ARTICLES

THE LIFE CYCLE OF A LARGE INFRASTRUCTURE DISPUTE IN THE OIL AND GAS INDUSTRY

*Lucy Greenwood**

ABSTRACT

This article considers the life cycle of a large infrastructure dispute in the oil and gas industry and provides advice on each of the three main stages of a dispute. It discusses the types of dispute resolution clauses that are applicable to major energy projects and considers how to get the dispute resolution clause right. It then looks at the issues involved in managing a major energy arbitration, including the difficulties of arbitrator selection. Finally, it examines the options open to a party at the end of a dispute, after the arbitral award has been rendered.

I. INTRODUCTION

It is almost impossible to comprehend the scale of some of the projects undertaken across the globe in the acquisition of hydrocarbons. In the ultra deep water of the Gulf of Mexico, the subsea development in the Cascade and Chinook fields has the deepest production risers in the world.[1] These free-standing hybrid risers are each over 2000 metres in height from the sea floor. To put this in context, the Burj Khalifa, currently the tallest building in the world, stands at a height of 828 metres. One of the largest oil platforms in the world, the Olympus Mars B, is also located in the Gulf of Mexico. It weighs 120,000 tons, the equivalent of more than 300 Boeing 747s. It is taller and has more floor area than the Superdome in New Orleans. These mega projects can generate mega disputes which can play out in public, through the courts and within the sphere of investment treaty arbitrations, but are also frequently determined behind the closed doors of international commercial arbitration.

There are five main stages in an exploration and production project, beginning with the discovery of hydrocarbons and ending with the decommissioning of the field. The first stage, exploration, consists of locating oil and gas reserves using technology, shooting seismic[2] and drilling wells. If a discovery is made, sampling

* Chartered Arbitrator, qualified in England and Wales and Texas www.greenwoodarbitration.com. The author has over twenty years of experience in energy-related disputes, as counsel and arbitrator and hears disputes under English and Texas law.

[1] *See* Offshore-Technology.com, Cascade and Chinook Subsea Development, Gulf of Mexico, https://www.offshore-technology.com/projects/cascadechinook/.

[2] "Shooting seismic" or "seismic shooting" is "[t]he initiation of seismic waves in the rocks by the firing of an explosive charge at a known point." *See* Mindat.org, Definition of seismic shooting (accessed May 4, 2020), https://www.mindat.org/glossary/seismic_shooting.

will be undertaken to determine the nature of the hydrocarbons and the depth and drilling challenges they present. The company will then move onto the appraisal stage to conduct a detailed assessment of the discovery and to determine whether it is viable to develop. The third stage is development, in which wells are designed, production and processing facilities are identified. After successful completion of the development phase, the company will move to the fourth phase, production. Depending on the size of the find, production can last from a few years to over 40 years. Astonishingly, the McClintock No.1 well in Pennsylvania is still producing (albeit in tiny quantities) over 150 years after it was originally drilled. Finally, once production has declined to where it is no longer viable, the field will be decommissioned and the relevant infrastructure dismantled (if appropriate). Disputes, both large and small, can and do arise at every stage of a project. Risk management and appropriate planning in relation to the nature of any potential dispute and how it is going to be determined is vital.

This article will focus on a commercial energy arbitration. There are three main stages in the life cycle of a major infrastructure dispute: (i) laying the groundwork to ensure that if a dispute arises, it is conducted as smoothly as possible; (ii) managing the dispute; and (iii) moving on after the conclusion of the dispute.

II. LAYING THE GROUNDWORK

Often known as the "3 am" clause, the dispute resolution clause is one of the most important clauses in a contract, even though it occupies an antisocial timespot in negotiations. Get it right and you can select an appropriate forum for any dispute, identify a predictable governing law and give yourself the opportunity to select one of three decision makers who will determine the dispute. Get it wrong and you can find yourself mired in a complex and expensive jurisdictional challenge and/or facing proceedings in courts which are alien to you and under a governing law which may have severe consequences for contract interpretation. Once the heads of agreement have been agreed, then it is up to the lawyers to paper the contracts and to include an appropriate dispute resolution clause. There is a vast spectrum of contracts which may be required in the life of a major energy infrastructure project. Each contract will need its own dispute resolution clause, which must complement, where appropriate, other contracts with which it may interact.

A. *Selecting the Right Dispute Resolution Clause*

Although there is often a compelling argument to be made to the effect that simple dispute resolution clauses are to be preferred, complex projects usually require more complex dispute resolution clauses. For reasons of enforceability, neutrality and confidentiality, arbitration tends to be the dispute resolution mechanism of choice in most, if not all, major international commercial contracts. The AIPN (Association of International Petroleum Negotiators) provides a model international dispute resolution agreement for inclusion in oil and gas-related contracts. The model agreement contains three main approaches: (i) a simple

arbitration clause; (ii) a more detailed arbitration agreement consisting of the essential elements of an enforceable agreement to arbitrate, with a variety of options and alternatives to fit the nature of the transaction or project, as well as the special concerns of the parties; and (iii) a multi-step dispute resolution process culminating in arbitration.[3]

1. The Effect of a Multi-tiered or Step Clause

Multi-tiered dispute resolution clauses have become relatively common in the energy industry. This is largely because, as noted, disputes can arise at every stage of the project and therefore there is often a need to seek to preserve long-term relationships and secure ongoing cooperation where possible. A so-called "multi-tiered" or "step" clause can help this by requiring parties to go through one or more steps prior to being able to have recourse to an arbitral tribunal or court to resolve their dispute. The steps might include, for example, informal negotiations between company representatives; formal negotiations at a senior level; and formal mediation or conciliation proceedings, all of which must be concluded before a party has the right to arbitrate or commence court proceedings. Including such clauses may increase the chance of a dispute settling at an early stage in order to preserve the commercial relationship between the parties.

There are both advantages and disadvantages to including such clauses in contracts relating to major infrastructure projects. Including a reference to mandatory mediation or negotiation should, all else being equal, increase the chances of settling a dispute at an early stage or, at least, provide an opportunity to narrow the issues in dispute before formal proceedings are commenced. Further, the time scales built into the clause for each step may encourage the parties to cool off before issuing proceedings (after which positions invariably harden). One disadvantage is the fact that the additional steps, by definition, prolong the time taken to resolve the dispute; moreover, if additional claims are identified at a later stage of proceedings, the parties will have to go back and complete the initial steps in relation to these new claims. This will require the first arbitration to be stayed, or the parties will have to go to the trouble of convening a separate tribunal to determine a related issue.

It is difficult to predict with any accuracy at the contract stage the nature of any disputes that may arise, but on balance a tiered clause provides a party with more options. Its popularity in the market indicates that it is usually considered to be more beneficial than not.

There is some debate about whether pre-arbitral steps in a multi-tier dispute resolution clause constitute jurisdictional conditions which must precede the start

[3] *See* Association of International Petroleum Negotiators, Model International Dispute Resolution Agreement (published 2017), available for purchase at https://www.aipn.org/forms/store/ProductFormPublic/international-dispute-resolution-agreement. One might also choose expert determination and litigation in lieu of arbitration, but these options are beyond the scope of this article.

of any arbitration.[4] If those steps are seen as jurisdictional conditions and are not fully complied with then an arbitral tribunal would not have jurisdiction to hear the dispute. There are therefore risks if there is a failure to comply with the pre-arbitral steps in a multi-tier clause. The position will, of course, change depending upon where the dispute is situated.

2. Stages of a Multi-tiered Dispute Resolution Clause and Getting It Right

Possible pre-arbitration stages include requiring parties to negotiate informally; requiring parties to conduct more formal negotiations with senior representatives from the respective companies; building in a formal mediation procedure, usually with reference to established mediation rules; and possibly submitting certain technical disputes to expert determination. Only if no resolution is reached in any of the earlier stages will the parties submit to a formal arbitration procedure that will result in an arbitration award which will be enforceable practically worldwide.

a. Negotiation/Mediation

Where parties wish to incorporate a requirement that the parties negotiate prior to commencing arbitration, they must provide sufficient detail as to the scope of the requirement. The clause should set out (i) the time period for the negotiations; (ii) a trigger for the beginning of the negotiation period; (iii) the seniority level of executives at the company who will participate in the negotiations; (iv) how the negotiations are to take place (face-to-face or by telephone); and (v) provide an event that triggers the termination of the negotiation stage (for example, the expiration of the negotiation period).

Similar considerations apply in relation to a formal mediation step. If including a formal mediation requirement, parties should consider identifying a mediation institution in the clause and/or the mediation rules that will apply to the mediation. They must again set out a fixed time period for the negotiation together with clear events that trigger the beginning and end of the period. It is important to keep in mind that parties can always agree to extend a time period if, in their view, negotiations are progressing well. It is almost impossible to agree anything if negotiations are going badly. As a general point, drafters should avoid using indeterminate statements that require the parties to negotiate, mediate or conciliate "genuinely" or in "good faith," as this type of requirement is impossible to police and inevitably leads to acrimony.

Naturally the transition between each stage of the dispute resolution process must be clearly stated and to ensure that the steps are not considered binding jurisdictional conditions precedent, the clause should clearly say so, if that is what

[4] *See, e.g., BG Group PLC v. Argentina*, 572 U.S. 25 (2014) (in a dispute over conditions precedent to an international investment arbitration, a 5-justice majority of the Court decided a domestic litigation requirement was *not* jurisdictional; a 4-justice dissent disagreed).

the parties have agreed. Similarly, if parties want the steps to be mandatory pre-conditions then the clause should contain language to this effect.

b. Expert Determination

As part of the steps prior to arbitration, parties could also consider including an expert determination clause in their contracts. In highly technical contracts this can be a cost-effective alternative to arbitration or litigation before national courts. It is frequently used in construction contracts but could also be applicable in certain oil and gas-related contracts.

In essence, expert determination is where the parties seek a decision from an independent expert on a dispute. The decision can be contractually agreed to be binding or non-binding. Generally, the types of dispute that are suitable for expert determination involve single issues of a technical nature. It is therefore possible to identify potential technical issues that may arise and carve them out for reference to expert determination if disputes develop. The procedure to be followed by the expert will be entirely determined by the scope of the parties' agreement and this will also determine whether the parties are to be bound by the determination.

c. Arbitration

Most, if not all, major international energy contracts will contain a reference to arbitration as the mechanism by which disputes are to be finally resolved. The reference to arbitration will usually contain a reference to instutional arbitration rules, although it is possible to set out an *ad hoc* arbitration procedure in the contract itself. Arbitrations can be "administered" by arbitral institutions, or they may be "ad hoc,"—that is, with no reference to an institution. Most major oil and gas contracts will provide for an arbitral institution to administer the arbitration. The services such an institution will provide include assistance in selecting arbitrators, managing the file, addressing any challenges asserted against the arbitrators and assisting in relation to hearings and other case management issues. An unadministered arbitration will put much of the burden of this on the arbitral tribunal.

B. *Governing Law*

When it comes to selecting a governing law of an agreement, parties have an almost unlimited choice. English law is one of the most commonly chosen governing laws in commercial contracts, often, it is said, because it provides relative certainty of outcome in its application to the factual circumstances surrounding the agreement. English law is relatively certain for several reasons: it is well-developed and reasonably precise, there is a system of binding authority in place, so the same issue raised between different parties under a different set of facts should be decided in the same way, and there is a clear set of principles to be applied when a clause's meaning is disputed. For similar reasons the laws of Texas are often applied in oil and gas contracts.

C. *Seat*

The "seat" of the arbitration ties the arbitration to a legal system, the jurisdiction where the seat is located. This is true even if the arbitration hearings are held in a different country, the arbitrators and counsel are from different jurisdictions and the parties are based all over the world. The seat is essentially a legal fiction to give a structure to the arbitration in order to permit access to national courts to support and assist the arbitration process. The seat is only really important when things go wrong in an arbitration or in the event that an award is challenged in the courts of the seat after it has been rendered by the tribunal.

III. MANAGING THE DISPUTE

If a dispute arises in the course of a large infrastructure project—or, more likely, *when* a dispute arises—it is important to act quickly to protect the company's position. There are a number of practical considerations to address before either initiating or responding to an arbitration request.

A. *Practical Considerations before Embarking upon an Arbitration*

Prior to embarking on an arbitration, the obvious and not-so-obvious issues to be undertaken are: Above all, as discussed above, careful attention must be given to the detail of any mult-tier or step clause in the contract, particularly in relation to any time limits. All the pre-arbitral steps should be carefully documented prior to embarking on an arbitration. Even if there are no formal "steps," there may be issues with the formalities of any written notice required prior to issuing proceedings. On the Respondent's side, similar considerations apply in relation to any counterclaim. Clearly documents should be addressed at a very early stage to ensure an appropriate document retention policy is implemented and significant witnesses should be identified and interviewed. Any potential experts should be identified early and retained appropriately.

B. *Choosing the Arbitral Tribunal*

Most major infrastructure arbitrations will generally be decided by three tribunal members, one arbitrator appointed by each party and one chair. The chair will either be appointed by the co-arbitrators (with varying degrees of input from the parties) or by the relevant arbitral instution.

1. Selecting the Party-Appointed Arbitrator

There is surprisingly little information available when it comes to identifying potential arbitral candidates, although the situation is changing. When it comes to choosing an energy arbitrator, parties may be better informed than they would be in

other industries. The Energy Arbitrators List[5] was created by an *ad hoc* industry group in 2005 and is maintained by the International Centre for Dispute Resolution. The list was updated in 2014 and is currently undergoing a major overhaul. Arbitrators are selected for inclusion on the list by an independent review committee of industry leaders and legal experts based in the UK, US, Europe and South America. The database is searchable by country, region, and keyword, and it includes detailed information on arbitrator experience in 13 separate industry categories. These include upstream, downstream, and midstream contracts; petrochemicals; commodities trading; investor/state disputes; regulated utilities; and renewables.

Ensuring that you are appointing the right person for the job once you have identified potential candidates is, of course, a challenging issue. The fear of getting it wrong encourages conservative choices in picking an arbitrator, which may not always lead to the best result. If the "right" arbitrator for the case is one who is efficient, experienced, and diligent, then parties and counsel need to test that with both the arbitrator and with others who have experience with that arbitrator. Selecting an arbitrator is one of the most crucial decisions a party will make in an arbitration. The freedom to choose an arbitrator is one of the reasons why the parties chose arbitration to resolve their disputes in the first place. Arbitrators must ensure that they are providing up-to-date, accessible information on their experience and suitability for appointments to enhance their chances of being selected.

2. Selecting the Chair

Leading researchers in artificial intelligence are in universal agreement that the most important ingredient in any expert system is knowledge.[6] Expert knowledge cannot be taught. It has to be acquired over time. As Matthew Syed states, "good decision-making is about compressing the informational load by decoding the meaning of patterns derived from experience."[7] Good decision-making emerges through practice. The energy industry, with its particular challenges and nuances, is a field in which experience in deciding its disputes is arguably even more valuable. It is not simply about selecting an arbitrator who will understand the technical aspects of an energy dispute; it is also about having confidence that an experienced arbitrator can and will decode the evidence before them and discern patterns which lead to a better and fairer result. Almost every arbitration requires the interpretation of a contract and that is a transferable skill, but an arbitrator who has been steeped in industry disputes for a decade will bring an additional level of reasoning to the decision-making process. A chair, however, should not just bring industry

[5] *See* International Center for Dispute Resolution, Energy Arbitrators List, available at www.energyarbitratorslist.com.

[6] *See* MATTHEW SYED, BOUNCE: MOZART, FEDERER, PICASSO, BECKHAM, AND THE SCIENCE OF SUCCESS , 42 (2011) ("Programmes that are rich in general inference methods … but poor in domain-specific knowledge can behave expertly on almost no tasks," quoting Bruce Buchanan, Randall Davis and Edward Feigenbaum, artificial intelligence researchers).

[7] *Id.* Page 43.

knowledge to the tribunal. He or she must have significant case management expertise. Mega disputes require mega management skills.

C. *Arbitral Procedure*

A flexible procedure is the one tool available in arbitration that can radically alter people's perception of arbitrations. Innovative use of the unique flexibility of arbitration procedure could and should become a unique selling point for arbitrators. Arbitrators should become known for their ability and willingness to take a creative approach to timetabling, rather than reaching for the security of a well-tried and tested Procedural Order. Arbitrators should be promoting their speed in publishing the award following the hearing, and those appointing the arbitrators should be factoring this information into their decision to appoint the individual in question. In the small world that is international arbitration, it would not take long for arbitrators to become individually known for adopting a different approach during the procedural conference and parties should, increasingly, be looking for an arbitrator who not only is a good case manager but is also creative in attitude and approach.

IV. MOVING ON

Once the award has been issued, the parties will need to pause and review their options. Often the period immediately following the award is a fertile period for settlement of the dispute. Anecdotally, it appears that the vast majority of arbitration awards are either voluntarily complied with or settled shortly after the award is rendered. If any payment under the award is not made, parties will need to consider applying to the local courts of the seat and/or the local courts of the jurisdiction where the assets are located to seek to enforce the contents of the award.

This is where we find the real advantage of arbitration on an international stage. The United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, known as the "New York Convention"[8] was once described as the "single most important pillar on which the edifice of international arbitration rests."[9] It celebrated its sixtieth birthday last year. Of course, the New York Convention was not born with the 159 signatories it has today. Ten years after the New York Convention was concluded, only 32 countries had ratified it and it was not until the late 1980s that critical mass was close to being reached.[10] Now, out of a total of 195 countries in the world, 80% are contracting states.[11] It is this critical

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[8] Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 6, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 38 [hereinafter the "New York Convention"].

[9] J Gillis Wetter, *The Present Status of the International Court of Arbitration of the ICC: An Appraisal* 1 AM. REV. INT'L. ARB. 91, 93 (1990).

[10] *See* Lucy Greenwood, *A New York Convention Primer*, DISPUTE RESOLUTION MAGAZINE (Sep. 12, 2019) *available at* https://www.americanbar.org/groups/dispute_resolution/publications/dispute_resolution_magazine/2019/summer-2019-new-york-convention/summer-2019-ny-convention-primer/.

[11] *Id.*

mass that makes the New York Convention the most important weapon in an international arbitration practitioner's arsenal. The Convention itself is an unassuming document. It is only 5 or so pages long, encompassing 16 articles, yet it is single-handedly responsible for the prevalence of international arbitration as a dispute resolution mechanism across the globe today.[12]

The aim of the Convention is to ensure the enforcement of foreign arbitration awards worldwide. It requires contracting states to recognise and enforce foreign arbitration awards in the same way as domestic awards by, essentially, converting the foreign arbitration award into a judgment enforceable by the court. A further aim of the Convention is to ensure that contracting states uphold valid arbitration agreements by staying court proceedings commenced in breach of such agreements. Contracting states may make declarations when they accede to the Convention. The most frequently made declarations are to apply the Convention only to: (i) recognition and enforcement of awards made in the territory of another contracting State (the "reciprocity reservation"); and (ii) differences arising out of legal relationships that are considered commercial under the national law (the "commercial reservation"). Given the extensive global reach of the Convention and the commercial nature of the vast majority of international arbitration proceedings, neither reservation has much impact in practice.

There are a number of limited grounds upon which a party can resist the enforcement of an award against it. Article V of the Convention allows the party against whom the enforcement of an award is sought to challenge its enforcement.[13] It is divided into two sections, Article V(1), which allows the losing party to challenge the execution of the award on, essentially, the basis of a violation of its right to due process; and Article V(2), which does not protect the interests of the losing party per se, but allows the courts of a contracting state to deny enforcement on the grounds that permitting the award to be enforced would breach the public policy of the state.[14] As an arbitrator, it is important to be extremely familiar with the provisions of Article V(1) to ensure that the award cannot be challenged on one of the due process grounds listed.

In full, these grounds are:

> (a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or
> (b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

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[12] *See* New York Convention, *supra* note 8.
[13] *See* New York Convention, *supra* note 8, art. V.
[14] *Id*., arts. V(1) & V(2).

> (c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or
> (d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or
> (e) The award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.[15]

The diligent arbitrator will therefore always confirm the validity of the arbitration agreement under which they are appointed and will always ensure that notice has been given of their appointment and the proceedings (particularly important in the case of unopposed arbitrations). The arbitrator will ensure that the parties have been given an opportunity to present their case and acquaint themselves with any particularities of the law of the seat of the arbitration to make sure that the arbitration was conducted in accordance with local laws. Protecting the award at the challenge stage will, at the least, remove ground (e) from the options available to the party resisting enforcement. Defences to enforcement under the Convention are construed narrowly.[16]

V. CONCLUDING REMARKS

The sheer scale and complexity of exploration and production projects means that the spectrum of likely disputes is equally enormous. However, all arbitrations are born from an arbitration clause and it is vitally important to get this right. Everything flows from a good arbitration clause. The next most important issue is the selection of the arbitrator as this will significantly impact how the arbitration is managed. Finally, parties need to be clearly advised on their options once the award is rendered as it may be preferable to settle the dispute post-award rather than to go to the expense of seeking enforcement of the award against assets located in a different jurisdiction.

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[15] New York Convention, *supra* note 8, art. V(1).

[16] For the narrow construction of exceptions to enforcement in the U.S., *see, e.g., Parsons & Whittemore Overseas Co., Inc. v. Societe Generale De L'Industrie Du Papier (RAKTA)*, 508 F.2d 969, 973 (2d Cir. 1974) (public policy defense should be interpreted "narrowly").