

**THE ISSUE OF RESOURCE NATIONALISM:
RISK ENGINEERING AND DISPUTE MANAGEMENT
IN THE OIL AND GAS INDUSTRY***

PROFESSOR A. F. M. MANIRUZZAMAN**

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I. INTRODUCTION

Resource nationalism has historically proved to be a cyclical phenomenon, and it is not new.¹ In various geopolitical contexts and

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situations, it has tended to assert the nation-state's sovereign authority over the upstream (and often even downstream) activities of international oil companies ("IOCs") in the petroleum industry. The specter of resource nationalism has often appeared with resource scarcity (whether manipulated or not²) and the consequent increasing energy prices in the world market. World politics could often be the driver behind it. The events of the 1970s leading to the demand for a New International Economic Order ("NIEO") by the developing world and of the recent past in Latin America and Russia divesting IOCs of their properties in those countries are the grim reminders of resource nationalism.³ Such a phenomenon is certainly a big risk factor for IOCs, and it leads to disputes between IOCs and their host states. There are ways and means—legal and extra-legal—by virtue of which such risks may be tackled.

The purpose of this article is to discuss these so that IOCs find them as useful tools for the purpose of protecting their interests in this vulnerable situation. The article first discusses the meaning of resource nationalism; it then proceeds to examine the role of the rule of law in the event of resource nationalism. This is followed by an appraisal of the risk-management toolbox, i.e., the legal and extra-legal means of risk and dispute management. The article then concludes with some remarks.

This article is written from the perspective of IOCs or foreign investors and will be concerned with the means that could be at their disposal. It will not deal with treaty aspects, the control of which lies immediately beyond their remit and is in a different sphere, as these are interstate

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** LLB (Honours), LLM (Dhaka), M.Int'l.Law (ANU), PhD (Cambridge), FRSA, MCI Arb, Professor of International and Business Law, School of Law, University of Portsmouth, U.K. and Honorary Fellow (Professorial), Centre for Energy, Petroleum, and Mineral Law and Policy, University of Dundee; Council Member, ICC Institute of World Business Law, Paris; Advisory Board & Academic Council Member, the Institute of Transnational Arbitration, U.S.A., Member, Swiss Arbitration Association; Member, European Court of Arbitration. He is a founding member of the IDR Group® (international dispute resolution specialists: idrgroup.org), based at Lamb Chambers, London. The author may be contacted by email: munir.maniruzzaman@port.ac.uk.

1. See generally Paul Stevens, *National Oil Companies and International Oil Companies in the Middle East: Under the Shadow of Government and the Resource Nationalism Cycle*, 1 J. WORLD ENERGY L. & BUS. 5 (2008).

2. See TOM BOWER, *THE SQUEEZE: OIL, MONEY, AND GREED IN THE 21ST CENTURY* (2009); see also Tom Bower, *A Bracing Walk through Vienna with Mr. OPEC*, THE SPECTATOR, June 6, 2009, available at <http://www.spectator.co.uk/essays/3665753/a-bracing-walk-through-vienna-with-mr-opec.shtml>.

3. See Jose L. Valera, *Changing Oil and Gas Fiscal and Regulatory Regimes in Latin America*, 2008 OIL GAS & ENERGY L.J. 3, at 150.

matters, although these may bear on the relationship between the host state and IOCs.

II. UNDERSTANDING RESOURCE NATIONALISM

Resource nationalism has been sparked by rising energy prices caused by various geopolitical and market conditions. Such a phenomenon has manifested itself in different forms and shapes of events over the years in a resource cycle. Resource nationalism being a cyclical phenomenon, the intensity of the nationalism of a resource-producing country is felt far more acutely at the upper end of the resource cycle than at the lower end when it begins. Resource nationalism can be better understood in the cause-and-effect scenario. In other words, what causes resource nationalism and what effects it produces or what consequences it leads to need to be appreciated in order to understand the phenomenon. Resource nationalism came and resource nationalism went, but one thing is painfully clear: it leaves a deep scar in the relationship between the contracting resource-producing country and the foreign investor (i.e., IOCs) or destroys such relationships altogether.

The last resource nationalism of the 1970s and 1980s came in the early 1970s with the Arab oil embargo when the Arab oil-producing countries reduced exports and raised prices in retaliation for Western support of Israel in the Yom Kippur War.⁴ It caused a rippling effect across the oil-rich countries. Resource nationalism manifested itself in resource nationalizations in many countries and led to the clarion call by the developing countries for the establishment of a NIEO.

The recent round of resource nationalism (2003–2008) in the oil-rich states was triggered by various factors such as increasingly high demand of energy in the emerging economies like China and India and the prolonged conflicts between the West and the Middle Eastern countries like Iraq and Iran. All these factors have contributed to the skyrocketing of energy prices, and the resource-rich countries have again found their energy resources as a strategic weapon as in the previous rounds of resource nationalism. The fallout of these events was felt across the globe and ignited again the passion for resource nationalism in countries including Russia, Venezuela, Algeria, Libya, Bolivia, Ecuador, Nigeria, Kazakhstan, and Indonesia. It has to be acknowledged that the current round of resource nationalism appears in a context different from that in the previous round of the 1970s–1980s. There happens to be new challenges, such as the constant concern for energy security because of the rising demand for energy, especially in the emerging economies, the

4. The cycle continued from the early 1970s to the mid-1980s.

urge to harness renewable energy sources, the current acute environmental awareness including climate change, and an anti-Western sentiment of resource-rich developing countries against economic globalization and the Western IOCs. In the latter context, resource nationalism appears more as resource protectionism, a shield against Western dominance in the energy sector through their IOCs. As usual, the initial action of resource nationalism manifests itself in the resource-producing countries' desire to control the resources by various measures, such as majority ownership at the initial stage, which may culminate into nationalization at the upper end of the cycle. Other specific manifestations of resource nationalism may be found in the resource-producing country's move to maximize revenue from oil and gas production by unilaterally changing the terms of the original contract (the phenomenon described by Harvard economist Raymond Vernon as "obsolescing bargain"⁵), by forced renegotiation of the original contract, or by other forms of economic coercion such as forced sale.⁶

An important dimension of the current round of resource nationalism across the globe has been the growing strength of national oil companies ("NOCs") to take control of their oil and gas resources and the consequent limiting of the access of IOCs to such resources.⁷ IOCs have

5. RAYMOND VERNON, *SOVEREIGNTY AT BAY: THE MULTINATIONAL SPREAD OF U.S. ENTERPRISES* (PAGE) (1971). By "obsolescing bargain" he means that "once oil was discovered and the investment sunk in development, relative bargaining power switches in favour of the host government which then tries to increase its fiscal take by changing the terms of the original contract." Stevens, *supra* note 1, at 5.

6. Detlev Vagts, *Coercion and Foreign Investment Rearrangements*, 72 AM. J. INT'L L. 17 (1978). For the very recent saga of the IOCs operating in Nigeria concerning the call for review of the existing contracts under the "Petroleum Industry Bill" (introduced in 2007, it has passed its first and second readings in the National Assembly of Nigeria as of May 2009), the purpose of which is to unbundle the Nigerian National Petroleum Corporation ("NNPC"), the Nigerian state-owned NOC, see Chika Amanze-Nwachuku & Chuks Okocha, *Oil Companies Oppose Review of Contracts: Why We're Unbundling*, THIS DAY ONLINE, May 8, 2009, <http://www.thisdayonline.com/ncomments.php?id=145540#220582>.

7. Sheila McNulty, *Oil Rich Nations Seek Majors Expertise*, FIN. TIMES, Mar. 10, 2009, available at <http://www.ft.com/cms/s/0/1ac507ee-0ddd-11de-8ea3-0000779fd2ac.html> ("The high prices had led countries such as Venezuela and Russia to raise barriers to the international oil companies, which have gone from control of 85 percent of the world's oil reserves in 1970 to less than 10 percent now."). See generally VALERIE MARCEL, *OIL TITANS: NATIONAL OIL COMPANIES IN THE MIDDLE EAST* (2006); Ryan J. Orr & Jeremy R. Kennedy, *Highlights of Recent Trends in Global Infrastructure: New Players and Revised Game Rules*, 17 TRANSNAT'L CORP. 97, 108-10 (2008); ENERGY FORUM OF THE JAMES A. BAKER III INST. FOR PUB. POL'Y AT RICE U. & PETROL. ENERGY CTR. OF JAPAN, *STRATEGIES AND INFLUENCE OF EMERGING NATIONAL OIL COMPANIES ON WORLD ENERGY MARKETS*, <http://www.rice.edu/energy/research/nationaloil/docs/PECNOCstudyprotocolfinal.pdf> (last modified July 8, 2008). In a speech at the opening of a recent Rome conference, ENI's CEO Paolo Scaroni said: "In the 1970s... the IOCs controlled nearly three-quarters of global oil reserves and 80% of production. Now they controlled 6% of oil and 20% of gas reserves, and 24% of oil and 35% of gas production. NOC held the rest. There is little sign the trend will reverse." *Resource Nationalism*, APS DIPLOMAT NEWS SERVICE, Apr. 28, 2008, available at http://findarticles.com/p/articles/mi_hb6506/is_18_68/ai_n29428955/?tag=content;coll.

also been kept at bay by increasing cooperative activities of the NOCs of the energy hungry states like China and India with their counterparts in many resource-rich countries.⁸ This phenomenon, known as NOC-NOC alliances, has been an anti-Western IOCs campaign—a further dimension of resource nationalism with a geopolitical edge.⁹ Thus, China has signed oil and natural gas agreements with Angola, Brazil, Iran, Nigeria, Venezuela, and Sudan over the past few years.¹⁰ This is a drive to ensure the steady and uninterrupted supply of oil and gas to meet their growing need. Asian NOCs such as China's China National Petroleum Corporation ("CNPC"), India's ONGC Videsh Limited ("OVL"), and Malaysia's Petronas have completely dominated Sudan's oil industry. It is remarkable that they have jointly raised national output from near 0 to 375,000 barrels per day ("bpd") within a decade. India is aggressively bidding in many resource-rich countries for control of the supply of energy. Very lately, IOC, OVL, and Oil India are reported to have been expected to invest \$4 billion in an Iranian gas field in association with National Iranian Oil Company for the purpose of liquefying the gas and exporting it to India in the form of liquefied natural gas ("LNG").¹¹ Venezuela has signed energy cooperation pacts with Angola, Syria, and China. Other Latin American NOCs have also stretched out to other countries. Brazil's Petrobras, which has enviable command of deep water technology, has invested in Libya, West Africa, the Gulf of Mexico, and South America. It has been noted, "A race for access to oil and gas began that could easily escalate into a 'new Cold War' for energy or into a 'Hot

8. Juan Vega, *China's Economic and Political Clout Grows in Latin America at the Expense of U.S. Interests*, 14 MINN. J. GLOBAL TRADE 377, 398–403 (2005); Rawi Abdelal et al., *Where Oil-Rich Nations Are Placing Their Bets*, HARV. BUS. REV., Sept. 2008, at 118, 123–24; Flynt Leverett & Jeffrey Bader, *Managing China-U.S. Energy Competition in the Middle East*, WASH. Q., Winter 2005-2006, at 187–201; David Zweig & Bi Jianhai, *China's Global Hunt for Energy*, FOREIGN AFF., Sept.–Oct. 2005, at 25–38. One article summarizes the activities of China's NOCs as follows:

China's national oil companies have invested in oil ventures in over twenty other countries in North Africa, Central Asia, Southeast Asia, Latin America, and North America. The total investment, stemming from this frantic shopping spree of buying up oil and gas fields and companies worldwide, is conservatively estimated at some US \$40B. The true figure is likely to be much greater.

David L. O. Hayward, *China's Oil Supply Dependence*, J. ENERGY SEC., June 18, 2009, <http://www.ensec.org> (follow "Archives," then follow "June 2009 Issue").

9. Stevens, *supra* note 1, at 26.

10. Rawi Abdelal & Adam Segal, *Has Globalization Passed Its Peak?*, FOREIGN AFF., Jan.–Feb. 2007, at 111.

11. In the next three to four years, OVL and its partners, Indian Oil Corporation Limited ("IOCL") and Oil India Limited, are expected to pump about \$4 billion to begin production from a gas field they discovered in offshore Iran. The Farzad gas field has in place reserves of up to 21.68 trillion cubic feet ("Tcf"), of which recoverable reserves may be 12.80 Tcf. *IOC, OVL, Oil India to Spend \$4 Billion on Iranian Gas Field*, ENERGY BUS. REV., May 1, 2009, http://oilgaspipelines.energy-business-review.com/news/ioc_ovl_oil_india_to_spend_4_billion_on_iranian_gas_field_090501/.

Resource War.”¹² The Western IOCs are thus seeing a paradigm shift in resource development in the wave of the recent round of resource nationalism, perhaps leaving them to reinvent their wheels. As it has been observed lately:

Squeezed between the twin pressures of resource nationalism and the state-sponsored NOCs of energy-hungry nations, IOCs are being locked out of the easier-to-exploit resources because NOCs can do it themselves, particularly with services companies that have technology for hire. This pushes IOCs towards conventional hydrocarbon frontiers—deep and ultra deepwater, harsh environments like the Arctic, and super-deep wells—that require cutting-edge technology. Or they can go for unconventional sources like oil sands, oil shale, ultra heavy crude, coalbed methane, or even methane hydrates, which require technological expertise that NOCs do not have.¹³

It merits here to provide some examples of resource nationalism in various resource-rich countries that will bring home the reality in the oil and gas industry. With ever-rising energy prices, Bolivia, Venezuela, and Ecuador claimed a right to a greater share in the profits of their natural resources. Bolivia enacted the Hydrocarbon Law (3058)¹⁴ in May 2005, requiring investors to alter their contracts and pay greater revenue taxes.¹⁵ In May 2006 Bolivia issued a Supreme Decree¹⁶ nationalizing the hydrocarbon sector.¹⁷ The Bolivian government thus raised its share of the sales from 50% to 82% from the biggest fields.¹⁸ In November 2001 Venezuela issued a new Hydrocarbon Law¹⁹ that prohibited private investors from owning 50% or more of the capital stock in upstream oil activities in the Orinoco Oil Belt, which is often considered to be equivalent to Saudi resources.²⁰ In early 2006 the Venezuelan government announced the mandatory conversion of the Orinoco Belt association agreements and risk profit-sharing agreements into jointly owned

12. Dietmar Dirmoser, *Energy Security: New Shortages, the Revival of Resource Nationalism and the Outlook for Multilateral Approaches*, COMPASS 2020, Aug. 2007, at 4, available at <http://library.fes.de/pdf-files/iez/05164.pdf>.

13. Ross McCracken, *IOCs, NOCs, Facing Off Over Scarcer Resources*, http://www.platts.com/Magazines/Insight/2006/december/qS2006t12l07m1m126sP33_1.xml.

14. Law No. 3058, May 17, 2005.

15. Maria V. Vargas, *Latin America: 2005 Developments in Hydrocarbon Law*, 1 TEX. J. OIL GAS & ENERGY L. 185, 185 (2006).

16. Supreme Decree No. 28,701, May 1, 2006.

17. Diego Rojas, *The Bolivian Nationalization of Hydrocarbons Process*, INT'L LEGAL NEWS, Jan. 12, 2007, http://www.imakenews.com/iln/e_article000722418.cfm?x=b11,0,w.

18. *Id.*

19. Decree No. 1,510, Official Gazette No. 37,323, Nov. 2, 2001.

20. Larry B. Pascal & Ramon A. Aspuru, *The Venezuelan Oil and Gas Sector—Are There Still Opportunities in the Era of Petronationalism?*, LATIN AM. L. & BUS. REP., June 30, 2008, at 3.

enterprises with Petroleos de Venezuela, S.A. (“PDVSA”), Venezuela’s state-owned company.²¹ The foreign investors were also required to waive any right to international arbitration and commit to resolve future disputes in Venezuelan court—a manifestation of the Calvo Doctrine.²² Faced with the prospect of losing access to one of the world’s largest oil reserves, many foreign companies such as French Total, S.A., Norwegian Statoil, the U.K.’s BP, and American Chevron²³—but not ConocoPhillips and ExxonMobil Corporation—bowed down to the government’s demands. Venezuela still continues with its nationalization plans in other sectors such as iron and steel.²⁴ Ecuador reformed its Hydrocarbon Law in April 2006 by virtue of which it required foreign oil companies to pay to the state 50% of their “extraordinary income” in the wake of increasing energy prices, and with the electoral win of President Rafael Correa that was increased to 99% by a decree.²⁵ The new constitution of Ecuador of 2008 has also subjected the access of foreign investors to international arbitration to some restrictions.²⁶

In Russia prior to 2000 about 90% of its oil production was in private hands. In the wake of the recent resource nationalism, the state-owned companies there have managed more than 80% of oil and gas production. Lately Gazprom, Russia’s state-controlled national company, has taken majority interests (51%) in Sakhalin II from the Anglo-Dutch firm Royal Dutch Shell and Kovykta under the pretence of alleged environmental violations.²⁷ Critics have labeled such sales as “forced nationalization.”

21. See Decree No. 1,510, Official Gazette No. 38,419, Apr. 18, 2006.

22. See E.A. Bastida et al., *Recourse to Arbitration in Oil and Gas Contracts in Venezuela*, 2006 OIL GAS & ENERGY L.J. 1; John Keffer & Maria V. Vargas, *Venezuela: Migrating Away from the Apertura Petrolera*, 2 TEX. J. OIL GAS & ENERGY L. 269, 278 (2007). For a discussion on the Calvo Doctrine, see Wenhua Shan, *Is Calvo Dead?*, 55 AM. J. COMP. L. 123, 159–62 (2007).

23. It has been estimated that if the contracts had remained in force, the companies stood to make an additional \$7.7 billion. See Stanley Reed & Stephen Ixer, *You’re Working for Chavez Now*, BUSINESSWEEK, May 15, 2006, available at http://www.businessweek.com/magazine/content/06_20/b3984012.htm.

24. Sarah Turner, *Venezuela Continues Along Nationalization Path*, MARKETWATCH, May 22, 2009, <http://www.marketwatch.com/story/tenaris-says-venezuela-to-nationalize-some-units>. See generally *Venezuelan Government Seizes Williams’ Operations*, WILLIAMS, May 8, 2009, <http://www.b2i.us/profiles/investor/ResLibraryView.asp?BzID=630&ResLibraryID=30017&Category=1579>.

25. See Decision of Provisional Measures, *Perenco Ecuador Ltd. v. Republic of Ecuador* (Fr. v. Ecuador), ICSID (W. Bank), Case No. ARB/08/6 at 4 (2009), available at <http://ita.law.uvic.ca>.

26. Juan Manuel Marchán, *The Treatment of Arbitration in the New Constitution of Ecuador*, NEWS AND NOTES FROM THE INST. FOR TRANSNAT’L ARB., Autumn 2008–Winter 2009, at 1.

27. *Shell’s Sakhalin II Causes Environmental and Social Damage on Sakhalin Island and Beyond*, PACIFIC ENVIRONMENT, <http://www.pacificenvironment.org/article.php?id=2876> (last visited Nov. 10, 2009).

One should not, however, lose sight of the fact that the specter of resource nationalism has not only manifested itself in the developing world but also has influenced the behavior of the resource-rich Western developed countries. In December 2005 the British government, pinched by a budget deficit, retrospectively increased, unchallenged in Parliament, the rate of tax to 50% for oil and gas producing companies in the North Sea.²⁸ It seemed to the IOCs that there was cash up for the government to grab, as creeping resource nationalism was then sweeping the world. In Canada Alberta's Finance Minister ordered in 2007 a complete review of Alberta's royalty and tax regimes with the goal of ensuring that Albertans are receiving a fair share from the energy development through royalties, taxes, and fees.²⁹ This resulted in the recommendations for increases in total government take from oil sands revenues from 47% to 64% to be implemented in 2009.³⁰ Recently, The Jakarta Post sarcastically commented, "Tax hikes in Britain and Norway are seen as more 'benign' examples of resource nationalism."³¹

Although resource nationalism is legal as a manifestation of the sovereign authority of the state, the method or the way in which it is exercised could be questionable, and in its wake could give rise to disputes between states and IOCs. The question is: How does the rule of law respond to resource nationalism in the case of such disputes when the cycle is going on? The following section examines this phenomenon.

III. RESOURCE NATIONALISM, DISPUTES, AND THE RULE OF LAW

When resource nationalism is fueled by high energy prices, the state's asserting of control over the activities of IOCs may lead to various disputes between the state and IOCs. The state's actions against or interferences with the IOC's interests could be tantamount to a breach of contractual rights, special promises, and standards of treatment, to creeping expropriation or even nationalization. Such disputes are very common in the wave of resource nationalism as has been experienced by many IOCs. The question is: To what extent does the rule of law prove to be effective? This also begs the preliminary question: What is the rule of law in the context of foreign investment? It has to be noted that the

28. See *Brown: Oil Tax is Fair*, GUARDIAN.CO.UK, Dec. 5, 2005, <http://www.guardian.co.uk/business/2005/dec/06/budget2006.oilandpetrol>; *Brown Doubles North Sea Oil Tax*, BBC NEWS, Dec. 5, 2005, <http://news.bbc.co.uk/2/hi/business/4500540.stm>.

29. Assel Amanova, *Stability of Investment Regime for Petroleum Operations in the Province of Alberta, Canada, and Kazakhstan*, 2008 OIL GAS & ENERGY L.J. 3. Canada has 174 billion barrels of oil sands, making it second only to Saudi Arabia in reserves. *Id.*

30. *Id.*

31. Hadi Soesastro, Op-Ed., *The Rise of Resource Nationalism in Indonesia*, JAKARTA POST, Sept. 13, 2007, at 7.

notion of a *rule of law* currently appears to be an evolving one, and it is often associated with such norms as development, amongst others.³² It is beyond the scope of this article to engage in that debate.

The intention in the present context is to underscore the notion as the positivistic one. The positive legal regime (in terms of the rule of law) that may be relevant for the regulation and protection of foreign investment is comprised of three layers of principles and rules, rather the three-pronged protective regime: (1) national legislation including stability agreements; (2) investment agreements between the parties; and (3) bilateral and multilateral treaties between the investor's home state and the host state where the investment is made.³³ The protection of foreign investment may be provided in relevant national legislation such as investment codes, specific legislation on investment, and stability laws that require foreign investors to enter into stability agreements with the host state for the security of investment for a specific period of time, for example 10 to 15 years. Examples abound from Latin America (i.e., Venezuela, Colombia, and Bolivia) and East Timor.

In addition to the protective regime in the host state's legislation, the investment contract between the parties by whatever name it could be known (for example, production sharing contract, joint venture, concession contract, service contract, works contract, and management contract)³⁴ often provides for various clauses such as stabilization clauses; renegotiation clauses; non-national law (for example, international law, general principles of law, and transnational law) clauses as the governing law of the contract; international arbitration clauses; compensation for expropriation, nationalization, or creeping expropriation/indirect taking clauses; and clauses for waiver of immunity of the state or state enterprise from both jurisdiction and execution.

The third prong of the protective regime is interstate treaties between the home state and the host state of the investors. There currently are about 3,000 *plus* bilateral and a few multilateral (such as the Energy Charter Treaty and the North American Free Trade Agreement) investment-protection treaties. They provide the platform for investor-state arbitration for any breach of treaty provisions by a high contracting party to the treaty (i.e., the states) against an investor from another state.

32. See generally MICHAEL J. TREBILCOCK & RONALD J. DANIELS, *RULE OF LAW REFORM AND DEVELOPMENT: CHARTING THE FRAGILE PATH OF PROGRESS* (2008); John Ohnesorge, *On Rule of Law, Rhetoric, Economic Development, and Northeast Asia*, 25 *WIS. INT'L L.J.* 301 (2007); David M. Trubek, *The Political Economy of the Rule of Law: The Challenge of the New Developmental State*, 1 *HAGUE J. ON RULE L.* 28 (2009).

33. See A. F. M. Maniruzzaman, *National Stability Laws for Protection of Foreign Investment: A Comparative Perspective*, *J. WORLD INV. & TRADE*, Apr. 2007, at 1.

34. See A. F. M. Maniruzzaman, *The New Generation of Natural Resource Development Agreements: Some Reflections*, 11 *J. ENERGY & NAT. RES. L.* 207, 210-19 (1993).

The legal regime as currently exists has been refined in its present state through practice—including legal opinions and arbitral proceedings—and arbitral jurisprudence over the last few decades.³⁵ This process has gone through several stages of refinement starting from the wave of nationalizations in the 1970s to the age of globalization fueled by the Washington Consensus in the recent past. The 1970s and 1980s resource nationalism has taught Western lawyers to fine-tune the legal tools for risk management so that foreign investors' interests are best protected. Now, several decades down the line, it begs the question: Whether the rule of law as reflected in the aforementioned legal regime has been able to play its proper and desired role in the current cycle of resource nationalism to protect foreign investors?

The answer to this question has to be a qualified one in light of the practical experience of many IOCs. It has to be acknowledged that the rule of law cannot always be a perfect protective shield in a crisis situation. There can be various geopolitical factors where the use of legal weaponry may prove riskier than the non-use of it. In the current resource nationalism in Russia and in many countries in Latin America, the governments' treatments of foreign investors or IOCs were so repugnant to the rule of law that the situations called for immediate legal remedies. As the political factors and the world market situation were not on their side, the IOCs had to bow down to the legally objectionable treatment by governments. The IOCs had to take political considerations—that energy prices were rocketing high, and resource-rich countries, as a consequence, were less willing to produce resources and to attract investment in the resource sector because of their deep pockets—in stride and realize it would be wise to bear the brunt of mistreatment by the state and accept its claim for more control rather than to lose access to resources. The motivation for not invoking the rule of law was driven by the fact that despite the slimming of their shares in resources by governments, IOCs still saw the prospect of making healthy profits through ever-increasing oil prices, which shot up to \$147 per barrel in mid-2008³⁶ from \$30 per barrel in 2003³⁷. Many companies were keen to cling to their fate whatever the circumstances, and the rule of law shield

35. There is a growing literature on the subject. *See generally* RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW (August Reinisch ed., 2008); ANDREW NEWCOMBE & LLUÍS PARADELL, LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT (2009); SERGEY RIPINSKY & KEVIN WILLIAMS, DAMAGES IN INTERNATIONAL INVESTMENT LAW (2008); STANDARDS OF INVESTMENT PROTECTION (August Reinisch ed., 2008).

36. Madlen Read, *Oil Sets New Trading Record Above \$147 a Barrel*, USA TODAY, July 11, 2008, http://www.usatoday.com/money/economy/2008-07-11-3815204975_x.htm.

37. *Will the Economy Skid on Oil?*, BUSINESSWEEK, Jan. 10, 2003, http://www.businessweek.com/bwdaily/dnflash/jan2003/nf20030110_5883.htm.

away for the time being. As ConocoPhillips and ExxonMobil Corp. declined to bow down to the demands of the Venezuelan government, they were forced to abandon their multi-billion dollar investments in Venezuela in June 2007.³⁸ They then went on to invoke the rule of law.³⁹ ExxonMobil also won court orders to freeze up to \$12 billion of Venezuela's global assets.⁴⁰ It was branded "the boldest response yet against the resource nationalism" in the current cycle, which could be an inspiration for the many multinationals that shied away.⁴¹

However, it has to be acknowledged that although at the upper end of the cycle of resource nationalism the host state might get away with anything under the banner of "oil sovereignty," it cannot be said that the rule of law is irrelevant or has no use or value.⁴² The rule of law is always an elixir in times of crisis of resource nationalism or beyond. Having recourse to it is up to the victims. Political considerations may prevail over the application of the rule of law in practical exigencies as mentioned above. However, the rule of law could operate as the sword of Damocles hanging over the perpetrator. This means that the violating state could be under the impression or pressure that once the high tide of the resource cycle recedes it would be accountable for its actions legally. Ultimately, the value of the rule of law stays dormant under the current of momentary political considerations. As the current cycle of resource nationalism is getting at its lower ebb with the downward spiral of energy prices around the world, there is the likelihood that the companies that were suppressed to bring legal actions, unlike ExxonMobil and ConocoPhillips as mentioned above, will consider ever more increasingly doing so as remedies for the breach of their rights. Even at the upper end of the cycle of resource nationalism, rule of law can proceduralize conflict and make the inevitable changes more palatable. As Professor Wälde notes:

Perhaps one can describe the function of law as one of 'smoothing' the spikes of volatility between the investor and the host state at the top end of the economic and political cycle. They slow down the

38. Kristen Hays & John Otis, *Two Oil Giants Defy Chavez: ConocoPhillips to Leave Projects in Venezuela; ExxonMobil Refuses to Sign*, HOUSTON CHRONICLE, June 27, 2007.

39. On October 10, 2007 ExxonMobil filed a request for arbitration before ICSID and, although it had been reported that ConocoPhillips continued to attempt a negotiated settlement, on December 13, 2007 it also filed a request for arbitration before ICSID. See ICSID, ICSID 08 ANNUAL REPORT 57, 58 (2008).

40. Sara Miller Llana, *Exxon Fights Chávez' Venezuela for Compensation in Courts*, CHRISTIAN SCI. MONITOR, Feb. 11, 2008, available at <http://www.csmonitor.com/2008/0211/p04s01-woam.html>.

41. *Id.*

42. *Id.* ("[In 2007] Mr. Chávez declared oil sovereignty by taking a majority stake in projects in Orinoco River Basin, which may hold the world's largest deposits of heavy crude.")

state's exploitation of dramatically increased bargaining power. They provide material to build new deals in a new architecture once the main pressure for a radical change in the relationship has evaporated. They also provide a procedure to impose costs on both sides for an exit of the investor from the country and so encourage both parties (and in particular, the politicians and the corporate executives in place towards the end of a dispute) to arrange the exit in a more civilized fashion in contrast with a rapid, violent and non-compensated expulsion. The cycle is not "neutered." But its effect is smoothed, proceduralized and delayed, with an agreed upon reasonable settlement often at the very end.⁴³

IOCs could think of some strategy well in advance before entering into a relationship with the host state that can help them manage disputes with the host state in a cycle of resource nationalism or any other time when the host state is in a stronger bargaining position. The strategy should be to develop and maintain some risk management tools that could be effective to avert or to manage the risk for which they are intended. The tools that could be developed may be both contractual and non-contractual. They could contribute to the dispute avoidance or management and help the parties continue their relationship with less hassle.

IV. RISK ENGINEERING AND DISPUTE MANAGEMENT IN RESOURCE NATIONALISM

IOCs should concentrate more on dispute management for viable business relationships. Exploration and exploitation of natural resources are not short-term options for IOCs as they involve serious commitments, including major risk-taking, financial implications, and responsibilities to various stakeholders, including shareholders and lending institutions. The following discussion briefly highlights the legal means and extra-legal means by which risk and disputes could be managed in the context of a contractual relationship between the IOC and the host state. In a recent study it has been noted: "Better-performing companies, with better political risk assessment capabilities, . . . experienced fewer cases of expropriation, government paying default, import/export license cancellation, or currency transfer restriction than other firms in [the] sample."⁴⁴

43. Thomas W. Wälde, *Renegotiating Acquired Rights in the Oil and Gas Industries: Industry and Political Cycles Meet the Rule of Law*, 1 J. WORLD ENERGY L. & BUS. 55, 86 (2008).

44. Mathew Shinkman, *The Investor's View: Economic Opportunities Versus Political Risks in 2007-11*, in WORLD INVESTMENT PROSPECTS TO 2011: FOREIGN DIRECT INVESTMENT AND THE CHALLENGE OF POLITICAL RISK 84, 94 (2007); see also Detlev F. Vagts, *Foreign Investment Risk Reconsidered: The View from the 1980s*, 2 ICSID REV.: FOREIGN INV. L.J. 1 (1987).

The parties can incorporate some mechanisms in the legal documents concerned that could avert non-commercial risks and manage disputes between the parties well in a cycle of resource nationalism. In the height of resource nationalism these mechanisms could even be valuable as a pressure mechanism. Though it might apparently fail to respond as effectively as expected in the context of various political considerations and geopolitical situations, there is no doubt that they could be a reminder to the host country that, when the resource nationalism loses its speed or recedes and the reality sinks in, these mechanisms might be activated, and the consequences would follow. These mechanisms could deter the deleterious actions by the host state against IOCs.

A. Legal/Contractual Risk-Mitigation Engineering

1. Governing Law Clause

It is well recognized that the host state can change its law at its whim, and the incorporation of the host state's law in the contract as its governing law is thus risky. As a means of averting such legal risk, it is advisable that IOCs incorporate international law or such other non-national legal systems, rules, and principles as the governing law of their contracts with host states. The advantage of this option is that it is beyond the scope of the host state's sovereign authority to change such law. It has to be recognized, however, that international law is not a self-sufficient legal system to deal with every aspect of a state contract. The practical and theoretical difficulties of the application of international law to state contracts have been discussed elsewhere.⁴⁵ The emerging popularity seems to be the application of both international law and the law of the host state, the former being the controller of the latter based on Article 42(1) of the ICSID Convention.⁴⁶ Thus, for example, the model contracts of Ghana (2000),⁴⁷ Mozambique (2000),⁴⁸ and Turkmenistan

45. See A. F. M. Maniruzzaman, *International Development Law as Applicable Law to Economic Development Agreements: A Prognostic View*, 20 WIS. INT'L L.J. 1 (2001); A. F. M. Maniruzzaman, *State Contracts in Contemporary International Law: Monist versus Dualist Controversies*, 12 EUR. J. INT'L L. 309, 309-28 (2001).

46. See generally CHRISTOPH SCHREUER, *THE ICSID CONVENTION: A COMMENTARY* 558 (2001); Emmanuel Gaillard & Yas Banifatemi, *The Meaning of "And" in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process*, 18 ICSID REV.: FOREIGN INV. L.J. 375 (2003); A. F. M. Maniruzzaman, *Conflict of Laws Issues in International Arbitration: Practice and Trends*, 9 ARB. INT'L. 371, 399 (1993); Ibrahim F. I. Shihata & A. R. Parra, *Applicable Substantive Law in Disputes Between States and Private Foreign Parties: The Case of Arbitration under the ICSID Convention*, 9 ICSID REV.: FOREIGN INV. L.J. 183 (1994).

47. Model Contract (2000) (Ghana), *Barrows*, (Article 26.1).

48. Model Production Sharing Agreement (Bid Round 2000), *Barrows*, (Article 34).

(1999)⁴⁹ represent this particular trend. There are also other options that could be found in practice, like the application of the principles common to two or more designated legal systems. Illustrations of this practice can be found in a Kuwaiti concession contract from 1967,⁵⁰ an Azeri exploration development and production sharing contract from 1999,⁵¹ and a Syrian development-and-production-of-petroleum contract from 2004.⁵² The purpose of providing for non-national legal systems or principles is to take the contract out of the influence or the jaw of the otherwise applicable national law of the host state. This could be a mechanism for the aversion of risk from change in law affecting the contract, and it could ensure stability in the contract regime.

49. Model Production Sharing Contract (1999), *Barrows*, (Article 31).

50. "The parties base their relations with regard to this Agreement on the principle of good will and good faith. Taking into account their different nationalities, this Agreement shall be given effect and must be construed and applied in conformity with the principles of law common to Kuwait and Spain, and, *in the absence of such common principles, then in conformity with the principles of law normally recognized by civilized states in general, including those which have been applied by international Tribunals.*" Dublin Tishrine Development Contract Dated 2004 for Development and Production of Petroleum Among the Government of Syria and Syria Petroleum Company and Dublin International Petroleum (Damascus) Ltd. (Tishrine and Sheikh Mansour Fields), *Barrows*.

51. Agreement on the Exploration, Development, and Production Sharing for the Block including the Padar Area and the Adjacent Prospective Structures in the Azerbaijan Republic, State Oil Co. of Azerbaijan and Kura Valley Development Co. Ltd. and Socar Oil Affiliate (Azerbaijan), Apr. 19, 1999, *Barrows*, (Article 24.1). The agreement states:

This Agreement shall be governed and interpreted in accordance with principles of law common to the law of Azerbaijan Republic and English Law, and to the extent that no common principles exist in relation to any matter then in accordance with the principles of the common law of Alberta, Canada (except for laws regarding conflicts of laws). This Agreement shall also be subject to the international legal principle of *pacta sunt servanda* (agreement must be observed).

Id. See also Agreement on the Joint Development and Production Sharing for the Azeri and Chirag Fields and the Deep Water Portion of the Gunashli Field in the Azerbaijan Sector of the Caspian Sea, State Oil Co. of the Azerbaijan Republic and Amoco Caspian Sea Petroleum Ltd., BP Exploration (Caspian Sea) Ltd., Delta Nimir Khazar Ltd., Den Norske Stats Oljeselskap A.S., Lukoil Joint Stock Co., Mcdermott Azerbaijan, Inc., Pennzoil Caspian Corp., Ramco Hazar Energy Ltd., Turkiye Petrolleri A.O., and Unocal Khazar Ltd., art. 23.1, Sept. 20, 1994, available at http://www.bp.com/liveassets/bp_internet/bp_caspian/bp_caspian_en/STAGING/local_assets/downloads_pdfs/pq/ACG_PSA.pdf; Agreement on the Exploration, Development, and Production Sharing for the Shah Deniz Prospective Area in the Azerbaijan Sector of the Caspian Sea, State Oil Co. of the Azerbaijan Republic and SOCAR Commercial Affiliate, BP Exploration (Azerbaijan) Ltd., Elf Petrol. Azerbaijan B.V., Lukoil Int'l Ltd., Oil Industries Engineering and Construction, Statoil Azerbaijan A.S., and Turkish Petrol. Overseas Co. Ltd., art. 23.1, June 4, 1996, available at http://www.bp.com/liveassets/bp_internet/bp_caspian/bp_caspian_en/STAGING/local_assets/downloads_pdfs/pq/SD_PSA.pdf.

52. "The Parties base their relations with respect to this Contract on the principles of good will and good faith. Taking into account their different nationalities, this Contract shall be given effect and be interpreted and applied in conformity with principles of law common to the SYRIAN ARAB REPUBLIC and England, and in the absence of such common principles, then in conformity with the principles of international law normally recognized including those which have been applied by international Tribunals." Syria: Model Contract for Exploration, Development & Production of Petroleum 2004: Basic Oil Laws & Concession Contracts: Middle East: Supplement 166, New York, *Barrows*, 2005.

2. Dispute Settlement Clause: Arbitration/Mediation

The provision for an international dispute settlement mechanism such as arbitration or mediation in the contract between IOCs and the host state could also be a risk management tool and a boon for stability in the contractual regime. The apprehension of IOCs or any foreign investor is quite understandable based upon the fact that the decision of the host state's court in a developing country, where legal systems are not as well developed as in the developed world, could be manipulated against the IOC's interest. The provision for an international dispute settlement mechanism is not only a safeguard against such apprehension, but also it could be a source of stability for the relationship between the parties. The third-party dispute settlement could be even more important than the governing law of the contract alone, in the sense that an international arbitral tribunal might interpret the chosen host state's law in light of international law on the basis of various international elements of the contract concerned, and thus could come up with an acceptable decision on the dispute. On the other hand, even if non-national law or international law is chosen as the governing law of the contract, a court in the host state deciding the dispute might not even give effect to that chosen law, owing to the peculiarity of the host state's legal system.

Although an arbitration clause is a waiver of sovereign immunity from jurisdiction, it does not provide immunity from execution.⁵³ The parties must provide for sovereign immunity from jurisdiction as well as from execution; otherwise, the IOC's interest may be frustrated. Although the waiver of immunity from jurisdiction by way of an arbitration clause is straightforward, special care needs to be made in drafting an effective arbitration clause that may relate to the place of arbitration and the status of the state party (especially when a state entity, representative, or state enterprise is involved on behalf of the state) to the contract.

Most important, efforts also must be made to provide for an effective and enforceable waiver-of-immunity-from-execution clause in the contract. An example of such a clause could be found in the Baku-Tbilisi-Ceyhan ("BTC") Pipeline-Azerbaijan Host Government Agreements ("HGAs"), and all other BTC HGAs in identical terms, which is worth considering, as follows:

Each state Authority hereby waives any claim to immunity in regard to any proceedings to enforce this Agreement or to enforce any

53. See Emmanuel Gaillard, *Effectiveness of Arbitral Awards, State Immunity From Execution and Autonomy of State Entities: Three Incompatible Principles*, in 4 STATE ENTITIES IN INTERNATIONAL ARBITRATION 179 (Emmanuel Gaillard & J. Younan eds., 2008); A. F. M. Maniruzzaman, *State Enterprise Arbitration and Sovereign Immunity Issues: A Look at Recent Trends*, DISP. RESOL. J., Aug–Oct. 2005, at 80.

interim or conservatory order or any final award rendered by an arbitral tribunal constituted pursuant to this Agreement, including immunity from service of process, immunity from jurisdiction of any court, and immunity of any of its property from pre-judgment attachment based on an interim or conservatory order or from execution based on a final award; provided, however, that notwithstanding anything to the contrary in this Agreement, the waiver of immunity with respect to property in this Section 17.11 shall only apply to property owned or controlled by state Authorities located outside the Territory and shall not apply to (i) property which is used or intended for use solely for the exercise of diplomatic rights, including the state's diplomatic missions, consular posts, special missions, missions to international organisations or to international conferences and including their furnishings, means of transportation and funds held in bank accounts solely for use in funding such missions, posts, organisations and/or conferences; (ii) property of a military character or used or intended for use for military purposes; (iii) property constituting or forming part of the essential cultural heritage of the state or part of its archives and not placed or intended to be placed on sale, including museums, archaeological sites and artifacts, libraries and related historical preservation and research facilities, cemeteries, monuments and other similar property; (iv) property forming part of an exhibition of objects of scientific or historical interest which is outside the Territory and not placed or intended to be placed on sale; and (v) ships and aircraft . . . used solely for governmental service⁵⁴

Mediation is not yet popular as a third-party dispute resolution mechanism in the context of investor-state disputes.⁵⁵ Although mediation has many advantages over arbitration—such as cost effectiveness, confidentiality of the process, expediency, and flexibility—state authorities or government officials try to avoid mediation due to political considerations.⁵⁶ Disputes between the host state and IOCs could

54. Host Government Agreement between and among the Government of the Azerbaijan Republic and the State Oil Co. of the Azerbaijan Republic, BP Exploration (Caspian Sea) Ltd., Statoil BTC Caspian AS, Ramco Hazar Energy Ltd., Turkiye Petrolleri A.O., Unocal BTC Pipeline, Ltd., Itochu Oil Exploration (Azerbaijan) Inc., Delta Hess (BTC) Ltd., art. 17.11, Oct. 17, 2000.

55. Stephen M. Schwebel, *Is Mediation of Foreign Investment Disputes Plausible?*, 6 TRANSNAT'L DISP. MGMT. (Mar. 2009).

56. See Jack J. Coe, Jr., *Toward a Complementary Use of Conciliation in Investor-State Disputes—A Preliminary Sketch*, 12 U.C. DAVIS J. INT'L. L. & POL'Y 7 (2005); Jeswald W. Salacuse, *Is There A Better Way? Alternative Methods of Treaty-Based, Investor-State Dispute Resolution*, 31 FORDHAM INT'L L.J. 401 (2007); Jeswald W. Salacuse, *Mediation in International Business*, in STUDIES IN INTERNATIONAL MEDIATION 219 (2002); Ucheora Onwuamaegbu, *The Role of ADR in Investor-State Dispute Settlement: The ICSID Experience*, 22 NEWS FROM ICSID 12 (2005); Lester Nurick & Stephen J. Schnably, *The First ICSID Conciliation: Tesoro Petroleum Corporation v. Trinidad and Tobago*, 1 ICSID REV.: FOREIGN INV. L.J. 340, 343 (1986); Thomas

often be politically sensitive, and that is why government officials shy away from this risk of political muddy water. It can be said that although all disputes may not be politically sensitive, there are disputes that could easily be resolved by way of mediation in order to defuse tensions between the parties.⁵⁷ In the wave of resource nationalism this method could operate as a safeguard mechanism in time of need and urgency. There could also be a combination of both the methods, i.e., mediation and arbitration, in the same proceeding. There is already a plethora of literature on the *modus operandi* of the combination of these methods.⁵⁸ In certain situations the combinations of these methods may be helpful depending on the types of disputes, and both could operate as a twin tool for risk as well as dispute management.

3. Stabilization Clause

As a safeguard measure against the state's legislative and regulatory measures, IOCs often incorporate stabilization clauses in their contracts with the state.⁵⁹ This practice is quite common to contracts entered into with developing countries and their state enterprises. This is mainly for political risk factors, as may be anticipated in developing countries. Contracts with developed countries are not usually found to include such stabilization clauses, as such political risks are not a major concern for IOCs because of the stable legal regimes available there.⁶⁰ The inclusion of stabilization clauses is not only the concern of IOCs but also of other stakeholders, including the lending financial institutions. Looking at the development of stabilization practices over the last four decades or so,

W. Wälde, *Efficient Management of Transnational Disputes: Mutual Gain by Mediation or Joint Loss in Litigation*, 22 ARB. INT'L 205 (2006).

57. See Wälde, *supra* note 56.

58. See generally David C. Elliott, *Med/Arb: Fraught With Danger or Ripe With Opportunity?*, 62 ARB. 175 (1996); Captain Fook Choon Lee, *Case History on Transnational Mediation*, 2001 ASIAN DISP. REV. 28; L. Randolph Lowry, *Mediation: Fulfilling Its Promise for Effective Dispute Resolution*, 2001 ASIAN DISP. REV. 24; A. F. M. Maniruzzaman, *The Problems and Challenges Facing Settlement of International Energy Disputes by ADR Methods in Asia: The Way Forward*, 2003 INT'L ENERGY L. & TAX'N REV. 193; *The Med-Arb Debate Continued*, 61 ARB. 111 (1995); Haig Oghigian, *Making Mediation/Arbitration Hybrid Work: A Personal Experience*, 2001 ASIAN DISP. REV. 82; Haig Oghigian, *On Arbitrators Acting as Mediators*, 68 ARB. 42 (2002); Alan Shilston, *Arb-Med? Arb-Con Is Preferable*, 63 ARB. 241 (1997); Alan Shilston, *Medarb? – Why Not Arb-Med?*, 62 ARB. 161 (1996); Peter Talbot, *Should an Arbitrator Act as a Mediator in the Same Dispute?*, 67 ARB. 228 (2001); Lord Woolf, *Mediation in Arbitration in the Pursuit of Justice*, 75 ARB. 169 (2009).

59. See A. F. M. Maniruzzaman, *The Pursuit of Stability in International Energy Investment Contracts: A Critical Appraisal of the Emerging Trends*, 1 J. WORLD ENERGY L. & BUS. 121, 121–57 (2008); A. F. M. Maniruzzaman, *Some Reflections on Stabilization Techniques in International Petroleum, Gas and Mineral Contracts*, 2005 INT'L ENERGY L. & TAX'N REV. 96.

60. See ANDREA SHEMBERG, *STABILIZATION CLAUSES AND HUMAN RIGHTS* (2008), available at <http://www.reports-and-materials.org/Stabilization-Clauses-and-Human-Rights-11-Mar-2008.pdf>.

stabilization clauses may be classified as *classic* or *modern*. The stabilization clause in a contract bears legal significance, especially for the higher amount of compensation than in the case where the clause is absent. The classic stabilization clauses aim at prohibiting the exercise of the state's sovereign authority to interfere with the IOC's interests by legislative or regulatory means, while the modern stabilization clauses attempt a balance between the state's authority to exercise its sovereign power and the contracting IOC's interests. In the latter case, it means that if the state's exercise of its sovereign authority disturbs the original balance of the contract agreed to between the parties at the time of the execution of the contract, the state authorities should maintain the original balance at all times during the lifetime of the contract by way of a predetermined formula that could be accompanied by the duty of the state to pay compensation for the loss incurred by the IOC concerned, or to negotiate with the IOC concerned in good faith to do so.⁶¹ There could also be a provision that in case of the parties' failure to reach an agreement as to how the equilibrium of the contract has to be rebalanced, recourse must be had to the third-party dispute settlement mechanism, i.e., arbitration. Furthermore, the stabilization clause should be accompanied by international law or non-national law, which may even be the *lex mercatoria* or transnational law if the parties choose it,⁶² meant to be applied specifically to the context of the stabilization clause concerned. The provision of the application of the law of the host state to the stabilization clause will not hold water in reality, as that law can be changed at will by the host state by virtue of its sovereign authority. In that respect, the stabilization clause may lose its efficacy and may not protect the expectations of the parties. However, there are views that no matter what law applies to the contract, the stabilization clause in the contract deserves its own enclave status rooted in international law, and the consequences flowing from the stabilization clause will be governed by international law, with national law having nothing to do with it.⁶³

61. See Agreement on the Exploration, Development, and Production Sharing for the Block including the Padar Area and the Adjacent Prospective Structures in the Azerbaijan Republic, *supra* note 51, art. 24.2.

62. See A. F. M. Maniruzzaman, *The Lex Mercatoria and International Contracts: A Challenge for International Commercial Arbitration?*, 14 AM. UNIV. INT'L L. REV. 657 (1999).

63. See Prosper Weil, *Les Clauses de Stabilisation ou d'Intangibilité Insérées dans les Accords de Développement Économique*, in MÉLANGES OFFERTS À CHARLES ROUSSEAU 301 (Charles Rousseau ed., 1974); Prosper Weil, *Problèmes Relatifs aux Contrats Passés entre un État et un Particulier*, 128 HAGUE RECUEIL DES COURS 101 (1969); Prosper Weil, *Droit International et Contrats d'État*, in LE DROIT INTERNATIONAL: UNITÉ ET DIVERSITÉ, MÉLANGES OFFERTS À PAUL REUTER 549 (Paul Reuter ed., 1981); Prosper Weil, *The State, the Foreign Investor, and International Law: The No Longer Stormy Relationship of a Ménage à Trois*, 15 ICSID REV.: FOREIGN INV. L.J. 401, 406 (2000); see also *Texaco v. Libya*, 52 I.L.R. 389, 447-48 ("[C]ontracts between States and private persons can, under certain conditions, come within the ambit of a particular and new branch of international law: the international law of contracts.").

Although there is limited support for this view in literature and in the arbitral jurisprudence,⁶⁴ this view is not widely regarded as authoritative. In international law, stabilization clauses have been given effect by awarding higher compensation than in the case where such a clause is found absent. Such a clause could be considered an additional weighty factor for the assessment of compensation.⁶⁵

However, it has to be borne in mind that stabilization clauses may have to be limited in effect by human rights and environmental considerations,⁶⁶ as will be highlighted later in this article in the context of corporate social responsibility.

4. Progressive Taxation/Profit-Sharing Method

In the wake of increasing oil prices in the recent past, various governments, as shown above, have taken the chance to increase their revenue by unilaterally imposing additional fiscal obligations on IOCs. Such unilateral actions of a government to increase its income in the context of increasing oil prices may even be taken despite any relevant stabilization clause, i.e., freezing clause, prohibiting it to do so.⁶⁷ A government can destabilize by its behavior the economic balance of the contract between the host state and the foreign investor and render the project unviable. During the long term of a petroleum contract, changing circumstances may have significant impact on the fiscal regime of the contract. Under the changing circumstances (e.g., oil price hikes or bonanza discoveries of new fields), the government may have to take unilateral actions in response to nationalistic sentiments and political

64. See *Revere Copper & Brass, Inc. v. Overseas Private Investment Corp.*, 56 I.L.R. 258 (1978); *Texaco v. Libya*, 17 I.L.M. 1 (1978).

65. A. F. M. Maniruzzaman, *Damages for Breach of Stabilization Clauses in International Investment Law: Where Do We Stand Today?*, 2007 INT'L ENERGY L. & TAX'N REV. 246.

66. See generally Lorenzo Cotula, *Reconciling Regulatory Stability and Evolution of Environmental Standards in Investment Contracts: Towards a Rethink of Stabilization Clauses*, 1 J. WORLD ENERGY L. & BUS. 158 (2008); Sheldon Leader, *Human Rights, Risks, and New Strategies for Global Investment*, 9 J. INT'L ECON. L. 657 (2006); Olivier de Schutter, *Transnational Corporations as Instruments of Human Development*, in HUMAN RIGHTS AND DEVELOPMENT: TOWARDS MUTUAL REINFORCEMENT 403 (Philip Alston & Mary Robinson eds., 2005).

67. See Gastón Bilder, *BOLIVIA: "Transitorily" Hikes Hydrocarbon Royalties to 82%*, 2006 OIL GAS & ENERGY L.J. 4. It has been noted:

[T]he Bolivian government increased its revenue in the wake of the oil price hike in the world market despite the fact that previous Hydrocarbons Law (section 52 of Hydrocarbon Law No. 1689) and the Shared Risk Contracts currently in effect guaranteed that 'the regime for the canon and royalties – during the term of the contracts—for the exploration, exploitation and commercialization of hydrocarbons shall remain stable.' There is no doubt that the creation of the new 32% surcharge (i.e., royalty) breached the stability guarantee set forth in the previous Hydrocarbon Law and in the Shared Risk Contracts.

Id.

pressure in the host country to increase its take, even by violating stabilization clauses to the contrary. The automatic solution to such situations could be through the development of a progressive taxation system that would operate as a built-in fiscal mechanism without needing the parties to a petroleum contract to renegotiate the deal. This will save the time and troubles of the parties for renegotiation. The progressive taxation system would operate on the basis of a predetermined equation and not as a surprise imposed by the government unilaterally. It would cater to the interests of both the parties and of the other stakeholders (e.g., lenders) involved as well.

In the progressive taxation system, a method has evolved that provides an automatic adjustment of the increased profitability of the project to the host country's share. It is known as the "economic resource rent" concept. Although originally developed in the mining industry, it is now applied to the hydrocarbon sector. In the U.K. and in Australia the method is known as the Petroleum Revenue Tax ("PRT") and the Resource Rent Tax ("RRT") respectively. In some countries it is also known as the Windfall Profit Tax, the Petroleum Profit Tax, or the Additional Profit Tax. This progressive taxation system can be found in practice in Papua New Guinea, Thailand, Russia, Kazakhstan, Tanzania, and Peru. Recently Algeria⁶⁸ and Alaska⁶⁹ have joined the league. It is not a substitute for income tax (which is payable anyway). Instead, it is an additional payment to the government based on the profits earned by the company and determined by applying a formula that has been explained by an expert in the following terms:

The tax applies if and only if in any year after the taxpayer's accumulated receipts exceeded the accumulated value of expenditure multiplied by an interest rate ("accumulation rate") which is established at a level which reflects the cost of money plus risk attaching to the industry. In any year in which such a calculation produces a positive result the surplus is taxed at the specified rate . . . [A]⁷⁰ proportion of the positive excess (not all) accrues to the government.

68. Article 101 of the Algerian Hydrocarbons Law 05-07 was amended to provide a windfall profits tax from August 1, 2006. It is assessed on earnings from oil over \$30 per barrel and is based on oil production levels. Tax varies from 5% to 50%. *Barrows*. See also the Algerian Decree (06-440) of Dec. 2, 2006: Defining Tax Rates on Windfall Profits, *Barrows*.

69. In Alaska, the Petroleum Profit Tax was promulgated in August 2006. The purpose of this tax is to increase government revenues for Alaska and at the same time provide more incentives to invest in the development of the remaining oil and gas resources. See 2006 Alaska Sess. Laws ch. 2, § 5 (codified as amended at ALASKA STAT. § 43.55.011(e)-(i) (2006)).

70. John C. Kinna, *Investing in Developing Countries: Minimisation of Political Risk*, 1 J. ENERGY & NAT. RES. L. 89, 98 (1983). See also Ross Garnaut & Anthony Clunies Ross,

However, issues may arise in regard to various aspects of this method such as the triggering rate of return, the *accumulation rate* to be applied, and the formulation and administration of the system. There are no straightforward answers to these issues as the relevant circumstances may vary. A practical solution needs to be found by taking into account variable factors such as the nature of the project, field-by-field variations in the same country, and relevant practices in other countries.

The main advantage of this progressive taxation system is the stability of the parties' contractual relationship, as the state party does not need to take any unilateral action to increase its take when windfall profits accrue. It gives the fiscal regime the needed flexibility in changed circumstances for the viability of the project.

For the long-term stability of the contractual relationship between a state and an IOC, the progressive taxation system, as discussed above, could prove a very useful tool.

5. Political Risk Insurance

In order to avert political risks, IOCs can take out insurance coverage for those risks. A growing number of government-sponsored agencies and commercial organizations now offer insurance against political risks such as breach of contract, the expropriation of property, currency inconvertibility, political violence, and others.⁷¹ Among the government-sponsored agencies are the U.S. Overseas Private Investment Corporation ("OPIC") and the World Bank's Multilateral Investment Guarantee Agency ("MIGA"). Furthermore, investment-insurance programs similar to that of the OPIC and MIGA may be available from export credit agencies ("ECAs") in many countries including some developing countries. However, such programs may be subject to respective national objectives, which may impose strict requirements for eligibility. There are also a number of private insurers such as the American International Group, Lloyds of London, Sovereign Risk Insurance Limited, Chubb, and Zurich Emerging Markets Solutions, which offer comparative alternatives. There are, however, comparative

Uncertainty, Risk Aversion and the Taxing of Natural Resource Projects, 85 *ECON. J.* 272, 284–85 (1975).

71. See INTERNATIONAL POLITICAL RISK MANAGEMENT: LOOKING TO THE FUTURE (Theodore H. Moran & Gerald T. West eds., 2005); INTERNATIONAL POLITICAL RISK MANAGEMENT: NEEDS OF THE PRESENT, CHALLENGES FOR THE FUTURE (Theodore H. Moran et al. eds., 2008); NOAH RUBINS & N. STEPHAN KINSELLA, INTERNATIONAL INVESTMENT, POLITICAL RISK, AND DISPUTE RESOLUTION: A PRACTITIONER'S GUIDE ch. 3 (2005); Jennifer M. DeLeonardo, *Are Public and Private Political Risk Insurance Two of a Kind? Suggestions for a New Direction for Government Coverage*, 45 *VA. J. INT'L L.* 737 (2004); S. Linn Williams, *Political and Other Risk Insurance: OPIC, MIGA, Eximbank and Other Providers*, 5 *PACE INT'L L. REV.* 59 (1993).

advantages and disadvantages of the public and private sources that IOCs are to weigh for their individual requirements and situations. In such private insurance programs various types of political risk coverage may be found: Confiscation, Expropriation, Nationalization and Deprivation (“CEND”) risks, Forced Abandonment and Selective Discrimination, and terrorism and political violence.⁷²

B. Risk and Dispute Management Strategy

Apart from the legal tools for the management of risks mentioned above, there also could be extra-legal tools that can be used for risk and dispute management as well as for dispute avoidance. In this process a balance could be struck between economic and social concerns of host countries and the profit-making purpose of IOCs. Among the extra-legal tools one may mention the following: (1) equity participation by the host government; (2) taking care of the social, environmental, and health needs of the host community; (3) involvement of various stakeholders in the project (transparency); (4) early detection and prevention mechanism for disputes; and (5) involvement of international financial institutions upon which the host state’s future development budget depends.

1. Equity Participation by the Host Government

Equity participation by the host government is diplomatically and strategically important for both risk management and dispute avoidance. In times of crisis or in the wave of resource nationalism, the host state’s ownership in the project could prove to be a shield against the unilateral action by the host state, lest the project be unprofitable and the unilateral action be potentially dangerous for the project. Since the state has some interest at stake, it will try to guard it by all means. If it fails to do so, the government could be confronted with the political risk of its own fate. This measure seems to have an appeal in the infrastructure industry, especially for projects that are politically sensitive.⁷³ As far as the energy

72. George Joffé et al., *Expropriation of Oil and Gas Investments: Historical, Legal and Economic Perspectives in a New Age of Resource Nationalism*, 2 J. WORLD ENERGY L. & BUS. 3, 12–13 (2009). Forced abandonment means, “An insured being forced to abandon the insured interests because of the host country’s actions.” *Id.* Selective Discrimination means:

The passing of a law, etc. by the host government which has to be ‘selectively and discriminately’ applied against the project or the insured and which either ‘expressly and selectively’ prevents or restricts the operation of the project so as to the cause the ‘permanent and total’ cessation of the project’s activities, or which legally prevents the insured from participating in the benefits of the project.

Id. at 13.

73. There happens to be a trend in private projects of increasing equity sharing between private investors and government sponsors. For example in East Asia, there is a slight trend of increasing co-ownership—from 50% of projects in 1990 to 65% of projects by 2004—while in

industry is concerned, equity participation by the transit country in oil and gas pipeline projects is worth considering for the purposes of risk management and dispute avoidance.⁷⁴

2. Corporate Social Responsibility: Social, Environmental, and Health Considerations for the Host Community

Although the Equator Principles, sponsored by the International Finance Corporation (“IFC”), have been applied by financial institutions to manage social (which includes both health and human rights issues) and environmental issues in project finance, IOCs need to consider these aspects and other related ones to reflect them in their contracts with the host state.⁷⁵ Such practice is found in some limited spheres, though it is not yet ubiquitous.⁷⁶ These aspects could be factored into IOC’s corporate social responsibility (“CSR”) program, which could, in turn, be used as a risk management as well as a dispute avoidance tool.⁷⁷ This notion of CSR has to be understood in the sense that, as opposed to the prevailing approaches to it,⁷⁸ CSR is a business opportunity as well as a

Africa co-ownership appears to have decreased markedly—from 50% of projects in 1990 to 25% of projects by 2004. See Kassia Yanosek et al., *Emerging-Market Infrastructure Investors: New Trends for a New Era?*, J. STRUCTURED FIN., Winter 2007, at 6.

74. See PAUL STEVENS, TRANSIT TROUBLES: PIPELINES AS A SOURCE OF CONFLICT (2009), available at http://www.chathamhouse.org.uk/files/13571_r0309_pipelines.pdf.

75. The Equator Principles address the problem of the Environmental and social impacts, which large infrastructure and resource projects could have on local communities.

76. See generally BTC Co., BTC PROJECT ENVIRONMENTAL AND SOCIAL ANNUAL REPORT (OPERATIONS PHASE) 2008, available at http://www.bp.com/liveassets/bp_internet/bp_caspian/bp_caspian_en/STAGING/local_assets/downloads/pdfs/e/2008_BTC_annual_environment_and_social_report.pdf; INT’L FIN. CORP., INTRODUCTION TO HEALTH IMPACT ASSESSMENT (2009), available at [http://www.ifc.org/ifcext/sustainability.nsf/AttachmentsByTitle/p_HealthImpactAssessment/\\$FILE/HealthImpact.pdf](http://www.ifc.org/ifcext/sustainability.nsf/AttachmentsByTitle/p_HealthImpactAssessment/$FILE/HealthImpact.pdf); INT’L FIN. CORP., PERFORMANCE STANDARDS ON SOCIAL & ENVIRONMENTAL RESPONSIBILITY (2006), available at [http://www.ifc.org/ifcext/sustainability.nsf/AttachmentsByTitle/pol_PerformanceStandards2006_full/\\$FILE/IFC+Performance+Standards.pdf](http://www.ifc.org/ifcext/sustainability.nsf/AttachmentsByTitle/pol_PerformanceStandards2006_full/$FILE/IFC+Performance+Standards.pdf); SHELL INT’L LTD., SHELL GENERAL BUS. PRINCIPLES (2005), http://www-static.shell.com/static/aboutshell/downloads/who_we_are/sgbps/sgbp_english.pdf; Shell, Social Investment, http://www.shell.com/home/content/my-en/society_environment/dir_socialinvestment_0313.html (last visited Nov. 10, 2009). Shell’s commitment to social investment is stated:

Contributing to society through corporate citizenship or social investments has become a major focus in the company’s efforts to demonstrate our commitment to the society in which we operate. Shell looks for opportunities to contribute positively to the goals of society and add social value in ways that will impact positively on our business. Very often our social investment programmes are run in partnership with other private, voluntary and community-sector organisations based on shared objectives, common approaches and complementary resources.

Id.

77. See Beth Kytte & John Gerard Ruggie, *Corporate Social Responsibility as Risk Management: A Model for Multinationals* (Corp. Social Responsibility Initiative of the John F. Kennedy Sch. of Gov’t, Harv. Univ., Working Paper No. 10, 2005).

78. JENNIFER A. ZERK, MULTINATIONALS AND CORPORATE SOCIAL RESPONSIBILITY: LIMITATIONS AND OPPORTUNITIES IN INTERNATIONAL LAW 29–32 (2006) (describing various understandings of CSR).

business strategy, rather than a business cost or burden.⁷⁹ Although CSR has not yet established international legal obligations for multinational corporations (“MNCs”) with respect to human rights,⁸⁰ it could at best be considered based on moral imperatives and ethics.⁸¹ The prevailing approaches to CSR have failed to appreciate the interdependence of business and society; rather, they have focused on the tension between them.⁸² The prevailing approaches have neither added credibility to MNCs’ operations nor much well-being to the host community or society where they operate. The root cause could be attributed to the corporate attitude as reflected in the Friedmanite view of the social responsibility of business.⁸³ There is thus a need for the integration of business and society so that they can benefit from each other. As Porter and Kramer note, “The essential test that should guide CSR is not whether a cause is worthy but whether it presents an opportunity to create shared value—that is, a meaningful benefit for society that is also valuable to business.”⁸⁴ From a pragmatic point of view, if business needs to gain any reputation and make any impression on society for its long-term interests, business needs to engage meaningfully with society, which is more than just showcase philanthropy, public relations, and glossy CSR reporting. Companies’ meaningful engagements with the host society may provide an opportunity to develop much needed mutual trust and long-term cooperation between them.⁸⁵ Of course, how much engagement is not too much could be determined on a case-by-case basis. The World Economic Forum has developed a framework to help business leaders in this regard. As its Executive Chair, Klaus Schwab, sums it up:

The framework developed by the forum encourages the stakeholder approach to corporate engagement and refers to this as “corporate

79. See Michael E. Porter & Mark R. Kramer, *Strategy and Society: The Link Between Competitive Advantage and Corporate Social Responsibility*, HARV. BUS. REV., Dec. 1, 2006, at 78, 80.

80. See Special Representative of the Secretary-General, *Report of the Special Representative of the UN Secretary-General on the Issue of Human Rights and Transnational Corporations and the Other Business Enterprises delivered to the Human Rights Council*, U.N. Doc. A/HRC/8/5 (Apr. 7, 2008); Larry Catá Backer, *Multinational Corporations, Transnational Law: The United Nations’ Norms on the Responsibilities of Transnational Corporations as a Harbinger of Corporate Social Responsibility in International Law*, 37 COLUM. HUM. RTS. L. REV. 287 (2006).

81. See generally Peter Singer, *Can Business be Ethical?*, PROJECT SYNDICATE, 2009, http://www.project-syndicate.org/print_commentary/psinger49/English.

82. Porter & Kramer, *supra* note 79, at 83.

83. MILTON FRIEDMAN, *CAPITALISM & FREEDOM* 133 (1962) (“[T]here is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud.”).

84. Porter & Kramer, *supra* note 79, at 84.

85. Jeffrey D. Sachs, *Addressing Political Risk in the Energy Sector*, in *WORLD INVESTMENT PROSPECTS TO 2011: FOREIGN DIRECT INVESTMENT AND THE CHALLENGE OF POLITICAL RISK* 80, 81–82 (Laza Kekic & Karl P. Sauvart eds., 2007).

social responsibility.” This involves how a corporation responds to the expectations of its stakeholders—the wide community of all the organizations and individuals that are in any way affected by or interested in its actions: shareholders, owners, investors, employees, suppliers, clients, consumers—while trying to increase the company’s value. Corporate social responsibility means addressing the wider financial, environmental, and social impact of all that a company does. It entails minimizing the negative effects of the actions of a company and maximizing the positive ones on stakeholders as well as on the communities in which the enterprise operates and the governments with which it must work.⁸⁶

CSR is now the reality facing IOCs, or any big business for that matter, and it must be handled professionally. There appears to be a universal moral consensus, though not legal yet, that companies owe some duties to the host society. The U.N. Global Compact, launched in 1999, has now articulated ten core principles to guide companies in their business activities that relate to human rights, the environment, labor issues, and anti-corruption.⁸⁷ More than 3,000 companies in about 120 countries have signed up to the U.N. Compact, and they are committed to self-assessment against those principles on a voluntary basis. Although the principles on those aforementioned aspects are not legally binding, they bear a moral force behind them that has joined this huge number of sponsors together. There will be a time when all ten core principles of the U.N. Compact could be part and parcel of CSR with a greater degree of legitimacy. In due course, many principles will have to be further refined in order to conceptualize CSR and accommodate in it the relevant pressing issues of the days ahead, such as companies’ duties for climate change (i.e., climate responsibility), sustainable development, and socially responsible investment.⁸⁸ It is not surprising that many IOCs are

86. Klaus Schwab, *Global Corporate Citizenship: Working with Governments and Civil Society*, FOREIGN AFF., Jan./Feb. 2008, at 107, 113.

87. See U.N. GLOBAL COMPACT OFFICE, CORPORATE CITIZENSHIP IN THE WORLD ECONOMY: UNITED NATIONS GLOBAL COMPACT (2008), available at http://www.unglobalcompact.org/docs/news_events/8.1/GC_brochure_FINAL.pdf.

88. Bjorn-Tore Blindheim, *Corporate Social Responsibility: The Economic and Institutional Responsibility of Business in Society*, in ARCTIC OIL AND GAS: SUSTAINABILITY AT RISK 57 (Aslaug Mikkelsen & Oluf Langhelle eds., 2008). For more on climate responsibility and an examination of the current and future duties of companies in affecting climate change, see generally NICHOLAS STERN, A BLUEPRINT FOR A SAFER PLANET: HOW TO MANAGE CLIMATE CHANGE AND CREATE A NEW ERA OF PROGRESS AND PROSPERITY (2009); ARCTIC COUNCIL, OIL AND GAS GUIDELINES (2009), available at <http://arctic-council.org/filearchive/Arctic%20Offshore%20Oil%20and%20Gas%20Guidelines%202009.pdf>; MICHAEL A. LEVI, THE CANADIAN OIL SANDS: ENERGY SECURITY VS. CLIMATE CHANGE (2009), available at http://www.cfr.org/content/publications/attachments/Oil_Sands_CSR47.pdf; PER MICKWITZ ET AL., CLIMATE POLICY INTEGRATION, COHERENCE, AND GOVERNANCE (2009), available at http://www.peer.eu/fileadmin/user_upload/publications/PEER_Report2.pdf. For an examination of sustainable development, see Oluf Langhelle et al., *Framing Oil and Gas in the Arctic from a*

nowadays making an effort to engage meaningfully with the host society in different degrees for a better relationship for their future prospect.⁸⁹ As one commentator noted, “Projects that fail either the developmental or environmental imperatives are bound to fail politically in the long term.”⁹⁰

3. Transparency

In a recent study, two authors concluded that:

The wisest and most committed foreign investors cannot rely entirely on external guarantees of property rights, whether they are reformed or not. Turning to an improved system of dispute resolution is still likely to strain business relationships. Ultimately, security for most investors lies in how a particular project is perceived by its hosts—by government officials, but also in a democratic Third World by the press, labor, and nongovernmental organizations [(“NGOs”)].⁹¹

Transparency of corporate activities could heal many grievances of corporate stakeholders (i.e., the host government, the shareholders, the host community, and NGOs, among others), and it may be a boon for the security of corporate investment. It is worth remembering the adage: “Sunshine is the best antiseptic.” Many of the misunderstandings between IOCs and their stakeholders could be allayed in a transparent process of IOCs’ operations in the host country. Methods of such transparency have often been suggested in various forums such as: (1) inclusion of representatives of various stakeholders in the project-planning, decision-making, and negotiating processes, and (2) full disclosure of all contractual terms and all payments between host country and the investment companies.⁹² As has been observed in a recent

Sustainable Development Perspective, in ARCTIC OIL AND GAS: SUSTAINABILITY AT RISK 15 (Aslaug Mikkelsen & Oluf Langhelle eds., 2008) (examining oil and gas sustainability issues in the Arctic); and see generally LYUBA ZARSKY, INTERNATIONAL INVESTMENT FOR SUSTAINABLE DEVELOPMENT: BALANCING RIGHTS AND REWARDS (2005). For an examination of socially responsible investments by companies, see generally BENJAMIN J. RICHARDSON, SOCIALLY RESPONSIBLE INVESTMENT LAW: REGULATING THE UNSEEN POLLUTERS (2008); ELIZABETH ULMAS, HUMAN RIGHTS AND SRI IN NORTH AMERICA: AN OVERVIEW (2009), available at <http://www.reports-and-materials.org/Umlas-Human-Rights-and-SRI-Jan-2009.pdf>.

89. See, e.g., ROYAL DUTCH SHELL PLC, SHELL GENERAL BUSINESS PRINCIPLES (2005), available at http://www.shell.com/home/content/aboutshell/who_we_are/our_values/sgbp/sgbp_30032008.html (follow “English”); see also Mahdi Zahra & Abdullahi Shehu, *Environmentalism Versus Oil Nationalism in the Niger Delta: Current Concerns and Dilemma of the Multinational Oil Industry*, 2006 OIL GAS ENERGY L.J. 3.

90. Sachs, *supra* note 85, at 82.

91. LOUIS T. WELLS & RAFIQ AHMED, MAKING FOREIGN INVESTMENT SAFE: PROPERTY RIGHTS AND NATIONAL SOVEREIGNTY 298 (2007).

92. The need for full disclosure of contractual terms is exemplified by the fact that:

The ultimate source of contractual instability in Russia, Bolivia, and many other countries, is not arbitrary host-country behaviour but rather the lack of legitimacy of

Harvard study: “Proponents of corporate environmental and social transparency argue that voluntary disclosure of corporate practices is an important step toward greater corporate engagement with stakeholders and more democratic corporate governance.”⁹³

There is no denying that it is human nature that mutual communications among individuals cannot harbor any doubt or at least can minimize it. Thus, transparent dealings between IOCs and the concerned stakeholders would deter many misgivings between them, avoid many social and political risks, and thereby prevent disputes between them. In an age of rising shareholder activism and engagement,⁹⁴ however, fueled by the global financial crises due to the irresponsible activities of international banks and financial institutions, IOCs or any investing companies will have to be more transparent than ever and cannot be content with the attitude “business-as-usual.”

4. Early-Detection-and-Prevention Mechanism for Disputes

Many trivial disputes, when spiraling out of control, could often be very risky for IOCs in terms of business and the relationship with the host state. Prevention is better than cure. To use a healthcare metaphor: major health problems may not develop if minor ailments or health problems could be, at the very inception, prevented or effectively dealt with. Similarly, in the case of oil and gas projects, there should be mechanisms in place that would work like radar for early detection of grievances or disputes as well as prevention mechanisms. In this respect, IOCs need to be proactive and understand the cultural milieu in which they operate. Disputes might have a gestation period to develop, or there may be an abrupt outbreak. Whatever their nature, early detection mechanisms would help management determine what to do in the situation. Efforts must be made to resolve any problem amicably between the parties before it escalates into a dispute. Such an approach may be better described as dispute management rather than dispute settlement. Once the problem hardens as a dispute, there could still be a chance for early

the contractual process in the first place. The negotiations between investors and the state are habitually secret, and the resulting terms are almost always secret as well. An air of corruption hangs heavily over most deals. The public has no confidence in the legitimacy of the investor-state relationship.

Sachs, *supra* note 85, at 81.

93. Erin M. Reid & Michael W. Toffel, *Responding to Public and Private Politics: Corporate Disclosure of Climate Change Strategies* (Harv. Bus. Sch., Working Paper No. 09-019, 2008); see also David Hess, *Social Reporting and New Governance Regulation: the Prospects of Achieving Corporate Accountability Through Transparency*, 17 BUS. ETHICS Q. 453 (2007).

94. See BENJAMIN J. RICHARDSON, *SOCIALLY RESPONSIBLE INVESTMENT LAW: REGULATING UNSEEN POLLUTERS* 180–85, 468–70, 502–04 (2008); see also Reid & Toffel, *supra* note 93.

settlement by way of mediation before it goes beyond control as a political football and attracts lots of publicity. In a case where oil and gas are the state's main source of national revenue, such political repercussions are not out of the question. Once the dispute reaches a certain point and has lost the chance of an early resolution, there may not be any turning back. So, early dispute management could be a blessing for IOCs in terms of their saving many hundreds of hours of corporate management time that could be wasted away in arbitration or litigation. The overall outcome for the parties concerned in the early detection process will be a win-win situation.

Perhaps employing people from different social groups and communicating with them on a regular basis about the impact of the IOCs operations in a particular locality would keep the management well-informed of what is happening on the ground on a day-to-day basis. A sign of stress reflected on the host community by the presence of the IOC could be a ground for discussion and dialogue with their representatives and thus could defuse any tension that might be existing at a given time. Depending on the situations, the IOC might figure out what needs to be done to avert any forthcoming dispute.

5. Involvement of International Financial Institutions

As investment in developing countries is prone to political risk, it may be a good idea to involve international financial institutions like the World Bank, the Asian Development Bank, and other similar institutions, as deemed appropriate, as guarantor, lender, or investor in the project. The reason why this could help manage and minimize political risk is that the host government would think twice before inflicting any injury to the IOC as it might jeopardize the project that, in turn, could upset the influential financial institutions involved. Indeed, the World Bank and the regional developmental banks can wield enormous influence on developing countries, which often rely on those banks for the financing of their development programs. It may happen that by upsetting these institutions the government of a country might face political risk for its own fate for being unable to get as much development aid as the public expected.

V. CONCLUSION

In the above discussion I examined the nature and the forces that mold resource nationalism. I have examined the role of the rule of law in the context of resource nationalism and outlined some legal and extra-legal devices that could minimize the risk of resource nationalism and help manage dispute in a mutually beneficial way for both the parties, i.e., the

host state and an IOC. I have also indicated how a balance of interests could be maintained between the interested parties in the oil and gas industry. Lawyers' roles in the matter of extra-legal devices should be beyond their traditional roles as an adviser, drafter, negotiator, and litigator. Lawyers' professional duties should be meant to add value to their clients' work or business.⁹⁵ Although the world is increasingly looking toward alternative and renewable energy resources, fossil fuels will remain with us for a while, and demand for it will be increasing for a considerable time ahead.⁹⁶ Thus, we cannot leave the current scenery of oil and gas overnight. Lawyers will be involved in their clients' oil and gas business for many years to come. They can add value to their business clients' work when they can contribute to the resolution of their business problems. This can only be possible when lawyers can engineer their legal knowledge toward the resolution of business problems. In real life, lawyers seem to perform extra-legal or often moral duties for clients who come from various walks of life. Professor Susskind makes an interesting observation of the roles of lawyers in real life situations:

Private client lawyers (for example, those who advise on divorces or draft wills) tell me that their job is not really about the law; rather, they insist, they are experienced counsellors, confidantes, therapists even, in whom their clients have unwavering faith in relation to their personal problems. In similar vein, litigators say that their primary role in life is that of project manager rather than provider of legal advice; corporate lawyers claim to be deal-makers and negotiators much less than legal draftsmen; capital market lawyers suggest they are transaction managers rather than gurus of finance law; in-house lawyers maintain they are risk managers more than legal counsellors; banking lawyers assert their clients come to them not for legal advice but for their market knowledge; and high street solicitors insist that they rarely undertake legal research. Even judges say that they are

95. See Ronald J. Gilson, *Value Creation by Business Lawyers: Legal Skills and Asset Pricing*, 94 YALE L.J. 239 (1984).

96. Oil today accounts for 35% of global energy supply—the largest share of any form of energy. In 2008 world oil demand was 85.2 million bpd. IHS Cambridge Energy Research Associates estimates global oil demand in 2035 could range from 97 million bpd to 113 million bpd. One article goes on to state:

[D]espite increased emphasis on alternative energies, the predominant sources of energy worldwide for decades to come will continue to be oil, natural gas, and coal. Crude oil prices have tripled since 2002 and show no signs of reverting to earlier levels (from the last oil boom to the early 2000s, prices remained below \$30 per barrel). Global demand for oil remains strong and will increase even more to accommodate rapid growth in China, India, and other emerging markets.

Abdelal et al., *supra* note 8, at 121.

becoming . . . case managers.⁹⁷

Lawyers' professional duties, thus, cannot be confined merely to giving legal opinions, negotiating and drafting contracts, and litigating disputes. There should be more to it. Whatever sophisticated drafting techniques and skillful wording of a contract is invented, the desired goal may not be realized in changing circumstances over the long life of the contract, especially in the extractive industry. What is required is not only the legal skills of lawyers but also their foresightedness, practical knowledge, and wisdom to devise certain mechanisms that could help their clients, like IOCs, through the rough times, such as a period of resource nationalism, which tend to turn up in a cyclical order. This will add value to IOCs' business. As is well known, business people look forward to resolving business problems, and lawyers look forward to resolving legal problems. If these two functions could be merged as far as possible into the lawyer's role, the lawyer would be considered a value-creating entity for businesses and not just as an unproductive troublemaker. In order to protect the interests of their clients in the best possible ways, lawyers need to be creative in their tasks, perceptive of probable risks and uncertainties for their business clients, and devise solutions while drafting and negotiating international petroleum contracts. The extra-legal devices that lawyers can contribute, along with their legal and practical skills, to the creation of trust and good faith between the parties, may lubricate the wheels of commerce and thereby suppress disputes.⁹⁸ In this respect a lawyer is more than a lawyer as may be increasingly expected in today's world of business. As Sir Walter Scott once said:

“A lawyer without history or literature is a mechanic, a mere working mason; if he possesses some knowledge of these, he may venture to call himself an architect.”

97. Richard Susskind, *How the Traditional Role of Lawyers Will Change*, TIMES ONLINE, Nov. 5, 2007, <http://business.timesonline.co.uk/tol/business/law/article2522535.ece>; see Charles Fried, *The Lawyer as a Friend: The Moral Foundations of the Lawyer-Client Relation*, 85 YALE L.J. 1060 (1976).

98. Mark C. Suchmann & Mia L. Cahill, *Hired Gun as Facilitator: Lawyers and the Suppression of Business Disputes in Silicon Valley*, 21 LAW & SOC. INQUIRY 679, 680 (1996).