
A Study of the Legal and Social Causes Requirements of International Oil Companies to Enter into Joint Operating Agreements (JOAs)

Nejad Ali Almasi¹, Sahel Aalikhani^{2*}

1. Professor Faculty of Law and Political Science, University of Tehran, Iran.
2. Ph.D. student of private law, Campus Kish, University of Tehran, Kish, Iran.

Article history:

Received date: 17 September, 2017

Review date: 22 October 2017

Accepted date: 16 November 2017

Printed on line: 28 February 2017

Keywords:

Joint operating agreement- parties-
operating committee- operator.

Abstract

In recent years, technologies have been developed which have made it possible to commercially develop vast quantities of petroleum and natural gas resources that were previously known to exist but which could not be commercially developed using conventional techniques. When the co-owners of petroleum and natural gas rights decide to use a joint venture structure, they typically enter in to a joint operating agreement (joa) to govern operations relating to the jointly owned petroleum and natural gas rights. A JOA is the constitution which the tenants in common that co-own the joint land right must adhere to for the duration of their co-ownership. Where it is held by several persons, the concession typically that those persons will be jointly and severally liable to the government for the proper performance of the terms of the concession. This means that government could, if it so wished, look to enforce the terms of the concession against any one the parties which are together the concession holders. The JOA reallocates the position of joint and several liabilities between the parties through provision that the party's liability inter se will be apportioned according to several predetermined share. The JOA typically relates to a single concession and applies in respect of petroleum operations in the area which is identified within that concession.

Please cite this article as: Almasi N A, Aalikhani S. (2017). A Study of the Legal and Social Causes Requirements of International Oil Companies to Enter into Joint Operating Agreements (JOAs). **Iranian journal of educational Sociology**. 1(2), 201-205.

* Corresponding Author e-mail: sahel.aalikhani@ut.ac.ir

1. Introduction

The present article aims to examine the nature of Joint Operating Agreement's (JOA) and its key features. The key features of JOA investigate that why influential players as international oil companies conclude these agreements. JOAs are usually made in capital-intensive resource industries by the companies intend to limit their exposure, particularly in limiting cost or liability. This contract helps financing, intelligence, access to market and access to project itself.

The normal form of association that creates the framework in which exploration for, and exploitation of, resources occurs is the JOA which is often seen as a form of joint venture. Since the structure of JOA is found in most contractual joint ventures, it can be considered the joint venture par excellence.

There are several factual scenarios for joint ownership of an oil and gas interest. The most common scenario occurs when owners of respective oil and gas leases put their interests together to meet a standard spacing unit that is legislatively prescribed. In addition, the economic risk of an unprofitable well is another frequent reason for joint ownership. Mineral depletion has obliged investors to drill deeper than ever before to obtain production. This type of drilling operation is expensive. These costs have encouraged even the largest companies to share the risk and cost of drilling with a joint investor. The best scenario to leverage these risks is sharing them through joint development agreements, the most common of which is the JOA. Several issues should be taken into account by investors or operators when entering into a JOA. A well designed JOA shall define each of these issues plainly and provide the individual requirements of the parties." The most conventional issues that should be defined include: who will be the operator, what acreage will be covered under the agreement, the production profit distribution, and division of the exploration costs among the parties. The parties of the JOA would be stuck in expensive and lengthy litigation if they fail to properly address one of these important issues. One oil and gas author has warned drafters by stating that the cost of correctly drafting "a thousand different agreements may be nominal in comparison to the cost to their client of a major deficiency" leading to litigation.

There is generally a standardized form for JOAs that is modified by the parties. The American Association of Petroleum Landman (A.A.P.L.) first developed a model form operating agreement in 1956. This standardized form was developed as an instruction for the lawyers involved in the development talks between operators and non-operators. The operator will be in charge of the day-to-day production while the non-operator will only share in the costs and profits from the production. Commonly, the operator is an experienced party in the oil and gas industry. Therefore, the operator in the JOA shall be granted extensive rights in production decisions. Typically, operators have a large financial investment in the development and production process. Thus, they will commonly make decisions that will be beneficial for both parties. The issue of duty arises between the parties when the interests of the operator and the non-operator diverge.

2. literature Review

JOA typically consists of two or more legal entities that share their property and expertise to establish a single business enterprise. In such enterprises, the parties have a joint proprietary interest a joint right to control and share profits and losses. Like a partnership or to the "Memorandum and Article of Association" of a company, a JOA also comprises the "constitution" which governs the joint venture. JOA is a specified project hence it is clearly defined and limited in scope. JOAs is typically specific that among the parties the relationship is one of the tenants in common and not one of partnership. A joint binding agreement or an area of mutual interest agreement (AMI) usually comes before a JOA; such agreement aims to facilitate co-operation between oil companies and prevents them from undertaking activities with

others. The area of mutual interest is often incorporated as a term of JOA. In addition, the limited scope of a JOA is essential for restricting the co-ventures' potential fiduciary duties.

JOA can only completely established when there is a degree of surrendering of control, that's why the choice of co-ventures is very crucial. The trust and confidence of other parties actually depends on the free choice of a partner; this is called *deflects personae*. JOA entails a durable relationship and a large number of financial contributions by each member, so the free choice of co-ventures is very important. JOAs set limitations on the sale of interests in the venture to outsiders. This type of *delectus personae* forms the basis of mutual trust and consequently increases the collaborative fiduciary relationship and corresponding fiduciary responsibilities on the co-venture. Additionally, the abilities and performance of each co-venturer is clear in this kind of participation in the management of the venture. Furthermore, the percentage of interests determines each party's rights to ownership and benefits, liability to cost, expenses and risks.

One of the feature of the joint venture is common ownership of assets; it strengthens the sharing of risk, makes the relationship closer. In an incorporated joint venture, the co-venturers own the corporation and, indirectly, the assets. It is while in a contractual joint venture, the assets are owned as tenants in common. A co-venturer has different proportional interest in the assets, and they arrange separate funding of its interest in the JOA, and also give security to its lender over its interest in the assets. Under JOA, co-venturers have interest in the mutual undertakings which form choose in action. The associations between the co-venturers and the *delectus personae* is amplified under jurisdictions where co-venturers agree not to partition their interest. A joint venture requires common ownership in which the parties contribute to the venture both in terms of services and finances which are used for production purposes. Thus, it creates mutual trust and guarantee the future contribution.

Concerning to other joint ventures than joint operating agreements, the Operator is generally recognized as the manager. An Operator is assigned by the parties to a JOA to act on the side of the joint venture. It is more efficient that one person performs the operations rather than each exercise its separate rights. The Operator's role is significant as it proposes budgets and plans and holds meetings. Also, the Operator plays the role of the agent in relation to third parties, including government liaison with the prior consent of the other parties. As a party to the JOA, the Operator has the liabilities as the other parties; i.e., its percentage interest share of joint obligations.

The committee has overall control on the joint operations within four stages: exploration, appraisal, development, and production. This committee is made up of co-venturers or their representatives. The majority usually makes decisions, and the percentage is specified in the JOA. A co-venturers voting right is in proportion to its interest. The committee has given the Authorization for Expenditure (AFE). The collaborative fiduciary relationship imposes fiduciary constraints on co-venturers in voting. Therefore, co-venturers should act honestly and in the best interest of the venture where such constraints apply. The courts determine this requirement based on the co-venturers' incentives.

When the operator in trust for the parties brings and interest for the parties or conduct a duty, the operator shall be subject to a fiduciary obligation. It is worth noting that a fiduciary relationship legally or practically affects the relationship of that other person. Therefore, the operator has the following obligations under the JOA: to disclose any personal interest that he may have in the property, account for the money invested, to exercise the account procedure in compliance with the principles of JOA, to protect and keep the property without misuse and finally not to misuse the information imparted.

In a JOA a project is funded by the operator making calls upon the co-venturers to increase their respective shares of the expenditure in compliance with the terms of their agreements. In case a party fails to fulfill a request and causes a default, JOA provides that non-defaulting parties take up the shortfall pro rata. There are a variety of sanctions that can be applied on the defaulter including loss of voting rights or of product rights and ultimate abetment or more drastically, forfeiture of its interest.

Joint ventures are rarely an association of equals. Therefore, it leaves enough space for conflicting views. "Sole Risk" and "Non-Consent" clauses are included in the JOA to avoid such disputes. A participant who has voted for a program but has been overruled by the majority and still wishes to proceed with the program represents the classic "Sole Risk" situation. The second situation where an opponent participant is reluctant to participate in the majority approved program-is generally referred to as "Non-Consent." These clauses intend to allow those co-venturers who want to continue with certain work to do so without opponents. A sole risk project effectively redefines the scope of the venture. The wells created under this clause fall into the scope of a sub-venture, the venture includes those who join in. So, a non-consent operation can also be treated as a sub-venture of a larger kind. The sole risk parties share the risk, costs, and rewards of the operation between themselves proportional to their interest in the sole risk venture. When such a venture is successful others can join upon paying a substantial premium, whereas under a non-consent venture late participation is possible with or without the payment of premium, depending on the provisions of the JOA.

3. Discussion

Joint venture incorporates an agreement between the parties for an enterprise developed for a single project, involving a sharing of project risk. In addition to the involvement in the management and control of the venture, the co-venturers' participation creates a common interest in the success of the project. The JOA is commonly used as a legal structure for natural resource exploration and development. There is common ownership of the property of the venture and input in its management. The venture is restricted to a defined geographic area as it puts limitations of the relationship between the co-venturers. The main difference between the JOAs and the joint venture is the possibility of sub-ventures formed through the sole risk and non-consent operations. JOAs are the contractual nexus that balance exploration and production expectation interests against conflict with a particular regulatory regime. Due to the flexibility of the JOA, it can be developed to meet expectations and goals of parties. It encourages exploration and development, while neither requiring a party to involve in inexpensive risk venture non-prohibiting a party from performing ventures when the requisite operating committee pass mark vote is not obtained. JOA provides the oil and gas industry with a flexible, well-written document to govern international oil and gas operations.

پژوهشگاه علوم انسانی و مطالعات فرهنگی
پرتال جامع علوم انسانی

References

- Bean G M D. (1995). Fiduciary Obligations and Joint Ventures. Oxford. PP: 3-4
Bean: Fiduciary Obligations and Joint Ventures. op. cit .at 12.
- Eyring H J. (1987). Comment, The Oil and Gas Unit Operator Duty to Nonoperation Working Interest Owners. Brigham Young University Law Review. 1293, 1294-1297.
- Forbes J R, S-Lang A G. (1987). Australian Mining and Petroleum Laws.2nd end, Sydney, pra.1907
- Hazlett G W. Drafting of Joint Operating Agreements. Rocky Mountain Mineral Law Institute, 3(1957), 277.
- Kunitz E.O.et al: Oil and Gas Law: Cases and Materials. St. Paul(MN),3rd end ,1999.622.
- Lowe J S. Oil and Gas Law. Eagan (MN), 3rd, 1995. 437-438.
- Maliss v. (1983). Bankers Trust Co, 717 F 2d 683.
- Smith E E. (1993). International Petroleum Development Agreement. Journal of Natural Resources and Environmental Law ,8, 62.
- Taylor M P. (1989). G-Winsor, P. P: The Joint Operating Agreement: Oil and Law. London.

