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# Argentina

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## LEGAL MEMORANDA

### ARGENTINA

*The following is a brief summary of recent reformatory regulations concerning export policies and a short article concerning new regulations in the Oil and Gas industry.*

#### I. EXPORT POLICIES

By Decree No. 1490/85, the Federal Executive Power created a Committee of Export Policies. This Committee is made up of Ministers of the Economy, Foreign Affairs, and Public Works, as well as the Secretaries of Foreign Trade and Planning. The President of the Republic is the President of the Committee. In his absence, the Minister of Economy sits as alternate President.

This Committee is in charge of: (i) Defining the general export policies; (ii) establishing the different jurisdictions and responsibilities among all agencies involved in one way or another with export promotion; (iii) coordinating all public sector activities connected with international trade relations, including all matters concerning international agreements, international or regional agencies, and bilateral committees; and (iv) surveying the effectiveness of all export promotion incentives and the results of the policies adopted. Under Decree No. 1490/85, the Committee must also be informed of all negotiations involving foreign purchases by the foreign sector. By Decree No. 1524/85 an Executive Secretary of the Committee has been appointed, whose official rank will be Undersecretary.

#### II. NEW REGULATIONS ON OIL AND GAS EXPLORATION AND EXPLOITATION

Under Law No. 17.319, oil and gas exploration, exploitation, industrialization, transportation, and marketing may be carried out by either state-owned, private, or mixed enterprises.<sup>1</sup> Participation

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1. Law No. 17.319, art. 2, published in the Official Bulletin of June 30, 1967. See, Bosch, *Present, Past and Future of Oil and Gas Legislation in Argentina*, INT'L ENERGY L.,

in the private sector has steadily increased over the past thirty years, increasing from almost nothing in 1955 to twenty-five percent in 1960. It grew to thirty-four percent in 1965 and by 1970 it was thirty-two percent. Private enterprise activity shrank in 1975 to twenty-seven percent, but as of 1984 it had climbed to an all-time high of thirty-four percent.<sup>2</sup> In a dramatic effort to foster the development of Argentine oil and gas potential, the Executive announced that 164 oil and gas areas (148 on-shore and 16 off-shore) will be opened soon for private oil exploration and production. On August 5, 1985, the Government issued Decree No. 1443, which permits foreign and domestic private parties to work as contractors for, or in partnership with, the Argentinean oil and gas development association, called Yacimientos Petroliferos Fiscales (YPF). The Secretary of Energy shall be the authority in charge of this particular regime.

#### A. *Authorization to Call for International Bids and Enter Into Agreements*

YPF, the state-owned petroleum enterprise, is authorized to call for international bids and to enter into agreements for the exploration and exploitation of oil and gas,<sup>3</sup> for areas designated by special decree of the National Executive Power.<sup>4</sup>

#### B. *Risk Allocation*

In all contracts executed under Decree 1443/85, all exploration risks fall upon the private enterprise which provides the technology, capital, equipment, machinery, and all other investments necessary for the development of the operation.<sup>5</sup>

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International Bar Association, Section on Energy Law and Natural Resources Law, 109 (M.B.) (1984). See also, Pigretti, *El Nuevo Régimen Legal de Los Hidrocarburos Líquidos y Gaseosos*, in ADLA XXVII-B-1486 (1967); and H. M. BUNGE GUERRICO, *MINERÍA-PETRÓLEO* 332 (1984).

2. See Cárdenas, *Argentina: Oil Policy. An Overview of the Past and a Glance Over the Near Future*, INT'L ENERGY L., 141 (M.B.) (1984).

3. Published in the Official Bulletin of 1985. Decree No. 1443/85 regulates articles 2, 11, and 95 of Law No. 17.319.

4. Decree No. 1443/85, art. 1.

5. *Id.* art. 2.

### C. *Rights Over Resources*

The contracting party shall not acquire any mining rights over the oil and/or gas deposits it may discover. Furthermore, it shall not own the oil and gas it obtains from any discovered deposits. All oil and gas shall be delivered to YPF.<sup>6</sup> Contracts executed under Decree 1443/85 shall not be considered concessionary, if "concession" is defined as "a relationship in which the host country 'concedes' control or sovereign rights over the country's oil resources."<sup>7</sup>

The contracting party may exercise, on behalf of YPF, (and with YPF's intervention), all rights recognized by the Mining Code relating to both investment and personal property, that is located either inside or outside the contractual area.<sup>8</sup> All requests in connection with these rights must be made to the Secretary of Energy. Opposition to the occupation of land on the part of the contracting party by the surface owner, or his disagreement with the compensation determined, can neither suspend nor hinder the performance of the work authorized by an oil and gas contract, provided that the contracting party guarantees to the land owner compensation for any damages incurred.

### D. *Obligations of the Contracting Party*

Contracting parties must always carry out their specific program of work in accordance with generally accepted practices prevailing in oil and gas exploration and exploitation.<sup>9</sup> Specifically, they shall: (i) Use techniques which balance both the characteristics of the field and the size of the reserves in order to allow for maximum production, while still ensuring that the oil field is exploited rationally; (ii) avoid all discharges, spills, or any other damage to the oil fields through wrongful drilling, poor operation, inad-

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6. *Id.* art. 3.

7. See Cameron, *Petroleum Licensing. A Comparative Study*, FIN. TIMES BUSINESS INFORMATION LTD. (n.d.).

8. See Argentine Mining Code, articles 42, 48, *et. seq.* Under the Code, a mine concession includes the right to demand the sale of the corresponding land. If the land is cultivated, the concession holder is to pay the corresponding indemnity. Once the concession has been granted, the surface property and the adjacent property are subject to several easements, following the payment of the corresponding indemnity. These easements include, *inter alia*, the right to: (i) Occupy the land necessary for the construction of buildings, roads, railways, docks, warehouses, etc.; and (ii) use natural waters; etc. Article 4 of the Code provides equivalent coastal rights to companies involved in off-shore exploration.

9. Decree No. 1443/85, art. 5.

equate conservation, illegal abandonment procedures, or improper disposal of hydrocarbon waste. If the responsibility for such damages is attributable to the contractors, as determined by the Secretary of Energy, the contractors must pay the royalties and requisite fees; (iii) maintain adequate security procedures; (iv) avoid or minimize damages which could injure agriculture, fisheries, communications, and underground waters during the drilling activities; (v) avoid polluting the waters and coasts; (vi) respect all National or Provincial Park regulations; (vii) deliver to YPF, at a date to be established, all reports on production and technical information obtained during the contract; (viii) allow YPF permanent access to work areas for performance of necessary inspections; (ix) agree not to flare gas, unless authorization is received from the Secretary of Energy. If gas is flared, then royalties are paid as fines.

#### E. *Procedure for Awarding Contracts*

Contracts entered into through the procedure governed by Decree No. 1443/85, shall, as a general rule, be awarded through international competitive bidding. On a case by case basis, YPF shall issue the corresponding bidding regulations.

The criteria followed by YPF for awarding contracts shall be: (i) The number of "units of work" proposed by the bidders; and (ii) the offered percentage of payment in local currency.<sup>10</sup> YPF is authorized to grant direct discretionary awards if: (i) An emergency arises whereby specialization or a specific technical or economic solution is necessary; and (ii) the bids result in no offers, or inadequate offers. A direct discretionary award requires a resolution of the Board of Directors of YPF, and is subject to subsequent ratification by a decree of the Executive.<sup>11</sup>

#### F. *Contractual Structure*

All contracts executed under Decree No. 1443/85, either through competitive bidding or direct discretionary awards shall have the following components:

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10. *Id.* art. 6.

11. *Id.* art. 7.

### 1. Seismic Option Period

During the seismic option period, the contracting party must perform geological, geophysical, geochemical, and photogeological surveys, in addition to other exploratory works. The seismic option period shall last up to three years, depending on YPF's classification of the respective area. This classification is made on a case by case basis, taking into account both the costs and risks involved. Contracting parties shall commit a minimum number of work units, at a cost determined in advance. At the end of the period, the parties shall have the option to: (i) Start the exploration period, committing themselves to drilling works; or (ii) relinquish their option over the drilling area, discharging both parties from any further obligations.

### 2. Exploration Period

During the exploration period, the contracting parties must undertake minimum annual drilling obligations. The duration of the period shall last up to four years. These four years must be divided into sub-periods of two years. YPF can renew the exploration period for another two year period when technical reasons render this course of action advisable. All periods run from the date on which the contracting parties start exploration. The contractor must notify YPF of their starting date. Each contract must have a clause which partially relinquishes exploration rights at the end of each period. If the contractor's work exceeds the work that he agreed to do, the contract may provide that partial relinquishment be postponed. If no commercial discoveries are made during the exploration period after drilling the agreed upon number of wells, the contract area must be relinquished in full.

### 3. Exploitation or Development Period

In the event of a discovery, the contracting party shall have a period of one year to evaluate its commercial viability. The contracting party may then propose that the Secretary of Energy declare it commercially viable. During this period, all the exploration commitments must be fulfilled. The above mentioned one year period may be extended by YPF for an additional year, at its discretion.

Once the contracting party declares a discovery, the Secretary

of Energy, at the request of such party, shall declare it commercially viable. The Secretary shall also confirm that the Federal State retains all property mining rights vis-a-vis the discovery.

This declaration must be made within ninety days, tolling from the effective reception of the proposal by the Secretary of Energy. If the Secretary remains silent, it shall be understood that the commercial viability has been accepted as of the ninetieth day. The declaration authorizes the contracting party to start the exploitation phase as per the respective contract.

All working and development programs must be submitted to YPF for approval. YPF may object to them or request amendments to meet their standards. YPF may also, if the respective crude oil is of a quality which cannot be processed in Argentina, request that the contractor purchase it all. The contracting party shall have a term of up to twenty years to perform all development and production. This term is computed on an individual basis and is independent from circumstances connected with other discoveries or areas.

In the event of gas discoveries, the Secretary of Energy is empowered to condition commercial viability on three things: The development of the natural gas market; the capacity for industrialization; as well as the availability of transportation mechanisms. If the contracting party, at its own risk, commits to make all investments necessary to industrialize the gas in Argentina, the Executive can authorize its exploitation. However, commercial discoveries may not be suspended for more than ten years.

If a field is declared commercially viable prior to the expiration of an exploration period, the balance of the period can be added to the exploitation period. Notwithstanding this carryover, the exploitation period cannot exceed thirty years, beginning from the expiration of the exploration period.

At the end of the exploitation period, the contracting party must relinquish the contractual area and all of its fixed installations as well as those installations necessary to maintain the area in exploitation. The property of these installations shall be transferred to YPF, free of charge.

#### 4. Guaranties

The amount to be invested in the committed minimum work

programs must be guaranteed in a manner, and to an extent, determined by each contract. The individual contractual agreements may also contain penalty clauses triggered by contractual defaults.

#### 5. Royalties and Fees Based on Exploitation Results

The following payments shall be made to YPF, calculated on the value of total production from the contractual area: (i) a twelve percent royalty to the Federal State; and (ii) an eight percent to eighteen percent fee to YPF. This fee shall be fixed on a case by case basis, taking into account the characteristics of each individual area and the amount of risk involved in exploration. The fee shall have two parts. One part shall be "fixed" and compensate the prior exploration work performed by YPF. The other part shall be a function of the production obtained in the area (i.e., it shall increase and/or decrease with production).

The balance, once the royalties and fees are paid, shall be considered the "total production" from the area, and shall be paid to the contractor (or to him and YPF, if YPF elects to participate as a joint-venturer). In no event may the royalty and fee exceed (on an aggregate basis) thirty percent of the value of the "total production".

#### 6. YPF's Participation

YPF shall have the option to participate with the contracting party in the development of an area when a commercial discovery is proved. This option extends for the entire exploitation period and to all of the exploitation area.<sup>12</sup>

The option to participate in the exploitation of an area must be made during the ninety working days following the Secretary of Energy's declaration that a particular discovery is commercially viable. YPF's participation shall be at a minimum of fifteen percent and a maximum of fifty percent. If YPF exercises its right to participate it must do so on a pro rata basis according to its selected share participation.

In the event that the technical and economic conditions that

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12. *Id.* art. 8, para. f. The association shall be a "temporary enterprise union". These non-corporate joint ventures are widely used in Argentina for the construction of public works. They are not separate legal entities. Their members have limited liability.

YPF took into account at the time of declaring a discovery commercially viable vary substantially, YPF shall have another one time option to create a joint venture. This second chance is for a period of ninety days, counted from the date on which YPF is informed of the said variation.

## 7. Compensation to Contractors

In the event YPF does not exercise its participation option, the contracting party's compensation for the oil produced and delivered to YPF shall be as follows:

(a) *Oil*: A percentage of the international price, on an FOB basis, which is calculated after deducting both the royalty and the fee mentioned above in (6);

(b) *Natural Gas*: According to the following alternatives, the one which yields a higher price: (i) a percentage not to exceed, for each 1000 m<sup>3</sup>, or fourteen percent of a reference crude price to be determined by the Secretary of Energy. This reference crude price shall be the same for all contracts. From the above mentioned percentage, the parties shall discount the value of the royalties and fees; or (ii) the gas transfer price from YPF to *Gas del Estado*, less royalties and fees.

(c) *Liquid Gas*: In the event liquid gas is delivered to YPF, each metric ton shall be compensated on the same basis as oil.

## 8. Manner of Payment

The participation owed to the contracting party for oil and gas produced and delivered to YPF shall be paid in local and foreign currency, in the proportion agreed to in each contract.

YPF shall have the option to pay the foreign currency portion with: (i) products - detailed in an exhibit of each contract and valued on an FOB basis; or (ii) crude oil. Argentina must have been declared by special decree to have become self-sufficient regarding its oil needs. This includes reaching an adequate level of reserves.

In the event of payments in kind, the quantities to be delivered shall be calculated in a manner that shall give the contractor an amount in foreign currency equal to the amount he would otherwise have received if he was given direct payment in foreign currency.

If the crude produced by the contractor is of a quality which is not suitable to be processed in the refineries located in Argentina, the contractor shall be paid with crude oil. YPF may require that, in these particular cases, the contractor purchase YPF's product share (if any). Because all the production is exported, both the royalty and the fee shall be paid in foreign currency. Income tax withholdings, however, shall be made in local currency. Natural gas shall be paid in local currency, unless industrialized or marketed for export.

## 9. Operations

Contractors shall always operate the area, whether or not YPF elects to participate in the development of the area.

## 10. Waivers

Provinces with gas deposits located in their territory will be able to grant reductions or even waive the royalties and the percentage of the fees which correspond to them. This is to encourage industrialization in the region, in accordance with the general guidelines established by the Executive.

These circumstances shall be expressed to the Secretary of Energy and the YPF, in order to transfer the corresponding benefits to the contractors or to the third parties that establish the respective industries.

## 11. Bidding

Participants in the calls for bids shall provide a guarantee that their offer will be maintained. Calls for bids must be published for five days in the Official Bulletin to constitute adequate notice. The deadline for filing offers shall be not less than forty-five days from the day of publication.

The YPF shall analyze all offers and shall be entitled to request modifications from the highest bidder necessary for acceptance. Once a contract is awarded by YPF, it must be executed by the parties and approved by a specific decree of the executive.<sup>13</sup>

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13. Decree No. 1443/85, arts. 10 and 11.

### G. *Taxation*

Contracting parties shall be subject to the general tax structure. An annual surface duty, payable in advance, is to be calculated for every two kilometers of the contractual area. The proceeds are to be used to cover the expenses incurred by the Secretary of Energy in its monitoring of the performance of contractual obligations. The amount of the fee is to be determined individually by the corresponding bidding documentation. Contracts may include a clause that, in the event of adverse changes in the federal taxation system in force at the date of the call for bids or of the execution of the contract, contractors shall be entitled to price adjustment.<sup>14</sup> Contractors shall be subject to the buy-national regulations, regarding both the purchasing of goods and the contracting of services.<sup>15</sup> These regulations allow the purchase abroad of items which are neither manufactured nor likely to be manufactured in Argentina.

### H. *Comment*

Contractual terms should take into account the worldwide declining trend prevailing in the oil and gas market. Less governmental intervention should increase the likelihood that Argentina will benefit from substantial foreign oil and gas investment and obtain the important spin-off benefits deriving from investment.<sup>16</sup>

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14. *Id.* art. 12.

The Provinces may receive 25% of the fees paid by contractors to the Federal State, provided they commit themselves not to alter or increase the existing Provincial tax system vis-a-vis: (i) The contracts; (ii) the respective activities performed by the contractors under them; or (iii) the goods or equipment used in connection therein.

15. Law No. 18.875 and Decrees No. 5340/63 and 2930/70.

16. Decree No. 1443/85, art. 15.