

State procurement challenges

When government players change, businesses could encounter new rules and both sides could end up disadvantaged

When governments contract for products and services, they enter into what is commonly known as "procurement" contracts. Normally, regulations are enacted to ensure that such contracts are entered into fairly and transparently. Thailand has such a procurement law entitled the Regulation of the Office of the Prime Minister on Procurement (1992).

As these are contracts with governments, the question will arise as to what can be expected when there is a change of government. How can companies best deal with changes in government and what effects can such changes have on procurement contracts?

Thailand's PTT Exploration and Production Plc (PTTEP) has succeeded in bidding on an exploration and production sharing agreement (EPSA) in Bahrain. After five years of negotiations between PTTEP and the Bahraini government, there was a change of governments both in Thailand and Bahrain. A review of this contract's history is a perfect study in the issues that may arise with procurement contracts in the face of changing laws and governments.

In 2003, the Bahrain Petroleum Company (Bapco) issued a notice of public tender under the auspices of the Bahrain Ministry of Oil to 15 international oil companies to seek bids for petroleum exploration in Bahrain's offshore Blocks 1, 2 and 3. This was followed by a formal notice by the ministry, which restated the terms and expressly offered the following:

"Whether your company might be interested in entering into a Technical Evaluation Agreement under which existing seismic data would be reprocessed and interpreted in return for the right of first negotiation with regard to one or more or part of these Three Blocks, or a 'promote licence' whereby you may select an exclusive area within Bahrain's offshore area to study all available data for a limited period with the right to roll over into a PSA or a tax and royalty on agreed terms."

When none of the international oil companies made a bid, H.H. Sheikh Salman bin Khalifa Al-Khalifa, then the vice-chairman of Bapco, made exhaustive efforts to meet with the oil companies and create interest in Bahrain's offer.

Owing to these efforts, PTTEP accepted the invitation and offer of Bapco and the ministry. A technical evaluation agreement (TEA) was executed between the parties in May 2005. The TEA was in the form of a first option, giving PTTEP the right to evaluate Blocks 1 and 2 and move to enter into an EPSA to explore and develop the petroleum.

During the course of the bidding and PTTEP's one-year evaluation, Bahrain saw several changes in government. First, a significant amendment to the constitution was enacted, revising the makeup of the Bahrain government. A new government agency was also created named the National Oil & Gas Authority (NOGA) to oversee Bapco.

When PTTEP completed its evaluation and sought to enter into an EPSA for Blocks 1 and 2 under its right of first negotiation, NOGA interceded and blocked Bapco from doing so. Utilising its new authority, NOGA's chairman directed that a new bidding round be initiated under the Bahrain Government Tender Law that dealt with government procurement contracts. Bapco, through its newly appointed Chairman H.H. Sheikh Salman, objected to the NOGA chairman's implicit breach of the agreement with PTTEP.

Under Thai law, while government procurement and bidding is controlled by the Regulation on Procurement, petroleum exploration and production itself is governed by the Petroleum Act. Thailand's regulation on procurement is limited to "purchase", "service" and "employment" agreements. EPSAs are legally treated as "concessions", which differentiate them from either a "purchase", "service" or "employment" agreement.

For this reason, the Energy Ministry (through the Department of Mineral Fuels) issues announcements for bids following their own internal bidding procedures. The Bahrain Government Tender Law similarly did not apply to EPSAs or petroleum concessions.

Notwithstanding, Bahrain's NOGA chairman (who also acts as Bahrain's Tender Board Chairman) directed that a new public tender be started in 2007. That second public tender has since been completed, and PTTEP was again successful as bidder.

PTTEP and Bahrain both suffered a three-year delay as a result of the re-bidding which, by the time of its conclusion, resulted in a decreased offer from PTTEP than had been originally obtained following the original efforts of Bapco and its chairman H.H. Sheikh Salman. While Thailand's government also saw a military coup during the course of these events, this had no effect on PTTEP and its dealings with Bahrain during the entire process.

Government procurement agreements can be a risky proposition for contractors in the face of government change, owing primarily to the fact that there is little control or influence a party may have to ensure that contract terms are duly recognised and enforced following the government change. Even the strongest procurement contract will normally provide for adjudication under the laws and in the jurisdiction of the foreign government.

Unless such foreign jurisdiction has a strong and independent adjudicating body, they are likely to be influenced in favour of their own government. One potential solution is to provide for arbitration in a neutral jurisdiction with enforcement against collateral (e.g. bank letters of credit) that cannot be affected by any government change.

However, even where it is possible to litigate a breach of a procurement agreement and obtain a fair and enforceable judgment, few such cases are initiated. Contractors fear that even if successful, they will hurt their relationship with the government and suffer repercussions in the future through lost opportunities.

However, any government will lose credibility if it fails to uphold the contract terms entered into under its predecessors (and as a result, obtain less valuable bids in its tenders of procurement contracts, as was the case with NOGA's rebidding in Bahrain). This economic principle will normally keep governments honest in their dealings with contractors, despite government change.

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