EXAMINING THE RELEVANCE OF STABILIZATION CLAUSES IN PETROLEUM SHARING AGREEMENTS VIS-À-VIS STATE SOVEREIGNITY- LESSONS FOR UGANDA

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APRIL 2022

DECLARATION

I, **DEEPA VERMA REG. No. J21M23/010** hereby declare that this dissertation is my work and it has not been submitted before to any other institution of higher learning for fulfillment of any academic award.

Signed………………………………………

Date………………………………………….

APPROVAL

This is to certify that, this dissertation entitled "**EXAMINING THE RELEVANCE OF STABILIZATION CLAUSES IN PETROLEUM SHARING AGREEMENTS VIS-À-VIS STATE SOVEREIGNITY- LESSONS FOR UGANDA**" has been done under my supervision and now it is ready for submission.

Signature……………………………………………

Associate Professor George W.K.L. Kasozi
(Academic supervisor).

Date…………………………………………………

DEDICATION

"Study hard my daughter" he said, "wish I was blessed with this opportunity, but sadly I was not"

I dedicate this thesis to a simple man of few words my father – the late Rajinder Pal Verma (Raj) whose words propelled me to greater academic heights.

A further dedication to my two pillars of strength- Uncle Kaka and Aunty Gudo whose unsparing support made the achievement of my academic dreams possible, but who sadly did not live long enough to see this milestone.

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LIST OF ACRONYMS

IOCs	International Oil Companies
FOCs	Foreign Oil Companies
OGM	Oil and Gas Management
HG	Host Governments
PSAs	Petroleum Sharing Agreements
NOC	National Oil Company
FIC	Foreign Investment Contract
PAU	Petroleum Authority of Uganda
UNOC	Uganda National Oil Company
PSNR	Principle of state Sovereignty over Natural Resources
OECD	Organization for Economic Co-operation and Development

ABSTRACT

Stabilization clauses are clauses in private contracts between IOCs and HGs that largely protect the interests of the IOCs in case of changes in the host country's law during the project's life cycle. Stabilization clauses are thought to be a good strategy to encourage investment since they provide a favorable investment environment.

Despite the necessity and importance of stabilization clauses, as shown above, these clauses are said to be in conflict with the principles of State sovereignty in general, which allows a particular State to decide on how to manage its internal affairs, and in particular, the principle of state sovereignty over natural resources (PSNR), which allows the host state to explore and exploit its natural resources without interference.

In the case of Texaco v. Libya,[1] it was held that stabilization clauses limit the host State's sovereignty because the HG committed to waiving its sovereignty. Further in the case of *LETCO* v. *Liberia* (ICSID),[2] the tribunal held that the major rationale of stabilization clauses is to protect against arbitrary actions of HGs and can therefore not totally impair the sovereign power of states.

The Doctrine of State sovereignty enables States to exclusively control among others, their natural resources. These clauses, however, inhibit exercising State sovereignty by limiting HGs from exercising their sovereign powers such as enacting or amending the national laws. Thus, this research undertakes to examine the relevance of stabilization clauses in petroleum sharing agreements vis-à-vis State sovereignty with an aim of providing lessons for emerging oil and gas economies to developing countries such as Uganda.

[1] 17 ILM 1978, p. 1
[2] 26 ILM 666-7

CHAPTER ONE:

INTRODUCTION

1.0. Introduction.

Petroleum is believed to be one of the most important commodities on the market today.Ownership of petroleum resources has shifted in recent years, particularly in developing nations, to the State or national oil firm. Petroleum agreements typically demand a large sum of money andlong-term commitments to proceed with the exploitation and exploration of petroleum resources,leaving investors exposed to risk for a certain length of time. Due to the volatility nature of oil prices, several investors have realized that their investment will be unprofitable after they have signed the contract. These and other factors may persuade the investor to seek changes to the agreement in response to changing political and environmental conditions. As a result, theinvestors attempt to avoid having to renegotiate the original agreement due to subsequent changesin the HG's laws.

Ultimately, investors have a variety of options for dealing with the risk inherent in petroleum agreements, including as risk distribution, risk management, risk insurance, and risk shielding. The most common is risk mitigation, in which the investor utilizes political, economic, and financial clout to persuade the host State not to change its laws. Stabilization and adaptation clauses are the most common ways for long-term contract parties to share risk and ensure contractual stability. Finally, investors can limit their risk by incorporating clauses like international arbitration, choice of law, adaption clauses, and stabilization clauses in their contracts.

Energy investments, in particular those in the oil and gas industry are typically expensive ventures requiring huge sums of capital, high levels of expertise and skills. These projects also involve high profile risks such as conducting geological surveys, transportation, exploitation and storage of the deposits discovered. In most cases these perquisites are often not readily available in developing countries, leaving oil rich States with no choice but to grant development rights over oil and gas fields to International Oil Companies (IOCs) that have the skills and capital required to invest in the oil and gas projects. These development rights are granted either through concessions or contractual arrangements depending on the level of control given to the IOCS and level of Host

Governments' (HG) participation.[3]

Under concessions IOCs are granted absolute ownership and proprietary rights over the oil and gas fields which are usually for long periods of time, ranging from 70-90 years with the HG only benefitting from the taxes and royalties paid from the oil and gas.[4]

The contractual arrangements include the Petroleum Sharing Agreements (PSAs) which have been widely adopted in the oil and gas industry today. According to Taverne[5] PSAs are defined as a form of contract between an oil company (IOCs) and a State entity usually the National Oil Company (NOC), where the latter authorizes or grants rights to the former to exploit and develop an oil and gas field. The IOC provides the technical and financial services for the oil and gas operations and in return is compensated by the HG for the risk taken and services rendered in accordance with the terms of the PSA.[6]

Most petroleum and exploration contracts carried into between the host state who owns the resources and a foreign investor include a stabilization provision to prevent either party from unilaterally altering, abrogating, or terminating the contract entered into by both parties.

PSAs have been widely accepted in this industry due to the fact that by their nature, these contracts maintain the sanctity and equilibrium of contractual obligations between the contracting parties through the provisions of stabilization clauses with practitioners have arguing that these clauses are essential because they ensure sustainability of the PSA merits.

Given the volatility of oil and gas prices, unpredictable geology, and global rivalry for precious capital and know-how, governments keep fiscal regimes under constant scrutiny; the dynamics of

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[3] Nutaroot Pongsiri, "Partnership in Oil and Gas Production-Sharing Contracts" (2015) 17(5) International Journal of Public Sector Management 431–442.
[4] Tade Oyewunmi, "Natural Gas Exploration and Production in Nigeria and Mozambique: Legal and Contractual Clauses" (2015) 13(1) O.G.E.L. 2.
[5] Bernard Taverne, "Production Sharing Agreements in Principle and Practice" in M.R. David (ed.), Upstream Oil and Gas Agreements (1996), p.44.
[6] N'di and T.W. Walde, "Stabilising International Investment Commitments: International Law versus Contract Interpretation" (2003) 1 O.G.E.L. Archive Issue 32.

what constitutes a "fair share" of resource rent are essentially unstable. While both governments and investors have the same goal (to maximize the exploitation of the hydrocarbon resource), governments generally want to ensure that the country gets a fair share of the resource; investors, on the other hand, want a minimum return on investment and a simple and stable tax regime. The problem with these goals is that the interaction between governments and investors is dynamic, making long-term budgetary stability a tough notion to achieve in practice.

International oil firms normally conduct extensive due diligence on the HG's geological, socioeconomic, political, legal, and fiscal environments before committing to an investment. The findings will be used to negotiate the project's financial and other aspects. This is in addition to establishing criteria for evaluating the commercial viability of the business being undertaken. The goals of the two main actors in petroleum exploitation, the HG and IOC, not only differ but frequently collide. While international oil firms are motivated by the desire to maximize profits, host countries are motivated by revenue maximization and the achievement of other governmental goals. This is where any potential disputes between these two principals stem from.

Petroleum exploration initiatives are not only expensive, but they also take a long time to complete. Many developing countries lack the financial and technical resources needed to develop their petroleum resources, so they turn to well-capitalized foreign oil companies for help. The HGs might include developing countries with political and economic crises, as well as a history of coups and counter-coups. They may offer financial incentives to persuade corporations to invest the capital, skills, and management required to successfully exploit their petroleum resources. Once an investment is made, international oil firms become susceptible since they may not be able to readily withdraw without major financial consequences. They are at the mercy of the HG at this point.

IOCs seek risk mitigation strategies from the beginning of their petroleum exploration and exploitation operations to defend against future demands from the HG to reconsider the initial terms of their petroleum agreement. Petroleum price cyclicality has the ability to make a seemingly profitable agreement appear undesirable if prices climb significantly in the future. This is the most typical source of conflict between IOCs and the HG, which is looking for changes to the original

agreement in reaction to political pressure and changing conditions.

Investors' quest for legal and fiscal stability is motivated by their desire to regain a respectable return on investment in the shortest amount of time possible. Investors are concerned about a variety of financial and non-financial factors. Threats of confiscatory actions, such as direct expropriation, and other subtle maneuvers that infringe on investors' rights are among them. Changes in labour law, as well as increased health, safety, and environmental criteria, may make international oil firms wary of incurring more operational costs.

The objective for IOC at the start of a project is to develop a risk management framework to limit or at least reduce the exercise of HG legislative prerogatives that could have a negative impact on profits. This is best achieved through the enactment of *stabilization clauses.*

According to Cameron the term stabilization applies to all the mechanisms contractual or otherwise, in the context of international energy contracts, this is intended to provide for the benefit of specific economic and legal conditions which the parties consider to be appropriate at the time they entered into the contract.[7]

In a nutshell, stabilization clauses in PSAs are those clauses or provisions aimed at specifically stabilizing the legal regime governing the PSAs and maintaining the status quo of the regulatory regimes of the HG at the time of contracting.[8] Depending on the type of stabilization clause , IOCs may seek protection against unilateral modifications of the PSAs and against HGs taking over the rights of the investors.

1.1. Background to the Study

Stabilization clauses form a regular step in the oil contracting process. The past experiences in oil and gas regions like the North Africa and the Middle East of nationalizing and expropriation of IOCs' assets resulted in to several energy disputes. This is one of the factors that led to the adoption of stabilization clauses in PSAs by IOCs in several jurisdictions as a deterrent mechanism to the

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[7] Cameron, P., 2010. International energy investment law: The pursuit of stability. OUP catalogue.p.69

[8] Bertrand Montembault, "The stabilisation of state contracts using the example of oil contracts. A return of the Gods of Olympia?" I.B.L.J. 2003, 6, 593-643

nationalization movements.

Nationalization comprises of HGs taking over IOCs' assets or the sector entirely. It encompasses physical takeover or seizure of IOCs assets or enactment of laws and regulations that vest HGs with powers to transfer or takeover assets in the entire sector, or even adopt measures that will affect the economic equilibrium of a contract such as introduction of new taxes which in the long run can frustrate production or investment in the oil and gas sector. When the oil prices are high, HGs tend to deviate from certain contractual obligations in order to take larger shares of the windfall revenues this also influenced the adoption and use of stabilization clauses in PSAs.[9]

Oil, gas, and natural resource riches are abundant in emerging countries, accounting for a significant portion of the GDP, export earnings, government income, and employment. Its economic and social transformation potential is obvious for any country capable of effectively harnessing it in a single generation by converting non-renewable natural resources into capital, allowing a country to transition from poverty to at least middle-income status and allowing its citizens to enjoy a better quality of life.

The inclusion of large unknowns when the fiscal regime is originally set at the start of the province opening – which is often before a single exploration well has been dug – is one among the reasons why governments find it difficult to maintain long-term fiscal stability. Oil and gas basins invariably grow in unforeseen ways: few predicted the riches in the North Sea, the Deep-water Gulf of Mexico, or the shale revolution when drilling first began in the 1970s.

Oil and gas investors' appetite is influenced not only by tax rates, but also by the extent to which the government shares the project's risks, despite the fact that firms, unlike governments, have the ability to diversify certain levels of risk. Governments, on the other hand, can reduce one major risk – fiscal risk – by ensuring budgetary stability. A constantly tweaked tax structure tends to erode investors' faith in government policies, resulting in a greater discount rate to compensate for increased risk, lowering the value placed on future income streams and raising investment barriers. As a result, budgetary stability protects the foundation upon which investment decisions are made.

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[9] Nouriel Roubini, "Is Resource Nationalism Back?" (2009) Forbes.com

Despite these alluring advantages, petroleum fiscal systems are rarely stable in practice. Because circumstances are always changing, any tax system must allow for some flexibility in order to adjust to changing situations and evolve in response to substantial changes in the external environment.

Various scholars agree that stabilization clauses date back to the period between the first and second World Wars, when host governments began to take over concessionary contracts from foreign investors, prompting the inclusion of stabilization clauses in concessionary agreements to ensure that those concessions would be completed.

The origin of stabilization clauses in PSA's dates back as far as the 1930's when they were introduced in the new oil provinces of the Middle East. Their actual usage became common in the 1960s as a result of several oil-producing countries nationalizing and expropriating petroleum industry assets in order to profit from rising oil prices. After that, scholars attributed the drop in interest in the use of stabilization clauses to UN Resolutions and writings from scholars in the 1970s that viewed stabilization clauses as incompatible with the principle of state sovereignty over natural resources (PSNR), which must be exercised in the interest of national development and the well-being of their people. The clauses were used as a means to deter the expropriation and nationalization of resources which characterized the 1970s and 1980s. These clauses target the risks that may cause losses to the investors. Such risks include; changes in the legal and regulatory frameworks, direct expropriation, and gradual loss of investment value by a series of measures over time or the loss of future anticipated opportunities.

Because of the devastating drop in mineral prices in the mid-1980s, which drastically reduced the revenue that developing countries received from their extractive industries, governments were encouraged to enact policies aimed at attracting foreign direct investment as a means of generating more revenue, which resulted in the unexpected return of stabilization clauses. Stabilization clauses are in essence contractual assurances of negotiated terms against future legal or regulatory changes by providing legal and fiscal stabilities. The operation of stabilization clauses in most cases affects a country's sovereignty. This therefore calls for negotiation between parties so as to

attain a middle ground within an IOC's desired privileges and the state's sovereignty.

State Sovereignty

Although effective and flexible negotiations throughout the project cycle play a crucial role in encumbering energy disputes, there are other aspects that should be taken into consideration as far as energy projects are concerned such as the concept of State sovereignty. One finds a struggle between IOCs pushing for stabilization clauses to secure their investments and States accepting the same at the cost of their sovereignty.

According to Karen, the principle of State sovereignty is a concept of international law that is to the effect that a State is supreme in as far as its territory and independence in international relations is concerned.[10] According to this principle, peoples and nations' rights to permanent sovereignty over their natural wealth and resources must be exerted in the interests of national progress and the well-being of the people of the state concerned. The principle of State sovereignty was further enhanced by the UN General Assembly Resolution 1803 adopted in 1962[11] which is to the effect that States and their people have a 'permanent sovereignty over their natural resources'.

Important to note though, is the fact that although the IOCs operate both in developed and developing countries, they do not apply the same standards with respect to negotiating stabilization clauses in the former. One finds that the developed economies do not offer stabilization clauses at all, clearly keeping their State sovereignty intact compared to developing countries that always incorporate such clauses at the cost of their sovereignty simply to attain favor of investments in the oil and gas sector. This is partially because developed economies have stable governments with expected political stability, unlike developing ones where the regimes are usually unstable, associated with many political risks. Cases in point are changes in governments through coups as was the case in Africa and Latin America in the 1960's and 70's thus making the issue of

[10] Karen Gevorgyan; Concept of state sovereignty: Modern attitudes. http://ysu.am/files/Karen_Gevorgyan.pdf accessed 23rd April, 2021

[11] Petra Gumplova, (Sovereignty over natural resources – A normative reinterpretation, 2019), Cambridge University Press. <https://www.cambridge.org/core/journals/globalconstitutionalism/article/sovereigntyover-natural-resources-a-normative-reinterpretation/70CCEAEDEB6EE45ADC7CE88BE6A3D0BC>

stabilization clauses in oil and gas contracts increasingly an important subject.[12]

With regard to the doctrine of State sovereignty and the legislative mandate of the HG in mind, this paper advances a discussion on whether stabilization clauses are still relevant in the 21st century moving forward or should investors instead of advocating for stabilization clauses find other avenues to protect their investments, while preserving State sovereignty of host states over their natural resources. The paper is aimed at providing lessons for Uganda's emerging oil and gas industry.

1.2. Statement of the Problem

Stabilization clauses are clauses in private contracts between IOCs and HGs that largely protect the interests of the IOCs in case of changes in the host country's law during the project's life cycle. Since investments are subject to the rules of the HGs, there is a danger that domestic laws would change, thereby affecting the investment. The investment contract is particularly damaged if the host state exercises its power and expropriates the investor. Expropriations of this nature have occurred on a worldwide scale, prompting investors to take steps to reduce the danger of expropriation or assure compensation.

Stabilization clauses are frequent in long-term investment contracts, such as those involving public infrastructure or the extractive industries, despite the fact that they are not included in all investment contracts, the necessity and importance of stabilization clauses, as shown above, are said to be in conflict with the principles of State sovereignty in general, which allows a particular State to decide how to manage its internal affairs, and in particular, the principle of state sovereignty over natural resources (PSNR), which allows the host state to explore and exploit its natural resources without interference.

The underlying problem proceeds from the fact that some States consider the idea of permanent sovereignty over their natural resources to be sufficient basis for unilaterally terminating a

[12] Nalule, V.R., 2021. Land Access in the Perspective of the African Energy sector. In Land and the Extractive Industries: Challenges and Opportunities in Africa. Hart Publishers.

concession deal, despite the presence of a stability clause in the investment agreement.

The Doctrine of State sovereignty enables States to exclusively control among others, their natural resources. Most IOCs lobby for the inclusion of stabilization clauses in PSAs in pursuit of investment protection against unforeseen political and legal events such as changes in the HG's laws. These clauses, however, inhibit exercising State sovereignty by limiting HGs from exercising their sovereign powers such as enacting or amending the national laws. Their continued use could result into commercial conflicts between HGs and IOCs. Thus, this research undertakes a legal analysis of stabilization clauses and their efficaciousness in guaranteeing equity in oil and gas exploration with the intention of examining the relevance of stabilization clauses in petroleum sharing agreements vis-à-vis State sovereignty.

1.3. Purpose of the study

The purpose of this research is to examine the relevance of stabilization clauses in PSAs vis-à-vis State sovereignty aimed at providing lessons for Uganda's emerging petroleum industry.

1.4. Significance of the Study.

i. To the Researcher.

The study enables the researcher to fulfil one of the basic requirements for the award of the degree of master of laws (LLM) Oil and Gas of Uganda Christian University, Mukono (UCU).

ii. To the policy makers.

The study helps to recommend and illustrate practical solutions to the policy makers. Through the extensive research carried out, oil and gas practitioners will be able to learn more of how to draft stabilisation clauses without compromising State sovereignty while at the same time protecting the IOC's investments.

iii. The study will equally be useful to other researchers and/ or academicians in the field of oil and gas, energy governance and geologists aspiring to improve their knowledge on negotiating PSAs in the oil and gas industry

All in all, this study will enable an investigation into the legality of stabilization clauses and, as a

result, whether they can be simply implemented, taking into account the interdependence of the validity and enforcement of international investment treaties. Given the importance of stabilization clauses in protecting investors' rights and interests, and the fact that investment benefits both the investor and the host state, this study is important because it aims to assess the validity and enforcement of those important clauses incorporated in international investment agreements in the event of changes in law, and to examine if the rationale and purpose of the clauses are still valid.

1.5. Justification of the study.

The past experiences of HGs nationalising IOCs' assets, high levels of capital required and the high risks in the oil and gas industry are some of the major reasons for the increased use of stabilisation clauses in PSAs by IOCs/investors in a bid to protect their investments. However, stabilisation clauses because of their freezing nature, have over time been known for limiting States in exercising their sovereign powers as such clauses limit their powers to amend the legal regimes in relation to the PSAs. Thus this research examines the relevance of the stabilisation clauses vis-à-vis State sovereignty with the aim providing lessons for Uganda's emerging petroleum industry.

1.6. General objectives

The general objective of this research is to examine the relevance of stabilization clauses in PSAs vis-à-vis State sovereignty with the aim providing lessons for Uganda's emerging petroleum industry.

1.6.1. Specific objectives

i. To find out the relevance of stabilization clauses in PSAs.

ii. To find out the legal implications of stabilization clauses on the sovereignty of resource rich States.

iii. To find out whether Stabilization Clauses are still relevant in the 21st Century.

iv. To evaluate the legal framework that governs the oil contracting system in Uganda's oil and gas sector.

v. To provide to the emerging Ugandan Oil and Gas sector a peak into the future of the effect of stabilization clauses in PSAs, so that they learn from the lessons of other mature provinces.

1.7. Research Questions

i. What is the relevance of stabilization clauses in PSAs

ii. What are the legal implications of stabilization clauses on the sovereignty of resource rich states?

iii. Are Stabilization Clauses relevant in the 21st Century?

iv. What is the legal framework governing Uganda's oil and Gas contracting system.

v. What lessons are there for Uganda?

1.8. Scope of the Study

The scope of the study is divided into three perspectives, these include Content, Time and Geographical.

1.8.1. Content Scope

The study encompasses international oil and gas laws, regulations, and practices. There's also some literature on the oil and gas industry, specifically on stability clauses. The information also includes a comparison of stabilization clauses in the oil and gas sector from different jurisdictions

The content of this study focuses on examining the relevance of stabilisation clauses in Petroleum Sharing agreements vis-à-vis State sovereignty with the aim of providing lessons for Uganda's emerging oil and gas industry.

The research focuses on discussing how the inclusion of stabilization clauses in PSAs has undermined State sovereignty in favor of investors in the oil and gas sector. The researcher reviews literature on stabilization clauses and how they have been adopted and used in PSAs. The research puts forward recommendations on how the IOCs investments can be protected without compromising State Sovereignty.

1.8.2. Time Scope

This study focuses on data from the pre 2008 PSAs to present PSAs. This period was used because of the availability of good quality and reliable data relevant to the topic under investigation.

1.8.3. Geographical Scope.

This study is carried out in Uganda and covers data from oil producing countries that currently use or have previously included stabilisation clauses in their PSAs.

1.9. Theoretical framework.

The principal-agency theory will be used to base the study's findings and analysis. The principal-agent theory is a hypothesis that describes how a single person can act as both a principal and According to Chiappori et al the basic premise of the principal-agency theory is that the agent must have a clear understanding of the principal's wants and the ability to meet those demands competently. The principle must maintain a close watch on the agents' performance and create reward mechanisms that motivate them to achieve the desired outcomes. Indeed, when a procurement contract is well-defined and arranged, it is easy for the principal and agents to meet each other's needs quickly, resulting in prompt contract execution.

The principal-agent theory can be proudly applied to this study with a case firm or government as the principal and contractors, service providers, or suppliers as agents. Because it emphasizes the significance of solid contractual and negotiation requirements and specifications, as well as an objective process for monitoring the feasibility of oil and gas projects, the theory is relevant to the research. It will be simple for the principal and agents to satisfy each other's expectations in an efficient manner when contract requirements, team roles and responsibilities, and KPIs are clearly defined, resulting in timely contract execution at the predetermined performance level.[13]

1.10. Chapter synopsis

The research comprises of five (5) chapters which are as follows;

Chapter one

The Chapter entails the introduction, background and explanatory parts of the study highlighting the statement of the research problem, general and specific objectives, research questions, the significance and scope of the study.

Chapter two

Covers the literature review where available literature on the topic under study is reviewed in much

[13] Oluka, P &Basheka C, Determinants and constraints to effective procurement contract management in Uganda, a practitioner's perspective 2012 It is always recommended to look at the original work, because if you refer to what is said by an author in another scholar's work, you would be almost providing heresy evidence. For that reason please try to access Basheka's work.

broader detail and at this stage the researcher identifies and compares what other authors have previously discussed in relation to the topic under investigation and further assesses the legal framework that governs stabilization clauses in Uganda.

Chapter three

This is comprised of, detailing the research methods that the researcher relied on in conducting this research.

Chapter four

In here is the detailed discussion of the findings of the study taking into consideration the research observations.

Chapter five

This is the last chapter of this study that discusses the conclusions drawn from the research findings and further discusses the recommendations to the findings or research gaps.

CHAPTER TWO:

LITERATURE REVIEW

2.0. Introduction

Literature Review is a comprehensive summary of previous research on the topic under investigation. It includes a selection of data, evidence, surveys, scholarly articles and other sources relevant to the topic under research.[14]

This chapter reviews and provides a critique of the available literature on stabilization clauses in PSAs vis a-vis State sovereignty. The literature has been reviewed on the basis of the study objectives. An Analysis has been made of domestic legislation, international treaties and conventions, case law, textbooks, law journals, publications, working papers, and Internet sources. These materials have a big influence on the discussion that follows. In the review, the strength and weaknesses of the legal framework was analyzed. Also, important textbooks and articles were reviewed to obtain and contextualize scholarly opinions for the guidance of this paper. This chapter further presents the identified research gaps which the study intends to address.

2.1. Stabilization Clauses as a Concept

Stabilization provisions are incorporated in some investment agreements between foreign investors and specific states. Stabilization clauses are provisions in an investment contract that state that any future changes in the host state's law that would be harmful to the investor will not be applied to the contract in question. In this situation, the host state's and investor's interests are balanced, and the long-term contract is stable as a result of this, and it is not subject to regulatory changes.[15]

Stabilization provisions, according to *Cotula,* imply a host government's pledge not to change the regulatory framework controlling an investment contract through legislation or any other means. In this scenario, the law that governs the investment project was frozen at the moment the contract

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[14] HART, C, Doing a Literature Review: Releasing the Social Science Research Imagination. London: Sage Publications 1998.
[15] R. Dolzer and C. Schreuer, Principles of International Investment Law, New York, Oxford University Press, 2008, p.75.

was signed and will remain so for the duration of the contract. The clauses in question are intended to stabilize the terms and conditions of an investment project, thereby assisting in the risk management of that project. Stabilization provisions come in a variety of shapes and sizes, and they can prevent a state from nationalizing, expropriating, or changing the contract, among other things.[16]

Despite the above attempt to define stabilization clauses, their precise legal meaning and effect have never been fully clarified, because some scholars and practitioners argue that states' sovereignty allows them to enact or change a law whenever the circumstances require it, and that stabilization clauses only obligate the host state to compensate the foreign investor protected by the clauses if the latter is harmed by the retaliation.[17]

Though stabilization clauses are designed to protect a specific investment project throughout its life, there are several different forms of stabilization clauses, which will be discussed in the next section.

2.2.Summary of Literature reviewed

According to Thomas, Investments in the oil and gas sector are capital intensive, complex and fraught with risk. With IOCs on one hand, interested in contractual regime stability, financial predictability, and an internationally enforceable dispute resolution mechanism while on the other hand, HGs want regulatory flexibility and maximum tax benefits.[18]

The relationship between the HG and IOC is not only a commercial one but also one of mutual dependency.[19] The HG owns the natural resources while the IOCs invests the required capital, expertise and technology in the exploration, exploitation and development of the hydrocarbons.

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[16] L. Cotula, Regulatory Takings, Stabilization Clauses and Sustainable Development, a paper prepared for the OECD Global Forum on International Investment VII "Best Practices in promoting investment and development", in Paris 27-28 March 2008, available at http://www.oecd.org/investment/globalforum/40311122.pdf accessed on January 16, 2022.

[17] R. Dolzer and C. Schreuer, Principles of International Investment Law.

[18] Thomas J. Pate, 'Evaluating Stabilization Clauses in Venezuela's Strategic Association Agreements for Heavy-Crude Extraction in the Orinoco Belt: The Return of a Forgotten Contractual Risk Reduction Mechanism for the Petroleum Industry,' 40 U. Miami Inter-Am. L. Rev. 347 (2009)

[19] Thomas J. Pate, 'Evaluating Stabilization Clauses in Venezuela's Strategic Association Agreements for Heavy-Crude Extraction in the Orinoco Belt: The Return of a Forgotten Contractual Risk Reduction Mechanism for the Petroleum Industry,' 40 U. Miami Inter-Am. L. Rev. 347 (2009)

To facilitate negotiations between the IOCs and HGs, several contractual and legal techniques have been adopted in order to mitigate the risks associated with oil and gas investments such as the inclusion of stabilization clauses in PSAs in order to ensure contractual stability that deter HGsfrom changing the existing legal and regulatory framework that may affect the terms of the PSAs.

Mansour et al,[20] based on a survey of 20 nations (19 developing countries and Mexico), examine how fiscal stabilization clauses have changed since the late 1990s. Considerable changes in the oil and gas business occurred during this time, including significant price fluctuations, prompting governments around the world to examine the sector's fiscal treatment, frequently in order to collect a larger portion of the oil rent. Because fiscal stability is such an important part of developing countries' fiscal regimes, it's worth looking into whether it's been tightened or destroyed. Due to the current state of the oil market and expected price volatility, a review of the literature on fiscal stability and country experience is particularly important.

Oil GDP in the selected nations (excluding Mexico) accounts for almost 70% of oil production in low- and lower-middle-income countries (it was only a third in the early 2000s). Oil exports and government revenue from oil contribute for around 10% of GDP in these countries, with the latter accounting for about one-third of total government revenue. This implies that fiscal stabilization and its revenue impact, if any, could have considerable budgetary implications for governments and businesses.

The author addresses the primary factors that cause HGs to alter the fiscal terms they initially agreed to with investors - mostly in contracts, but also in laws that apply to everyone, such as hydrocarbon and tax laws. He also discusses the qualities and motivations for the various types of stability. Although these triggers are global, stability provisions are usually only granted in underdeveloped countries. He evaluates the effectiveness of such mechanisms by examining the experiences of various countries, and he analyses the key challenges surrounding the design and implementation of fiscal stabilization policies. He examines the findings of country reviews and

[20] Fiscal Stabilization in Oil and Gas Contracts: Evidence and Implications, Oxford Institute for Energy Studies, Paper: SP 37, [online] available at; https://www.oxfordenergy.org/wpcms/wp-content/uploads/2016/02/Fiscal-Stabilization-in-Oil-and-Gas-Contracts-SP-37.pdf (accessed on 30th January, 2022)

adds comments from a small group of industry specialists. The fifth section finishes with some policy recommendations.

Stabilization clauses according to Talal were largely a result of the unpredictable and past actions of the HGs such as nationalizing IOCs assets that had adverse effects on the interests of IOCs in the oil and gas industries.[21]

According to Chioma, the principle of *"pacta sunt servanda"* under international law is the back bone of stabilization clauses in PSAs. It is to the effect that the sanctity of a contract must be kept.[22] Chioma emphasizes that stabilization clauses play a key role in stabilizing the contractual regimes which is key in oil and gas investments especially in developing countries. The author further states that a well drafted stabilization clause provides necessary economic equilibrium necessary for the overall effectiveness of PSAs.

2.3. Defining Stabilization Clauses

There is no universally accepted definition of stabilization clauses however many authors have defined these clauses generally to mean assurances given by HGs to IOCs not to alter the contract regimes in order to ensure contractual stability.[23] IOCs want to be insulated from future legal and fiscal changes that might may negatively affect the contract.[24]

Cameron in his book asserts that the term stabilization in as far as international energy contracts are concerned, applies to all the contractual mechanisms which aim at preserving the life of the contract, the economic and legal conditions which the parties considered to be appropriate at the time of contracting.[25]

Abdullah defines stabilization clauses as those that comprise of contractual mechanisms that

[21] Talal A.Q. Al-Emadi, "Stabilisation Clauses in International Joint Venture Agreements" (2010) 3 I.E.L.R. 54.
[22] Eze Emem Chioma; "Examining the crucial impact of a well drafted stabilisation and renegotiation clause on production sharing agreements" I.E.L.R, 2015, 5,212-217
[23] Al-Emadi, "Stabilisation Clauses in International Joint Venture Agreements" 54, 55
[24] Ochieze, "Fiscal Stability: To what Extent can Flexibility Mitigate Changing Circumstances in A Petroleum Production Tax Regime" 252, 257
[25] Cameron, p., 2010. International energy investment law: The pursuit of stability. OUP catalogue.p.69

insulate petroleum contracts from change in the legal environment and are usually in the form of government guarantees providing that terms negotiated between the IOCs and HGs will not be altered or changed through promulgation of regulations or legislations.[26]

According to the author, stabilization clauses aim at preventing State legislative intervention in negotiated contract regimes by protecting foreign investors from State intervention in petroleum development projects by altering legislative and regulatory frameworks.

Ghene et al define stabilization clauses as those terms in private commercial contracts between investors and HGs whose aim is to address the issue of changes in the legal framework during the life-time of a project.[27]

The author identifies three main types of stabilization clauses namely freezing, equilibrium and hybrid clauses;

Freezing clauses prevent the applicability of new laws to an already negotiated contract, freezing the laws of the HG either in its entirety or to limited aspects of the projects. Equilibrium clauses cover the financial losses that may accrue to an investor as a result of changes in the law. While hybrid clauses are a combination of both the freezing and equilibrium clauses that also aim at protecting the stability of the contractual regime.

According to Abdulla, stabilization clauses may be comprehensive or limited in scope. It can be comprehensive if it comprises of restrictions on legislative changes by HG. A comprehensive stabilization clause completely bars a HG from making any changes in the national laws regarding the contract.[28] On the other hand, a stabilization clause is limited in scope if it is applicable to specific elements of the contract such as tax, employment, social welfare. According to the author this is most preferred stabilization clause by many oil producing countries.

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[26] Abdulla Faroque, "Validity and Efficacy of stabilization Clauses; Legal Vs Functional Value" 317-336, 2006

[27] Katja Ghene & Rumulo Brilo, "Stabilization Clauses in international investment law: Beyond balancing and fair and Equitable Treatment."

[28] Abdulla Faroque, "Validity and Efficacy of stabilization Clauses; Legal Vs Functional Value" 317-336,

Karasira, [29] Stabilization clauses are provisions in an investment contract that state that any future changes in the host state's law that would be harmful to the investor will not be applied to the contract in question. Despite the reality of stabilization clauses, governments' sovereignty allows them to enact necessary legislation that applies to all sectors and activities. In terms of economics, sovereignty allows a State to exert control over its domestic economy. Many developing countries began questioning the legitimacy of concession agreements that their governments had entered into with foreign investors in the 1950s, based on the idea of permanent sovereignty of States over their natural resources.

Even if host state sovereignty has been cited as a reason for not enforcing stabilization clauses, international investment law stipulates that the parties' agreement to an investment contract prevails, to the extent that the applicable law chosen by the parties is the one referred to by the tribunal in the event of a dispute. In a similar spirit, the notion of contract freedom permits the parties to choose the law that will govern their contract. This is why, because they deal with the law that regulates the investment contract during its life, stabilization clauses should be implemented in accordance with the principle of contract freedom.

However, a particular host state may be asked to enact legislation to comply with international commitments, particularly those connected to human rights and environmental protection. As a result, stability clauses that are concerned with providing for compensation in the event of a host state action that is averse to the investment project are advised, rather than barring a given state from managing its internal affairs through necessary and applicable laws.

2.4. Legality of Stabilization Clauses

The legality of stabilization clauses can be conceptualized in the context of their legal impact and the laws governing them. By their structuring, stabilization clauses comprise of the terms and

[29] November, Enforceability of Stabilization clauses in Oil and Gas contracts, University of Rwanda, [online] available at; http://dr.ur.ac.rw/handle/123456789/1264 (accessed on 29th January, 2022)

conditions in the contract from which parties to a contract cannot deviate and such terms are usually governed or subjected to both domestic and international investment laws.

Dolzer et al., in their text noted that the legal framework that governs international contracts between IOCs and HGs are hybrid in nature since they are comprised of both private and public law harmonizing both domestic and international laws[30].

S.W. Schill emphasized that international investment laws fall under both the public and private law domain. International investment codes establish the standards through which investors and international commercial transactions with private States/entities can be protected and treated globally and this is regardless of whether the investors are in developing or more developed economies.[31]

Stabilization clauses ensure that the equilibrium of a contract is maintained and governed by the laws that were in place at the time the contract was being entered into. Stabilization clauses are a creature of international law since they are usually used in international commercial contracts that involve different States or companies from different jurisdictions.

In the context, stabilization clauses are a creature of international law and are governed by both domestic and international laws. This is the reason why parties to international commercial contracts such as the PSAs usually choose a mutually agreed legal regime that shall be applicable during the dispute resolution process.

2.5. Purpose of stabilization Clauses

There are several contractual agreements in place via which parties invest in oil reserves. Concession agreements, service contracts, and production sharing contracts are the most common approaches. The necessity to safeguard foreign investors from the risks of the business is a

[30] R. Dolzer and C. Schreuer," Principles of International Investment Law," New York, Oxford University Press, 2008, p.3.
[31] S.W. Schill, "International Investment Law and Comparative Public Law," Oxford, Oxford University Press, 2010, p. 836.

fundamental problem in petroleum contracts. This raises the question of whether including stabilization clauses in a business agreement to freeze the parties' rights and obligations is legitimate and does not infringe on the host state's sovereignty.

The State accepts that existing and future laws will not affect the contractual terms agreed upon with the investor, preserving contract sanctity by protecting the investor from unaccepted actions by the HG. The main goal of stabilization and adaptation clauses is to maintain the initial contractual terms and conditions as previously signed by both parties. Aléa de la souveraineté is the French term for this provision that safeguards the investor. The contract's primary law is unquestionably the law in effect at the time the contract was signed, prohibiting the adoption of new laws to control the transaction.

However, before a petroleum agreement's stabilization clause can be implemented, the host State must accept the provision's terms. Acceptance indicates that it has relinquished its power to unilaterally change the management on which investors rely. According to recent research, most host States view stabilization clauses as a way to recruit investors and provide a conducive environment for them to invest in petroleum exploitation and exploration, and they accept stabilization as a way to ensure the investors' loyalty.

The host State in underdeveloped countries claims that the agreement is governed by their national law because it concerns the concept of State sovereignty. As a result, if a stabilization clause in an international petroleum deal is governed by national law, it will be ruled null and void. In the event that a breach of contractual terms containing a stabilization clause is discovered, an arbitral award may order the State to stop enforcing the new laws.

The purpose of many international petroleum agreement is to give the host country access to expertise and technology that they can’t afford. Investors rely on stabilization clauses to guarantee investment stability to ensure a thriving performance of their investment. Because a stability clause is included in an agreement to prevent the host State from making unnecessary changes to its laws and legislation, disagreements are inevitable. When a disagreement arises between an investor and a host State, the choice of law to manage the issue in relation to stabilization provisions is critical.

When a dispute arises in a concession agreement, the appropriate law to govern the transaction is usually the host State's domestic law. As a result, when such a contract contains a stabilization clause, it is now considered to be governed by international law rather than the laws of the Host state. This topic has sparked a slew of disagreements between rich and developing nations all over the world.

Developing countries usually include a stabilization clause in their agreements because of their alleged lack of bargaining strength at the time the deal was reached. For example, developing countries like Ghana will go to any length to entice multinational oil companies to participate in the exploitation and exploration of their freshly discovered oil resource. Because of their inferior negotiating position, the host State is flexible in distributing rights to foreign investors and is willing to accept any terms inserted by the investor due to their desire and desperation to find how much reserve exists within their territory.

Since the host State's lack of experience and capital, international investors have the most bargaining power during the exploration stage. At this point, foreign investors would ensure that they had the majority of the decision-making power in relation to exploration, including decisions about well site, depth, and target zones of exploratory wells, as well as the exploration budget. After exploration is completed, the host State's authority grows stronger, which may lead them to either offer licenses to foreign investors, as in the case of the United Kingdom, or to engage in the exploitation of the resources by sharing costs.

i. Insulation from political risk

Stabilization clauses protect IOCs from political risks in HGs. Political risks are many but majorly IOCs protect themselves from changes in government in HGs which may result in the direct taking, such as expropriation or nationalization or indirect taking of property of IOCs.[32]

Bertrand states that stabilization clauses aim at stabilizing PSAs by neutralizing the effect of

[32] Oscar Schachter, International Law in Theory and Practice 314 (1991); S.K. Chatterjee, The stabilization Clause Myth in Investment Agreements, 5 J. Int’l Arb. 97–111 (1988);

prerogatives of the HGs that would otherwise allow it to unilaterally modify the legal regime of such agreements.[33]

ii. Encouragement of Investment

One of the reasons why stabilization clauses have been accepted by developing countries is to encourage investment. Whereas on one hand they play a protection function for the IOCs, their investment promotional function is clear to the HGs. They give confidence to IOCs from the commencement of investment.[34]

iii. Others

Deloitte, (2014),[35] International oil firms are concerned about the possibility of modifications to the fiscal terms of petroleum agreements signed with the host country, which could jeopardize the exploration and exploitation project's commercial viability. Despite objections that stabilization provisions limit their sovereign legislative power and permanent control over natural resources, governments in developing countries have agreed to add stabilization terms in their petroleum deals in response to investor requests. These clauses serve as a deterrent to unilateral host revision of the initial contract conditions through legislative or administrative action, at least in theory. The importance of stabilization provisions to foreign investors, the host State, and other stakeholders in the petroleum industry is discussed in this study.

The purpose of including stabilization clauses is to reaffirm the host State's conviction in the sanctity of contracts and to provide assurance that budgetary commitments made under investment agreements will outlast the administration that welcomed the enterprise and last for the duration of the project. Despite claims that this encumbers their sovereign legislative power as well as the permanence of sovereignty over natural resources, host States (mainly developing nations) are frequently agreeable to these requests.

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[33] Bertrand Montembault, 'The Stabilisation of State Contracts Using the Example of Oil Contracts: A Return of the Gods of Olympia', 6 Int'l Bus. L.J. 593, 599 (2003).
[34] Abdulla Faroque, "Validity and Efficacy of stabilization Clauses; Legal Vs Functional Value" 317-336, 2006
[35] Stabilisation Clauses in International Petroleum Contracts Illusion or safeguard?, [online] available at; https://www2.deloitte.com/content/dam/Deloitte/ug/Documents/tax/tax_StabilisationClauses_2014.pdf (accessed on 29th January, 2022)

As a result, the value, if any, that stabilising clauses bestow to various stakeholders in petroleum exploitation investment partnerships is examined in this article. It also describes the scope and character of their work. It also suggests that a stabilization provision may not always be the solution for investors seeking stability in long-term energy investment operations.

2.6. Types of Stabilization Clauses

Different types of stabilization clauses are a result of the negotiation and bargaining process between the IOC and HGs. These clause can be divided into three broad categories namely; intangible clauses, stabilization clauses in the strict sense and economic stabilization clauses as discussed below;

A. Stabilization clause stricto sensu (Freezing clause)

A freezing clause is a form of stabilizing provision in which the host country pledges not to enact legislation or make regulatory changes that would harm the agreement throughout the contract's lifespan. The freezing clause is the most common clause included in petroleum contracts, despite the fact that some practitioners believe it is obsolete. According to an AIPN survey, freezing clauses are featured in most oil and gas contracts. It's called a freezing clause because it prevents the host state from enforcing new legislation relevant to the investment's already agreed-upon rules. The applicable law under a freezing clause is the law in effect at the time the contract was signed, rather than any subsequent legislation. The freezing clause is separated into two types.

There are two types of freezing clauses: full freezing and limited freezing. Full freezing clauses apply to both fiscal and non-fiscal matters, whereas limited freezing clauses apply to a specific set of legislative measures. The limited freezing provision, for example, could exclusively pertain to taxation difficulties. Informally, full and limited freezing clauses are occasionally used to protect investors from having to comply with new social and fiscal regulations or accepting damages from the government for the expense of compliance.

If a stability clause in a contract is a full freeze clause, the IOC will be exempt from any new social or environmental legislation enacted after the contract is signed. For example, the IOC may be

exempt from a law imposed to raise the minimum wage or taxation, among other things. As a result, the IOC might exploit the freeze clause to avoid having to comply with the new law's terms. Also, if there is a limited freezing provision, the terms provided in the clause will determine whether the IOC can utilize it to avoid the new law's implementation. In some cases, full freezing clauses are introduced to reduce the effectiveness of new laws. The reason for this is that they allow the corporation to rely on it to avoid having to apply the new laws.

The freezing provision in international petroleum agreements allows investors to address their rights and obligations under the Foreign Investment Contract (FIC) with the government. The clause allows the corporation to continue to rely on the argument that newly adopted legislation is not binding on it. The freeze clause would amount to compensation from the host state to the international oil firm if the host state enacts new legislation that affects the contractual arrangements between it and the international oil company. As a result, the host country would compensate the IOC in order for them to comply with the new legislation

This kind of stabilization clause aims at maintaining the legislative status quo over the life time of a project. According to Abdulla, this is a comprehensive stabilization clause which blocks the legislative competences of HGs and may take the following forms;

i. A stabilization clause that freezes the municipal and national laws of the HG for the whole period of the contract. This is to the effect that the HG cannot amend the existing laws that may adversely affect the management and control of the contract and even subsequent laws cannot be applied to the contract.

ii. The other form is the clause that provides for inconsistences in the legislation and the provisions of the PSA and are to the effect that in case of conflicts between the new legislation and the contractual provisions, the stabilization clause prevails.

Thus, this kind of stabilization clause does not erode state sovereignty to legislate; it only implies that subsequent legislation will not apply to the contract.

B. Intangible clause

These clauses prohibit unilateral changes to a PSA.[36] According to Farouq, intangible clauses are to the effect that a contract cannot be modified or rescinded except by the mutual consent of the parties to the contract.[37] Therefore a HG cannot unilaterally modify or terminate PSA.[38]
These clauses do not contain an explicit waiver of legislative sovereignty but rather seek to prevent unilateral modifications of contract by the HG.

Such clauses are more consensual in nature, because the mutual consent of the parties is required in order to change the contractual obligations. The main difference between the stabilization clause *stricto sensu* and an intangible clause is that the former intends to protect IOCs from HG legislative intervention in the contract through changes in the applicable law or the enactment of new legislation while the latter aims to protect IOCs from the HG's exercise of administrative power to modify or change the contract one-sidedly. A stabilization clause *stricto sensu* limits the legislative competence of the State, whereas an intangible clause shields the IOC against the excessive powers of the HG acting as public authority to change the contract terms.[39]

The requirement of mutual consent for modification of contractual provisions may also be implied where the contract in question is silent.[40] In such cases, a party's consent may be deemed to be given by subsequent conduct acquiescing in unilateral actions by the other party that have the effect of altering the contract terms.

C. Economic stabilization or equilibrium clause

The economic equilibrium clause, like the freezing clause, can be separated into two categories:

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[36] Deloitte & Touche; 'Stabilisation Clauses in International Petroleum Contracts Illusion or safeguard?' April, 2014

[37] Abdulla Faroque, "Validity and Efficacy of stabilization Clauses; Legal vs Functional Value" 317-336, 2006
[38] Eze Emem Chioma; "Examining the crucial impact of a well drafted stabilisation and renegotiation clause on production sharing agreements" I.E.L.R, 2015, 5,212-217
[39] P. Weil, 'Les clauses de stabilisation ou d'intangibilité insérées dans les accords de développement économique, in MELANGES OFERTS A CHARLES ROUSSEAU' 301–44 (1974), translated and cited in A.Z. El Chiati, 'Protection of Investment in the Context of Petroleum Agreement,' 204 RECUEIL DES COURS 115 (1987).
[40] A.F.M. Maniruzzaman, 'Some Reflections on Stabilization Techniques in International Petroleum, Gas and Mineral
Agreements,' Int'l Energy L. & Taxation Rev. 96, 98 (April 2005).

full economic equilibrium and limited economic equilibrium.

The term "full economic equilibrium clause" refers to terms that protect against the financial impact of a change in law on the contract, which would eventually result in reimbursement from the HG. “Limited economic equilibrium clauses” on the other hand are those that impose some restrictions on the application of the economic equilibrium clause included into the contract. For example, the condition stipulates that the IOC must suffer a certain amount of financial damage before receiving compensation. As a result, regulatory adjustments are possible under the economic equilibrium clause as long as attempts are taken to restore economic equilibrium.

It should also be noted that several economic equilibrium clauses include recommendations for determining whether or not economic equilibrium has been harmed. In comparison to other forms of stabilization clauses, research has revealed that the utilization of economic equilibrium clauses has improved. In certain nations, however, the terms "economic equilibrium" and "freeze clause" are used interchangeably in the same contract.

This kind of stabilization clause bars HGs from enacting legislation or taking any administrative measures which may in turn increase the costs of the project and can sometimes require HGs to compensate IOCs if subsequent legislation or modifications in the law adversely affects or causes economic loss to the IOCs.[41]

The economic stabilization clauses are increasingly being incorporated in petroleum laws or codes, investment laws and petroleum contracts. In relation to state sovereignty, economic stabilization clauses do not prevent States from exercising their sovereign powers of enacting new laws or making modifications to the existing laws however they try to mitigate the adverse impacts on the economic equilibrium of a contract which may arise out of such changes in the law.

D. Hybrid Clause

As the name implies, a hybrid clause combines the features of both a freezing clause and an economic equilibrium clause. This form of stabilizing clause mandates the host state to return the IOC to its previous position before to the legislative change. Hybrid clauses, like the other two

[41] Abdulla Faroque, “Validity and Efficacy of stabilization Clauses; Legal Vs Functional Value” 317-336, 2006

types of stabilization clauses, are divided into two groups. There are two types of hybrid clauses: complete hybrid and limited hybrid. A full hybrid clause protects investors against financial consequences of a change of legislation by requiring compensation, whereas a restricted hybrid clause protects investors from financial consequences of a limited change of law.

2.7. Classification of provisions of stabilization Clauses

According to Thomas, drafters of PSAs and other contractual arrangements can choose to use different types of stabilization clauses.

Stabilization clauses were initially freezing in nature but over time they have been modified due to a number of reasons which include incompatibility with HGs legal frameworks, increased capacity of HGs thus increasing their bargaining powers, increased awareness of HGs in a far as regulation is concerned. Due to these considerations, provisions on stabilization clauses have are more flexible maintaining both the unilateral actions of States and the economic equilibrium of the contract

The different types of stabilization provisions can be categorized into four groups as seen below;

The Classic Freezing Clauses	Provides for the greatest investor protection, stipulating that the laws and regulations applicable to the agreement are those in force at the time of the execution of the agreement.
Stipulated Economic Balancing	Implies that the contract terms are to remain in effect but with a clear stipulation that new laws will nevertheless apply to the IOC; however, if the new laws affect the stabilization provision, the agreement is to be automatically amended, in principle without negotiation, so that the economic balance between the parties will be restored.
Non-specified Economic Balancing,	Provides that any new law will be applicable to the IOC but that if a new law affects the stabilization provision, the agreement will be automatically amended so that the economic balance between the parties will be restored; however in this case the provision only stipulates that the amendment is to result from mutual agreement without specifying the nature of the amendment.
Negotiated Economic Balancing	Provides for the weakest form of stability for the IOC, indicating that any new laws will apply to the IOC and that the agreement will be automatically amended to reflect such new laws, but that such amendments are to stem from new negotiations between the parties with the goal, but not the assurance, of restoring the economic balance between the parties

The potential impact of stabilization clause

The purpose of a petroleum contract's stability clause is to safeguard the foreign investor from domestic laws interfering with foreign investment contracts (FIC). In the event that a State violates the stability clause, it will be held accountable for damages and compensation. As explained in the preceding chapter, the stabilization clause effectively prevents a sovereign State from modifying its rules and legislation if it would influence the rights and obligations of an international oil corporation exploring or exploiting a host State's oil field. In other words, by agreeing to a stabilization provision, the State has given up the ability to unilaterally change the terms of the contract that were agreed upon at the outset.

When analyzing the influence of the stabilization clause and how it impacts IOCs, it's important

to understand how this clause affects them and what laws control this contract. International law is usually the appropriate law in a contractual connection between a foreign country and a host State in a petroleum transaction.

The reasoning behind this is that international law provides more protection for foreign investment than the host country's laws. The contract is governed by international law, which ensures the contract's firmness throughout the project's duration. Although recent research suggests that a host State may raise an objection relating to inalienable sovereign rights before an international arbitrator in order to avoid the stabilization clause's impact. Once a host State has signed and ratified a contract that includes a stability provision, it is bound by it and cannot enact new legislation to manage the deal unless the multinational oil firm agrees.

Validity and effects

Stabilization clauses are recognized in international law, as is a State's right to bind itself to their enforcement. "Nothing may preclude a State in the exercise of its sovereignty from committing itself definitively by the issue of the concession and from granting to the concessionaire rights," according to the tribunal in the case of *Texaco vs Libyan Arab Republic.*[42]

IOCs should however be very clear in what they intend to stabilize when accepting the terms of a stabilization clause, and stabilization clauses should expressly state that their terms are binding regardless of future amendments or negotiations of the IOCs unless both parties mutually agree in writing to change the rules if the aforementioned stabilization clause. The major question that arises, regardless of how plain the term of stabilization provisions is, is how effective these clauses are. The argument between industrialized countries emphasizing the purity of contracts based on the theory of *'pacta sunt servanda'* has remained for many years, making this subject difficult to address. There's also the debate about emerging countries asserting sovereignty over natural resources and relying on the 'rebus sic stantibus' concept. I would briefly want to discuss these principles based on the success of petroleum agreements' stabilizing clauses.

[42] ILM, 1978, at 1 et seq.; Int'I l. Rep. 1979, at 389 et seq

The Doctrine of Pacta Sunt Servanda.

The doctrine of pacta sunt servanda, which implies that any contract entered into by two consenting parties will be directed in good faith, despite some discrepancies in definitions supplied by various authorities. In international conventional law, the notion of pacta sunt servanda can also be found. According to Article 26 of the Vienna Convention on the Law of Treaties:

"Every treaty now in existence binds the parties to it and must be carried out in good faith."

According to Anzilotti, the idea of pacta sunt servanda is the most extreme suggestion of using the international legal system.

The doctrine of rebus sic stantibus

Simply put, this ideology establishes permanent sovereignty over natural resources. In modern international law, this principle is regarded as fundamental. The problem of natural resource sovereignty arises in the context of a host State's cooperation with foreign oil firms in the exploration and exploitation of natural resources on the State's territory. The HG has an inherent and unalienable right to amend the law in its territory. This principle applies to stabilization and adaptation clauses and has acquired a lot of traction in recent years.

The assessment of the effectiveness and effects of stabilization clauses in petroleum agreements is framed by the two basic theories outlined above. This raises important problems such as, 'Does the State's ability to pass legislation be limited by the stability clause?' 'Do they make the contract's terms unchallengeable?' This challenge has persisted in both developed and developing countries that produce oil. The argument, in my opinion, can go both ways. Stabilization provisions, on the other hand, do not prevent the host State from enforcing new legislation because the State is a sovereign body, nor do they make the contract terms unchangeable because both parties can agree to amend particular contract terms at any moment throughout the contract's life. On the other hand, such a clause ties the host State's hands because, although being a sovereign State, it is unable to implement new legislation without first considering the interests of foreign investors and receiving their agreement.

According to Emeka (2008)[43] high gas prices, as seen recently, signal a rejection of international petroleum contracts as host governments demand a larger part of profits based on a variety of reasonable and flimsy assumptions, raising questions about the efficacy of stabilizing clauses in such agreements. Stabilization provisions were added to international petroleum contracts to limit political risk and protect the fiscal framework. While practitioners and clients benefit from stabilization clauses based on international arbitration precedents, this article points out that such comfort may be misplaced in the absence of the necessary international anchor, which may be lacking in international petroleum, and thus emphasizes the need for such anchor, as well as drafting, client management, and litigation considerations for practitioners.

According to Teacher Law, (2013)[44] Due to a lack of experience and capital, oil-producing countries enter into investment contracts with international investors to raise the level of production of their oil fields. Foreign investors are particularly cautious about investing due to the nature of petroleum agreements, the risk involved, and the amount of capital required to carry out exploration and development of a particular oil field. The degree of stability is significant to foreign investors because the less stable a project appears to be, the less likely an investor is to sign a long-term contract with it. In order to entice foreign investors, host countries have recently included stabilizing clauses. There is a strong link between investment stability and equity. The purpose of a stabilization clause is to enhance the legal connection between the host country and foreign investors.

Finally, the authors look at the function of international arbitration in addressing conflicts originating from stabilization clauses, as well as the use of renegotiation to resolve limits imposed by this so-called "freeze clause" present in most petroleum agreements. This would include, in part, the responsibility of International Court for Settlement of International Disputes (ICSID) in resolving disputes resulting from contract renegotiations.

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[43] Anchoring Stabilization Clauses in International Petroleum Contracts. The International Lawyer, 42(4), 1317–1338. http://www.jstor.org/stable/40708046

[44] Impact of Stabilization Clause on Petroleum Agreements. Retrieved from https://www.lawteacher.net/free-law-essays/commercial-law/impact-of-stabilization-clause-on-petroluem-agreements-commercial-law-essay.php?vref=1

Cameron (2006),[45] focuses on contract stabilization procedures in the worldwide oil and gas industry. It focuses on the stabilization clauses that are frequently included in oil contracts between HGs and IOCs.

The first section of the study looks at the context in which stability difficulties occur, as well as the numerous explanations sometimes out by host governments for modifying the regulations.

The second section looks at stability tactics and how they are enforced, noting that the traditional stabilisation clause amounted to an attempt to 'freeze' the terms and conditions for the duration of the contract, whereas the modern approach allows for negotiation between the parties. A review of legal precedent reveals a number of published awards that are directly relevant to disputes over the first type of stabilisation; however, guidance on the second type of stabilisation is currently limited to cases that are primarily concerned with related issues such as indirect expropriation. This section focuses on topics that are mostly related to financial commitments.

The third section focuses on contract stability in non-financial sectors, with a particular emphasis on the risks of instability to IOCs coming from unilateral changes in areas that are frequently expressly excluded from petroleum contract stabilization clauses.

According to IFC, 2009[46] the goal of stabilization clauses in Oil and gas contracts is to impact on a State's ability to carry out its international human rights duties. The said paper looked into whether stability clauses can be used to limit the application of new social and environmental rules on investment activities over the life of the investment or to get compensationfrom host countries for the expenses of complying with such new laws. Because social and environmental laws (labour and employment, non-discrimination, health and safety, environment,and protection of culturally significant property) are some of the more easily identifiable legislativeareas that can both protect rights and impact investors, this study used them as a surrogate for human rights obligations.

[45] Stabilisation in Investment Contracts and Changes of Rules in Host Countries: Tools for Oil & Gas Investors, Association of International Petroleum Negotiators, [online] available at; https://www.international-arbitration-attorney.com/wp-content/uploads/arbitrationlaw4-Stabilisation-Paper.pdf (accessed on 24th January, 2022)

[46] Stabilization Clauses and Human Rights, [online] available at; https://www.ifc.org/wps/wcm/connect/0883d81a-e00a-4551-b2b9-46641e5a9bba/Stabilization%2BPaper.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-0883d81a-e00a-4551-b2b9-46641e5a9bba-jqeww2e (accessed on 27th January, 2022)

The contract data used in this study comes from a sample of actual and model investment contracts. (The contracts are actual agreements between government and investor parties.) The models are intended to serve as a starting point for government negotiations, although they may vary dramatically before final agreements are reached.) These contracts and models were mostly developed by private international law firms in response to an invitation from the IFC to participate in the study. These legal firms supplied a sample of contracts from the last ten years, representing a wide range of sectors and geographical locations. A literature analysis on stability clauses and relevant international arbitration decisions was conducted for this project, as were interviews with lawyers who represent investors and host states (negotiating investment contracts or litigating contract disputes), as well as industry lawyers. For this study, no interviews with government officials were undertaken. Interviews were conducted with academics who have worked on host-government agreement negotiations and with nongovernmental organizations (NGOs) that have studied host-government agreements and human rights. The focus of the study was on the writing of stabilization provisions, with only a brief mention of their formal enforcement.

The majority of the stabilization clauses analyzed were structured in a way that can either shelter investors from having to adopt new environmental and social laws or offer investors with an option to be reimbursed for compliance with such laws, according to this study. None of the OECD contracts in the study provide exemptions from new regulations, and they only seldom provide remuneration for compliance with the same breadth of social and environmental legislation as non-OECD countries.

It is important to note that as a result of shifting attitudes toward environmental issues, a new set of risks for investors in the petroleum sector has emerged. This is reflected to some extent in the body of international law that is growing to address such concerns, as well as in the conditions of petroleum contracts during the last 10-15 years.

However, in order to give investors with the long-term stability they desire, established definitions of standards such as Good Oilfield Practice must be revisited. Efforts should be taken, in particular,

to build an industry-wide code that host governments may refer to in future agreements and enforce.

Companies and host governments will need to recognize the balance between flexibility and assurance in establishing provisions, and a benchmarking approach to the formulation of industry standards appears to capture that balance.

2.8. Principle of State sovereignty

According to Bellina et al, State sovereignty refers to the political position of a State as the highest authority within a territory. The extent of a State's authority is defined by its boundaries which delimit its jurisdiction from that of other States.[47] State sovereignty is seen as the ability of a State to represent its people or citizens in order to achieve and promote common interests as a whole. State power emanates from society and State sovereignty is the institutional expression of the ultimate sovereignty of the people.[48]

The principle of State sovereignty applies to all sectors and activities of a country and thus a country has power to exercise its sovereign powers in enacting or amending national laws and adopting such policies that benefit its people.

The argument is that stabilization clauses limit State sovereignty and restrain its legislative powers which shifts balance of bargaining power to IOCs or private entities. Stabilization clause reduces HGs' legislative sovereignty which may in turn be detrimental to the protection of the environment, workers' rights, and democracy and are a hindrance to development.

According to Muttitt; stabilization clauses are patronizing in that they envisage the political risk on the IOCs rather than the HGs. IOCs presume that political risks may arise thus justifying the

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[47] Séverine Bellina, Dominique Darbon, Stein Sundstøl, Ole Sending. 'The Legitimacy of the State in Fragile Situations.' [Research Report] Organisation for Economic Coopération and Development DAC;development and aid committee. 2009. halshs-02422968

[48] Séverine Bellina, Dominique Darbon, Stein Sundstøl, Ole Sending. 'The Legitimacy of the State in Fragile Situations.' [Research Report] Organisation for Economic Coopération and Development DAC;development and aid committee. 2009. halshs-02422968

need for the inclusion of stabilization clauses in PSAs and according to him, this is *"investment colonialism at its most extreme"* because stabilization clauses tie the HGs capability to make new laws which may hinder developments or advancements in the sector.[49]

However authors like Abdullah argue that stabilization clauses cannot be declared invalid on the basis of State sovereignty. He asserts that the principle of State sovereignty has been abandoned by the UN general Assembly on permanent sovereignty over natural resources, the Charter on Economic Rights and Duties of the States because neither of the resolutions of these bodies suggests that a State, in the exercise of its sovereignty, may abandon contractual commitments undertaken voluntarily and instead the resolutions require that they observe foreign investment agreements entered into for the purpose of developing natural resources.
The author affirms that stabilization clauses in a negotiated contract should be seen as a self-imposed limitation on the sovereignty of States.

On the other hand according to Thomas[50], all stabilization clauses with a freezing nature are invalid under international law. He further states that sovereignty over natural resources has assumed a character of *jus cogens* a customary norm from which no derogation is permitted.[51] This position was largely discussed at the General Assembly of the United Nations that passed Resolution 3171 that gave States the right to expropriate as an expression of their sovereignty in order to safeguard natural resources.

Gehne et al assert that Legal arguments should resolve around the extent to which stabilization clauses would deal with the sovereignty of the HGs. The author cited the case of Texaco v. Libya,[52] where it was held that stabilization clauses limit the host State's sovereignty because the HG committed to waiving its sovereignty. Further in the case of *LETCO v. Liberia* (ICSID),[53] the

[49] Greg Muttitt, 'Nationalising Risk, Privatising Reward', International Journal of Contemporary Iraq Studies, September 2007.
[50] Thomas J. Pate, 'Evaluating Stabilization Clauses in Venezuela's Strategic Association Agreements for Heavy-Crude Extraction in the Orinoco Belt: The Return of a Forgotten Contractual Risk Reduction Mechanism for the Petroleum Industry,' 40 U. Miami Inter-Am. L. Rev. 347 (2009)
[51] Ian Brownlie, 'Principles of Public International Law,' 489 (6th ed. 2003).
[52] 17 ILM 1978, p. 1
[53] 26 ILM 666-7

tribunal held that the major rationale of stabilization clauses is to protect against arbitrary actions of HG and can therefore not totally impair the sovereign power of states.

2.8.1. Sovereignty of States as a major threat to Stabilization Clauses

Sovereignty has been deemed a peremptory principle under international law, according to K. Hossain (jus cogens). In this regard, there are no exceptions to the law of sovereignty.[54] That standard is explained in the sub-sections below in relation to stabilizing clauses.

Sovereignty of States in general

In general, national sovereignty refers to the absence of external interference in a State's internal affairs. It is an international law principle that "nothing contained in the present Charter shall authorize the United Nations to intervene in matters which are essentially within the domestic jurisdiction of any State, or shall require the Members to submit such matters to settlement under the present Charter," as stated in the UN Charter.[55]

Thus, in essence, a State's internal affairs are solely under the control of the concerned government, as other States and international organizations are banned from interfering.

2.8.2. Principle of Permanent Sovereignty of States over their Natural Resources

States' sovereignty is unrestricted and so applies to all sectors and activities. In terms of economics, sovereignty allows a State to exert control over its domestic economy. In this context, the notion of permanent sovereignty of States over their natural resources has existed since 1952, and it was regarded as a right to development for colonized countries because their economic activities were controlled by foreign firms.[56]

Many developing countries were able to contest the validity of concession agreements that their governments had entered into with foreign investors or that were imposed during colonization for

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[54] K. Hossain, 'The Concept of Jus Cogens and the Obligation Under The U.N. Charter' (2005) 3:1 Santa Clara Journal of International Law, at 89, available at https://digitalcommons.law.scu.edu/cgi/viewcontent.cgi?article=1011&context=scujil accessed on January 16, 2022.

[55] Charter of the United Nations, art.2 (7), available at https://treaties.un.org/doc/publication/ctc/uncharter.pdf accessed on January 19, 2022.

[56] N.Q.Dinh, Droit International Public, 6th Ed, Paris, L.G.D.J, 1999, pp.996-997.

the exploration and exploitation of natural resources during the decolonization period, according to R. Pereira and O. Gough. The main justification in support of the concession agreements' contention was that they tended to be substantially one-sided, as developing countries saw them as heavily favouring the interests of the concerned international investors.[57]

The UN General Assembly Resolution on Permanent Sovereignty over Natural Resources (RPSNR) was enacted on December 14th, 1962, in an effort to strengthen the sovereignty of newly independent and other developing states, as well as to safeguard the advantages of natural resource development.[58]The RPSNR acknowledged the host State's power to nationalize and expropriate the foreign investor's property if sufficient compensation is made. In addition, each country has the right to create its own economic system and exercise sovereignty over natural resources, according to the Resolution.[59]

The UN General Assembly established the Charter of Economic Rights and Duties of States in 1974, in addition to the Resolution on Permanent Sovereignty over Natural Resources (RPSNR). This charter declares that each State is free to exercise full permanent sovereignty over all of its riches, natural resources, and economic activities, including possession, use, and disposal. It also provides that each State has the right to regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its own laws and regulations, as well as its own national objectives and priorities, and that no State can be forced to give foreign investment preferential treatment.[60]

In article 2, paragraph 2, of the UN Charter of Economic Rights and Duties of States, each State

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[57] R. Pereira and O. Gough, 'Permanent Sovereignty over Natural Resources in the 21st Century: Natural Resource Governance and the Right to Self-determination of Indigenous Peoples under International Law' (2013) 14, Melbourne Journal of International Law, at 455-456, available at http://classic.austlii.edu.au/au/journals/MelbJIL/2013/15.pdf accessed on January 19, 2022.

[58] Preamble of the General Assembly resolution 1803 (XVII) of 14 December 1962, "Permanent sovereignty over natural resources" available at https://www.ohchr.org/EN/ProfessionalInterest/Pages/NaturalResources.aspx accessed on January 26, 2022.

[59] Declaration of General Assembly through Resolution on Permanent Sovereignty over Natural Resources, available at https://www.ohchr.org/EN/ProfessionalInterest/Pages/NaturalResources.aspx accessed on January 26, 2022.

[60] UN Charter of Economic Rights and Duties of States, art.2 (1), available at https://www.aaas.org/sites/default/files/SRHRL/PDF/IHRDArticle15/Charter_of_Economic_Rights_and_Duties-_of_States_Eng.pdf accessed on January 19, 2022.

has the right to regulate and supervise the activities of transnational corporations within its national jurisdiction, and to take measures to ensure that such activities comply with its laws, rules, and regulations, as well as its economic and social policies. It further provides that multinational firms are not allowed to interfere in a host country's internal affairs, and that in the event of a compensation disagreement, the host country's domestic law will apply.

While stabilization clauses seek to ensure that newly elected laws are not incorporated into investment contracts, the principle of sovereignty and the aforementioned legal instruments assert that the concerned host States have the authority to enact the necessary legislation whenever they see fit, and that these States should not be subjected to multinational company interference.
The concerned host States, in particular, have the right to regulate and supervise transnational corporations' activities within their national jurisdictions and to take measures to ensure that those activities comply with their laws, rules, and regulations; and to freely exercise full permanent sovereignty over all of their wealth and natural resources, including possession, use, and disposal. They also have the authority to nationalize and expropriate the foreign investor's assets.
The aforementioned host governments' prerogatives of making laws, ensuring their enforcement, regulating and overseeing transnational firms, and the access to the countries' national resources are clearly detrimental to the main objective of stabilizing clauses.

A number of countries still provide for stability in the form of ‘freezing’ obligations in the contract. However, given the high risk of unilateral action at some future date this is in itself a highly unreliable mechanism. Perhaps in recognition of this, the long-term trend has unmistakably been one in which economic balancing has been favored, often involving negotiations between the parties about the result.

The risks of unilateral action by HGs are as real today as they have always been, and they are evident in a wide variety of governments. As a result, the inclusion of a stabilizing clause provides the possibility of additional security. However, an over-eager desire on the side of host governments to provide such assurance may stem more from an investment promotion policy than a clear understanding of the commitment made. Investors would be prudent to exercise extra caution when designing procedures that could be used in enforcement at a later date.

The host government has a wide range of tools at their disposal for enacting unilateral actions. Other mechanisms derived from the petroleum law regime will almost always provide the government with opportunities to persuade the investor of its position or reach a compromise agreement.

The dangers of unilateral action to the host government (such as damage to its reputation as an investment destination) provide potential remedies. The ability to negotiate about the differences that lead to a planned unilateral action should be aided by an understanding of the potential implications.[61]

An open-ended approach to negotiated economic balancing however is also a high risk strategy. It should be complemented by details and penalties for noncompliance: imposition of time limits on negotiations, recognition that compensation must follow a loss or damage and recourse to arbitration if the negotiations fail.

In a number of cases the NOC will play a central role in fiscal stabilisation. It may provide for adjustment by paying any additional taxes out of its share of profit petroleum or royalty under a PSA or it may reimburse the IOC directly out of general revenues. Under a rate of return system, the NOC could pay from its share of royalty and/or excess profits tax. However, the NOC share of production may prove insufficient or it may be pre-sold.

The object of an economic balancing provision is not to address an act of expropriation by the HG but other approaches to stabilisation do take this into account. A more difficult area is the impact of an act of ‘creeping expropriation’.

States can revise contracts unilaterally. The real issue in designing the appropriate stabilisation mechanisms is not so much whether the host government can unilaterally change the contractual relationship but rather what is the result of such legislative action for the investor in terms of lump sum damages or possible specific performance of stabilisation mechanisms.

[61] M Mansour & C Nakhle, January 2016. Fiscal Stabilization in Oil and Gas Contracts: Evidence and Implications, Oxford Institute for Energy Studies.

The growing interest in cross-border pipeline projects is generating new approaches to stabilisation involving a more complex set of legal arrangements. It is too early to say whether such arrangements are as effective as they are innovative in their approaches to fiscal stability.

The major findings of this chapter show that stabilization clauses are intended to protect investment projects by addressing investment risks that may arise as a result of a change in the legal framework. The biggest challenge appears to be State sovereignty, since it obligates nations to implement necessary legislation in the public good, particularly in terms of existing and developing international norms and standards in the social and environmental fields. Overall, what matters is how stabilization clauses are interpreted. When it comes to interpreting stabilizing clauses in light of relevant law, good faith is regarded the best tool for avoiding unfair advantages.

2.9. The Oil contracting system in Uganda

2.9.0. Production Sharing Agreements (PSAs)

A PSA is a legal contract between one or more investors and any governmental entities to lay out the rights, duties, and obligations of each party for exploration, development, and production of mineral resources in a specific location for a specific time.[62] Of all the legal contracts in the oil and gas industry, a PSA is one of the most significant. It is used as an instrument by all parties to realize a quick return on their investments and increase revenue as much as possible while sharing out the risks.[63]

Typically, the agreement is between the HG, where the minerals are located, and the parties who wish to drill and operate in that country, these parties are usually IOCs. The contract regulates the percentage of oil and gas production that each party receives after the recovery of a specific amount of cost and expense by all parties.

The HG licenses the execution of exploration and production activities to an IOC. The IOC bears the mineral and financial risk of the initiative and explores, develops and ultimately produces the

[62] CourtHouseDirect.com Team, November 2019, What is a production sharing agreement? [online] available at; https://info.courthousedirect.com/blog/what-is-a-production-sharing-agreement (accessed on 25th June, 2021)
[63] Ibid

field as required.[64] When successful, the company is permitted to use the money from produced oil to recover capital and operational expenditures, known as "cost oil". The remaining money is known as "profit oil", and is split between the government and the company.[65]

PSAs can be beneficial to governments of countries that lack the expertise and/or capital to develop their resources and wish to attract foreign companies to do so. They can be very profitable agreements for the oil companies involved, but often involve considerable risk.

These Agreements are the ones that are most widely used by HGs as contracts in the oil and gas industry, and is becoming the leading choice for most countries in their relationship with IOCs. However, there are many jurisdictional variations, and being aware of and understanding these is crucial for oil and gas practitioners working in this space. Thus it is imperative to also have a comprehensive, in-depth overview of PSA in key oil and gas jurisdictions around the world; to make a critical analysis and evaluation, and features contributions from an international group of leading experts and academics who address the legal, economic and political aspects of PSAs[66].

2.9.1. Background of PSA’s

PSAs were first developed in Indonesia in 1966 to give the HG more control over their resources. This type of contract soon became popular with a number of governments when crude oil was in tight supply and the price was rising rapidly.[67]

After independence nationalistic feelings were running high and foreign companies and their concessions became the target of increasing criticism and hostility. In response to this the government refused to grant new concessions. In order to overcome the subsequent stagnation in oil development, which was a disadvantage to both the country and the foreign firms, new petroleum legislation was brought in.[68]

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[64] PSAs grant certain rights, such as exploration and production, from the host government to an international oil company to prospect and develop resources.

[65] Lubogo Isaac Christopher – The Law of Oil & Gas in Uganda- First Ed.

[66] Flavio G. I. Inocencio, 2021. Production Sharing Agreements: A Global Legal Handbook, Globe Law and Business Limited

[67]Petroskills, April 2021. Introduction to Production Sharing Contracts, [online] available at; https://www.petroskills.com/blog/entry/00_totm/apr21-sub-introduction-to-production-sharing-contracts#.YNW2ZOgzbIU (accessed on 25th June 2021)

[68]Kirsten Bindemann, October 1999. Production-Sharing Agreements: An Economic Analysis, Oxford Institute for Energy Studies, WPM 25

PSAs were regarded as acceptable because the government upholds national ownership of resources. The major oil companies were initially opposed to this new contract form as they were reluctant to invest capital into an enterprise which they were not allowed to own or manage. More importantly, however, the Foreign Oil Companies (FOCs) did not want to establish a precedent which might then affect their concessions elsewhere.[69]

The first PSAs were therefore signed by independent FOCs who showed a greater willingness to compromise and accept terms that had been turned down by the majors. Furthermore, it has been argued that the independents saw this as an opportunity to break the dominance of the big oil companies and gain access to high quality crude oil.[70]
Thus challenged, the major FOCs bit the bullet and entered into PSAs (and found that in reality the foreign firm usually manages and operates the oilfield directly). From Indonesia PSAs spread globally to all oil-producing regions with the exception of western Europe where only Malta offers this type of contract.

PSAs are distinguished from other types of contracts in two ways. First, the FOC carries the entire exploration risk. If no oil is found the company receives no compensation. Second, the government owns both the resource and the installations. In its most basic form, a PSA has four main properties. The foreign partner pays a royalty on gross production to the government. After the royalty is deducted, the FOC is entitled to a pre-specified share of production for cost recovery. The remainder of the production, so called profit oil, is then shared between government and FOC at a stipulated share (for example 65 percent for the government and 35 percent for the FOC). The contractor then has to pay income tax on its share of profit oil. Over time PSAs have changed substantially and today they take many different forms.[71]

One highly specific feature of the mineral sector is that exploration and development of mineral resources must take place where the resources are located. Ventures in this sector are of a high-

[69] Ibid
[70] Barnes, P. 1995. Indonesia. The Political Economy of Oil. Oxford: Oxford University Press.
[71] Supra note 7

risk nature in the physical, commercial, and political sense as it is difficult to determine in advance the existence, extent and quality of mineral reserves as well as production costs and the future price in the world market. Profitability is not assured, and the fact that the resource is finite requiresthe continual acquisition of new deposits. Since virtually all mineral ownership regimes are basedon State sovereignty companies may have to concern themselves with government policies and regulations in more detail than they would in other sectors.[72]

The government decides whether resources can be privately owned or whether they are State property. If they are state owned the development can be conducted by a state company or it can be contracted to a private firm. Most countries grant development rights to private companies through a process of either negotiation or bidding.[73]

The most common combination of agents in mineral development is a HG which represents a developing country with one or more mineral resources and a multinational company from a developed country. It is not surprising that the objectives of the two frequently clash. The main aim of the multinational firm is profit maximisation whereas the government of the host country is mainly interested in maximising its revenue.

Since the objectives of firm and government do not necessarily coincide and indeed may diverge substantially, it is all the more important that they identify the likely sources of future conflicts and write a contract that is as comprehensive as possible. This divergence of objectives is frequently manifested in a lack of trust between the contractual partners. The relationship worsens if the government changes existing legislation and applies the new rules to contracts agreed under the old regime. Other potentially contentious issues are the taxation of the (foreign) firm and the split of revenue between firm and government.

PSAs can be complicated. Parties often disagree about various parts of the contract. Because both parties are trying to maximize revenue and minimize risk, it isn’t surprising that agreements that

[72] Ibid
[73] Ibid

seemed pretty clear at signing receive differing interpretations from a party under stress.[74]
Some of the arguments stem from the amount of time the agreements are in place. Personnel and process changes on both sides can change the understanding of the contract language. Changes in fiscal practices or political problems in-country can create other issues. Non-aligned operating or subcontractor agreements and economic cycles cause a few.

Tensions from what may be called “cost oil” develop from the difference in desires of the IOC and NOC. The IOC wants a guarantee that upfront costs are recovered. The NOC doesn’t want to allow cost recovery unless it sees these costs as having been “properly incurred.” The NOC wants proof of efficiency and due diligence on the part of the OIC before awarding any money.
So-called “profit oil,” which is the allocation of production left after “cost oil,” is also controlled by the PSA. The NOC wants profit oil right as soon as possible, regardless of what is going on with cost oil. Usually, a tax windfall or oil and gas royalty arrangement has something to do with it. Since tax rates can be 60% to 80%, it isn’t surprising the parties would like a hedge against taxes.
For example, IOCs prefer a stabilization agreement to buffer such early profit-taking to make sure taxes and other financial arrangements already in the PSA are not replaced by NOCs trying to puff up government revenues.
The expiration of the PSA can cause problems as well. There may be disagreements about everything from the transfer of operations to the accuracy of asset register or termination cost accruals. Most of the problem lands on the IOC in these cases, so the contractor typically works to get the most possible out of a field before the PSA ends.

PSAs within the United States are also possible, between the lessor (acting in place of a NOC) and the lessee (operating in place of an IOC). However, these agreements don't have the same track record as they do internationally, and they are poorly understood. Typically, a PSA is introduced for an allocation well that royalty owners of tracts crossed by the wells have agreed to share production.

[74] Supra note 1

Uganda first announced intentions to start oil production and development in 2006. Many years down the road, Uganda has started entering into contracts and agreements with different IOCs for purposes of exploration, development and production of the resource. However, few Ugandans understand or even know the terms agreed upon in those contracts. Partly, this is because the final negotiated contracts are highly confidential and therefore not readily available to read but secondly and most importantly, the model PSA is overly technical for an ordinary citizen of Uganda to comprehend.

It is important to break down the mysteries of the PSA and the whole norm of the same in the Ugandan perspective. The country recently discovered the presence of oil in the Albertine region and therefore has only entered into a few contracts regarding its exploration, development or production. Therefore, there is little or no knowledge about the operation of these contracts or even experience in as far as Uganda is concerned.

2.9.2. The Purpose of Production Sharing Agreements

PSAs allow the HG, sometimes called the national oil company or NOC, to maintain a certain amount of control over the development of oil and gas within the country. The agreement also helps NOCs gain the expertise they may lack for exploration and development of hydrocarbons within their borders.[75]

NOCs gain the expertise they need through the IOCs with whom the agreement is signed. IOCs typically bring the technology and expertise in strategic decision making to the table. In many ways, most of the risks of oil and gas development within these agreements fall on the IOC.[76]

The PSA also outlines how costs and profits are to be shared from a particular oil or gas field from the very start that is to say; Capital expenditures for exploration; Development and operational expenditure for normal operations; and Profits once production begins.

Although the IOC shoulders most of the risks, the more the IOC contributes in the early phases, the higher the share it can expect in return. This is always reflected in what is called cost oil. Therefore, the higher the initial costs of production, the bigger the share of the produce in form of

[75] Supra note 1
[76] Ibid

cost oil.

The IOC takes on most or all of the costs and risks of exploration. The NOC begins or increases its contribution after minerals are found, and the site is developed into a production unit with normal operations. The PSA is most beneficial to the NOC because it provides time to generate momentum for project management. Also, the NOC can develop new fields and reservoirs with no risk and little cost to itself.

2.9.3. The legal framework governing PSAs in Uganda.

It is important to note that Uganda has not for a long time had any streamlined law that manages the Oil and Gas sector. This is because the resource was not of much concern until the early 1980s. Prior to 1980 the colonial government did not believe that oil and gas resources were available in sufficient quantities to justify its exploitation.[77]

The **Petroleum (Exploration and Production) Act, No. 20 of 1985** that was repealed by the Petroleum (Exploration, Development and Production) Act 2013 was the only law applicable to the management and regulation of all activities in Uganda's oil and gas sector.[78]

Since discovery of commercial oil and gas deposits, Uganda has through the parliament and the relevant institutions enacted different laws to regulate the oil and gas sector and among these include; the Constitution of the Republic of Uganda 1995[79], the National Oil and Gas Policy, 2008, the Petroleum (Exploration, Development and Production) Act, 2013[80]; the Oil and Gas Revenue Management Policy, 2012, the Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act, 2013[81]; and the Public Finance Management Act of 2015. A further analysis of the above legal regime shall be discussed below;

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[77] Okuku, J.A. (2015), „Politics, the State and Limits of Oil-led Development in Uganda". Paper presented at Makerere Institute of Social Research (MISR) Seminar, Kampala p.4; https://misr.mak.ac.ug/sites/default/files/events/UGANDA%20OIL-LED%20DEVELOPMENT.pdf (accessed 26th June, 2021)

[78] J. Oloka-Onyango; "Courting the Oil Curse or Playing by the Rules? An Analysis of the Legal and Regulatory Framework Governing Oil in Uganda" https://www.jstor.org/stable/pdf/j.ctvt9k690.9.pdf?refreqid=excelsior%3Aa7571c7c5f7529c2a0adb8525320fd8d (Accessed on 26th June, 2021).

[79] This was through the amendment of the Constitution to include the current Article 244

[80] Section 6 (2) (4); the Act was passed to handle upstream oil development

[81] See Section 8 and 9; the Act was passed to handle midstream oil development.

i. The Constitution of the Republic of Uganda, 1995, as amended.

The 1995 Constitution of Uganda is the primary source of regulation of the Ugandan oil sector. This is because the Constitution is the supreme law of the country and it provides that the Government must ensure that resources are used for the benefit of all Ugandans.[82]

The Constitution under Article 244(2) mandates the Parliament of Uganda to make laws regulating the exploitation, exploration and development of petroleum and mineral resources, and the management of the revenues arising from petroleum exploitation and other related activities.

Article 41(1) of the Constitution of the Republic of Uganda states that every citizen has a right to access information in the possession of the state or any other organ or agency of the state except in cases where the release of such information is likely to prejudice the security, Contract Transparency in Uganda's Petroleum and Mining Sectors Contract Transparency in Uganda's Petroleum and Mining or sovereignty of the state or interfere with the right to privacy of any other person.[83]

ii. The Petroleum (Exploration, Development and Production) Act, 2013

The Act gives life to the National Oil and Gas Policy of Uganda (2008) by putting in place an effective legal framework and institutional structures for ensuring that processes of exploring, developing and producing of petroleum resources in Uganda are carried out in a sustainable manner that guarantees optimum benefits for all Ugandans, both the present and future generations.[84]

The Act also created a conducive environment for the efficient management of petroleumresources of Uganda by providing for institutions to manage the petroleum resources and regulating the petroleum activities which includes licensing, exploration, development, productionand cessation of petroleum activities or decommissioning as well as ensuring public safety and protection of public health and the environment in petroleum activities.[85]

The Act regulates the licensing and participation of commercial entities in petroleum activities. It

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[82]Objective XIII of the National Objectives and Directive Principles of State Policy, and Article 244(1) of the 1995 Constitution of Uganda.

[83]Bagabo, P., Mugyenyi, O., Magara, S., and Twebaze, P., Contract Transparency in Uganda‟s Petroleum and Mining Sectors, Kampala: ACODE Policy Research Paper Series No.94, 2019 https://media.africaportal.org/documents/Contract_transparency_in_uganda.pdf (accessed on 26th June, 2021)

[84] Petroleum (Exploration, Development and Production) Act, section 1

[85] Ibid

expressly states under Section 5 that:

> *"Petroleum activities under Ugandan jurisdiction shall not be conducted without an authorisation, license, permit or approval in accordance with this Act."*

The Act under Section 6 gives power to the Government to enter into agreements relating to petroleum activities consistent with this Act with any person with respect to the granting or renewing a license, the conduct by a person, of petroleum activities on behalf of any person to whom a license is granted.[86]

The Act[87] further states that;

"The Minister shall develop or cause to be developed a model Production Sharing Agreement or any other model agreement as may be entered into by Government under this section which shall be submitted to Cabinet for approval."

Under section 6(3), The Minister shall lay before Parliament the model Production Sharing Agreement or any other model agreement approved by Cabinet under section 6(2) and it shall be this model agreement approved by Cabinet that shall guide negotiations of any future agreements under this section.

The Act[88] also promotes transparency in conducting petroleum activities and to this effect the specific provision in the Act tends to expressly require the Petroleum Authority to

"ensure transparency in relation to the activities of the petroleum sector and the Authority"

The NOC in line with above requirement of the law and the principle of Access to information enshrined in the Constitution of the Republic of Uganda[89] makes the model PSAs available to the public through its website.[90]

iii. The Petroleum (Refining, Conversion, Transmission and Midstream Storage) Act, 2013.

This Act was also enacted to give effect to Article 244 of the Constitution. it was promulgated to regulate, manage, coordinate and monitor midstream operations; to enable the construction, placement and ownership of facilities; to provide for third party access to facilities; to regulate

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[86] Section 6(1), Ibid
[87] Section 6(2), Ibid
[88] Section 11(2d), Ibid
[89] Article 41(1) of the 1995 Constitution.
[90]See https://www.unoc.co.ug/wp-content/uploads/2018/06/MPSA.pdf (accessed 26th June, 2021)

tariffs for facilities; to provide for an open, transparent and competitive process for licensing by the minister; to provide for additional and particular health, safety and environment regulations not sufficiently regulated in other laws; and to provide for cessation of midstream operations under the Act and decommissioning of facilities.[91]

The Act covers areas similar to the Petroleum (Exploration, Development and Production) Act that is to say institutional arrangements[92], licensing[93], decommissioning[94], state participation and national content[95], liability for damage due to pollution[96], health and safety[97], and information and documentation[98].

Section 8 of the Act provides that;

The Government may enter into an agreement relating to midstream operations consistent with this Act, with any person in respect to the following matters;

(a) The grant of a licence;

(b) The conditions for granting or renewing a licence;

(c) The conduct by a person, of midstream operations on behalf of any person to whom a licence is granted; and

(d) Any other matter incidental or connected to the matters in paragraphs (a), (b) and (c).

The Act therefore makes an effort to allow the government to enter into agreements like the PSAs. Uganda has not ratified any international conventions that would bind it to fulfil other obligations under international law. However, it has signed many contracts for purposes of oil production, with the latest being the East African Crude Oil Pipeline (EACOP).

iv. Model Production Sharing Agreement.

According to Article 30.2 of the Model Production Sharing Agreement:

30.2. The parties agree that the terms and conditions of this agreement are based on the existing laws of the republic of Uganda and the terms contained in this Agreement. If, following the

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[91] See the long title of the Petroleum (Refining, Conversion, Transmission And Midstream Storage) Act, 2013

[92] Part II, ibid

[93] Part III, ibid

[94] Part VI, ibid

[95] Part VII, ibid

[96] Part IX, ibid

[97] Part X, ibid

[98] Part XI, ibid

following the Effective Date, there is a change in the laws of Uganda which substantially and adversely alters the economic benefits accruing to the Licensee, the Licensee may within 36 Calendar months from the date on which any such change has legal effect, notify Government accordingly and thereafter the Parties shall negotiate to agree upon the effect of the changes in law and the necessary adjustments to the Agreement in order to maintain the economic benefit of the licensee which existed at the effective date of this agreement PROVIDED that the licensee shall comply with the requirement of the law at all times.

30.4. For avoidance of doubt, the provisions of paragraph 30.2 above are intended for maintaining the original economic benefits under the Agreement as at the effective date and shall not prevent the Government from enacting laws intended to levy additional profit tax on additional profits.

The model provides for how participating interests are to be shared between the parties; the responsibilities and grant of rights; the requirement of exploration work programmes; budgeting; the aspect of discovery, development and production; keeping of records, writing reports and keeping data; the aspect of bonuses paid to government; royalties to government; participation of the State in the OGM; recovery of cost; production sharing; the aspect of taxation; valuation and measurement of petroleum; transportation of Oil by pipeline; marketing and lifting; domestic requirements; the aspect of natural gas; training of local expertise, research and employment of locals; title to assets; foreign exchange control; assignment of participating interests; the aspect of prevention of danger to person, property or environment; dispute resolution; force majeure; annual acreage rentals; termination of contracts; accounting and audits; notice; the laws applicable to the contract; the representation of the entire agreement and its amendment; waiver clauses; and the concept of confidentiality.

All these provisions will be tailored to suit each agreement concluded by the government of Uganda with other entities for the exploration, development and production of petroleum.

The host state's exercise of sovereign authority cannot be totally controlled by a stabilizing clause. These adjustment provisions have been designed to take into account this reality while also safeguarding the contract's economic balance. As stated in article 30.4 above, the government may amend the fiscal regime in anticipation of growth in order to profit from such developments without jeopardizing the IOC's initial economic benefits.

Still exercising its sovereignty, the government may select which laws are exempt from the application of stability provisions, particularly those whose changes or imposition over time are unlikely to have a substantial impact on the company's anticipated economic gains. "This indicates that the IOC shall have to, at all times, react to any changes that may occur in such laws or to any such regulations that may be imposed from time to time," says paragraph 5 of Uganda's model PSA. It's also worth noting that any stabilizing clause that goes against the constitution's requirements is null and void.

Given the exercise of sovereign authority by States, one would wonder how effective a stabilization clause would be in preserving an oil company's assets from expropriation or nationalization. In view of Articles 30.2 and 30.4 of Uganda's model PSA, if the discussions outlined in Article 30.2 do not result in an amicable resolution, the disagreement may be brought to the United Nations Commission for International Trade Law Arbitration Rules. A thorough examination of some of the Arbitral decisions over time demonstrates that the modern result of the basic stabilization clause aimed at forbidding expropriation is to render it unlawful, rather than invalidating it, which impacts the amount of compensation that may be granted.
In *TOPCO v. Libya I.M.1;*[99] for example, the tribunal stated that "the government could not exercise its sovereignty to nationalize in violation of its specific contractual commitments in the stabilization clauses, and nationalization in the face of these stabilization clauses amounted to a breach of the deeds of concession."

The Protocol Agreement between AGIP and the Congolese government guaranteed the legal standing of AGIP's local company in AGIP v. Congo, ICSID Case No. ARB/77/1. The government agreed under Articles 4 and 11 of the agreement not to enact any legislation or decrees that would change the company's legal status. The International Center for Settlement of Investment Disputes (ICSID) tribunal determined that AGIP's Congolese subsidiary's nationalization was manifestly in violation of the stabilization terms, was illegal under international law, and required the government to compensate AGIP in full.

[99] Ad hoc Award of January 19, 1977

As a result, a breach of a stability clause gives rise to compensation obligation under international law, regardless of whether the breach results in formal or de facto expropriation, and whether the property is physical, such as real estate or a factory, or intangible, such as contract rights. The problem is the amount of compensation that must be paid. In this context, the legality or illegality of a nationalization may have an impact on the compensation criterion as well as the amount of compensation due.

However, the Ugandan Model Production Sharing Agreement is not conclusive because the researcher would not find any literature confirming that it is the actual PSAs that have been entered into with the IOCs.

2.10. Conclusion

Stabilization clauses are one of the most widely preferred contractual mechanism by IOCs. However the argument is that stabilization clauses limit State sovereignty and restrain their legislative powers which shifts balance of bargaining power to IOCs or private entities to the detriment of the HGs. There is however limited literature expounding on the relevance of stabilization clauses in PSAs in this era vis-à-vis State sovereignty. That problem also partly explains why even the presently available literature is largely shallow with hardly in-depth analysis of this topic. The above review is not conclusive as there is wide literature at the reader's disposal.

CHAPTER THREE:

RESEARCH METHODOLOGY

3.0. Introduction

This chapter presents the research approach and methods used in the conducting of this research. It presents the methods that were used to collect data and the data analysis tools.

Methodology is the systematic way a researcher conducts a research.[100] It thus follows the methodology adopted in this research that is derived from the objectives and research questions in chapter 1 respectively on the one hand and the literature review in Chapter 2 on the other hand

3.1. Legal Context and Research Setting

3.1.1. Research Design

A research design is the conceptual structure through which research is conducted.[101] Traditionally, there are two methods of conducting a research, notably: quantitative[102] and qualitative[103] research methods.

It is the overall approach used to report on all the research objectives in an intelligible and logical manner in order to address the research problem. The research design is basically comprised of the research methods through which data is collected and analyzed.[104]

The research methods adopted enabled the researcher to study and analyze the materials available in order to successfully respond to the research questions. The research design enables the researcher to thoroughly analyze the data and have the research problem addressed in an

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[100] Jan Jonker and Barjan Pennink, The Essence of Research Methodology: A Concise Guide for Masters and PHD Students in Management Science (London, Springer, 2010) 17

[101] Kothari C.R, "Research Methodology Methods and Techniques: New Age International Limited," 2004

[102] Quantitative Research refers to a systematic empirical inquiry and measuring of events. It also involves the performing of statistical analysis of numerical data. It is scientific in nature, and tends to be employed when a theory is already well developed and is just being confirmed. 'See' Marry John Smith, Contemporary Communication research methods. (Belmont.CA, Wadsworth inc,.1988)

[103] Qualitative research refers to a systematic empirical inquiry into meaning and aims at understanding a social or human problem from multiple perspectives. 'See' Gay D Shank, Qualitative Research: a personal Skills approach (upper saddle River, Merrill, Prentice Hall, 2002)5.

[104] Kirshenblatt-Gimblett, Barbara. "Part 1, What Is Research Design? The Context of Design. Performance Studies Methods Course syllabus. New York University, Spring 2006< https://library.sacredheart.edu/c.php?g=29803&p=185902#:~:text=The%20research%20design%20refers%20to,measurement%2C%20and%20analysis%20of%20data.>

unambiguous manner.

The research questions for this study are best addressed through a qualitative research design.[105] The suitability of this method is a result of being in position to identify and appreciate gaps in the available literature. This research method has the capacity to help the researcher identify how and where the study fits in the already existing epistemological body of knowledge.

It is through the qualitative based methodological framework that it became evident that pre-existing literature hardly expounds on the relevance of stabilization clauses vis-à-vis State sovereignty in fairly sufficient detail.

This study perceives stabilization clauses as a phenomenon which the research is designed to examine and explore using socio-legal lenses. Thus, this research study adopted a qualitative methodology to allow the researcher to be alert to the different perspectives surrounding the legal framework on PSAs and their use in the oil and gas industry.[106]

Qualitative research approaches tend to also involve an in-depth probing and application of subjectively interpreted data.[107] This legal research also involved using the desk top approach that relies on law library to locate authoritative decisions. This method was equally resourceful in identification of applicable legislation and useful discussions from secondary sources. In this regard the archival based method enabled the researcher access useful literal materials that were analyzed further to ensure that the materials are useful in formulating substantial conclusions of the study results and making satisfactory recommendations.[108] This method enabled the researcher to appreciate and understand the PSA contents and context advanced in other materials

Adopting a qualitative methodology for this study is instrumentally vital in providing an insightful description of perceptions of other scholars. Special attention was given to viewpoints of different

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[105] Edmondson, A. C., & McManus, S. E "Methodological Fit in Management Field Research" : The Academy of Management Review, (2007) 32(4), 1155-1179

[106] Van de Ven, A. H. (2007): "Engaged scholarship: a guide for organizational and social research". (Oxford University Press', 2007)

[107] Oso, W.Y & Onen, D (2009): "A general guide to writing research proposal and report". (Nairobi: The Jomo Kenyatta Foundation, (2009).

[108] Ibid

scholars to develop a better understanding of explanatory account for theoretical and practical realities.[109]

3.2. Area of Study

Contextually, the study focuses on the relevance of stabilization clauses in PSAs in regard to State sovereignty with lessons for Uganda's oil and gas industry.

3.3. Research Method

The researcher used doctrinal and textual based qualitative research methods. These research methods involved critical analysis of different literature, from textbooks on PSAs.
The doctrinal and textual based research approaches are important in identifying appropriate online publications, reports, and journal articles on the subject of PSAs.

Doctrinal research also known as, theory-testing or knowledge building research in the legal academia is the established traditional genre of research in the legal field.[110] Chynoweth asserts that doctrinal research methodology is the process of undertaking legal analysis.[111] The method includes studying existing literature as well as researching more on some related cases and authoritative materials through an analytically methodological manner. This was be done with a view to develop a better understanding of the research subject matter. Given that the study relates to a legal research that touches on the legal and policy regimes, the researcher thought it wise to use the doctrinal method.

The need to appreciate and articulate the legal aspects of this research such as case law as indicated in the literature review is highly unlikely to require the researcher undertake field data collection. That is simply because such information could be acquired through the desk and library research methods. Henceforth being the study of legal nature, partly justifies why the researcher chose this methodology as the best method to be used to carry out the research.

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[109] Kvale, S. (1996): "Interviews: an introduction to qualitative research interviewing: Thousand Oaks," 1996.
[110] Desmond Manderson and Richard Mohr, "From Oxymoron to Intersection: An Epidemiology of Legal Research" (2002) 6(1) Law Text Culture 159, 161. For a breakdown of empirical and doctrinal PhDs in Australia see Desmond Manderson, 'Law: "The Search for Community' in Simon Marginson (ed), Investing in Social Capital (University of Queensland Press," 2002) p. 152.
[111] Paul Chynoweth, "Legal Research' in Andrew Knight and Les Ruddock (eds), Advanced Research Methods in the Built Environment Wiley-Blackwell," 2008 p. 37.

3.4. Sample and Sampling Techniques

In this study the researcher used documentary review to analyze the evolution and adaptation of stabilization clauses in the oil and gas industry. It is these documentary materials that are subject of investigation to examine the relevance of stabilization clauses in PSAs. The rationale behind documentary review is founded on its effectiveness in providing clear and comprehensive evidence.[112] The researcher relied on desk research in reviewing the documents.

3.5. Data Collection Strategy/Methods

Qualitative research is the approach that was used in undertaking data collection. It involved reviewing, content and textual analysis and attempting to uncover the deeper meaning and significance of the issues being researched.

Data relating to the relevant legal regimes pertaining to the phenomenon under study the oil and gas industry was reviewed and analyzed and is to be used in answering the research questions.

3.5.1. Documentary Review

Documentary research method is the use of sources or documents as authoritative basis for supporting arguments of an advanced academic proposition. The process of undertaking documentary research often involves conceptualizing, reviewing, using and assessing relevant documents.

In the secondary analysis of qualitative data, the relevance of good documentation is unlikely to be underestimated. This is mainly because it provides the necessary background and the much-needed context, both of which make re-use not only a more worthwhile but also a systematic endeavor. Secondary data was obtained through using both published and unpublished documents.

The researcher reviewed various publications, magazines and newspapers, reports, textbooks, journals and different sources of published information.

Analysis of the data gathered from these reports was undertaken to understand the phenomenon

[112] Mvgalakwa. M, The Use Of Documentary Research Methods' (2006) Social Research Reports African Sociological Reviews'' Vol. 10 Issue 2 p. 221.

under study.

3.6. Data Analysis Plan

The study employed qualitative data analysis. Brief descriptions, explanations, or directions, as well as the usage of prose tables, were included. In an essay, however, this type of descriptive material will be provided in the form of prose or even lists. Data analysis is the process of putting order, structure, and meaning into a massive volume of data. The purpose of data analysis is to gather information that is both relevant and useful. The analysis can be used to describe and summarize data, as well as to uncover correlations between variables, compare variables, identify differences between variables, and forecast outcomes.

The qualitative data was analyzed using both thematic analysis and content theoretical analysis. When analyzing the legal, policy and institutional frameworks, the researcher adopted a gap analysis plan. Gap analysis is a way to compare existing policies and practices to identify the gaps with regards to compliance to relevant required standards.

The steps involved in gap analysis include; finding out the existing laws, practices and the current situation, determining what the best practice is, developing a plan to fill the identified gaps in the laws and policies and carry out an implementation plan to arrive at the objectives which are based on the best practices.

This included processes and procedures for transitioning from qualitative data to some kind of explanation, understanding, or interpretation of the individuals and situations under inquiry. In qualitative data analysis, an interpretive philosophy is frequently applied. This is a study of qualitative data's symbolic and meaningful content. When analysing interview data, for example, the researcher may attempt to determine any or all of the following: someone's worldview, why they hold that position, how they got at that opinion, and what they have been doing. In the qualitative data analysis process, the writing and identification of themes are usually two processes.

3.7. Ethical Considerations

This research study followed UCU Law Students Research guidelines and was designed in line with UCU Research ethics procedures. The objectives of the study respect and take into

consideration all institutional ethical procedures, associated benefits and risks, and privacy and confidentiality measures.

3.8. Conclusion

This chapter details the research methodology that was be used to address the research questions. It provides evidence that the design was selected considering time and resource constraints of this project and also provides a detailed description of the research process, including data collection and analysis. The Qualitative approaches involved an in-depth probe and application of subjectively-interpreted data which was used in this study.

CHAPTER FOUR:

RESULTS AND ANALYSIS

4.0. Introduction

This chapter gives an analysis of the findings of this study in accordance with the research questions and objectives of the study.

4.1. Recap of research objectives

The main objective of this study is to examine the relevance of stabilization clauses vis-à-vis the principle of State sovereignty with the aim providing lessons for Uganda's emerging petroleum industry.

The other specific objectives of the study are;

i. To find out the relevance of stabilization clauses in PSAs.
ii. To find out the legal implications of stabilization clauses on the sovereignty of resource rich States.
iii. To evaluate the legal framework that governs the oil contracting system in Uganda's oil and gas sector.
iv. To find out whether Stabilization Clauses are still relevant in the 21st Century.
v. To provide to the emerging Ugandan Oil and Gas sector a peak into the future of the effect of stabilization clauses in PSAs, so that they learn from the lessons of other mature provinces.

4.2. Summary of findings

It is important to know the kind of stability a given stabilization clause aims to achieve as this can be used as the yard stick in the examination of the relevance of stabilization clauses vis-à-vis State sovereignty.

Sometimes stabilization clauses such as the economic equilibrium stabilization clauses are drafted in such a way that protects both the HGs and IOCs however such scenarios are very rare in the oil and gas sector. In many cases, these clauses are crafted to only protect the interests of investors from adversative effects such as changes in the HG's laws without considering the positive effects that such a change in law may cause to both the investors and HG. Actually some stabilization

clauses allow IOCs to switch back and forth as and when a certain change in law may affect their investment allowing IOCs to benefit only when the laws are favorable to them without due regard to the HG. This kind of practice has raised a debate on the true purpose of stabilization clauses.
On the surface and in principle, these clauses aim at ensuring legal and regulatory framework stability and to maintain economic equilibrium of a contract. However this is not the case where an unexpected event that affects the economic equilibrium of a contract positively like a rise in oil prices occurs, HGs do not benefit equally from the windfall profits.

Stabilization clauses should be crafted in a balancing manner in order to cater for the interests of both HGs and IOCs. It is a finding of this research that stabilization clauses are rarely drafted in such a way, rather they are drafted to only insulate and benefit the investors to the detriment of HGs. This is achieved by allocating risks that may arise as a result of changes in law to the State while allocating the positive benefits that may accrue as a result of such a change in law to the IOCs.

4.2.1. Validity and Legal Effect of Stabilization Clauses

The validity and legal effect of stabilization clauses has been a subject of debate by many authors and academicians especially in relation to the conflict between these clauses and the principle of State sovereignty over their natural resources.[113]

Stabilization clauses, specifically freezing clauses restrict the applicable laws and regulations applicable to an agreement to be those laws and regulations that were in existence at the time the contract was concluded. These freezing clauses restrict the HGs from making any changes in the legal regime that may be to the detriment of the IOCs.
Other types of stabilization clauses like the economic equilibrium clauses are to the effect that HGs shall compensate the IOCs for any financial losses suffered as a result of any changes in the legal regime applicable to an agreement already concluded.

The arbitral jurisprudence has over time changed the scope of stabilization clauses not to only

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[113] Thomas W Wälde and George Ndi, ‘Stabilizing International Investment Commitments: International Law Versus Contract Interpretation’ (1966) 31 Texas Intl LJ 215, 217 and 261

cover the change in text of laws but also the change in the interpretation of the said text. This was witnessed in the case of ***Duke Energy International Peru Investments No. 1, Ltd v Peru,***[114] where the arbitral tribunal held that an inclusion of a stabilization clause in an agreement did not only mean that the legal environment in place at the time the contract was signed wouldn't be changed but also included the interpretation and application of that law and emphasized that it would not be changed to the detriment of an IOC.

And on the other hand according to Thomas[115], all stabilization clauses with a freezing nature are invalid under international law. He further states that sovereignty over natural resources has assumed a character of *jus cogens* a customary norm from which no derogation is permitted.[116] This position was largely discussed at the General Assembly of the United Nations that passed Resolution 3171 that gave States the right to expropriate as an expression of their sovereignty in order to safeguard natural resources.

It is a finding of this research that although stabilization clauses are in negotiated contracts and the rules of international commerce are thus applicable to such agreements, the principle of State sovereignty is one that cannot be deviated from. As was noted in the United Nations that passed Resolution 3171 on permanent sovereignty over their natural resources, stabilization clauses should not encumber states from changing their national laws whenever need be in the favor of foreign direct investments.

Foreign direct investments has through several perceptions, been inclined to the need for inclusion of stabilization clauses in agreements especially with developing countries. Nevertheless, it is a finding of this research that all countries aim at attracting foreign investments for growth of their economies and the use of stabilization clauses in favor of foreign direct investments should not be limited to only developing countries.

Therefore, the legal validity and effect of stabilization clauses is to the extent of their impact on

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[114] ICSID Case No ARB/03/28, Award of 18 August 2008

[115] Thomas J. Pate, 'Evaluating Stabilization Clauses in Venezuela's Strategic Association Agreements for Heavy-Crude Extraction in the Orinoco Belt: The Return of a Forgotten Contractual Risk Reduction Mechanism for the Petroleum Industry,' 40 U. Miami Inter-Am. L. Rev. 347 (2009)

[116] Ian Brownlie, 'Principles of Public International Law,' 489 (6th ed. 2003).

the Sovereign status of a State.

Legal effect of stabilization clause *Stricto Sensu*

The legal effect of stabilizing clauses is largely determined by the clause's specific structure. The legal effect of a stabilization clause *stricto sensu* is to determine whether its presence in a petroleum contract can change the contract's legal nature to "enclave status," or whether nationalization or expropriation of petroleum projects, or a unilateral change or termination of a contract containing a stabilization clause by a host state, should be treated as an unlawful act under national and international law.

Prohibition of Nationalization or Expropriation

A key point concerning the legal effect of the stabilization provision *stricto sensu* is whether the clause forbids nationalization and expropriation of a foreign contractual firm, a matter that has vexed arbitral tribunals for a long time. According to one extreme interpretation based on pacta *sunt servanda*, a stabilizing provision prevents otherwise legal state nationalization. As a result, nationalizing a foreign-owned company in violation of a stabilizing clause is an illegal conduct that can only be justified by a significant change in circumstances. This was the conclusion reached by the arbitral tribunal in the Texaco arbitration, which found that the Libyan government's nationalization was a violation of the stabilization clause and an illegal act under international law.[117]

Later arbitrations rejected this line of reasoning, holding that nationalization is always a legal act and that a stabilising provision cannot abrogate a state's ability to nationalize under international law. The tribunal in the Liamco arbitration held that non-discriminatory nationalization that is not accompanied by illegal acts or conduct is not an infringement of a stabilising clause. The panel in the Aminoil arbitration found that while a simple and direct reading of stabilising provisions would lead to the conclusion that they restrict any form of nationalization, this assumption is incorrect. As a result, it concluded that limiting a state's right to nationalize is a "particularly severe endeavor" that cannot be assumed without express expression.

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[117] Supra note 55

Limitations on a sovereign's authority to nationalize may be possible, according to the Aminoil decision, but they would have to be explicit and fair. Finally, the Aminoil tribunal decided that a stabilization provision must be understood narrowly, and that it should only be used to defend against confiscatory measures. As a result, regardless of the form or wording of the specific stabilizing provision, it cannot prevent lawful nationalization, which is recognized as a state's inherent authority under international law, because a contractual obligation cannot trump a general international law norm.

Another implication of the Aminoil decision is that a stabilisation provision may be lawful as a temporary restriction on state sovereignty if it is only in place for a short length of time. On the other hand, in the face of major social and economic changes in the host country, a stabilisation provision for an unduly long term, such as sixty years, may be justified. As a result, the legal precision of such a phrase in terms of its duration and extent of application, as well as explicit reference of the legal repercussions that may result from its violation, undeniably enhances its legal effect.

Internationalization of Contract

The presence of a stabilization clause, according to contract internationalization theory, has the legal consequence of giving the contract including it an international character. As a result, international law governs the parties' rights and obligations under the petroleum contract, and unilateral cancellation of the contract is an internationally illegal act. Indeed, some arbitral tribunals have recognized a stabilization clause's internationalization effect, citing the presence of a stabilization clause as an important indicator that the contract has been internationalized, removing it from the host state's municipal law and subjecting it to international law principles.
The introduction of a stabilizing clause in the Texaco award transformed the legal nature of Libyan petroleum concessions, converting them to internationalized ones.[118] The nationalization of an

[118] "This Concession shall be construed throughout the period of validity in accordance with the Petroleum Law and the Regulations in force on the date of execution of the agreement of amendment by which this paragraph (2) was incorporated into this concession agreement," says clause 16(2) of the concession agreement. Without the Company's permission, any alteration or repeal of such Regulations will have no effect on the Company's

Italian firm was also deemed to be in violation of article 11 of a 1974 agreement guaranteeing the investor's position for 99 years, which was upheld in the 1979 AGIP arbitration.[119] The tribunal determined that it was necessary to apply international law in conjunction with Congolese law in relation to this stability clause. The tribunal determined that the applicability of a stabilization clause "results not from the automatic play of sovereignty of the contracting state but from the parties' common-will stated at the level of international legal order."

Some observers believe that the essence of a stabilization provision is to prevent a state from unilaterally amending a state contract, and that international law governs the contract over the host state's law. Others argue that without an arbitration clause or an applicable law clause providing for broad principles of law or international law, the introduction of a stabilization clause does not fully internationalize the contract. The Sapphire arbitration in 1967 gave birth to the theory of contract internationalization, with the tribunal holding that "these concessions give the contract a particular character, which lies partly in public law and partly in private law," and that "this contract has a quasi-international character, which releases it from the sovereignty of a particular legal system."[120]

4.2.2. Presumptions and Realities on Stabilization Clauses

There are quite a number of perceptions as to why stabilization clauses are used in contracts and two in particular stand out; one of the presumptions is that there are high levels of political risk and instability in developing countries and the second one is that developing countries compete amongst each other in a bid to attract IOCs foreign direct investment. Even though the presumptions are true in theory the finding of this research is that neither is true. International players in the extractives industry have promoted stabilization clauses as a cure for the above presumptions.

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contractual rights. Professor Dupuy's proposal for contract internationalization was founded on the following premises: I These agreements are not administrative contracts; (ii) Resolutions of the United Nations General Assembly purporting to assert the host state's exclusive authority in matters of nationalization are not positive international law; (iii) deeds of concession fall into the category of an economic development agreement." Texaco, 17 I.L.M. 3 (1978).

[119] AGIP, 21 I.L.M. 726, 727–28 (1982)

[120] Saphire International Petroleum Ltd. v. National Iranian Oil Co., 35 I.L.R. 136, 171–73 (1967).

4.2.3. Presumption of competition among developing countries to attract IOCS/ Foreign Direct Investment

Proponents for stabilization clauses argue that foreign investments aid economic development in developing countries, however such investments come with several uncertainties thus the need for stabilization clauses.[121] However it is important to note that investments in developing countries are not only driven by the HGs' interests but also the interests of the IOCs.[122]
HGs in most cases attract foreign investments in order to increase revenue and benefit from foreign and in most cases advanced technology[123], with a view that these will lead to increased output and productivity which will in return enable the host countries to favorably compete on international scenes regardless the level of development.[124]

On other the hand, the desire of foreign investors to expand and invest in other countries and that of HGs to attract foreign investment is more or less the same. Foreign firms invest abroad in order to increase their return on investment.
It is therefore the submission of the researcher that it is not true that the rationale of foreign investment in developing countries is to improve the latter's economic future whereas this may be the positive effect of foreign investment, it is not the objective of the foreign investors.

As a result, it is critical for HGs to strike a balance between their development goals and the profit goals of IOCs.[125] The risks linked with oil and gas projects should be proportional to IOC earnings, and it is critical to determine if a given stabilization clause achieves this balance.
It is also important to note that, regardless of the level of development, industrial development, or location, most countries' policies, standards, and strategies for attracting investment are nearly identical, implying that there is competition for investment everywhere, including both developing

[121] Christopher T Curtis, 'The Legal Security of Economic Development Agreements' (1988) 29 Harvard Intl LJ 317, 365.
[122] EIU, World Investment Prospect to 2011: Foreign Direct Investment and the Challenge of Political Risk (EIU 2007) 67.
[123] OECD, Foreign Direct Investment for Development, Maximising Benefits, Minimising Costs (OECD 2002).
[124] Andrew Sharpe and Meghna Banerjee, Assessing Canada's Ability to Compete for Foreign Direct Investment (CSLS 2008); UKTI, Britain Open For Business :Growth though International Trade and Investment (UKTI 2011) 5.
[125] EIU, World Investment Prospect to 2011: Foreign Direct Investment and the Challenge of Political Risk (EIU 2007) 67.

and developed countries, and that the use of stabilization clauses in contracts cannot be justified Therefore, it is important for HGs to balance their development objectives with the IOCs' objectives to make profits.[126] The risks associated with the oil and gas projects should be commensurate to the profits earned by IOCs and it is important to find out whether a specific stabilization clause meets the required balance.

It is also important to note that the policies, standards and strategies to attract investment are almost the same in most countries regardless of the level of development, industrial development and location which implies that there is competition for investment everywhere and this includes both in developing and developed countries so attraction of foreign investment cannot be a justification for the use of stabilization clauses in contracts.

Increased industrialization in developed countries has led to an increased demand for supply of energy such as oil and gas and as reserves in these countries reduce, the developed countries support their home firms' investments in less developed countries with unexploited reserves or natural resources in order to meet the demand in their own countries. The competition among IOCs usually from developed countries to invest in natural resource exploitation in developing countries is higher than the competition presumed among the developing countries to attract foreign investment.[127]

Whereas it is an accepted fact that developing countries lack the requisite capital, technology and other resources to harness or exploit the natural resources like oil and gas justifying the need to attract foreign investors (IOCs), there's also a scramble by IOCs for these natural resources implying that benefits from the exploitation and production of these natural resources not only accrue to the HGs but also the IOCs. It is therefore not fair to use stabilization clauses in developing countries in order to create a favorable investment climate for the IOCs to the detriment of the host states especially in the African countries.[128]

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[126] EIU, World Investment Prospect to 2011: Foreign Direct Investment and the Challenge of Political Risk (EIU 2007) 67.
[127] Jim Jubak, 'A Global Bidding War for Oil (20 October 2011) <http://money.msn.com/investing/a-global-bidding-war-for-oil-jubak.aspx?page=2> accessed 22 January 2022.
[128] Andrea Shemberg, 'Stabilization Clauses and Human Rights (2009) Report, paras 53 – 56

4.2.4. Presumption of high political risks in developing countries

Before delving into the specifics of this premise, it's crucial to understand what constitutes a political risk. Regrettably, no commonly acknowledged definition of a political risk exists. Terrorism, war, government breach of contract, adverse legal regime changes, insurgency, and restricted currency transfer and conversion are some of the events that have been highlighted as posing a political risk.[129]

Authors have taken steps to differentiate between the different categories of political risks. One author in particular is D. Wagner whose differentiation analysis was premised on the relevance and he points out the types of political risks to include;[130]

i. Firm-specific political risks.
ii. Country specific political risks.
iii. Government risks
iv. Instability risks

According to Wagner, Firm-specific political risks are those risks that are discriminatory in nature and are faced by specific companies or firms while country specific political risks are those risks that affect the whole country.[131]

The author further differentiates government risks and instability risks. He defined government risks to include those risks that are a result of government enactments, policies, actions like breach of contract, imposition of high taxes, legal regime changes among others and on the other hand he defined political risks as those risks that are a result of political factors like power struggles, politically instigated riots, civil wars, strikes etc.[132]

The distinctions above are relevant to this research because they highlight the kind of risks that the stabilization clauses were intended to mitigate.

<http://www.ifc.org/ifcext/sustainability.nsf/content/publications_lessonslearned> accessed 22 January 2022.

[129] World Bank, World Investment and Political Risks (World Bank 2010) 17 – 19

[130] Daniel Wagner, 'Defining Political Risks' (IRMI, October 2000) <http://www.irmi.com/expert/articles/2000/wagner10.aspx> accessed 22 January 2022.

[131] Daniel Wagner, 'Defining Political Risks' (IRMI, October 2000) <http://www.irmi.com/expert/articles/2000/wagner10.aspx> accessed 22 January 2022

[132] Daniel Wagner, 'Defining Political Risks' (IRMI, October 2000) <http://www.irmi.com/expert/articles/2000/wagner10.aspx> accessed 22 January 2022

Accordingly what amounts to political risks that stabilization clauses are intended to mitigate exist in all countries regardless of whether developed or developing countries. The argument that stabilization clauses are only fit to be used in developing countries where such risks are higher is misleading and discriminatory in nature since it is influenced by perceived political risks to only exist in developing countries.

Because competition for investment and political or government risks that stabilization clauses aim to control or minimize exist in equal measure in both developed and developing countries, the findings of this study show that developing countries, like developed countries, can change their fiscal policies, legal regimes, and regulatory changes in the oil and gas sector.

Therefore just like developed countries, the findings of this study show that developing countries can also change their fiscal policies, make legal regime and regulatory changes in the oil and gas sector since competition for investment and political or government risks that stabilization clauses target to control or minimize exist in equal measure in both developed and developing countries.

It is also the submission of the researcher that just like developed countries attract foreign investment without offering stabilization clauses, developing countries can as well attract the investment in the extractives industry without the stabilization clauses and this is because offering stabilization clauses does not guarantee an obvious increase in investment in the industry.

4.3. Conclusion

Stabilization clauses have been interpreted differently by different arbitral tribunals and one in particular is ***LIAMCO v The Government of the Libyan Arab Republic*,**[133] where the tribunal held that a state has powers to make changes to its national laws regardless of the contracts enteredinto implying that stabilization clauses and other contractual undertakings do not bar states from making changes in national laws.

This position has been a subject of debate and some authors like Abdullah argue that stabilization clauses cannot be declared invalid on the basis of state sovereignty. He states that the principle of state sovereignty has been abandoned by the UN general Assembly on permanent sovereignty over

[133] Ad hoc Arbitration Tribunal award of April 12, 1977

natural resources, the Charter on Economic Rights and Duties of the States because neither of the resolutions of these bodies suggests that a state, in the exercise of its sovereignty, may abandon contractual commitments undertaken voluntarily and instead the resolutions require that they observe foreign investment agreements entered into for the purpose of developing natural resources. The author asserts that stabilization clauses in a negotiated contract should be seen as a self-imposed limitation on the sovereignty of states.

The principle of permanent sovereignty over natural resources is to the effect that natural resources like oil and gas should be exploited to benefit the country and its people and states should have control over their natural resources to the exclusion of others.

It is the conclusion of this research from the findings highlighted above, that whereas stabilization clauses are important in order to protect foreign investments, they should not be used discriminatively and in isolation of developing countries

CHAPTER FIVE:

CONCLUSION AND RECOMMENDATIONS

5.0. Introduction

This Chapter encompasses the general conclusions drawn from the findings of the study and goes further to highlight and discuss the limitations to this research and puts forward the recommendations to the findings of the study.

5.1. Discussion of conclusions

From the previous chapter that discussed the findings of this study, general conclusions were drawn from which lessons for emerging industries can be drawn especially for developing countries.

First and foremost, the backbone of stabilization clauses is the doctrine of pacta sunt servanda that provides for the sanctity of international agreements and is to the effect that parties to a contract are required to perform all their obligations under contract in good faith in order to ensure stability of the contract.[134] Chioma emphasizes that stabilization clauses play a key role in stabilizing the contractual regimes which is key in oil and gas investments especially in developing countries. The author further states that a well drafted stabilization clause provides necessary economic equilibrium for the overall effectiveness of PSAs. This doctrine is so much upheld and emphasized in international oil and gas contracts that are highly prone to changing circumstances. Therefore stabilization clauses are used to mitigate the presumed political risks in resource rich countries.

Secondly, it is observed that contractual stability can be achieved through legal and economic approaches. The legal approach is comprised of the contractual and legislative approaches. The contractual approach includes the use of stabilization clauses and the legislative approach includes the reliance on the legal framework in place to ensure sanctity of the contracts. The economic approach is comprised of the commerce rules and techniques enforced in a fiscal system like the taxation mechanisms. The legal approaches are used to deter political risks that may negatively

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[134] Eze Emem Chioma; "Examining the crucial impact of a well drafted stabilisation and renegotiation clause on production sharing agreements" I.E.L.R, 2015, 5,212-217

affect petroleum contracts like changes in the laws whereas the economic approaches are tailored to facilitate investment in the sector.

Thirdly, it has been observed from the study that stabilization clauses are an encumbrance on the sovereignty of states. Whereas the use of stabilization clauses is an element of contractual mechanisms to ensure contractual stability, they are used in favor of IOCs which may sometimes prejudice the host governments' interests. States enjoy the sovereignty to utilize their natural resources and deal with them to benefit their people which sometimes can call for amendment of laws to ensure that they are not mismanaged and maximum revenue collection. Stabilization clauses like the freezing clauses encroach on such powers by restricting or freezing the country's laws and any changes to such laws must not be to the detriment of the investors. Even though some tribunals have held that stabilization clauses are legal, debates have ensued as to the extent of their validity and effect on the sovereignty of states.

Fourth, the study observes that stabilization clauses are used mainly because of two perceptions namely, competition for foreign direct investment and political instability. It is the submission of the researcher that competition for foreign direct investments doesn't only exist in developing countries but also in developed countries and therefore stabilization clauses should be applied in equal measure. On the other hand, the political risks envisaged in developing countries which the stabilization clauses are used to mitigate, exist in all countries. The political risk is limited to changes in law and this can be done in any country whether developed or developing and therefore political risks and attraction of foreign direct investments cannot be used as a justification for the use of stabilization clauses.

5.2. Limitations of the Study

In conducting this study, the researcher interfaced a number of challenges which turned out to be limitations to the study. These are as follows;

i. limited time

Studying and analyzing petroleum contracts requires a lot of time which the researcher didn't have at disposal because of the timelines within which this research was supposed to completed and submitted for examination purposes and this hindered the researcher form exhausting all the

available researchable materials that could have been or provided reliable information.

ii. Limited funds

Conducting any research project requires some funds to facilitate the researcher in procuring the required materials like the journals that could have provided reliable information to aid the research however these funds were not readily available and thus this was a limitation in conducing this research.

iii. Inadequate literature

Whereas some authors have written about stabilization clauses in petroleum sharing agreements, there is very limited literature that is accessible on the relevance of stabilization clauses in PSAs vis-à-vis state sovereignty, the phenomenon that that this research was investigating. The inability to access vast material on the topic under study was a limitation in conducting this research.

iv. Inability to access information not in public domain

Petroleum contracts are considered to be confidential documents that are not readily available to the public. And because of this confidentiality policy, the researcher was unable to access the current PSA models in order to give a detailed critique and analysis of the relevance of the stabilization clauses in PSAs vis-à-vis State sovereignty.

5.3. Recommendations for Future Research; Lessons for Uganda's emerging oil and gas industry

5.3.1. To grant or not to grant stabilization clauses.

From the findings of this study, recommendations proposed to deter the impact of stabilization clauses on state sovereignty must not only focus on the scope of the clause but the way they are granted and the purpose for which they are to be used. Several factors have to be put in consideration by host states before they decide on whether or not to grant the stabilization clauses.

The proponents of stabilization clauses claim that these clauses are essential in encouraging foreign direct investments and attracting investors in the extractives industry especially in developing countries. However from the discussion in section 4.2.3, the presumption of competition among developing countries has been rebutted as a justification for the use of stabilization clauses. It the

submission of the researcher that, developing countries can attract foreign investment into the extractives industry with or without stabilization clauses. The presumption of competition for foreign direct investments among developing countries is unjustified and therefore before a host state grants stabilization clauses in contracts, it must find establish the rationale for which the investor is demanding for the stabilization clause. The investor must at least prove to the host state that it is legitimate and necessary that stabilization clauses are granted depending on the circumstances since the political situation cannot be the same in all developing countries.

Economically, IOCs demand for stabilization clauses on grounds that they invest huge sums of capital in highly risky projects in developing countries presumed to have high political risks thus justifying their demand for the stabilization clauses. Some IOCs demand for higher shares of rent in order to lower their risks instead of stabilization clauses. It is therefore that before a host government grants stabilization clauses, an assessment is conducted in order to determine how much to give away to the investor and if it is economically viable for a host state to give high shares of rent in return for stabilization clauses or lower the risk premiums for the investors where applicable.

Several econometric studies have been conducted and one in particular is one that was conducted by Margaret McMillan and Andrew Waxman on US multinational corporations that invest in extractive industries in developing countries.[135] The McMillan econometrics study used the Chad-Cameroon pipeline project as a benchmark and it was observed that IOCs obtained good deals from developing countries due to high levels of corruption and poor governance and theydemanded stabilization clauses in order to mitigate the presumed political and government risks and were entitled to higher percentages in profit sharing.[136]

Some developing countries often rely on recommendations from high level institutions like the World Bank, however, the McMillan econometrics study also found that even in deals that

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[135] Margaret S McMillian and Andrew R Waxman, 'Profit Sharing between Governments and Multinationals in Natural Resource Extraction: Evidence from a Firm-level Panel' (2007) Brookings Trade Forum 149; Paul Collier, The Bottom Billion: Why the Poorest Countries are Failing and What Can Be Done About It (OUP 2007) Part 2.
[136] Margaret S McMillian and Andrew R Waxman (n 1) 159 – 160

involved the World Bank in negotiations, their involvement never yielded good deals for host governments.[137] Therefore this should be a lesson for countries like Uganda whose oil and gas industries are still in their infancy stages not to enter into a contract simply because the terms therein have been approved by World Bank. It is therefore important that developing countries conduct their own assessments on whether to have stabilization clauses in a given contract or not depending on the circumstances of a particular state regardless of whether institutions like World bank have recommended stabilization clauses or not.

The rationale for self-assessment is that through these assessments, a state is able to realize their competitive advantage on the market and this can be used as a bargaining tool before committing by entering into an unfair agreement with foreign investors. Resource rich countries should also realize that IOCs are also competing to invest in their extractive industries and in cases where a number of IOCs are bidding to invest in a particular resource, stabilization clauses may not be necessary in the circumstances.[138]

In order to attract foreign investments into the extractives sector, developing countries should develop a highly attractive and competitive environment that encourages investment. A good investment environment can only be afforded to investors through adequate legal protection mechanisms like adoption of flexible investment laws and fiscal regimes and through these legal mechanisms host states can opt for flexible stabilization clauses like those that cover only laws or regulations that are discriminatory among the companies since all laws must be applied in the same way to all players in the same sector and not be applied in a discriminatory manner as was held in the tribunal award in ***CMS Gas Transmission Co. v Argentina***.[139]

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[137] Margaret S McMillian and Andrew R Waxman (n1) 166
[138] William F Arnold, 'Mongolia Mining Sector Competitiveness and the Use of Stability Agreements' (2004) Report on Mongolia Economic Policy Reform and Competitiveness Project, 5
[139] ICSID Case No ARB/01/8, Award of 12 May 2005 [293] – [295]

5.3.2. Conduct Impact Assessment for Stabilization Clauses

The relevance of stabilization clauses in some countries is premised on several factors and one cannot rule out the fact that they are necessary in some countries since the circumstances that warranty whether or not to use stabilization clauses are different in different countries.

In circumstances where it is viable or necessary to use the stabilization clauses, it is important that a host state conducts a stabilization clause impact assessment to determine the extent of the legal implications of the choice of stabilization clause to be granted. The rationale of this impact assessment is to identify the impact of the chosen clause on the country's ability to enact new laws or amend/modify the existing laws and have such implications evaluated and mitigated in order to preserve the host state's sovereignty. The impact assessment also benefits the IOCs since it is conducted in public, it mitigates the consequences of contracts that are negotiated in secret since they usually turn out to unstable.

5.3.3. Time bound and Flexible stabilization clauses

The above recommendation requires an impact assessment for stabilization clauses is done in order to ensure that the choice of the clause should be able to benefit the host state without discouraging investment.

Whereas developing countries are presumed to be high risk investment destinations by many IOCs, not all developing countries are politically insecure. Therefore researcher submits that the need for stabilization clauses in some jurisdictions cannot be ruled out. However, in circumstances where stabilization clauses are necessary, the clause used should be flexible and have a time frame.

In order to preserve their sovereignty, host states where stabilization clauses are to be granted should set time frames within which to review these clauses. These clauses should be flexible in order to ease the restraints that such a clause may have impose on the State.

5.3.4. Publicize PSAs

It is the finding of this research that PSAs are not in the public domain, making it suspect. Reason being HGs are driven by the desire to attract investment by incorporating stabilization clauses at the detriment of its nationals. There is always a fear that once this agreements are made public and

this is discovered there will be an upheaval among the citizens because the sovereignty of the HG would have been compromised.

For example in Uganda in the past, the Government has enticed investors with attractive investment packages leaving one to wonder if they have not included stabilization clauses in the PSA in pursuit of the same. Not to mention the fact that there are corruption tendencies in public offices making the chances of including stabilization clauses high.

Since the State deals with the natural resources on behalf of its citizens, these PSAs should be made public to expose, if any, corruption that may have played a role in the inclusion of stabilization clauses. It is a recommendation of this research that countries should enact strict laws on publicizing these PSAs in order to deter the inclusion of undesired stabilization clauses that may compromise State sovereignty.

5.3.5. Empower institutions and experts

It is a finding of this research that stabilization clauses are used because of the risks associated with oil and gas investments especially in developing countries. It is also a finding of this research that stabilization clauses are included in PSAs because IOCs that demand for their inclusion have a higher bargaining position since they bear a higher risk by investing in the petroleum sector.

With the increased popularity of cross-border pipeline projects, new ways to stabilization are emerging, necessitating a more complicated set of legal agreements.

It's therefore a recommendation of this research that governments of resource rich countries like Uganda that are entering into these PSAs should invest more in empowering experts in the industry. It is also important that key institutions like Parliament that play a key role in enacting laws that regulate the industry should be empowered so that they have experts who sit on the oil and gas committees in order to enable and facilitate the enactment of flexible legal frameworks that do not only protect the state's interests but also attract investment.

The government should also invest more in training the technical staff in key offices and government departments like PAU, UNOC and the Energy ministry so that they have the capacity to draft and negotiate petroleum contracts with international players in the sector.

5.3.6. Apply the doctrine of 'Police Powers' in the interpretation of stabilization clauses

The police power doctrine is to the effect that States have inherent powers or rights to enact regulations to protect public interests and it cannot be held to have acted wrongfully if a given regulation was enacted through the due process.[140]

The preceding proposals centered on whether and how stabilization provisions should be given. The question now is what can be done to alleviate the limits imposed by the stabilizing clauses that have already been approved given the fact that these clauses typically last for long periods of time. While some of these issues may be settled by dialogue, many will very certainly be resolved through international arbitration, as is increasingly the case.[141]

As a result, arbitral tribunals play a critical role in harmonizing existing stabilization clauses with long-term development. This is especially true because, in most circumstances, the fear of international arbitration deters governments from establishing or enforcing policies that encourage sustainable development which may in turn compromise their sovereignty. And, as some commentators have pointed out, these threats have been successful owing to arbitral tribunals' near-universal support for stability provisions. As a result, it is critical that arbitral courts reconsider their interpretations of stabilisation clauses and begin to read them in a way that accommodates host states' legitimate pursuit of long-term development.[142]

In *Duke Energy Electroquil Partners & Electroquil S.A. v Ecuador,*[143] the tribunal observed that the investor's expectations must be valid and reasonable at the time the investment is made in order to be protected. All aspects must be considered in determining the rationality or validity of the investment, including not only the facts surrounding the transaction, but also the political, economic, cultural, and historical context in the host country. Furthermore, such expectations must

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[140] Hubner, J., Police powers in Philip Morris V. Uruguay, in Risse, J. et al, SchiedsVZ, German Arbitration Journal, Vol. 16, Issue 5, pp 288-294

[141] International Financial Corporation, May 27, 2009. Stabilization Clauses and Human Rights, A research project conducted for IFC and the United Nations Special Representative of the Secretary-General on Business and Human Rights.

[142] ibid

[143] Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador, ICSID Case No. ARB/04/19

stem from the conditions that the State provided to the investor, and the latter must have relied on them while making his or her investment decision.[144]

Although this case included a treaty duty based on the fair and equitable treatment norm, it is contended that the same logic can and should be applied to contractual stabilising clauses.

Many arbitration rulings are focused on commercial, rather than national, factors, some critics have contended that arbitrator decisions inevitably empower investors at the expense of states.

According to a survey of arbitral cases, tribunals do not apply this rationale to contractual promises of stability since such guarantees are viewed as a "particular commitment" by host states not to change their laws to the prejudice of investors. While this is true, the fact that a host state made a "specific commitment" should not prevent a tribunal from evaluating the reasonableness or legitimacy of that "specific commitment" in light of the host state's political, socioeconomic, cultural, and historical circumstances at the time the commitment was made.[145]

The fact that many of these clauses are given through opaque processes by unelected, unaccountable, and/or notoriously corrupt regimes justifies the necessity for tribunals to examine their legitimacy and reasonableness. As a result, because of a "particular commitment," investors should not be awarded a blanket right to a fair expectation of stability. In other words, they should not be allowed to exploit stabilization terms provided by corrupt dictators to oppose legitimate development measures adopted by future governments. As a result, it is recommended here that, contrary to arbitrators' current position, an investor's legitimate expectations should not be confirmed solely on the basis of a stabilising provision. The approach outlined in *Duke Energy v Ecuador*[146] should be used instead to enable uphold the doctrine of state sovereignty.

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[144] Duke Energy Electroquil Partners & Electroquil S.A. v Ecuador, ICSID Case No ARB/04/19, Award of 18 August 2008 [340]
[145] Karasira Denis, 2019. Enforceability of Stabilization Clauses in Oil and Gas Contracts, University of Rwanda.
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