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## THE NEW ARGENTINE PETROLEUM LAW REGIME\*

Uisdean R. Vass\*\*  
Carlos Valiente-Noailles†

### I. INTRODUCTION

On October 22, 1991, at the World Petroleum Congress in Buenos Aires, Argentine President Carlos Saul Meném articulated his intention to create a market-oriented regime for oil and gas exploration and production in Argentina. The "Argentina Plan" gives foreign and domestic oil companies the opportunity to acquire exploration permits over large areas of Argentina's sedimentary basins. But the "Argentina Plan" is only part of the picture: The Argentine oil market has been completely deregulated, and oil companies may now sell their production at market prices, export their oil, and even repatriate all their post-tax profits. The Meném administration's approach includes divesting the nationalized oil company, Yacimientos Petrolíferos Fiscales (YPF), of many of its assets and requires YPF to increase its operational associations with private enterprise. YPF will soon privatize a majority of its shares. The state gas distribution company, Gas del Estado, will also be privatized.

The innovations enacted by President Meném are sweeping and, given Argentina's recent past, revolutionary. Partly because of these changes, Argentina's economy has rapidly improved since 1989, and the country is more politically stable. These major developments have established Argentina as an attractive location for increased foreign petroleum

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investment, exploration, and production.<sup>1</sup>

## II. ARGENTINA AND ITS PETROLEUM INDUSTRY

Oil was discovered in Argentina early in the twentieth century. The first major find was made in the Province of Chubut in 1907,<sup>2</sup> and by 1920, private oil companies had received permission to begin exploration and development.<sup>3</sup> President Yrigoyen's Radical Party government established YPF as the national oil company in 1923.<sup>4</sup> By 1945, YPF had become the dominant petroleum producer in an isolated, protected economy.<sup>5</sup> But even though private oil companies were never entirely excluded from Argentina, their presence has been precarious at times.<sup>6</sup>

In 1946, Juan Perón was elected President and promptly enacted a series of corporatist measures. In so doing, he granted enormous powers to the trade unions, boosted the state's economic participation, and discouraged foreign investment. Immediately after Perón's reforms were implemented, both the economy and the demand for petroleum grew rapidly. Foreign imports increased dramatically when cash-strapped YPF, starved of drilling equipment, failed to meet the rising demand for more oil.<sup>7</sup> Despite the shortfall in production and YPF's inability to

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1. An excellent historical work on Argentina is DAVID ROCK, *ARGENTINA 1516-1987, FROM SPANISH COLONIZATION TO ALFONSÍN* (1987).

2. Wolfgang J. Müller & Thomas G. Stern, *The Evolution of Petroleum Contracts in Argentina—Issues of the Foreign Investor's Legal Protection*, 7 J. ENERGY & NAT. RESOURCES L. 189 (1989). Other important fields were later discovered in the Neuquén, Salta, and Mendoza Provinces. *Id.* at 189.

3. *Id.*

4. *Id.* Some scholars claim that YPF is the world's oldest nationalized oil company. While this may be true, *stricto sensu*, it should be noted that the British government acquired a controlling interest in British Petroleum as early as 1911. A MANUAL OF UNITED KINGDOM OIL AND GAS LAW 10-11 (Terence Daintith & G.D.M. Willoughby eds., 1977).

5. Müller & Stern, *supra* note 2, at 189.

6. Earlier legislative drafts of Ley de Radicación de Capitales Extranjeras No. 20,557 (Arg.), would have completely excluded foreign participation in the Argentine oil industry. Müller & Stern, *supra* note 2, at 191.

This policy is consistent with the Spanish legal tradition, which has regarded minerals as being the patrimony of the State (or Crown) since the earliest of times. See discussion in Tomislavo E.J.P. Dabinovic, *Petroleum Service Contracts in Argentina, Brazil and Colombia: Issues Arising from Their Legal Nature*, 5 J. ENERGY & NAT. RESOURCES L. 15, 15-16 (1987) (reviewing Royal Mining Ordinance for New Spain (1783), the Ordinances of Alcalá (1378), Toledo (1574), San Lorenzo (1584), and The Laws of the Indies (1688)). Indeed, the Argentine government owns all hydrocarbons found in the subsoil of Argentine national territory and on the Argentine continental shelf. Significantly, however, this ownership derives from article 1 of the Argentine Hydrocarbons Law, No. 17,319, *not* from the Argentine Constitution.

7. Müller & Stern, *supra* note 2, at 190. A full account of the Perón era appears in ROCK, *supra* note 1, at 262-319.

meet the new demand, Perón asserted that Article 40 of the 1949 Constitution prohibited the holding of concession rights by private oil companies and refused to solicit the aid of such companies to develop and explore Argentina's hydrocarbon resources.<sup>8</sup> In 1955, a revolution overthrew President Perón. Two years later, the Constitution of 1949 was repealed, along with the prohibition against foreign oil exploration. In its place, the prior Constitution of 1853-60, which contained no equivalent to Article 40, was reenacted.<sup>9</sup> Despite this fact, President Frondizi caused a political firestorm when he entered into service contracts with private companies between 1958 and 1963.<sup>10</sup> When Frondizi was deposed in 1963, his next elected successor, President Illia, declared these service contracts null and void and brought suit against various major foreign oil companies, including Exxon and Shell subsidiaries, to enforce his decision. With only a few exceptions, these lawsuits settled.<sup>11</sup>

Argentina experienced a series of profound crises during the 1970s and early 1980s and remained inhospitable to private foreign investment. These crises included the economic collapse of the government of Isabel Perón, bouts of hyper-inflation, the Montoneros terrorist war, the subsequent counter-terror of the armed forces, and the disastrous Falklands/Malvinas War.<sup>12</sup> In 1983, democracy returned to Argentina with the advent of President Raul Alfonsín's Radical Party government. Although Alfonsín successfully reestablished democracy, the new government lacked the support that it required to undertake painful but necessary economic reforms.

Alfonsín's administration did make one major contribution to the

8. A major exception, however, was the celebrated "California Contract," which may have played a role in the anti-Perón revolution of 1955. ROCK, *supra* note 1, at 316.

9. This version of the Argentine Constitution, which remains in force today, contains no equivalent of Article 40 of the 1949 Constitution. Thus there has been no constitutional impediment to the private exploration and development of hydrocarbons in Argentina for over 30 years.

10. See discussion in Müller & Stern, *supra* note 2, at 190-91; Dabinovic, *supra* note 6, at 24-25.

Argentine service contracts have historically been quite similar to mineral concessions. For example, they have typically involved private companies exploring and developing defined tracts at their own risk and being paid a fee by YPF on the basis of the volume of petroleum produced. Formulas for the payment of the private companies have varied from contract to contract. With a few early exceptions, however, true mineral concessions, which are the equivalent of oil and gas leases, date only from the inception of the Meném regime.

11. See Müller & Stern, *supra* note 2, at 199-200. Dabinovic comments that the Illia government's filing of suit to enforce its own annulment decree was rather odd, legally speaking. Dabinovic, *supra* note 6, at 24. "The service contracts were annulled, and though the Government of the day claimed that such annulment was enforceable by itself, as a lawful termination would have been, it soon found out that the reluctance of the contractors to oblige could only be overcome by threats of legal action." *Id.*

12. These events are covered in ROCK, *supra* note 1, at 320-403.

Argentine oil industry by implementing the so-called "Houston Plan" in 1985. This program opened large parts of Argentina's sedimentary basins to service contractors. The government offered the first bidding invitation in 1985. The invitation covered 164 blocks, which represented a total of 516,238 square miles, both on- and offshore.<sup>13</sup> Decree No. 623 of 1987 restricted YPF's rights in a third bidding invitation, which attracted a strong industry response.<sup>14</sup> The government's terms, however, were not truly satisfactory to private industry because of YPF's broad control over development and production prices. But the Houston Plan's goal of boosting exploration and development in the face of declining production was a partial success. As of the beginning of 1991, private firms had spent \$174 million of total exploration commitments of \$292 million.<sup>15</sup> The Houston Plan, however, was a conservative precursor to the present government's oil and gas program.

As of the beginning of this decade, Argentina was the fourth largest petroleum producer in Latin America, behind Venezuela, Mexico and Brazil. YPF had earlier made significant new discoveries of natural gas in Neuquén (including the important Loma de la Lata field) and in Tierra del Fuego.<sup>16</sup> However, YPF, a cash-hungry giant, dominated the industry and set the prices of hydrocarbons, especially gas, at below-market levels. Partly as a result of this practice, some analysts estimated that as of 1990 only ten to twenty percent of Argentina's territory had ever "been tested for oil."<sup>17</sup> Offshore exploration has been scanty, to say the least.<sup>18</sup> Until very recently, the Argentine petroleum industry has been a sleeping giant.

### III. THE PROGRAM OF THE CURRENT ADMINISTRATION

In July 1989, the Meném administration took office amid skyrocketing inflation and a deepening recession.<sup>19</sup> The new Perónist government

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13. Decree No. 1443 (Arg.). An authoritative analysis of the Houston Plan can be found in Tomislavo E.J.P. Dabinovic, *The New Argentine Legal Regime for the Petroleum Industry: Decree 1443 of 6 August 1985*, 4 OIL & GAS L. & TAX'N REV. 75 (1985/86) and Tomislavo E.J.P. Dabinovic, *The Restated Version of the Argentine Model Contract*, 6 OIL & GAS L. & TAX'N REV. 142 (1987/88). See also Müller & Stern, *supra* note 2, at 203-07.

14. Twenty-seven companies made thirty-four offers for thirty blocks.

15. *Argentina Pushes to Court Foreign Operators*, OIL & GAS J., Jan. 14, 1991, at 51, 53.

16. *Id.* at 52. John Barham, *Argentina Faces Oil Free-For-All*, THE FIN. TIMES, Jan. 23, 1991, at 21.

17. Carlos Brezina, *Sweeping Overhaul of Argentina's Energy Sector Urged*, L.A. TIMES, Oct. 19, 1990, at D2.

18. *Argentina Pushes to Court Foreign Operators*, *supra* note 15, at 52.

19. *Argentina to Allow Foreign Firms to Produce, Export Hydrocarbons Output from State*

responded with ambitious reforms, which included privatizing the nationalized telephone and airline companies, controlling the federal budget, and battling inflation.<sup>20</sup> From the beginning, President Meném identified the oil industry as vital to the program of economic transformation. The administration's petroleum goals can be summarized as follows: (1) to expand exploration and development by eliciting the assistance of domestic and foreign oil companies and private capital; (2) to maximize production, enabling Argentina to become a net exporter of oil to surrounding nations such as Brazil, Uruguay, and Paraguay, and thus earn precious foreign currency reserves and expand trade; and (3) in keeping with the first two goals, to streamline and privatize YPF and Gas del Estado.<sup>21</sup> These goals, however, are not simply one aspect of the government's general economic policy. Rather, the Meném government regards oil and gas and its secondary industries, such as petrochemicals, as the engine that will drive the Argentine economy forward.<sup>22</sup> The nation's abundant unexplored acreage, underdeveloped oil fields, and considerable production have always been among its most attractive economic assets from the standpoint of foreign investors.

#### A. *The Argentina Plan*

The Argentina Plan, established by Decree 2178 of October 21, 1991, is one of the most recent and most notable of the free market reforms.<sup>23</sup> President Meném promulgated the Decree pursuant to the authority granted by Law 17,319 of 1967 (Argentina's Basic Hydrocarbons Law).<sup>24</sup> The Preamble to Decree 2178 captures its significance:

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*Fields*, PLATT'S OILGRAM NEWS, Feb. 9, 1990, at 2. ("'Argentina is now more open for foreign investment just as the economy is collapsing' said one oil consultant.").

20. Robert Allen, *Pace of Change Quickens as Argentina Forges Ahead with Privatization Plans*, OIL MARKET LISTENER, Dec. 18, 1991, at 1, 2 (noting that when Meném took office, inflation had been running at a rate of 3000% per year).

21. See generally Decree No. 2178 (1991) (Arg.).

22. *Argentina Opens Door for Foreign Investment in Petrochemical Projects*, PLATT'S INT'L PETROCHEMICAL REP., May 3, 1990, at 1. ("Meném is counting on foreign investment in the petrochemical industry to help revive growth in Argentina's \$65 billion economy . . . . The petrochemical industry is the fastest growing sector of the economy.").

23. Since 1989, the Meném administration has granted additional service contracts to private companies using the Houston Plan mechanisms.

24. Argentine Hydrocarbons Law No. 17,319, art. 2 (1976) (Arg.). Risk Contract Law No. 21,778 (1978) (Arg.), substantially amends the Basic Hydrocarbons Law. A major new amendment to Law No. 17,319 is now passing through the Federal Congress in Buenos Aires which contains three major provisions. First, it provides that the interests and rights of the national government in the country's oil and gas will, with certain exceptions, be transferred to the Provinces. The boundary of a maritime province extends 12 miles out to sea from the low tide marks. However, the federal government would retain its oil and gas rights in the federal district of Buenos Aires and on

The policy implemented by the Argentine Government in connection with hydrocarbons is intended to reactivate the production by means of the privatization and deregulation of the industry. There is a need to increment hydrocarbons reserves which have decreased to levels that may impair the rational exploitation strategy of said hydrocarbons.

The mentioned reactivation must be based on an exploration program of hydrocarbons comprising the entire national territory and its continental shelf.<sup>25</sup>

The forceful language contained in the Preamble expresses the Argentine Executive's goal of increasing exploration and production using market mechanisms. Decree 2178 reflects a number of exceptionally important aspects and innovations. The plan that the Decree prescribes calls for numerous departures from Argentina's traditional policy toward private oil companies, including the granting of petroleum concessions to foreign oil producers.

### 1. True Petroleum Concessions and an Exploration Commitment Bid System

The Argentina Plan directs the Undersecretariat of Fuels to offer private oil companies true petroleum property rights similar to those available under an American oil and gas lease.<sup>26</sup> Before this change, private companies had only the opportunity to bid for service or risk contracts with YPF.<sup>27</sup> Under Decree 2178, companies are invited to bid for exploration permits.<sup>28</sup> The first areas offered, which are described in the Decree's Annex I, are open for bids in June 1992.

A private company can obtain an exploration permit on a given block by submitting an exploration commitment bid.<sup>29</sup> The Argentine

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continental shelf acreage more than 12 nautical miles offshore. Second, YPF will be granted exploration permits or, where appropriate, exploitation concessions in the areas assigned to it. Finally, the bill approves the YPF privatization program. *See Hydrocarbon's Bill: Federalization of Hydrocarbons*, ENERGY & NAT. RESOURCES NEWSL. (Cardenas & Dabinovic, Buenos Aires, Argentina), Oct. 1991, at 2.

25. Decree No. 2178.

26. The Ministry of Energy & Mining, now in the form of the Undersecretariat of Fuels, is granted principal regulatory authority over Argentine petroleum operations pursuant to Argentine Hydrocarbons Law, No. 17,319, art. 97. A few pre-World War II concessions still remain in force. These concessions are governed by the law in force when they were awarded. *Id.* art. 8.

27. It should be emphasized that the Argentine Hydrocarbons Law clearly has provided for the granting of concessions. But not until now has any Argentine administration exercised its right to grant them. Argentine Hydrocarbons Law, No. 17,319, ch. II, §§ 2, 3 (permits and concessions).

28. Decree No. 2178, art. 1.

29. There are separate "bidding conditions" for each block, which have to be paid in advance. Available technical data will be provided on receipt of payment of the conditions. *Id.* art. 12. It is

exploration permit, with its periodic subdivisions, corresponds to the primary term of an American oil and gas lease or to the initial term of a British production license.<sup>30</sup> The exploration permit is divided into three periods. The first period may consist of two or three years onshore, or of two, three, or four years offshore, depending on the particular block.<sup>31</sup> The second period in any given block consists of one year less than the first period,<sup>32</sup> and the third period consists of two years less than the first period.<sup>33</sup> A provision of the Basic Hydrocarbons Law grants permit holders the right to add a one year extension to each exploration period.<sup>34</sup> But Decree 2178 prohibits the extension of the first exploration period. Decree 2178 allows the permit holder to add the year that it could otherwise have added to the first exploration period to the second or third period. Under no circumstances, however, can a period last longer than four years.<sup>35</sup>

The lengths of the exploration periods are important from the standpoint of the exploration bid mechanism. All bids must include a minimum amount (K) of 300 work units, valued at \$5000 each.<sup>36</sup> Thus, the minimum work commitment for any block is \$1.5 million of exploration. The permit holder may complete the minimum work units during any of the three periods, but can only carry its permit into the second period by committing to drill at least one exploratory well.<sup>37</sup> Similarly, the permittee must commit to drill at least one exploratory well in the third period.<sup>38</sup> Decree 2178 also requires the bidder to specify the amount of

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possible under the Argentine Hydrocarbons Law to obtain separate licenses to conduct surface seismic testing in areas not covered by exploration permits or reserved to YPF. Argentine Hydrocarbons Law, No. 17,319, arts. 14-15.

30. The exploitation concession is equivalent to the secondary term of the oil and gas lease or license. For a comparison of the American and British petroleum regimes, see Uisdean R. Vass, *A Comparison of American and British Offshore Oil Development During the Reagan and Thatcher Administrations: Part I*, 21 TULSA L.J. 23, 66-71 (1985) [hereinafter Vass I], and Uisdean R. Vass, *A Comparison of American and British Offshore Oil Development During the Reagan and Thatcher Administrations: Part II*, 21 TULSA L.J. 225 (1985) [hereinafter Vass II].

31. Decree No. 2178, annex II, art. 5.1.4.

32. *Id.* art. 2.14.

33. *Id.* It is contemplated that the latter regulation may result in certain exploration permits not running for a third period. See *id.* art. 9.2 ("If the EXPLORATION PERIOD consists of only two PERIODS pursuant to clause 2.14.").

34. Argentine Hydrocarbons Law, No. 17,319, art. 23.

35. Decree No. 2178, annex II, art. 9.2.

36. *Id.* art. 5.1.1. These units may include geophysical work as well as the actual drilling of wells. *Id.*

37. *Id.* arts. 5.1.2, 5.1.3. The permit may be allowed to continue for a second period without the drilling of an exploratory well, if the permittee can convince the Undersecretariat that a delay is justified for technical reasons. *Id.* art. 5.1.2.

38. *Id.* art. 5.1.3.



extra work units (U) to which it will commit during the first period.<sup>39</sup> Finally, the bidder must indicate how many years (T) the exploratory program will take.<sup>40</sup> Blocks are awarded on the highest G basis, where G equals the sum of U (additional work units pledged in the first exploration period) and the K (the minimum work commitment) divided by T (the program's length in years).<sup>41</sup>

The Undersecretariat of Fuels retains the discretion to require the winning bidder to commit to extra work units and can reject bids that it considers unsatisfactory.<sup>42</sup> Use of the G formula will serve to reduce the Undersecretariat's use of discretionary powers. Significantly, the Undersecretariat is authorized to dispense with the exploration bid if it considers that the acreage could be leased more appropriately by a bonus system.<sup>43</sup> The Undersecretariat has already exercised this discretion in certain low risk areas.<sup>44</sup>

Decree 2178 provides security for the Argentine government in case a permit holder fails to meet the obligations imposed by the permit. The exploration permit holder is required to post a guarantee for the payment of pledged work units before the beginning of the appropriate exploration period.<sup>45</sup> If the permit holder reneges on its commitment and surrenders all or part of the block, it is required to pay to the Argentine government the dollar value of the unexpended work units.<sup>46</sup> Although Decree 2178 does not specify any surrender obligations, the Basic Hydrocarbons Law appears to require the surrender of fifty percent of any given block at the end of each exploratory period.<sup>47</sup>

The Decree allows a permit holder to change the nature of its interest in a block. If in its judgment the permit holder makes a commercial discovery, it has the right to turn the exploration block, or the appropriate portion thereof, into an exploitation concession.<sup>48</sup> In such a case, the permit holder must pay a royalty of twelve percent to the appropriate

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39. *Id.* art. 5.1.1.

40. *Id.* art. 6.1.

41. *Id.* ( $G = U + (K/T)$ ).

42. *Id.* art. 6.2.

43. *Id.* art. 5.

44. See *Argentina to Invite E&D Bids on 1.37 Million Sq. Km.*, OIL & GAS J., Nov. 4, 1991, at 25 [hereinafter *E&D Bids*]. However, it seems that the bonus is required *in addition* to the minimum work commitment of \$1.5 million.

45. Decree No. 2178, annex II, arts. 10.1.1 to 10.1.2.

46. *Id.* art. 9.4.

47. Argentine Hydrocarbons Law, No. 17,319, art. 26.

48. Decree No. 2178, annex II, art. 9.3.

provincial government or to the federal government, if the discovery occurs in the federal capital territory or on the federal offshore.<sup>49</sup>

The work commitment scheme used in Argentina may serve to increase bid participation among local companies like Perez Companc or Astra. Smaller companies may fare better with exploration bids because the successful bidder is able to spend its committed funds on exploration. In the United States, in contrast, the commonly used bonus bid is a direct payment to the government and a total loss to the bidder.<sup>50</sup> The Undersecretariat may also use its discretion to encourage Argentine oil companies to participate in the bidding process.<sup>51</sup>

The bid system established under the Argentina Plan is similar to the British system. However, the Argentine exploration bid system is more formula-based than the United Kingdom's exploration bid mechanism. The Argentine version, which requires defaulters to compensate the state for unspent but committed monies, *and* to provide security, is more efficient than the British equivalent. The British government has little recourse for unexpended commitments.<sup>52</sup>

## 2. The Size of the Exploration Blocks and the Total Area Offered

It will be interesting to see what sort of bids are made in the first round of bidding.<sup>53</sup> The minimum bid of \$1.5 million per block is negligible in exploration terms,<sup>54</sup> particularly given the huge areas of the blocks offered.<sup>55</sup> The largest blocks consist of 15,000 square kilometers (sq. km.) offshore and 10,000 sq. km. onshore. The smallest onshore blocks are in the 1000 sq. km. range.<sup>56</sup> Compared to their British and American counterparts, these blocks are huge. On the United Kingdom

49. *Id.* art. 9.9. Law 17,319 provides that exploration permittees must pay a royalty of 15% on any production made at the pre-concession stage. Argentine Hydrocarbons Law, No. 17,319, art. 21.

50. For a full discussion of the vices and virtues inherent in various bid systems, see Vass I, *supra* note 30, at 66-71 (discussing the cash bonus, royalty, profit share, and work commitment variables).

51. Bidders must establish a domicile in Buenos Aires and must prove their own technical competence and financial soundness. See Decree No. 2178, annex II, arts. 4.1 to 4.2.

52. Vass II, *supra* note 30, at 237.

53. These bids will be awarded in April 1992.

54. See, e.g., *E&D Bids*, *supra* note 44, at 25 ("For example, a [single] 2000m offshore hole is worth 1000 WU's (work units), a [single] 2000[m] onshore hole is worth 300 WU's.").

55. As in the United Kingdom, there is an additional flat fee for each square kilometer. This small fee is assessed annually. Decree No. 2178, annex II, art. 9.5.

56. *E&D Bids*, *supra* note 44, at 25.

Continental Shelf (UKCS), blocks average about 250 sq. km.,<sup>57</sup> while an American Outer Continental Shelf (OCS) oil and gas lease is only about one-tenth the size of the average British block.<sup>58</sup>

Decree 2178 is significant in that the blocks offered for bidding comprise a large percentage of Argentina's total sedimentary basins, and 140 of these giant blocks have been put up for bid in the first round. Only the acreage made subject to prior service contracts and the areas in the central producing areas reserved for YPF have been excluded from the bidding process.<sup>59</sup> Companies that own service contract rights have been given the option to convert their tracts into exploration permits or into concessions if the tracts are already productive.<sup>60</sup> The Argentina Plan also contains an additional market-oriented feature: Interested parties can, at any time, regardless of whether a bidding round is pending, request the right to bid on a selected tract. Such a tract might be available because it had been offered but not bid on; it was the object of a rejected bid; or it was never offered for bidding at all.<sup>61</sup> These tracts must be generally advertised to other potentially interested parties after the initial expression of interest.<sup>62</sup> This system could be characterized as an "open" bid model. By implementing this open bidding system, Argentina has provided the means for the petroleum industry to submit input into the permitting process.<sup>63</sup>

Development by the Argentine government differs from that of the United Kingdom in other ways than the method of bidding and the size of the blocks offered. The United Kingdom's success in rapidly developing the UKCS was possible largely because of the easy availability of large areas for licensed exploration and development.<sup>64</sup> In this respect, the Argentine government may be more successful than the British government in that its exploration and development program seems even more ambitious.<sup>65</sup> Most Argentine petroleum has historically been located on the land mass and not, as in the United Kingdom, on the Continental Shelf. Oil companies in Argentina are taxed like other

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57. Kenneth W. Dam, *Oil and Gas Licensing and the North Sea*, 8 J.L. & ECON. 51, 55 (1965).

58. Vass II, *supra* note 30, at 306.

59. Decree No. 2178, art. 1.

60. Decree No. 1212, art. 3. (1989) (Arg.).

61. Decree No. 2178, arts. 4, 12.

62. *Id.*

63. In the United States, Secretary of Interior Watt sought to involve industry in the choice of OCS tracts for leasing. Vass I, *supra* note 30, at 64.

64. Vass II, *supra* note 30, at 237-38.

65. Argentina has a lax system of environmental controls. There is no equivalent, for example, of the United States National Environmental Policy Act. One of the results is that the Argentine

corporations, at the rate of only twenty percent of profits.<sup>66</sup> Comparatively speaking, this is a very mild petroleum tax regime. Indeed, the Argentina Plan may well succeed in its attempt to stimulate exploration and development.

### B. *The Deregulation of YPF's Marketing Role*

Another recent and significant change in the Argentine petroleum industry is the deregulation of oil marketing. Until the end of 1990, YPF produced about sixty percent of Argentina's oil.<sup>67</sup> Previously, oil produced under service contracts had to be sold to YPF for a fixed fee, which was often set below market prices and in the local currency.<sup>68</sup> YPF would then sell the oil directly to domestic and commercial customers. Additionally, YPF had in place a quota system under which it sold some oil to certain major oil companies, for example Shell or Exxon, who then marketed the oil. This system constituted a major impediment to free enterprise hydrocarbon development.<sup>69</sup>

With the passage of Decree 1212 of 1989, the Argentine government abandoned the quota system, and since January 1, 1991, has allowed private companies to sell their oil production on the free market at the market price.<sup>70</sup> Companies that had previously entered into service contracts with YPF were given the opportunity to negotiate new production concessions.<sup>71</sup> Private producers were given the right to export all of their oil, and to repatriate all of their post-tax profits.<sup>72</sup> The Argentina Plan expressly grants the same privileges to new exploration permit holders.<sup>73</sup>

Before January 1, 1991, considerable concern existed in Argentina, given the impending Gulf War, that deregulation would result in massive

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government, like its British counterpart, has virtually untrammelled authority to select and license vast areas of the country for mineral development.

66. Decree No. 2411, art. 9 (1991) (Arg.) (abolishing former special hydrocarbon tax rate of 55%).

67. Roger Vielvoye *Argentina on Track for Oil Industry Revamp*, OIL & GAS J., Jan. 7, 1991, at 25.

68. Some of the latest service contracts had established fixed fees per barrel which approached international oil prices.

69. Shortly after oil marketing was deregulated, Vernon Jones, chairman of Apco Argentina Inc., a major "working interest" under the service contract for the Entre Lomas field, noted that "[t]his development gives us the incentive to further develop the field." *Argentina Deregulates Output from Entre Lomas Field*, PLATT'S OILGRAM NEWS, Jan. 28, 1991, at 2.

70. Decree No. 1212, arts. 3, 4.

71. *Id.* art. 3.

72. *Id.* art. 6.

73. Decree No. 2178, art. 6.

price increases. However, the government held firm over repeated objections from many quarters. International oil prices did not rise because of the war. Because of the government's perseverance, it has achieved deregulation of oil marketing, an absolutely necessary condition for the rapid development of the Argentine oil industry.

### C. *The Privatization of YPF*

By late 1990, the Argentine government decided to transform YPF into a private company by selling a majority of its stock to investors on the national and international markets in 1993.<sup>74</sup> The processes of streamlining YPF's operations and divesting its assets, however, began at the outset of the Meném administration.

The current president of YPF, Jose Estenssoro, has had extensive experience in the oil industry. Mr. Estenssoro, who was appointed by President Meném in 1990, has consistently advocated a market-oriented approach: "In every action we take, we'll reduce . . . [YPF's] share of participation. If Argentina's oil industry is going to grow, it's going to grow because of participation by the private sector."<sup>75</sup>

YPF's competitiveness has been hampered by problems that were (and to some extent, remain) legion. The company has historically been "notoriously inefficient."<sup>76</sup> According to one commentator, YPF's on-shore oil reserves cost fourteen dollars per barrel to produce as of early 1991. At the same time, private companies in Argentina produced the same oil for six dollars per barrel.<sup>77</sup> During the same period, YPF lost around 2,000 cubic meters of oil per day because it could not pay day-to-day maintenance costs.<sup>78</sup>

YPF's problems were not limited to high production costs. The company also incurred excessively high labor costs. Dominated by the Oil Workers' Trade Union, Sindicato Unido Petroleros del Estado

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74. *Argentina's YPF to Be Turned into Majority Private Firm; Asset Sales Set*, PLATT'S OILGRAM NEWS, Jan. 10, 1991, at 4. YPF became an incorporated entity, a *Sociedad Anónima*, in January 1991. The federal government currently owns 55% of the stock, and the provincial governments own 45%.

75. *Argentina's YPF Homes in on Privatization*, OIL & GAS J., Sept. 30, 1991, at 26.

76. Barham, *supra* note 16, at 21.

77. *Id.*

78. *Argentina Seeks Foreign Money for Drilling*, PLATT'S OILGRAM NEWS, Sept. 20, 1990, at 3.

(SUPE), YPF regularly ran up heavy deficits. In the 1980s, losses sometimes amounted to over \$1 billion per year.<sup>79</sup> With operations that included exploration, production, transportation, refining, marketing, and shipping, YPF became “a sluggish monster with 37,500 employees and the distinction of being one of the few major oil companies in the world that regularly managed to lose money.”<sup>80</sup>

YPF has also created environmental problems. YPF has typically conducted its operations with little regard for the environment.<sup>81</sup> Gas del Estado, the nationalized gas distribution system, has suffered from many of the same problems that plagued YPF.<sup>82</sup>

Faced with this scenario, the government developed a counter-program. One of the most important elements of the program is the deregulation of oil marketing. A major process of corporate streamlining and restructuring, and in some cases actually divesting (or “hiving off”) assets and operations, has also been set in motion. In general terms, the privatization of YPF bears some resemblance to Margaret Thatcher’s privatization of the former British National Oil Corporation (BNOC).<sup>83</sup>

However, the differences between the British and Argentine privatization schemes are also interesting. BNOC had a less dominant market position than YPF and simply used its still extensive exploration and production assets to float the new privatized company, Britoil. Additionally, BNOC retained its more circumscribed role in oil trading for several years after the privatization of its upstream activities. The YPF saga has taken different turns.

### 1. New Corporate Policies.

The reforms of YPF include measures to reduce its bloated labor force. In July 1989, YPF employed over 37,000 full-time and 15,000 temporary employees.<sup>84</sup> By August 1991, the combined total had been

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79. Malcolm S. Forbes, Jr., *Latin America—Next Economic Powerhouse*, FORBES, Sept. 16, 1991, at 23, 192.

80. Eugene Robinson *The Battle for the Soul of Latin America*, WASH. POST, Nov. 3, 1991, at A1, A25.

81. John Barham *Privatisation Leads to Oilfield Clean-Up*, THE FIN. TIMES, May 29, 1991, at 16. (“As a general rule, YPF ran its oilfields with astonishing disregard for basic environmental and operational safeguards.”).

82. *Meném Appoints Another Chief of Argentina’s Troubled Gas del Estado*, PLATT’S OILGRAM NEWS, Sept. 6, 1990, at 4.

83. For an analysis of the privatization of BNOC, see Vass II, *supra* note 30, at 272-79.

84. *Argentina’s YPF Oil Co. Hopes to Go Public by 1993*, REUTERS, Sept. 5, 1991, available in LEXIS, Nexis Library, Reuters File [hereinafter REUTERS].

reduced to 29,500.<sup>85</sup> YPF president Estenssoro intends to reduce YPF's total work force to 12,000 by 1993.<sup>86</sup> Clearly, changes such as these reflect an internal transformation made all the more remarkable because of SUPE's historically enthusiastic support of the Perónist party in general and of Meném in particular. Through its once powerful leader, Diego Ibañez, SUPE has sought to oppose the privatization program, but without success.<sup>87</sup> Estenssoro has managed to overcome opposition from this quarter.

Estenssoro also believes that YPF, in its old form, engaged in too many different types of operations.<sup>88</sup> Therefore, in addition to reducing its work force, YPF has begun to sell surplus assets. These assets include drilling rigs, tankers, and pipelines.<sup>89</sup> YPF is also divesting certain unproductive operations. The best examples of these operations are the refineries at Campo Duran (association or sale) and Dock Sud (sale).<sup>90</sup> The program of selling certain secondary fields and offering joint ventures in others is discussed below.

## 2. The Offering of the Secondary Fields

The first major element of President Meném's plan to privatize YPF's operations was the enactment of Decree No. 1055. The Preamble to the Decree notes that some of YPF's fields were inactive or suffered from low production, and that it was necessary to bring in private enterprise to "reactivate" them.<sup>91</sup> The Decree went on to define areas of "secondary interest" as those YPF-operated fields that had been inactive for five years or more, or that produced less than 200 cubic meters of oil per day.<sup>92</sup> The Decree required YPF to assist the Energy Secretariat in identifying the fields that were to be offered as exploitation concessions to

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85. Anne Harrison, *Argentine State Oil Giant to Go Public in 1993*, UPI, Aug. 21, 1991, available in LEXIS, Nexis Library, UPI File.

86. REUTERS, *supra* note 84.

87. *Array of Threats to Cavallo's Policies; Runaway Prices, Provincial Overspending, Union Defiance*, LATIN AM. WKLY REP., June 27, 1991, at 10; see also Barham, *supra* note 16, at 21. ("Mr. Diego Ibañez of the oilworkers' union likened the dismemberment of YPF to selling an inheritance.")

88. Harrison, *supra* note 85. ("We're spread too thin, we're all over the country but don't have depth.")

89. See YPF, WHAT YPF OFFERS THE MARKET (The Transformation Group Coordinator, Roque Saenz Pena Avenue 777, 8th Floor of 829, Buenos Aires, Argentina; also on file with *Tulsa Law Journal*).

90. *Id.*

91. Decree No. 1055, pmb. (1989) (Arg.).

92. *Id.* art. 2.

domestic and international bidders under a bonus system.<sup>93</sup> Bidders were given the right to dispose freely of the petroleum produced from their concessions.<sup>94</sup>

The program of selling the secondary fields has met with considerable success. The first sales of secondary fields were finalized in September 1990. A total of 133 secondary fields were sold in 1990 alone.<sup>95</sup> The first round of bidding attracted 125 offers, from which the government raised \$252 million.<sup>96</sup> The program of selling secondary fields still goes on today presenting oil companies with an opportunity to acquire marginal oil supplies cheaply. The reserves involved, however, are relatively small.

### 3. The Offering of the Central Areas

In addition to establishing the tender system for secondary fields, Decree No. 1055 created a new category of "Areas of Enhanced Recovery." This new category included all fields, other than secondary fields, in which YPF was carrying out enhanced or secondary recovery.<sup>97</sup> The government had decided at an early stage that YPF would retain large portions of Argentina's exploratory and productive acreage. However, the Argentine government recognized that it could not achieve its goal of revitalizing the country's oil industry without help. It was also clear that YPF needed assistance from private oil companies and allowed them to associate with YPF to raise output from the country's central producing fields.<sup>98</sup> The executive decided to put these areas up for international and domestic association or for joint venture bids.

Under Argentine law, a joint venture contract that created such an association or joint venture is classified as a *Union Transitoria de Empresas*.<sup>99</sup> In other words, private companies would be invited to pay a money bonus for the right to associate with YPF. Each field would have different bidding conditions to cover such details—for example, the level of participation offered and the nature of the operating responsibilities to

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93. *Id.* art. 4.

94. *Id.* art. 5(d).

95. *Newsletter*, OIL & GAS J., Mar. 18, 1991, at 3.

96. Will Ollard, *Argentina: Tricky Upstream Sell-Off*, PETROLEUM ECONOMIST, Nov. 1990, at 16-17.

97. Decree No. 1055, art. 9.

98. *Id.* pmb. ("Likewise, in those oilfields operated by YPF yielding a higher production [i.e., non-secondary fields] it is necessary to attain a higher recovery of oil through the adoption of techniques of associated production.")

99. *See* Law No. 19,550 (Arg.) (on corporations).



be assumed by the successful bidder. However, the Decree provided that each "participating compan[y] must offer modern technology."<sup>100</sup> These association contracts will run for twenty-five years.<sup>101</sup>

The administration projects that YPF will seek associations with private firms in a total of twenty-five fields.<sup>102</sup> However, YPF began the program in 1990 by soliciting association bids for four of its best producing fields: Puesto Hernandez in Neuquén Province (approximately 36,900 barrels per day (bpd)), El Huemul in Santa Cruz Province (approximately 16,300 bpd), Vizcacheras in Mendoza Province (approximately 13,300 bpd), and El Tordillo in Chubut Province (approximately 12,700 bpd). In total, these fields represent about thirteen percent of all Argentine oil production.<sup>103</sup>

The initial round of bidding on the newly offered associations was moderately successful. By early March 1991, YPF had received ten bids from groups representing both foreign and local companies. Awards were announced in April, and the successful bidders were: Occidental and the Argentine firms Pérez Companc and Petrolera Patagónica (Puesto Hernandez); Total (El Huemul); Repsol of Spain and Astra of Argentina (Vizcacheras); and Santa Fe Energy and Technint (El Tordillo). The sale raised slightly over \$600 million.<sup>104</sup> This amount was somewhat disappointing, because the Argentine government had anticipated that bids would total more than \$1 billion. The fact that post Gulf War oil prices were low probably accounted for much of the shortfall.<sup>105</sup>

The association program of the central areas is a critically important aspect of YPF's privatization. The goal of the program is to introduce private capital and technology in an effort to boost production and at the same time preserve some of YPF's assets for full privatization in the future. The sale of the secondary areas is also significant, even though much smaller reserves are involved. The policy has already begun to show results. Argentine oil output in 1991 increased slightly over the figures from 1990 and reached the country's highest level of production

100. Decree No. 1055, art. 11(b) (emphasis added).

101. *Id.* art. 11(e).

102. *Foreign Firms Bid to Associate with Argentina's YPF in 4 Concession Areas*, PLATT'S OIL-GRAM NEWS, Mar. 6, 1991, at 4 [hereinafter *Foreign Firms Bid*].

103. *YPF Oilfields Attract Foreign Companies*, LATIN AM. WKLY. REP., Mar. 21, 1991, at 3.

104. *Argentina to Allow Majority Ownership of Major Fields by Foreign Companies*, PLATT'S OIL-GRAM NEWS, July 26, 1991, at 3.

105. *Foreign Firms Bid*, *supra* note 102, at 4.

in nine years.<sup>106</sup> Further gains seem likely to follow.

#### 4. Privatization of Gas del Estado

Although the Argentine government has not yet completed its plans to deregulate the gas industry and privatize Gas del Estado, the Argentine Congress is now examining a bill that addresses these areas. N.M. Rothschild, a British investment bank, has been appointed to advise the Argentine government on how to privatize Gas del Estado.

Like the United Kingdom, Argentina has a well developed gas transmission and distribution system. However, Argentine gas production has historically been hampered by Gas del Estado's artificially low gas prices. Deregulation of this system should spur the exploration and development of natural gas.

### IV. OTHER IMPORTANT MACRO-ECONOMIC DEVELOPMENTS

The new Argentine petroleum regime has evolved in the context of broader market-oriented changes to the economy. Given President Meném's goal of exporting significant quantities of crude oil to surrounding nations, it is important to note the recent formation of MERCOSUR, a new common market composed of Argentina, Brazil, Uruguay, and Paraguay.<sup>107</sup> The primary objective of this union is to implement a progressive program of eliminating internal tariffs.<sup>108</sup> A secondary objective of the agreement is to achieve the economic integration of the member countries by 1995. MERCOSUR will also establish uniform customs tariffs for imports outside the member states. A common commercial policy concerning other countries and trading blocks is also on the agenda.

For the first time in recent history, Argentina has opened its economy to foreign competition. There is now a simplified three-tier division of the import tariff structure. Finished products are taxed with an import duty of twenty-two percent, while intermediate goods are taxed at eleven percent. Capital goods whose equivalents are not produced in Argentina are not subject to any duty at all. The government has also eliminated all import and export quotas and other qualitative constraints.<sup>109</sup>

106. *Argentina: Oil Output in 1991*, CHRON. OF LATIN AM. ECON. AFF., Jan. 21, 1992, at 1.

107. Treaty of Asuncion, Mar. 16, 1991 (ratified by Argentine Congress by Law No. 23,981 (Arg.)).

108. *Id.* art. 5(a), addendum I.

109. Decree No. 2184 (1991) (Arg.).

The government has also embarked upon a vigorous general privatization program. The aim of this program is to transform the economy from the state-controlled to the free market model. Entel, the telephone system, and the nationalized airline, Aerolineas Argentinas, were privatized in 1990. Apart from YPF and Gas del Estado, other planned privatizations include those of the electric and railway systems, the State Navigation company and waterways, and the Post Office. Secretary of the Economy Cavallo has also succeeded in curbing inflation and stabilizing the currency. Inflation now runs at less than two percent per month, a figure far below Argentina's traditionally exorbitant inflation rate. The current Argentine government seems committed to the creation of a market oriented economy, and specifically, to the fostering of a petroleum industry based on free enterprise.

#### V. CONCLUSION

The government of Argentina has altered the face of the Argentine oil industry, which the government considers critical to Argentina's economic development. Under the Argentina Plan, private companies may now obtain mineral permits and concessions. Production from oil concessions can be sold at market prices and exported anywhere in the world. Profits from such production are subject to total repatriation. Large quantities of exploration acreage are readily available, and only ten to twenty percent of Argentina's territory has ever been properly explored. Much oil has already been discovered onshore. The tax regime is mild. YPF, the once dominant state oil company, is being streamlined with a view to privatization, and Gas del Estado will soon follow suit. Argentina's production is likely to significantly increase as is the level of its oil exports. The sleeping giant is awakening.