

Petrobras in Bolivia: Is there a rule of law in the “primitive” world?

Fabio Costa Morosini & Michelle Sanchez Badin**

1. Introduction

What might lie behind a heterodox approach to legal disputes arising in the struggle for energy resources? Here, the State parties turn to bargained solutions, instead of reaching for remedies available in contracts and in investment treaties, as suggested by the mainstream literature on rule of law of the investment regime.¹ The First Part of this case-note explores the main regulatory instruments put in place between Brazil and Bolivia in relation to the regulation of hydrocarbons, which include documents as diverse (from a normative perspective) as memorandum of understandings, gentlemen’s agreements, standard treaties, contracts and exchange of diplomatic letters. Part II explores the political momentum in Bolivia that gave rise to a referendum and later the Decree expropriating foreign corporations operating in the country, and introduces the legal remedies available to Brazil and Petrobras. Part III explores the aftermath of the case, describing the new contractual arrangements between Petrobras and YPF and theorizing on the rule of law format that has employed through public-private negotiated processes. The case is concluded with a word of caution: mainstream explanations of what constitutes winning a case in international law and the legal processes involved therein need to be reconceptualized to include more holistic approaches and alternative legal formats.

* Associate Professor at the Federal University of Rio Grande do Sul School of Law and a research fellow at the National Council of Scientific and Technological Development (CNPq, Ministry of Science and Technology, Brazil). Specialises in international economic law.

* Professor at Getulio Vargas Foundation São Paulo School of Law, Brazil. Her research and teaching are mainly in the field of international economic law.

The authors would like to thank Marilda Rosado de Sa Ribeiro and Celso Lafer for discussing specific issues concerning this case, and Ricardo Flores Filho and Anna Carolina Cortellini for research assistance. We are also thankful to Bruno Pegorari for editorial assistance. Previous teaching materials on this case, with a different focus, were prepared by André Corrêa and Michelle R. Sanchez Badin at FGV. We thank them and other researchers involved in this research for sharing primary documents unavailable otherwise. Part of these teaching materials is available in Portuguese at <<http://ejurparticipativo.direitosp.fgv.br/material-de-ensino>>. See also: André R. Correa and Michelle R. Sanchez Badin, ‘Regulating property in the natural gas sector in Bolivia: any impact to the development of Bolivia and Brazil?’ (Seminario en Latinoamérica de Teoría Constitucional y Política, Buenos Aires, 2008) <http://digitalcommons.law.yale.edu/yls_sela/63/> accessed 23 April 2018. All errors remain ours. We reclaim the term “primitive” to react to a label that has been used by some scholars in the North to describe Brazil’s trade and investment relations with other countries in the Global South, based on our personal academic exchanges in 2015. Since then, we have tried to react to these simplistic characterizations in relation to Brazil and the Global South. See Fabio Morosini and Michelle R. Sanchez Badin (eds), *Reconceptualizing International Investment Law from the Global South* (CUP 2017) 326.

¹ For a critical approach on the uses of the rule of law by the World Bank, see Alvaro Santos, ‘The World Bank’s Use of the Rule of Law Promise’ in David Trubek and Alvaro Santos (eds) *The New Law and Economic Development: a Critical Appraisal* (CUP 2006).

I. Unveiling the public-private interaction in the design of the Bolivia-Brazil legal relations

Official bilateral relations between Brazil and Bolivia date back to 1867, when they signed a Treaty of Friendship Commerce and Navigation to regulate territory boundaries and freedom of navigation.²³ From then on, Brazil and Bolivia signed several other instruments to govern different aspects of what came to be a fruitful bilateral agenda.⁴

It soon became clear that relations between Brazil and Bolivia would center around hydrocarbons. Bolivia's rich natural endowment in oil and gas could be put into use in Brazil's large consumer market and rapid industrialization. Thus, Brazil and Bolivia started signing a series of agreements to promote and regulate their oil and gas transactions. In 1938, they signed a treaty on Bolivian outbound oil and its uses, where Brazil committed to perform topographic and geologic studies in Bolivia.⁵ In 1958, Brazil and Bolivia signed an agreement concerning technical studies about hydrocarbons with the purpose of improving their transmission from Bolivia to the Brazil.⁶ These agreement give the tone of Brazil and Bolivia relations: 1) Brazil's more developed economy and expertise in oil and gas production would assist Bolivia in developing their own sector; 2) Such assistance would come at the expense of Brazil benefiting from Bolivia's oil and gas reserves.

In 1988, under the rubric energy integration, the governments of Brazil and Bolivia conducted several negotiations and issued a series of documents - from exchange of diplomatic letters to treaties and contracts. In general lines, they stated Bolivia's commitment to sell hydrocarbons to Brazil and Brazil's commitment to buy Bolivian hydrocarbons.⁷ From the perspective of international law, it is worth noting that Petrobras's contracts with YPFB have been, from the start, embedded in bilateral diplomacy. In 1989, for instance, after Bolivian ENDE signs an energy supply contract

² See Roberto C. Albuquerque, 'A Nacionalizacao do Gas e Petroleo na Bolivia a Luz do Direito Internacional' (2006) RFDUSP Revista da Faculdade de Direito da Universidade de Sao Paulo 101, 479, 483-84. We avoid using the term nationalization to describe the situation in Bolivia because by the time the measures that gave rise to this dispute were adopted Bolivia's hydrocarbons already were the property of the country, according to its Constitution

³ Treaty of Friendship, Limits, Navigation, Commerce and Extradition [Treaty of Ayacucho] (La Paz, 27 Mar. 1967), the Empire of Brazil and the Republic of Bolivia, entered into force 22 Sep. 1868.

⁴ Arbitration Treaty (Petropolis, 25 Jun. 1909), the United States of Brazil and the Republic of Bolivia, entered into force 10 May 1912.

⁵ Treaty about Bolivian Outbound Oil and its Uses (Rio de Janeiro, 25 Fev. 1938), the United States of Brazil and the Republic of Bolivia, entered into force 15 Sep. 1938.

⁶ Agreement, by Exchange of Reverse Notes, on the Oil Supply of the Brazilian Market [Ata de Robore] (La Paz, 29 Mar. 1958), the United States of Brazil and the Republic of Bolivia, entered into force 29 Mar. 1958.

⁷ Agreement, by Exchange of Reverse Notes, Reference to the Joint Permanent Commission for Coordination (Brasilia, 17 Jun. 1988), the United States of Brazil and the Republic of Bolivia, entered into force 17 Jun. 1988. The governments of Brazil and Bolivia manifested in their notes the political decision to initiate the energetic integration between both countries.

with Brazil's ELETROBRAS and ELETROSUL, the Ministries of Foreign Affairs of both countries exchange correspondences to confirm the contract and its terms, which suggests state engagement beyond their state-owned enterprises.⁸ This type of pattern is repeated in 1992 in the supply contract of natural gas between Petrobras and YPF. In this case, in addition to exchanging diplomatic letters,⁹ the governments of Bolivia and Brazil entered into a Treaty of Partial Reach about Trade Promotion between Brazil and Bolivia for the supply of natural gas.¹⁰ This set of documents constitutes a network of public and private instruments complementing each other. And, for some, this has been qualified as a primitive form of legal apparatus in investment relations. We, however, reject the label of primitiveness and suggest that this is an alternative formulation of international law.

In addition to those legal instruments binding Bolivia and Brazil, and Petrobras and YPF in the hydrocarbon sector, Petrobras had made its investments in Bolivia under the protection of a standard Bilateral Investment Treaty (BIT) signed between Bolivia and The Netherlands. Although Brazilian officials rejected the standard BIT model protection for foreign investments, Petrobras International Braspetro BV, an incorporated subsidiary with headquarters in The Netherlands was able to benefit from protection under Dutch BITs, including the one signed with Bolivia, in 1992.¹¹ As a typical 1990 BIT, Petrobras could have recourse to a regime quite protective of its investments in Bolivia. Materially, Petrobras was protected under the standards of treatment available to foreign investors, such as national treatment and fair and equitable treatment. Procedurally, Petrobras was entitled to challenge Bolivian measures before an arbitral tribunal, according to Article 9.6 of the BIT that reads:

“If both Contracting Parties have acceded to the Convention on the Settlement of Investment Disputes between States and Nationals of other States of 18 March 1965, any disputes that may arise from investment between one of the Contracting Parties and a national of the other Contracting Party shall, in accordance with the provisions of that Convention, be submitted for conciliation or arbitration to the international Center for Settlement of Disputes.”

In April 1996, under center-right and Chicago educated President Gonzalo Sanchez de Lozada, Bolivia issued a new hydrocarbon law.¹² This Law assured that Bolivian

⁸ Joint Declaration (Brasília, 29 Nov. 1989), the Federative Republic of Brazil and the Republic of Bolivia.

⁹ Exchange of letters between Celso Lafer, Ministry of Foreign Affairs of Brazil, and Ronald Mac Lean, Ministry of Foreign Affairs of Bolivia, on the Agreement on the purchase and sale of Bolivian gas to the Federative Republic of Brazil. (Santa Cruz de la Sierra, 17 Aug. 1992), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 17 Aug. 1992.

¹⁰ Agreement on the purchase and sale of Bolivian gas to the Federative Republic of Brazil. (Santa Cruz de la Sierra, 17 Aug. 1992), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 17 Aug. 1992.

¹¹ In force since 1994 and terminated in 2009.

¹² Ley de Hidrocarburos (Bolivia, 30 Apr. 1996).

hydrocarbons, in whatever form, felt under the property of Bolivia and that no concession or contract could change that.¹³ However, the Law allowed the State to conduct its hydrocarbon activities in the following manner: 1) Hydrocarbon exploration and commercialization: conducted by the State through state-owned YPFB, who could undergo risk-sharing contracts with national or foreign corporations; 2) Hydrocarbon transport and distribution: could be delegated, by means of administrative concessions, to national or foreign corporations; and 3) Hydrocarbon reformulation and industrialization: could be conducted by national or foreign corporation.

In other words, although the State of Bolivia exercised property over its hydrocarbons, there was ample room for foreign corporations' participation at different stages of oil and gas production. Importantly, under this Law, the exportation of gas as raw material would give Bolivia only 18 percent of future profits,¹⁴ a fact that would ignite protests from left-wing Bolivians in the years 2000.

In November 1991, Bolivia and Brazil launched negotiations for the construction of the pipeline connecting Bolivia's gas fields to Brazil – one of the largest infrastructure projects in the history of these countries.¹⁵ And, in February 1993, an agreement between Bolivia and Brazil made specific references to a private agreement to be signed between their state-owned companies, Petrobras and YPFB, and properly described the public-private network of agreements supporting their investments in the gas sector¹⁶:

“Taking into consideration the Agreement for the Promotion of Trade between the government of the Brazilian Federative Republic and the Republic of Bolivia (for the supply of gas), the preliminary contract for the purchase of gas between Petrobras and YPFB and the Agreement, by exchange of notes, signed in August 17, 1992, in Santa Cruz de La Sierra, the entry into force of the contract, in this date, elevates our bilateral relations at a more complex dimension. In this dimension, we strengthen the mutual knowledge we have acquired through the

¹³ Ibid art.1.

¹⁴ Ibid art. 18.

¹⁵ Letter of Intent in the Agreement on the purchase and sale of Bolivian gas to the Federative Republic of Brazil. (Santa Cruz de la Sierra, 10 Aug. 1992), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 17 Aug. 1992. Previous negotiations were undertaken by the parties under the idea of a regional integration in the energy sector, e.g. Agreement, by exchange of Reverse Notes, on the Use of Bolivian Natural Gas in the context of Energy Integration (La Paz, Aug. 2 1988), the Federative Republic of Brazil and the Republic of Bolivia, entered into force Aug. 2 1988; and Agreement, by the Exchange of Reverse Notes, on Energy Integration (Brasilia, 7 Jul. 1989), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 7 Jul. 1989.

¹⁶ Agreement, by exchange of reverse notes, on the sale of Bolivian gas to Brazil, regarding the Definitive Agreement between PETROBRÁS and YPFB (Cochabamba, 17 Feb. 1993), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 17 Feb. 1993.

previous years and the *spirit* of cooperation that moves us to build the future” (free translation by the authors).¹⁷

The call for public and private arrangements is a lively part of the narrative in this agreement, much like what happens in the contract for the supply of natural gas, signed in August 1996 between Petrobras and YPFB, whereby the former agrees to buy and the latter agrees to sell for a 20-year period.¹⁸ It is a take or pay contract, and like the public documents signed or exchanged by their sovereigns that make references to the content of contracts, this contract mentions the 1992 Treaty of Partial Reach about Trade Promotion between Brazil and Bolivia for the supply of natural gas, and recalls their mutual interest in energy integration. Such pattern of mutual support between public and private regulations confirms the hybrid feature of these relations that fall somewhere in between the public and private regulatory spheres.

The 1996 contract regulated, *inter alia*, the manner in which the gas was transported from Bolivia to Brazil, including the financing of Brazil-Bolivia pipeline; the characteristics of the gas and criteria for its measurement; prices established in US dollars; and created a committee to monitor the execution of the contract – composed of 3 representatives of each Party. In addition, disputes arising from the execution of the contract could be taken to an arbitral tribunal:

“Every dispute, controversies and complaints that may arise from the interpretation or compliance with any clause of this contract [...] will be submitted exclusively to the American Arbitration Association of New York, under its Rules on International Arbitration.” (Free translation by the authors)¹⁹

Additionally, in 2003, Brazil and Bolivia signed a Memorandum of Understanding on Trade and Investment Promotion²⁰. This Memorandum elects a list of topics connected to trade and investment issues, including the financial support for these operations, as part of a single bargain. Moreover, this is a standard format of agreement that Brazil

¹⁷ The Agreement for the Promotion of Trade was signed in the structure of the regional organization named Latin America Integration Association, known as ALADI. See Agreement on the purchase and sale of Bolivian gas to the Federative Republic of Brazil. (Santa Cruz de la Sierra, 10 Aug. 1992), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 17 Aug. 1992.

¹⁸ Contract for the purchase and sale of natural gas (Rio de Janeiro, 16 Aug. 1996), Petrobras SA (a Brazilian mixed economy company created by Law 2004 of October 3, 1953 - President Joel Mendes Renno) and YPFB (a public company of the Bolivian State, represented by its executive president, Arturo Castanos Ichazo). (On files with authors).

¹⁹ “Todas las disputas, controversias y reclamos que podían suscitarse de la interpretación o cumplimiento de cualquiera de las Cláusulas del Contrato [...] se someterán exclusivamente a la American Arbitration Association de New York, aplicándose su Reglamento sobre Arbitraje Internacional”. See Contract for the purchase and sale of natural gas (Rio de Janeiro, 16 Aug. 1996) Petrobras SA and YPFB, cl 17.2.

²⁰ Memorandum of Understanding for the Promotion of Trade and Investment (Brasilia, Nov. 18 2003), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 18 Nov. 2003..

regularly employs to regulate its foreign economic relations.²¹ The Memorandum also created an executive working group led by diplomats from both countries, with the occasional participation of other public and private stakeholders.²² Similar structures have been used in the new Brazilian agreements on cooperation and facilitation of investments.²³

II. The (un)expected expropriation of hydrocarbons in Bolivia

By the beginning of the 2000s, at the domestic level, Bolivia was undergoing political unrest,²⁴ and the country's property rights over its hydrocarbons, including its governance structure, was at the heart of the debate. Left-wing Bolivians, a coalition of peasants and workers, accused President Sánchez de Lozada of selling Bolivia's resources to powerful countries and started a series of protests to regain property rights and control over hydrocarbons. These protests, which came to be known as the "Gas War", paralyzed the country, generated several deaths and left many injured, and culminated in President Sánchez de Lozada's renouncing and in Mr. Mesa Gisbert, then Vice-President, stepping up.²⁵

Attempting to respond to mounting criticism domestically, President Mesa called a binding referendum on Bolivia's energy policy.^{26,27} On July 18, 2004, 60.06 percent of

²¹ E.g. the Angola case analyzed by the authors in Michelle R. Sanchez Badin and, Fabio Morosini 'The Brazilian Approach to South-South Trade and Investment Relations: The Case of Angola' (2015) 43 *Denver Journal of International Law and Policy* 489.

²² Memorandum of Understanding for the Promotion of Trade and Investment (Brasilia, 18 Nov. 2003), the Federative Republic of Brazil and the Republic of Bolivia, entered into force 18 Nov. 2003, art. 3.

²³ Michelle R. Sanchez Badin and Fabio Morosini 'Navigating between Resistance and Conformity with the International Investment Regime' in Fabio Morosini and Michelle R. Sanchez Badin (eds), *Reconceptualizing International Investment Law from the Global South* (CUP 2017).

²⁴ From 2001 to 2006, Bolivia had five presidents in office: (1) Jorge Quiroga Ramirez (2001-2001); (2) Gonzalo Sánchez de Lozada (2002-2003); (3) Carlos d. Mesa Gisbert (2003-2005); (4) Eduardo Rodríguez Veltzé (2005); (5) Evo Morales (2006-...).

²⁵ See Roberto C. Albuquerque, 'A Nacionalizacao do Gas e Petroleo na Bolivia a Luz do Direito Internacional' (2006) *RFDUSP Revista da Faculdade de Direito da Universidade de Sao Paulo* 101, 479, 490.

²⁶ Referendum Vinculante sobre la Política Energetica del Pais (Bolivia, May 19, 2004), DS N. 27507. The questions asked were: 1) Are you in favor of revoking Hydrocarbons Law N. 1689, promulgated by Gonzalo Sanchez de Lozada? 2) Are you in favor of the State of Bolivia regaining property rights over all Bolivia's hydrocarbons reserves at the "well head" (boca de pozo)? 3) Are you in favor of President Carlos Mesa's policy to employ gas as a strategic asset to reach the Pacific Ocean? 4) Are you in favor that Bolivia exports gas under the framework of a national policy that: covers the domestic consumption of gas, promotes gas industrialization within the national territory, charges taxes on oil companies up to 50 percent of value of producing oil and gas, and allot the revenues of gas exports and industrialization mainly to education, health, roads and jobs?

²⁷ It should be noted that the referendum raised criticism from peasants and workers. According to them, the referendum was antidemocratic, because it was not intended to respond to their dissatisfaction, but to create momentum for a new hydrocarbons law that would not substantially differ from the existing one - especially in relation to foreign participation in Bolivia's hydrocarbon industry. See Roberto C. Albuquerque, 'A Nacionalização do Gás e

Bolivians voted in favor of the referendum. To contemplate the popular will expressed in the referendum, Bolivia revoked Hydrocarbons Law N. 1.689 and issued a new one, Law 3.058 of 17 May 2005.²⁸ Under the new Law, the State of Bolivia regained property rights over its hydrocarbons at the “well head,” to be exercised by YPFB.^{29,30} In other words, private and foreign corporations were no longer allowed to operate in Bolivia without the participation of YPFB. Importantly, the new law increased the “government taking” over oil and gas revenues. While in the previous law the government retained only 18 percent revenues, under the new law the government retains 50 percent³¹ - 18 percent in royalties and 32 percent in taxes levied on foreign corporations’ profits.³²

Even if the binding referendum at first sight seemed to contemplate the popular will, it raised strong criticism from peasants and workers – the drivers of this movement, as well as disagreement between President Mesa and Congress. More extreme critics argued that the questions formulated in the referendum were misleading and served only to confirm the *status quo*, an agenda attributed to the right-wing political elites.³³ Significant sectors of the Bolivian society remained skeptical about real changes brought by the new hydrocarbons law and continued to pressure for raising the royalty rate to 50 percent. In the light of increased discontent with his government, President Mesa stepped down on July 7, 2005.

In December 2005, Evo Morales took office as the first indigenous President of Bolivia. His political platform was built on resisting U.S. influence in Bolivia, favoring agrarian reforms and regaining complete ownership of the country’s natural resources. On May 1st, 2006, Morales issued the politically acclaimed Supreme Decree N. 28701, in which the state of Bolivia regained property, possession, and total and absolute control of its hydrocarbons. The main reforms were structured around three axis: 1) the property and exploration of gas; 2) Increase in tax revenues and royalty fees; and 3) Regaining control of certain activities and acquisition of the shares of foreign companies operating in the gas

Petróleo na Bolívia a Luz do Direito Internacional’ (2006) RFDUSP Revista da Faculdade de Direito da Universidade de São Paulo 101, 479, 490-91.

²⁸ Bolivia’s measures were part of a backlash against neoliberal policies experienced in different parts of the world and reaching its peak in 2005. See United Nations Conference on Trade and Development [UNCTAD] World Investment Report (Geneva, 2006) 23.

²⁹ Law N. 3.058 (Bolivia, 17 May 2005) arts 5 and 6.

³⁰ *ibid* art 17.

³¹ *Ibid* art 8.

³² These new rates, however should be put into perspective: the rates applied go back to Bolivia’s practice before 1996. In the 1990s, the country underwent a large privatization scheme and lower the royalties retained by Bolivia over its hydrocarbons in order to attract foreign investment following recommendations from the IMF and the World Bank. Seen from this perspective, the measures adopted by Morales are not that extreme. See Stephan Lefebvre and Jeanette Bonifaz, ‘Lessons from Bolivia: re-nationalising the hydrocarbon industry’ Open democracy UK (London, 24 November 2014) <<https://www.opendemocracy.net/ourkingdom/stephan-lefebvre-jeanette-bonifaz/lessons-from-bolivia-renationalising-hydrocarbon-indust>> accessed 23 April 2018.

³³ Albuquerque, ‘A Nacionalizacao do Gas e Petroleo na Bolívia a Luz do Direito Internacional’ (2006) RFDUSP Revista da Faculdade de Direito da Universidade de Sao Paulo 101, 479, 492-96.

production business.³⁴ In this case, specifically, this meant that: 1) Petrobras subsidiaries' production of oil and should be rendered to the state-owned company YPF; 2) YPF overtook the commercialization of hydrocarbons, defining its conditions, volume and price, both at the internal market as well as for export purposes; 3) new values should be applied to oil and gas revenues: 82 percent to the state (18 percent in royalties; 32 percent in taxes, and 32 percent for YPF); and 4) that the stocks of *Chaco SA*, *Andina SA*, *Transredes SA*, *Petrobras Bolivia Refinacion SA*³⁵ and *Compania Logistica de Hidrocarburos de Bolivia SA* were nationalized in order for YPF to assume control.

The measures taken by Morales produced negative economic effects on foreign corporations operating in Bolivia, including Petrobras, one of the country's largest foreign investor in the hydrocarbons sector. The measures taken by Morales raised several inconsistencies: (1) they conflicted with the Bolivian domestic legal process, including the hydrocarbons law in force at the time; (2) they breached contractual arrangements between foreign investors and YPF; and (3) they violated certain international investment agreements signed by Bolivia. Under existing rule of law, Petrobras was then left with at least three legal alternatives:

Petrobras could have sued YPF for breaching their 1996 contractual arrangements and demanded compensation under an AAA arbitration proceedings. (**Alternative # 1**)

Petrobras could have initiated an Investor-State arbitration against Bolivia, under the 1992 BIT between Bolivia and The Netherlands, asking for compensation to be decided in accordance with arbitration rules of the International Convention on the Settlement of Investment Disputes (ICSID) (**Alternative # 2**)

Petrobras could make use of the chain of agreements and other documents between Brazil and Bolivia developed under the rubric of regional integration on energy. Under these arrangements, Petrobras could access the Bilateral Working Group and work out a solution with Bolivia. (**Alternative # 3**)

To the surprise of many, Petrobras opted not to pursue any legal claim against YPF or Bolivia before an international arbitral tribunal, and, instead, decided to join public-

³⁴ In the case of Petrobras, YPF gained full control of two oil refineries: San Alberto and San Antonio. Petrobras and Brasil acquiesced and agreed on a compensation.

³⁵ By the time Bolivia issued the Decree, there were six Petrobras companies in the country: 1) Petrobras Bolivia SA (PEB), in control of production, exploration and commercialization of hydrocarbons; 2) Petrobras Bolivia Refinacion SA (PBR), in control of refinement, commercialization and transportation of products, by-products and other hydrocarbons; 3) Petrobras Bolivia Distribucion SA (PBD), in charge of commercialization, importation and exportation of hydrocarbons and by-products and industrial and automotive lubricant; 4) Petrobras Bolivia Transportes SA (PBT), owner and operator of the GASAM gas pipeline, between Brazil and Bolivia - GASBOL; 5) PETROGASBOL, in control of engineering, materials purchase and construction of the GASBOL pipeline; and 6) TRANSIERRA, a corporation in which PEB holds shares and is in charge of the operation of the Yacuiba-Rio Grande pipeline (GASYRG). See Marilda Rosado de Sa Ribeiro 'Sovereignty over Natural Resources Investment Law and Expropriation: the case of Bolivia and Brazil' (2009) 20 *Journal of World Energy Law & Business* 1, 7.

private negotiation under the third alternative described above. In the following section we explore what might explain Petrobras' course of action post-expropriation and its contribution to the theory of international dispute settlement.

III. Towards and an alternative rule of law in investment dispute settlement?

By the time the expropriation occurred, Brazil was governed by President Lula. From an ideological perspective, Lula was sympathetic to Morales' claim to regain control over Bolivia's natural resources.³⁶ Following the Decree, dismissing discontentment within Brazil, Lula issued the following statement in his Closing remarks at the XXX Summit of Mercosur States, in July 21, 2006:

"I have already demonstrated my comprehension to Bolivia's decision to nationalize its gas. I have stated in the Brazilian media and to many other aligned Presidents: do not expect me to bring a dispute against Evo Morales and Bolivia. We have reached the maturity to, although diverging and amid adversities, build consensus." (free translation from the authors)³⁷

Five months after the Decree expropriating foreign corporations operating in Bolivia, Petrobras was the first foreign company to officially abide to the new regulatory environment and enter into a new contract with YPFB for a new term of 22-years.³⁸ The first innovation of this contract was to assure YPFB's property rights over its hydrocarbons during all stages of production³⁹ ("at the well head"), but the contract also limited Bolivia's risks⁴⁰ and responsibilities. Technically, the parties switched from a

³⁶ In a seminar to celebrate bilateral relations with Bolivia in Sao Paulo, in December 5, 2015, Lula made the following statement prior to issuing the expropriatory decree: "Evo asked me: how would you react if we were to nationalize Petrobras?" Lula answered: "The gas is yours, the oil is yours. And that is how we reacted, respecting the sovereign right that Bolivia had over its soil." (Free translation from the authors). See Rubens Ricupero *A diplomacia na Construção do Brasil: 1750-2016* (Versal Editores 2017) 660.

³⁷ Ministério de Relações Exteriores [MRE] 'Resenha de Pol. Ext. Brasil', (Brasília 2006) a. 33, n. 99, 2o semestre, 52.

³⁸ Contrato de Operación entre Yacimientos Petrolíferos Fiscales Bolivianos y Petrobras Energía S.A. Sucursal Bolivia (La Paz, 28 Oct. 2006) (on file with the authors). As stated by UNCTAD: "In Bolivia, all foreign oil TNCs agreed to convert their production-sharing contracts into operating contracts, and to turn control over sales to YPFB, Bolivia's State-run oil company, as stipulated in the decree for the nationalization of oil and gas resources of May 2006. In addition, the Government reached a deal in 2007 with Petrobras (Brazil) to renationalize the country's only two oil refineries acquired by Petrobras in 1999 as part of a broad privatization programme." See UNCTAD World Investment Report (Geneva, 2006) 59.

³⁹ Contrato de Operación entre Yacimientos Petrolíferos Fiscales Bolivianos y Petrobras Energía S.A. Sucursal Bolivia (La Paz, 28 Oct. 2006) (on file with the authors) cl 4.3: "This Contract does not confer to its Holder [Petrobras] at any moment any property right over oilfields, which will remain at any time under State ownership. Even so, this Contract does not confer to the Holder at any moment property rights over hydrocarbons, which will be property of YPFB." (Free translation from the authors).

⁴⁰ See, for example, *ibid* cl 4.1, concerning the subject matter of the contract, where Petrobras undertakes the execution of the contract at its own risk, covering all costs - workers, technology, premises, materials and resources necessary for the its execution. YPFB, on the other hand, assumes no risk nor responsibility.

production-sharing contract to an operation contract (a type of services contract).⁴¹

The bilateral narrative between Brazil and Bolivia of peaceful relations kept its smooth course following the measures announced by Morales. Examples of such narrative directly connected to the settlement of the case of Petrobras' investments in Bolivia include:

- May 10, 2006; Joint Statement by Ministry of Minerals and Energy of Brazil and the Ministry of Hydrocarbons and Energy of Bolivia. Making references to Decree 28,701 and to the interest of the parties to deal with the issues bilaterally, a Joint Committee was created composed by representatives of the two ministries, YPFB and Petrobras, in order to discuss the transition and all pending issues concerning the new contract and forms of supply of gas to Brazil. This committee should be assisted by three working groups at the technical level.
- December 17, 2007; Joint Declaration. "Brazil-Bolivia: aiming at a strategic partnership." This document highlights the spirit of partnership and fraternity that permeates their bilateral relations, and put forward an agenda of furthering political integration through UNASUR; integration in the energy and infrastructure sectors; strengthening bilateral trade; technical and educational cooperation, and other areas. It should be noted that in the visit to Bolivia that gave rise to this document, Lula was accompanied by several representatives of the private sector interested in doing business in Bolivia. This could be read as evidence of Brazil's fostering new investments in Bolivia.
- December 17, 2007; Memorandum of Understanding on Energy between the Ministry of Minerals and Energy of Brazil and the Ministry of Hydrocarbons and Energy of Bolivia. This MoU details the implementation of new projects mentioned in the Joint Declaration (immediately above) – such as new regulations and competent agencies, financing mechanisms, and the involvement of state-owned enterprises. And, as the MoU elected diplomatic negotiations as the dispute settlement mechanism.

Coming back to the question posed in the title of this case, we challenge the notions that turning to contracts and investment treaties' provisions are the sole manner in which to resolve investment disputes. Alternatively, one should consider the combination of different instruments, such as those used in this dispute, as another type of rule of law. There is no doubt that Petrobras investments and the supply of gas to the Brazilian market were adequately settled under a negotiated process.⁴² This settlement was led by

⁴¹ About these and other current models of contract in the extractive industry, see UNCTAD World Investment Report (Geneva, 2007) 160. Another regulatory innovation available in the contract and that could work in Bolivia's favor relates to dispute settlement. The new contract states that disputes will be settled according to the arbitration rules of the International Chamber of Commerce, to take place in La Paz, in Spanish and under Bolivian laws. *Ibid* cl 22.

⁴² As well as other foreign companies, Petrobras froze its investments in Bolivia during 2006. But, by the beginning of 2007, Petrobras already took part of a new bid on a project to export Bolivian natural gas to Argentina. See UNCTAD World Investment Report (Geneva, 2007) 57.

a techno-political diplomacy, that included the Presidents of each country in the Joint Declaration, high-level technical diplomacy – the Bolivian Ministry of Hidrocarburos and the Brazilian Ministry of Energy –, and representatives of companies directly involved (Petrobras and YPFB).

It could be argued that the choice of instruments used by Brazil and Bolivia, and its oil and gas companies, in this case leads to a “primitive” type of rule of law, considering that there was a close public-private connection that could make unclear the prevailing interests and the rationality underneath. We, on the other hand, reject this label. This was a very peculiar situation: a context of few players in the market quite dependent on one another. Considering their limited alternatives, the costs of opting for Alternatives 1 and 2 seemed too high. The few players are the ones that jointly share decisions on: 1) policy planning for building the pipeline and the whole supply chain of the gas from Bolivia to Brazil; 2) financing resources to the projects, including the public support from Brazilian public banks; and 3) the connection of their legal arrangements (both public and private). The cost of an “exit strategy” to BITs and international arbitration⁴³ in this case could be unbearable.

Finally, it should be noted that the recourse to the techno-diplomatic negotiations was in tune with the macro political decision in Bolivia to withdraw ICSID and to denounce its BITs as the rule of law for inward investment.⁴⁴ And, almost ten years later, based on experiences such as this one with Petrobras in Bolivia, Brazil decided to include in its model agreements on cooperation and facilitation of investments an enlarged process of dispute prevention. The nature of this system is again a public-private structure facilitating techno-diplomatic coordination. Should we still read such types of arrangements as a “primitive” rule of law?

⁴³ UNCTAD identifies that the recourses to dispute settlement under traditional BITs take place when the situation is perceived by the foreign investors with “no possibility to continue their investment activities”, see UNCTAD World Investment Report (Geneva, 2007) 166. See also Brent Zaup, ‘A Neoliberal Nationalization? The Constraints on Natural-Gas-Led Development in Bolivia’ (2010) 37 Latin American Perspectives 123, about the structures of limited options in the case of Bolivia (and Brazil).

⁴⁴ Bolivia had twenty-three BITs in force, most of them signed during the 1990s. See data and agreements available at UNCTAD investment policy hub: <<http://investmentpolicyhub.unctad.org/IIA/CountryBits/24#iiaInnerMenu>> accessed 23 Apr. 2018. Bolivia send the notice to withdraw from ICSID in May 1st, 2007. This decision came into force only six months later, in November 2007. As to the BITs, for some of them Bolivia waited until their termination date without renewing it; and others were collectively denounced in 2013. It is not easy to access if there is any BIT still in force in 2017, due to inconsistencies under the main public databases.