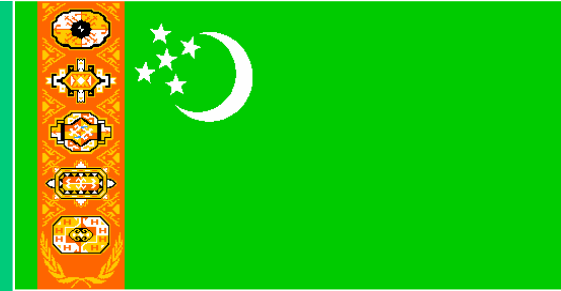


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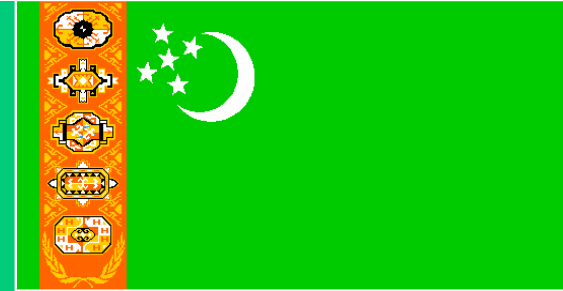
LEGAL ASPECTS OF INTERNATIONAL PETROLEUM TRANSACTIONS IN TURKMENISTAN

TIOGE-2004

By

Jeffrey I. Gordon and Serge A. Lomako

Mayer, Brown, Rowe & Maw LLP



APPLICABLE LAW

- International Treaties
- Laws of Turkmenistan
- Contract
- International Private Law
- Local and International Customary Rules
- Foreign Law



MULTILATERAL INTERNATIONAL TREATIES ENERGY CHARTER TREATY

- **Compensation in case of Expropriation**
- **Repatriation of Capital and Profits in Hard Currency**
- **Observance by Local Authorities**
- **International Dispute Resolution**
- **Energy Transit Protocol**



BILATERAL TREATIES

Treaty Between Turkmenistan and Great Britain On Protection of Investment of 9 February 1995

- Expropriation and nationalization is forbidden
- Restitution or adequate compensation
- Unrestricted repatriation of investment and returns
- International dispute resolution



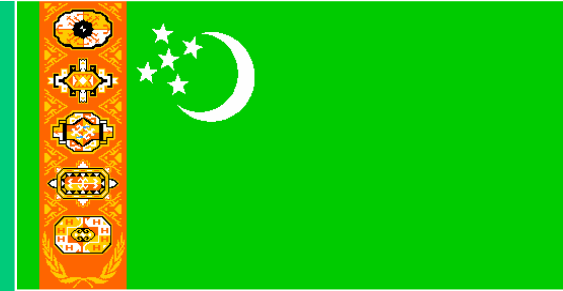
A SPECIAL LAW ESTABLISHES THE SYSTEM AND HIERARCHY OF LAWS OF TURKMENISTAN

- **Constitution**
- **Constitutional Laws and Laws adopted by Halk Maslahaty (Referendum)**
- **Laws**
- **Presidential Decrees, Decrees by Medjlis (Parliament)**
- **Decrees of the Cabinet of Ministers**
- **Acts by the Ministries and other Central Bodies of State Governance**
- **Resolutions by Khyakims (District or City Heads)**
- **Decisions by Gengesh's (Village Councils)**



KEY LAWS OF TURKMENISTAN USED IN THE PETROLEUM INDUSTRY

- Law on Hydrocarbons
- Civil Code
- Investment Laws
- Other Laws and Normative Acts, such as the Law on Subsoil and the Oilfield Development Rules



INVESTMENT LAWS

- Presidential Decree on Protection of Foreign Investment
- Law on Foreign Economic Activities
- Law on Investment Activities
- Law on Foreign Investment
- Law on Concessions
- Law on Enterprises



PETROLEUM LAW

Petroleum Law (1997 Law on Hydrocarbons)

**Presidential Decree 3189 (Establishment of the
Competent Body on Hydrocarbons; Model JVA; Model
PSA)**

**Law on Subsoil, oilfield operations rules, licensing
rules, other legal normative acts**



PETROLEUM OPERATIONS defined in Petroleum Law:

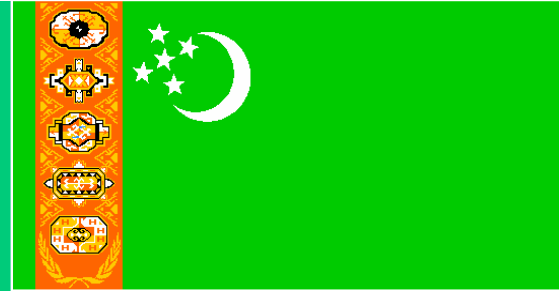
“All Exploration and Production Operations and related operations for treating, metering, saving, storing, marketing, delivery and transportation of Petroleum and its derivatives as well as other operations connected to the implementation of a Contract.”



TITLE TO PETROLEUM

Petroleum in its natural state in or upon the land in the territory of Turkmenistan is the exclusive property of Turkmenistan.

The quantity of Investor's entitlement share, as well as the place and time when title passes to Investor, should be stipulated in the contract.



GRANTING OF PETROLEUM RIGHTS

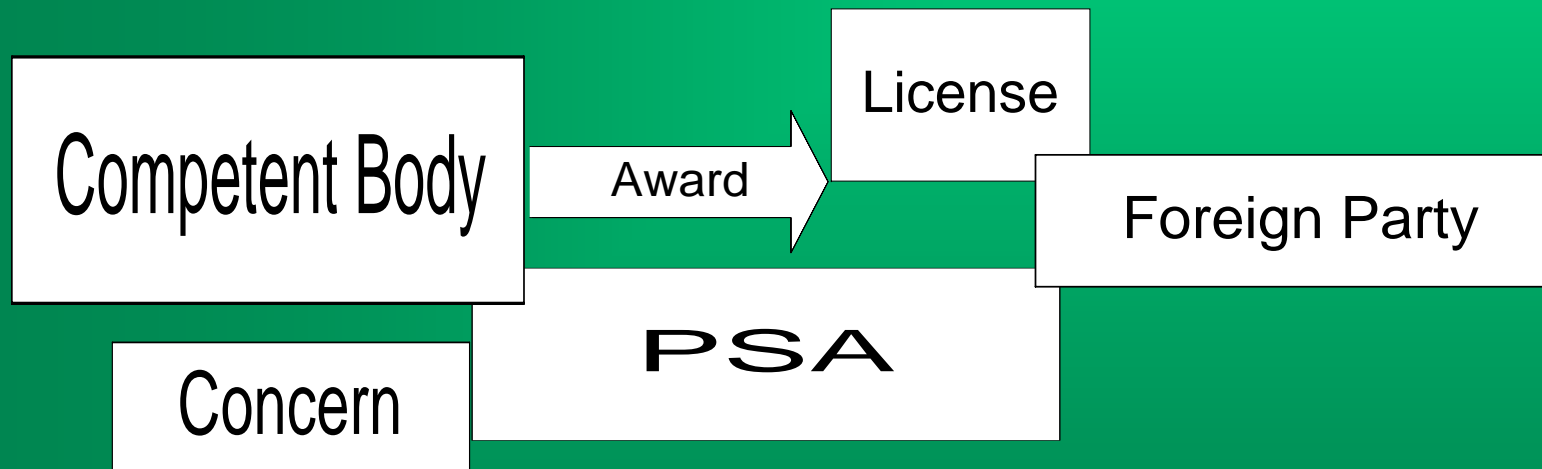
Petroleum rights are granted on the basis of a Joint Venture Agreement or Production Sharing Agreement, and a License.

The grantee may be a local juridical person, or a foreign juridical or physical person.

Foreign juridical persons must register with the State Agency for Foreign Investments (SAFI) before entering into JVA or PSA.

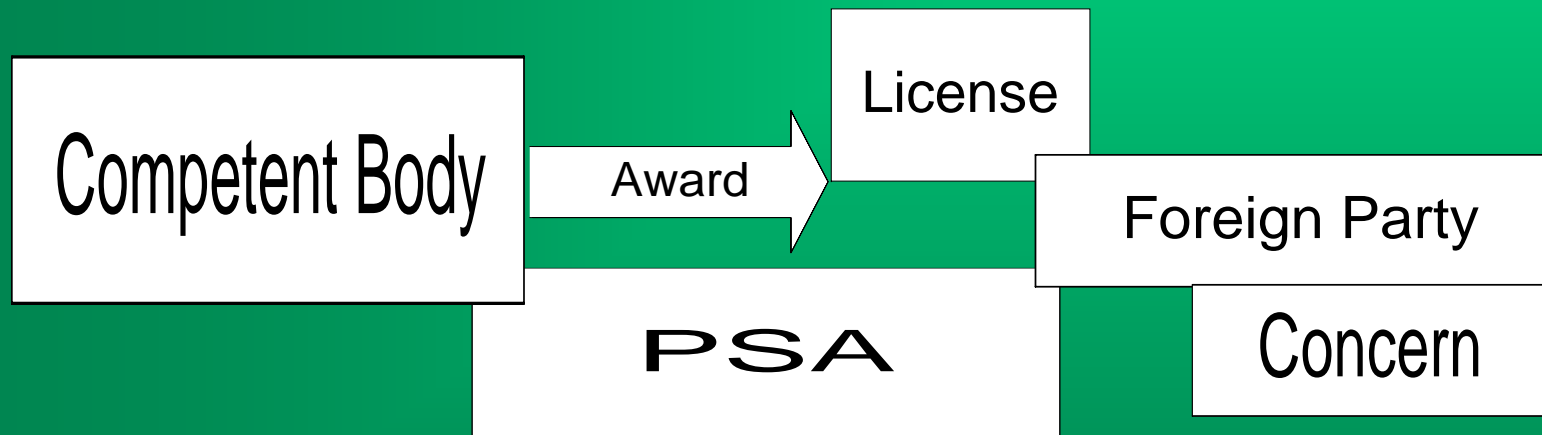


ACQUISITION OF PETROLEUM RIGHTS



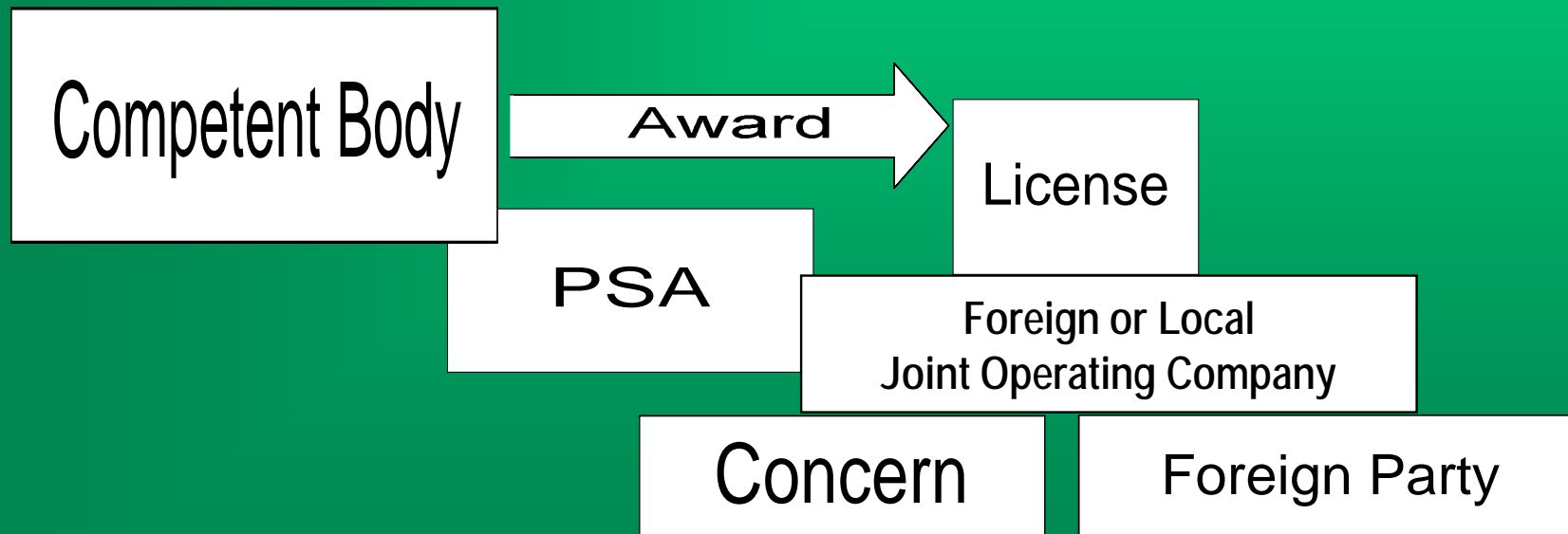


ACQUISITION OF PETROLEUM RIGHTS



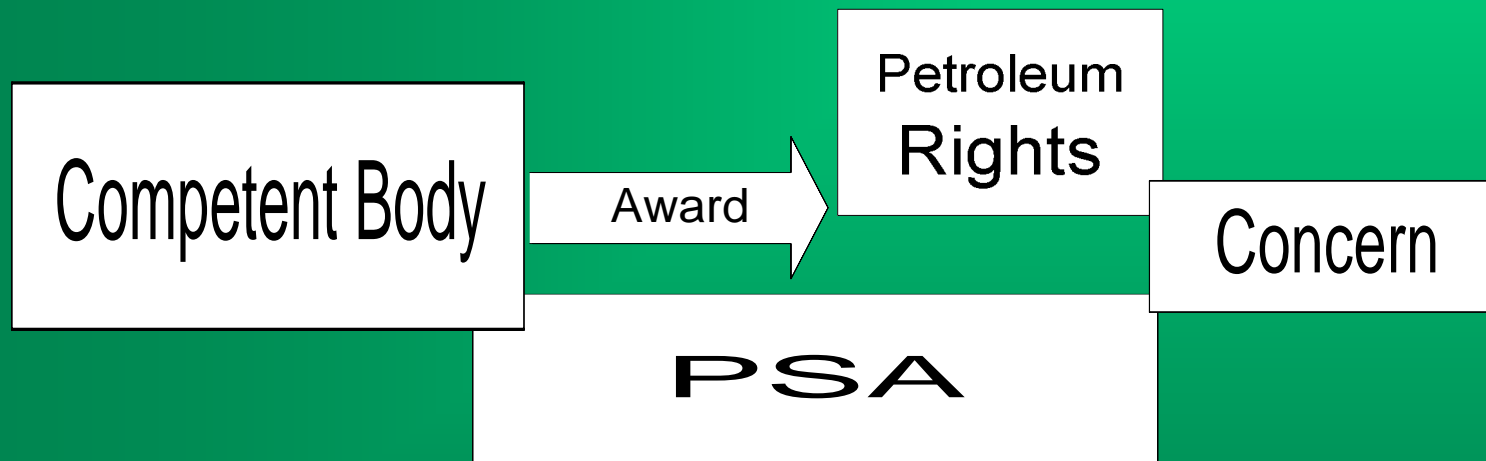


ACQUISITION OF PETROLEUM RIGHTS





ACQUISITION OF PETROLEUM RIGHTS





PETROLEUM RIGHTS

TYPES OF LICENSES

- Exploration License
- Production License
- Combined Exploration and Production License

PETROLEUM RIGHTS



Exploration License

- exclusive right to carry out Exploration Operations, valid for up to 10 years (six years initially, with the option to extend twice for two-year periods ("6+2+2" formula)).
- a commercial discovery in a particular area gives rise to the priority right to obtain a Production License in that area.
- does not prohibit small-scale production and sale (contract may provide for such a pilot-scale production and sale).

PETROLEUM RIGHTS



Production License

- exclusive right to carry out Production Operations in a specified area, sell or dispose of petroleum.
- valid for up to 25 years (20 years initially, with the option to extend once for five years ("20+5" formula)).
- Does not prohibit "exploitational exploration" (survey during the production operations, which can be provided in the contract);



PETROLEUM RIGHTS

Combined Exploration and Production License

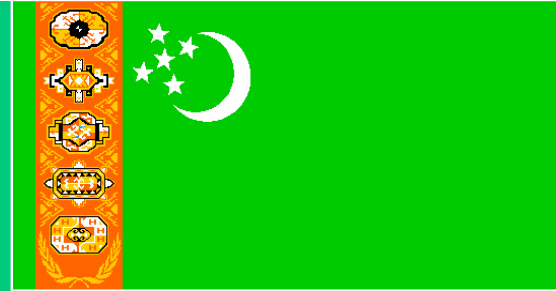
- Exclusive right to carry out Exploration Operations and Production Operations.
- Valid for up to 35 years (26 years initially, with the option to extend for nine years, subject to certain requirements)
- Normally, the Combined License term is considered as the succession of Exploration License and Production License; the granting authority would be reluctant to deviate from the term-extension formula, keeping it as follows: "6+2+2" (Exploration), then "20+5" (phase); the form of the Combined License, and the form Instrument of Extension can be suggested by the Foreign Party based on the model form licenses.

SUSPENSION OF LICENSE



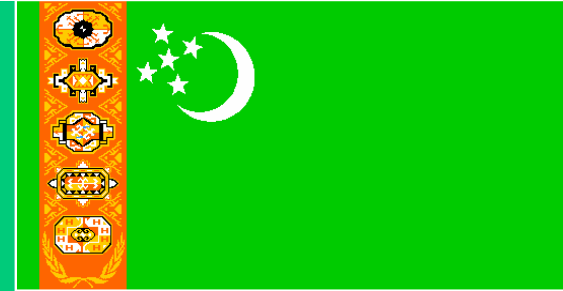
Suspension of License upon written notice from the Competent Body in the event that the License holder:

- conducts Petroleum Operations not provided for in the License
- carries out activities within the framework of the License, but not under the program provided for in the Agreement
- systematically violates Turkmen Law with respect to the protection of underground resources or environmental and safety regulations
- Reinstatement of License upon rectification
- Adjudication



Revocation of License by the Competent Body in the event that the License holder:

- fails to remedy the causes of any suspension within the fixed deadline
- is found to have deliberately submitted false information to the Competent Body which materially affected the Competent Body's decision to issue the License
- deliberately delays signing and registering the Agreement or commencing Petroleum Operations
- revocation of license renders the Contract (PSA, JVA) null and void
- No reinstatement of revoked License
- Still, adjudication is available



CONTRACT

Production Sharing Agreement

Joint Venture Agreement (not widely used)

Combination of PSA, JVA, and other types of contract

Service Contract



CONTRACT

Service Contract

- **No model form under Turkmenistan law**
- **Turkmenbashi Civil Code**
- **Industry regulations**
- **Local and international business practices**

CONTRACT



PSA and JVA

- Model Form under Petroleum Law
- Transferability of Foreign Party's interests
- Stability
- Governing law
- Freedom of Contract
- Investor's share not limited



CONTRACT: PSA and JVA

- Petroleum Law, Model JVA, and Model PSA were designed mainly for onshore oilfields
- Specificity of offshore oil, onshore gas, and offshore gas can justify substantial additions to the Model Form that can be suggested by the Foreign Party
- Gas clause is practically absent in the Model Form and requires substantial drafting
- Pipeline clause requires substantial drafting

CONTRACT: PSA and JVA



Production Sharing Agreement

Master and Servant

Servant owes fiduciary duties to Master

Joint Venture Agreement

Partner and Partner

Partner owes fiduciary duties to other Partner

CONTRACT: entry into effect



Production Sharing Agreement and Joint Venture Agreements become effective upon:

- **Execution of the Agreement**
- **Registration of the Agreement with appropriate State agencies (including those responsible for health and sanitation, environment, underground resources and Petroleum Operations) and**
- **Issuance of a License by the Competent Body to the Contractor**

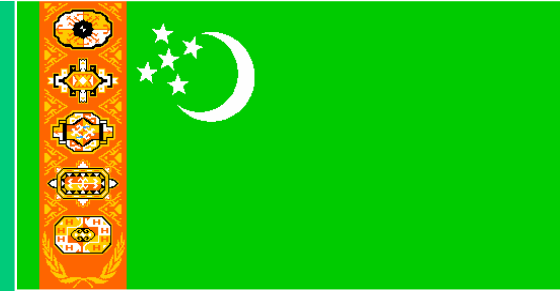
TAXES AND BONUSES



Contractor is subject to:

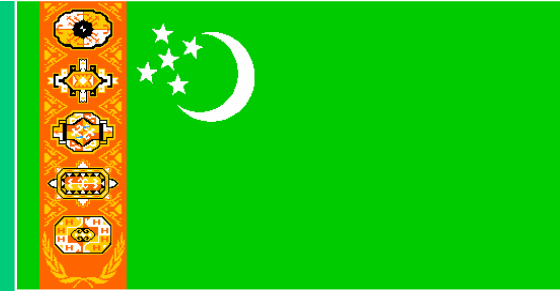
- a profits tax
 - at the rate established by Turkmen Law
 - Agreement will establish procedure for determining taxable profits
 - using international standards of accounting
 - employing hard currency as the monetary unit

CONTRACT



- under certain conditions, an enterprise is exempt from profits tax until it has recovered its initial investment
- production royalty
 - Agreement will determine rate
- bonus
 - Signing bonus
 - Production bonus

CONTRACT



PARTIES' SHARES: PSA and JVA

- Shares of the parties to PSA and JVA are determined by the contract, with due regard to existing practices;
- Contract may establish future modification of percentage shares of the parties, based on certain events like break-even point or commercial discovery;

FINANCING



Borrowing and holding foreign currency

- Foreign Party is entitled to maintain offshore bank accounts to hold only the proceeds of sale of Foreign Party's entitlement share
- No restriction on borrowing of hard currency by Foreign Party
- Revenue from sale of Foreign Party's entitlement share in petroleum is exempt from any future conversion requirement

FINANCING



Contract Security

- In general, Turkmen Law permits taking security over the following:
 - Immovable property
 - Movable property (including goods in circulation, such as hydrocarbons)
 - Shares
 - Subsoil and land use rights
 - Licenses
 - Agreements
 - Offshore bank accounts

FINANCING



Stability

- Legal and permitting regime
 - Agreement itself creates a stable legal regime by giving the Contractor contractual rights which cannot be unilaterally revoked
 - In the event of a change in law, a foreign investor may require that it be governed by the law that was in force at the time of its registration in Turkmenistan for a period of 10 years

FINANCING



- **Fiscal regime**
 - Taxes applicable to the Contractor are limited to those set forth in the Petroleum Law
 - No tax, duty, fee or other impost on profit derived from Petroleum Operations shall be levied on the Contractor or its shareholders beyond those anticipated in the Agreement



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