

# Understanding upstream Host Government Contracts

*Series no. 2 - Types of Host Government Upstream Contracts*

As mentioned in the previous article, the Host Government Upstream Contracts (HGUC's are classically grouped into three (3) types, namely;

- (1) Concessions or Licenses
- (2) Production Sharing Contracts
- (3) Risk Service Contracts.

In this article we are going to elaborate more on Concessions or Licenses





# Concession or License

A concession or license is an agreement by which the host government grants the contractor also known as a (Concessionaire/Licensee) the exclusive right to explore for and produce hydrocarbons in a given area of land for a certain period of time, in exchange for payment by the concessionaire/licensee of a royalty, typically assessed on production.

In early days of exploration and production, concessions were basically an arrangement in which the government transferred complete control and ownership of hydrocarbon reserves and the land surrounding it to a private oil company (usually an IOC) for longer periods of time, it could be even 70-90 years. All risks and rewards were borne by the IOC's in return.

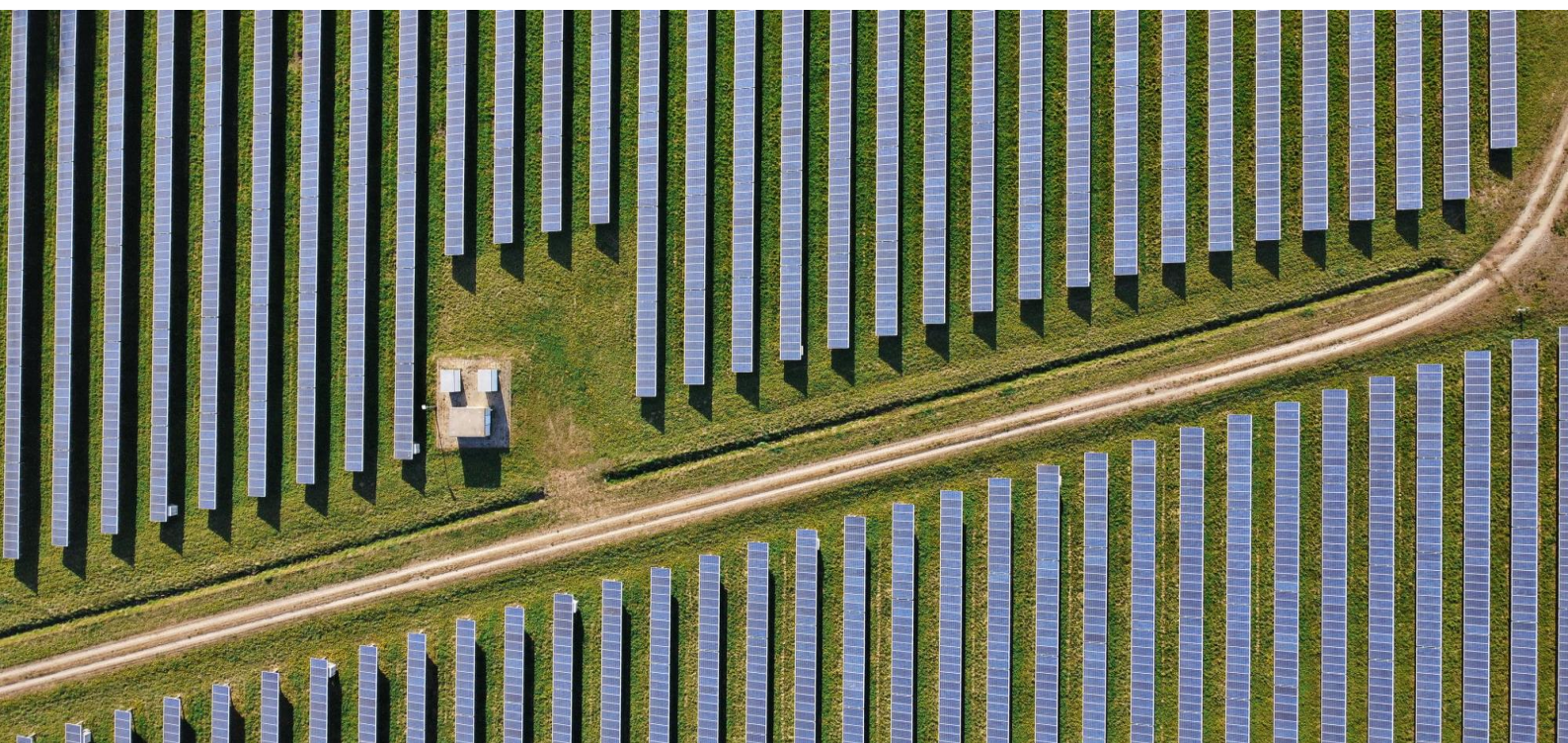
Permanent sovereignty of natural resources was declared in the year 1962 under the United Nations (UN); this drastically changed the nature and outlook on the concession type of contracts. This meant that national governments could take active part in Exploration and production (E&P) activities in with a concession or license agreement in operation, this is done through the country's NOC either by entering into a Joint Venture Agreement (JVA) or Joint Operating Agreement (JOA) with an IOC seeking to explore and produce in their respective country. As a result, the NOC as a government representative bears some of the exploration and production risks, particularly financial and rewards of the operations to the extent of its participating interests under the JVA/JOA.

Rights and duties of a contractor in Concession/ license; first and foremost, the contractor under this kind of agreement is vested with exclusive rights to explore for hydrocarbons in a specified area, to produce or develop any discovery found therein, take into possession of the oil and gas ultimately produced and free disposal of such production. Some governments issue a complete license for exploration and production but some do issue only an initial exploration license that upon commercial discovery thereof, an automatic production license will be granted to the contractor or apply for the same through appropriate host government agencies. Attention must be put to ensure that the contractor does not face any unnecessary encumbrances in obtaining the production license after initial exploratory activities; various examples of rights usually granted to contractors in kind of contract are vivid in the Danish 5th Round Model License, September 1997 as follows: 'The License confers upon the exclusive right to explore for and to produce hydrocarbons, as defined in section 1, within the area referred to under section 2.

Traditionally the early concessions' type of contract did not impose any obligation to the concessionaire apart from payment of royalties, that has long changed and now the contractors are required under many such contracts to submit a work program as a condition for retaining the licensed area, this will be followed by development plan to bring such plan to completion.

Consequently, with regard to issues of ownership and allocation of production under a License agreement, despite the fact that the contractor has an exclusive right to them, some contracts impose an obligation on them to supply the domestic market first under given circumstances.

Examples of countries that have adopted the concessions/licenses include the UK, Nordic countries led by Norway, Sweden and Holland, South America countries like Brazil; other includes Australia, New Zealand and etc.



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