

COLOMBIA – TOWARDS A NEW PETROLEUM CONTRACTUAL REGIME

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INTRODUCTION

Recently, with the expedition of Decree 1760 of the 26 of June 2003, the Colombian Government split and modified the Empresa Colombiana de Petr leos and created the National Agency for Hydrocarbons (ANH). This Decree is a fundamental and structural change in the way Colombia manages its hydrocarbon reserves. It is not simply an administrative reform of this governmental establishment but rather a change in the contracting policy for petroleum.

Article 332 of the Colombian Constitution establishes the fundamental principle that this nonrenewable natural resource belongs to the Nation. Decree 1760 took away from ECOPETROL the management of hydrocarbon reserves and gave this responsibility to the new organization (ANH).

At the same time, the aforementioned Decree repeals Decree 2310 of 1974, which is the angular stone of the association contracting system, with all its regulatory resolutions. This regime was the State's then current petroleum contracting system which was in use until December 31, 2003.

It is then the challenge of the ANH to design, promote, negotiate, celebrate, follow up and manage the new hydrocarbons exploration and production contracts in Colombia.

It is important to make an analysis of the petroleum contracting systems looking at the past, analyzing what presently exists and what may be future tendencies for the new Century. We will look at the ANH's document presented for public consultation since the beginning of this year, "Elements of New Contracting for Hydrocarbon Exploration and Production", and we will make some recommendations to the new Colombian contracting system.

I. CONTRACTS IN COLOMBIA

1.1. CONCESSION CONTRACT

At the end of the 19th Century and early 20th Century, like the rest of the world, Colombia began hydrocarbon exploration and exploitation under the concession contracting system.

The poet JORGE ISAAC was the first Colombian to request from the government this kind of contract. In 1886 he subscribed the concession contract to develop Cerrejón's carboniferous reserves. In 1890 he signed a similar contract to explore and exploit asphalt and petroleum reserves in the Sierra Nevada de Santa Marta and the Gulf of Urabá.

The writer, convinced cattlemen from the Sinú region to invest risk capital in this venture. People like DIEGO MARTÍNEZ, FRANCISCO BURGOS and PRISCILIANO CABRALES that had been touched by the dream of the poet, set the stage that redirected the entrepreneurial activity of these illustrious citizens.

These early attempts by the poet were unsuccessful; not only because he did not manage to discover reserves but also because he could not motivate national or international companies to invest in the search for and commercialization of this natural resource. Beaten by these difficulties and with the help of the liberal leader and martyr RAFAEL URIBE URIBE he managed to sell his rights to the Panamerican Investment Company. These rights were never cancelled by the company. Like most of the oil forerunners, at that

time, already economically and morally devastated and without a capital that would allow him a decent life, Isaac took refuge in the city of Ibagué where he lived the last years of his life.

In 1893 Mr. FRANCISCO BURGOS subscribed one of these concession contracts with the National Government known as the Wiedmann Contract, for an area in the Sinú Valley. The contract expired in 1905 without having drilled a single well and affected by the civil war of the thousand days (*guerra de los Mil días*).

We could say that these initial concession contracts were the first step for the successful oil concessions of 1905. These contracts were based on law 30 of 1903 and became known as the contracts that initiated the Colombian petroleum industry. The De Mares Concession¹ in the Middle Magdalena Valley, which gave origin to the Empresa Colombiana de Petróleos on the 25th of August 1951 when this concession reverted, and the Barco Concession, located in the province of Norte de Santander. These landmark concessions were of such magnitude that they were the two only sources of hydrocarbon production in Colombia during twenty (20) years, from 1921 to 1941.

Colombia adopted the concession system because it was the one in use in the other countries of the world that had some traces of petroleum, such as Iran, Russia and others, private companies (the Standard Oil Company, Nobel Brothers, Anglican Persian Oil Company, etc.), proposed this contracting system that, because of the complexity of the operations and technical requirements, and the great economic risks inherent in the industry, in addition to the ignorance of states on this subject² was adopted by the States and their governors.

1 SANTIAGO, MIGUEL ÁNGEL, *Crónica de la Concesión De Mares*, Editorial Presencia Editores, Bogotá, 1986, pág. 22.

2 MEDINA ARROYO, FERNANDO, artículo “Las limitaciones a las modalidades sobre contratación petrolera en Colombia”, revista *Petróleo: política de contratación y competitividad*, Pontificia Universidad Javeriana, Educación continuada, pág. 22.

Law 120 of 1919 was considered to be the first hydrocarbon law, as it was the first exclusive regulation for petroleum exploration and exploitation, in an independent way from the mining activity. This law regulated the concession contract in the stages of exploration and production, as well as the petroleum easement³.

1.2. REGULATION OF CONCESSION CONTRACTS

During 1927 and 1931, the Colombian government studied the Concession System, with the help of four expert States (Mexico, England, Rumania and the United States) and the result was the formal and legal regulation of the concession contract by means of law 37 of 1931. This Law actually came to be the first Colombian Petroleum Code.

Having being regulated as an administrative contract and considering that it was a regulated contracting system; the Concession Contract had clauses that were fixed, rigid and completely unchangeable. One of the reasons why Colombia adopted this rigid contracting system was the discussion about the private vs. public ownership of the subsoil. This discussion has nowadays being completely resolved. It is necessary to note that this law declares that the petroleum industry is of public benefit and maintains the legal regime of the petroleum easement.

Almost 30 years later, and due to the importance that the oil industry acquired in the 50's, the concession contract was regulated in chapters III, IV and VI of decree 1056 of 1953, which since then became known as the new Petroleum Code.

The new petroleum code was modified in 1961 by means of the law 10, through which the government implemented more favorable conditions for the State, this at the same historical time when producing countries confronted the oil companies, that gave birth

3 ARCE ROJAS, DAVID, artículo "Historia del petróleo", revista *Vniversitas*, Pontificia Universidad Javeriana, n° 92, 1997, pág. 393.

to a new contracting systems known as the production sharing contract (Indonesia) and to reforms of the concessions in Saudi Arabia, Iran, Egypt and others countries.

Among the changes introduced by this law were the reduction of the exploration phase, the acceleration of the devolution of the acreage, the improvement of the use of natural gas and the increase in the percentage of the government's share in production.

1.3. COLOMBIA'S "HAND OVER" OF HYDROCARBON PROSPECTIVE AREAS

With the expedition of law 20 in 1969, that regulated the pre-republican private property rights of the petroleum reservoirs in the country, article 12 created the basis for future association contracts. In addition it created the "hand over" of hydrocarbon prospecting areas, by giving ECOPETROL certain areas to be explored and exploited directly by the company or in association with national or foreign capital. In fact, areas in the Tolima province were contracted with private investors by ECOPETROL⁴.

This modality had a precarious initiation, and short existence, because just at the beginning of the following lustrum the system was already modified through the expedition of the decree 2310 of 1974⁵.

1.4. THE ASSOCIATION SYSTEM

The concession systems and the "hand over", existed in Colombia until the expedition of Decree 2310 of 1974, when the concessions system was abolished for the future. A policy was adopted that granted ECOPETROL the exclusive faculty to carry out the exploration and exploitation of hydrocarbons property of the State; in this manner ECOPETROL was given extended faculties to carry

4 ARCE ROJAS, DAVID, *ibídem*, pág. 395.

5 ARCE ROJAS, DAVID, "Naturaleza legal de las contratos petroleros", revista *Universitas*, n° 87, 1994, pág. 61.

out these activities, directly or indirectly, as well as through contracts with national or international individuals or companies, under the modalities of association, service contracts or any other contracting system, different from the concession contract.

By means of article 1 of decree 2310 of 1974 and its regulatory decree 743 of 1975, ECOPETROL's Board of Directors was granted extended faculties to design the different contracting modalities and the terms and conditions of the contracts which ECOPETROL would subscribe. These laws gave faculties to ECOPETROL to establish the terms and conditions of the petroleum contracting system with only one limitation that the contracts which ECOPETROL celebrates require for their validity the approval of Ministry of Mines and the Energy by means of a ministerial resolution.

1.5. DEVELOPMENT OF THE ASSOCIATION SYSTEM

During the almost 30 years of life of this system, there were developed several modalities of the association contract which responded to the political and economic conditions at the time at which they were offered to the companies. The legal base of the association contracts, decree 2310 of 1974, was derogated through article 57 of Decree 1760 of 2003.

Within the association system it is worth point out, the following variations:

- *The risk sharing contract.* Used in 1987 with the intent to increase foreign investment in the country, it was proposed that ECOPETROL participated in a percentage of the exploration costs, and as a result the distribution of the production was greater for the State Company.
- *The production sharing contract.* By means of the expedition of Decree 2782 of 1989, this modality was introduced by which the production was distributed based on an incremental scale of proven reserves.

- *The association contract with “factor R”*. In 1994, due to the little success of the previous contracting modality, ECOPETROL established this option for distributing the production as a function of the profitability of the discovered oil field and not based on the magnitude of the discovered reserves. This “factor R” was applied when the accumulated production of the contracted area reaches the amount of 60 million barrels of oil.
- *The incremental production contract*. Again ECOPETROL, in an effort to increase the production and reserves in areas of direct operation by the State Company, offered this contracting system, in which the investment was wholly on the part of the private company, aiming to use advance technology to drill within the operation areas and thus increase the production and the reserves. A base line sets the minimum production of the field and the delta of the production is distributed between ECOPETROL and the company.
- *Association Contract with Favorability Clause*. Recently created through the expedition of Decree 1760 of 2003. Because of the period of time existing between the date of expedition of this decree and the enforceability of the new contracts underwritten by the ANH it was necessary to include in the existing association contracts a clause, well-known in the industry as “favorability” clause, that provides “mechanisms to equalize economic conditions”. The purpose of this clause is to allow the companies associated with ECOPETROL to enter in the future in contracts that the ANH may offer, in areas of the same type to that which it has now under contract, when the economic conditions are more favorable than those under which they are now working.

II. MODERN PETROLEUM CONTRACTS

In order to compare the petroleum contracting system in Colombia with those that at the moment are in operation in the world, it is necessary to review the elements and basic characteristics of these modern contracts⁶:

- *Modern Concession Contract.* This contract grants private investors a number of rights and privileges similar to those of the early concession. The concessionaire acquires ownership rights over its contracted area. Also he enjoys full managerial control of the operation and owns most of the production. The intervention of the State is restricted to royalties and tax collection.
- *Production Sharing Contract.* The private investor is merely a contractor in this contract modality but it maintains the property rights under the concession. The rights that derive from this contract are personal and not real as they are it in the concession contract. The operation and management of the project are under the control of the state oil company. The property of the extracted petroleum is just transferred to the private party at the point of export, that is, at the moment in which the product passes the bridle of the vessel through which the petroleum will be exported. In the same manner the right of property of the equipment used in the exploration and operation of petroleum is transferred to the State at the moment at which these enter the national territory. This contract is based on the production sharing and not on profit sharing.
- *Risk Services Contract.* This kind of contract is totally different to the concession system. In these contracts the private party

6 GAO, ZHIGOU, *International Petroleum contracts: Current Trends and new directions*, Graham & Tortman ltda/martinus Nijhoff, 1994, pág. 201.

does not take any risk, on the contrary, it is merely a contractor with certain rights in the provision of services. The contractor receives money as payment for services rendered, and clauses for production purchase options may exist. The State maintains the ownership right of the hydrocarbon and has the direct control of the development and production strategies.

- *Hybrid Contract.* These have been denominated Hybrids because they combine the most useful elements of existing contracts with the purpose of reaching the expectations and providing for the necessities of the producing Countries. There are so many contracts as countries that use them; this is the reason why the generalization becomes difficult. The common characteristic is that they are more complex and sophisticated than the previous ones. We could say that its nature is of risk taking, with right to share in the production and in the management and operation of the project.

2.1. BASIC PRINCIPLES OF MODERN PETROLEUM CONTRACTS

Whatever descriptive label may be given to these prototypes and hybrids, modern petroleum contracts have two essential elements in common⁷:

1. That the property right of the natural resource and the right to explore and to exploit hydrocarbons are in the hands of the State. The venture capital takes the risk and the costs of the exploration.
2. During the period of 1960 to 1990 all the modern contracts had clauses that increase the control and the management of the project by the producing State. Nevertheless, it is important to

7 BUNTER, MICHEL A.G., *The promotion and licensing of petroleum prospective acreage*, Kluwer Law International, The Hague, 2002.

mention that the recent trend in the last years has been the deregulation and privatization of the industry.

Modern petroleum contracts are also noticeable for the extensive responsibilities and obligations to be assumed by investors. These involve not only petroleum operations but also social and economic development in the area of petroleum operation. Obligations such as use and training of local personnel, technology transfer, the use of local goods and services, environmental protection, management of community relations, physical protection and dealing with NGOs are known as the “Soft Issues”. They have been introduced to these contracts in the third quarter of the last century⁸.

2.2. THE OBJECTIVES OF MODERN PETROLEUM CONTRACTS

Upon examining the advantages and disadvantages of modern petroleum contracts, it is difficult to make claims about which is the best of all. There is probably no best contract form but only a relatively better contract form. The ideal contract is one that provides a rational commercial foundation for the relationship, and effectively meets the legitimate aspirations and objectives of both parties. In order to identify an ideal contract form, it is necessary to look at the objectives of the contracting parties and therefore the contract that is chosen is the one that meets the necessities of both parties. For this reason we can conclude that the objective of the modern petroleum contract is to be fair and to strike a balance between the objectives of the producing State and the investing party, and to maintain the commutability, genetic as much as functional, of the contractual relation and thus avoid an unstable relation. In other words the contract needs to maintain the economic equilibrium through the life of the contract.

The objectives of the government can be summarized as follows:

8 GOA, ZHIGOU, *ibídem*, pág. 204.

1. Maintaining control over the natural resource.
2. Attracting risk taking investment.
3. Securing fast exploration and exploitation.
4. Meeting domestic consumption requirements.
5. Maximizing national revenue from petroleum.
6. Developing local technology and expertise.
7. Promoting national economic growth through petroleum development by oil companies.

Whereas the objectives of the investors are:

1. Finding oil and gas discoveries.
2. Obtaining a reasonable rate of return.
3. Securing crude oil supply.
4. Ensuring sufficient security of investment.
5. Retaining as much flexibility and control of the operation as possible⁹.

2.3. THE LEGAL NATURE OF INTERNATIONAL PETROLEUM CONTRACTS

A few remarks on the legal characterization of world petroleum agreements are necessary. Since there are two schools of thought with respect to the legal nature of petroleum contracts at the international level, we will make a reference to them. For some jurists from western countries, the petroleum contracts acquire status of international agreements because they contain well-established international principles such as *Pacta sunt servanda* and *Rebus sic stantibus*. Other writers, mainly representing the producing countries, have asserted that such agreements should be governed by the law of the host state based on fundamental principles of private international law and that the contracts can be amended by the government for the public interest.

9 TAVERNE, BERNARD, *An introduction to the regulating of petroleum industry*, Graham & Torteau Ltda /martines nijhoff, 1994.

Since this theoretical discussion will remain, as long as each school of thought will provide more arguments and theories to sustain their position, it is preferable to separate ourselves from this analysis and to present our position.

Modern petroleum contracts are a mixture of private and public law.

The private law elements are a logical consequence of the contractual and commercial nature of the business. The public elements are a result of the intervention of the government in the control of the production, fuel domestic supply, and the rules for occupational health and safety, amongst others.

In the Colombian case the association contract, is a State contract that is governed by its own rules and especially by private law in accordance with decree 2310 of 1974 and decree 743 of 1975. In the case of the contracts that will be issued by the Hydrocarbon National Agency, starting the 1st of January, 2004, and in accordance with numeral 5.3 of article 5 of the Decree 1760 of 2003, these contracts need to be in agreement with the terms of article 76 of Law 80 of 1993. This is to say, that these contracts will be governed by the regulations applicable to exploration and exploitation contracts for natural resources, which will be developed by the Hydrocarbon National Agency under the criterion of objective selection and under the principles of transparency, economy and responsibility established by the rules for public contracting of Law 80.

In other words, these new petroleum contracts will be State agreements and they will be governed by the provisions of private and public law as applicable to them.

III. TRENDS IN PETROLEUM CONTRACTUAL DEVELOPMENT

To be able to give a recommendation to the State, so it will be able to design contracts that adjust to the international reality of the petroleum industry, it is necessary to study the way in which the

main trends of the last 20 years have evolved and to identify the direction in which the contractual relation between the petroleum producing states and the investors has developed.

In addition to the characteristics previously explained, general trends have emerged from recent contractual developments as follow¹⁰:

1. *Mutuality of interests.* Most important among these trends is perhaps the mutuality of interest between governments and companies. Based on the understanding that reciprocity is the foundation of any successful operation, each side has accepted its limitations and has taken steps to recognize a mutuality of interests in their relationship in order to encourage maxim cooperation for the common good.

The typical example of these trends is when petroleum producing countries frequently revise the contractual terms and conditions to meet the commercial interest of oil companies in a changing market. Also the companies day to day acquire greater social and economic responsibility towards the government of petroleum the producing countries. In this way the relationship based on mutuality of interest has evolved, replacing the one of permanent confrontation.

This trend of mutuality of interest has made the contractual relation more stable and constructive.

2. *Contractual convergence and synthesis.* As a consequence of direct antithesis of the classic concessionary system, over the past decades there have been clear trends towards convergence of contract terms and perhaps synthesis of the modern petroleum agreements. The pace of assimilation accelerated as terms of these contracts became more publicized, and became increasingly influenced by one another.

10 GOA, ZHIGOU, *ibidem*, pag. 221.

As a result of this process, modern petroleum contracts share many common elements such as work obligation, minimum expenditure, relinquishment, employment and training of nationals and preference of local good and services.

As a matter of fact, you can say that 80% of operation clauses in the modern petroleum agreements are the same, irrespective of the type of contract.

As a conclusion, there are a few real differences between most formats and contracts in use.

3. *Standardization.* This is a noticeable trend of the last 30 years. The different petroleum producing countries have generated formats or predetermined models of contracts and for the contracting process. In a similar manner the petroleum companies have developed standard clauses to regulate special facets of oil production. Nevertheless, it is recommendable to negotiate each contract individually although it may include standard clauses.

The standardization of contracts brings certain benefits as government officials and company representatives can become familiarized with petroleum agreements. It also facilitates the negotiation of contracts and agreements, reducing transaction time, costs and other problems, finally improving and simplifying the management and administration of the contract.

4. *Sophistication.* In general recent petroleum contracts have reached a high degree of sophistication. This complexity is perhaps partly due to the gradual development and maturity of the legal infrastructure and growing familiarity with legal frameworks for the petroleum industry in producing countries. Consequently, financial and fiscal clauses are increasingly well designed and frequently upgraded to become much more sophisticated.

On the other hand, clauses have been developed with a high level of sophistication to regulate “Soft Issues”, such as the clauses that regulate community relations and security and human rights clauses.

5. *Flexibility*. The evolution towards contractual flexibility is also apparent in petroleum contracts. The development of contract terms in general, and of fiscal instruments in particular, that maintain the economic balance from the beginning and through the life of the contract allocating profits in a way that is more responsive to the profitability of an operation make the deal fairer to both sides.

In theory, the commutative that is derived from a perfect mutuality of obligations allows equitable terms for developing both small and large fields. This flexibility adds the element of stability that is required by a contract of this nature. There is a close relationship between equity and stability. The relation between fairness and stability is well known.

A contract with sufficient flexibility has the advantage of being able to respond to a wide range of economic variables within the terms of the contract, with the consequent conflict and renegotiation reduction. The change of the petroleum policies of the oil producing countries are no longer an imposition and confrontational and have evolved to be a clear cooperation and transparent negotiation.

6. *Reduction in government control*. Since the 80s there has been a decline of the role of the State. Governments have been reducing their involvement by introducing such measures as granted royalties or royalty exemptions and the reduction in or not at all government participation. This phenomenon shows a clear transition from bureaucracy to business in the government-company relationship.

Modern petroleum contracts and legislation are likely to provide for more rational governmental prerogatives. Government participation will be more gradual and optional, changing from a majority participation to participation in information, training and technology transfer and to obtaining additional fiscal participation in the case of profitable ventures. The participation of the State is less intrusive evolving from a micro management to a macro management concept that merely requires the transmission of information, or consultation with the government.

The size of the government take is more reasonable, from more than 50% take to a profit split that varies according to the field's level of profitability.

7. *Contractual dynamism.* Governments and companies have moved from the static and changeless relationship defined by the concession agreement towards an evolving relationship marked by dynamism and mutability. The petroleum contracts are periodically and systematically reviewed and adjusted to maintain the contractual equilibrium. This new pattern of relationship can be characterized as dynamic, evolving in a manner that is necessarily adjustable to the prevailing conditions while still recognizing the legitimate interest of the contracting parties.

Petroleum contracts are inherently dynamic because they are extremely complicated documents designed to govern a long term relationship, negotiated on the basis of existing conditions and assumed factors that will not be confirmed for many years. Additionally, they are agreed between parties whose bargaining positions may change over the life of the contact. Now days, many producing countries believe that provisions for renegotiation are an essential feature in any satisfactory agreement.

The advantages of a review clause include the following:

First, it serves as a pre-notification to both parties of review and possible revision so that surprises and misunderstanding

can be minimized. Second, potential friction and conflicts can be avoided through the operation of a legitimate process; and finally, the review and revision process can provide an opportunity for both parties to find a new equilibrium. The commutative is not just for the origin of the contract it has to be applied during the life on the contract¹¹.

8. *Reallocation of rights and obligations.* In many aspects the petroleum contracts have migrated from the contractual inflexibility of the concessions system to mutability; first, with respect to the reallocation of the contracts within the domestic legal system. The original concession contracts were designed for the international legal system, however in the modern petroleum contracts, this concept has become obsolete.

Second, with respect to reallocation of petroleum goods and services, it is now standard in the petroleum contracts that the contractor has to give preference to local goods and services.

Finally, to reduce the dependence on aliens and eventually developing a national industry, with regard to reallocation of human resources and expertise, training of nationals and the transfer of technology, all oil contracts contain clauses pertaining to these issues.

9. *Geographical preference.* Analyzing modern petroleum contracts there are indications of preference for the form of contracts base on the geographical location. One can conclude that the production sharing contract is of greater acceptance in Asia and the Pacific Basin, whereas in Western Africa the modern concession is used more frequently while the hybrid contracts are preferred in the South American countries.

11 SÁNCHEZ, RAFAEL JURISTA, *La ejecución del contrato de obra pública*, impreso en Hauser & Menet, S.A., España, 1983.

10. *Rationalization process.* Since the 1980's and until now, the tendency has been to look at the conception of the sovereignty of the State as global and it has been expressed in several ways such as the deregulation, decontrol, demonopolization, debureaucratization, decentralization and globalization

This phenomenon is driven by several internal and external factors. At the national level most of the petroleum producing countries has been pressed by an increase of the demand of fuels, limited by its production and a short budget. At the international level the drivers include international competition for risk capital and globalization.

This phenomenon named the rationalization process has caused important reforms in oil policy of the petroleum producing countries as well as in the policies of the investment of the companies.

Recently in many petroleum producing countries the State monopoly that existed through the public oil company have been dismantled. The state companies have been sold to private investors searching for greater efficiency and better managerial practices, which, apparently, are perceived to be in the private sector.

11. *Third party intervention.* The phenomenon of globalization and the knowledge that now townships have about exploration and exploitation of oil, the environmental impact that this extractive industry generates, and the wealth that is implicit in the oil industry due to the great sums of money that are invested, have generated a world wide tendency of people alien to the oil activity, to want to intervene and prevent this activity. It is argued that this way of exploration and exploitation of the natural resources is not in accordance with the interest of the human being.

National and international NGO's intervene arguing the protection of the environment. They interpose *defacto* actions and legal procedures against the extractive petroleum activity. Another group of citizens adducing a similar interest argues that the oil activity violates its fundamental rights and liberties and raising the human rights flag accuse the oil companies of violating said rights.

In some countries of the former Soviet Union and in Colombia there exist some delinquent gangs specialized in draining the hydrocarbon transport systems with the purpose of illicitly selling this product. Finally, and with greater presence in Colombia, illegal groups attack and destroy petroleum facilities causing enormous damage to the environment and extraordinary economic losses to the country and the oil companies. All these actions are violations of the International Humanitarian Law.

In modern petroleum contracts there is a trend to establish a sophisticated clause that governs the actions to be taken because of the existence of these kinds of illegal actions. Additionally they include the different legal and juridical actions that can be taken by the producing countries.

I want to emphasize the government and oil companies' passive behavior with respect to the attacks to oil industry facilities, having at their disposal a good legal tool which is the International Humanitarian Law. I do make a call to the government and to the oil companies no just to define the human rights policy but also to use the International Humanitarian Law as a good way to promote the peace that is badly needed in Colombia¹².

12 ARCE ROJAS, DAVID, *Petróleo y derecho internacional humanitario*, Pontificia Universidad Javeriana, 1999, pag. 92.

IV. BRIEF ANALYSIS OF THE NEW COLOMBIAN CONTRACTING SYSTEM FOR PETROLEUM EXPLORATION AND EXPLOITATION

As it was mentioned hereinabove, the ANH recently submit to the oil industry the new basis for the contracting system for petroleum exploration and exploitation. These new elements under debate deserve some reflection.

The objectives of the new policy are, amongst others, (i) apply the legal order of decree 1760 of 2003; (ii) To increase dramatically the oil activity by means of encourage 2D and 3D seismic campaigns, drilling exploration wells, thereby incrementing proven reserves and production; (iii) last but not least, to become self sufficient with respect to the domestic fuels demand and to generate a production surplus for export.

In order to achieve these objectives, the ANH has designed a strategy base on various elements, starting with improving competitiveness of Colombia to attract oil investment in either small, medium or large projects. The ANH has introduced four basic changes:

- The investor is compensated 100% for the exploration risk. The government will not intervene in any phase of the project. If the government wants to participate in the project, it can do so by means of a “farm in” agreement through ECOPETROL and in similar conditions to those for any other investor.
- The investor’s production shared participation is base on the total production after deducting the royalties.
- The State take is just royalties and taxes. The State will only get additional benefits in case they are generated by the project. The State take is mainly oriented to sharing additional benefits generated in non active areas through a high price market. In active areas the additional benefits are derived from a high price market or through lower costs.

- The duration of the exploitation period could be up to the total drainage of the field reserves. It will apply for the filed not for the total contract.

Additionally, the ANH has announced that the new contracting regime will be governed by the current oil industry principles, such as:

- a) Appropriate balance between Risk and compensation.
- b) Avoid freezing areas through incentives, penalties and guarantees.
- c) Achieving harmony between the size of company and the conditions of the project.
- d) Operational flexibility for the investors.
- e) Flexibility in the agreed work schedule with the ANH as prepared by the investor, but with rigorous fulfillment.
- f) Integral management of the petroleum resource, base on the geological, reserves and discovery information furnished by the contractor, amongst others.
- g) Permanent follow up without intrusive intervention, with the exception of essential issues; and finally.
- h) Flexibility for the special case of the exploration and exploitation of heavy crude and gas.

From a first study of the objectives, strategies and principles that will govern the new hydrocarbon contracting system, it can be inferred that the new Colombian petroleum contract will be a modern concession contract, in which the State take will be royalties

and taxes and the exploration and exploitation risk will be taken by the investor. It will be a very flexible system that will be governed by the harmony and commutative principles throughout the life of the contract. It is missing tow of the current trends in modern petroleum contracts which are social responsibility and respect for the contractual jurisdiction when exogenous factors intervene. These parameters are mentioned by decree 1760 of 2003, but do not find eco in these first contractual bases.

V. CONCLUSIONS

1. In Colombia, like in the rest of the world the concession was used at the end of C XIX and the first half of C XX. Known as the period of the concession.
2. Modern contracts first appeared in second half of C XX and the production sharing Contract in the 1960's. The Services Contract without Risks in the 1970's and the Hybrid Contract in the middle of the 1970's. This was the Confrontation phase of oil contracting.
3. Modern contracts changed their direction to one of mutual interest, commercial viability and stability. Cooperation phase.
4. The governments of the producing countries have changed their philosophy for contracting from one based on political ideology to the one based on pragmatism and from bureaucracy to businesses vision.
5. The future of petroleum contracts will be governed by the criterion of the interdependence between commercial viability, sustainable development and stability.

6. The future oil contracts must be oriented under three principles: Flexibility, Commutability and Harmony

VI. RECOMMENDATIONS

The Hydrocarbon National Agency has the challenge to present to the oil business community a new petroleum contracting system for our Country. This is a challenge of great importance for which the agency must consider world wide trends of the petroleum Industry in addition to the internal situation of our Country.

Therefore, and as a member of the academic community, I dare suggest to the national government that this new hydrocarbon contracting system must be guided by the following principles:

1. National sovereignty over hydrocarbon resource.
2. Commercial viability.
3. Flexibility.
4. Commutability and dynamism.
5. National Sovereignty over renewable natural resources (environment).
6. Legal, Commercial and Political stability.
7. Harmony.
8. Social Responsibility and Respect for the contractual jurisdiction when exogenous factors intervene.