

Negotiation and Relationship
Management Services
for Oil & Gas Companies

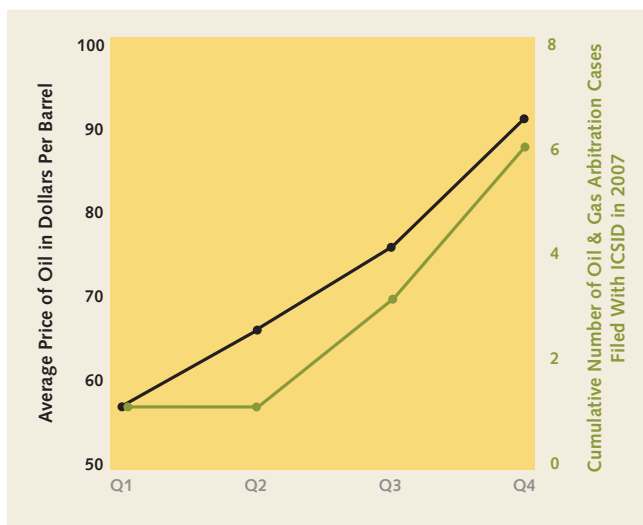
Problem

Oil and gas companies face unusually difficult negotiation and implementation challenges.

Economic Uncertainties

Often there is considerable uncertainty about both what a field will yield and for how long, and about the economic conditions that will exist as it does so. Extraction requires enormous investments up front for economic returns reaped much later. Moreover, unexpected field shutdowns — whether the result of technical problems, protests, or political instability — can permanently reduce output. Likewise, dramatic changes in economic conditions, such as \$100/barrel oil, may stretch contract terms, at least in the eyes of some parties, beyond the bounds of reasonableness.

Correlation Between Oil Prices and Arbitration Cases Filed With ICSID*



* ICSID: International Center for the Settlement of Investment Disputes
Source: U.S. Energy Information Administration; ICSID

Unpredictable Governments

Contracts are often with governmental entities whose integrity and reliability over time may be suspect, and whose decision makers and elites are certain to change over time, often with little or no warning or confidence that any new regime will understand or honor bargains that may have been struck years or decades previously. Once major investments have been made, host governments have an economic incentive

to find excuses to renegotiate royalty rates and other contract terms, and are likely to see anything gained as pure upside. Regimes of international arbitration and enforcement are cumbersome, time-consuming, and unpredictable. Even if arbitration produces a favorable decision for a company, it may result in an adversarial relationship with the host government, leading to expensive, time-consuming hurdles to permitting, regulatory approvals, inspections, visas for key personnel, importing equipment and supplies, and enforcement actions. Because such mechanisms are inappropriate for anything beyond a major contractual breakdown, companies are incented to settle less catastrophic disputes by making incremental concessions, which have the perverse effect of encouraging governments to press, over time, for more concessions.

Results Dependent on Relationships

In practice, real economic returns are often dependent on the quality of working relationships developed and maintained with key stakeholders in the host country. Yet these often vary dramatically over time based on the relative skills of local management — often expatriate engineers whose focus and strong suit are not “people skills.” When such relationships are poor, inevitable conflicts escalate, rather than getting worked through, in the worst cases leading to breach or even expropriation.

Short-Term Solutions May Cause Long-Term Problems

Moreover, each contract renegotiation sets a precedent that affects other contractual relationships around the world, but in a slow dance that plays out over a period of years longer than the tenure of most area managers. Partly as a result, most negotiations are carried on more as firefighting exercises to manage the short-term bottom line, with relatively little thought given to potential longer-term consequences. Few companies have a long-term strategic vision for the kind of contractual regime they would like to evolve, let alone a plan they enforce for proactively shaping that evolution.

Lack of Global Strategic Contract Management

Yet billions of dollars ride on a company’s ability to manage such complex negotiations and ongoing relationships systematically, effectively, reliably, and

globally, whatever changes occur in personnel, strategy, or the prevailing economic or political climate. While companies have many experienced and capable managers trying to cope with such challenges, most have not invested in these skills as a core competence. Most companies do not have world-class mechanisms for ensuring that key negotiations and host-country relationships are systematically assessed, prepared for, and managed, including planning for predictable (and even unpredictable) contingencies and precedential effects.

Solution

Vantage Partners helps oil and gas companies:

- Use systematic methodologies to prepare for and achieve optimal results in critical negotiations;
- Repair critical relationships that have been damaged;
- Launch new critical relationships with a firm and sustainable foundation;
- Establish and implement frameworks for maintaining productive host-country relations over time;
- Develop a long-term strategic vision and framework for managing and shaping the evolution of contractual regimes over time on a global basis;
- Build individual capabilities to do these things reliably and sustainably over time;
- Build organizational capability for the company to do these things reliably and sustainably over time without Vantage help, despite changes in personnel or external climate.

Often the focus of our work is on helping people learn to prepare systematically for critical interactions, with a clear understanding that the value of most deals will be determined during implementation, not by a signature on some piece of paper. This will be the result of the relationship built during the negotiation. Vantage teaches people how to build a good working relationship while negotiating a good, profitable substantive deal.

Case Study: Settling a Dispute Over Contract Renewal

Foreign Government had refused for seven years to renew Oil Company's contract. The original contract for 25 years was renewable by its terms for a second 25 years "under identical terms and conditions at the Company's sole discretion." There was no claim of

poor performance, though working relationships had been strained for years. Company initiated international arbitration and Government responded by initiating local court action to declare the contract unconstitutional. Government won at trial and the case was on appeal, but the independence of the local Supreme Court was suspect.

In Vantage's initial diagnostic session, we discovered that both sides suspected, based on the obviously one-sided wording of the contract language, that the original contract, negotiated under a prior regime, was the product of corruption and fundamentally not legitimate. Moreover, it became clear that no settlement would be possible so long as that perception existed, because it would be impossible to obtain the requisite political approvals. Luckily, new research revealed that the language in question was a creative option proposed by the Government to create a 50-year contract — necessary to the economics — without violating the constitution's 25-year limit on contract duration (with the possibility of renewal). Showing the current Government team an old videotape of the Government's original negotiator, who had a well-known reputation for integrity, explaining the deal changed the negotiating relationship and established the possibility of settlement. There was still a lot of work needed to reach a settlement and win all needed approvals, but the parties succeeded because they were now working together to do a deal that made sense and felt legitimate.

Vantage facilitated regular strategy sessions during which the team:

- Modeled multiple scenarios to determine what contractual arrangement made economic sense;
- Thought through how to help the Government team understand the economics well enough to understand and accept the target approach;
- Applied various analytical tools to understand the constraints on the Government's choices and the competing perceptions of different stakeholders, which in turn helped the team develop a nuanced and carefully sequenced influence strategy.

In the end, an agreement was reached worth hundreds of millions of dollars to both parties that was then jointly marketed by the combined Company and Government teams, ultimately securing all 14 required approvals.

Case Study: Surviving a Radical Change in Government

In the early 1960s, Oil Company became the first company granted the right to explore for and produce natural gas in Foreign Country, as part of the government's long-term strategy to develop the energy sector. In trying to attract foreign investment, the Government had put in place discovery and production incentives, including significant upside for continued production to meet anticipated future local demand.

Following a crisis in the Foreign Country's currency, the sensitivity to foreign exploitation of indigenous resources increased. At the same time, an increase in the price of foreign oil further fueled demand for indigenous gas. The gas sector had been so efficient as to ensure an abundant supply. With a new, pro-business but populist government in place, the pressure to reduce prices, particularly on discretionary production volumes, also increased. As the producer of nearly half of Country's natural gas, Oil Company was a likely target. Relationships with some key individuals became particularly strained, and Oil Company was mired in a stalemate with Government officials, as key gas contracts were coming up for renewal.

Vantage worked with Oil Company negotiation teams to prepare their strategy and structure their teams. Team planning sessions focused on:

- Understanding the nature of the Ministry's resistance;
- Creating proposals that would meet the Government's legitimate interests, while at the same time defending the fairness of Oil Company's long-term contracts;
- Developing a strategy to elevate the negotiations to the appropriate level.

Through multiple discussions with various Ministries, it was clear that there were very different perceptions, and even different understandings, of the contracts in place and why they were structured as they were. In the end, the team developed a strategy that not only helped meet the Government's need, but positioned the Company to demonstrate publicly their commitment to the Foreign Country, the Government, and to the people, paving the way for signing of contract extensions worth billions of dollars and continued collaboration.

Case Study: Building Sustainable Community Relations

Many of Oil Company's operations were in remote, very poor areas of Foreign Country. Instant communities would form around (often on) any installation, creating difficult safety and environmental challenges. Moreover, people quickly learned how easily operations could be shut down or otherwise disrupted by protests, strikes, blockades, or sabotage. This encouraged efforts at petty extortion from various groups and local officials, who operated within a tradition of bribery and graft.

The challenge for the Company was to maintain a positive public image, good community relations, and smooth operations without making illegal payments, setting bad precedents, encouraging extortion and escalating demands, or relying on armed repression from government forces.

To meet these challenges sustainably, Vantage:

- Worked with Company (in facilitated joint sessions involving national and expatriate staff) to articulate a set of guiding principles and policies drawn from successful case studies to govern effective approaches in the community;
- Created a Host Country Relations Handbook that explained this framework and the rationale for it, and provided multiple illustrations of how to handle common difficult situations, including disagreements among managers;
- Delivered customized workshops for regional managers that involved practice in applying this framework by role playing real and realistic situations.

About Vantage Partners, LLC

Vantage Partners leads the field of negotiation and relationship management, building on more than 25 years of research and consulting experience with the world's leading companies. An independent spin-off of the Harvard Negotiation Project, Vantage Partners helps organizations negotiate and manage their most important and complex business relationships.

Vantage consultants are recognized thought leaders, speakers, and writers on the subject of negotiating and managing critical business relationships, with articles published in the *Harvard Business Review*, *Sloan Management Review*, and the *Negotiation Journal*. Books we have written or co-authored include:

- *Getting to YES: Negotiating Agreement Without Giving In*
- *Getting Ready to Negotiate: The Getting to YES Workbook*
- *Difficult Conversations: How to Discuss What Matters Most*
- *The Point of the Deal: How to Negotiate When Yes Is Not Enough*

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