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The use of arbitration in natural gas and petroleum exploration concession agreements in Brazil

In the scope for the development of newer energy resources, the Petroleum Law (Law n.º 9,478/97) was duly necessary for the implementation of a new regulatory framework, right after Constitutional Amendment n.º 09/95 had already provided modifications in what it concerned a monopoly by the Federal Government. Within a more flexible environment, exploration and production (E&P) activities began so as to allow the arrival of private *players* increasing (or rather, starting) competition in the sector, thus, originating the need to foresee means of resolving any conflicts that may result from the concession contracts. Such thought is deemed pivotal for the juridical security of the concessions regarding attraction of investments to the market sector. Not withstanding this economical and consumption relationship, such investment amounts swollen as they may be, cry for quickness in conflicts resolution in order to avoid financial losses and delays in strategically outlined plans for the oil & gas exploration.

Concerning concession contracts, on one side, the State part is represented by the government and its one-sided Judiciary Power. By the same means, the Federal Government acts upon the contracts, regulating over them and influencing on conflict resolutions. Possibly, public sector acting in a settlement or conflict resolution lawsuit may be temerarious. Willing to provide the investor with some reassurance in what it relates the success of his investment, the Petroleum Law and also Law n.º 11.909, legal document enacted in 2009 establishing procedures for the exploration of natural gas, have fostered the neoliberal tendency that has settled in Brazil since the 1990th decade, by promoting alternative methods of dispute resolution, especially in what concerns the public bids with the National Agency of Petroleum, Natural Gas and Biofuels ("ANP") and the consequent concession agreements.

Serving as a magnet for private entities to join the E&P, this government body has alerted the government of the need to modernize it legislative composition on issues like choice of jurisdiction and dispute resolution bodies, being a safety margin for the private investor.

In the legal scenario of regulation of agreements firmed with ANP the method of arbitration has been constantly developing its pertinence and importance. Law 9,307/96 foresees the due use of arbitration in Brazil. As is known, this mechanism unburdens the courts and gives the parties a rapid solution on disputes arising from their investments. Its use in the concession contracts for the exploration of natural gas, an increasingly used energy resource, is often made through the inclusion of an arbitration engagement clause. These clauses are binding, in a manner that both parties bond to this provision, the public and private parties (notably, in a prior or joint phase to the arbitration, the Judiciary may have subsidiary role).

Having already been, when in its formulation, inserted in the Petroleum Law, in article 43, X, the possibility of use of mediation and, if later required, being able to resort to international arbitration for the settlement of conflicts came in handy for the attraction of foreign investors. Unfamiliar with the Brazilian legal system, conflicts may be more feasibly resolved when analyzed by expert referees.

Besides bare-bones infrastructure and a favourable tax regime, the perspective of resorting to private international law aids in the protection of the capital invested. This new milestone in the regulation of the exploration and trade of this energy resource at national level is reasoned by strong pressure from investors, who felt the need to objectify the biddings standards and procedures, even with the provision of the opportunity to administer potential disputes through mediation and, subsequently, if suitable, by referees with detailed knowledge, bringing more efficiency and soundness for the concession.

This being, as well as in the referred law, the new rules on natural gas exploration (Law n.º 11.909/09), which regulates this activity that was already timidly addressed by the Petroleum Act, has in articles 21, XI, clear understanding as related to the specific mean of arbitration. While in the past few years natural gas has fastened to occupy a growingly important role in Brazil's energy grid, at the same pace legal authorities and private players realized the need to establish an independent regulatory framework. Worthy to state that agreements entered under the terms of the gas legislation are fairly comparable to those firmed under the terms of oil exploration concession, once both types of concession are governed by the ANP.

The provision of arbitration clauses for dispute resolution in gas trading agreements (art. 48) and transmission concession agreements admits arbitration for mixed corporations (government-controlled corporations) and state owned companies (as seen in the largely known case *Lage* – decided by the Federal Supreme Court). Today, it is commonly accepted the use of arbitration for these types of companies as they exercise business directed activities. The new legislation, therefore, promoted the drafting of art. 49 in the natural gas law, which sets forth that these companies may join the arbitration convention, outlined in concession agreements.

With focus on the new regulation of natural gas, regarding the growth of its importance at national level, it is indeed worth taking every possible measure to assure the effective and faithful compliance to agreements as to their merchantability and supply. The ultimate consumer must also be shielded against time-consuming contractual fights by the creation of agile mechanisms that will contribute to the enhancement of these services. In this context, there is no doubt that, under a legal point of view, the arbitration clause constitutes one of these mechanisms.

The perspective regarding the use of arbitration has been under constant development. The legislative boards have fabulously drawn permanent attention to this matter since then, modernizing conditions surrounding the natural gas trade. While the Petroleum Law had already fixed the inclusion of arbitration in concession contracts, the gas law has escalated continuously its appearance, for example, in art. 24, III, inserting this engagement clause in contracts firmed with the gas shippers. Authorities have successfully secured conditions for a smooth provision of the supply service, bearing in mind the concession unchains a network of activities and even a minor delay in any step of this chain may affect it as a whole. The law also underlines the arbitration possibilities in terms of the commercialization agreements, in article 48. This item,

valuably listed by this new legal instrument, had been omitted from the law that prescribed petroleum exploration services.

Essential for consumers and highly profitable for those exploiting it, this sector of industry is characterized, still, for the senior operational risks involved. Timing, maintenance, staff recruitment, thus, the assumption of labour charges and liabilities, this whole lot brings uncertainties on the actual return of investment. The formalization of joint ventures for the exploration of natural gas has been resorted to in the current concession agreements. Unlike in other economic sectors, competitors may join and employ collective efforts and become appointed for the E&P services owned by the state. Frequently, the formation of such joint ventures are intended to combine efforts so as to divide operational risks as well as to improve their respective portfolios of investments and their business strategies on a short, medium and long term. Exploratory agreements with private investors habitually require a considerable investment sum, which in a short term period, would be virtually impossible to be collected by the Government without leaving a deep wound in social directed policies. Arbitration is, in these cases, the less tiring and most effective mean of settling disputes, which arise, almost in every case, due to fixation of these partnership agreements. Arbitration norms are powerful tools of social control in order to guarantee the balance of the actions between the State and the deprived initiative, in the implantations of great projects

A contrary view would allege the unconstitutionality of the use of arbitration in such concession contracts, as they would address to inalienable law (public service granting). Nevertheless the Arbitration Law discloses in art.1^{st,} the exclusive use of this resolution mechanism for cases involving asset interest law, while natural gas concession agreements seek major profit as to justify its commercialization. As well as in the case of oil and, even, electricity, the trading of natural gas configures itself as an alienable right since the purchase and sale of gas is purely a commercial activity and alienable, transferrable to the ownership of another.

Such concession agreements relate to state-controlled services. The classification for these concessions in public service hall is underlined by art. 175 of the Brazilian Federal Constitution and clarifies itself in business perspective, leaving aside a political aspect. Based on this line of reasoning, lies an evaluated doctrinal understanding that the legal nature of these contracts, given their consumer targeted content, is fully commercial in which the concession process has become a mere step in a profit-seeking oriented plan. Natural gas or petroleum concession agreements have been increasingly worked on a private basis. Clever, also, it is to spot the similarity to constitutional norms cannot, however, conceal the fact that an investment made by a private party is sheltered by the contract. This comprehension has been following a progressionist world trend of fostering innovative and alternative tools of conflict resolution. The use of arbitration may clearly be very beneficial to serve collective interests.

The Government has increasingly concluding contracts with arbitration clauses on natural gas exploration based on recent court precedents, and, finds support in the binding effect of such clauses. It is the best manner of attracting the investor and, nonetheless, keeping the Government bond to the public service it has granted. It may well be spotted the non-violation of art. 5th, XXXV of the Federal Constitution

(indeclinability of the state jurisdiction), as the engagement clause sets forth a possibility, not an obligation. Any sort of coercion or intimidation will turn the contract void, with the constraining party being subject to court action. Nevertheless, the arbitral sentence duly ratified before Court has a judicial enforcement.

The recourse to arbitration mechanisms is pivotal for the welfare of the investor – State relation. State control is effectively granting hold of a money-making public asset and needs to observe legally enforced principles such as impersonality, publicity and concrete equality. The Government is looking for a business partner so weary judicial disputes among them can only pose obstacles. In order for the private investor to resolve controversies against the State it ought to be equipped with fairly competitive means, resulting in judicial celerity and avoiding procrastinating appeal arguments inflow as well as ensuring a reduced formality degree and broad negotiating power.

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