

# Obligations of Contractor in Iraqi Oil Service Contracts

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## **ABSTRACT**

*The oil contracts have adopted on a number of procedures to regulate the legal framework for the conclusion, begin with choosing foreign companies then negotiating to the agreed upon final contract and signing a contract by the competent authorities. After the contract is approved, it enters another stage which is the implementation phase. This phase manifest the certain rights in favor of its parties, as well as their commitment to the implementation of the duties and obligations specified in the contract. The aims of this paper is to discuss the types and nature of the most important obligations arise toward the contractor for oil service contracts conducted by Iraq after 2008 adopts an analytical approach legal deductive reasoning to conducting a profound analytical for those commitments*

**Keywords:** *Oil Contract, Contractor, Obligations.*

## **I. INTRODUCTION**

Once ratified and approved by its parties, a contract enters the implementation phase. This stage denotes the certain rights of the parties, and their commitment to exercising their duties and obligations as specified in the contract. The rights and obligations of the oil contracts vary depending on the nature of the contracts. Oil contracts have evolved since oil was discovered, and so did the rights and obligations of the foreign companies and the national party. Under a concession contract, the foreign companies have powers and wide rights particularly to explore, extract, and produce oils in all state lands that are under occupation. The length of the contract can stretch to seventy years compared to the simple rights of the national party.

After the liberation of most oil states from occupation, oil contract formula has evolved from a concession contract to joint contracts. In the latter, the rights and powers of the foreign companies are confined and the duration is reduced. Also reduced is the land area for investment and the nature of the obligations. The nature of the

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obligation placed on the foreign company has determined the establishment of the joint project with the national side in order to allow the producing countries to participate in the oil operations. Nevertheless, few criticisms have been directed to this type of contract, most notably regarding the control of foreign companies on the production rates and profits (Khilfe, 2013).

Other developments have evolved the oil contracts, where the rights of oil-producing countries have widened and increased the obligations owed by the foreign companies so as to create a balance between the rights and obligations of each party. Appeared were other types of oil contracts that specify the role of the foreign companies to carry out specific acts in accordance with the contract agreement without having the powers and wide rights (Hamid, 2014).

Oil contracts carried out by the Iraqi government after 2008 have been service contracts and were named the rounds of licenses. The contracts have been conducted with foreign companies who were selected from a specific mechanism by the Iraqi Ministry of Oil/Petroleum Contracts and Licensing. These foreign companies were given mandate to carry out specific actions agreed upon in the contract. The contracts determine the role of the foreign companies as a contractor, and it has been using the term contractor or contracting contract under the terms and conditions of contracts (Petroleum of Contracts and Licensing Directorate, 2012).

The evolvement of oil contracts in Iraq has raised a question: **What** are the characteristics and the nature of the obligations contractor (foreign oil companies) toward oil national companies in Iraqi oil service contracts after 2008? This paper aims to discuss the types and nature of the most important obligations contractor (foreign oil companies) conducted in Iraqi oil service contracts after 2008.

This study adopts an analytical approach of legal deductive reasoning. The analytical approach assists the researcher in conducting a profound analytical study for each part of the study (Mutaiota, 2008). It is not necessary for the researcher to merely deliver what is available; he or she has to analyze every part of the research in order to determine its features and defects. This allows the researcher to analyze the oil contracts, their respective features and conditions, and their legitimate nature. The study depends on both primary and secondary resources for data. The primary resources include oil contracts, Laws and constitution whereas the secondary resources consist of authoritative books, journals, Internet sources, and other related publications on this topic.

## **II. Obligation of contractor to carry out work agreed in the contract**

The contractor is not only legally obliged to carry out work that is incorporated in the oil contract but, they have to also exercise due diligence in the process (Al-Fadhli, 2009).

This is stipulated also stipulated in Article 150.1 of the Iraqi civil law that: *"must perform the contract, according to which its included and in a manner consistent with the dictates of good faith."*

All oil contracts signed by the national oil companies are subjected to Iraqi laws. The terms and conditions contained in the said contracts must also be consistent with the nature of oil contracts (Article 19 of the Oil Contract).

The obligations to implement the commitments in accordance with the general principles of the contracts are: the obligation to achieve a particular result or the obligation to exercise due diligence. For example, if the contractor's obligation is to construct a building, the contractor would not have fulfilled his obligation until and unless he has complete the construction of the building. In the case of the obligation to exercise due diligence, we can use the same example to illustrate this point. The contractor is obliged to ensure that the newly constructed building shall not have any major defects and is safe for use. Therefore, if the newly constructed building does not have any major defects and can be used safely for the function it was built for we can say that the contractor has exercise due diligence during the construction of the building (Al-Jubouri, 2007).

If the contractor is committed to complete the work in accordance with the terms and specifications contained in the contract (Albahja, 2008), and if the contract do not have the terms and conditions of the business to be implemented in explicit details, the contractor is committed to implement the contract by following the good practice standards of the industry and to achieve the result that meets the objective of the contract (Haddad, 2007).

For oil contracts, contractors are oblige to observe due diligence. In prospecting and exploration contracts, the contractor must ensure that they have trained and experienced human resources with the requisite expertise and the correct and proper tools and modern technical instruments that is necessary for the purpose of carrying out prospecting and exploration work. Immaterial of whether or not the prospecting and exploration work carried out by the contractor discover oil or not, if the above-mentioned good work practice is carried out properly, it would be difficult for the national oil companies to allege that the contractor did not fulfilled its obligations imposed by the terms of the oil contract.

On the other hand, if the contractor is committed to achieve a particular result as can be found in a development and increase-production contract, not only must the contractor complete the construction of the plant, it must also ensure that there is an increase in production. Thus, the contractor's responsibility does not end just because it has taken the necessary care and made the required effort, but it must achieve the result which is consistent with the contract (Aerara, 2011). Also, whether the oil contract requires the contractor to incorporate due

diligence when carrying out its work or if they are to complete the agreed work, they must complete it within the specific time that is stated in the oil contract (Mubarak et al., 2009).

In the oil contracts that were signed by the national oil companies in 2008 and beyond, the focus were on two types of commitments from the contractors. The first type involves the commitment by the contractor to prospect and explore for oil and gas in undiscovered fields (contractor need to exercise due diligence), while the second type involves the commitment by the contractor to develop and increase production in producing and non-producing fields that have already been discovered ‘contractor has an obligation to produce results’ (Licensing Directorate).

For the implementation of these works, the contractors must make plans, conduct studies, produce work programs and budget to cover the costs and expenses of all the work that must be carried out including exploration or up to the stage of commercial production. In the case of successful exploration operations in the non-producing fields or increase and development of production in the producing fields, the work must be completed within the periods specified in the contract and it must also comply with the approved practices in the oil sector (Article 1.9 of the Oil Service Contract).

On top of that, all the plans, programs and budgets together with the work carried out by the contractor will be under the control, guidance and participation of the Committee of Joint Management of the Fields. This committee is set up by the national oil companies and its members are drawn from the national oil companies and the contractor. The committee is responsible for managing the processes and general supervision on all matters relating to oil operations. The committee is also empowered by the oil contract to form a Joint Operating Body-and it acts as an operator. Its members are also drawn from the national oil companies and the contractor. The number of members from each party is determined according to terms of the contract. This body is responsible for the implementation of the agreed oil operations. The powers and duties of the Committee of Joint Management of the Fields and the Joint Operating Body is specified in the contract (Alfoada, 2012).

Based on the above, the commitment of contractor is determined according to the type and nature of the work agreed upon in the contract, such as carrying out prospecting and exploration work or the achievement of development and production increment. In order to successfully carry out their work, the contractors were committed to developing plans, programs of work and budget under the supervision and guidance of the national oil companies and through the formation of joint committees and joint operating bodies.

### **III. Obligation of contractor to spend on the oil operations**

Under the terms of the contracts, contractor have undertaken to bear the necessary expenses that will be incurred in the implementation of the oil operations. The specific time period and the specific amounts of money to be spent will be in accordance with the plans, programs and budget (Article 2.2.D of the Oil Service Contract).

There are several types of expenses that will be incurred by contractors after the contract the contracts they have signed becomes effective. The first type of expenses are called oil expenses (Article 1.63 of the Oil Service Contract) and it includes expenses necessary to cover the work of prospecting, exploration, evaluation, production and other activities associated with these operations. The second type of expenses are called complementary (Article 1.84 of the Oil Service Contract) expenses and it includes money spent on complementary works that is indirectly related to the implementation of oil operations. Examples of such type of expenses are: expenses incurred for the delivery of water to the workplace, expenses incurred for building an access road for the transportation of machinery and workers to facilitate oil operations or expenses incurred for the construction of infrastructures for the transfer of associated gas or crude oil and other works that complement the major oil operations. Both of these expenses (oil expenses and complementary expenses) will be paid to the contractor by the national oil companies after the oilfields have successfully started production or the production rates have achieved a pre-fixed target. The said expenses will be paid to the company in installments, and it will be discussed when we deal with the national oil companies' obligations.

Another type of expenses are non-refundable (Article 4 and 10 of the Oil Service Contract) expenses and as the name itself suggest, it means that the contractor is committed to spend the money without having the right to claim the expenses back the national oil companies. Examples of such type of expenses are: bonuses that are imposed on the contractor at the conclusion of the contract as bonus signature, bonus discovery or production as well as taxes imposed on the company's income and any other expenses not related to oil operations directly or indirectly.

### **IV. Obligation of contractor to notify and informing the national party**

The moment the contractor signs an oil contract they are obliged to notify and inform the national oil companies about everything related to the contracted oil operations and any other operations from the start of the contract date. The contractor will notify and inform the national oil companies by providing them with written reports and statements of operations. Through the use of this type of obligation the national oil companies are kept informed of the progress of contract operations (Haddad, 2007).

There are provisions in the oil which requires the contractor to provide to the national oil companies quarterly and annual reports. The reports must include information concerning the conduct of petroleum operations that are carried out (Article 15 of the Oil Service Contract), all data and samples obtained during oil operations such as geological and geophysical data as well as production rates and other reports and statements concerning the oil operations (Article 14.2 of the Oil Service Contract).

The goal of compelling the contractors to submit the quarterly and annual reports is to enable the government of Iraq to keep abreast of the conduct and progress of petroleum operations and the extent of the achievements (Alfoada, 2012).

## **V. Obligation of contractor to develop human resources and train national cadres**

Some oil contracts have clauses that require the contractors to to human resource development. To comply with this requirement the contractors build schools, install training and scientific centers or other facilities (Haddad, 2007). They contribute to social and economic development through the training of staff and national cadres and help them to raise their skills and knowledge (by helping them to acquire academic qualifications) so as to enable them to contribute their services to national industry (Alfoada, 2012).

One of the terms found in the oil contracts is that the contractor must give priority, when hiring, to the Iraqi cadres who have the relevant qualifications for the jobs (Article 26.1 of the Oil Service Contract). These companies, after consulting with the national oil companies must develop and implement programs to train national staff on all the various operations that is related to the oil industry (Article 26.4 of the Oil Service Contract). The oil contract also compels the contractor to allocate an annual sum of money to set up a fund to be used for training, research and scholarships and this fund is used for the purpose of development of national cadres skills in the oil industry and conducting scientific studies and research inside and outside Iraq (Article 36.3 of the Oil Service Contract).

## **VI. Obligation of contractor to relinquish land**

Under this term of the contract the contractor is obliged to reduce the land area that have been identified and agreed upon in the contract. The reduction may be gradual or all at once and it is after a period of time have elapsed as specified in the contract. As a result, the contractor's operations are limited to the actual producing fields and they are obliged to return the untapped areas to national oil companies (Alwan, 1982).

In the oil contracts signed by the Iraqi government, the relinquishment of land are from oil fields that have several oil-producing reservoirs, undeveloped discovered reservoirs and undiscovered potential reservoirs.

Therefore, the land to be relinquished is part of the reservoir itself and the land lies within the field that is subject of the contract (Alfoada, 2012).

It can be seen that under the terms of the contracts the contractors are obliged to relinquish land in favor of the national oil companies of Iraq and these land are part of oil fields or reservoirs that have been ratified in the plans and programs which the contractors have not developed or increased its production. The terms of the contract also covers the relinquishment of discovered undeveloped oil reservoirs where the contractor did not achieve commercial production or the relinquishment of the potential undiscovered oil fields. The time line for the relinquishment of the land to the national oil companies are specified in the contract (Article 5.1 of the Oil Service Contract).

## **VII. Compliance with Iraqi laws by contractor**

Contractor operating in Iraq are subject the laws and regulations of Iraq enacted by the Iraqi government (Article 19 of the Oil Service Contract). An important law that is directly applicable to contractor is Preservation of Hydrocarbon Resources Law No. 84 of 1985. This objective of the law is stated Article 1: *"First: This law aims to maintain the hydrocarbon wealth from damage, waste, and exploited it according to the bases sound scientific technically and economically.*

*Second: Hydrocarbon wealth means the crude oil, associated gas and derivatives. "*

This law includes a number of special articles relating to the maintenance of hydrocarbon wealth during the operations carried out by contractors or the national oil companies .The processes involved in prospecting and exploration for oil or gas involves drilling operations, extraction and production as well as the instructions for development of oil reservoirs and production, refining and manufacturing, warehousing and other operations that is related to controls in the oil sector (Law No. 84 of 1985).

Article 35 is about the rights of the contractor to use a portion of gas for the purposes of conducting extraction operations and production, provided that it is explicitly stated in the oil contracts but after approval has been obtained from the national oil companies as the law requires that all surplus gas becomes the property of the national oil companies (Article 11 of the Oil Service Contract).

Under the terms of the contract and subject to national laws, the contractors are required to have operational offices in Iraq at specific times as outlined in the contract (Instructions of branches and offices of the foreign companies No. 5 of 1989).

## VIII. CONCLUSION

It is clear that the oil contract binds all the parties to the contract. As a result, the contractor and the national oil companies will each have their own set of obligations as well as rights that is in favor of the respective parties after the oil contract is ratified and becomes enforceable.

Oil contracts concluded by Iraq after 2008 can be categorized as contracts for service. At that time, before an oil contract is signed the national oil companies will determine the type of specific work that needs to be done by a contractor. Once the type of work is identified the national oil companies will then conduct a tender exercise to select a contractor.

Under the terms of the contract, the contractor is committed to carry out a number of obligations and duties including the obligation to implement the agreed works in accordance with the conditions set out in the contract and to follow good standard practice of the industry so as to achieve the main purpose of the contract. Under the terms of the contract, the contractor will spend money to enable them to complete their work.

The contractor must notify and inform the national oil companies on all its operations by providing reports, studies and programs on the progress of the work., They must abandon the areas and territories where oil operations have not succeeded or that falls outside the actual areas of operation, as well as comply with to laws and regulations issued in Iraq and related to the oil sector. The contractor also out their operations diligently and provided training the national cadres according to terms of the contract.

Despite the fact that the oil service contracts conducted by Iraq after 2008 have raised an obligations towards each of the parties, which is considered a kind of balance in the contractual relationship between the national party and the foreign company, however there are some aspects or suggestions that can be recommended by the researcher:

1. legislate the oil and gas draft, which contributes to the determination and establishment the basis and rules of the oil contract according to nature of oil activity from exploration, extraction or production that the current contracts are draft proposed by the Department of contracts and licenses of oil in the Iraqi Ministry of Oil and subject to change with the existence of disagreement and legal controversy on the legal basis of contracts.

2. Add others conditions to the future contracts or to oil and gas draft includes guarantees for the national party to ensure its rights and subjecting them explicitly to Iraqi laws.



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