Argentina's Exploration Plan: The Return of Exploration Permits and Exploitation Concessions

By Luis A. Erize*

Introduction

The new oil and gas exploratory programme for Argentina, anticipated by President Menem on October 20, 1991 at the 13th World Petroleum Congress Opening Ceremony, and, later on, in Houston, on November 14, is now finally launched, as from March 31, 1992. Introductory seminars, presided over by the Secretariat for Hydrocarbons and Mining, and organized jointly by Intera Information Technologies and Cullen, Valdez Rojas y Asociados S.A., were held in London (March 18) and Houston (March 24) referring to the economics, geology, taxation and legal framework related to the project. The Argentine Exploration Plan is a clear example of the market oriented economy the government has decided to set as the new business environment, open to international corporations.

The legal status of the exploration programme and of the Hydrocarbons Law

The legal framework is Decree 2178/91, of October 21, 1991, published in the Official Gazette on November 21 ("Decree"), implementing the Hydrocarbons Law, No. 17,319, enacted in 1967. The Hydrocarbons Law ("HL"), on which the Argentina Plan is based, was thought of as a manifold instrument, allowing the enforcement of different oil policies: (i) *either* production sharing or service contracts entered into with YPF, the state-owned oil company, *or* (ii) exploration permits and exploitation concessions granted to the private sector. After an initial call for bids in 1967, the HL, issued by a military government, was not used since for the grant of concessions such as the ones now considered. The law was instead extensively applied by the previous Alfonsin government with the Houston Plan launched in 1985, superseded now by the new, much bolder, Argentina Plan.

The HL is valid and in force, as the Supreme Court has since long established that a validation of a "law" enacted by the military government may be the result of any confirmation whatsoever by any of the powers stemming from a democratic government. This doctrine by the Supreme Court was once more affirmed in the case of *Godoy,* December 27, 1990. The Supreme

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Court has thus made a more ample construction of the acknowledgement of the legal status of laws enacted during military governments. The previous doctrine from the Supreme Court, while accepting the validity of such "laws", had nevertheless requested such acts to be ratified or validated by Congress, either expressly or implicitly.[1]

This is precisely the case for the HL, as the legislative power thereafter passed laws that regulate certain aspects of the HL, therefore confirming its status as a law. Law 23678, enacted in June, 1989, reestablished the scheme previously set forth by Decree 631/87, on royalties computation (that had been set forth in the HL), and its allocation to the provinces. Later on, Law 23697, sections 32 to 34, amended partially Law 23678 an4 was reversed by Law 23897. This frequent reference by the legislature to aspects dealt with by the HL evidences its legislative status. Because of the validation of the HL by the laws mentioned above, the HL is valid according to any of the standards dealt with by the Supreme Court since the democratic government took office.

The past: exploration and exploitation 1967—1989

Following the HL's second alternative, that allowed the Executive to entrust the private sector with the exploration and exploitation of oil and gas, 20 exploration permits were awarded at the end of the 1960s.[2]

No new exploration permits according to the HL were granted thereafter, and it was only after Law 21778 (the Risk Contracts Law — 1978) that exploration was resumed by the private sector. This law set forth a legal framework different from the one set forth by the HL for the exploration and exploitation of oil and gas, through "risk service contracts", establishing (a) specific exploration periods; (b) work commitments (seismics — exploratory wells); and (c) once a commercial oil discovery was made, obligations to deliver to the government the oil and gas produced at the given price, adjusted according to variation formulas mixing international crude oil prices and local inflation factors, *etc.* Payment in kind to the private sector company could be requested by it only after a presidential decree declaring that an adequate level of supply and reserves had been reached for domestic purposes, allowing for export of the surplus.

The Houston Plan *(1985)* established services contracts for the exploration and, if successful, exploitation of oil and gas, with specific exploration and exploitation periods, different from those established in the Risk Contracts Law or in the HL. Work commitments were set forth (seismic options or exploratory well).

The contractor had to (i) request the government's approval in case of commercial oil discovery; (ii) after that, offer to YPF up to *50* per cent. participating interest in a joint venture upon reimbursement of the share in some of the costs incurred; (iii) deliver to YPF all the crude oil produced, at international oil prices for equivalent oil with a 20 to 30 per cent. discount for royalties and fees to be paid to YPF; (iv) receive only part of said price in US dollars at the official market rate, and the balance in local currency;

[1] *Soria, Silverio F.* v. *Dirección Nacional de Vialidad,* CS, April 2, 1.985, *La Ley,* Buenos Aires, Vol. 1985-D, p. 324. For a round up of the various stages of the Supreme Court's doctrine, up to 1990, see Alfredo Augusto Keisinan, 'De facto laws in the Court Jurisprudence

Present Trends", *La* Ley, vol. 1990-C, p. 853.

[2] For more details, see the 1969 *Oil & Gas Report,* issued by the office of the President an official publication relative to these ventures. Though seismic lines were run and explanatory wells drilled, no discoveries were made, and all the areas were relinquished.

and (v) receive payment in kind only in case of YPF's payment default (besides Decrees 1443/85 and 623/87, Decree 127/87 referred to this guarantee). About 70 "Houston" contracts were signed. In 64, investments have been made; 12 areas were relinquished — plus another two, partially, and about 13 remain in the exploratory stage. Most of the work units programmed were executed in the case of seismics; less, in the case of exploratory wells. The last call, at the end of 1989, under the Houston Plan, proved to be unsuccessful, as few companies turned up.

These "Houston" contracts can be appropriately labeled as "service contracts" or "risk service contracts" whereby the contractor is paid in cash for the oil produced, even if the contractor is the one that finances the development with risk capital. The Houston Plan kept for YPF the option to join the contractor in a joint venture in a sort of production sharing formula, but no sliding scale for different levels of production was considered.[3]

Decree *1589/89* gave the option (section 1) to contractors of the Houston Plan to amend their contracts according to the new deregulation in order to have free disposal of the crude oil produced when a commercial discovery was made, and Decree 2411/91 gave YPF power to renegotiate with them, as well as with the risk service contractors of Law 21778, for the conversion of such contracts into exploration permits and exploitation concessions under rules similar to the ones established in the Argentina Plan.

The property in oil and gas produced reverts to the exploitation concession holder according to section 6, HL (section *5,* Decree 2411/91, reproducing section 6, .HL, with more precise language than the one adopted in the Decree), and a special suspension of the obligatory relinquishment of the areas not in production may be requested for up to five years until transport and market are assured.

Practically all the rules set forth under the Argentina Plan are reproduced in this Decree for the contracts thus converted, though certain "enhancements" for the! ex-contractor are granted with respect to the Decree provisions.[4] I

[3] The sliding scale formula applicable in other countries is described by Alfred J. Boulos, in "Mutuality of Interest Between Companies and Governments — Myth or Fact?" International Bar Association *Energy Law '9O,* (1990), at p 20.

[4] *E.g.* payments in kind on account of royalties may be effected by delivery to the federal government, instead of to the provinces, in case of conflict in their computation. It should be remembered that in both reconverted Houston Plan contracts and exploitation concessions under the HL and the Decree, the payment of royalties is made on account of the federal government. In the Houston Plan reconverted contracts, this rule allows the ex-contractor to stay clear of any dispute with the Province, thus electing to deal exclusively with the federal government. This possibility does not exist in the Argentina Plan concession, probably because it does not derive from previous contracts with YPF, as is the case for the Houston Plan.

As for the right to withhold exploration areas above the *50* per cent. relinquishment rule at the beginning of each period, the ex-contractors of the Houston Plan may use the *5* years' suspension rule for a specific area, till the market or facilities for transport of oil and gas mature (even if section 11 of Decree 2411/91 says the transport will be at the ex-contractors' sole risk), while this suspension faculty is granted by the Decree exclusively for the case of predominant gas producing fields, subject to the further development of the natural gas market and transport, with no reference to crude oil restrictions.

Resolution 1504/91 of the Ministry of Economy has further confirmed that YPF is authorized to waive its right (i) to collect the 8 to 18 per cent. yearly fee on production of said fields, and (ii) to participate in a joint venture with the concession holder once a commercial oil discovery is made. Both rights, now able to be waived, had been granted under the Houston Plan contracts and are meant to be exchanged against the waiver by the contractor of the take or pay clauses, now meaningless if access to the free market is assured. The extent of the actual waivers will depend on a case by base analysis.

A similar development of the government — private sector relationship may be observed in exploitation contracts. Many different forms of exploitation services contracts have been experimented with in the past, overlapping partially in different periods.[5] Several "geologic layers" of risk contracts, exploitation contracts ("capital account"; "reimbursement account"; "incremental production curve" contracts), and services contracts, *etc.* each having a different structure, were concluded with the private sector.

Most of the exploitation contracts have been subject to a continuous renegotiation, such as the one in its time authorized by Decree 836/82. "Additional clauses" were approved establishing crude oil price increases for the incremental production to be obtained with new work commitments, over and above the decline curve expected under these contracts. At present, Decree 1212/89 has been the framework for its conversion into concessions or joint ventures with YPF under the principles of free disposal of the oil produced. Practically all of these contracts are now renegotiated with new formulas.[6]

Each of the renegotiations completed in 1991 is in itself a different story, as it involves the mutual waiver by YPF and the contractors of acquired rights and expectations, of the most varied nature: price formulas and adjustment, past claims on taxation and discounts, *etc.* These discussions have led far away from the essentials of a negotiation based on compensation (or reciprocal compensation) such as questions of assets valuation and earning capacity, a concept of discounted cash flow.[7] Rather, they have considered the profile of this industry in the future, size of the "stock" or interest subject to negotiation, future growth potential and decline curve, return on investment, *etc.* But the negotiation process itself, and the settlements reached, are the best evidence that the government carries on its oil and gas policy keeping in mind the interests and the acquired rights of the oil companies, while attending to the public interest.

As a conclusion, it may be said that the government is shaping all previous ventures into outright joint ventures or concessions under a free oil and gas market. The exploitation concessions resulting from the Argentina Exploration Plan will thus have, at the time they are granted, a large caseload of precedents.

The call for bids under the Argentina Plan I

One hundred and fifty areas (two thirds of Argentina's potential exploration areas), are being offered to private companies to develop exploration activities (International Public Bid E.0l/91) and all the basins are included. The onshore areas are 99, covering 852,000 km^2, while the offshore areas are 51,

[5] For a description of them, see Adrian Pérès, "The Private Activity in the Oil Industry of the Argentine Republic", *El Derecho,* Buenos Aires, Vol.97, p.931, and "Recent Developments in the oil & natural gas industry in Argentina", a letter from Abeledo Gottheil Abogados, May 7, 1990.

[6] For a strongly argued review on the renegotiation periods, see Arturo Sabato "Notes on the oil exploitation in Argentina", *Environmental and Natural Resources,* Vol II, No. 3, (La Ley, Buenos Aires) p. t3. On the present renegotiation, see an interview with Eng. Ruben Maltoni "Deregulation and reconversion", *Petrochemical Review,* No. 79, Aug—Sept 1991, p. 5330.

[7] See E. Lauterpacht, CBE, QC in "Security of investment abroad – Recent arbitral and judicial developments, principally on the question of compensation", *Energy Law '90 (1990),* p.

471.

covering 519,000 km^2. The maximum sizes of each of the areas is 10,000 km^2 (onshore) and 15,000 km^2 (offshore). Exploration permits are to be awarded in a continuous, revolving, bidding process. Beside the 140 areas identified for this purpose, the enforcement authority will receive any proposal for other area delimitations on surfaces not held already by YPF or other parties, provided the size limits above described for each area are not surpassed. The awards will be granted every two months (end of June, August, October, December, 1992, and March 1, 1993), and the exploration permits within the following 10 days. Each of the first three rounds will include a group of areas, and each subsequent call after the first one will also include the areas not yet awarded under the previous calls (section 4, Decree), together with others, that may have been requested by potential bidders (sections 4 and 12, Decree). The provinces will be able to submit under the plan the areas already reserved for them.

The bidding

The bidding is subject to the traditional submitting of two envelopes, envelope A regarding the experience and qualification of the bidder, as set forth in prequalification forms (the bidder is also requested to start separately its registry application with the Registry of upstream oil companies, with the National Direction of Oil Policy at least 10 days in advance to the submission of the offer), and envelope B consisting in the offer itself, setting forth (i) the work units (for the definition and appraisal of work units, see "The Exploration permit terms" hereinbelow) committed over and above the 300 basic or minimum ones required in the call, plus (ii) the time assigned in the proposal for the first period of exploration (Bidding Conditions, "BC", sections 4 and *5).* A guarantee of USS 100,000, should be delivered with the offer (envelope A) for a 120 day offer maintenance period (section 3.6, BC).

The award criterion

The main criterion for the award of the areas is based on the commitments made by the bidder, in work units and time of exploration (section 6, BC). Tile award will be granted to the offer with higher work units commitment and shorter term, both factors to be defined with respect to the first exploration period. No signature bonus is required, except in some exceptional cases (section *5(3),* Decree), where areas involved are not high risk, because prospects are carried on in locations adjacent or relatively close to existing deposits. In formula terms, the award will be made to the bid with the highest amount G, where:

$G=U+(K/T)\ I$

U being the work units committed in the offer over and above K;
K, the minimum or basic Work Units requirement; and
T the first exploration period offered, in years.

Typically, G = U + (300); or U + (300); or (only for offshore areas)

2 3

U + 300

4

As a consequence, it may be said that the reduction of one year in the first exploration period (that automatically reduces the second and third exploration periods by an equal amount of time, as these periods are calculated as a fraction of the first one) means an advantage equal to the value of about 50 work units (onshore areas), that is to say, US$ 250,000. For offshore areas, a one-year reduction would make for a US$ 125,000 advantage (25 work units), and a two-year reduction would mean a USS 375,000 advantage (75 work units).

The exploration permit terms

The exploration permit holder will be granted a title or deed, as evidence of its rights over the area (basically, the right to be the only one to explore the area, and to obtain an exploitation concession if a commercial discovery is made by it).

Following section 20, HL, the holder of the exploration permit will have to limit the exploration area, make the proper markings, and (i) do the necessary work, according to the work units' commitments made in the offer over and above the minimum ones established in the bid conditions (at least 300 working units for the first exploration period, assessed at USS *5,000* each, according to an appraisal chart provided in the BC, consisting in reflective seismics, reprocessing, 3D seismics, or even an exploration well, at the bidder's choice), and (ii) drill at least two exploration wells, one to be executed during the second exploration period (able to be postponed to the third exploration period, if justified on technical grounds), and the other during the third period (sections *5.1.1., 5.1.2.,* and 5.1.3., BC). The exploration permit holder will forward a guarantee of fulfillment of its work commitment for the first exploratory period, and a further guarantee is to be submitted at the beginning of each of the following exploration periods (sections 10.1.1. and 10.1.2., BC) for the relevant exploration programme.

In case of withdrawal by the exploration permit holder (or in case the holder of the permit gives prior notice to the enforcement! authority of the decision not to comply with a particular work unit commitment, without withdrawing from the area, provided the time of each period is not altered), the work unit is replaced by equivalent cash to be paid to the government.

An annex of the Decree makes a pre-established assessment of the value of the work commitments, valid not only for the comparison of the offers, but also for the computation of indemnity to be paid to the government in case of lack of completion (section 9.4., BC) and for determining, up to a certain extent, their interchangeability. This is a step forward, to avoid the usual discussions on the investment's assessment. Law 21778 had referred to a control of expenditure for the computation of the investment committed, and other service contracts (restricted to exploitation only) went further along this line, introducing great

uncertainty and a source of conflict.[8]

Exploration periods: extension period I

The prospecting term of the first period of exploration will be two to three years (four if it is an offshore area) (according to section 5.1.4., BC). The second period will be one year less than the first period offered, and the third period, two years less than the first period (thus, if the first period offered is two years, no third period exists) (sections 2.14 and 9.2., last paragraph, BC). In total, the maximum term is six years (onshore) or nine years (offshore), plus extensions.

The maximum extension period is four years instead of the maximum of five that was established in section 23, HL. The holder of the exploration

[8] Cf. P.L. Folmer in "Envolving relationships between Energy Companies and their Host Governments", *Energy Law '90: Supra* note 7, at pp. 35-36.

permit may anticipate the use of this extension term, by adding one more year to the second period (section 9.2. BC), therefore enabling him to pay during that year the fee corresponding to second exploration period, instead of the one applicable to the extension period (section *9.5.* of the BC, second paragraph). Though section 9.2. of the BC grants this right for "each" of the periods following the first one, it is obvious that it does not apply to the last one, as no "anticipation" of the extension would then be possible.

Relinquishment of areas

The call provides for the future relinquishment of part of the area, according to the minimum established under section 26, HL, at the end of each of the exploration periods (at least 50 per cent. of the remaining area at the end of each exploration period with the following exceptions). The exploration permit holder may keep (section 9.3): (i) the blocks where a commercial discovery has been declared, and therefore included in the exploitation concession, plus, for one more year, those blocks where a declaration of commercial discovery is under study; and (ii) for *5* years, predominantly natural gas fields, subject to the future, adequate development of the natural gas market or transport facilities (further delays may be accepted by the enforcement authority if the market conditions are no better than during the previous suspension period).

Determination of commercial discovery

The government wants to keep the exploration permit awards system simple and flexible (section 5(2), Decree), and has therefore used the scheme described in sections 16 to 26, HL, with the right for the holders of such exploration permits to obtain automatically an exploitation concession once a commercial oil discovery is made, subject to section 27 to 38 of the same law (section *2.5,* BC). According to section 22, HL, the exploitation concession must be granted within 60 days of the declaration of commercial discovery by the exploration permit holder according to acceptable economic and technical

criteria, having submitted the delimitation of the exploitation area. Under the Houston Plan, the commercial discovery declaration was anything but automatic, as the "proposal" by the contractor was subject to acceptance by the enforcement authority, either expressly or through the passage of time without an answer (section 8, C, Decree 1443/85 and amendment by Decree 623/87, same section). The HL reference to technical and economic criteria is only the reproduction of the standards the exploitation concession holder has to comply with, according to sections 31 and 32, HL (make the necessary investments, in reasonable time, to develop the whole field, using the most rational and efficient methods, for the maximum production of hydrocarbons compatible with an adequate economic exploitation ensuring adequate conservation of its reserves). Section *2.5,* BC, stressing the role of the oil company in the obtaining and extent of the concession, defines as the exploitation concession, the set of rights (and obligations) over all the exploitation blocks as determined by the exploration permit holder.

The exploitation concessions

The term

When a commercial discovery declaration is made by the exploration permit holder, the exploration permit is to be transformed into an exploitation concession for a 25 year term (section *35,* HL). Though not specifically referred to in the Decree, section 35, HL, allows a further 10 year extension to be granted by the Executive Power.

The royalty payment, in cash or in kind

The concession holder will have to forward a guarantee of fulfillment of its obligations. The royalties to be paid to the Province by the exploration permit or the exploitation concession holder, on account of the national government, will be (section 9, Decree, and 9.9, BC) up to 12 per cent. (15 per cent. on the oil obtained from the field during the exploration periods as set forth in section 21, ML) on the production assessed at the transfer price of the crude oil out of the oil well.[9] Said royalties shall be paid in cash, unless the enforcement authority requires such a payment in kind. The enforcement authority has stated that the new policy would require payment in cash. But special payments in kind can be made (section 9.9. third paragraph, BC) to the province (state) where the concession area is located, if agreed upon, or if unresolved disputes on the price assessment arise when no such price is available *(e.g.* because of integrated operations). The provinces are empowered to make the necessary controls in any and all areas for checking the flow of production and, hence, the royalty due.

Taxation

There is no production sharing formula, and the general tax regime applies (income tax and others)[10], therefore excluding the special income tax substitute referred to in section *56,* ML (section 8, Decree, states that this special tax is

"not applicable"). Argentina has no tax ring fencing legislation, and consolidation of several exploration and exploitation activities within the territory *(e.g.* income of one of the areas offset by expenses of the others) performed by the same company, is the rule. The fiscal treatment, and royalty established, on the exploitation concession, make these fall into the category described as "tax and royalty regime".[11] At March 1992, general income tax was 20 per cent. on the subsidiary's profits, plus 20 per cent. on after tax dividends, once distributed, for an overall 36 per cent. impact on foreign companies' profit remittances, or, if a branch is used, a 36 per cent. income tax on the fiscal year's profits.

A tax reform project with the intent to limit taxation to distributed profits only has been withdrawn. The reform would not have taxed profits unless distributed. Distribution of profits of joint ventures to joint ventures (if corporations incorporated in Argentina), or of dividends of subsidiaries to holding companies (incorporated in Argentina) would not have been considered as a taxable distribution, leaving a flat 30 per cent. income tax to be assessed on distributed profits (dividends) by the holding companies or by the companies holding an interest in joint ventures. A different tax of 18 per cent. assessed on "primary surplus" (revenues, less investments and expenses
-including wages) would have been created, and considered as an anticipated

[9] I.e. the sales price effectively obtained, less the deductions for transport cost allowed by sections 61 and 62, and section 56, paragraph (c) 1., HL; in a similar way, section 111, D 1757/90, and Resol. of the Subsecretary of Fuels 30/91 *fixing* in principle a 4 per cent. maximum discount for these costs -unless evidence is forwarded showing higher costs effectively incurred-in accordance with the same guideline as set forth in Law 23697, section 33).

[10] Mainly assets tax, value added tax and the provincial turnover or sales tax. The tax on liquid fuel (on processed hydrocarbons and natural gas) is assessed on the consumers.

[11] Boulos, *supra*, note 3.

payment of the income tax. Thus, net income from one area might have been offset by net expenses from another area (up to the share of its participating interest), even if said areas were held by different joint ventures.

The redrafted tax reform project, approved by the House of Representatives, as well as by the Senate's approval, returns to the traditional scheme, but raises the corporation profits tax to 30 per cent. while it eliminates the withholding tax on after tax dividends, in effect reducing the overall impact on foreign investors' profits to 30 per cent. instead of the previous 36 per cent. Branches are consequently also taxed at the 30 per cent. level. [12]

Stability clauses

The new stability clauses, already included in the last concessions awarded during this year, are also set forth in the plan. They guarantee the 12 per cent. royalty ceiling, and discard any future, new, taxation that may prove discriminatory against the holder of the permit or the concession, including the assets and net worth involved, any transactions or related business, and sale of oil and gas (section 8, Decree).

Yearly fee

The holder of exploration permits is subject to the payment of a fixed yearly fee

(section *57)* related to the acreage subject to the exploration permit, and the holder of an exploitation concession, to a yearly fee according to section *58,* HL, adjusted by the variation of crude oil prices (section 102, HL). During the term of the exploration permit, the yearly fee doubles when passing to the second period and triples in the third, while it increases dramatically in the extension period, as a disincentive to such a request.

Property rights and restrictions: environmental regulations

The HL, section 1, assigns to the national government the "inalienable and imprescriptible" property in the subsurface oil (the reservoirs), but grants the exploitation concession holders the exclusive right to exploit the oil fields subject to the concession granted (section 27, HL), for which purpose a title (first, on the exploration permit, section 16 HL, and section 8, BC; afterwards, on the exploitation concession, section 2.18 and section 55 HL) is issued by the Executive, and the public deed registered with the National Registry. Though the wording for the description of federal ownership in the subsurface oil is similar to the one set forth in section 27 of the Mexican Constitution'[3] its consequences are quite different, as the declared governmental property in subsurface oil and gas does not impair the right of the concession holder to the crude oil and natural gas once produced.

The property in the subsurface oil is a matter of discussion between the provinces and the national government and its allotment to one or the other is presently being analysed by the Congress. The main issue on practical

[12] For a comparison of different taxation effects under concessions, production sharing contracts, association contracts, risk service and other service contracts, see Murk DO. Lels "World Wide petroleum legislation — a historic overview", Buenos Aires, Oil & Gas in Argentina, seminar held 10/13 December, 1985, International Center for Management Information, and, more recently, Remo Mannarino "Economic and fiscal aspects of petroleum risk contracts", preprint of the 13th World Petroleum congress, Buenos Aires, October, 1991, though the presentation of the latter's paper at the Congress gave information on Argentina's taxation that has to be updated.

[13] See Ewell E. Murphy, Jr, "The Dilemma of Hydrocarbon Investment in Mexico's Accession to the North American Free Trade Agreement", (1991) 9 J.E.R,L., 262, note 13.

grounds is the provinces' claim to differentials on past royalties due by YPF. The government is procuring agreements in order to settle those differences. The National Supreme Court, on August 2, 1988 ruled in a claim made by the province of Mendoza against the nation that Congress had been empowered by the Constitution (section 67, paragraph 11) to pass the Mining Code, and therefore vested with the authority to decide on such issues as the allocation of property rights, and on the call for bids on exploration permits and exploitation concessions of oil and gas. The ruling also acknowledged that the Hydrocarbons Law had been enacted validly according to the authority granted by section 67, paragraph 11 of the Constitution.[14] As the Hon. Marc Lalonde puts it, foreign companies are "in for a rough ride when the various levels of government ... have difficulty reconciling their respective interests" (right to the resources, rate of depletion, taxation at the different levels of government, *etc.).*[15] The court precedents here mentioned are of the utmost importance for defining that the HL does not oppose the Constitution; the payment of royalties directly made by the concession holder to the provinces, but on account of the federal government, and the special clauses protecting the exploration permit or the concession holders from any new, discriminatory, taxation, are the shield to keep the private companies clear from this debate and its consequences.

Environmental protection seems however an open issue, as the Constitution (sections 14, 17, 26, 28, 67, paragraphs 4, 9, 11, 12, 16; section 107; section 104; and section 108) assigns authority to both federal and local government on this subject, and legislation and enforcement at both levels have not reached in the past a satisfactory level.[16] An amendment of HL currently being discussed in Congress will, if passed, further confirm the provinces involvement in the environmental control of the oil fields.

The federal government has in the past used its authority to define the safety rules under which the exploration, exploitation and transport of hydrocarbons should be made (Decree 963/70) and section 69 HL recites the obligations for the permit or concession holders in this respect. For spills in the sea, ports and rivers, Law 22190 establishes a clean up obligation. Law 23456, ratifying the 1969 Brussels Convention on open sea oil spills, is also applicable. Vented gas regulated under Decree 415/79 is now given free to the province, if vented by YPF (Law 24009).

Other obligations of the exploitation concession holder

The HL, section 31, requests the exploitation concession holder to make the necessary investments and perform work for the development of the field, according to the most rational and efficient techniques corresponding to the importance and nature of the proven reserves, assuring the maximum production of hydrocarbons, compatible with an adequate and cost efficient

[14] Guillermo J. Cano, in "Natural Resources and Energy", Buenos Aires, 1979, Ed. La Ley,

p.107/8, is, together with Mr. Pedro J. Frías, the principal sustainer of the doctrine of Provincial property in natural resources, including oil and gas, though he considers that both the provinces and the federal government have concurrent authority as for the development of the exploitation of these natural resources. Also, see G. Bidart Campos, "The old problem of the mining property — The oil in the context of a federal regime", *El Derecho,* Vol. 129, p. 471, as opposed to "The oil and gas reservoirs are of the Federal property. Its present regime is according to the Constitution", by Carlos Emérito Gonzalez, *El Derecho,* Vol. 129, p. 464.

[15] *Energy Law '90, supra,* note 7, at p. 44.

[16] For a review of Latin America's stand in 1989 on this issue. with the relevant information for Argentina gathered by ourselves, see Paul C. Nightingale and Gregory A. Bibler, "Environmental Law in Latin America", *International Environmental Reporter,* October 1989.

exploitation of the reservoirs, strictly abiding to criteria of conservation of the reserves (non-premature depletion). Section 32, HL, requests that within 90 days of the commercial oil discovery declaration, a development programme be communicated to the enforcement authority, referring to the investments planned, and periodical updates have also to be forwarded.

This purpose does not seem to be far away from the "compatible objectives" described by Alfred J. Boulos for the energy companies and host governments, under the "common objective to maximize the economic development of the country's hydrocarbon resources".[17] Due to the special situation of Argentina as an oil producing country, unable to influence in any way the world's oil and gas market due to its marginal contribution (quite recent) to the aggregate offer, and therefore with no ability to influence the market price, the energy policy issues that may be relevant for OPEC countries are of no avail in Argentina, where the prospect to "keep reserves in the ground" does not have the same significance as in those countries. Depletion of the field should therefore be a matter to be dealt with on technical terms, with a long term view of the economics of the situation.

It is true, however, that Argentina does not seem to have set a framework of priorities for the development of its energy resources: oil, gas, hydro, nuclear, which might well be the result of an all-too-confident trust in the free market forces to decide, though this seems to ignore the many consequences of natural monopolies and the challenge of creating a free market environment.'[18]

Free crude oil disposal

The holder of the exploitation concession will have the free disposal (section 6, Decree; following section 3, Decree 1589/89, and sections 14/15 of Decree 1055/89) of the crude oil or gas produced, and sell it locally at free market prices (section 9, Decree 1212/89) or export it, free and clear of any withholdings, custom duties, or any other related taxes: section 6, 2nd. para., Decree). In case a deficit of supply to the local market arises and is the subject of a prior notice by the government, 12 months in advance, as a consequence of which the crude oil must be sold locally, the ML, section 6 (and section 6 of Decree *1589/89)* guarantees to the concession holder the import parity price of crude oil. For a full display of opportunities under the "free disposal" principle, many issues such as pipeline batching have still to be addressed to allow the sale of crude oil of a specific quality. A correction formula is nowadays applied, for balancing the value of crude oil received by the pipeline and the one corresponding to the oil delivered. Swaps are the practical, if not ideal, solution. As for export, there is a lack of sufficient infrastructure (storage tanks, ports, harbour capacity for large tankers, pipelines, *etc.).* These factors induced a local market price nearer to the export parity at the beginning of 1991 (when YPF set a kind of reference price, as it supplied the refineries of the private sector to close the gap between offer and demand, until sufficient crude oil should be flowing under the renegotiated contracts' operation). The market has since evolved

[17] *Supra,* note 3.

[18] See Luis A. Erize, “Business Agreements — From the public sector towards the private sector in concentrated markets”, Buenos Aires, IDEA, vol. XIV, No. 144, July 1990, p. 14, at 17, where the need of a government tutoring for building new market conditions for energy, unable to he generated spontaneously, is stressed.

into a more regular behaviour.'[19] This is one of the areas to be closely monitored in order to guarantee a full transparency of market practices.[20] The case for natural gas is different, as its price has still not been deregulated (section 10, Decree 12 12/89). Expectations are that this will happen in 1992 or 1993. The concession holder has the free disposal of natural gas, unless a sales agreement is made with Gas del Estado, the state-owned natural gas company (section 2, Decree *1589/89).* Open access to gas pipelines is granted at uniform tariffs (section *15,* Decree 1055/89 and section 7 of Decree 1589/89), but section 43, HL, subjects it to excess capacity available in the pipeline. The existing gas pipelines are going to be offered in 1992 for private bidding for non-exclusive concessions, the regulatory framework having been recently passed by the legislature.

Foreign currency availability

Under the present foreign exchange rules (Decree 530/91), the whole of the foreign currency resulting from any kind of exports is free from any requirement of local currency conversion; the monetary system established by the convertibility law has stripped the Central Bank of its previous authority to purchase and sell the foreign currency related to exports/imports. As a guarantee of protection against future changes of the present foreign exchange regime, the holders of exploitation concessions are assured that at least 70 per cent. of the foreign currency resulting from crude oil exports will always be free from any future change establishing a legal requirement to convert foreign currency amounts into local currency (section 6(3), Decree). The twist of the Decree and BC is that the 70 per cent. guarantee of future remittances is currently surpassed by the present legal framework of Decree 530/91. This 70 per cent rule applies now as a default clause (section 6, last paragraph, Decree) in case of future exchange restrictions, as they do not exist at this time.

The limits

Section 25, HL, establishes a limit for being simultaneously a holder of exploration permits or exploitation concessions for more than five areas, either directly or indirectly. This may be circumvented, through the incorporation of separate subsidiaries or the formation of joint ventures, holding, each of them, the maximum amount of permits or concessions (section 10, Decree). But if joint ventures are formed, the owners of participating interests in them will nevertheless be jointly and severally liable, as the application form for submitting the offer includes such express commitment. The construction made by section 9.10, BC, set forth by Decree 2178/91 of this limitation of section *25,* second paragraph, HL, and 34, second paragraph, HL, is exactly the opposite of the one imbedded in the call for bids made when HL was initially enacted in 1967, when it was stressed (resolution SEEM 23 1/67, sections 1, 2 and 3) that

for the computation of the ceiling on permit or concession holdings, the limit would apply to each of the joint venturers, as if they were sole holders of each permit or concession. To the contrary, section 9.10, BC, now states that each joint venture, regardless of

[19] See *Carla Petrolera*, Buenos Aires, Year I, No. 1, November 1991 issue, Ed. Mercado, pages 3/4, "The New Rules", comparing import/export parity prices and prices of crude oil paid by the refineries.

[20] For a non-oil sector originated comment on this, see Daniel Artana, "How to resolve conflicts on deregulation", *El Cronista,* February 27, 1991.

the distribution of the participating interests in it, shall be computed as a separate entity, therefore freeing each interest owner from having to compute the joint venture's concession as if it was a concession granted to each of them for the scope of the limitation to *5* permits or concessions.

Approval for farm-outs or project-financing, establishing liens on the concession's rights will now be delegated to the Ministry of Economy and Public Works, instead of being granted by the Executive (section 13, Decree, and section 73, HL).

Arbitration

The winner of the exploration permit award may request an arbitration clause (section 11, Decree and section 86, HL) for resolving disputes on penalties for lack of performance (sections 79 to 83, HL). Nevertheless, the offer application form does not include this possibility at this early stage, as it refers to submission to the jurisdiction of the Buenos Aires Federal Courts.

Indemnity clause

The Decree includes a very important protection for the exploration permit or exploitation concession holder, by explicitly stating that the Executive will hold them harmless in case of frustration of their operations due to governmental acts, covering damages, interests and even loss of profit (section 14, Decree, with reference to section 519 of the Civil Code). The unlimited reference to the Civil Code principle, that allows the inclusion of loss of profit, goes beyond the usual rule for the extension of said indemnisation when frustration of administrative contracts is the consequence of governmental acts. It now peacefully acknowledges the ample indemnity clause for the consequences of such governmental acts, even if such acts may be reputed as reasonable.

Epilogue

The Argentina Exploration Plan is by far the most attractive proposal up to now for international oil companies wishing to explore for oil and gas and run the associated risks, as no forced partners are imposed, nor posted prices established. A free market is on the move, successfully, and the stability of the legal framework described above comes from the fact that the Argentina Plan, as well as the oil and gas policy implemented in the other upstream activities,

result from the 22 year-old hydrocarbons law, confirmed by successive political regimes, that gave the Executive the authority to choose between the private sector and the government as leader of the oil and gas process. The choice has now been made.