

THE EFFECT OF STABILIZATION CLAUSES IN PETROLEUM CONTRACTS IN DEVELOPING COUNTRIES LIKE NIGERIA*

Abstract

The petroleum industry is an integral part of Nigeria's economy since the discovery of oil in commercial quantity in Oloibiri Bayelsa State in 1956. The Petroleum Industry is a very complex industry which requires a lot of technology and finance to run, developing countries like Nigeria don't have such capital and technology to run their oil industry independently thereby forcing them to partner with international oil companies. In a bid to give assurances to the investments of the international oil companies, Stabilisation Clauses are inserted into agreements between the parties. This work examines whether Stabilisation Clauses are in anyway beneficial to the host state. The work will interrogate the benefit(s) of Stabilisation Clauses to both the international oil companies and the host states. The methodology adopted is doctrinal, with a qualitative approach for appraising the effect of Stabilisation Clauses in petroleum contracts in the oil industry. The analysis and legal deductive reasoning are based on information from primary and secondary sources such as textbooks, articles in journals, periodicals, law reports, legislation and internet sources. In the course of this work it was discovered that Stabilisation Clauses can be used to boost the transfer of technology to developing countries like Nigeria. It was also discovered that the host country could still modify the terms of a petroleum contract even with the presence of the freezing Stabilisation Clause which tend to suspend the legislative powers of the host state once the contract has been completed. It was recommended that the government of host states should always involve experts when dealing with international oil companies as this will give them the opportunity to know the type of Stabilisation Clauses that exist and the one that best fits their peculiar situation.

Keywords: Clauses, Contracts, Countries, Petroleum, Stabilisation.

1. Introduction

Stabilisation clauses are provisions in investment contracts that accommodate the risk of regulatory changes for investors.¹ Stabilisation clauses are very important clauses in petroleum contract throughout the world. Given their high level of protection, stabilisation clauses may cause conflict between international oil companies and developing countries regulation to protect human rights or more generally to work towards sustainable development. The debate on stabilisation clauses closely relates to the more general call for coherence between investors rights, legitimate public interest and states human rights in international investment law. There is increase public criticism regarding the one-sidedness of investment law, protecting investors rights at the same time anchoring investors responsibilities for human rights and sustainable development. Some start to question the contribution of international investment law to sustainable development and its positive effect on the rule of law. Investment law today aims at the protection of economic (human) rights such as the freedom to trade and conduct a business, property rights related to business activities and other human rights issues that are relevant to development and long-term sustainable growth.

The first thing that comes to mind at the sight of Stabilisation Clauses in petroleum contracts of developing countries like Nigeria is the protection it gives to the investor against the host state. This is because when considering the sustainability of a long-term petroleum agreement, recourse is majorly given to the political and fiscal factors without considering other factors such as labour concerns, public interest, human rights and environmental hazards posed by petroleum activities of the International Oil Companies. (IOCs). Oil producing countries like Nigeria enter into investment contracts with foreign investors to improve the level of production of their oil fields due to lack of expertise and capital. Foreign investors are extremely careful of investing due to the nature of petroleum agreements, the risk involved and the amount of funding required to carry out exploration and exploitation of a particular oil field. A high degree of stability is important to foreign investor because once an investor becomes uncomfortable with a project, the less interest he will give towards that project. In recent times host states include Stabilisation Clauses to attract foreign investors. There is a strong relationship between stability and equity of investments. Stabilisation Clauses play a role in strengthening the legal relationship between host states and foreign investors.

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¹K Gehne R Brillo, 'Stabilization Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment' (2014), 2013(46) *Nccr Trade Regulation, Swiss National Centre Of Competent Research* 9,10,11. <<http://telc.jura.uni-halle.de/sites/default/files/BeitraegeTWR/Heft%20143.pdf>> accessed on 8 January 2018

Ultimately, investors have various means to tackle risk inherent in petroleum agreements for instance, distributing out the risk, risk management, ensuring the risk and finally shielding the risk. The most common is shielding the risk whereby the investor uses political, economic and financial influence to daunt the host state from changing its existing laws. Stabilisation clause is a major way of sharing risk between parties to a long-term contract to ensure contractual stability. Investors can therefore reduce risk by including clauses like international arbitration, choice of law, adaptation as well as stabilisation clauses in their contract. For example, a production sharing contract between PERTAMINA and CONOCO provides: ‘This contract shall not be annulled, amended or modified in any respect except by the mutual consent in writing of the parties.’²

2. Emergence of Stabilisation Clauses in Petroleum Industry

The origin of Stabilisation Clauses began after the first and second world wars. This was as a result of nationalization of United State companies in Latin American Countries. The important aim of inserting such a clause was to protect the companies from expropriation by making any taking by a host state unlawful.³ The assumption is that by agreeing to a stabilisation clause, a state accepts to freeze its executive and legislative powers during the life of the agreement. In other words, the presence of such a clause evinces the will of the parties to respect the sanctity of the contract. In *Texaco Overseas Petroleum Company (TOPCO) v Libya*⁴ the tribunal held that Libya, having submitted to a Stabilisation Clause in the agreement cannot violate the special contractual undertaking on grounds of exercise of right of permanent sovereignty. Subsequently, interest in the use of Stabilisation Clauses appeared to diminish substantially. This was partly because developing countries were influenced by some United Nation (UN) Resolutions in the 1970s that highlighted a possible conflict between Stabilisation Clauses and the principle of Permanent Sovereignty of States over their natural resources (PSNR).⁵ Newly independent developing countries thus sought to obtain international recognition of their right to restructure these inequitable concessions and re-establish their sovereignty over their natural resources through nationalisation or similar means. After several attempts to formulate the principle within the context of the UN, a compromise was finally agreed by the UN General Assembly in 1962⁶ wherein the right of states to permanent sovereignty over their natural wealth and resources which must be exercised in the interest of their national development and wellbeing of their people was recognized.

After the recognition, the developing countries became reluctant to accept Stabilisation Clauses as that would impose a limitation on the exercise of this right. Furthermore, several developing countries including Saudi Arabia, Nigeria and Indonesia considered it unnecessary to grant Stabilisation Clauses as they also believed their huge reserves offered sufficient incentives for foreign investors to bear the political risks associated with their investments.⁷ In addition, the UN Resolution also endorsed the right of states to nationalise and expropriate on grounds of public utility, security or the national interest subject to the payment of appropriate compensation.⁸ As Stabilisation Clauses were originally developed to protect against these acts, the clauses became less relevant.

In the light of the above sentiments, predictions were made that even if Stabilisation Clauses were to be included in contracts, hosts states would no longer accept them.⁹ These predictions were however short-lived following the mid-1980s catastrophic fall in mineral prices that significantly reduced the revenue developing countries received from their extractive industries. Their governments were encouraged to enact policies to attract Foreign Direct Investment (FDI) as a means of obtaining more revenue.¹⁰ Consequently, Stabilisation Clauses made an unexpected comeback

²Law Teacher, ‘The Law Essay Professionals’<https://www.lawteacher.net/free-law-essays/commercial-law/impact-of-stabilization-clause-on-petroleum-agreements-commercial-law-essay.php> accessed on 8 February 2018.

³ O Dike, ‘Nationalization of Foreign Asset by Host State: A Failure of Stabilization Clause?’ *University of Dundee* (2006) 10. <<https://www.eisourcebook.org/cms/Failure%20of%20Stabalization%20Clause.pdf>> accessed on July 24 2019.

⁴ 53ILR (1977)

⁵A Kilangi, ‘Permanent Sovereignty over Natural Resources General Assembly Resolution New York, (1962), *Audio Library of International Law* <http://legal.un.org/avl/ha/ga_1803/ga_1803.html>

The principle of PSNR is a principle of international law that emerged in the 1950s mainly in response to the perception that during colonial rule, inequitable concessions were imposed on vulnerable host states.

⁶ Permanent Sovereignty over Natural Resources, 14 December 1962, UN Doc A/Res/5217

⁷ F Sotonye, ‘Stabilisation Clauses And Sustainable Development In Developing Countries’ (2014) *PhD*

Thesis, University of Nottingham 12. <http://eprints.nottingham.ac.uk/14466/1/PhD_Thesis.pdf> accessed on 18 February 2018.

⁸ *ibid*

⁹ *ibid*

¹⁰ *ibid*

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as they formed part of the new fiscal regime that several developing countries enacted with the support of the World Bank to attract FDI into their extractive industries.

However, whilst the original clauses had been developed to guard against acts of nationalisation and expropriation at the time, the re-introduced Stabilisation Clauses were drafted to protect investors from the adverse effects of changes in the laws of the host state even if such changes fell short of expropriation or nationalisation. In other word, modern day Stabilisation Clauses may be drafted to allocate all the political risks associated with a project to the host states. For example, the scope of the stabilisation clause in the Host Government Agreement (HGA) covering the Azerbaijan part of the Baku-Tbilisi-Ceyhan (BTC) Pipeline project covers the following issues:

The interpretation or application of Azerbaijan Law (whether by the courts, the executive or legislative authorities, or administrative or regulatory bodies), the decisions, policies or other similar actions of judicial bodies, tribunals and courts, the state authorities, jurisdictional alterations, and the failure or refusal of judicial bodies, tribunals and courts, and/or the state authorities to take action, exercise authority or enforce Azerbaijan Law.¹¹

3. Stabilisation of Contract in the Oil Industry

The issue of contractual stability represents a major source of conflict between the IOCs and the HCs, while the IOCs are more concerned with stricter stability clause the HCs prefer a more flexible contractual regime. The IOCs, therefore, involve the principle of sanctity of contract (*pacta sunt servanda*), the legal consequence of this reasoning is that the HC is not entitled unilaterally to modify or terminate the contract with the IOC. The practical effect is that the contract cannot be renegotiated or reviewed. The HCs counters the (IOC) argument by relying on the principle of Permanent Sovereignty over natural resources.¹² The principle of Permanent Sovereignty over natural resources and the impact of stabilisation clauses was recognized by the tribunal in the case of *Parkerings Compagniet AS v Lithuania*,¹³ where the arbitral tribunal recognised each State's undeniable right to exercise its sovereign legislative power and enact, modify or cancel laws but also recognised the impact of a stabilisation agreement or clause. Bilateral investment treaties do place some limits on the host state sovereignty in an effort to provide stable and legal framework for investors. For instance, in *ADC Affiliate LTD and ADC & ADMC Management LTD v Republic of Hungary*¹⁴ the tribunal asserted that while a sovereign State possesses the inherent right to regulate its domestic affairs, the exercise of such right is not unlimited and must have its boundaries. Chowdhury¹⁵ argues that stabilisation clauses are ineffective if it ties the hand of the host state for a very long period. His assertion finds support in *Kuwait v American Independent Oil Company (AMINOIL)*¹⁶ where the arbitral tribunal refused to read a Stabilisation Clause as preventing the state of Kuwait from nationalizing a concession that spanned for 60 years. Petroleum contracts often span between 20–30 years, or even more.¹⁷

Stabilisation and Adaptation¹⁸ clauses are goodtwo ways the parties can achieve a common objective as they allocate between them the risk inherent in a long-term transaction. Obviously, there is a level of risk that experienced parties have to accept to bear in this kind of transactions to ensure contractual stability. The insertion of Stabilisation Clause may insinuate that the State has accepted that its legislative and administrative powers in modifying the contractual conditions agreed with the investor has been circumscribed but this is not completely true as renegotiation is a major characteristic of a long-term contract whether or not it is expressly stated. In other to save the parties of any legal tussle it is advisable to include an Adaptation Clause to petroleum contracts as it operates in the presence of a change of circumstances beyond the control of the parties which causes a substantial modification of the economic equilibrium of the contract. It may be invoked by the party whose obligations have thus become more onerous, its objective being to protect the aggrieved party, be it the State (or the State entity) or the investor. The important issues that should be covered by Stabilsation Clauses include political, fiscal, technological,

¹¹ *ibid*

¹² L Atsegbua(ed), *Oil and Gas Law in Nigeria: Theory and Practice* (2nd edn. Benin City; New Era Publisher, 2004) pp 169, 170

¹³ (2007) ICSID Case No. ARB/05/8

¹⁴ (2006) ICSID Case No. ARB/03/16 (Cyprus/Hungary BIT).

¹⁵ S R Chowdhury, *Permanent Sovereignty Over Natural Resources: Substratum of the Seoul Declaration*, *The Hague*: (Martinus Nijhoff Publishers, 1988) 59

¹⁶ (1982) 21 ILM 976

¹⁷ P Bernardini, 'Stabilization And Adaptation In Oil And Gas Investments' (2008) 1(1) *Journal of World Energy Law & Business*, 98. <<https://academic.oup.com/jwelb/article/1/1/98/1003122>> accessed on June 18 2018.

¹⁸ *ibid*

environmental, labour concerns and other important issues that may be of public concern like human right protection.

4. Types of Stabilisation Clauses in the Oil Industry

The types of stabilization clauses in the oil industry are i) Freezing clause, ii) Economic equilibrium clause, iii) Hybrid clause. Freezing clause is perceived as a selfish clause as it does not allow for future negotiations. It is the most far-reaching type of Stabilisation Clause which aims to ensure that the law, fiscal regime or other essential economic conditions applicable to the investment will not change over the life of the project, therefore, it freezes the legal regime on the day that the agreement was made and does not allow for any future legislative changes to apply to the investor. This type of clause is more advantageous to the IOCs than the HC. The effect of a freezing clause may suggest that the sovereignty of the host state has been impeded.¹⁹ The host may unilaterally modify the initial terms of the contract when there is a call to protect public interest, this was shown in the case of *BP Exploration Co (Libya) Ltd v Government of the Libyan Arab Republic*²⁰ the tribunal held that although the Stabilisation Clause limited Libya's freedom to alter or amend unilaterally the terms of the concession, nonetheless Libya could do so if the amendment was in public interest.

Parties favour clauses which ensure that adjustments and revisions can be made to a contract if the rights or interests of the foreign investors and citizens of the host state are adversely affected by a change of circumstances.²¹ These changes are better resolved with the presence of Economic Stabilisation Clauses in international contracts. The Economic Equilibrium Stabilisation Clause ensures the balance of the interests of the parties concerned.²² The State's exercise of sovereign authority is not contractually barred; rather such action is counterbalanced by the provision that the economic equilibrium of the contract as of the effective date of the contract will be maintained during the lifetime of the contract.²³ i. It is worth noting that there are a number of exceptions found in modern petroleum contracts and relevant national legislation to economic balancing provisions. For example, the economic equilibrium of the contract cannot be expected to be re-established when the new law or decree is enacted: (i) in response to a breach or lack of compliance by the contractor with any provision of the agreement concerned; or (ii) with the intent of protecting health, safety, environment or security. ii When the contract (and Stabilisation Clause) is governed by domestic law, the foreign investor's interest could be at stake as the state party can change its law reducing the effect of the Stabilisation Clause, especially when it is a freezing clause and it stands alone. No matter what law governs the contract, either the law of the host state or international law or any other non-national law, the state's exercise of sovereign authority in the public interest cannot be denied either in the context of Freezing Clauses or Economic Stabilisation Clauses. In particular, in the context of exploration and exploitation of natural resources, such powers are well recognized by the principle of permanent sovereignty of the state over natural resources. The consequences of states exercising their authority for the public good in the presence of stabilization clauses will depend on the type of such clauses and the applicable law. If the Stabilisation Clause is invalid under the law of the host state, international law may not come to its rescue.

As the name implies, hybrid clause simply consists of a mixture of the characteristic of both freezing clause and economic equilibrium clause. This type of Stabilisation Clause requires the host state to reinstate the IOC to the same position it was before the change of law was made. Hybrid clause has two categories: the full hybrid clause and the limited hybrid clause. A full hybrid clause shields the investors from financial implication caused by change

¹⁹E Oshionebo, 'Stabilization Clauses in Natural Resources Extraction Contracts: Legal, Economic and Social Implications for Developing Countries' (2010)(10) *Asper Review of International Business and Trade Law*.8

²⁰ (1979) 53 ILR 297

²¹E EChiomu, 'Examining the Crucial Impact of a Well-drafted Stabilisation and renegotiation Clause on Production-sharing Agreements' (2015) *Int'l Energy L.Rev.*2<https://energycharter.org/fileadmin/DocumentsMedia/Events/CCNG_2015_Michael_Polkinghorne.pdf> accessed on June 20 2018

²² A F M Maniruzzaman, The Pursuit of Stability in International Energy Investment Contracts: A Critical Appraisal of the Emerging Trends, (2008)1(2) *Journal of World Energy L. & Bus.* 124<<https://poseidon01.ssrn.com/delivery.php?ID=267119122101066069121095009086026077034092086004057035102125022103105109076068109087038017120036122008044068100011102009000109009046056035086101125121031083113004035054023094113102021090114114010004096074116003090001067087114110115014026126104008009&EXT=pdf>> accessed on May 27 2018.

²³*ibid*

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of law by ensuring that compensation is made, while limited hybrid clause shields the investors from financial issues of some limited change of law.

In the practice of Stabilisation Clauses, the special representative of the Secretary General for Business and Human Right (SRSG) Study analysed that freezing clauses still belong to modern investment contract practice with respect to Sub-Saharan Africa,²⁴ Eastern and Southern Europe,²⁵ Central Asia,²⁶ the Middle East²⁷ especially in the extractive industry (eg petroleum industry). In the 1970s and 1980s, in the aftermath of colonisation, the use of freezing commitments came under pressure as the freezing effect considerably reduces the sovereign power of the host state. The study shows that even though freezing clauses are designated to be outdated, they are still commonly used. Some still consider them to be the best and most secure form of contractual stability.²⁸ Frequent use of freezing clauses by a host state with respect to different investors over time may cause legal battles as different laws may be used on different investors. Freezing clauses usually do not feature in contracts with the Organisation for Economic Co-operation and Development (OECD) countries.²⁹ Here, limited economic equilibrium clauses addressing specific regulatory risks prevail. In OECD contracts, their scope is generally restricted to discriminatory regulation and they may exclude regulation on safety, security and other public concerns, such as environmental or social legislation.

5. Benefits of Stabilisation Clauses to both the International Oil Companies and Host States

Stabilisation clauses assure the investor of any future actions of the government or any laws made by the host government which may affect the terms of the contracting agreement (especially political and fiscal legislations that may affect the interest of the investor). This is because the host state cannot unilaterally modify the terms of the contract without the consent of the IOC. This was held in the case of *Libyan American Oil Co (LIAMCO) v The Government of The Libyan Arab Republic*,³⁰ where the tribunal held that a Stabilisation Clause which provided that the contractual rights expressly created by the concession shall not be altered except by mutual consent of the parties prevented the state of Libya from cancelling or modifying unilaterally the content of the agreement. The host state's acceptance of Stabilisation Clause in petroleum contracts clearly shows the host state's readiness to do serious business and this plays a great role in strengthening the legal relationship between the host state and foreign investors as it brings confidence to the contracting parties, this kind of confidence helps to strengthen the relationship of the parties as well as creating room for future transactions. They safeguard the interest of the foreign investor intending to invest in a country which has different socio-economic conditions prevailing and different legal systems in practice. Stability Clauses help the IOCs to keep their part of the contract as an erring IOC cannot reestablish the economic equilibrium clause of the contract when modification is made by the host state as a result of the breach caused by the IOC. The government of developing countries can accept the insertion of Stabilisation Clause in their petroleum contract in exchange for transfer of technology; this bargain will go a long way to benefit the developing countries in the near future as it will improve the technology of developing countries which will in turn boost their local content.

Another benefit of Stabilisation Clause in oil and gas contracts is that it helps to find appropriate investors for huge oil and gas projects. Most of the times, with all the uncertainties attached to oil and gas sector of fluctuating taxes and prices of oil and gas, investors are discouraged to invest. However, the presence of Stabilisation Clauses assures the investors against uncertain losses due to changes in laws, taxes, etc of any form and woos investors for huge oil and gas projects all over the world. Investors and states use Stabilisation Clauses to form part of the ground rules upon which the investors operate the project, guide informal dealings and formal negotiations between the parties to the agreement, and serve as a formal protection of rights if a dispute should arise.

²⁴libyaegyptalgeria, sudan,

²⁵bosna and romaniaalbania

²⁶ Kazakhstan, Uzbekistan and Turkmenistan

²⁷ saudi arabia, united arab emirate, iran, iraq, kuwait

²⁸ K Gehne & R Brillo, 'Stabilization Clauses in International Investment Law; Beyond Balancing and Fair Equitable Treatment', (2014) 2013(46) ncr Trade Regulation 9,10,11 <<http://telc.jura.uni-halle.de/sites/default/files/BeitraegeTWR/Heft%20143.pdf>> accessed june, 2018

²⁹ The Organisation for Economic Co-operation and Development (OECD) countries include Australia, Austria, Belgium, Canada, Chile, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States.

³⁰ (1981) 20 ILM 151

6. Legal Value and Effect of Stabilisation Clauses

The legality and binding nature of Stabilisation Clauses was upheld in *Texaco v Libya*,³¹ *Kuwait v American independent oil company*,³² *(Aminoil) AGIP v Congo*,³³ *Revere Copper v OPIC*.³⁴ This reflects the dominant position in international arbitration awards. In addition, the legal value of Stabilisation Clauses may be reinforced by provisions in investment treaties, whereby a state commits itself to honour contractual undertakings vis-à-vis nationals of another state party (umbrella clause).³⁵ Two issues are highlighted from the aforementioned cases, first, the *Texaco*, *Aminoil*, *AGIP* and *Revere Copper* awards all involved expropriations rather than lesser forms of regulatory change. The legality and binding nature of Stabilisation Clauses therefore relates to commitments not to nationalise rather than not to regulate. The case of *Aminoil* went further to state that the Stabilisation Clause in the concession must expressly prohibit nationalisation. On the other hand, the legality and binding nature of Stabilisation Clauses restricting the right to regulate and the consequences of regulatory changes not amounting to expropriations have not yet been properly tackled in published arbitral awards.

The second issue is that the legal validity under international law does not evade issues concerning the legality of Stabilisation Clauses under the domestic law of the host state, including constitutional principles on the separation of powers and on the competence of the executive to enter into commitments that prevail over legislation adopted by parliament (freezing and consistency clauses). Issues concerning legality under domestic law are likely to vary across national legal systems. Where Stabilisation commitments are indeed unconstitutional, the implications of this may be complicated by the longstanding principle of international law whereby states cannot plead the provisions of their domestic legal system to justify non-compliance with, or legal challenges to their international obligations. In *Revere Copper v OPIC*,³⁶ the arbitral tribunal held that under international law the commitments made in favor of foreign nationals are binding notwithstanding the power of Parliament and other governmental organs under the domestic Constitution to override or nullify such commitments.

Beyond the legality of Stabilization Clauses, a key issue is the legal effect of such clauses if their provisions are violated. Violations may include outright expropriation in breach of an intangibility clause, or regulatory change in breach of a freezing clause. In the case of economic equilibrium clauses, parties are under an obligation to negotiate in good faith so as to restore the economic equilibrium following regulatory change; but they are not under an obligation to reach an agreement. Therefore, while failure to agree does not breach the clause, violations may include refusal to renegotiate, or intentional obstructing of negotiations, accompanied by refusal to compensate as provided by the clause.

Issues concerning the consequences of breaches of Stabilisation Clauses have been tackled in some arbitral awards, although mainly with regard to expropriation. In this context, payment of compensation emerges as the main legal effect of such breaches.³⁷ Under freezing clauses, the host state must usually pay compensation if it applies regulatory changes to the investment project. On the other hand, economic equilibrium clauses are only triggered where a minimum threshold is met - namely, where the economic equilibrium of the contract is affected. At this point, parties to the contract come under an obligation to negotiate in order to restore the economic equilibrium; failure to do so (or to comply with alternative routes provided by the clause) triggers a violation of the clause.

Regulatory change includes legislation, the judicial or administrative interpretation of existing provisions, and other measures that affect the economic equilibrium of the investment project would require the government to pay compensation, even if those measures per se do not amount to regulatory taking. That said, the amount of compensation payable for breach of a Stabilisation Clause is not necessarily comparable to that payable under the regulatory taking doctrine. By definition, a regulatory taking entails a substantial deprivation of property rights. The amount of compensation reflects therefore the fact that an expropriation has taken place. On the other hand,

³¹ (1977) 53 ILR The arbitrator held that —the right to nationalise is unquestionable today and part and parcel of state sovereignty; but that contractual commitments not to nationalize are a manifestation and exercise of sovereignty — not its alienation. In other words, sovereignty encompasses the right of states not to exercise their right to nationalize and to enter binding commitments to that effect

³² *supra*

³³ (1982) 21 ILM 726 [AGIP]. Award, 30 November 1979

³⁴ (1978) 56 ILR 257

³⁵ See, for example, Article 10(1) The International Energy Charter Consolidated Energy Charter Treaty 2016

³⁶ *supra*

³⁷ *Agip case supra*

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Stabilisation Clauses may trigger payment of compensation for lesser interferences in the economic equilibrium of the contract. Apart from extreme cases where breach of a stabilisation clause amounts to expropriation, the aim is not to compensate the investor for expropriation but rather to restore the economic equilibrium of the contract. Compensation is therefore likely to be lower than compensation payable for a full expropriation.

7. Limitation of Stabilisation Clauses

Limitation of Stabilisation Clauses³⁸ has to do with exempting socially desirable host state regulation from their remit. This option has been publicly discussed mainly with regard to human rights standards, but it can be applied to others (e.g. environmental) standards as well. With regard to human rights, the merits of this approach have been discussed by Sheldon Leader.³⁹ According to this author, state sovereignty is limited by the international obligation to realize fundamental human rights. Therefore, Stabilisation Clauses are valid and legally binding, but their scope is restricted in that they cannot impair the human rights held by third parties, and they cannot prevent genuine host state action to progressively realize human rights. In other words, this approach entails building a human rights exception into stabilisation clauses, whether explicitly or implicitly; host state regulation to promote the full realization of human rights is outside the scope of the Stabilisation Clause.⁴⁰ The 2003 Baku-Tbilisi-Ceyhan Pipeline Company (BTC) Human Rights Undertaking is a unilateral commitment of the BTC consortium not to interpret the very broad Stabilisation Clause that is included in the BTC contracts in a way that prevents host state regulation from pursuing not only human rights but also environmental goals (as reflected in the formula, health, safety, and environmental standards (HSE), provided that such regulation meets specified requirements aimed at preventing host state abuse. While the undertaking is a unilateral commitment on the part of the consortium, it constitutes a legal, valid and binding obligation and cannot be revoked without the consent of the host states.⁴¹ This argument was central in the reasoning developed by the Texaco arbitrator to reconcile Stabilisation Clauses with state sovereignty.⁴² The undertaking also commits BTC not to seek compensation under the economic equilibrium clause in connection with any action or inaction by the relevant host government that is reasonably required to fulfill the obligation of the host government under any international treaty on human rights including the European Convention on Human Rights (ECHR), labour or HSE in force in the relevant project state from time to time to which such project state is then a party.⁴³

On the negative side, however, the undertaking is an ex-post tool, which was negotiated only after a very broad Stabilisation Clause had been signed and as a result of civil society mobilization against that clause. While the undertaking does emphasize its binding nature, questions remain as to the value that international arbitrators would attach to it should a dispute arise. This is particularly so given that, far from being a mutually agreed amendment to the investment contract, the undertaking is a unilateral commitment entered into by the investor alone. Arguably, integrating a compliance with international law exception in the contract itself and during the negotiation phase would have been a preferable solution.

8. Problems Facing the Enforceability of Stabilisation Clauses

It is safe to say that Stabilisation Clauses are enforceable in the court of law but this is however not without some hurdles. For easy understanding this paper tries to divide these problems into 2, to wit; enforceability under domestic law, and enforceability under international law.

Enforceability under Domestic Law

(a) Constitutional Issues

One of the main issues to consider in relation to enforcement of a Stabilisation Clause is whether, under the constitutional laws of the host jurisdiction, the host state is able to bind itself in this way.⁴⁴ The issue of separation of power is a very serious concern that needs to be looked into by both parties before deciding to include the freezing

³⁸ L Cotula, 'Regulatory Takings, Stabilization Clauses and Sustainable Development' (2008) *OECD Global Forum on International Investment*, 13 <<http://www.oecd.org/investment/globalforum/40311122.pdf>> accessed on 2 May 2018

³⁹ *ibid*

⁴⁰ *ibid*

⁴¹ The Baku-Tbilisi-Ceyhan Pipeline Company, —BTC Human Rights Undertaking, 22 September 2003, sections 3(e) and 6. The undertaking was published by the BTC as a response to pressure from human rights and environmental groups

⁴² *ibid*

⁴³ *ibid.* at section 2(d)).

⁴⁴ Constitution of Nigeria 1999 as (amended) s 4 gives right to the legislature to make laws

Stabilisation Clause in petroleum contract. The freezing clause effectively limits the host state's sovereign power to amend and update its laws.

(b) Domestic Laws

It is not uncommon for petroleum contracts to be enshrined into law by an act of the host state's legislature or decree by the executive thereby elevating the contract and the Stabilisation Clause within it up the hierarchy of norms within the constitutional system. However, even legislative or executive ratification of a petroleum contract cannot provide an IOC with absolute certainty that it can enforce the clause, as there is always the possibility of the contract being held unconstitutional by the judiciary or overturned by a subsequent act of the legislature or executive.

(c) Interpretation of Laws

Another practical issue can arise in the case of freezing clauses if the IOC cannot prove that there was a stable interpretation of the law at the effective date of the petroleum contract. This can be a particular problem with freezing clause which freezes the state's entire body of laws at the effective date of the contract, but even where the parties have identified a limited number of laws to which the freezing clause will apply, the issue remains that it might be difficult for the IOC to prove an established interpretation at the time of the alleged breach.⁴⁵

(d) Authority

International Oil Companies must also be alert to issues of authority. Some jurisdictions do not recognise to a lesser extent, the concepts of agency and implied authority. Therefore, it is important for the IOC to understand which host state entity is entering into the petroleum contract and whether the relevant minister or official signing the contract has actual authority to sign.⁴⁶ This may be particularly important where subsequent governments of the host state are seeking to unwind the actions of the previous government. Where the right authority signs the agreement, its actions will be binding on the state. This principle was applied and followed in the following *Eureko BV v Republic of Poland*⁴⁷ and *Wintershall AG v Government of Qatar*,⁴⁸

(e) Public Interest Considerations

It is important to note that under some jurisdictions, where compensation for a change in law might be considered as a punitive measure or not in the public interest, then enforceability of a Stabilisation Clause may potentially be challenged under domestic law. Stabilization clauses cannot survive where their continuous presence in petroleum contract becomes a threat to the citizens of the host state, this is evidenced in the case of *BP Exploration Co (Libya) Ltd v Government of the Libyan Arab Republic*⁴⁹ where the later unilaterally altered the terms of the concession based on public interest.

Enforceability under International Law

When considering the enforceability of a Stabilisation Clause, it is also important to consider whether international law provides either party with an additional avenue for, or defence against, enforcement of a Stabilisation Clause. Therefore, assuming that the contract has been validly entered into and is enforceable, the IOC's remedy for breach of a contractual Stabilisation Clause will be via the domestic law of the host state.

9. Stabilisation Clauses in Ghana and Israel

Ghana

The Freezing Stabilisation Clauses and the Economic Equilibrium Stabilisation Clauses have been part of Ghana's petroleum contracts for many years. However, after the discovery of oil in large scale commercial quantity in 2007,⁵⁰ Ghana resorted only to the Economic Equilibrium Stabilisation after the prospectivity of its acreage became firmly established in the petroleum industry. Ghana's migration from the use of freezing clauses to Economic Equilibrium Clauses basically unshackles the country from the rigid and constricting effect of freezing clauses.⁵¹ The country has purposely and deliberately moved from a position where it had surrendered its right to rearrange affairs when circumstances deemed it necessary, to a more empowered contractual status which allows it to

⁴⁵ G Booth, 'Stabilisation Clauses for International Oil Firms: Implementation and Enforcement', *OUT-LAW*, July 2015 <<https://www.pinsentmasons.com/out-law>> accessed on July 21 2019.

⁴⁶ *Op cit*

⁴⁷ (2005) Partial Award, Ad Hoc Arbitral Tribunal ICSID.

⁴⁸ (1989) 28 ILM, 795

⁴⁹ *supra*

⁵⁰ C D Hammond & T K Stephens, 'From Total Immunization to an Economic Balancing Act: The Trajectory of Stabilization Clauses in Ghana's Petroleum Agreements' (2019) (1875-418X) *Oil, Gas & Energy Law* (OGEL) <<https://www.ogel.org/journal-advance-publication-article.asp?key=593>> Accessed on 22 August 2019

⁵¹ *ibid*

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renegotiate and review the terms of its Petroleum Agreements to restore economic equilibrium as and when the exigencies so require.⁵²

Israel

The issue of Stabilisation Clauses has come into questioning in bilateral agreement in Israel. Recently, in the case of *The Movement for Quality Government in Israel v Prime Minister*,⁵³ there was a challenge on a key component of the government's controversial framework agreement to develop Israel's newly found natural gas fields, questioning its ability to enshrine the terms of the deal for years to come, without Knesset legislation.⁵⁴ The agreement would grant a two-company partnership to America's Noble Energy and Israel's Delek Group the rights to develop the Leviathan gas field in the Mediterranean, the largest yet found in Israel's territorial waters. The prime Minister of Israel Benjamin Netanyahu⁵⁵ appeared before the court where he urged the deal to be approved. Netanyahu sought to convince the judges to dismiss five petitions submitted by opposition parties and a handful of NGOs seeking an injunction against the plan.⁵⁶ This deal by the government was protested by the people but some predict that, without it, the companies may make good on their threats to pull out altogether. The public regards the stability clause as though the state surrendered to the gas companies. The HCJ found that the Supreme Court, which was a prerequisite for the Gas Plan, unduly restricted present and future governments' freedom to regulate the gas market and hence was undemocratic. The Government was given a period of one year during which it could adapt the Gas Plan. At the end of that year, if an alternative arrangement does not meet the requirements of the Judgment, the Gas Plan will be repealed.⁵⁷ From the foregoing it is clear that the Freezing Stabilisation Clause was present in the aforementioned agreement because the pain of the opposition and the NGO was due to the fact that the agreement limited the Israeli State's ability to regulate strategic sectors of her natural resources after the contract has been concluded.

10. Conclusion and Recommendations

The aim for the insertion of Stabilisation Clause is not solely to impede the sovereignty of the host state or enrich other nations but to ensure that the terms of the contract entered by both parties are kept. However, where the parties decide to modify some certain terms of the initial contract, such modifications should be done in good faith and in accordance with the law. Insertion of stabilization clause in a petroleum contract is not solely to the benefit of the IOCs as perceived by the works reviewed in this research, it could also be beneficial to the host state, for example the insertion of Economic Equilibrium Insertion Clause to a petroleum contract clearly make the IOCs to be more committed to the contract as they won't be restored economically where an alteration is being done on the terms of the contract as a result of their default in keeping with their part of the contract terms. Having said this, it is important that the Nigerian government should take a lot of considerations especially as it affects the populace before entering into petroleum agreement with multi-national oil companies vis a viz as it involves the insertion of stabilization clauses in petroleum agreement.

The Nigerian government should engage experts when going into petroleum agreements with IOCs as these experts will inform them of the different types of Stabilisation Clauses available and the one that best fit their peculiar situation. Every petroleum contract in a developing country like Nigeria must have a stability clause which possess the Economic Equilibrium Stability Clause as this is the most beneficial type of stability clause to a developing country and it allows for the renegotiation of contractual terms after the completion of the contract, the presence of this clause in petroleum agreement reduces legal tussles between the contracting parties and it is the most important type of Stabilisation Clause. It is almost impossible to separate legal dispute from freezing clause, therefore petroleum contracts that contain Freezing Stabilisation Clause should equally make room for settlement mechanism such as arbitration. An adaptation clause should be added to any petroleum contract that has stability clause. This would provide for the renegotiation of the contractual conditions in the presence of a change of circumstances. The renegotiation clause in an agreement allows modifying the agreement which is previously concluded between the parties rather than the termination of contract by either party when a dispute arises. Such flexibility to modify the terms reduces the risk of termination of the entire contract which results because of a dispute between the parties which arises during the course of business. Therefore, it can be termed as a means of stabilizing the relationship

⁵²*ibid*

⁵³(2016)HCJ 4374/15

⁵⁴This means the basic law of the state of Israel. Knesset is the unicameral legislature that makes law for the state of israel

⁵⁵R Wootliff, 'High Court challenges stability clause'(2016) The Times of Israel, 1.< <https://www.timesofisrael.com/high-court-challenges-stability-clause-in-controversial-gas-deal/>> Accessed on 22 August 2 2019.

⁵⁶*ibid*

⁵⁷*ibid*

between the parties. Also adding adaptation clause to a petroleum contract that has a stabilisation clause will help stop the criticism by developing countries like Nigeria relying on the principle of permanent sovereignty over natural resources and the developed countries relying on the sanctity of contract. Every petroleum contract with stabilisation clauses should also cater for environmental hazards and other unforeseen future incidents. It is almost impossible to carry out petroleum activities without causing environmental problems. Therefore, a lot of considerations should be given to the HC when drafting Stabilisation Clauses because their citizens stand to face many risks while the IOCs who are into the business are only concerned with profit making and nothing more pretentious.