Turbo-Charging Investor Sovereignty
Investment Agreements and Corporate Colonialism

BY NICHOLAS HILDYARD AND GREG MUTTITT

"We got a horrible contract with BP, horrible"
-President Saakashvili of Georgia, August 2004[1]

"Without having to amend local laws, we went above or around them by using a treaty."
-George Goolsby, Baker Botts Architect of legal regime for BP's Baku-Tbilisi-Ceyhan oil pipeline.[2]

Reconstruction and construction do not take place only in bricks and mortar. Long before the first foundation stone is laid for a major pipeline, road, mine or oilfield development, the project is constructed on the hard drives of investors, built of financial spreadsheets and legal agreements. Certainly, no less effort goes into engineering these aspects than the physical project itself, and their impacts on communities and the environment can be at least as profound.

But it is here that the analogy with bricks and mortar ends. For corporate investors, the body of project and financial law is a frontier against which they continually aim to advance. Reconstruction of a country's economy, whether following war or dramatic political change, is an opportunity not just to make profits, not even just to apply draconian measures to protect those profits – but to push forward accepted investment practice, setting precedents to be rolled out around the world.

Corporate power never stands still. Blocked from getting what they want in one arena, companies quickly move to develop new mechanisms for bypassing whatever obstacles have been put in their way. Working simultaneously at the national, regional and international level, corporations and their institutional allies in government are constantly assessing and exploiting the political space available to them, never taking it for granted and forever seeking opportunistically to expand its boundaries. Legal and other constraints on corporate behaviour are probed and challenged;[3] policy bodies assiduously monitored, courted and cajoled; and old alliances that no longer achieve the corporate goals of minimum regulation and taxes ruthlessly ditched in favour of new groupings that can deliver the goods. Pragmatic to the last, and operating against an endless and varied background of resistance, corporate power takes what is available to it and builds on it to establish precedent, expand its practice, and claim it as the norm, shoring up the gains made through changes in the law. Successes follow set-backs and set-backs follow successes: nothing is ever taken for granted except the need to rework the framework in which corporations operate in order to reinforce and expand their political base.

For the last three decades, for example, corporate power has lobbied aggressively to liberalise investment rules by removing "distorting" domestic regulations (such as performance standards[4] and constraints on repatriation of profits[5]) and empowering private investors to extract compensation from foreign governments for any legislation that adversely affected inward investments. For companies, the Holy Grail has long been a global investment regime, imposing binding rules favouring investors worldwide – a regime that enhances the companies' powers of retaliation in the event of their "investment rights" being infringed by elevating a simple contract dispute into a breach of international law, thus enabling their home governments to weigh in on their behalf.

To date, the companies have been denied that goal by civil society resistance. In the early 1970s, the USA pushed to include investment in the Tokyo Round of the General Agreement on Tariffs and Trade (GATT).[6] When that failed, due to opposition from developing countries, corporations pressed their national governments to secure corporate investment interests through bilateral agreements[7] and regional initiatives, including rights for companies to take their disputes with States to international arbitration. In the early 1990s, the companies moved back to the international stage, this time seeking to push a binding investment Treaty – known as the MAI or Multilateral Agreement on Investment – through the Organisation for Economic Co-Operation and Development (OECD).[8] When the negotiations collapsed following massive public opposition, corporate power returned to GATT's successor, the World Trade Organisation (WTO), only to be rebuffed once again.[9] This is unlikely to be the last attempt.

Unable as yet to achieve what they wanted through multilateral negotiations, corporations have reverted to Plan B (or perhaps it was always Plan A), once again relying on bilateral and regional Treaties to push their investment interests. On the one hand, companies are increasingly using the arbitration clauses of Bilateral Investment Treaties (BITs) to challenge national laws (including environmental laws), local administrative regulations, taxes and other governmental actions that are deemed detrimental to the value of their investments,[10] or to push through new obligations such as the requirement to "protect" intellectual property rights[11]. On the other, company lawyers are using existing or specially-negotiated BITs to turbo-charge standard concession agreements, imposing project-specific legal regimes – known as Host Government Agreements (HGAs) – that give companies effective control over the legislation and regulations that apply to their activities and require States to compensate them for *any* new laws that affect corporate profits.

Meanwhile, oil, gas and other extractive industry companies are also using and evolving legal instruments first developed in the 1960s – Production Sharing Agreements (PSAs) – and imposing new or tightened conditions which have allowed corporate power to gain almost complete control not just over the laws that apply to their activities but over the very development of the host States' natural resources. Having used Host

Government Agreements and Production Sharing Agreements to win hugely favourable investor rights in the countries of the former Soviet Union and in West Africa, corporate power is now applying the same legal instruments to impose a new era of resource colonialism in Iraq.

From Colonial to Neo-colonial

It is not new for investment agreements to give corporations extensive rights, prodigious profits and minimal obligations: where recently-negotiated investment agreements differ from those in the past is in the extent of their enforceability and their dominance over international, national and municipal law.

Generous agreements were signed during the colonial period, either by direct rulers, or by their local puppets. For example, in 1936, the British Governor of Nigeria, Sir Bernard Bourdillion, granted a consortium of BP and Shell rights to all of the oil in the entire country. In Iraq, the British-installed monarch Faisal in 1925 signed a concession with a consortium of British and French (later joined by American) companies. The Iraqi concession was for a period of 75 years, and along with two further concessions signed in the 1930s (one with a subsidiary of the same consortium; the other to a company which it subsequently bought out), the consortium obtained, like in Nigeria, rights to all of the oil in the entire country.

In the middle of the twentieth century, as colonial empires were crumbling, corporations had to seek new means to defend their investments, in particular from the growing nationalist movements. In the case of the oil industry, the collapse of empire was followed by the setting of tougher terms by host governments, the renegotiation of existing agreements, and in many cases nationalisation of assets.

A key test came in Iran, when populist leader Muhammad Mossadegh nationalised BP's (then known as the Anglo-Iranian Oil Company) oil operations in 1951, in a move reflecting popular frustration at the unfair terms of the 60-year concession agreement with the company.

As lawyer Anthony Sinclair has documented, BP lobbied hard to persuade its major shareholder, the British Government, to take up the defence of its contracts in the international courts.[12] Although the Government complied, its case failed because the company's contracts were deemed insufficiently rigorous to allow the International Court of Justice to hear the case.[13] Unable to achieve what they sought through the courts, the UK Government, together with the US, staged a MI6 and CIA sponsored coup.[14]

BP – and other companies - learned major lessons from this experience in Iran. Having failed to fend off nationalisation in the courts, BP was advised by its legal counsel that in future the company should include a special clause (known as an "umbrella clause") in its new contracts with Iran that would nestle the contracts within a UK-Iran treaty, thus ensuring that they would automatically be governed by international law.[15] A dispute between the company and Iran would thus be transformed into a dispute between the Government of the UK and the Iranian Government.[16]

In the event, such umbrella clauses were not included in the new contracts – although they were considered during the drafting – largely because it was deemed unlikely that the UK government would wish to become embroiled in the minutiae of every dispute under the contract. Nonetheless, the idea of "umbrella clauses" had been seeded – and over the coming decades, companies would further explore their potential, along with other legal instruments, to achieve greater corporate control over investments in an age of "decolonisation" and increasing nationalism.

By the 1990s, the avenues first developed by BP's legal advisors were beginning to bear fruit. With public funding for development through the multinational development banks declining, southern countries were under increasing pressure to agree to investment terms that were highly advantageous to companies in order to attract inward investment. Indeed, the companies and the MDBs repeatedly told them that they had no option but to do so.

Encouraged by this, companies began to expand the scope of investment contracts to gain exemptions a range of environmental and other legislation.

But the companies went beyond simply demanding exemptions to local law. Spearheaded by the multinational oil companies – or more accurately their lawyers[17] – corporate power began pioneering new legal arrangements (known as Host Government Agreements) which closely mimicked those first suggested by BPs lawyers in the 1950s.

The collapse of the Soviet Union, and the subsequent rapid liberalisation of its economy under conditions where the state was relatively weak and corporations strong, presented the ideal opportunity to roll out the new approach. New-style agreements were signed in the 1990s, not just in the former Soviet republics, but also (following the end of the Cold War and the discovery of deepwater oil extraction technology) across West Africa.

Learning the lessons of Iran, the new agreements explicitly sought to "internationalise" the investment contracts being signed with foreign states[18], thereby elevating contract disputes into violations of international law. In some cases, this has been achieved by invoking clauses in the new Bilateral Investment Agreements or regional trade agreements that have proliferated since the 1980s. In others, new treaties have been signed with the specific aim of shrouding individual contracts within their protective cloak. This has not only enabled the companies whose "rights" have been infringed to remove investor-state disputes from the jurisdiction of national courts, but also to mobilize the entire diplomatic weight of their home government against the offending host state to remedy the breach.[19]

THE CASE OF THE BAKU-TBLISI-CEYHAN OIL PIPELINE

As in Iran, BP has been at the forefront in designing and promoting the new agreements. Indeed, the legal regime which the BP-led consortium negotiated for the Baku-Tbilisi-Ceyhan oil pipeline project, which will transport oil from BP's Caspian oil fields via Georgia to Turkey's Mediterannean coast, has broken new ground in the use of international investment agreements to exempt companies from regulation and insulate them from local legal accountability. The agreements thus merit close analysis, not least because BP and other companies are promoting them as a template for future oil pipeline projects.

The legal agreements for the projects were drawn up in secret – when western non-governmental organisations investigating the project visited Azerbaijan in 2001, a year after the agreements had been ratified by Azerbaijan, the project documents were not even available to parliamentarians, let alone members of the public.[20]

The legal regime for the project consists of two layers of agreements: first an Inter-Governmental Agreement (IGA) between Azerbaijan, Georgia and Turkey, which has the status of a Treaty; and second, three separate Host Government Agreements between the companies in BTC Co, the consortium which owns and will operate the pipeline, and each of three countries. The HGAs are defined as private law contracts.

Under the agreements, which are specifically aimed at guaranteeing the "freedom of petroleum transit", a formulation that effectively claims rights for oil itself,[21] the three governments have all but surrendered sovereignty over the pipeline route to the oil consortium.[22] Not only do the agreements trump all existing and future laws in the three countries, other than the respective constitutions, but they also impose obligations that severely limit the State's ability to act in the interest of its citizens. Moreover, they go far beyond the norms of traditional concession agreements (see below).

Using Treaty Status to Trump National Law

Standard concession agreements are invariably subject to national host State law.[23] The HGAs for the BTC pipeline, by contrast, have been drawn up under (and therefore nest within) the framework of what is in effect an international investment treaty. The companies therefore claim that

HGAs automatically assume the status of international public law while simultaneously remaining private contracts.[24]

The internationalisation of the concession agreements for BTC reveals how well BP has learned the lessons of Iran. As "treaties", the HGAs have a privileged status since, as the European Bank for Reconstruction and Development (EBRD) notes, "in general, a treaty takes precedence over inconsistent domestic law, even subsequent domestic law."[25] The provisions in the HGA thus trump all domestic law. Moreover, as a "treaty", the HGA is far more difficult for a new government to overturn than an ordinary Act of the national legislature.

Although BP argues that a treaty between the three countries was necessary in order to ensure that the pipeline was subject to a uniform legal regime, other cross-border projects – notably many existing trans-border pipelines[26] – have long been operated without being subject to specially-negotiated treaties. Moreover, the regulations to which the pipeline is subject under the agreements differs significantly from country to country: for example, land acquisition is carried out differently in Turkey and Georgia, with affected citizens in Georgia receiving higher compensation. If uniformity was initially the avowed aim, therefore, it was quickly jettisoned once the pipeline began to be built. Indeed, the true explanation for placing the HGAs within a Treaty is revealed by James Goolsby of Baker Botts, the Houston-based energy-sector law firm which was the legal architect of the agreements: "Without having to amend local laws, we went above or around them by using a treaty."

In effect, BP specifically married two legal instruments – a BIT (or more accurately, given the three countries involved, a Trilateral Investment Treaty) and a private contract concession agreement – specifically in order to circumvent local law.[27]

Corporate Sovereignty

Until recently, exemptions from specified laws – usually those that companies find most onerous – used to be rare in investor-state contracts. Increasingly, however, there is a growing trend for exceptions and exemptions to be included in concession and other agreements.[28] Recently, for example, the Government of Belize not only exempted the proposed Chalillo Dam from any environmental laws other than those which the Canadian-owned project developer[29] had agreed to follow[30] but also to waive all taxes[31], except payroll taxes. An Act was also passed into law which put the project beyond legal challenge by any court[32] – thereby arguably violating the protection of judicial rights guaranteed under the Inter-American Human Rights Convention.[33]

But the exemptions gained by BTC Co go several steps further – exemptions which, as the project lawyers themselves have hinted, had to be pushed through over objections by the host governments.[34] Under the Host Government Agreements, the BTC consortium is exempted from *any* obligations under Azerbaijan, Georgian and Turkish law, aside from the Constitutions of the three countries, where those laws conflict with the terms of the agreements. In signing those agreements, the host governments have effectively abrogated[35] their executive and legislative powers to protect their citizens from potential environmental damage and associated health and safety hazards or to improve the regulatory regime. By locking themselves into a frozen and drastically weakened regulatory environment, the governments are thus less able to respond to new environmental and other threats or to the evolving understanding of risk.

The HGAs have already been invoked to override Georgian environmental laws and to force the Georgian Minister of the Environment to sign off on the pipeline route despite grave reservations about its legality under Georgian environmental law.[36] Both BP and the US government put pressure on the Minister, through then President Shevardnadze.[37] The Minister was forced first to concede the routing with environmental conditions, and then water down her conditions. Since the project agreements have a higher status than other Georgian laws, the environment laws the Minister referred to were simply irrelevant.

Ultimately, on the day of the deadline, the President called the Minister into his office, and kept her there until she signed, which was at about 4 o'clock in the morning.[38]

In Turkey, too, the HGAs have been invoked to set aside stricter environmental and social legislation. Critically, provisions in the HGA were invoked to truncate the "scoping period" for the Environmental Impact Assessment. In a letter to BTC Co, dated 29th November 2001, the Ministry of Agriculture and Rural Affairs waived the requirement for site investigations (despite an almost total absence of on-the-ground data on flora and fauna along the pipeline route) before granting approval for the pipeline route "in accordance with the Host Government Agreement".[39] The normal requirement, under Turkey's environmental regulations, for a 60-day period for the Ministry of the Environment to review and approve the final draft of the EIA, in order to give a development consent, was also reduced to 30 days for BTC, in order to ensure that BOTAS, the Turkish company contracted to build the Turkish section of the pipeline, could complete the project in the period specified under the project agreements.[40] The project agreements also overrode key provisions in Turkey's Expropriation Law which require the price for expropriated property to be negotiated: instead, it was compulsorily purchased, under an emergency law normally invoked only in times of national disaster or war, under the terms of the agreements.[41]

BP has countered that the exemptions it obtained were nothing out of the ordinary and are common to other concession agreements. The company states: "The creation of a prevailing legal framework is not unusual and has been used by extractive projects even in nations with highly developed legal systems, such as Chile, Canada and Australia."[42] Justifying the BTC Host Government Agreement, it adds: "The Prevailing Legal Regime (PLR) is designed to *supplement* the existing framework, rather than replace existing laws and regulations".[43]

In fact, the HGAs for the BTC project go far beyond simply "supplementing" existing legislation. As the term "Prevailing Legal Regime" (PLR) accurately reflects, they *prevail* over such legislation: indeed, their express intent is to provide investors with the right to exempt their projects from specified laws and regulations. BP is fully aware of this: indeed, BTC's own Citizens Guide to the Project Agreements explicitly acknowledges that the legal regime that the company has crafted for the project grants investors the power to "supersede provisions that directly conflict with project agreement requirements."[44]

Substituting Corporate Standards for National and International Law

Although BP accepts that the agreements trump local law,[45] it insists that they set out a more stringent and coherent environmental and social regulatory regime than would otherwise be available.

In fact, the Agreements replace hard law with voluntary, vague, and unenforceable corporate guidelines. Under the Intergovernmental Agreement,[46] the "floor" requirements for the project are a set of non-binding, loosely-worded and largely technical petroleum industry pipeline "standards". Where these "standards" conflict with local environmental and labour law, the "standards" win out.[47, 48] "Soft" industry guidelines have thus been allowed to replace "hard" law, with the environment and human and labour rights the losers.

As Amnesty International notes: "Instead of referring to internationally recognised human rights standards, the agreement between the state and the consortium says that the project is to be regulated by 'the standards and practices generally prevailing in the international petroleum industry for comparable projects.' Apart from the fact that on BP's own admission these standards have never been formulated, this is not a substitute of like for like. It jettisons the carefully worked out balances made by the regional and international bodies charged with fixing the dimensions of basic rights and instead the reference point becomes the consensus among actors in the petroleum industry on how things should be done."[49]

BP cites a clause in the Intergovernmental Agreement[50] to argue that the project *must* comply with "EU standards", [51] implying that the body of EU law will be honoured.[52] In reality, however, the IGA's commitments only extend to those (unspecified) "standards" that relate to "technical, safety and environmental" practices within the petroleum industry. Beyond this, the phrase "European Standards" remains undefined in any of the legal agreements or project documents which form the legal regime for the project. [53]

If (as BP has argued) the phrase is taken to refer to "European Union Directives",[54] the project falls below this floor in a number of important areas. For example, the "applicable EU Directives" listed in the Environmental and Social Impact Assessment (the project document that sets the legally-binding standards for the project[55]) do not include such key EU Directives as the Strategic Environmental Impact Assessment Directive (2001/42/EC), reflecting a "pick and mix" approach to the applicability of standards. In addition, the Supplementary Lenders Information Pack for Turkey makes no mention of either "EU standards" or "EU Directives" as the floor for the project. Instead it states: "The BTC project standards will adhere to Turkish and/ or World Bank standards, whichever is the more stringent".[56]

Further confusion arises from many project standards falling below those that would be required under relevant EU Directives. The Environmental Impact Assessment's Matrix of Environmental Standards and Guidelines clearly indicates, for example, that emission standards for the pipeline would exceed (or would be likely to exceed) three applicable European Union directives[57]: in the case of nitrous oxide, permitted emissions exceed relevant EU directive standards by 78% and the EU sulphur directive standards by 283%.[58]

The claim that "EU standards" provide a floor for the project also conflicts with the choice of field joint coating system for the pipeline in Azerbaijan and Georgia. Far from meeting "generally applicable industry practice in the European Union", the chosen coating is entirely experimental. As has now been confirmed by the UK government,[59] the coating (known as SPC 2888) has never previously been used on a similar operational pipeline anywhere else in the world – and is therefore outside the experience of industry practice whether in Europe or elsewhere.

The coating, which was not tested in field conditions on a polyethylene-coated pipeline (such as is being used in the BTC project) until after it had been selected by BP,[60] was chosen despite strong objections from Derek Mortimore, BP's own expert consultant, and in the face of criticism from within the industry. Reviewing the specification for the selected coating, Mr Mortimore, warned: "I am at a loss to understand why this specification has been issued. Purely as a coating it is underdeveloped and incomplete. As a field joint coating specification, it is utterly inappropriate as it does not confirm a protective system that can be successfully applied in all the conditions under which this pipeline will be constructed, nor does it confirm the integrity of the protection for the design life of the pipeline." [61] The pipeline coating system has since experienced multiple failures in the Azerbaijan and Georgia sections of the pipeline.[62] Recent press reports indicate that such failures continue despite remedial measures undertaken by BTC Co.[63]

Freezing out New Social and Environmental Legislation

"Stabilisation" clauses – under which governments agree to compensate concessionaires for changes in legislation that adversely affect their business – are now common to many concession agreements. When first introduced, companies sought to use the clauses to freeze the legal framework of the host State once-and-for-all by *prohibiting* changes to the law.[64] However, this quickly fell foul of the courts. As Marcos Orellana of the Centre for International Environmental Law comments: "This extreme construct was challenged on several grounds, including fundamental principles of self-determination and the permanent sovereignty over natural resources. After early arbitration cases involving Libya revealed that this rigid model broke in the face of political and economic crises, greater flexibility was introduced to stabilisation clauses, including obligations to negotiate if circumstances changed or to compensate if legal changes radically altered the expected economic returns of the project."[65]

That need for flexibility and the accompanying emphasis on negotiation is reflected in the model investment agreement that has been drafted by the United Nations Commission on International Trade Law (UNCITRAL), the inter-governmental body that makes recommendations on investment rules. UNCITRAL makes the rather obvious point that corporations, like citizens, should expect changes in the law: [66] indeed, such change is part and parcel of democracy. Stabilisation clauses should therefore be limited in their scope, only covering "specific legislative changes that target the particular project, a class of similar projects or privately financed infrastructure projects in general"[67] or changes in economic circumstances that could not reasonably have been foreseen at the time of the contract being signed.[68] The OECD similarly recommends that stabilisation clauses should not grant blanket rights to compensation for any new legislation that might adversely affect an investment but should be restricted to legislation that is clearly specified.[69] In addition, the OECD rejects the demand for generalised, unspecific damages in the event of new legislation incurring economic costs: the financial costs that are to be covered must be "clearly and precisely described".[70]

Moreover, in keeping with the stabilization clauses in standard contracts are generally "two-way" in their application. India's model concession agreement, for example, allows for the company to negotiate new terms where a change in law leads to a rise in costs – but equally for the government to seek amendments where new laws reduce the concessionaire's expenses.[71] Generic claims – such as "disruption to the economic equilibrium" of a project (the phrase used in the BTC stabilization clause)[72] – would not therefore be acceptable.

Indeed, the stabilization clauses in the BTC contract completely disregard both the letter and the spirit of UNCITRAL's recommendations: not only are they so broad brush as to effectively cover any new changes in social and environmental legislation[73] but they allow for no equality of treatment. Under the HGAs, the host governments are bound by the HGAs to compensate the BTC Consortium for *any* changes in the law that the three countries may introduce over the 40-year lifetime of the project (including changes aimed at improving protection of human rights or the environment) where such changes adversely affect the profitability of the project.[74]

The broad, sweeping nature of the BTC's stabilisation clauses led Amnesty and other human rights groups to warn that the clauses were likely to have a "chilling effect" on the State's adherence to human rights standards – the fear of having to pay compensation causing the three states not to implement new human rights obligations.[75]

Amnesty also warned that other clauses in the Intergovernmental Agreement and the HGAs could further freeze out action by the three governments to protect the public interest. In particular, Amnesty and others expressed grave reservations about: the HGA's stipulation that the pipeline may only be shut down in the event of an "imminent, material threat"; the specific denial within the Intergovernmental Agreement that the project has any public purpose (thus preventing governments from invoking a public interest defence for intervening to protect the public); and the wording of the clauses relating to security along the pipeline route, which could be used to justify severe human rights abuses.[76]

In September 2003, in an effort both to assuage concerns within the legal community and to ensure the support of the World Bank and other public funders, the BTC Co. published a Deed Poll, entitled the BTC Human Rights Undertaking,[77] in which it undertook not to invoke the compensation clauses in the HGA in the event of new laws being introduced for human rights or environmental reasons. Legal opinion, however, is divided on the efficacy of the Deed Poll, not least because it is only signed by the BTC Co. and does not form part of the bundle of documents that constitute the prevailing legal regime. Indeed, the HGAs and Intergovernmental Agreement remain unaltered.[78]

Moreover, BTC Co. has since qualified its commitments under the Deed Poll, stating that it reserves the right to invoke the stabilisation clauses if it deems new legislation to constitute "rent-seeking".[79] The Deed Poll also makes it clear that it does not apply where legislation introduced by the three governments is more stringent than EU standards, World Bank Group standards and existing international and human rights treaty obligations.[80] In effect, the Deed Poll places an explicit cap on the ability of the host governments to regulate as they (rather than BP) see fit, severely constraining their ability to pioneer new legislation that is more protective of the public interest than that in the European Union.

All the Powers of a State – without the Liabilities

Susan Leubuscher, the researcher who first alerted the international NGO community to the colonial nature of the new legal arrangements being put in place by oil companies under the umbrella of BITs, through her work on Exxon's Chad Cameroon oil pipeline, has warned that HGA-type contracts have the power to transform "multinational enterprises into *ad hoc* legal institutions with the power to dictate the law that governs their own relations with States and their activities within States."[81]

Such powers are evident from the provisions of the HGAs negotiated for the BTC pipeline. But whilst the companies have imposed obligations on the states – and taken over a number of prerogatives of the state (for example, in the case of Exxon-Mobil's Chad-Cameroon pipeline, the power to derogate from obtaining permits to enter private land[82]) – they themselves have been assiduous in protecting themselves from liability. Whilst, for example, the project agreements oblige the states to take any action necessary to protect the pipeline – a highly worrying prospect given the human rights record of the three states[83] – they also absolve the BTC consortium from any liability for any human rights abuses that might arise.

The consortium has also sought considerable protection for itself in the event of a pipeline leak – which many consider an inevitability, particularly given the controversy over the choice of anti-corrosion coating for the pipeline.[84] The rights of individuals to sue for damages that arise from the operation of the pipeline are minimal and the chances of a fair hearing are slim. In addition, individuals are likely to have to act against not only the companies but also their own national governments, since investment agreements place the onus on the states to ensure that the pipeline is operated safely. In all three states, such a challenge by ordinary citizens – particularly if it was likely to result in major costs to the state – is likely to result in political pressure being exerted on the courts.

Indeed, whilst the Agreements have created legal certainty for the companies, they have only been able to do so by causing legal mayhem for ordinary citizens. The layer upon layer of agreements, coupled with the hybrid public/private nature of the contracts, have severely muddied the waters of redress for third parties, potentially denying citizens access to justice. Indeed, the European Bank for Reconstruction and Development, in a commentary on the agreements, itself acknowledges the uncertainties. "Clearly [a right of action for local citizens if BTC Co. breaches the environmental or social standards set out in the HGA] cannot accrue as a matter of contract, since the third party is not part of the HGA. However, the argument is that, by virtue of the ratification of the HGA as a part of local law, the right becomes part of domestic legislation. *Presumably* on this basis such a right would also be enforceable in domestic courts, not just through the mechanism of international arbitration set out in the HGA. This provision granting rights to third parties in this manner is unusual in the context of such agreements and an *interesting* development"[85] (emphasis added). Interesting perhaps for lawyers, but a matter of livelihood for those directly affected – and an issue on which citizens have a right to expect clarity, not experimentation.

Undermining the Rule of Law

The use of HGAs is now openly endorsed by the multilateral development banks, such as the World Bank, which raised no public objections to the BTC contracts. On the contrary, the World Bank funded the BTC project, just as it had previously funded the Chad Cameroon pipeline, in the face of similar public concern over the project agreements.

Yet HGAs and the BITs under which they are being negotiated threaten more than just an increase in the power of already powerful corporations – problematic as this undoubtedly is. By allowing companies to supersede the state's national and international human rights and environmental obligations, as built up through years of domestic and international negotiation and civil society pressure, they also threaten to undermine the comprehensive international, national and local legal frameworks that have been patiently and painfully established over the years – a comprehensive framework which, as Kofi Annan has stated, "makes the modern world a far better place to live than before."[86]

Indeed, by lending their support to HGA-type project agreements, governments and multilateral institutions are taking foreign direct investment and corporate accountability in a direction that is precisely the opposite of that being encouraged by the UN. In that regard, the July 2003 report by the UN Commission on Human Rights on *Human Rights Trade and Investment* specifically recommends that investment agreements – far from overriding human rights law – should include among their objectives "the promotion and protection of human rights".[87] It also recommends that States should "avoid the situation where a requirement to pay compensation might discourage States from taking action to protect human rights."

DELIVERING THE INDUSTRY WISH LIST

If HGAs are being used – in conjunction with BITs – to allow corporate power to dictate the laws that frame its infrastructure investment projects, Production Sharing Agreements (PSAs) are being used to establish control over a state's natural resources. And, like HGAs, PSAs are now being adapted to guarantee corporate profits at the expense of states.

PSAs were first developed in Indonesia in the late 1960s, at a time when the European empires around the world were collapsing. PSAs were seen by many as reflecting a new era of national control over resources, and a rejection of the colonial-era concession agreements that had persisted for more than 50 years previously. In response, industry insiders reportedly viewed PSAs as having "something Communist" about them.[88]

But, compared with the nationalisations that took place in most major oil-producing countries just a few years later, PSAs quickly seemed rather more appealing. Now they are oil companies' contract of choice in most developing countries.

Symbolic sovereignty

It was not long after the introduction of PSAs that oil companies realised that – despite their apparent differences – PSAs could deliver just the same results as the old concessions. In particular, PSAs can provide oil companies exactly what they most seek when investing in a country: guaranteed access to oil reserves; predictability of tax and regulation; and the opportunity to make large profits. And like the colonial-era concessions, they can do this through either reasonable or draconian legal measures.

Professor Thomas Wälde, an expert in oil law and policy at the University of Dundee, has described PSAs as "A convenient marriage between the politically useful symbolism of the production-sharing contract (appearance of a service contract to the state company acting as master) [combined with] the material equivalence of this contract model with concession/licence regimes in all significant aspects".[89] He explains, "The government can be seen to be running the show - and the company can run it behind the camouflage of legal title symbolising the assertion of national sovereignty."

PSAs refer to the private investor as a

"contractor", while the state remains the owner or client. The implication is that the state calls the shots. However, in practice, the lead private company within the consortium is still the "operator", making day-to-day decisions, while the rights and obligations of either side are at least as closely specified in a PSA contract as in a standard concession contract, and any not explicitly specified are not actionable. Like with HGAs, this may go so far as to deny the state the right to regulate or legislate.[90] As a result, the change from concessionaire to "contractor" is essentially a terminological, more than a substantive, one.[91]

Most PSAs specify that any disputes would be resolved not in the courts of the country concerned, but in international arbitration tribunals administered by the International Centre for Settlement of Investment Disputes (ICSID) in Washington, DC or the International Chamber of Commerce in Paris. These arbitration hearings are generally closed to other than contract parties and are presided over by tribunals consisting generally of corporate lawyers and trade negotiators – as such, they tend to narrowly favour commercial interests rather than broader issues of national interest or sovereignty. As Susan Leubuscher comments, "[The] system assigns the State the role of just another commercial partner, ensures that non-commercial issues will not be aired, and excludes representation and redress for populations affected by the wide-ranging powers granted [multinationals] under international contracts".[92]

Also like HGAs, PSAs frequently contain stabilisation clauses, protecting the investor's profits from future changes in regulation. Often this is done by requiring the state partner (usually the state oil company) to bear the "risk" arising from legislative change. Whereas formerly, such provisions were applied to changes in taxation, by making the state oil company liable for taxes (payable out of the state share of profit oil), more recent contracts apply the same approach to reduced profitability arising from legislation as well.[93]

The majority of PSAs are ratified as Acts of parliament, making them laws in their own right, and many are negotiated within the framework of the Energy Charter Treaty, or make reference to BITs, thus nestling them within international agreements. Like the BTC Host Government Agreements, the provisions of PSAs generally include clauses setting out exemptions to national laws and obligations to compensate companies in the event of new legislation interfering with profits. [94]

Maintaining the economic status quo

PSAs also have profound economic implications for states, in the extraction of their non-renewable resources.

PSAs appear to shift the ownership of oil from companies to state, and invert the flow of payments. The mechanism is based on the division of the extracted oil into 'cost oil', which is used to repay development and production costs, and the remaining 'profit oil', which is shared between company and state in agreed proportions.

Whereas in a concession system, foreign companies are granted rights to the oil, and must compensate host states through royalties and taxes, in a PSA, the oil is defined as the property of the state, and the foreign companies are compensated both for the costs they have expended (through 'cost oil'), and for the risk they have taken in investing their capital (through their share of 'profit oil').

But just as a concession system can set any rate of tax and royalty (in theory, anywhere between 1% and 99%), so in a PSA, the profit oil can be split in any proportion (as can other features of the PSA).

There is a clear parallel with the legal aspects discussed above. In one of the standard textbooks on petroleum fiscal arrangements, industry consultant Daniel Johnston comments:[95] "At first [PSAs] and concessionary systems appear to be quite different [from each other] symbolic and philosophical differences, but these serve more of a political function than anything else. The terminology is certainly distinct, but these systems are really not that different from a financial point of view".

Importantly, PSAs are like concession systems in giving oil companies the potential for enormous profits. Unlike technical service contracts, where a contractor (often a company like the US oil services company Halliburton) receives a fixed fee for services carried out for a client (for example, a state oil company), or risk service contracts, where the contractor receives a specified rate of return on capital invested, in PSAs a company receives a share of overall profits from the venture.

In a project to extract natural resources, there are high risks that resources may not be found (exploration risk), that the development may not go to plan, or may over-run on costs (development risk), or that the project may be made unprofitable by changes in commodity prices (price risk). Meanwhile, large up-front capital investment is required to develop the infrastructure to extract the resource. The theory behind the PSA and concession models – and the model under which major oil companies like BP, ExxonMobil and Shell operate, in contrast to service companies like Halliburton – is that capital is risked by an investor. In some cases the project will be unsuccessful and the capital will be lost; these cases are offset by the successful ones, where very large profits are obtained.

While this model may be appropriate in some cases where risks are too high for a state to bear itself, or where a project is beyond the state's technical competence, they are increasingly being applied to lower-risk situations, in particular in the states of the Former Soviet Union. In countries such as Russia, Kazakhstan and Azerbaijan, PSAs – contracts designed to deal with high risk – are being applied to fields that were already discovered during the Soviet era, where the exploration risk is reduced to nil, in states that already possess considerable technical competence from their long history in the oil industry. As we shall see, much the same process is now being pushed – even more inappropriately – in Iraq.

Complexity as a weapon

Oil companies consistently argue for taxation to be based on profits, not on production. They argue that profit taxes can respond more effectively to economic circumstances, and ensure that the state obtains a share of any excess profits. This may be true, but there is another respect in which systems such as PSAs appeal to investors: that they are more complex.

At the other end of the scale from PSAs, the simplest system of payment to a state by a private investor which extracts its natural resources is the royalty, whereby a percentage of the total value of the resource is paid to the state, effectively 'buying' the resource. In this case, the amount owed by the company is readily and easily reckoned – it is a straight percentage of the output volume, multiplied by oil price.

But in a PSA, the system's very complexity throws up numerous ways in which companies can reduce their tax payment by the clever use of accountancy techniques. Not only do multinationals have access to the world's largest and most experienced accountancy companies, they also know their business in more detail than the government which is taxing them, so a more complicated system tends to give them the upper hand.

Thus a company can obtain profit not just from the *profit oil*, but also from *cost oil*. Although that is not intended in the deal, careful accounting and financial management can allow the companies to exploit loopholes in the tax rules. For this reason, the details of how profits are calculated, what costs are allowable and so on are very important.

Furthermore, while it is possible to devise ever more sophisticated tax systems, which respond better to both circumstances and policy priorities, the drawback is that complexity removes transparency: if the tax system is understandable only to experts, there is little chance of public accountability. Production sharing agreements often consist of several hundred pages of technical, legal and financial language. Even when they are not treated as commercially confidential (which they often are), they do not lend themselves to public scrutiny.

One result of this complexity can be that even when a government thinks it has got a good deal, it may later find itself receiving rather less income than it had bargained for – even in countries with long experience of oil development.

For example, in the Sakhalin II project in Russia's Far East, currently being developed by a Shell-led consortium, the way the PSA is written, all cost over-runs are effectively deducted from the state's revenue, not the consortium's profits.[96] During the planning and early construction of the project, costs have inflated dramatically. In February 2005, the Audit Chamber of the Russian Federation found that, as a result of the terms of the PSA, cost over-runs had already cost the Russian state $2.5 billion.[97]

Guaranteeing profits

Russia's Sakhalin II and Azerbaijan's Azeri-Chirag-Guneshli (ACG) PSAs are examples of a newer form of PSA, designed to guarantee private investors' profits. As explained above, PSAs divide 'profit oil' between state and private company in agreed proportions. In a more complex form, this split is not fixed at one level, but is given a sliding scale, intended to reflect the profitability of the venture.

The theory is that the more profitable a venture, the quicker costs are recovered, and so, the more is available for the state. Initially, the sliding scale was set according to the rate of production or cumulative production from a field. For example, in Syria, the state's share of profit oil ranges from 79% for fields producing less than 50,000 barrels per day, to 87.5% for fields producing more than 200,000 barrels per day.

Within these, production rates were used as a proxy for profitability – in general, the larger a field, the more profitable it is. A newer innovation was to base the sliding scale more directly on profitability – either the company's internal rate of return, or an 'R'-factor, which is defined as the ratio of cumulative receipts to cumulative expenditures.[98]

In the ACG PSA, the Azerbaijan state only gets 30% of the profit oil until the BP-led consortium has achieved 16.75% rate of return – a comfortable level of profits. After that, the state's share goes up to 55%. Only after the consortium has achieved a 22.75% rate of return – a high level of profits – does the state's share of profit oil go up to a more normal 80%.[99]

The Sakhalin II PSA goes even further. In that case, the Russian state gets no profit oil until the Shell-led consortium has achieved 17.5% rate of return. The state then receives just 10% for a further two years, and then 50% until the consortium has obtained 24% rate of return, after which the state receives 70%.[100]

Much as with the opposition to royalties, the argument for rate-of-return style PSAs is based on allowing the state to capture a reasonable share of profits, but in practice the impact can favour the investor. Effectively, there are three consequences:

1) the investor's profits are effectively guaranteed, by denying the state a fair share of revenue until the specified profit has been achieved;

2) while the specified level of profits is assured, this does not preclude the investor from obtaining much higher profits (at the more normal, lower share of profit oil);

3) it is in the investor's interests to inflate costs (a process known as 'gold-plating'), especially if the company can sub-contract operations to another company in the same group (for example, from one Shell subsidiary to another Shell subsidiary) – as the subcontractor profits from its work, the project operator still profits according to the PSA, and the state gets little or nothing.

As such, investors transfer much of their risk back to the state. The investor has achieved the gambler's dream – guaranteed comfortable profits, with a opportunity if successful of enormous profits.

FROM THE CASPIAN TO IRAQ

Having used PSAs and HGAs to establish control over the production and transport of oil out of the Former Soviet Union, oil companies see Iraq as a new frontier to push the approach out more widely.

Indeed, this move can be seen in one of the key players that pushed corporate-friendly tax and investment regimes in the Former Soviet Union, the lobby group International Tax and

Investment Center (ITIC).[101] Since its launch in 1993, ITIC has primarily focused on the former Soviet Union, and has offices in Baku, Almaty, Astana, Moscow and Kiev. More recently, it has expanded its work to lobbying for the use of PSAs in Iraq's oil industry.[102] Its 2004 strategy review concluded that this project "should be continued and considered as a "beachhead" for possible further expansion in the Middle East."[103]

Although oil was excluded from the sweeping privatisations enacted by US administrator Paul Bremer in 2003, major moves to open the sector to multinational oil companies are now imminent. A Petroleum Law will be enacted soon after the elections in early 2006, which according to sources in the government, will allocate all of Iraq's oilfields that are not currently in production to multinational oil companies. This is most likely to be through production sharing agreements (PSAs), the mechanism favoured by the oil companies.

Only 17 of Iraq's 80 known fields, and 40 billion of its 115 billion barrels of known reserves, are currently in production.[104] Thus the policy potentially allocates to foreign companies 64% of known reserves. If a further 100 billion barrels are found, as is widely predicted, the foreign companies would control 81% of the total, and if 200 billion were found, as some suggest, they would have 87%.

Officials in the Oil Ministry have publicly announced that long-term contracts will be signed with foreign oil companies during the first nine months of 2006.[105] In order to achieve this goal, officials have stated that negotiations should begin with the companies during the second half of 2005, in parallel with the writing of the Petroleum Law, in order to be able to sign soon after the law is enacted.[106]

These policies have been pushed heavily by the USA and the UK. Their roots lie in the US State Department prior to the 2003 invasion. In 2002, the State Department established its Future of Iraq project, in which Iraqi exiles and members of the then opposition, including current Oil Minister Ibrahim Bahr al-Uloum, met with US officials to plan for the future of Iraq after regime change. One of the group's key recommendations was the use of PSAs, with favourable terms to attract the companies.[107]

The Coalition Provisional Authority (CPA) appointed former senior executives from oil companies to begin setting up the framework for long-term oil policy. The first advisers were appointed in January 2003, before the invasion even started, and were stationed in Kuwait ready to move in. First, there were Phillip Carroll[108], formerly of Shell, and Gary Vogler, of ExxonMobil, backed up by three employees of the US Department of Energy and one of the Australian government. They were replaced in October 2003 by former executives of BP and ConocoPhillips. Shell itself was lobbying for the use of PSAs.[109]

During his first period as Oil Minister under the CPA and the Iraqi Governing Council, Bahr al-Uloum told the *Financial Times* that he was preparing plans for the privatisation of Iraq's oil sector, but that no decision would be taken until after the 2005 elections. He commented that: "The Iraqi oil sector needs privatisation, but it's a cultural issue", noting the difficulty of persuading the Iraqi people of such a policy. He further announced that he personally supported production-sharing agreements for oil development, giving priority to US oil companies "and European companies, probably".[110]

In August 2004, Interim Prime Minister Ayad Allawi issued a set of guidelines to the Supreme Council for Oil Policy, from which the Council was to develop a full petroleum policy – a policy that would eventually develop into the Petroleum Law. Allawi's guidelines specified that existing fields would be developed by the Iraq National Oil Company (INOC) and new fields by private companies through production sharing agreements.[111] He added that the Iraqi authorities should not spend time negotiating good deals with the companies, but should proceed quickly with terms that the companies will accept, while leaving open the possibility of later renegotiation.

In June 2005, Ministry officials announced that they were actively seeking discussions with multinational oil companies on the development of 11 oilfields in the south of Iraq, remaining open as to what type of contract would be used, and had held preliminary talks with BP, Chevron, Eni and Total.[112] The following month, the Ministry announced that alongside these direct discussions, it was also considering a licensing round, in which oil companies would bid for production sharing agreements on both known fields and exploration blocks.[113]

The precise terms of PSAs are subject to negotiation; however, once signed, they are fixed for 25-40 years, preventing future elected governments from changing the contract. Thus the contractual terms for the following decades will be based on the bargaining position and political balance that exists at the time of signing – a time when Iraq is still under military occupation. In Iraq's case, this could mean that arguments about political and security risks in 2006 could land its people with a poor deal that long outlasts those risks, and denies large chunks of revenue to a potentially more stable, and independent, Iraq of the future.

Given the central role of oil in Iraq's economy, and the long-term nature of the contracts, Iraq's rapid moves towards handing its undeveloped oilfields to multinational oil companies through production sharing agreements are a cause for concern. That this is occurring without public debate is wholly unacceptable. It is up to the people of Iraq how they choose to develop their oil; transparency and the provision of accurate information to inform debate are absolutely crucial.

BIT BY BIT: ESTABLISHING INTERNATIONAL LAW BY DEFAULT

As the use of PSAs, HGAs and BITs proliferate, so corporate power's institutional allies are once again pushing for a binding international investment agreement, arguing that the provisions established in BITs are now so generalised that they effectively constitute international customary law[114] – and that a new international framework is necessary to avoid the development of "multiple, bespoke regimes rather than a generic legal structure".[115]

BIT by BIT, agreement by agreement, the path is being laid to what corporate power has sought since the early 1970s – an international agreement, backed by the retaliatory measures available to bodies such as the World Trade Organisation, that would lock countries into an investment regime that puts investors' rights above those of the host country, its citizens and its environment.

There is, however, nothing inevitable about the process – much as corporate power would like to portray it as such. HGAs, BITs and PSAs are now major obstacles in the struggle for economic democracy. Supporting the emerging opposition to the corporate takeover of Iraq's oil wealth is perhaps one of the best starting points for a more general, globalised resistance.■

Notes:

[1] "We won't be bullied", Transitions Online, 9 August 2004

[2] Quoted in Eviatar, D., "Wildcat Lawyering", American Lawyer, 4 November, 2002

[3] Between 1991 and 2000, national governments introduced 1,185 regulatory changes, 95% of which were intended to create a more favourable legal regime for inward investment by foreign companies. See: Leubuscher, S., Multinational Enterprises – Masters of the Legal Universe, EU Forest Watch, June 2003, available from www.fern.org .

[4] Performance standards are measures which require foreign investors to achieve certain outcomes to foster investment, such as reinvesting a portion of profits domestically or undertaking to transfer technology. For discussion, see: Oxfam International, "The Danger of an investment agreement in the WTO", in Seattle to Brussels Network, Investment and Competition Negotiations in the WTO – What's wrong with it and what are the alternatives?, October 2002, p.5.

[5] Companies view constraints on transferring capital related to their investments out of a host country as a violation of what they consider a fundamental right. However, such constraints on capital transfers are a critical tool of economic management for governments during times of financial difficulties and are recognized as such in many bilateral investment agreements. See: Peterson, L.E., UK Bilateral Investment Treaty Programme and Sustainable Development: Implications of bilateral negotiations on investment regulation at a time when multilateral talks are faltering, Royal Institute for International Affairs, February 2004, p.8.

[6] For a brief history of investment agreements, see: Singh, K., "Multilateral Investment Agreement in the WTO: Issues and Illusions", Public Interest Research Centre/ Asia Pacific Research Centre, 2003, pp.10-12.

[7] Between 1985 and 2000, the number of Bilateral Investment Treaties (BITs) quadrupled, rising from 385 at the end of the 1980s to a total of 2,265 in 2003, involving 176 countries. Typically, such BITs require non-discrimination against foreign investors; place constraints on the rights of States to

expropriate foreign investments and guarantee compensation where expropriation takes place; and guarantee the right of investors to transfer capital abroad, albeit with certain exemptions. See: http://www.unctadxi.org/templates/Page__1007.aspx ; UNCTAD, Bilateral Investment Treaties 1959-1999, UNCTAD/ITE/IIA/2, New York and Geneva, 2000; UNCTAD, World Investment Report 2003: FDI Policies for Development, National and International Perspectives, United Nations, New York and Geneva, 2003; Cosbey, A., Mann, H., Peterson, L.E., von Moltke, K., Investment and Sustainable Development: A guide to the Use and Potential of International Investment Agreements, Institute for Sustainable Development, 2004, p.1; International Human Rights in Bilateral Investment Treaties and in Investment Treaty Arbitration: A research paper by the International Institute for Sustainable Development (IISD) for the Swiss Department for Foreign Affairs, April 2003.

[8] The Organisation for Economic Cooperation and Development is a grouping of the world's 29 richest countries. The MAI was roundly rejected by national parliaments and the public after its contents were leaked to non-governmental organisations and broadcast on the internet. Branded a "corporate charter" by its critics, due to concerns over its social and environmental implications, the MAI provoked demonstrations on the streets of several OECD capitals. Opponents ranged from environment and development NGOs to consumer groups, human rights bodies, trade unions, local governments, parliamentarians and church groups. The MAI negotiations, initiated in 1995, finally fell apart in 1998. The MAI was criticised for protecting the interests of the investor without any corresponding attention being paid to establishing legally-binding investor obligations and accountability. Its proposed "investor-state" dispute mechanism, involving closed tribunal hearings, was also seen as biased in favour of companies and lacking in mechanisms which would give effective legal standing to citizens to bring actions.

[9] At the 2003 Ministerial Conference of the World Trade Organisation in Cancun, the European Union pressed for negotiations on investment to be included in the Doha Round of the WTO but opposition from southern countries led to the EC withdrawing its demand.

[10] Most BIT disputes are conducted in closed session. However, research by the International Institute for Sustainable Development has identified BIT disputes challenging environmental regulation, land-planning and government oversight of essential public services such as water and sanitation. See: Peterson, L.E., Emerging Bilateral Investment Treaty Arbitration and Sustainable Development, Research Note, International Institute for Sustainable Development, 2003, available from: http://www.iisd.org/pdf/2003/investment_investsd_note_2003.pdf

[11] For a discussion on the use of BITs to promote corporate-friendly intellectual property regimes, see: Correa, C. M., Bilateral Investment Agreements: Agents of new global standards for the protection of intellectual property rights, GRAIN, August 2004, available from http://www.grain.org/briefings/?id=186. Correa's study concludes that the intellectual property clauses in BITs and investment chapters of free trade agreements "go beyond international norms since they extend to intellectual property rights not covered by the World Trade Organisation (WTO) TRIPS Agreement and incorporate the 'national treatment' principle without the exceptions provided for under international treaties".

[12] Sinclair, A.C., "The Origins of the Umbrella Clause in the International Law of Investment Protection", Arbitration International 20, 2005.

[13] See: Sinclair, A.C., "The Origins of the Umbrella Clause in the International Law of Investment Protection", Arbitration International 20, 2005: "The International Court of Justice declined jurisdiction because the terms of Iran's acceptance of the Court's compulsory jurisdiction under the Optional Clause was considered insufficiently wide to include a case that raised allegations of breaches of customary international law, rather than treaties: Case covering the Anglo-Iranian Oil Company Limited (United Kingdom v Iran) (Preliminary Obligations) Judgment of 22 July 1952, 1952, ICJ Pleadings, Oral Arguments and Documents 93."

[14] See, for example, Yergin, D., The Prize, pub Simon & Schuster, 1991, pp.450-478

[15] See Sinclair, A.C., "The Origins of the Umbrella Clause in the International Law of Investment Protection", Arbitration International 20, 2005.

[16] As Sinclair reports, "[The proposal was for] two instruments: (1) a contractual 'Consortium Agreement' between the Iranian Government and the National Iranian Oil Company, on the one hand, and on the other a consortium of oil companies including AIOC that would continue to operate a sector of the oil industry; and (2) an umbrella treaty that would incorporate the Consortium Agreement by annex and that would contain a provision by which the Iranian Government guaranteed on behalf of itself and NIOC to fulfill its terms." See: Sinclair, A.C., "The Origins of the Umbrella Clause in the International Law of Investment Protection", Arbitration International 20, 2005.

[17] For a description of the role played by international law firms, notably Baker Botts, the Houston-based energy law specialists, see: Eviatar, D., "Wildcat Lawyering", American Lawyer, 4 November, 2002

[18] Such contracts – known as "state contracts" or "investment agreements" – come in many forms, from procurement contracts to turnkey agreements, Build-Operate-Transfer (BOT) agreements and Production Sharing Agreements.

[19] Reyes,A.S., "Protecting the 'Freedom of Transit of Petroleum': Transnational Lawyers Making (Up) International Law in the Caspian", Berkeley Journal of International Law 24,(forthcoming June 2006) (manuscript on file with author).

[20] Subsequently, after pressure from NGOs on the multilateral development banks and export credit agencies funding the project, the agreements were made public. They are now available from: www.caspindevelopmentandexport.com

[21] Reyes, A.S., "Protecting the 'Freedom of Transit of Petroleum': Transnational Lawyers Making (Up) International Law in the Caspian", Berkeley Journal of International Law 24,(forthcoming June 2006) (manuscript on file with author).

[22] For detailed analysis of the legal implications of the agreements, see: Carrion. M., "Preliminary Analysis of the Implications of the Host Government Agreement between Turkey and BTC Consortium", Baku Ceyhan Campaign, October 2002, www.baku.org.uk ; Susan Leubuscher, 2 June 2003, 'The privatisation of justice: international commercial arbitration and the redefinition of the state'. http://www.fern.org/pubs/reports/dispute%20resolution%20essay.pdf;; Amnesty International, Human Rights on the Line – The Baku-Tbilisi-Ceyhan pipeline project, London, May 2003; Reyes,A.S., "Protecting the 'Freedom of Transit of Petroleum': Transnational Lawyers Making (Up) International Law in the Caspian", Berkeley Journal of International Law 24,(forthcoming June 2006) (manuscript on file with author).

[23] For examples, see: Peoples' Republic of China, Draft Concession Agreement, Article 26 – "The validity, interpretation and implementation of this agreement shall be governed by the laws of the Peoples' Republic of China", www.chineseinfrastructure.com/pg45_e.htm ; Government of Macedonia, Law on Concession, Article 8 – "The concession shall not be used contrary to the law and international agreements ratified by the Republic of Macedonia", www.

libertas-institut.com/de/MK/nationallaws/concession.pdf ; Government of India, National Highways Authority Concession Agreement, Jaipur-Kishangarh Highway, Article 43.1 – "This agreement shall be construed and interpreted in accordance with and governed by the laws of India", www.nhai.org/fvb.pdf

[24] For further discussion, see: Susan Leubuscher, 2 June 2003, 'The privatisation of justice: international commercial arbitration and the redefinition of the state'. http://www.fern.org/pubs/reports/dispute%20resolution%20essay.pdf ; Leubuscher, S., 'The Privatisation of Law' MRes thesis, Birkbeck College, 2003;; Amnesty International, Contracting out of Human Rights – The Chad-Cameroon Pipeline Project, 2005, http://web.amnesty.org/library/pdf/POL340122005ENGLISH/$File/POL3401205.pdf; Boyd-Carpenter, H. and Labedi, W., "Striking a balance: Intergovernmental and host government agreements in the context of the Baku-Tbilisi-Ceyhan pipeline project", LIT Online, EBRD, 2004, www.ebrd.com/pubs/legal/OL04e.pdf ; Reyes,A.S., "Protecting the 'Freedom of Transit of Petroleum': Transnational Lawyers Making (Up) International Law in the Caspian", Berkeley Journal of International Law 24,(forthcoming June 2006) (manuscript on file with author).

[25] Boyd-Carpenter, H. and Labedi, W., "Striking a balance: Intergovernmental and host government agreements in the context of the Baku-Tbilisi-Ceyhan pipeline project", LIT Online, EBRD, 2004, www.ebrd.com/pubs/legal/OL04e.pdf [26] Many pipelines have "umbrella" or "framework" agreements between the governments of the countries concerned but as Boyko Nitzov, Senior Expert (Investment) of the Energy Charter Secretariat, notes of those for Turkmenistan, Kazakhstan, China and Russia, "such agreements are often just non-binding political declarations that do not have much of an impact on national pipeline laws and regulations or investor risks". See: Nitzov, B., "The Energy Charter view on financing barriers, options, strengths and weaknesses – what is need (sic)", http://www.cbss.st/basrec/conferences/dbaFile4184.doc.

[27] The project agreements set up a legal hierarchy in which local law is relegated to the bottom rung. The main categories of the hierarchy are listed below: 1) The Constitution of the Republic of Turkey; 2) The Inter-Government Agreement (IGA); 3) The Host Government Agreement (HGA); 4) Turkish domestic law not superseded by the IGA or HGA; 5)Other regulatory requirements such as Governmental Decrees, Regulations, Communiqués, Ministerial Orders, Instructions, to the extent that they do not conflict with the IGA or HGA.

[28] For examples of exemptions to environmental impact assessment regulations being granted in the forestry sector, see: Miranda, M. with Blanco-Uribe, A., Hernandez, L., Ochoa J. G., and Yerena, E., All that glitters is not Gold: Balancing conservation and development in Venezuela's frontier forests, World Resources Institute, 1998, http://forests.wri.org/pubs_description.cfm?PubID=2912.

[29] The project was developed by the Belize Electric Company (BECOL), which at the time was 90 per cent owned by Fortis Inc of Newfoundland Canada. For further details of the project, see http://www.stopfortis.org

[30] Third Master Agreement between Government of Belize and Belize Electric Company Limited and Belize Electricity Limited, Franchise Agreement, Section 7.1, p.27: "The government covenants and agrees to waive, or cause to be waived, and indemnify the Producer against any private action under or with respect to, any or all environmental laws, rules or regulations now existing, or created hereafter, to which the Mollejon Project and the New Project may be subject other than any laws, rules or regulations set forth in the Mollejon Project Compliance Plan and the New Project Compliance Plan, as the case may be, to which the Producer has agreed to be bound." The project documents are available from http://www.stopfortis.org/3rdMasterAgreement.pdf

[31] Ibid, Section 12.1, p.29.

[32] Government of Belize, Macal River Hydroelectric Development Act 2003, Para 4 (d): "For the avoidance of doubt and for greater certainty, BECOL [Belize Electric Company Limited] shall proceed with the design, financing, construction and operation of the Chalillo Project in accordance with paragraphs (a), (b) and (c) of this section notwithstanding any judgment, order or declaration of any court or tribunal, whether heretofore or hereafter granted, issued or made" (emphasis added).

[33] Orellana, M., Personal communication, 29 September 2005.

[34] The resistance of host governments to the agreements is indicated by Stuart Schaffer, an international tax partner at Baker Botts: "We had to say to the government a lot, 'If you don't create a usable legal structure, no one will invest in this.'" See: Eviatar, D., "Wildcat Lawyering", American Lawyer, 4 November, 2002.

[35] Center for International Environmental Law, "The Baku-Tbilisi-Ceyhan Pipeline Project Compromises the Rule of Law", Washington DC, October 2003.

[36] Letter of 26 November 2002 from Nino Chkhobadze (Georgian Minister for the Environment) to BP CEO John Browne

[37] Letter of November 7 2002, from David Woodward (BP Azerbaijan) and Natiq Aliyev (Socar) to Eduard Shevardnadze. The US special envoy on energy, Steven Mann, was called in to "mediate" the dispute, and began by saying that if Georgia did not approve the routing within the deadline, it would not get investment in other big energy projects [Rustavi-2 TV, 25 Nov 02, reported on BBC Monitoring, 'Georgian environment minister under pressure to back pipeline impact report'].

[38] AFP, 'Georgia approves $2.9bn oil pipeline', 2 December 2002

[39] Letter from Dr. Huseyin Sungur, Ministry of Agriculture and Rural Affairs (General Directorate of Protection and Control) to General Directorate of Petroleum Pipeline Corporation, "BTC Crude Oil Pipeline Project EIA Activities", 29 November 2001, in EIA, Appendix A8 – Consultation Results, October 2002: "It is stated that regarding the Baku-Tiblisi-Ceyhan crude oil pipeline project, site investigation is not required by the Ministry of Environment, General Directorate of Environmental Impact Assessment and Planning, in accordance with the Host Government Agreements . . ."

[40] Letter from Prime Ministry Undersecretariat of Maritime Affairs, General Directorate of Marine Transportation, to Petroleum Pipeline Corporation, 30 November 2001, in EIA, Appendix A8 – Consultation Results, October 2002, A8-30. The letter states: " . . . our country undertook some commitments by means of the completion of the project on time according to the statements of the project agreement, accordingly, in order to assure that the project activities would be carried out as determined in the agreements and within the designated period, we are under the obligation of taking the required permission, licence and documents within 30 days beginning from the presentation date of the project stipulations, in that context the EIA Report studies was started, the EIA Procedure was carried out different than the EIA Regulations . . ." (italics added).

[41] Article 8 of Turkish Expropriation Law states that "the administration [in this case, BOTAS] shall assign one or more than one reconciliation commission ... for the purpose of executing and completing the purchasing works through bargaining over the estimated cost and through barter... the

bargaining negotiations shall be held on a date designated by the commission." (Italics added)

By contrast, the Resettlement Action Plan explicitly rules out any bargaining or bartering in the negotiation process. In its clearest explanation of the procedure that has been adopted, it states: "The Negotiations Commission begins discussions with landowners based on the range of land values established by the Valuation Commission. The "negotiation" process does not consist of bargaining. Indeed, as mentioned in Chapter 2, the negotiation commission has no room for bargaining. Rather, this commission explains the basis of valuation to affected communities and each of the affected titled deed owners. It provides detailed information obtained from each source specified under the Law and shows how valuation decisions have been reached." See: RAP Turkey Final Report, Chapter 5: Land Acquisition Procedures, 5.2.2, pp.5-12, November 2002. For more instances of this nature see Baku-Ceyhan Campaign, International Fact-Finding Mission: Baku-Tbilisi-Ceyhan Pipeline—Turkey Section, June 2003.

[42] BP, Response to NCP Request Filed by Friends of the Earth Against Project, unpublished, March 2004, p. 9.

[43] BP, Response to NCP Request Filed by Friends of the Earth Against Project, unpublished, March 2004, p.9.

[44] BTC, Citizens Guide to the BTC Project Agreements: Environmental, Social and Human Rights Standards", p.6: "It is important to note that the legal arrangements for BTC do not replace existing laws and regulations but are designed to build on and supplement the legal framework, and only supersede provisions that directly conflict with the project agreement requirements."

[45] BTC, "Citizens Guide to the BTC Project Agreements: Environmental, Social and Human Rights Standards", www.caspiandevelopmentandexport.com. The Guide acknowledges (p.6) that the project's legal regime grants investors the power to "supersede provisions that directly conflict with project agreement requirements."

[46] Intergovernmental Agreement, www.caspiandevelopmentandexport.com, Article 4. The standards specified are "international standards and practices within the Petroleum pipeline industry". Although the Agreement sets a floor by requiring that such standards should " in no event be less stringent than those generally applied within member states of the European Union", BP has acknowledged in meetings with NGOs that there are no "petroleum pipeline industry standards" (EU or otherwise) covering social and human rights – and that such standards as exist are primarily technical.

[47] BTC Co., Briefing note on environmental standards, Applicability and Enforcement, Supplementary Lenders Information, Final, June 2003.

[48] See for example, Host Government Agreement (Turkey), Appendix 5, Paras 3.3 / 4.2: "If any regional or intergovernmental authority having jurisdiction enacts or promulgates environmental standards relating to areas where Pipeline Activities occur, the MEP Participants and the Government will confer respecting the possible impact thereof on the Project, but in no event shall the Project be subject to any such standards to the extent they are different from or more stringent than the standards and practices generally prevailing in the international Petroleum pipeline industry for comparable projects.

[49] Amnesty International, Human Rights on the Line – The Baku-Tbilisi-Ceyhan pipeline project, May 2003.

[50] Intergovernmental Agreement, Article IV: "Each State shall cooperate and coordinate with the others and the applicable Project Investors in the formulation and establishment of uniform technical, safety and environmental standards for the construction, operation, repair, replacement, capacity expansion or extension (such as laterals) and maintenance of the Facilities in accordance with international standards and practices within the Petroleum pipeline industry (which shall in no event be less stringent than those generally applied within member states of the European Union) and the requirements as set forth in the relevant Host Government Agreement, which shall apply notwithstanding any standards and practices set forth in the domestic law of the respective State" (italics added).

[51] BTC Supplementary Lenders Information Pack, "BTC Briefing Ntote on Environmental Standards, Applicability and Enforcement, Final", June 2003, p. B3. The SLIP states: "The reference to EU standards provides a benchmark and floor for what must be considered 'international standards and best practices' for the purpose of the Project. As a result, the IGA [Intergovernmental Agreement] ensures that the BTC project must meet or exceed EU standards" (emphasis added).

[52] In fact, the only binding EC law relating to pipelines is Directive 94/22/EC on the conditions for granting and using authorizations for the prospection, exploration and production of hydrocarbons. Its Article 6(2) states that 'Member States may, to the extent justified by national security, public safety, public health, security of transport, protection of the environment, protection of biological resources and of national treasures possessing artistic, historic or archaeological value, safety of installations and of workers, planned management of hydrocarbon resources (for example the rate at which hydrocarbons are depleted or the optimization of their recovery) or the need to secure tax revenues, impose conditions and requirements on the exercise of [hydrocarbon activities]'. Since neither the BTC host States nor the corporation involved in the project are Member States of the European Union, however, the Directive will not apply to them.

[53] Neither the IGA nor the individual Host Government Agreements (HGAs) nor the Environmental and Social Impact Assessment define the meaning of the phrase "European standards". Although BTC Co's Human Rights Undertaking specifically equates "European Standards" with "European Union Directives", the document does not form part of the legal regime for the project. BTC Co has therefore replaced the clear-cut, legally-binding framework provided by enforceable host government legislation with a floor that lacks legally-enforceable definition.

[54] This interpretation is suggested by the Environmental and Social Impact Assessment's statement that: "All aspects of the Project will be undertaken in accordance with . . . EC Directives." See: EIA Commitments Register, unpaginated, ID APC1E17. See also: ID APC1E16: "The guidelines and standards set by the following organisations will also apply to the BTC project . . . European Union Directives and Guidance."

[55] BTC Co has confirmed that "the standards referenced [in the Environmental and Social Impact Assessment] are part of the prevailing legal regime governing the BTC project in each of the host countries." See: BTC Supplementary Lenders Information Pack, "BTC Briefing Note on Environmental Standards, Applicability and Enforcement, Final", June 2003, p.B3.

[56] BTC Environmental Impact Assessment, Supplementary Lenders Information Pack, Part D: Turkey, "Para 4.3.2 Environmental standards", p.51.

[57] The three directives are: Directive 1999/32/EC Limiting Sulphur Content in Certain Liquid Fuels; Directive 78/659/EEC; and the LCP Directive 2001/80/EC.

[58] BTC Pipeline Project – Matrix of Environmental Standards and Guidelines, March 2003, www.caspiandevelopmentande

xport.com

[59] As the UK Export Credits Guarantee Department (ECGD) stated in oral evidence to the Trade and Industry Committee on 16th November: "It is the first time [SPC 2888] has been used on a pipe with the polyethylene coating".[Minutes of Evidence taken before Trade and Industry Committee: ECGD Support for the Baku-Tbilisi-Ceyhan Pipeline, 16 November 2004, Tuesday 16th November 2004, Q 23.

[60] Gillard, M., Evidence to UK Trade and Industry Committee, Second Submission, 1st October 2004. Gillard points out: (i) All but one of the eight studies carried out on SPC 2888 to ensure it was the right choice were done long after BP awarded the contract (para 33); (ii) cold weather and curing tests of SPC 2888 were only conducted in the region in August and September 2003 (para 91); and (iii) a curing regime was only developed in December 2003 – after the coating had been applied and failed (para 89). Significantly, the results of the testing did not prove the SPC coating was fit for its intended purpose.

[61] Mortimore, D, AGT Pipeline Project, Review of Field Joint Coating Specification, November 2002. See also: Mortimore, D, Evidence to Select Committee on UK Trade and Industry, House of Commons, 2004.

[62] As predicted by Mortimore, the SPC 2888-coated sections of the pipeline have been subject to extensive cracking (26 per cent in Georgia alone).

[63] Mihailescu, A., "Cracks revealed in BTC oil pipeline", 21 September 2005

[64] Orellana, M, personal communication, 29 September 2005.

[65] Orellana, M, personal communication, 29 September 2005.

[66] United Nations, UNCITRAL – Legislative Guide on Privately Financed Infrastructure Projects, Prepared by the United Nations Commission on International Trade Law, New York, 2001, www.uncitral.org/pdf/english/texts/procurem/pfip/guide/pfip-e.pdf The recommendations made with regard to stabilisation clauses are found at pp.140-142. UNCITRAL notes: "All business organizations, in the private and public sectors alike, are subject to changes in law and generally have to deal with the consequences that such changes may have for business . . . General changes in law may be regarded as an ordinary business risk . . ." (para 123, p.141)

[67] United Nations, UNCITRAL – Legislative Guide on Privately Financed Infrastructure Projects, Prepared by the United Nations Commission on International Trade Law, New York, 2001, www.uncitral.org/pdf/english/texts/procurem/pfip/guide/pfip-e.pdf , para 125

[68] United Nations, UNCITRAL – Model Legislative Provisions on Privately Financed Infrastructure Projects, Prepared by the United Nations Commission on International Trade Law, New York, 2004, www.incitral.org/pdf/english/texts/procurem/pfip/model/annex1-e.pdf., Model provision 40, para 1 (c),p.27, Model provision 40. UNCITRAL sets out two model provisions (38 and 39) for addressing stabilisation clauses. These state: "The concession contract shall set forth the extent to which the concessionaire is entitled to compensation in the event that the cost of the concessionaire's performance of the concession contract has substantially increased or that the value that the concessionaire receives for such performance has substantially diminished, as compared with the costs and the value of performance originally foreseen, as a result of changes in legislation or regulations specifically applicable to the infrastructure facility or the services it provides"; and ". . . the concession contract shall further set forth the extent to which the concessionaire is entitled to a revision of the concession contract with a view to providing compensation in the event that the cost of the concessionaire's performance of the concession contract has substantially increased or that the value that the concessionaire receives for such performance has substantially diminished, as compared with the costs and the value of performance originally foreseen, as a result of: (a) Changes in economic or financial conditions; or (b) Changes in legislation or regulations not specifically applicable to the infrastructure facility or the services it provides; provided that the economic, financial, legislative or regulatory changes: (a) Occur after the conclusion of the contract; (b) Are beyond the control of the concessionaire; and (c) Are of such a nature that the concessionaire could not reasonably be expected to have taken them into account at the time the concession contract was negotiated or to have avoided or overcome their consequences."

[69] Multilateral Centre for Private Sector Development Istanbul, Basic Elements of a Law on Concession Agreements, OECD and Federation of Euro-Asian Exchanges, www.oecd.org/dataoecd/41/20/33959802.pdf, p.21, para18 (a): The OECD states: "The nature of the legislation must be described"

[70] Multilateral Centre for Private Sector Development Istanbul, Basic Elements of a Law on Concession Agreements, OECD and Federation of Euro-Asian Exchanges, www.oecd.org/dataoecd/41/20/33959802.pdf, p.21, para18 (a):

[71] See Government of India, National Highways Authority Concession Agreement, Jaipur-Kishangarh Highway, http://www.nhai.org/fvb.pdf , Articles 36.1 and 36.2

[72] Host Government Agreement (Turkey), para 7.2 (xi), available from www.caspiandevelopmentandexport.com

[73] The stabilsation clause (para 7.2 (xi) of the Host Government Agreement for Turkey reads: "The State Authorities shall take all actions available to them to restore the Economic Equilibrium established under the Project Agreements if and to the extent the Economic Equilibrium is disrupted or negatively affected, directly or indirectly, as a result of any change (whether the change is specific to the Project or of general application) in Turkish Law (including any Turkish Laws regarding Taxes, health, safety and the environment)."

[74] See: Host Government Agreement (Turkey), Article 7.2 (vi) and (xi); Georgia Host Government Agreement (HGA), Article 7.2 (vi) and (x); Azerbaijan HGA, Article 7.2 (vi) and (x), available from www.caspiandevelopmentandexport.com. The Turkey HGA states: "The Government hereby covenants and agrees (on its behalf and acting on behalf of and committing the State Authorities) that throughout the term of this Agreement:

"if any domestic or international agreement or treaty; any legislation, promulgation, enactment, decree, accession or allowance; any other form of commitment, policy or pronouncement or permission, has the effect of impairing, conflicting or interfering with the implementation of the Project, or limiting, abridging or adversely affecting the value of the Project or any of the rights, privileges, exemptions, waivers, indemnifications or protections granted or arising under this Agreement or any other Project Agreement it shall be deemed a Change in Law under Article 7.2(xi).

"the State Authorities shall take all actions available to them to restore the Economic Equilibrium established under the Project Agreements if and to the extent the Economic Equilibrium is disrupted or negatively affected, directly or indirectly, as a result of any change (whether the change is specific to the Project or of general application) in Turkish Law (including any Turkish Laws regarding Taxes, health, safety and the environment)."

[75] Amnesty International, Human Rights on the Line, 2003.

[76] Amnesty International, Human Rights on the Line:

The Baku-Tbilisi-Ceyhan Pipeline Project, May 2003, p.5. Article 12 (Security) of the Turkish HGA requires the State Authorities to "ensure the safety and security of the Rights to Land, the Facilities and all Persons within the Territory involved in Project Activities and shall protect the Rights to Land, the Facilities and those Persons from all Loss or Damage resulting from civil war, sabotage, vandalism, blockade, revolution, riot, insurrection, civil disturbance, terrorism, kidnapping, commercial extortion, organised crime or other destructive events." The inclusion of the broad concept 'civil disturbance' could be used to justify serious human rights breaches at the hands of the state in its attempts to ensure the stability of the project. The companies are absolved from any damages, including human rights abuses, arising from the security forces' actions.

[77] BTC Co, Human Rights Undertaking, www.caspiandevelopmentandexport.com

[78] For further concerns, see: Amis de la Terre et al., Review of BTC Environmental Impact Assessment – Legal Regime, www.baku.org.uk

[79] BP, Response to NCP Request Filed by Friends of the Earth Against Project, unpublished March 2004, p.20. BP states: "The economic equilibrium clause will not apply unless . . . the Project files an arbitration claim against the Government (a decision the Project is unlikely to take absent evidence that Government action is motivated by rent seeking behaviour and not environmental or social benefits". The company's response to Friends of the Earth was written after the promulgation of the Deed Poll.

[80] BTC Co, BTC Human Rights Undertaking, www.caspiandevelopmentandexport.com. See for example Para 2(a) " . . . provided that such domestic law is no more stringent than the highest of European Union standards as referred to in the Project Agreements, including relevant EU directives ("EU standards"), those World Bank Group standards referred to in the Project Agreements and standards under applicable international labour and human rights treaties."

[81] Leubuscher, S., 'The Privatisation of Law', 2003

[82] Susan Leubuscher, 2 June 2003, 'The privatisation of justice: international commercial arbitration and the redefinition of the state'. http://www.fern.org/pubs/reports/dispute%20resolution%20essay.pdf .

[83] In Turkey, the Gendarmerie, a police force which has been repeatedly criticized for its human rights abuses by the European Court of Human Rights, will be responsible for policing the project.

[84] For details, see: www.baku.org.uk

[85] Boyd-Carpenter, H. and Labedi, W., "Striking a balance: Intergovernmental and host government agreements in the context of the Baku-Tbilisi-Ceyhan pipeline project", LIT Online, EBRD, 2004, www.ebrd.com/pubs/legal/OL04e.pdf

[86] Annan, K, UN General Secretary, Speech to United Nations Millennium Summit, September 2000.

[87] United Nations Commission on Human Rights, Human Rights, Trade and Investment, E/CN.4/Sub.2/2003/9, 2 July 2003. The principle recommendations are sumarised at pp 3-4 and at pp.30-32, with a fuller discussion in 'Section III: The Human Rights Implications of Investment Liberalisation' (pp.17-24). The Report recommends: "(a)Including the promotion and protection of human rights among the objectives of investment agreements. Given States' international responsibilities with regard to the promotion and protection of human rights, States should consider including an explicit reference to the promotion and protection of human rights among the objectives of investment liberalization agreements; (b) Ensuring States' right and duty to regulate and the flexibility to induce new regulations to promote and protect human rights and the environment . Broad interpretations of expropriation provisions could affect States' capacity and willingness to regulate for health, safety or environmental reasons. Therefore interpretations, or even explicit declarations by parties to agreements, that recognize and protect States' responsibility to fulfil human rights are encouraged; (c) Promoting investors' obligations alongside investors' rights. There is a need to balance the strengthening of investors' rights in investment liberalization agreements with the clarification and enforcement of investors' obligations towards individuals and

[88] Thomas W Wälde, Editorial, in OGEL (Oil, Gas & Energy Law Intelligence), Volume III, issue #01 - March 2005

[89] Thomas W Wälde, July 1995, 'The current status of international petroleum investment: regulating, licensing, taxing and contracting', in CEPMLP Journal, Vol 1, no.5, pub. University of Dundee

[90] For example, the PSA for the Azeri-Chirag-Guneshli field in Azerbaijan states "Upon approval by the Parliament of the Azerbaijan Republic of this Contract, this Contract shall constitute a law of the Azerbaijan Republic and shall take precedence over any other current or future law, decree or administrative order (or part thereof) of the Azerbaijan Republic which is inconsistent with or conflicts with this Contract except as specifically otherwise provided in this Contract." [Article XXIII, clause 23.1]

[91] That is not to say that there was no change in the middle of the Twentieth Century: rather, that the increased bargaining power of host states at that time was reflected more in the economic terms of contracts, than in the contractual form itself. Now, however, the pendulum of bargaining power has swung back in favour of investors.

[92] Susan Leubuscher, 'The privatisation of justice: international commercial arbitration and the redefinition of the state'. http://www.fern.org/pubs/reports/dispute%20resolution%20essay.pdf , 2003.

[93] For example, in Azerbaijan's ACG PSA [Article XXIII, clause 23.2]: "In the event that the Government or other Azerbaijan authority invokes any present or future law, treaty, intergovernmental agreement, decree or administrative order which contravenes the provisions of this Contract or adversely or positively affects the rights or interests of Contractor hereunder, including, but not limited to, any changes in tax legislation, regulations, administrative practice, or jurisdictional changes pertaining to the Contract Area the terms of this Contract shall be adjusted to re-establish the economic equilibrium of the Parties, and if the rights or interests of Contractor have been adversely affected, then SOCAR shall indemnify the Contractor (and its assignees) for any disbenefit, deterioration in economic circumstances, loss or damages that ensue therefrom."

[94] A case in point is the PSA for Shell's Sakhalin II oil developments in Russia. Appendix E exempts the project from, amongst other laws, the Russia Water Code which forbids discharge of flows and drainage waters into spawning and wintering areas for valuable and protected fish species and into the habitats of Red Book protected wildlife and plant species. Destruction of salmon spawning sites as a result of oil spillage is a major concern in the project. Article 24 (f) also provides blanket compensation for breach of Shell's Article 24 (f)) The Russian Party shall compensate the Company for any damage caused to the consortium's "commercial position" by "adverse changes in Russian laws, subordinate laws and other acts taken by Government bodies after December 31, 1993 (including changes in their interpretation or their application procedure by government bodies and by the courts in the Russian Federation)."

[95] Daniel Johnston, 1994, International petroleum fiscal

systems and production sharing contracts, pub. Pennwell, p.39

[96] Ian Rutledge, The Sakhalin II PSA – A production 'non-sharing' agreement, November 2004, Pub. PLATFORM et al available at http://www.carbonweb.org/documents/SakhalinPSA.pdf

[97] See Associated Press, 10 February 2005, 'State Audit Chamber accuses Shell consortium of overspending'

[98] This approach is designed for exploration and production contracts, in which case it is not known how large or profitable any fields found will be. However, this has not stopped them being applied to pure production contracts on known fields – ACG and Sakhalin being two prime examples.

[99] ACG PSA, article XI, clause 11.6

[100] Sakhalin II PSA, section 14. For detailed analysis, see Ian Rutledge, November 2004, 'The Sakhalin II PSA - A production non-sharing agreement' (pub CEE Bankwatch Network, PLATFORM, Friends of the Earth, Sakhalin Environment Watch, Pacific Environment, WWF)

[101] Almost all of ITIC's 110 listed sponsors are large corporations, with roughly a quarter of these in the the oil sector. ITIC's Board of Directors contains representatives from Shell, BP, ConocoPhillips, ExxonMobil and ChevronTexaco.

[102] International Tax & Investment Centre (ITIC), Petroleum and Iraq's Future: Fiscal Options and Challenges, Fall 2004

[103] International Tax & Investment Centre (ITIC), Strategic Questions For Our Future, undated [2004]www.iticnet.org/publications/StrategicQuestions.pdf

[104] US Department of Energy, Energy Information Administration, Iraq – Country Analysis Brief, June 2005

[105] Christian Schmollinger, International Oil Daily, 15 June 2005, 'Iraqi officials hopeful foreign oil firms will return in 2006'

[106] Glen Carey & Faleh al-Khayat, Platts Oilgram News, June 22 2005, 'Iraq looks to woo majors for field revivals'

[107] US State Department Future of Iraq Project, Oil and Energy Working Group (Oil Policy Subgroup), April 2003, 'Iraqi oil policy recommendations after regime change', published in Middle East Economic Survey, 5 May 2003, pp.D1-D11

[108] Carroll described his role as not only to address short-term fuel needs and the initial repair of production facilities, but also to: "Begin planning for the restructuring of the Ministry of Oil to improve its efficiency and effectiveness; [and] begin thinking through Iraq's strategy options for significantly increasing its production capacity." [Philip J Carroll, November 2004, 'Personal commentary', in Oxford Energy Forum (pub Oxford Institute for Energy Studies)]

[109] For example, Walter van der Vijver, then Chief Executive Officer of Shell Exploration and Production, stated in 2003 that "...international oil companies can make an ongoing contribution to the region [the Persian Gulf]... However, in order to secure that investment, we will need some assurance of future income and, in particular, a supportive contractual framework. There are a number of models which can achieve these ends. One option is the greater use of Production Sharing Agreements, which have proved very effective in achieving an appropriate balance of incentives between Governments and oil companies. And they ensure a fair distribution of the value of a resource while providing the long term assurance which is necessary to secure the capital investment needed for energy projects" [Speech to ECSSR conference, A new era for international oil companies in the Gulf: opportunities and challenges, Abu Dhabi, 19 October 2003].

[110] Pelham, N., Financial Times, 5 September 2003, 'Oil to be privatised but not just yet, says Iraqi minister'

[111] "For new development of undeveloped oil and gas fields, and for exploration, all of which must start as soon as possible and in tandem with INOC's efforts, these should be accomplished through private sector investment via competent international ... oil companies... However, these new ventures should specifically not be allowed to partner with any state-owned enterprises, including INOC, in order to ensure state impartiality and avoid the pitfall of state interference in corporate enterprise management". [Cited in Middle East Economic Survey, 13 September 2004, 'Allawi outlines new Iraqi petroleum policy: INOC for currently producing fields/IOCs for new areas', pp. A1-A4]

[112] Middle East Economic Survey, 20 June 2005, 'Iraq fast tracks upstream contract talks with IOCs', pp.5-6

[113] Middle East Economic Survey, 11 July 2005, 'Iraq mulls bid round alongside direct talks with IOCs'

[114] Prosper Weil, a former President of the World Bank's Administrative Tribunal, has already claimed this status for the World Bank's own Guidelines on the Treatment of Foreign Direct Investment: "Looking beyond their limited objective and ostensibly low profile, the Guidelines may already be considered to constitute the written expression of rules of customary law. They are, therefore, to serve as a substitute for the major international convention which it has not been possible to elaborate thus far." See: Weil, P., "The State, the Foreign Investor and International Law", ICSID Review 15 (2000), p. 414, cited in Leubuscher, S., "Multinational enterprises – Masters of the legal universe", EU Forest Watch, June 2003, available from www.fern.org Likewise, Professor Thomas Walde, energy specialist at the University of Dundee, writes: "The common core of BITs can now be considered to be indicative of state practice and customary international law". However, it has also been argued that the provisions of BITs vary from one to another and that no general norms can therefore be derived from them.

[115] Boyd-Carpenter, H. and Labedi, W., "Striking a balance: Intergovernmental and host government agreements in the context of the Baku-Tbilisi-Ceyhan pipeline project", LIT Online, EBRD, 2004, www.ebrd.com/pubs/legal/OL04e.pdf Labedi, the senior counsel for the European Bank for Reconstruction and Development, and his co-author Harry Boyd-Carpenter of the legal firm Allen & Overy do not explicitly call for an international investment Treaty but nonetheless argue: "In the long term, it will be preferable for countries to evolve a framework, both specifically for concessions and generally for infrastructure works that can operate as a level playing field for all participants and across all projects, both concession-based and otherwise."