the degree to which each factor will impact the risk/reward analysis will change and potentially continue to change as the transaction matures. Further, each factor should not be considered in isolation; the risks and mitigants often overlap and are cross-correlated. The transactional risk/reward profile must also be integrated with the client's own tolerance for risk, factual peculiarities, and specific instructions. A negotiation strategy can then be developed with the client, as the risk/reward profile is translated into the deal itself; be that by contractual negotiation, regulatory strategy, or corporate organization.

2.2. Taxation

Taxation is a critical consideration in evaluating the viability and profitability of any proposed international transactions.

At its most basic, any international transaction should be structured with a view to minimizing overall tax burden, and, by extension, maximizing after tax income.

This will include, but not be limited to, structuring the transaction so as to minimize the prospect for 'double taxation'. Double taxation occurs, in general terms, when two or more States (typically, the State in which the income is earned, often referred to as the "source" State and the State in which the taxpayer is resident) impose taxes on the same income, where, in general terms, the State of residence does not credit, or sufficiently credit, taxes borne by the taxpayer in the source State, against taxes imposed by the residence State.

International transactions should also be structured with a view to minimizing tax filing and compliance burdens, which can add considerably to the cost of any such transactions, and to ensuring that any tax filing obligations that do apply, are identified in advance, and complied with, so as to minimize the prospect of costly penalties that can be assessed, where compliance with such tax filing obligations are overlooked.

Taxes to be considered, assessed, and evaluated, in international transactions, typically can include:

- income tax, at the entity (i.e. corporate) level,
- personal income taxes, in respect of any employees who may be exercising their employment in a foreign jurisdiction, or who may be rendering services in such jurisdiction, as an independent contractor,
- withholding tax, i.e., taxes imposed at source on certain 'passive' forms of income such as interest, rents, royalties and/or dividends realized from a sources within the foreign State, where a third party is tasked with withholding the tax from payments made or to be made by It, to a recipient who is a non-resident of the source State, and
- value added and/or sales taxes, applicable typically, on provision and/or procurement of certain services and/or supplies, in the foreign State.

To minimize the prospect for 'double taxation', and in order to provide a certain set of standardized rules pursuant to which a participant in an international transaction may be made taxable in a foreign State, countries around the world have entered into a broad network of bilateral income tax conventions, based broadly on the OECD Model Tax Convention on Income and on Capital. Canada has entered into 93 such bilateral income tax conventions, with an additional three having been signed, but which have yet to enter into force.

In order for a taxpayer to avail oneself of benefits under a tax treaty, a taxpayer must be resident of a contracting State, as that term is defined in the particular convention, and also must not otherwise be denied benefits, either by virtue of various treaty benefit denial provisions, or by country specific anti-avoidance provisions. Where a taxpayer qualifies for benefits under a treaty, such taxpayer will typically be entitled to avail themselves of, amongst other, reduced rates of withholding tax as provided for under treaty. Withholding taxes are found in practically all tax systems and are, as previously mentioned, typically imposed on dividends, interest, rents and royalties realized from sources within the source State, by a non-resident of that source State.

Since 2018, 93 jurisdictions have ratified a Multilateral Instrument (**MLI**) supporting the implementation of a series of tax treaty measures to update international tax rules and lessen the opportunity for tax avoidance or 'jurisdiction shopping' techniques historically applied by tax planners in Canada and abroad. Although the MLI entered into force in Canada at the end of 2019, Canada's tax treaty partners must also adopt the MLI provisions before the MLI will apply to a particular tax treaty between Canada and any such partners.

Given the complexities involved, the advice of tax experts is frequently sought to

optimize a client's operations in-country. This analysis will include not only local tax advice, but also Canadian tax advice, to ensure that your client's structure works 'from the top down, and the bottom up', as many tax experts describe it.

2.3. Bilateral and Multilateral Investment Treaties

There is also a global network of bilateral and multilateral investment treaties designed to protect foreign investors from a variety of wrongs that a foreign State might commit vis-à-vis foreign investment; the most significant of which include economic discrimination, expropriation, and nationalization. These treaties also often include protection for what is often called 'small e' expropriation, or instances where a State slowly removes the benefit of a foreign investment over time; the cumulative effect of which equates to a more formal nationalization or expropriation. In our experience, bilateral investment treaties have often proven to be of more practical value than many multilateral treaties, like the USMCA (previously NAFTA) or the *Energy Charter Treaty*. Although the Energy Charter Treaty is frequently invoked in the international petroleum sector, its provisions have been interpreted and applied inconsistently by arbitral tribunals and domestic courts, lessening its value as a potential tool of risk mitigation. A recent initiative has begun to modernise and reform the Energy Charter Treaty, although proposals are still in the preliminary stage.

These treaties can be powerful tools for tempering a counter party's bare economic interest by bringing into play the international standing of such party's home Government as a reputational wedge to be used from a foreign affairs perspective. Unfortunately, we have observed that many foreign Governments are not overly concerned about their popularity with the Canadian Government (and really, who can blame them?).

As is the case with double taxation avoidance treaties, not all countries have entered into bilateral investment treaties with Canada (again, Chad for example). In the absence of such treaties, a similar strategy can be adopted to assist a client to secure the benefits of a bilateral investment treaty. Specifically, bilateral investment protection which might not otherwise be available, may be procured by routing an international entity's corporate structure through a third country with common treaty links to Canada and the host country (again, in Chad's case, a country like France or Switzerland). However, as an illustration of how international risk mitigation techniques can sometimes operate at cross purposes, so-called 'tax haven countries' that have historically provided tax optimization do not often have bilateral investment treaties with other international jurisdictions. This may lead to a conundrum where tax optimization and favourable foreign investment protection may need to be weighed against each other to determine which offers the greater benefit in a particular situation.

At the risk of repetition, any tax/investment structure planning must be undertaken in advance of effecting an investment transaction with a foreign State, or the international venturer risks being denied the protections offered by bilateral or multilateral investment treaties.

2.4. Corruption Risk

Corruption continues to be an unfortunate reality which must be addressed when advising businesses engaged in international petroleum transactions. In our view, one of the most difficult tasks facing international counsel is effectively combatting corruption risks which can challenge international venturers in unanticipated ways and with varying severity of consequence.

By analogy, corruption is like the Hydra of ancient Greek lore – when Hercules cut one head off, two more grew in its place. Counsel for international venturers must be wary of each independent 'head' – the first, which is an external risk, and the second, which is internal to a client's operations management.

Corruption issues can be particularly challenging because: (a) the reputational risks of corruption often far outweigh the legal risks; and (b) the Canadian laws prohibiting corruptive practices use Canadian companies as tools to redress the cultural norms of other nations, including the use of bribery. For many international entities, the 'front page of the newspaper test' is as much of a concern as technically complying with Canada's extra-territorial corruption laws. While true, bribery is still prohibited by law.

Bribery is also commercially unwise. In practice, a company that is 'known to pay' simply attracts the corruptive attention of more officials looking for an ever-escalating 'contribution'. We have observed cases where corruption was in issue, but: (a) the payor never actually received a benefit from its payment; and/or (b) the benefit procured for the payor was later questioned in-country as 'corruptively won' with a great loss of asset value to the payor, or even the transfer of that asset to local interests.

As P.T. Barnum said, 'a sucker is born every minute'. As Forest Gump said, 'stupid is as stupid does'. Both are practical monikers to describe the commercial and practical realities of international practice.

Turning to the legal requirements, the apposite rules for Canadians are found within the federal Corruption of Foreign Public Officials Act (Canada) (**CFPOA**), which prohibits the giving or offering of a benefit to a foreign public official for the purpose of obtaining or retaining an advantage in the course of business. The

statute very broadly defines the terms 'benefit' and 'public officials', with only a narrow exception for reasonable costs associated with demonstrating goods. The CFPOA mirrors legislation in many other countries, all standardized under auspices of the OECD treaty. Further, most national anti-corruption legislation, such as the US *Foreign Corrupt Practices Act* (**FCPA**) and the UK *Bribery Act*, have a broad reach, extending their application beyond solely the US or UK (as the case may be) - based companies or individuals. For example, the FCPA will apply to Canadian companies trading securities in the US and any company "carrying on business, or part of a business". In the UK, a Canadian company could be subject to the Bribery Act's corporate offence of failing to prevent bribery, regardless of where in the world the bribery took place. As an illustration, a Canadian company carrying on business in the UK could be criminally liable under the Bribery Act for failing to prevent bribery taking place on its behalf in China.

While the three Acts are similar in many ways, there are some instances where behaviour may be permitted under one Act, but prohibited under one or both of the others. For example, the Canadian and US Acts apply to "foreign officials" or persons acting on behalf of a Government, department or agency. The FCPA also extends to political parties, party officials and candidates. The Bribery Act extends further still, covering bribes to public officials and private individuals in certain situations.

The US Department of Justice and the UK Serious Fraud Office have historically both been much more aggressive with prosecutions than the RCMP in Canada. However, Canada has seen some increase in anticorruption enforcement since the symbolic case of Niko Resources Ltd. - one of the first major CFPOA prosecutions, albeit arising from a self-reported case. Niko Resources Ltd. was a publicly traded corporation that conducted international business operations through wholly owned subsidiaries. In 2011, Niko pleaded guilty to offenses under the CFPOA for directly and indirectly provding improper benefits to a foreign public official in Bangladesh in order to further its business objectives. More recently, there has been evidence of a potential shift towards increased Canadian vigilance over foreign corruption in a civil context. Provincial securities regulators have appeared willing to investigate and prosecute alleged instances of foreign corruption - as in the case of Katanga Mining Ltd. Finally, it is still too soon to know whether Canada will see a surge of anticorruption enforcement in a (not unhypocritical) attempt to redeem Canada's heavily tarnished reputation in the wake of the recent SNC- Lavalin affair.

Rounding out this discussion on corruption and its potential impact on international venturers, we note that almost all host States have local laws (usually criminal laws) prohibiting bribery. These laws can be subject to selective application and enforcement against foreign commercial actors, exposing a client to further political and corruptive risks. While time in a Canadian prison is undesirable, time in a pris-

on in Latin America, the Middle East, or Africa is a much more frightening prospect.

2.5. Sanctions and Export/Import Controls

Any Canadian company considering international transactions should confirm whether its target markets are directly or indirectly subject to Canadian and United States sanctions or export/import restrictions. If sanctions apply, it will be necessary to complete due diligence on all parties involved and the transaction as a whole. In addition, there are a number of mitigation strategies that help clients understand, control and manage sanctions risks. These strategies include: the procurement of a legal opinion on specific sanctions matters, the provision of an end use certificate, strong contractual covenants on sanctions reporting, sufficient D&O liability insurance, corporate sanctions compliance policies, regular compliance policy training, and internal compliance audits and self-disclosure (if required).

The federal Government adopts country-specific Regulations under the Special Export Measures Act, as well as the United Nations Act and Justice for Victim of Corrupt Foreign Officials Act. At this time, Canadian sanctions are imposed on the Central African Republic, Democratic Republic of Congo, Eritrea, Iran, Iraq, Lebanon, Libya, Mali, Myanmar, Nicaragua, North Korea, Russia/Ukraine, Somalia, Sudan and South Sudan, Syria, Venezuela, Yemen, and Zimbabwe. Canada may also freeze assets and restrict the use of property under the Freezing Assets of Corrupt Foreign Officials Act. Canada controls international trade under the Export and Import Permits Act. For instance, any export or transfer of specific goods or technology to countries included in the Area Control List (e.g. Democratic Republic of Congo) must be authorized by an export permit issued pursuant to the Export and Import Permits Act.

In the United States, sanctions are adopted by the Federal Government under different categories of powers and issued through a variety of instruments, including Presidential Executive Orders and specific legislative acts or consolidations. The US list of blocked entities and individuals is consolidated by the Office of Foreign Assets Control in the format of the Specially Designated Nationals List, also known as the SDN List. By comparison, the Canadian sanctions lists are included as part of the individual regulations and there is no single, national database.

Most sanctions in Canada and the United States are imposed with no notice to ensure that blocked entities have no opportunity to evade or circumvent these restrictive measures. In the US, the regulator offers detailed answers to Frequently Asked Questions on most sanctions-related matters, whereas no such guidance exists in Canada or it is limited and provides little practical value. Similarly, the large body of sanctions enforcement case law in the United States permits a better understanding of the regulator's interpretation of specific issues and law enforcement posi-

tions. In Canada, there has been limited historical sanctions enforcement, and it is difficult to confirm the regulator's enforcement stance.

There are three steps to sanctions risk identification and mitigation. The first step is to understand what sanctions are, who they apply to, and how they work in practical terms. By their nature, sanctions are political instruments designed to influence the behavior of foreign States or State-owned entities. They are different from trade measures, which are involved in the so-called "trade wars", most recently those arising between China and the United States. Sanctions may endure from just a few months (e.g. recent US sanctions imposed on Turkey) to many decades with no end in sight (e.g. US trade embargo imposed on Cuba in the early 1960s and on Iran in the 1980s).

As legal and regulatory instruments, sanctions may result in both civil and criminal liability against corporations or individuals. In addition to significant fines and trade restrictions on corporate entities, individuals (e.g. both directors and officers of Canadian and US companies, and of their subsidiaries and affiliates) may face prison terms and fines, be prohibited from visiting Canada or the US and asset seizures. Therefore, directors and officers may also be exposed to sanctions. Their personal exposure should be carefully considered and mitigated. The mitigants may include: D&O sanctions-specific insurance coverage, indemnities, sanctions policies, and training. Most US nationals will likely be concerned about their ability to travel and work in the US; often the largest market for Canadian companies.

In practical terms, absent sanctions investigations or prosecutions, payments into and out of sanctioned jurisdictions are at risk of being frozen or significantly delayed due to screening by Canadian and international financial institutions. It is not uncommon for those institutions to request: lengthy questionnaires, details on end use clients, transaction information and/or the submission of invoices and other documentation in order to demonstrate compliance.

There may also be specific reporting and disclosure obligations on Canadians with respect to blocked individuals and entities and their property in and outside Canada. These reporting and disclosure obligations should be taken seriously. Canadian banks and financial institutions can be difficult to administratively manage on these issues because they may prefer the loss of a single client to facing sanctions questions from the US regulators. The overall risk tolerance of Canadian financial institutions is low when transacting with sanctioned countries and blocked persons.

As a general rule, the Government may enforce its sanctions rules if an offence is committed by its nationals or within its territory (i.e. a "nexus" is required for the Government to exercise its jurisdiction). However, the US Government often exercises its jurisdiction extra-territorially. By means of so-called 'secondary sanctions',

a Canadian company may be subject to US sanctions with respect to a transaction with non-US entities outside of North America.

Canadian companies are best to presume that both Canadian and US sanctions apply because most Canadian banks are registered issuers in the US and will be subject to US sanctions by default. If a client has significant commercial exposure in the US market, it is prudent to consider US sanctions, whether they technically apply or not.

US and Canadian sanctions are usually aligned, but important differences may still exist and need to be identified on a case-by-case basis. For instance, Cuba is not subject to any sanctions by Canada, but it is under a strictly enforced trade embargo by the US Similarly, Canada has lifted most of its sanctions on Iran, whereas the US reintroduced them with respect to over 16,000 entities and individuals in 2018, with restrictions continuing to escalate. US regulators are experienced when it comes to Iran and Cuba, and it is unwise to underestimate their knowledge of sanctioned persons, corporate entities, and transactions.

The US Government routinely carries on hundreds of investigations and prosecutions resulting in multi-million-dollar fines, asset freezes, and lengthy jail terms. By comparison, only one reported sanctions case has reached Canadian courts. Lee Specialties was found guilty of the sale of prohibited goods to Iran and agreed to pay a settlement in the range of $100,000; an unthinkably small sum in the US.

As a second step, it is important to clearly understand what is prohibited and what is permitted under the applicable sanctions' regime at any given time. In most cases, sanctions target specific entities or sectors, and business transactions are still allowed outside of these restrictions. Specific exemptions may be legislated or available upon request (e.g. for humanitarian purposes or to enable a Canadian or US company to transition out of the sanctioned jurisdiction). Grandfathering mechanisms may allow projects and transactions that were initiated before sanctions came into effect to continue without penalty or restriction. Put simply, what applies to one country does not necessarily apply to another jurisdiction. Sanctions may also shift in terms of scope, prohibited persons, and they may be relaxed, lifted, or tightened up in a fairly short period of time.

The scope of sanctions varies depending on the purposes pursued by the Government. They may involve a list of prohibited entities and individuals, which are "untouchable". Sanctions may be designed to prohibit short or long-term financing provided to a listed entity, including contractual financing. For example, an overdue account receivable from a listed entity may be considered a prohibited loan to a listed person. Sanctions could also target an entire sector of the economy – as is the case with the oil and gas sectors of Iran and Russia. In Iran, the US sanctions

target both the development of oil resources and oil exports from Iran. In Russia, the US and Canadian sanctions focus on a list of equipment used in Arctic, offshore, and shale projects.

The third step is to manage and mitigate sanctions restrictions in order to ensure compliance. Any sanctions process should start with comprehensive due diligence on all persons involved and the transaction or project as a whole. Diligence includes the investigation of foreign entities and individuals linked to the transactions to confirm they are not under sanction. Close attention should be paid to all Stated-owned or Government-related persons, together with any agents involved in the proposed transaction. Diligence may also involve the preparation of legal opinions and further disclosure requests to evidence management's full consideration of the issue.

Once due diligence is complete, contracts in the sanctioned jurisdiction should include strong sanctions language, permitting a client to: (a) back out of the contract in case of sanctions, whether based on force majeure or otherwise, and (b) put local agents and partners on strict notice and hold them accountable for compliance.

In certain cases, an end-use certificate from the foreign counterparty may be helpful to establish that the goods and services will not be used for any prohibited purposes. Canadian companies must exercise reasonable due diligence and review/research the entities and projects involved to ensure that they do not fall under any of the prohibited categories. A legal opinion on the proposed transaction may be similarly helpful in these circumstances. It is also a good idea to develop a sanctions-specific policy and conduct regular training for your staff and partners both in Canada and overseas. All these measures will likely be considered mitigating circumstances by the Government in case of any investigation or prosecution by the Canadian or US authorities.

A well-developed and maintained sanctions file evidencing these mitigation measures, will also assist in deals with financial institutions and any Government agencies. The resulting paper trail makes a significant difference in these circumstances and can help reduce or eliminate sanctions liability (e.g. reduce any fines, protect corporate board and management, help maintain key Government licences and approvals, bank accounts, insurance coverage, and other important commercial attributes in place).

2.6. AML Risk

Thirteen agencies in Canada oversee Federal anti-money laundering and anti-terrorist finance initiatives carried out under international treaty. These agencies, which include the RCMP and CSIS, work under the auspices of the Proceeds of

Crime (Money Laundering) and Terrorist Financing Act and the Criminal Code to limit the access of criminal and terrorist elements to the Canadian economy. As with sanctions, regulatory oversight is supplemented by reporting and disclosure obligations placed on Canadian financial institutions and professions; including the legal profession.

2.7. Law of the Sea

Since the United States and Russia encountered industrial oil flows in the Gulf of Mexico and South Caspian Sea in the early-twentieth century, the petroleum industry has pursued offshore oil and gas discoveries - first into 'shallow waters' and then into increasingly deeper water. The definition of 'shallow' versus 'deep' water has been, by necessity, industry driven, rather than being tied to a precise legal definition. 'Deep water' is, in fact, a dynamic concept, which is constantly changing and heavily dependent on local factors such as local technical levels, economic efficiencies, governmental policies, and geographic conditions. Consequently, the concept of 'deepwater' exploration varies across countries and time.

By comparison, international maritime law has historically been more concerned with dichotomizing petroleum ownership into categories based on distance from the coast rather than sea depth. Neither method lends itself to crisp, indisputable results.

In the 21st Century, over half of all major oil and gas discoveries were made in deepwater areas and, from 2012 to 2014, over 70% of the top 10 annual oil and gas discoveries were made in deepwater areas. As the number of major deepwater petroleum discoveries rise, and the petroleum industry explores further into ultra-deepwater, international maritime law will become increasingly applicable to international petroleum transactions.

Under the UN Convention on the Law of the Sea (UNCLOS), coastal States may generally claim a territorial sea of up to 12 nautical miles from shore and an additional continuous zone of the same length seaward of the territorial sea. In principle, where a continental shelf is contiguous to a country's coastline, that country is also afforded an Exclusive Economic Zone (sometimes called an EEZ). UNCLOS permits that country's regulation of economic activities in that EEZ, including fishing, shipping, and oil and gas exploration.

While the delineation of territorial seas and EEZs is relatively straight forward, ownership of seabed minerals and pollution control of mining activities pursuant to the 'continental shelf doctrine', codified to a large extent in UNCLOS, is more contentious. Further, two States with adjacent or opposing coast lines can have overlapping EEZs and continental shelves. Accordingly, coastal States have been known to

disagree over the location of the maritime boundaries, from time to time. We refer to historical disputes between Romania/Ukraine, Vietnam/China, and Guyana/Surinam by way of example. Similarly, the People's Republic of China has made a political policy of challenging the UNCLOS rules with its construction of large air bases on atolls in the South China Sea for the express purposes of expanding its maritime claims to the concern of the Philippines and Vietnam in particular.

Recently, a number of petroleum discoveries have been made beyond an EEZ. For example, this was the case with the 2018 Bay de Nord discovery 270 nautical miles offshore of Newfoundland and Labrador. The Bay de Nord discovery is beyond the outer limit of Canada's EEZ, but there is little dispute that it is within Canada's 'extended continental shelf' rights under UNCLOS. If oil is produced from the discovery in 2025 (as predicted), it will likely be the first petroleum produced beyond 200 nautical miles from shore.

In cases where an offshore 'wellsite' is located beyond a host State's EEZ (whether as part of the host State's continental shelf or not), there is a question as to which (if any) laws of the host State even apply. For health and safety and reasons alone, this is potentially problematic.

For financial reasons, exploration and producing petroleum beyond the EEZ is not ideal either. Article 82 of UNCLOS States that any developments beyond the EEZ require the payment of royalties to the International Seabed Authority, which is then to distribute those royalties to landlocked countries. This authority is based in Jamaica and has little experience or even planned processes for the collection or distribution of royalties. It is an unelected body with no real oversight for collecting and distributing taxes, with no rules.

There is an associated debate at the national level as to whether those royalties should be paid for by the project's operator or by the host State. Restated, is a petroleum company expected to pay both national and international royalties? A few jurisdictions which have issued petroleum exploration rights which have the potential (if a discovery is made) to trigger the host State's obligations under Article 82, have established yet-untested frameworks for Article 82 payments. In both the Norwegian and US regimes, industry will receive credit for the amount of any Article 82 payments as a deduction in the calculation of petroleum taxation or royalties payable to the host State. In Canada, Canada-Newfoundland and Labrador Offshore Petroleum Board has issued notices that production licence holders may be required to pay or contribute to Canada's Article 82 obligations. Not surprisingly, the Federal Government has been coy on its response so far and the matter is far from settled.

2.8. Dispute Resolution

Legions have been written on the subject of 'dispute resolution' in the corporate-commercial realm, but the majority of principles applicable to disputes between or amongst domestic entities in Alberta are unsuitable or even counterproductive in the international sphere. The practical realities of international dispute resolution are often poorly understood by Canadian trained lawyers with a predominantly domestic practice.

For the purposes of this section, 'dispute resolution' is constrained to consider 'adjudicative dispute resolution' where a judge or arbitrator determines the outcome of the dispute. Obviously, the commercial negotiation of a dispute is the first, and usually only, step taken to resolve a problem. As is emphasized in other sections of this paper, 'adjudicative dispute resolution' is often pursued as a last resort by commercial parties faced with a dispute that crosses international borders.

In any event, when one of the parties has reached the point where they feel the intervention of a third party 'adjudicator' is warranted, two basic questions arise: first, do the parties have the freedom to chose whether to arbitrate or litigate their dispute; and second, if litigation is required or warranted, what is the 'proper forum' for litigating the dispute?

In most international petroleum disputes, each party's home jurisdiction and the 'local' jurisdiction will have an interest in the dispute. Note that local courts may have exclusive jurisdiction over legal issues relating to in rem title to assets in-country. For example, if an interest granted by the State under a production sharing contract is classed as an interest in land, as a conflict of laws principle, local courts may not permit the jurisdiction of foreign courts.

Where the parties have the right to choose between jurisdictions, which occurs most of the time, there are some obvious risks to attorning to the jurisdiction of local courts; transparency and corruption being two. Also important is whether an award of the foreign court will be 'recognized' and 'enforced' by Alberta courts.

There are two basic routes by which you can enforce a foreign judgment in Alberta. The most convenient and expeditious method is through application under the Reciprocal Enforcement of Judgements Act (Alberta). Regrettably, there are very few reciprocating jurisdictions to which the Act applies. At present, they are the common law provinces and territories of Canada (and so not Quebec), the Commonwealth of Australia and the bordering States of Washington, Idaho and Montana.

Further, even where you are fortunate enough to obtain a judgment from a reciprocating jurisdiction, like Montana, such a judgment can still be disputed pursuant to

the Act.

A foreign judgment creditor is also always free to rely on the common law route for enforcement articulated in the Supreme Court of Canada's decision in *Morguard Investments Ltd.* v *De Savoye*. However, this involves the possibility of another lengthy court application of which there are no guarantees of success.

On a risked basis:

- if a client is more likely to be sued by a counterparty, then there may be some practical benefit to agreeing to the use of the foreign courts knowing that a plaintiff may face great difficulty enforcing a judgement from its home country in the defendant's country; or
- if a client is more likely to sue a counterparty, then Alberta courts are likely counterproductive and international commercial arbitration will be a better solution.

Next we turn to arbitration. There are actually two types of arbitration – international and domestic. In the international realm, the former is the forum of choice and is protected by the 1958 *UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (the so-called NY Convention). The latter is irrelevant and counterproductive.

Under the NY Convention, the courts of a contracting State must enforce an arbitral award issued in another contracting State where the parties to the dispute have agreed to international commercial arbitration. A failure to do so exposes one contracting State to the complaint of the other contracting State under the treaty itself; meaning that the commercial interests of a powerful actor in a non-rule of law country that refuses to enforce the foreign arbitral award may erode the reputation of that actor's home country on the international stage. This is a powerful counterbalance to 'bad behaviour' and, with 161 contracting States, there is broad global cover.

If a counterparty's assets are mainly located in its home jurisdiction then award enforcement in that home jurisdiction under the NY Convention is probably the most practicable scenario for the foreign claimant to recoup a loss. It is critical to recall that the NY Convention only protects arbitral awards issued outside the home State of the counterparty.

If the seat of the arbitration is inside the home State of the counterparty, then the resultant award will be considered a domestic award governed by local law on domestic awards – without the application of the NY Convention. In fact, many domestic arbitration laws give local courts wide authority to reopen the merits of case.

This includes the *Arbitration Act* (Alberta), which, in our policy view, gives Alberta courts so much discretion that the agreement of the parties to arbitrate is effectively and inappropriately vitiated.

The use of domestic arbitration can allow a foreign counterparty (especially a powerful State-Owned Enterprise) to reopen the matter in local courts or pressure local courts by corruptive or other means to block award enforcement. This sleight of hand is often employed by sophisticated counterparties to avoid responsibility for paying an award. It is a trap to be avoided.

Finally, a word about arbitration directly against foreign Governments. If the counterparty is a host Government, there is another dispute resolution tool to consider. The ICSID Convention is a treaty ratified by 154 contracting States under the auspices of the World Bank. Under Article 6 of the ICSID Convention, rules were drawn up for the arbitration of claims against contracting States. Failure by a contracting State to pay on a losing arbitration award impacts that State's ability to receive IMF or world bank funding; again, a powerful counterbalance to any 'bad behaviour'.

2.9. National Laws

The following table provides a summary of how the national laws of the 'host country' can impact both operations conducted within the host country and the participants involved in conducting those operations. This is not meant to be an exhaustive list, but will give practitioners a guide to risk identification at a national level.

Foreign Investment Laws	Many countries have special laws to protect foreign investment or provide additional benefits/protections to foreign investors To qualify for those benefits, foreign investors must often complete registration or other regulatory requirements These laws may be administered by a Ministry of Finance in parlour with the National Bank to regulate both currency control and repatriation issues
Joint Venture Rules	Governments may prescribe the manner in which a foreign company enters into a joint venture or partnership with a local entity Some countries may require the joint venture to be carried out as a corporate venture (ref. China and Saudi) either contractually or in the form of a jointly held company Other countries may specify the minimum holding of the local partner (ref. Saudi, UAE, Kuwait, Algeria)
Free Trade Zones	Foreign Governments often establish Free Trade Zones in-country to promote manufacturing and trade – both domestic and international The incentives vary: low lease rates for land, VAT exemptions, local ownership exemptions, preferential bid treatment with State Owned Enterprises, etc. These zones often have strict regulatory criteria for qualification. For example, a free trade zone for export manufacturing may not necessarily be used for domestic sales in-country, or to protect a company from specific duties. The requirements may act in concert with foreign investment, currency control, and repatriation laws These free trade zone schemes often have administrative and registration requirements that can create an administrative burden and risk of their own (ref. Kazakhstan)
Transfer Pricing	As is the case in Canada, Governments may prescribe value limits on the transfer of an asset from a foreign affiliate to a local entity The values ascribed to the sale of goods or services between a foreign affiliate and a local company will need to be reviewed from a Canadian and host Government tax perspective

Currency Control	Governments may set the value of local currency in reference to a basket/average of foreign currencies, while trying to control the flight of capital and access to hard currency (ref. Russia, China, Kazakhstan) Transactions that take place inside the host country must usually be in local currency, unless there is a scheme to use hard currency (ref. Colombia) Hard currency transactions may require *prior* registration with the State's National Bank. This might include hard currency payments for the sale of goods/services for export, but also incoming payments for share capital or loan proceeds. Where prior registrations are required, note that there may be delays regarding when the money is actually available for use
Repatriation of Profits	In addition to currency control matters and withholding taxes to non-residents, there may be limits on a company's ability to repatriate its profits to its home jurisdiction by dividend or other distribution Most countries permit repatriation of profits after the payment of dividend tax, but in times of financial instability, those transfers may be prohibited (ref. Russia 1999; Indonesia/Asian Currency Crisis 1999) This risk is strongly correlated to political risk and forex risk
Environmental Laws	It is financially and reputationally important to understand the requirements of environmental laws in host countries In emerging-market countries, the environmental laws are often less stringent than in Canada, but there is still a reputational risk to companies for not following the highest applicable standard, whether required by the host country or not Running afoul of these laws can prevent or stall a project and place a client in a risked political position in-country. It is crucial to fully diligence this before a client enters a country, rather than court the risk of a non-compliance event A breach of environmental laws is highly correlated with governmental, community, and labour relations risk
Patents and IP Protection	The host country may be a party to the *Patent Cooperation Treaty* and other IP protection treaties Aside from treaty status, the client should diligence the host country's historical treatment of respecting and enforcing patent rights (ref. China, India) Consider other ways to commercially manage IP risk *aside from* relying on treaties, recalling the naivety of relying on laws in non-rule-of-law countries. There is a correlation between these risks and Sanctions in relation to sensitive IP relating to weapons, strategic technology and currency controls.

Import – Export Restrictions	Host countries may place restrictions on data that can be exported from the country, including seismic data that is regarded as State-owned (ref. Indonesia) Home jurisdictions of the parties may similarly prohibit the export of certain technologies into certain countries, often for military reasons (eg. LIDAR technology) (ref. Iraq) Restrictions on trade of certain substances or technologies may also be triggered by import/export control under foreign laws, local laws or international treaty. For example, end-use certificates and reporting may be necessary (ref. sale of uranium or other elements used in weapons development or nuclear power)
Lack of Equity – Relieve Against Forfeiture	Most host Governments with civil law systems do not recognize 'equity law' concepts familiar in common law jurisdictions For example, many civil law jurisdictions do not recognize the concept of a trust. This makes strata title, default trustee status, and sole risk operations difficult to enforce under joint operating agreements Civil law systems also tend to have stringent relief against forfeiture laws. In cases where a joint operating agreement requires full forfeiture of a party's interest for financial default, the enforcement of such a remedy in-country may not be possible

2.10. Above-Ground Risks

As emphasized in this article, the 'legal risks' of international petroleum transactions comprise only one of many different types of risk. Legal risks are frequently not even be the most formidable risks to a project or deal. 'Above-ground risks' or 'country risks' (those risks endemic to the particular host-country itself) are risks stemming from host Governments' policies, macro-economic conditions, security factors, labour challenges, political conditions, and even cultural and historical factors.

It is impossible to accurately forecast which events or circumstances will be more important than others in an international petroleum transaction or which risk sources are most likely to occur or carry the most serious challenges. While difficult to forecast, a failure to accurately identify, analyse, and mitigate above-ground or country risks can spell disaster for the project or international endeavour. In other words, above-ground or country risks often have the potential to trigger consequences of the greatest magnitude and effectively mitigating all but one 'country risk' may still be insufficient to ensure project success or longevity.

2.10.1. Political Risk – Governmental and Community Relations

Political instability risk is the hallmark of emerging-market jurisdictions. It can emanate not only from governmental (executive) or legislative actions (such as the State changing laws and regulations), but also from non-governing political parties, special interest groups or unions. Political and social actors can generate political instability from both inside and outside the host country, whether focused on driving change within the host-country itself or arising from inter-State discord and conflict. Like a double-edged sword, international investors will entertain political risks in exchange for a higher rate of return.

In this section we delve into the more salient forms of political risk. The cause of political and/or Government instability can vary widely from: the risk of repeated minority Governments with alternating objectives (ref. Israel); to a Government coup or attempted coup (ref. Gabon); to the complete collapse of a central Government (ref. Libya and possibly Venezuela).

Political instability can also arise from conflicts between two levels of stable Government. For example, governmental authorities in Guangdong Province in China do not always follow the dictate of the Central Government on foreign withholding tax matters. Similarly, the Province of Neuquén in Argentina favours limiting the instability of federal currency controls, so as not to discourage further unconventional oil and gas investment in Neuquén.

The foregoing examples also demonstrate the importance of understanding the difference between governmental relations and community relations. The degree of congruity between Government and community interests will vary widely in each host country. Rarely does a Government effectively represent all their constituents - especially if the country is regionally, culturally, or religiously diverse. However, a significant number of host countries fall at the opposite end of the spectrum; where the governing elite act without regard to the needs and interests of their constituents.

Where certain segments of a population have the intrinsic potential to cause significant disruption within a host country, whether alone or in combination, concerted efforts must be made in the area of political due diligence. Intelligence gathering and acquiring an advanced understanding of relations between community and governmental and the delicate balance between the two is a necessary first step.

Managing these risks will then involve careful planning, and even more careful communication and continued intelligence gathering. In order to execute a sustainable, long-term new country entry, it is helpful to steer a client from away from being overly close with any one faction in a politically divided scenario.

Political risk is not only generated by a host Government's relations with other national actors, but also by the State's view of the benefits of foreign investment to the host country. Political risk also encompasses the issues of contract sanctity, new taxes, expropriation, and nationalization. We have observed over the years that the governmental pendulum swings between courting industry investment in times of low oil prices and 'taking back value' in times of high prices. 'Taking back value' also often occurs after an exploration company makes a major discovery.

One need look no further than the history of Alberta's own provincial policy to demonstrate this tendency, but many other examples remain: China's and Algeria's petroleum windfall tax, Hugo Chavez's antics in Venezuela and the nationalization of YPF in Argentina.

While bilateral and multilateral treaties provide some protection against these policy swings, counsel will do well to consider the impact of policy changes as part of the negotiation plan and set up commercial counterbalances which can be triggered in the future as the need arises. For example, an upstream company might consider a clause which adjusts the cost recovery formula (see Section 3.1 below) in its favour where the State increases the applicable tax burden.

A final risk sits at the intersection of State-sponsored nationalism and powerful oligarch interests in counties; an intersection that sits in a worrisome neighbourhood. In some countries, State pressure to nationalize is merely a front for the transfer of assets to oligarchs. Historically, this has proved to be the case in Former Soviet countries and in Nigeria, but is not uncommon in other jurisdictions, like Indonesia. Many powerful national actors have used governmental and administrative abuse of process to amass great wealth – all while wrapped in the national flag.

2.10.2.Macro-Economic Risks

Macro-economic risks have a tendency to be overlooked by lawyers, because legal practitioners traditionally have not viewed such considerations as within their 'legal scope'. This perspective can be disastrous; for example, for countries with a history of macro-economic instability, the purchase price can be less important to a foreign investor than the relevant price escalators.

Macro-economic risks include: inflation, foreign exchange (forex) fluctuations, bank liquidity (e.g. protection of deposits), and changes to applicable law. Many of the risks are correlated to each other, meaning a problem with one can be quickly compounded by the others.

Commercial actors in inflationary countries are often happy to push inflation and

forex risk on unsuspecting foreign investors, particularly petroleum service companies. The use of a price escalator tied to a consumer index is vital.

It is also wise to address the risk of a change to applicable law. If the host State changes the tax laws to increase the tax base on foreign investors, the net-back to those investors may be significantly affected. A similar result could arise from a change to laws that increases the cost of operations. In those scenarios, should the parties rebalance the arrangement? Is it appropriate for the foreign actor to take on all of the host country risk for a change in law?

To avoid liquidity risks with local banks, encourage your client's treasury department to develop finance policies and procedures which move cash from in-country accounts to foreign accounts, while still permitting sufficient local working capital.

A final risk involves the nexus between macro-economic risks and sanctity of contract. Certain Governments have an excellent historical record for following written agreements; for example, Brazil and Colombia. Sanctity of contract with other Governments has proved to be more problematic; for example, Kazakhstan and China. While the basic approach to sanctity of contract is historically and culturally informed, there is no doubt that macro-economic difficulties tend to incentivize Governments and private actors to ignore contractual terms that are not in their favour. This doubles the importance of mitigating macro-economic risk exposure for the client, as that risk may lead to yet further commercial risk exposure.

2.10.3. Labour and Union Relations

Labour, and more particularly union-related issues, can impact an international petroleum venture in a variety of ways from cost and productivity issues on one end, to strikes and blockades on the other.

Some countries, such as Abu Dhabi, have few formal requirements for either union or labour relations. Other countries have a more pronounced set of requirements, with unions playing a much larger role in society and governmental policy. Examples of such States include France and Argentina. Labour unions often play a significant role in community representation as they strive to achieve a high level of local employment with foreign operators. This is the case in Colombia and Mexico. A similar community connection exists in non-unionized countries, where local community leaders press for high levels of local employment. This is the case in Chad and Kenya.

In countries where unions and labour relations policies tend to influence the investment, a client should realistically identify the value burden of additional costs and operational delays from a mixed local and foreign workforce and incorporate

this burden into its economic forecasts and assumptions. Clients should also have a detailed understanding of the nature and scope of local labour/union laws and strictly comply with these requirements. Failure to execute on a well-developed local labour/union plan can well lead to strikes, blockades, theft, vandalism, and even personal security risks.

2.10.4. Security Risk

In our view, helping a client manage security risks arising from field operations is the second most difficult task facing an international lawyer. The two key risks that emanate from operational security are: (a) the cost of security (e.g. as provided by private contractors or the State), and (b) liability and reputational risk when security enforcement exceeds merely defensive needs (e.g. human rights infringement in Sudan). For a detailed review of this subject, we refer to: F. Stewart and A. Cioni, 'Holistic Security Risks Management Strategies For E&Ps: Optimizing Performance By Reducing Surface Risk' (2018) 1 *Journal of World Energy Law and Business*. In describing security risks, that article states:

> [...] it is also useful to review what a risk constitutes in the rubric of field security operations. It is a complex question. Discretely, field security risk could present in the form of assault, kidnapping, murder, terrorism, vandalism, theft, insurrection/riot and violent state suppression of unrest. These risks are often quantified in terms of likelihood and severity when judging whether investment in a given area is even practicable. The risk to a petroleum company of vandalism may be less pronounced than the reputational risk of a murder perpetrated against a citizen of the host state. The risks vary enormously from country to country and are informed by a complex interaction of factors, such as: history, politics, race, language, economics, crime, policing, labour relations, infrastructure investment, literacy, poverty, pollution, health and even the constitutional division of governmental authorities.

Briefly stated, it is a complicated problem. Mitigation of these risks may seem beyond the influence of counsel, but lawyers can play an important role in lowering these risks by being the lynchpin between the different skill sets that oversee field operations (e.g. community relations, Government relations, operations, procurement and compliance). The above-cited article suggests a best-practice approach to the issue along with a series of potential strategies to lower field security risks.

2.10.5. Marketing Risks

National economies literally need to be fueled. At present, petroleum is the global fuel of choice for transportation and heating, and even electrical generation in gas-fired plants. Accordingly, most Governments carefully oversee the fuel mix driving

their economies, in particular the cost of those fuels. Fuel prices can become the focus of debate, with populist Governments keen to curry favour with voters who benefit from low or subsidized prices. We reference riots over fuel prices in 2018-2019 in Haiti, France, Iran, Zimbabwe, and Belize – all in times of low international oil prices.

These political pressures can translate into small 'n' nationalization of the petroleum sector; effectively what amounts to regulated fuel prices and/or restricted export rights for foreign producers operating in-country. As discussed, these risks may be met in part by bilateral or multilateral investment treaties, or ICSID arbitrations, but other commercial techniques, such as taking security for payment, may further reduce the risk.

Part 3

Upstream

3. Upstream Specific Risks

Having broadly surveyed international risk and risk mitigation, we now turn to the application of these factors to companies pursuing the exploration and production of petroleum (an **Upstreamer** or **Upstreamers**).

3.1. Tenure Rights

The issue of mineral ownership and the right to authorize oil and gas exploration and development is not always certain. More than one Government body within a State may claim the authority to issue mineral tenure. A number of private and State entities may claim ownership rights - especially in those instances where private ownership currently exists or once existed but was later abolished by the State. In other circumstances, occupying military forces and aboriginal groups may also claim rights of ownership or authority over mineral rights. Finally, many federations in the world pose special challenges to the prospective petroleum venturer. Today, there are only about seven jurisdictions in the world were private freehold ownership of mineral rights is even possible, including Canada, the US, and Australia.

Even where ownership of petroleum is not an issue and, by constitution, the State holds title to all petroleum in situ, a host-country's system or mechanism of mineral tenure (through which the private sector acquires an interest in State oil and gas rights) can vary significantly from State to State and even vary within a State, over time. Even in those jurisdictions with high regard for the rule of law, the terms and conditions that apply to mineral tenure - even the grant of rights themselves - are subject to change. Governments recognize that oil and gas development is lengthy, capital intensive and high-risk. Further, most Governments appear to understand that mineral tenure is one area where investors look for stability and certainty. For example, recently in Alberta the *Royalty Guarantee Act* came into force purportedly to assure investors making long-term oil and gas investments in Alberta that the rules would not change halfway through a project; at least not until a new Government is in power with the authority to repeal the *Royalty Guarantee Act*.

Alberta solicitors are familiar with most aspects of the Alberta tenure regime. Alberta Crown leases grant an undivided beneficial interest in oil and/or natural gas - a profit-a-prendre for an uncertain term. The words of grant in the province's standard form petroleum and natural gas licences and leases grant the holder the right to access another's property and win, work and remove a valuable resource. The Crown owns the corporeal estate (i.e. the oil and gas in place) and the lessee has an incorporeal right in relation to the oil and gas in place. Once severed (i.e. captured or extracted), title to the oil and gas in place passes to the lessee as personal prop-

erty.

Many of the features of Alberta's tenure regime are found in other jurisdictions around the globe. For example, in the Russian Federation, ownership of Russia's subsoil minerals is allocated to the State by the Russian Constitution and is subject to the joint jurisdiction of the federal Government and the regional Government where the deposit is located. Therefore, subsoil deposits themselves cannot be subject to purchase, sale, gift, inheritance, contribution or pledge. Madagascar has a similar regime.

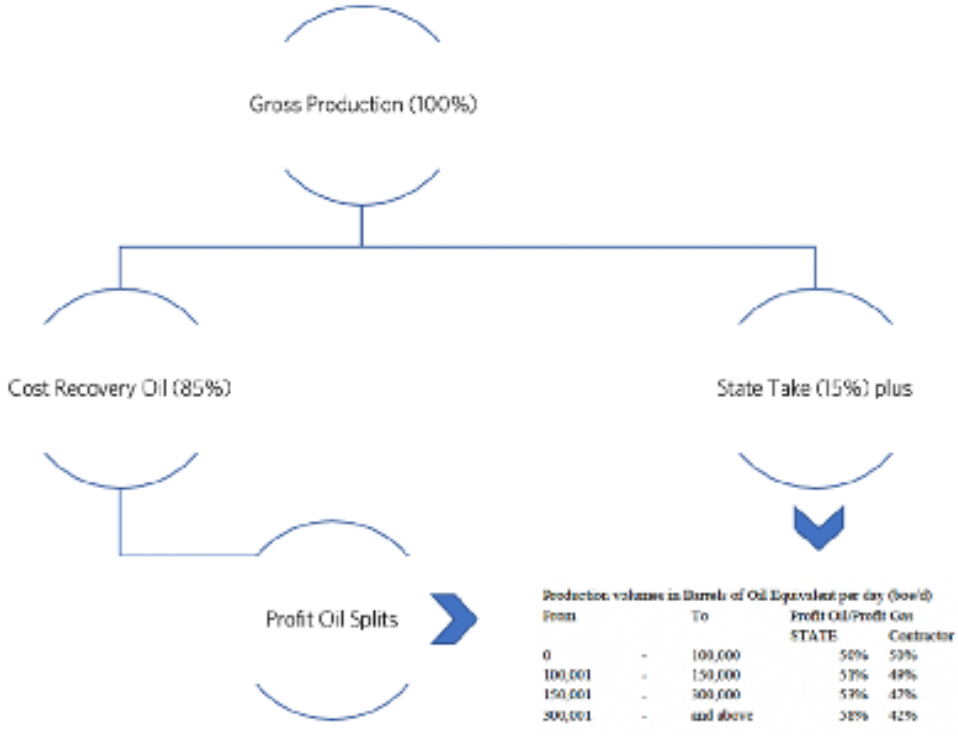
Internationally, the grant of rights to explore for and produce petroleum is most often made by contract, although licenses are still issued in certain States. In the late 19th and early 20th centuries, grants were often made by way of concession. These arrangements were often one-sided, in favour of a large Western E&P company, such as Anglo-Persian's (now BP) concession with Persia, Royal Dutch Shell's concession for Saudi Arabia and Royal Dutch's pervasive concessions in Indonesia. The asymmetry lead to considerable political risk after World War II as post-colonial States began asserting the national interest of their new States. Those ownership tensions remain with the industry to this day.

In response to those tensions, in particular Royal Dutch Shell's holdings in-country, Indonesia proffered a new granting instrument in 1960 under Law 44; namely the Production Sharing Contract (**PSC**). While other granting instruments do exist (e.g. joint venture agreements, service contracts (e.g. Ecuador, Malaysia and Iraq) and tax/royalty agreements such as France and the U.K.), the PSC is now generally the granting vehicle of choice for most countries.

Under a PSC, a contractor (typically an E&P company), is granted the exclusive right to explore for and produce petroleum in a given contract area. The contractor holds no rights to petroleum in situ (in place), instead the mines and minerals continue to remain owned by the State. The contractor is granted something akin to a profit-a-prendre or a contractual license. In fact, in some countries, the contractor never holds title to the hydrocarbons that it has captured/lifted. In these circumstances, the contractor acquires agency rights to sell State petroleum that the contractor has reduced to its possession.

As the name indicates, the chief commercial feature of a PSC is the sharing of production between the contractor and the State. This sharing is impacted by a concept called 'cost recovery'. Under a PSC, the contractor takes all of the capital risk of exploration. If no resources are found or produced, then the contractor has no assets or profit to offset its significant exploration activities, such as seismic acquisition.

If resources are discovered and produced, the contractor is able to recoup its sunk exploration and development costs (often plus marginal deemed interest to compensate for the cost of capital) by taking a higher allocation of petroleum (**Cost Oil**) at the commencement of production. This allocation mechanism persists until the declining balance of sunk costs reaches zero, whence the parties revert to the base sharing arrangement (**Profit Oil**). Note that in jurisdictions such as Algeria and Egypt there are percentage cost recovery limits that the contractor is allowed in any one year or in aggregate. The following diagram illustrates Cost Oil and Profit Oil splits from a production sharing contract in Latin America:



Other common features of PSCs include:

Contract Phases	Exploration Phase(s): The commencement of the PSC's term, where the contractor is permitted to explore for petroleum, is called the Exploration Phase. There are often three subphases of: three, two and two years respectively. The Minimum Work Obligations of the first subphase are commonly the least capital intensive. Thereafter, the investment requirements of each subsequent subphase increase to the drilling of one or more wells. Appraisal Phase: If there is a petroleum discovery from an exploration well, the contractor and Government must then assess that discovery to determine whether it can be economically produced. This is known as the Appraisal Phase and is often not limited to a set time period. Development Phase: If a discovery is worthy of a full field development, then the parties will enter the Development Phase to manage the drilling and construction work required to build the development infrastructure. Production Phase: This phase commences upon the first non-test related production of oil/gas and typically lasts for a period of 25-30 years. If the field produces beyond this period (beyond the term of the PSC), the contractor's rights will terminate and revert solely to the State along with all of the field infrastructure. In some instances, the State may choose to continue production in association with a new contractor once the PSC term has expired (e.g. the Al Shaheen oil and gas field offshore Qatar was originally operated by Maersk Oil Qatar under a PSC on behalf of the State of Qatar). In 2016, France's Total replaced Maersk as operator via a tender process.
Minimum Work Program	In order to secure a PSC in a bid round, competing E&P companies offer Minimum Work Programs, describing the activities and investment capital the company is willing to expend during the Exploration subphases. For example, an operator might offer a 3D seismic acquisition in the first subphase, followed by an exploration well in each subsequent subphase. The State chooses from amongst the competing bid offers to determine which company will provide the most value to the State under a PSC. So long as a contractor completes its Minimum Work Program obligations for an Exploration subphase, it has no obligation to conduct further activities during that subphase, nor does it have to proceed to the next subphase if the PSC area is proving less prospective.

Relinquishment	When moving from one Exploration subphase to another, the contractor will likely have to relinquish some percentage of the PSC contract area to the State. At the end of the Exploration phase as a whole, all areas not associated with a discovery will return to the State.
Management and Oversight	The contractor acts as the operator for day-to-day activities relating to the PSC. The operator is overseen by a Management Committee comprised of the contractor and the State. Committee votes often require unanimous approval and the Committee's oversight covers such important matters as: annual budgets, procurement operations, training programs and selection of well locations.
Cost Recovery Controls	Given the nature of cost recovery, many Governments take the view that all contractor expenditures ultimately represent governmental expenditures (i.e. losses to the State) in the form of Cost Oil. As a result, Governments pay close attention to Management Committee approval of expenditures on procurement contracts. Similarly, Governments often conduct cost recovery audits in an attempt to control - and as a commercial matter - negotiate the value of the contractor's sunk costs. There can result in significant delays due to audit challenges.
Domestic Marketing Obligations	Originally, PSCs permitted the export of all volumes. PSCs now commonly require contractors to sell a portion of the production domestically at "market rates", which may or may not reflect international pricing. This risk is especially pronounced for gas production. This risk is strongly correlated to political risk (e.g. the temptation of a populist Government to force a contractor to subsidize domestic energy prices) and forex risk (e.g. sale proceeds in domestic currency).

3.2. Proper Issuance of PSC

State sovereignty allows a host country to establish the process through which a PSC may be awarded. Further, the host country can determine what consideration is required prior to the grant of the PSC, such as fees or bonus payments. However, when a host country places even a modicum of value on the rule of law, adherence to a State's national laws effecting the issuance and approval of a PSC is imperative.

While many of these laws may seem merely procedural in nature, a failure to strictly follow these requirements can taint a client's interest. Many countries require parliamentary, ministerial, or presidential approval of a PSC and gazettal (i.e. publi-

cation in the official Government gazette of laws, as often seen in civil law jurisdictions). Without those approvals, the agreement may not be operative or enforceable, nor should expenditures be made prior to gazettal.

As noted above, the question of corruption often arises where a host-country's laws are circumvented and, less frequently, even when they are not. Even purportedly 'legal' Government demands for large signature bonuses or seismic data purchases that are not warranted from a value perspective may be a red flag for corruption.

Most countries award PSCs either through competitive or discretionary public bid rounds. If a company is offered preferential access to a PSC by being permitted to conduct direct negotiations with the State, it is prudent to review the legality of that access as a bulwark to corruptive activities.

Even if preferential access is permitted and above board, it is wise to document all of the client's dealings with the State. This will allow the client to later demonstrate the legality of the process to third-party investors, farminees, purchasers, and anti-corruption regulators; an effective tool for preserving the value of the PSC interest.

3.3. Transfer Approvals

The petroleum industry is perhaps the most geo-politicized business in the world. Governments have great interest in overseeing which companies (and nations represented by those companies) operate in their territory. From the 1960s until about the 2000s, host Governments' need to manage the E&P companies operating within their borders, motivated prior State approval for the transfer of an interest in a PSC.

To obviate this requirement and any associated capital gains on the transfer of an interest, some operators side-stepped the consent requirements by selling shares in the offshore holding company above the local holding company. Governments cottoned on to this strategy and began closing the loop between 2005 and 2010 by requiring governmental consent for change of control transactions. The results of that effort varied from country to country. Some, like Indonesia, brought in consent rights for share transfers while taxing capital gains on share sales outside the country. Other counties, like Brazil, did not alter their granting instruments, but did include change of control limits in the form of a parent company guarantee required of a contractor under those granting instruments.

Other States not only required consent, but also purported to give the State a right-of-first refusal on the transfer or a PSC interest, or the sale of shares in a company that holds an PSC interest. Kazakhstan famously did so on a retroactive basis. The self-grant of pre-emption rights was particularly problematic where the share deal

in question was in respect of a public company. Could a foreign Government really run around a stock exchange floor in a Western country trying to pre-empt every share trade with a self-serving local statute? This further demonstrates the degree to which geopolitics can influence the petroleum industry.

3.4. NOC Back-In Rights

Many PSCs or petroleum statutes grant the national oil company (**NOC**) the right to acquire an equity stake in any petroleum development project carried out in-country after the Exploration Phase (a **Back-In**). The quantum of the stake varies between about fifty percent (e.g. China) through to fifteen percent (e.g. Chad). The purpose of a Back-In is to increase the State's effective share of production while simultaneously providing training and experience to NOC personnel.

The Back-In right is optional, at the NOC's discretion. Typically, the NOC is required to give a participation notice to the contractor late in the Appraisal or early in the Development Phase. The contractor is typically required to fund the NOC's proportion of the development costs, but is reimbursed through an assignment of the NOC's Cost Oil entitlement until those costs are repaid (sometimes together with, but often without, deemed interest).

A Back-In poses some conflict of interest issues for a contractor, who must then deal with: (a) the Government as a counterparty to the PSC; (b) the Government as Regulator; and (c) the Government (qua NOC) as a joint venture partner. This conflict can lead to asymmetrical commercial situations that are difficult to manage, as the foreign contractor finds itself surrounded by different State demands and influences.

3.5. Joint Operating Agreements

In most international jurisdictions, more than one party may hold an undivided interest in a PSC. Accordingly, most E&P companies will seek out partners to share the not insignificant risks of exploration and production granted by a PSC. In these circumstances, the co-venturers will agree to bear their 'working interest' or 'participating interest' share of all the rights, duties, benefits, and obligations of the PSC. This co-ownership can exist not only in the PSC itself, but also associated chattels, oil and gas facilities and infrastructure, funds, and other kinds of personal property.

The relationship of the co-venturers is typically governed by a more formal, written, multiparty joint venture agreement called a Joint Operating Agreement or JOA. Often considered the most significant contract in the upstream oil and gas business, the JOA defines and details the fundamental relationship among joint venture parties over their long-term relationship from initial hydrocarbon exploration to

production. Through the JOA, the joint venture partners agree on a set of rules for the management of operations under the PSC, as well as how the costs of those operations will be financed. The JOA's provisions are also meant to address various contingencies that can develop during the duration of that relationship.

Different model form JOAs have been developed over time which have evolved to accommodate the particular geographic, operational, regulatory, economic, and political context of the jurisdiction in which the oil and gas resources are located. This includes the particular geology common in the region; the environmental impacts; the location (for example if the resource is located in a remote frontier or offshore); the production profile; the legal nature of the rights granted and tenure regime; and the nature or sophistication of local oil and gas law.

The more commonly used standard form JOAs are often designed for a particular country or region. These include the American Association of Petroleum Landmen Form 610 model (2015); the Oil and Gas UK Limited model - for use on the UK Continental Shelf; the Australian Mining Petroleum Law Association model form, issued in 2011; and the CAPL (Canadian Association of Petroleum Landmen) standard form, the most recent of which was issued in 2015.

In addition to these region-specific model JOAs, the Association of International Petroleum Negotiators has also produced a model form of JOA which has a much broader international scope and is intended to be adapted to those jurisdictions where there is no reputable region-specific JOA.

For fifty years, legal practitioners and industry participants have written about JOAs; this compendium of research and analysis includes an accounting of their evolution, analysis of the broader issues which are common to many JOAs and a lexical analysis of specific terms and clauses.

For a more detailed analysis of both the regional JOAs and the more internationally applied AIPN model form JOA, please refer to The AIPN Joint Operating Agreement: A Practical Guide by Reginald Fowler, Peter Roberts, Eduardo Pereira (2019) Globe Law and Business Limited. What follows is a short summary of the more salient features of a JOA:

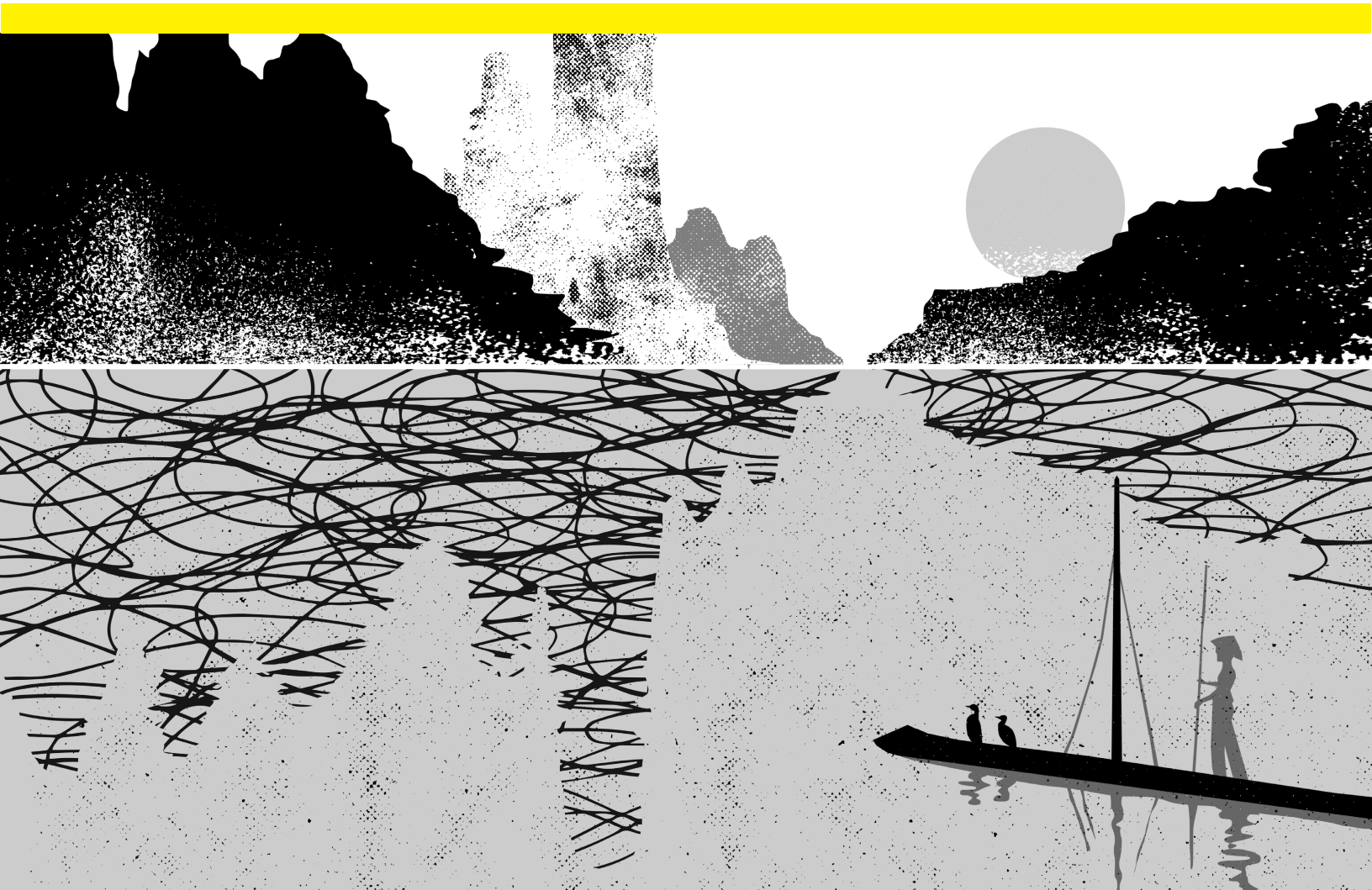
Operatorship	The joint venture parties typically select one of their number to serve as operator. The operator conducts the day-to-day business of the joint venture, subject to specific limits prescribed by the JOA. The boundaries of the operator's powers, including economic approval thresholds, are often points of negotiation. This is particularly true of the voting threshholds to applicable to operations matters. Operations are conducted at the expense of the joint venture parties but under the supervision of the Operating Committee. Costs and liabilities will typically be born by the parties in proportion to their participating interests. However, in certain circumstances, the operator's conduct may be so grievous that the operator will be solely liable. The threshold of egregious conduct that will lead to an operator's sole liability is usually negligence, gross negligence, wilful misconduct, or some hybrid thereof. Following BP's large scale blow out on the Macondo well, this question is often a subject of intense negotiation between the parties.
Operating Committee	The Operating Committee is comprised of a representative of each joint venture party. Each representative holds a vote equal to the participating interest of the appointing party. The voting threshold for various matters is often of commercial concern. Parties will examine not only their voting rights with their current holdings, but also an analysis of what level of participating interest they may wish to hold in the future. The Operating Committee approves all Annual Work Programs and Budgets and material cost-overruns. Above *de minimus* levels, the Operating Committee also votes on procurement, litigation and operational matters (such as well locations and well design). These are points of supervision by the Operating Committee over operator discretion, serving as a 'health check' on important matters like Health Safety and Environment. These points are often negotiated. For certain fundamental decisions, like field abandonment or PSC extensions, the unanimous approval of the Operating Committee may be required or preferred.

Annual Work Programs and Budgets	Each fall the operator prepares a draft work program and budget for the next calendar year. This work program and budget must reflect the Minimum Work Program obligations owed to the State under the PSC. Once approved by the Operating Committee, each joint venture partner is legally obliged to pay its participating interest share of the cost and liabilities associated with the field operations (unless a liability arises as a result of operator gross negligence or wilful misconduct).
Cash Calls and Financial Default	Once the Operating Committee has approved an annual work program and budget, the operator may request advance funding from each joint venture partner for its participating interest share of the costs for the next month or quarter. The JOA may also require the delivery of financial security to the operator for those payment obligations. Similarly, each joint venture partner must provide its participating interest share of credit support where applicable law or the PSC requires the delivery of financial security to the State to cover the risk of: PSC operations, abandonment obligations and contractor default of the PSC. If a joint venture partner fails to provide its share of funding or credit support, then the other parties have a variety of remedies for the default: The forfeiture, in favour of the other partners, of all or part of the defaulting party's participating interest for no consideration. A sale of all or a portion of the defaulting party's participating interest to the other partners for a discounted price. Other remedies include the sale of the defaulting party's petroleum entitlement to pay the debt; the loss of the defaulting party's voting rights; the loss of transfer rights or pre-emptive transfer rights; and the loss of the right to current operational information Note the above-explained prohibitions or restrictions that civil law jurisdictions may apply to these remedies; effecting their enforceability.

Transfer Rights	The transfer of a participating interest by a joint venture party often requires the consent of the other parties (in addition to any State consent rights under a PSC). It may also trigger the pre-emptive transfer rights of the other parties. These can include rights for first refusal, rights of first negotiation, tag along/drag along rights, or shotgun rights. Less frequently, such consent or pre-emptive rights might apply to change of control transactions. Careful consideration of these terms should be given in relation to a client's ability to carry out future financing. Direct and indirect pre-emptive transfer rights are amongst the most heavily negotiated items in a JOA. Parties need to carefully consider their risk tolerances in being exposed to the project, while also considering their future liquidity in relation to their funding of future project costs under the JOA.
Sole Risk Operations	For some proposed operations, joint venture parties may have the right to opt out and not pay their proportionate share of the costs (nor receive their proportionate share of the revenue if the operational is successful). Alternatively, minority joint venture parties may be 'drug along' with the other parties to fund a proportionate share of a work program and budget approved by the Operating Committee. Where an opt-out is permitted, the other joint venture parties may still choose to continue with the operation on their own, at their own risk. This is called a Sole Risk operation. Specific rules set out when a Sole Risk may be carried out. In some JOAs, Sole Risk non-participants may be able to rejoin a Sole Risk operation by the payment of a hefty penalty fee to the participating parties. While this mechanism is rarely used in international joint ventures (i.e. outside of the US and Canada), it is an important feature, acknowledging the reality that some partners are more risk tolerant than others or wish to proceed more aggressively with a project. Without the sole risk provisions, the pace of the project may be dictated by the most cautious and risk adverse of the parties or face outright deadlock.
Governing Law	English law is most frequently chosen as the 'governing law' of the JOA, particularly where the joint venture partners are from different jurisdictions. Sometimes the JOA adopts the laws of the project's host country. In these cases, it is important to recall that civil law jurisdictions do not necessarily have all of the legal concepts used or mentioned in a typical JOA (such as trusts). See the prior discussion regarding those risks.

Part 4

Midstream & Downstream



4. Midstream – Downstream Specific Risks

The midstream petroleum industry is often described as that part of the industry that processes, stores, markets, and transports commodities such as crude oil, natural gas, and natural gas liquids. By comparison, the downstream industry often includes oil refineries, petrochemical plants, petroleum products distributors, retail outlets, and natural gas distribution companies. Companies engaging in this sector are colloquially called Midstreamers or Downstreamers.

Although these bright line distinctions may be appropriate in North America, in many parts of the world, midstream activities are commonly included as part of other operations and many oil and gas companies are considered integrated because of their ability to combine upstream, midstream, and downstream activities as part of their overall operations. In fact, it is common to see fully integrated projects (e.g. including Upstream, Midstream, and Downstream) in countries where industrial infrastructure is scant. The Rovuma and Area 1 LNG projects in Mozambique are examples of such projects.

Many of the risks faced by Upstream companies also apply to Midstream and Downstream operators looking to construct, own or operate pipelines or refineries abroad. As with upstream projects, Midstream and Downstream projects are capital intensive with profit returned over the many years of the project's life. Unlike Upstreamers, the profits on most Midstream and Downstream projects is bracketed to a utility rate of return of eight to fifteen (8-15%) percent. Whereas Upstreamers take more risk in the search for large reserves, Midstream and Downstream companies take less risk in exchange for stable, but healthy income.

4.1. Tenure Rights and JVs

Tenure rights for large Midstream and Downstream projects are usually derived: (a) as a result of a Government-backed process to open an infrastructure project up to private investment; or (b) as a result of a decision by one or more companies to commercially invest in an infrastructure project without Government involvement. The latter is less common in emerging markets or in jurisdictions where there is a heightened risk of expropriation or nationalization.

In the first scenario, tenure rights may be offered by license, concession, or joint venture agreements with the Government, NOC, or Government owned-utility company. The issues in these agreements are akin to those associated with PSCs above. The major exception being the full exposure of a proponent to in-country risks – there is no real 'export' market for a pipeline or refinery inside a nation.

While these agreements may provide a Midstreamer or Downstreamer with some

certainty of investment terms, a proponent must always keep an eye on changes to applicable law to ensure those terms are not indirectly altered.

For example, a pipeline or refinement facility may be classed as a strategic or common asset requiring governmental tariff regulation or price controls on the products created by the refinement process. Similarly, the allocation of capacity rights in the facility may be subject to regulation. This can pose significant investment risk in situations where an Upstreamer invests in Midstream or Downstream assets to capture a higher-net back.

4.2. Other Common Risks

Risk aversion drives the need for detailed risk assessment. Most Midstream and Downstream organizations are generally well suited for this task, but may lack the necessary information in-country to make an accurate assessment. Typically, the high-level risks of a Midstream, or Downstream project are as follows:

- The local tax burden, as offset by the benefits of any applicable Double Taxation Treaties
- The credit risk of timely tariff payments over the life of the project, as potentially mitigated by the issuance of payment guarantees by the State or a utility company
- Forex risk, currency controls and repatriation limits can all negate an operator's ability to realize on its return
- Inflation, particularly where tariff rates are fixed and do not reflect an increased cost base in-country
- Expropriation is always a possible political outcome, particularly where a certain piece of midstream or downstream infrastructure is perceived to be of strategic national importance by the State. In countries with no applicable bilateral investment treaty, protection against expropriation is purely commercial unless the forum for dispute resolution is ICSID. Even where investment treaties apply, project proponents must still plan for and guard against 'creeping' expropriation – the State's accretive carving back of previous benefits granted to the proponent. This type of State action is more difficult to fit squarely into a standard expropriation claim.
- Since midstream or downstream infrastructure typically have a large footprint, community relations are often an issue. There is a nexus between these projects, community relations, surface access rights, and local employment/labour relations. Without a clear engagement plan created by local experts, the risk of project resistance or delay can be elevated.

Part 5

Petroleum Service

5. Petroleum Service Specific Risks

Many of the same risks posed to Upstream players are also an issue for petroleum service providers looking to sell their goods and services in a host country (a PS Company or PS Companies). However, the nature of petroleum services is generally more transactional that Upstream, Midstream, or Downstream activities. The notable differences are the lack of a PSC and, typically, extensive assets in country.

Typically, PS Companies chase one-off projects lasting a few weeks to two or three years at most. This more temporary duration means that risk analysis for PS Companies is different than the risk analysis for Upstream, Midstream, or Downstream players.

5.1. Typical Risks

With a constrained profit margin for each job, it is important to understand which risks could degrade a PS Company's return on a given job. The obvious starting point for most PS Companies is the examination of in-country financial risks. A diligent analysis of the following usually tells a company whether it is even worth chasing business in a foreign country:

- Local tax burden, as offset by the benefits of any applicable Double Taxation Treaties
- Forex risk, currency controls and repatriation limits
- Inflation risk
- Credit risk
- Debt servicing ratios
- Foreign Reserves
- IMF loans and their influence on fiscal policy
- Political unrest or instability
- Ratification of international treaties

While seemingly obvious, this preliminary step is often skipped – making the later mitigation of those risks more difficult.

As a second diligence pass, we encourage PS Company clientele to then assess the cost burden and organizational expansion required to comply with in-country rules regarding: tax, licensing, immigration, community consultation, employment, and labour and community consultation. In our experience, many companies fail to fully understand the costs of compliance; which can have a huge impact on profitability.

Managing these risks usually requires the retention of the right experts in-country, either as employees or consultants. Stepping into a foreign country and assimilating these experts into the company's organizational structure is typically a large, transformative step. Many PS Companies fail to assess that degree of transformation and burden on managment, or the costs with either.

5.2. Local Partners – Joint Venture Matters

Many host countries have a legislative scheme to increase the use of local labour, manufacturing and materials. These criteria are often used to favour the use of those local resources for petroleum sector services provided in-country to the NOC or other upstream operators.

The schemes vary from country to country. Some prescribe the degree of local ownership in any company licensed to carry out petroleum services. Others do not dictate local ownership, but instead mandate 'procurement points' where local resources are employed by foreign service companies. Recalling that many PSCs give the Government input on procurement matters via Management Committee voting, some Governments will require such procurement points to be included in the operator's bid evaluation when awarding work for PSC operations. These schemes have been employed in countries like Kazakhstan, Brazil, Qatar, UAE, and Nigeria.

In the light of the above, it is often necessary for PS Companies to engage a local agent under a distribution agreement, or a joint venture partner under a license and/or joint venture contract. The success of the either most heavily depends on the quality and experience of the local agent/partner involved.

The selection of a local agent can be bewildering. In countries like Saudi Arabia, thousands of individuals present themselves as the 'best line into' Saudi Aramco. Representations are often made about the degree of social clout or Wasta, as it is often called by Gulf Arabs. Everyone is a royal prince with fantastic connections to other princes. It is very difficult to assess the efficaciousness of these agents – an assessment which is entirely commercial and political. We are often called on by our clients to assess the possibility of terminating an agency agreement in circumstances where the local agent has simply failed to execute any part of its job.

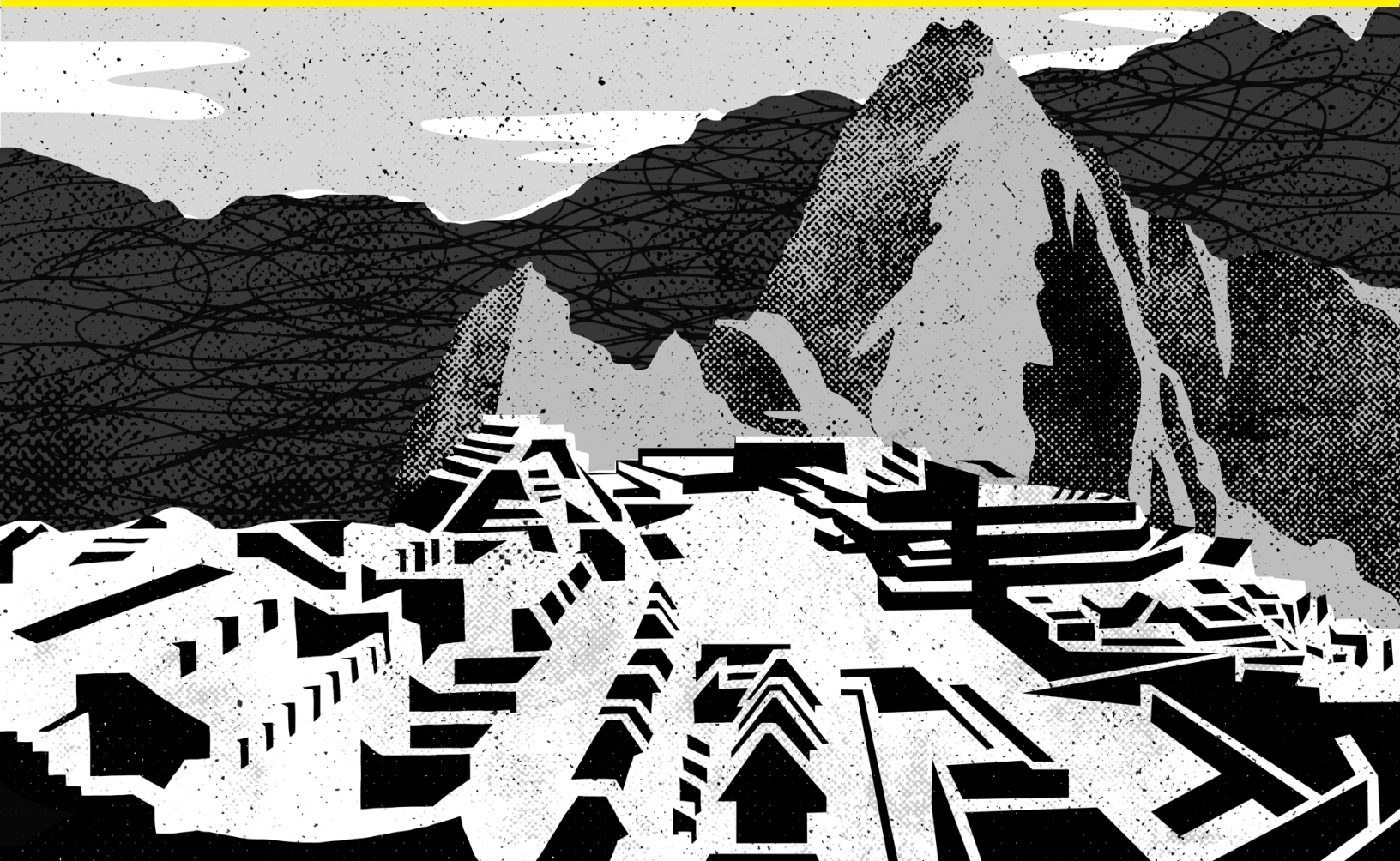
If the selection of a local agent is tough, the choice of a joint venture partner is even more difficult. Agency relationships tend to be more transactional and do not also involve the investment of capital in facilities and equipment – both typical features of a joint venture arrangement in the petroleum services sector. This redoubles the danger, adding capital and operating cost risk on top of the risk of finding an efficacious local agent.

Applicable law may require that disputes between a PS Company and its local agent/partner be decided by local courts or domestic arbitration, instead of by international commercial arbitration protected by the NY Convention. We reiterate our comments about the relative risks of domestic dispute resolution. Where the local agent/partner is powerful, lack of access to an untainted forum may also be a political risk.

The hallmark issues in agency or joint venture agreements are usually:

- **Term and Exclusivity**: How long will the agency/venture last? Will the local agent/partner have the benefit of exclusivity during the entire term? Can exclusivity be lost as a remedy for poor performance?
- **Intellectual Property Rights**: In parlour with discussions on exclusivity, is a client bound to provide the agent the right to represent any new products developed? Even if those products service different market segments? What will the agent do to help protect the abuse of the client's IP in-country?
- **Non-Competition Covenants**: Will the agent/partner be permitted to represent a competitor's products in-country at the same time? Is it possible to safely identify your client's exact market segment to avoid conflicts of interest?
- **Marketing Covenants**: What metrics can be used to ensure a focused and consistent marketing effort by the local agent/partner? Often these covenants are very weakly stated.
- **Credit Risks**: Will your client only be paid once the agent/partner is paid in-country? What financial risk does the agent/partner carry for slow payment or no payment? For example, local representatives are loath to press a NOC for payment on a client's behalf if the representative thinks that doing so will jeopardize their larger relationship with the NOC. In this way, credit risks can also pose conflicts of interest. In addition, clients should carefully follow in-country accounting regulations (for example, electronic invoicing as required in Colombia).

Conclusion



6. Conclusion

As this paper has demonstrated, the petroleum industry is heavily geo-politicized. This fact requires lawyers and commercial professionals to consider risk and risk mitigation well outside the bounds of the typical Canadian 'lawyer box' when advising clients in the upstream, midstream, downstream, or petroleum service sectors.

The key to de-risking a foreign venture is fulsome diligence before the commencement of the project or transaction. In this case, diligence includes the tolling of the commercial, political, operational, technical risks – each of which differs widely from sector to sector and country to country. Input from local counsel will be invaluable in this effort, as will a practical consideration of which risks will not be sufficiently addressed by legal protection alone. As an output, the diligence process will then permit the creation of an execution strategy keyed on the commercial realities of operating in the foreign State. That strategy should presume the erosion of the client's negotiated position as a hedge against negative future changes.

Once a project or deal has launched, effective legal representation requires a great degree of practicality. The solutions to a problem in a jurisdiction where laws are not followed are unlikely to be the same as the solutions to a problem in jurisdictions where laws are followed. Recall the above-described metaphor; the goal of counsel is to amass commercial poker chips. Some of those poker chips may be used during the negotiation of the deal or commencement of the project, but some will be kept for later. This is especially true in countries where the signature of a contract is not the culmination of a negotiation, but rather the starting point for a series of negotiations over the duration of their commercial relationship.

CITO

— ENERGY GROUP —

CITO.ENERGY

Cito Energy Group

501, 304 -8th Ave SW
Calgary AB
Canada T2P 1C2

(403) 536 1418

info@citoenergy.law

Chief Contacts:

Pat Cunningham: pat@citoenergy.law
Tony Cioni: tony@citoenergy.law