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# Oil Regulation

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# Chile

## Alvaro Araya and Matías Novoa M

Novoa & Araya Abogados

### General

- 1 Describe, in general terms, the key commercial aspects of the oil sector in your country.

The hydrocarbon sector plays a crucial role in the Chilean energy network. According to the National Energy Commission (CNE), the net hydrocarbon consumption accounted for 55 per cent of primary energy consumption in 2009: oil and oil products reached 43 per cent, while natural gas corresponded to 12 per cent.

Ownership of hydrocarbon deposits is granted to the state by the political constitution. An important feature of the Chilean oil sector is the potential and actual access of the private sector to explore and exploit crude oil (upstream) and to refine crude oil and distribute products (downstream). The structural reforms in this market began in the late 1970s, when regulation allowed the state to exercise its right to exploit oilfields not only through the state-owned company Empresa Nacional del Petróleo (ENAP) but also through administrative concessions granted to private companies, or special oil operation contracts (CEOPs) to be executed with private companies. Then in 1978, the distribution segment was liberalised, as well as the import and export of oil and oil products. Eventually, full pricing freedom was established in 1982. As a result of these reforms, private companies entered in association with ENAP in the upstream sector, while new market entrants took part in the product distribution sector.

### Upstream

In this segment of the industry, ENAP has played a major role since until 2000 it was the only company that produced and refined crude oil in Chile. The exploration and production of crude oil in Chile is concentrated in the Magellan Basin (in the extreme south of the country), in three geographical areas: continental, Tierra del Fuego island and offshore (Magellan Straight). The major part of crude oil and natural gas exploitation has been carried out in offshore fields since the late 1970s. However, crude oil production has fallen significantly over time, going from 2.4 million cubic metres in 1981 down to approximately 0.2 million cubic metres in 2011.

As mentioned above, the private sector may participate in this segment through administrative concessions or CEOPs. In practice, private companies have been allowed to participate in hydrocarbon exploration and exploitation activities in Chile exclusively through the CEOP mechanism. The CEOP is a binding agreement between the state of Chile and a private company or consortium of companies (a contractor) that provides for the exploration and exploitation of hydrocarbon deposits at the contractor's risk. The CEOP also establishes the applicable legal framework for the exploration and exploitation activities including, among others, a special tax regime, as well as the exploration and exploitation phases and their durations, the minimum investment obligations and the compensation of the contractor in case of exploration success, in cash or in the form of a share of the production that is transferred to the contractor for

its own marketing. The first CEOP in Chile was the Golfo de Penas CEOP signed in December 1977 with two US-based companies, Arco and Amerada Hess. By 2011, a total of 31 CEOPs have been signed. Currently, there are 11 CEOPs in execution in the Magellan Basin (nine of them executed after an international bid process launched by the Chilean government in 2007), plus other five new CEOPs in Magellan that will start during 2012 after being recently awarded, and three in other locations. No major hydrocarbon deposits have been discovered so far.

Despite the exploration efforts, domestic oil production is of almost no importance (1 to 2 per cent of country oil demand), being the demand for the vast majority of domestic consumption met by imports. This is due not only to a steady decline in domestic production but also to a significant increase in fuels consumption from the second half of the last decade.

### Downstream

In the refining sector, domestic production is conducted exclusively by ENAP through its refineries, supplemented with imports supplied by ENAP and certain wholesale distributors. ENAP's plants (Biobío Refinery and Aconcagua Refinery, near the most populated central region of Chile, and Gregorio Topping for local usage in Magallanes) serve approximately 85 per cent of the oil products' domestic market, yet having capacity enough to serve 100 per cent.

In the storage sector, the dominant company is also ENAP. However, there are several other companies that have their own storage capacity, such as Copec, Shell/Luksic and Petrobras. In total, in 2007, the storage capacity in oil terminals, liquid fuels and liquefied gas was about 3.3 million cubic metres (35 per cent crude oil, 7 per cent liquefied gas and 58 per cent for clean and heavy products).

When it comes to the transport of crude oil and refined products, Sonacol plays the leading role in the central regions of the country, using a pipeline network. Sonacol is owned by the main distribution companies and ENAP. There is another pipeline connecting the Biobío Refinery with storage facilities in San Fernando, which is also owned by ENAP. Thus, in practice, over 70 per cent of the refined products for the domestic market are transported through the pipeline network located mainly in the central region. This network, not counting the existing networks in the Magallanes area, totals 825km in length. Besides such networks, Chile has an extensive network of pipelines and other lines in the Magallanes area, both onshore and offshore, which allows the transport of crude oil from the fields to storage facilities, where it will be locally refined or shipped to the central region. In the rest of the country the supply is met by shipping. In addition to Sonacol transport capacity, distribution companies have fleets of trucks to ensure fuel supply in areas far from ports and/or pipelines. Besides, according to the CNE, there are 34 oil-related marine terminals distributed throughout Chile, but mainly located in regions not served by pipeline systems (northern and southern sides of the country). Finally, there is a pipeline between Chile and Argentina opened in early 1994 with an hourly pumping capacity

of 750m<sup>3</sup> and a length of about 220km, owned by privately held companies and ENAP in both countries. For more than 11 years, Argentina exported crude oil to Chile, but in early 2006 oil deliveries were indefinitely suspended.

With regard to the distribution sector, a small number of private companies commercialise both ENAP's domestic production and imported products. As mentioned above, the liberalisation of wholesale distribution in 1978 and retail distribution in 1982 sought the entry of new companies to the industry and an increase in competition between them. However, the structure of the liquid fuel market has not changed significantly since then, given that existing companies (Copec, Petrobras, Shell/Luksic and Terpel) have a market share over 90 per cent and they are also vertically integrated into the storage and transport markets.

In addition to the publicly available information provided by the Ministry of Energy, the National Energy Commission and Empresa Nacional del Petróleo, the main source of the industry information included in the foregoing paragraphs was the article 'La Industria del Petróleo en Chile' published by professors Agostini and Saavedra (Estudios Públicos 114, Otoño 2009).

- 2 What percentage of your country's energy needs is covered, directly or indirectly, by oil as opposed to gas, electricity, nuclear or non-conventional sources? What percentage of the petroleum product needs of your country is supplied with domestic production? What are your country's energy demand and supply trends, especially as they affect crude oil usage?

As aforementioned, the hydrocarbons sector plays an essential role in the Chilean energy network, accounting for 55 per cent of primary energy consumption in 2009. Energy demand grows at an average of 6 per cent per year, mainly caused by the development of big mining projects.

Therefore, Chile presents a high degree of dependence and vulnerability with regard to energy derived from hydrocarbon sources. The dependence is aggravated by the rising of imported oil prices, a severe natural gas supply shortage resulting from restrictions imposed by Argentina and the irregularity of hydroelectricity, the main source of power generation in Chile. In addition, according to the experts, the country must duplicate its energy production in the next 10 to 15 years, in order to meet the anticipated growth of demand for electric power.

According to recent changes in electricity laws that regulate power generation, a minimum percentage of generation will have to be obtained from non-conventional sources. Nowadays non-conventional renewable sources account for nearly 3 per cent of electric generation, and by 2024 it is expected that they will represent at least 10 per cent of power generation.

- 3 Does your country have an overarching policy regarding oil-related activities or a general energy policy?

The government's declared energy policy focuses on promoting the security, efficiency and sustainability of the energy supply, mainly by establishing sound and stable regulations to provide the right incentives for the private sector to carry out and make the bulk of the necessary investments.

In furtherance of the above, the government has pursued by means of medium- and long-term strategies to diversify the energy matrix (in terms of both fuels and suppliers); achieve greater energy autonomy; and encourage a more efficient and intelligent energy use through policies that promote the development of traditional power generation sources, and the use of alternative renewable energy sources, such as geothermal, solar, micro hydroelectric, wind and biomass projects, and liquid biofuels, such as ethanol and biodiesel.

Nuclear generation facilities are also being considered as a possible long-term alternative.

However, so far those strategies have not been proven to be effective. Regarding fossil fuels, Chile has opened bidding processes to award oil exploration contracts in Magallanes to enhance oil discovery, but only on a small scale.

#### Regulation overview

- 4 Describe the key laws and regulations that make up the general legal framework regulating oil activities?

The Chilean political constitution reserves for the state the 'absolute, exclusive and inalienable' ownership of hydrocarbon deposits, pointing out that the exploration and exploitation of those can be carried out either directly by the state, by its companies (ENAP) or by means of administrative concessions or by CEOPs.

CEOPs are regulated by Law Decree No. 1,089 of 1975 (DL 1,089). CEOPs are signed between a local or foreign investor and the Chilean state. These contracts do not affect state ownership over the hydrocarbons reservoirs. Instead, the investor assumes the exploration risk and may receive compensation in cash or in kind (the oil discovered), with a 50 per cent maximum income tax rate.

ENAP is regulated by its Organic Law, Law No. 9,618 of 1950, which grants ENAP the right to explore and exploit hydrocarbon fields without an administrative concession or a CEOP. Additionally, the law acknowledges to ENAP certain legal prerogatives in order to impose easements or right of way to third private parties. Law No. 9,618 authorises ENAP to develop its legal purposes, directly or through other companies in which it may participate.

Liquid hydrocarbon import, transportation, storage and marketing is subject to a number of specific technical regulations regarding safety, quality and other matters, including Supreme Decrees (issued by the Ministry of Economy) No. 160 of 2009 (the Safety Code for Facilities and Production and Refining Operations, Transportation, Storage, Distribution and Supply of Liquid Fuels) and No. 310 of 1983 (the Safety Code for Rail Transportation of Liquid Fuels); and the Decree having Force of Law No. 1 of 1978 (DFL No. 1), issued by the Mining Ministry, that provides that any importer of liquid fuels must be previously registered in a register kept for such purpose by Superintendence of Electricity and Fuels (SEC).

In addition, hydrocarbon marine terminals can only be installed with a maritime concession granted by the Ministry of Defence, in accordance with Decree-Law No. 340 of 1960 on maritime concessions and Decree No. 2 of 2006 the Ministry of National Defence.

At present, the decommissioning regime of oil facilities is governed by the CEOPs provisions and the government environmental approval (under the environmental impact assessment system). Since November 2012, CEOP contractors will be required to submit a special decommissioning plan to the National Geology and Mining Agency (Sernageomin), establishing the procedures, obligations and guarantees before the state.

In terms of international regulations, it should be noted that Chile is a signatory state to the Substitute Protocol of the Eighth Additional Protocol to the Economic Complementarity Agreement No. 16 between Chile Republic and Argentina Republic (ACE 16) Regulation for Marketing, Operations and Transportation of Hydrocarbons Liquids – Crude Oil, Liquefied Gas and Liquid Products Of Petroleum and Natural Gas and the following international conventions: the International Convention for the Prevention of Pollution of the Sea by Oil of 1954, the Convention on the Prevention of Marine Pollution by Dumping of Wastes and Other Matters of 1972 and the International Convention on Civil Liability for Oil Pollution Damage of 1969.

- 5 Identify and describe the government regulatory and oversight bodies principally responsible for regulating oil activities.

In general, it can be said that the Ministry of Energy and the National Commission of Energy (CNE) are the main entities in charge of the issuance of policies and regulations for the oil sector, while the supervision of and compliance with such regulations are within the responsibilities of the Superintendency of Electricity and Fuels (SEC). On the other hand, the Ministry of Environment and the Superintendency of Environment are the entities responsible for environmental matters (with respect to all activities including oil) and the Ministry of Defence is the authority responsible for maritime concessions (in relation to maritime oil facilities).

#### Ministry of Energy

The Ministry of Energy has the responsibility of developing and coordinating the plans, policies and regulations for the proper operation of the energy sector, supervising its performance and advising the government in all matters related to energy. Furthermore, this ministry coordinates the different entities related to energy in Chile, including those in connection with oil and refined products. The Ministry of Energy is, by law, the chairman of the board of directors of ENAP.

#### National Commission of Energy (CNE)

According to its Organic Law (DL No. 2,224 of 1978), the CNE is a technical entity in charge of analysing price, tariff and technical regulations for the companies dealing with energy production, generation, transportation and distribution, in order to have the most secure, reliable and efficient energy system. It is an independent agency, which reports to the president through the Ministry of Energy.

#### Superintendency of Electricity and Fuels (SEC)

The SEC Organic Law (Law No. 18,410 and Law No. 19,613) states that such entity is in charge of the compliance with all regulations related to generation, production, storage, transportation and distribution of all fuels, gas and electricity. The SEC has the authority to impose fines and, if necessary, to take over the administration of deficient services, at the expense of the concessionaire, when applicable.

In relation to upstream activities performed through CEOPs, the Ministry of Energy – on behalf of the president of the Republic – is the authority in charge of the enforceability of the applicable regulation. In addition, in the specific case of these contracts, the CNE, the Ministry of Finance and the Central Bank also participate in those CEOP provisions regarding issues such as energy, taxes and foreign exchange, respectively. Finally, a coordinating committee, formed by representatives of the state and of the contractor, will supervise the implementation of the CEOP according to the conditions, terms and dates agreed upon by the parties.

#### Ministry of Environment and the Superintendency of Environment

With regard to environmental issues, the relevant authorities are the Ministry of Environment and the Superintendency of Environment. The Ministry of Environment is, in general, responsible for the protection and conservation of biological diversity and renewable natural resources and water resources, promoting sustainable development and the integrity of environmental policy and regulations. The Superintendency's main responsibility is to monitor compliance with the obligations contemplated in the resolutions approving environmental impact assessments, as well as compliance with government plans to prevent environmental damage or to clean or restore contaminated geographic areas, for all economic activities, including those related to oil and refined products. However, the scope of faculties of this Superintendency will be somewhat limited until the special law regulating environmental courts is passed.

#### Ministry of Defence

The Ministry of Defence, through its maritime undersecretary, is the granting authority of the above explained maritime concessions granted in order to install and operate facilities or terminals for receipt of oil or oil products.

- 6 What government body maintains oil production, export and import statistics?

Traditionally, information about the industry has been produced and processed by different entities, including the Ministry of Mining, CNE, SEC, the National Statistics Institute (INE), the Central Bank and also ENAP. At present, given the creation of the Ministry of Energy (early 2010 in accordance with Law No. 20,402) and the consolidation in this new entity of the powers previously exercised by the Ministry of Economy and the Ministry of Mining, the oil statistics will be kept by this new Ministry. In fact, Resolution 2176/2009 of the Ministry of Mining (now replaced in these issues by the Ministry of Energy, as explained) regulated the formats through which the CEOP's contractors must submit to the Ministry the economical and technical information that must be submitted in compliance with their respective obligations under the CEOP.

#### Natural Resources

- 7 Who holds title over oil reservoirs? To what extent are mineral rights on private and public lands involved? Is there a legal distinction between surface rights and subsurface mineral rights?

As explained above, oil reservoirs belong to the state of Chile. Apart from ENAP activities, the government participates in the oil sector mainly by the execution of CEOPs, signed between the local or foreign investor and the state in order to carry out exploration and production in specific oil or gas fields. These contracts do not affect state-ownership of the fields due to the fact that these are not concessions, but instead they grant certain relevant rights and benefits to both parties. The investor gets retribution in money or in kind (hydrocarbons), subject to common taxation (at a maximum income tax rate of 50 per cent) and is able to export the hydrocarbon it has received in payment, with prior government authorisation. The state has the right of purchase in return, paying the contractor a price predefined in the CEOP.

Under Chilean law, the owner of the surface lands has no rights over the minerals found under the surface of the lands. Mineral substances and hydrocarbons can only be exploited either by a concession (judicial concession in the case of mining and an administrative concession in the case of hydrocarbons) or by a contract with the state (in the case of hydrocarbons), and in both cases are subject to special taxes or royalties payment. Conversely, the subsurface mineral right does not generate any surface right, except the right to impose legal easement and rights of way.

- 8 What is the general character of oil exploration and production activity conducted in your country? Are areas off-limits to exploration and production?

About 15 per cent of the exploration and production is offshore, the remaining is onshore. All areas may be explored, but regulations establish some restrictions on special areas devoted to national parks, forests, border regions, shores, etc. According to the constitution, the president of the republic is entitled to terminate, at any time, without expressing the cause, but granting the corresponding indemnification, those administrative concessions or special operation contracts related to exploration in areas which have been declared of importance with respect to national security.

As a general rule, it can be stated that oil activity is not banned at any place, but some regulations make it physically or economically unfeasible because of the severe restrictions or high costs involved in complying with them.

**9** What government body regulates oil exploration and production in your country? How are rights to explore and produce granted?

As explained above, the Ministry of Energy is in charge of executing CEOPs with private investors interested in crude oil exploration and production in specific fields. Therefore, the execution of CEOPs is the mechanism by which the state grants rights to explore and produce oil. The CEOPs do not affect the state's domain over hydrocarbon deposits and other chemical elements and compounds in them, nor do they represent franchises or grant any rights over such hydrocarbons, elements, and compounds, or any direct right to acquire the proprietorship or profit from them. Before a contract is signed, it is necessary to obtain a favourable report from the CNE, a decision from the Central Bank about the exchange rate regime and a report from the tax authority (the Internal Revenue Service) regarding taxation issues.

Apart from the exclusive right to explore and exploit hydrocarbons within the conceded area, a system of benefits, exemptions and exceptions is established for those private sector contractors who sign these types of contracts. This regime further grants the contractor the following benefits: tax invariability, freedom to export the hydrocarbons they receive in exchange for the fulfilment of their duties, freedom to make use of the currency they receive and free access to currency in case they should sell any of their own equipment or other assets. In addition, under this system the rights and easements established in the Mining Code in favour of mining research, exploration and exploitation also apply to the contractors. Finally, the system authorises the expropriation of all those plots of land which the president of the republic may consider necessary for the exploration and exploitation of hydrocarbon deposits carried out by CEOP contractors. Nevertheless, this power has never been exercised so far.

**10** If royalties are paid, what are the royalty rates? Are they fixed? Do they differ between onshore and offshore production?

Since CEOP contractors do not obtain the ownership of the discovered hydrocarbons, there is no a proper system of royalties in Chile. Instead, the CEOP contemplates a retribution to the investor in money or in kind (hydrocarbons), which usually depends on the so-called recovery factor, defined as the accumulated income obtained by selling the products over the accumulated expenses incurred in the exploration and exploitation of the conceded area. The percentage of the production or the income to be obtained as retribution is variable as a function of the recovery factor. The formula is different for each CEOP, with this formula being one of the several aspects of the negotiation process with the state.

**11** What is the customary duration of oil leases, concessions or licences?

CEOPs have two phases, the exploration phase and the exploitation phase. The first generally lasts seven years, divided in three periods of three, two and two years each. If an oil discovery is made and declared commercially feasible, the exploitation phase of the discovered reserve must be started on a short time, lasting as long as necessary to complete the exploitation of the discovered reserves but not exceeding 35 years in total (including the exploration phase). After the finalisation of each of the exploration periods, portions of the conceded area have to be relinquished to the state. At the end of the exploration phase, all the area which is not included in exploitation lots has to be relinquished.

**12** For offshore production, how far seaward does the regulatory regime extend?

Chile is a signatory to the Montego Bay Treaty. Therefore, and according to Supreme Decree No. 1,393 of 1997, the Chilean regulatory regime extends 200 nautical miles seawards – known as the country's exclusive economic zone.

**13** Is there a difference between the onshore and offshore regimes? Is there a difference between the regimes governing rights to explore or produce different hydrocarbons?

There is no any difference between onshore and offshore regimes, except that the activities performed offshore fall into the jurisdiction of the Chilean Office of Maritime Affairs and Merchant Marines (Directemar) of the Ministry of Defence, which has to give approval to the activities to be performed, as well as to the installations and facilities required for exploration and exploitation.

**14** Who may perform exploration and production activities? What criteria and procedures apply in selecting such entities?

There is no specific regulation concerning the process for selecting entities that will participate in the exploration and production process. As previously mentioned, CEOPs may be awarded by direct negotiation or, as in the case of the blocks included in the 2007 bid, through a tender process. In practice, regardless of the selecting mechanism, the authority has systematically requested from the interested investors a certain level of experience and credential in the oil activity, and a minimum investment exploration programme guaranteed by the companies. In the case of the 2007 bid process, it was required that the proposed block operator certified that its average yearly production in all fields operated between 2005 and 2006 was greater than or equal to 2,500 barrels of oil, and an annual average investment between 2005 and 2006 in exploration and production activities amounting to at least US\$10 million.

Foreign companies may participate in the bidding process or in direct negotiations with the state, but the government usually requires that the selected contractor must incorporate a Chilean company to execute the CEOP and perform the oil activities in the granted area.

In a recent bidding process led by ENAP, a group of oil companies were invited to participate as operators of five blocks (previously explored and exploited exclusively by ENAP), by offering investment in oil exploration activities at operator risk and granting a participating interest to ENAP on the eventually discovered new oil and gas reserves. ENAP awarded the blocks and constituted joint ventures with the awarded companies, which applied for a CEOP with the state. All the awarded companies are well established companies in the oil business.

**15** What is the legal regime for joint ventures?

As in other jurisdictions, joint ventures are categorised as either incorporated or unincorporated. An incorporated joint venture is the formation of a legal entity by two or more companies to develop certain projects. The corporate forms most commonly used are the limited liability company and close (privately held) corporations.

Unincorporated joint ventures are structured through the execution of a consortium agreement, which is widely used in the hydrocarbon exploration and exploitation sector. Consortia are regulated mainly by the specific contractual rules established in the CEOP and in the joint operating agreement. As a practical matter, international model forms of joint operating agreements, such as that of the Association of International Petroleum Negotiators (AIPN), are widely used as a framework for unincorporated joint ventures.

- 16** How does reservoir unitisation apply to domestic and cross-border reservoirs?

There are no regulations concerning conflicts among neighbouring blocks in domestic reservoirs. Therefore, the respective CEOP's contractor must inform the Ministry of Energy and negotiate unitisation agreements. Applying general rules, if the parties are not able to reach an agreement, the dispute shall be settled by the courts, based on best industry practices and the general rule of law. We do not know of any cases concerning cross-border reservoirs in the country, notwithstanding the fact that there are oil and gas fields shared by Argentina and Chile (on the Atlantic front of the Magellan Strait).

#### Transfers to third parties

- 17** Is government consent required for a company to transfer its interest in a licence, concession or production sharing agreement? Does a change of control require similar approval? What is the process for obtaining approval?

CEOPs being contracts between a consortium and the state, any change in participating interests, partial or total, of any of the consortium parties, will be considered an amendment of the contract and must be approved by the state. Actually, most of the CEOPs regulate specifically the assignment of CEOPs' interests. In practice, a preliminary agreement between assignor and assignee has to be submitted to the Ministry of Energy in order to request approval. The assignment usually involves transfer of guarantees over exploration commitments, but as these are only one for the entire consortium, a new guarantee must be issued by the new consortium to replace the old one, with approval by the coordinating committee. No express change of control provisions are contemplated in the CEOPs. Concerning the administrative process itself, the amendment must be formally approved by the Ministry of Energy and by the National Comptroller. The procedure takes approximately three months.

#### Decommissioning

- 18** What laws or regulations govern decommissioning of oil and gas facilities and pipelines? In summary, what is the obligation and liability regime for decommissioning? Are there any other relevant issues concerning decommissioning?

As part of the CEOPs obligations, guarantees must be given to the state covering the abandonment of wells and other installations after the end of the exploitation phase, in accordance with what was established in the government environmental approval, under the environmental impact assessment system.

In relation to wells, facilities and pipelines used for the exploitation activities, if the CEOP ends while the reservoirs are still producing, they have to be transferred to the state at no charge, and the state will receive them in the conditions that they are.

In November 2012 Law No. 20,551 that provides that CEOP contractors will be required to submit a special decommissioning plan will come into force. This plan must be submitted for approval by the Sernageomin and must be prepared pursuant to the environmental qualification approval. The requirements, including guarantees to secure the obligations before the state, differ according to the reservoir capacity (whether it exceeds 600m<sup>3</sup> per day of oil or 1 million cubic metres per day of natural gas). In the case of mergers, acquisitions, spin-off, dissolutions or any other legal act or transaction involving a total or partial change of ownership, form, composition or legal status of the company subject to the procedures for decommissioning, the assignee or successor will be also obligated. However, this Act provides that CEOP contractors with a CEOP in force at the time of enactment of this Act will remain subject to the procedures, guarantees and obligations provided for the respective contracts.

#### Transportation

- 19** How is transportation of crude oil and crude oil products regulated within the country and across national boundaries? Do different government bodies and authorities regulate pipeline, marine vessel and tanker truck transportation?

The regulation's scope is limited to the applicable safety standards for oil and fuels transportation. The rules for the transport of liquid fuels through trucks and pipelines are mainly contained in Supreme Decree No. 160 of 2009 (the Safety Code for Facilities and Production and Refining Operations, Transportation, Storage, Distribution and Supply of Liquid Fuels) of the Ministry of Economy.

There are different authorities that regulate and control the transportation of crude oil and crude oil products, depending on whether the transportation is through a pipeline network, by marine vessel or by tanker truck transportation.

The Energy Ministry and the Transport Ministry are the government bodies that regulate and control the transport by pipeline system and by tanker truck, respectively.

In the case of a marine vessel, the Directemar is the authority by which Chile controls the compliance of laws and international agreements relating to national maritime territory, in order to protect human life, the environment, natural resources and regulate activities taking place in the aquatic area of its jurisdiction, and to contribute to the nation's maritime development.

Finally, regarding international agreements that regulate transportation across national boundaries, the Substitute Protocol of the Eighth Additional Protocol to the Economic Complementarity Agreement No. 16 between Chile and Argentina (ACE 16), which was explained above, should also be noted. Also, Chile is a signatory to several international conventions regarding international cooperation in case of oil pollution that may affect the sea.

- 20** What are the requisites for obtaining a permit or licence for transporting crude oil and crude oil products?

In order to construct and operate an oil pipeline, the operator must be enrolled in the registry of oil operators of the Superintendency of Electricity and Fuels, without the need of a concession. The foregoing is without prejudice to the need to comply with applicable environmental regulations, in particular the requirement of an environmental study assessment, as provided in Law No. 19,300, the most important environmental legal statute. From the point of view of technical and safety conditions, the oil transport must fulfil the requirements provided by Supreme Decree No. 160/2009 of the Ministry of Economy.

#### Health, safety and environment

- 21** What health, safety and environment requirements apply to oil-related facility operations? What government body is responsible for this regulation; what enforcement authority does it wield? Are permits or other approvals required? What kind of record-keeping is required? What are the penalties for non-compliance?

Overall, companies operating oil-related facilities must comply with the general and basic principles concerning employee health and safety laws that are contained in the Chilean Labour Code and various statutes covering those matters. The Chilean administrative branch has a special entity (the Department of Labour) in charge of the enforcement of those labour standards, with authority to impose fines against violators. In addition, with regard to safety standards, the SEC has the responsibility to seek compliance and also the authority to impose fines and declare the cessation of operations of the violators.

Regarding environmental regulation, the Chilean constitution guarantees all persons the right to live in a clean environment and

establishes that the law may determine specific restrictions in exercising particular rights and privileges in order to protect the environment. Law No. 19,300 of 1994 is the most important environmental legal statute and together with its related regulations, sets down the legal framework, including the environmental impact assessment system (EIAS).

The environmental legal framework has been recently amended. Currently, the Ministry of Environment (and its regional offices), the Council of Ministers for Sustainability, the Superintendency of Environment, the Department of Environmental Assessment and Environmental Court (not yet in operation) are the main regulatory authorities in this field. Compliance with environmental regulations is controlled by several institutions (pending the establishment of environmental courts). The maximum fine applicable is US\$40,000.

- 22** What health, safety and environmental requirements apply to oil and oil product composition? What government body is responsible for this regulation; what enforcement authority does it wield? Is certification or other approval required? What kind of record-keeping is required? What are the penalties for non-compliance?

Specific Chilean environment laws do not set requirements applicable to oil and oil product composition. Oil and oil product composition is governed by rules issued by the administrative branch. The official national standards, technical standards and quality criteria for the various types of oil, fuels derived from oil and any other kind of fuel can be declared through a supreme decree issued by any of the state departments. Accordingly, there are numerous decrees concerning quality of liquid fuels, including Supreme Decree No. 132/1979 of the Ministry of Mining and Supreme Decrees No. 456/1997, No. 133/2004 and No. 319/2006 of the Ministry of Economy, Promotion, and Reconstruction.

### Labour

- 23** What government standards apply to oil industry labour? How is foreign labour regulated? Are there anti-discrimination requirements? What are the penalties for non-compliance?

There are no special rules for the oil industry, therefore the Labour Code and general immigration rules apply, including the prohibition of any discriminatory acts within the scope of labour relationships. At least 85 per cent of the workers of one given employer who employs more than 25 employees must be Chilean. Foreign workers are required to obtain work visas to work in Chile and individual employment contracts of foreign nationals must include certain mandatory clauses (including but not limited to the employer's obligation to pay travel expenses to the foreign country in case of termination of contract).

In relation to the penalties for non-compliance of labour standards, the Chilean government has a special entity (Department of Labour), dependent on the Labour Ministry that is responsible for monitoring and controlling the compliance of the labour regulation in all sectors, including the oil industry. Among its faculties, said agency may impose fines on companies that violate the labour regulation. The amounts of the penalties are contemplated in the Labour Code and will depend on the gravity of the infraction and the number of workers the company has.

### Taxation

- 24** What is the tax regime applicable to oil exploration, production, transportation, and marketing and distribution activities? What government body wields tax authority?

In relation to upstream activities (ie, taxes applicable for CEOP contractors), DL No. 1,089 establishes the general tax regime and a

number of special rights and exemptions, which are defined specifically for each CEOP, through supreme decree.

Regarding direct taxes, the general rule is that the hydrocarbon transfers to the contractor accounting for its retribution, and those reacquisitions from the contractor executed by the state or its enterprises, as well as their corresponding acts, contracts and documents are declared tax exempt. This exemption shall also apply to those instruments documenting special operation contracts and any other operation, act or agreement executed by the same parties and in any way connected with the mentioned contracts. Finally, hydrocarbon exports carried out by the contractor shall also be exempt from any taxes or assessments.

With respect to income taxes, the contractor shall be subject to a single tax calculated on their compensation, equivalent to 50 per cent, or shall be affected by the general regime of the Income Tax Law contained in Decree Law (DL) No. 824 of 1974, the terms of which will remain unchanged for the entire duration of the contract. At present, the tax rate on corporate earnings is 18.5 per cent (this is a temporary percentage for 2012; it is contemplated that it will return to the customary percentage of 17 per cent for 2013 and thereon; nevertheless, at present the Congress is analysing a tax reform, which establishes permanently a tax rate on corporate earnings of 20 per cent). However, whatever the regime, the president of Chile may reduce the tax rates according to the special conditions of the contract and other considerations identified in the DL No. 1089. In addition, the shareholders of the contractor are tax-exempt in relation to the income received or accrued arising out of the respective CEOPs, and contractors may recover the value added tax (19 per cent according to Sales and Services Tax Law contained in Decree Law No. 825 of 1974) supported or paid on the import or purchase of goods and services used in connection with the exploration and exploitation activities.

Whatever the regime set, it will replace all other taxes, direct or indirect, which could otherwise be applicable and be unchangeable for the term of the CEOP.

In relation with downstream activities (ie, marketing of oil products), Law No. 18,502 of 1986, imposes a specific tax on automotive consumption of compressed natural gas and liquefied petroleum gas and the first sale or importation of automotive gasoline and diesel oil.

There is also a specific tax affecting the sale of gasoline and diesel oil to end customers, created in 1984. After several changes, those taxes currently account approximately the equivalent of US\$480 per cubic metre of gasoline and US\$120 per cubic metre of diesel oil. New changes have been proposed to this tax recently, as part of a wider tax reform.

In order to prevent or mitigate major fluctuations in the domestic prices of oil products, the Fuel Price Protection System (SIPCO) was created (replacing the Oil Prices Stabilisation and the Fuel Prices Stabilisation Funds previously existing). The relevant regulation provides a variable component of the current fuel-specific tax, which will allow such specific tax to drop when international prices exceed a certain level, operating in reverse when fuel prices fall sharply worldwide. The mechanism set reference prices, which represent the expected price in the medium- and long-term market. In addition, weekly prices are calculated by the Ministry of Energy and the National Energy Commission to achieve parity with the international fuel market within the internal system.

### Commodity price controls

- 25** Is there a mandatory price-setting regime for crude oil or crude oil products? If so, what are the requirements and penalties for non-compliance?

There are no specific rules for pricing. They are subject to negotiation among the parties involved, in an unregulated environment. Transactions between related or affiliated companies must be realised at



**Update and trends**

No relevant news or special industry developments occurred during 2011.

In the upstream segment of the industry, the most important development was the CEOP bidding process led by ENAP relating to five blocks (previously explored and exploited exclusively by ENAP) awarded to well-established companies in the oil business. Despite the relatively high number of outstanding CEOPs in the Magellan basin, no major oil deposits have been discovered. The main recent regulatory change has been Law No. 20,551, which provides that CEOP contractors will be required to submit special decommissioning plans for approval by Sernageomin. However, such new obligations will be applicable only for CEOPs executed after November 2012.

There are no significant changes in the distribution segment of the industry either. The sole development is again relating to the Terpel network (an important network of 206 service stations

making up 10 per cent of the market). Due to the purchase of Terpel Organization by COPEC and the order to divest Terpel Chile issued by the Antitrust Court (otherwise COPEC would concentrate more than 75 per cent of the market), COPEC announced that Luksic/Shell (16 per cent of the market) will purchase the network. However, the Antitrust Court, in a recent decision, banned such acquisition, ordering that the final controller Terpel network has to be a truly new entrant in the distributions segment. Luksic Group announced that the Antitrust Court decision will be challenged before the Supreme Court. Therefore, it appears that the Terpel network is still available for acquisition. Apart from that, there has not been any increase in the competition between the players, and the structure of the market has not changed significantly.

an arm's-length basis. However, taking into consideration the high market share of ENAP, the CNE has recommended ENAP to apply for the fuels a price policy called 'parity prices'. These prices are determined and actualised weekly as the total cost that any importer would have if it decides to supply the local demand with imported products. This policy intends to simulate an artificial competitive fuels market, precluding ENAP to act as a monopoly.

**Competition, trade and merger control**

- 26** What government bodies have the authority to prevent or punish anti-competitive practices in connection with the extraction, transportation, refining or marketing of crude oil or crude oil products?

According to the Law Decree No. 211 of 1973 (DL 211), the Antitrust Court and the National Economic Prosecutor (FNE) are responsible for enforcing competition law in Chile. The FNE Office is an independent administrative entity in charge of investigating conduct that may constitute DL 211 infringements, representing the public interest before the Antitrust Court and seeking enforcement of resolutions, decisions and instructions issued and passed by the Antitrust Court. The Antitrust Court is a special, independent court of law, subject to the supervision of the Supreme Court, whose role is to prevent, correct and sanction anti-competitive conducts, and to decide all cases that the FNE or private persons may submit to its consideration. It is also in charge of issuing general guidelines for the enforcement of competition law.

- 27** What is the process for procuring a government determination that a proposed action does not violate any anti-competitive standards? How long does the process generally take?

DL 211 states, generically, that anyone who carries out or enters into, individually or collectively, any conduct, act or agreement that hampers, restricts or hinders free competition or that tends to produce such effects, will be sanctioned through the measures contemplated in such legislation. Additionally, DL 211 enumerates certain offences, but in a merely exemplary basis. Consequently, any transaction, including mergers or acquisitions, performed in the oil industry could be subject to the oversight of the Antitrust Court or the National Economic Prosecutor, and such transactions can be blocked in accordance with antitrust regulations. It is not possible to know in advance if a particular transaction will be subject to the scrutiny of the competition authorities. However, the National Economic Prosecutor has issued a general and non-mandatory guidance for mergers and acquisitions operations, which any interested party may follow in order to have the competition authorities review the transaction and give feedback on before the transaction goes ahead. Proceedings before the Antitrust Tribunal may take between one to three years, and its resolutions shall be subject to the relevant judicial review by the Supreme Court.

**International**

- 28** To what extent is regulatory policy or activity affected by international treaties or other multinational agreements?

International treaties must be submitted for approval by the National Congress in order to be mandatory. International treaties have the same hierarchy level as any law and, therefore, the chronological or

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specialty criteria shall be applied if there is any conflict with internal regulation.

Chile has signed agreements for the promotion and protection of investments with many countries throughout the world. It is a member of the World Trade Organization (WTO), a signatory to the Kyoto Protocol on climate change, the ICSID Convention and the Stockholm Convention on Persistent Organic Pollutants, and it has an Economic Complementation Agreement with Argentina concerning oil interconnection. Chile has also signed many double taxation treaties (with, for example, Argentina, Brazil, Canada, Colombia, Mexico, Spain, Norway, South Korea) and free-trade and economic association agreements (Canada, the United States, the European Union, Mexico, South Korea, New Zealand, Singapore, Brunei and China).

**29** Are there special requirements or limitations on the acquisition of oil-related interests by foreign companies or individuals?

There are no restrictions on foreigners owning oil-related rights and interests. No domestic partner is required. There is a generic obligation to comply with the laws of Chile, with certain special requirements. Foreign investment in Chile is primarily governed by Decree Law 600 of 1974. This law states that foreign investment authorisa-

tions shall be expressed by means of contracts to be signed by the Foreign Investment Committee on behalf of the state of Chile and the foreign investors. The purpose, time and method of capital investment are defined in these contracts, and the investors' basic rights as well, namely, the right to remit or transfer both capital and profits, the right to have access to the foreign exchange market, the invariability of the tax system and the right not to be discriminated against. Alternatively, foreign investment can be ruled by chapter XIV of the Compendium of Foreign Exchange Regulations of the Central Bank of Chile. This regulation that does not contemplate the same guarantees and rights granted by a contract governed by Decree Law 600, but assures the repatriation of an investment and its profits.

**30** Do special rules apply to cross-border sales or deliveries of crude oil or crude oil products?

The only regulation on cross-border issues is the Substitute Protocol of the Eighth Additional Protocol to the Economic Complementation Agreement No. 16 between Chile Republic and Argentina Republic (ACE 16) Regulation for Marketing, Operations and Transportation of Hydrocarbons Gas Liquids – Crude Oil, Liquefied Gas and Liquid Products of Petroleum and Natural Gas.

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