THE ROLE OF LAW AND POLICY IN THE OFFSHORE PETROLEUM DEVELOPMENT OF CHINA

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This thesis examines the legal and policy regime applicable to the petroleum activities on the continental shelf of China. The distinguishing characteristics of this regime are revealed by way of a comparative analysis of the salient features of the offshore petroleum laws of China, the United Kingdom and Canada.

The modern Chinese offshore petroleum law and policy is essentially the product of the development of the domestic petroleum industry. The formulation of the contemporary regime was greatly influenced by the petroleum policies implemented by previous governments of China. The thesis therefore examines the history of the development of the modern Chinese petroleum experience and the current situation of China's offshore oil and gas industry. This establishes a context within which the presentation of the promulgation of China's offshore petroleum law and policy in the 1980s can be analyzed.

China opened its continental shelf for foreign oil and gas development somewhat later than other countries with offshore petroleum resources. Accordingly, China had the opportunity to study the experiences of other states, and to adopt selectively elements from foreign regimes to the advantage of its economic development. China's offshore
petroleum law and policy displays not only unique Chinese characteristics but also incorporates features common to many other offshore petroleum jurisdictions. The thesis identifies these special characteristics and common elements. The two together comprise the Chinese legal regime governing offshore hydrocarbon activities.

The goal of the policy of opening the offshore area to foreign oil companies is the promotion of the development of China's economy while safeguarding its sovereignty and economic interests. The analysis of China's offshore law and policy indicates how the Chinese government intends to reach this goal by means of law-making, and also how the interests of foreign investors are protected and the benefits accruing are shared. Accordingly, special attention is paid to an analysis of the Regulation of the People's Republic of China on the Exploitation of Offshore Petroleum Resources in Cooperation with Foreign Enterprises, and the Model Petroleum Contract drafted by the China National Offshore Oil Corporation.

China's offshore petroleum law and policy was formulated in the early 1980s. Since then, great changes have taken place in the international petroleum industry. The government of China has accordingly seen the need to modify its offshore petroleum policy from time to time. The thesis offers some comments on the modification of China's policies.

The thesis presents a comparative analysis of the oil
and gas laws of China, the United Kingdom and Canada, undertaken to show the differences in approach and substance between China and advanced oil producing countries in terms of legislation governing the development of the petroleum industry. Lacunae in the Chinese regime are also identified.

The thesis concludes with some suggestions on how China's offshore hydrocarbon law and policy should be improved in order to better serve the future development of China's offshore petroleum industry.
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Chapter One

The Evolution of China's Petroleum Law and Policy

I. Introduction

China has been aware of the existence of petroleum within its borders since the eleventh century BC. It was, at one time, the most advanced nation in the world as regards the development and utilization of crude oil. Although China's


2. The detailed description on the discovery of petroleum and natural gas was first made by Ban Gu of Han Dynasty (25BC-220AD) who recorded the petroleum reservoir in Gansu Province. The hydrocarbon reservoir in Gansu Province and in Xinjiang Uygur Autonomous Region were described in some other historic chronical of dynasties which followed. Crude oil was utilised in China a long time ago. The Chinese people used crude oil as fuel, illuminating material, lubricant and the raw material to make Chinese ink. Crude oil also served as a medicine to cure skin ulcers [the pharmaceutical value of crude oil were written down in the Pharmacopoeia of the Song Dynasty (960-1127AD)]. When people forged steel in ancient times, crude oil was used as cooling medium. Crude oil was used as a weapon as well as the key ingredient of gun power [in 578AD, when the Turks attacked Jiuquan City of Gansu Province, the local people burned down the enemy's military attacking appliances with burning crude oil and saved the city. Gun powder was invented by the Chinese people. In the Song Dynasty (the 11th century AD), the gun powder industry
modern petroleum industry dates from 1877, it was not until the 1960s that China became a major oil producing country in world terms. The large scale development of its offshore petroleum industry only began in the last decade.

A vital part of China's general petroleum policy, policies and laws governing offshore hydrocarbon activities were implemented by the PRC government to control cooperation between Chinese and international oil industries. This was a step of historic proportions, taken by the Chinese government to challenge its traditional oil policy, and to open up

was very prosperous and three main recipes to make gun powder contained oil products such as dense crude oil and asphalt. To serve the military purpose, the central government of the Song Dynasty then recovered a great amount of crude oil in Shaanxi Province]. The Chinese people in Sichuan Province also have a long history of using natural gas. Sichuan province bears a rich natural gas reserve and the people there started burning natural gas to boil down salt from bittern in Han Dynasty (206BC-220AD) and kept doing so until recently [Sichuan Province is far away from the sea and the transportation there is difficult. People in Sichuan Province could hardly acquire sea salt and had to drill wells for bittern in the underground and then boiled down bittern into rock salt. When people drilled bittern wells, they discovered natural gas. It was, therefore, natural that the Sichuan people used natural gas as a fuel to make salt. In ancient times, natural gas wells were called fire wells in China]. The Chinese people drilled wells to recover crude oil in the 11th century and drilled natural gas wells in the 2nd century BC, much earlier than the earliest recorded uses of western countries (the American people believed the well drilled in 1895 in Oil Creek near Titusville of Pennsylvania was the first oil well ever drilled in the world. It was 800 years later than that in China. Similarly, the English people were believed to be the first nation in the world to utilise natural gas in 1669, which was over one thousands years later than the Chinese people). See Chen Cheng-siang, Zhong Guo De Shi You (Petroleum of China) (Hongkong: Tiandi Publishing Ltd, 1979) at 15-25.
bright new prospects for the development of China's petroleum industry.

It has long been a desire of the Chinese government to tap China's offshore oil resources. The Chinese government has for some years hoped the development of its offshore petroleum industry would help resolve China's energy crisis and also bring in much needed revenue. However, China does not have sufficient capacity to recover offshore petroleum resources on its own, particularly in the deep sea area. Bound by a conservative ideology, the Chinese government had at one time no intention to cooperate with foreign oil companies which alone had the necessary expertise, even if this meant forgoing offshore petroleum development.

This attitude changed dramatically in the early 1980s when the Chinese government decided to open the offshore area to foreign oil companies. But the reason for this change in policy, its permanence, and future direction, remain major concerns of the majority of oil companies which are interested in China. The answers to these issues may be found by a review of China's past oil policies.³

³. For a more detailed analysis of the rationale behind China's interest in offshore oil, please see Chapter 2. intra. at 44-51.
The oil policies adopted by previous Chinese governments were the most important roots of China's present petroleum policy, and are hence of crucial importance in the present context. Virtually all the policies formulated by either previous or present Chinese governments relating to the petroleum industry stemmed from common roots. This in turn can be explained by reference to China's history and conventions, and the character of its social economic development.

China has been a country with a dominant centralised state power for thousands of years. A fundamental legislative principle adopted by all the powerful central governments which ruled China down the years provides that all profitable mines belong to the state, and the mining industry would be run directly by the government. These factors have given rise to two distinctive legal features which permeate the history of the development of China's petroleum industry. First, since the beginning of the modern petroleum industry era in China, ownership of petroleum resources is vested exclusively in the state. Second, the exploration and development activities of the petroleum industry have been totally controlled by government. These two features have characterized the process of petroleum policy making of the non-communist and the present Chinese governments and will be
important factors in assisting in understanding of legislative conceptions relevant to China's petroleum industry.

For such of its history, China has been a large scale agricultural country, with a self-sufficient economy; its governments were content that this should be so. Such social and economic conditions tends to result in an inward looking society. This was the case with China, which developed a government-sanctioned closed-door policy which rejected foreign influence. This trend was marked particularly in the case of the regimes in power before the late Qing Dynasty and after the establishment of the People's Republic of China in 1949 until the late 1970s. This fundamental consideration was the source of China's policy of self-reliance. The closed-door policy and the self-reliance policy dominated the development of China's petroleum industry for thirty years.

Even today, the self-reliance policy remains the most favourite principle of the PRC government in running the

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4. In 1772 the British government sent George Lord Macertner as an envoy of the British King to China to ask the Chinese government to agree to establish trade relations with Britain. The request of the British government was rejected by China. In a letter written by the Chinese emperor Qian Long to the British King, the first paragraph read as follows: "The Heavenly Dynasty (China) is abundant in natural resources and produces everything. It does not need to exchange goods with foreign countries to supply itself." Self-reliance acted as policy of the feudal dynasty was typically demonstrated in this example. See Guo Tingyi, Jin Dai Zhong Guo Shi Gang (The Outline of Recent Chinese History) (Hongkong: Chinese University Pressing House, 1979) at 41.
country, and holds a decisive balance in China's present petroleum policy. However, a conservative philosophy is revealed by these policies.

Historically, has China suffered frequent military, political and economic aggression from better developed western capitalist countries, largely due to its backward economy. These events promoted the development of a mentality which considered issues such as safeguarding sovereignty over natural resources, protecting national economic interests and handling foreign investment to be of paramount importance in developing China's petroleum law and policy. Regarding those subjects, the legislatures of pre-PRC governments made great contributions to solving the problem. In the 1980s, when the PRC government "opened China's door" again to the world, and decided to invite international petroleum industries to participate in offshore oil activities, it had plenty of experience to assimilate from China's former petroleum law and policy in dealing with foreigners.

5. Another important factor accounting for the boasting of the Chinese government of its self-reliance policy is that Mao Tsetung, Chairman of the Chinese Communist Party and the founder of the PRC, was born from a traditional peasant family. Because self-reliance used to be an utmost target pursued by most Chinese peasants for thousands of years, Chairman Mao's family background affected the formation of his world outlook. When Chairman Mao was in power, to great extent, this ideology generated the policy of the Chinese government. Chairman Mao was a strong advocate of self-reliance policy.
The development of China's modern petroleum industry took place under three generations of governments: Qing Dynasty\textsuperscript{6}, Guomindang regime\textsuperscript{7}, and the PRC. To develop China's petroleum industry, these three Chinese governments implemented their respective petroleum policies in legislation. The Qing government promulgated its law governing the recovery of petroleum in 1908. The Guomindang government promulgated similar laws in 1929 and 1931 respectively. In 1982, the current Chinese government promulgated its first petroleum law. Reflecting the continuous development of China's petroleum industry, China's present petroleum regime is a result of the evolution of the hydrocarbon laws and policies which were originally made by previous Chinese governments since the Qing Dynasty. The first law adopted by the Qing government on the mining of petroleum was very simple, but it laid down the principles influencing both the Guomindang government and the PRC government in their individual legislation regarding the petroleum industry. Along with the development of China's petroleum industry, China's petroleum law and policy grew more and more mature. In spite of their different political backgrounds, the later petroleum law has always been influenced by the previous one, as was China's

\textsuperscript{6} The last feudalist dynasty of China, 1644 - 1911.

\textsuperscript{7} Guomindang means National Party, which ruled mainland China between 1912 - 1949.
offshore petroleum law and policy.

When a new government took over the petroleum industry from the previous one, it also inherited the former official petroleum policy and reformed the policy to serve itself better. Ever since its establishment in China, the petroleum industry has been controlled directly by the ruling classes of the country, and enjoyed priority in legislation. Although the content differs, the petroleum law and policy of the Chinese governments at various times shares a degree of consistency, and there are inner relationships and many aspects in common among them. All the positive factors of the former petroleum policies of China were retained in that promulgated by the PRC. The study of the evolution of petroleum law and policy established by previous Chinese government will therefore be essential in analyzing the current law and policy governing China's offshore petroleum industry, which follows to a certain extent the basic principle of the former Chinese legislation.

II. Qing Dynasty's Petroleum Policy

China's modern petroleum industry was established in the late Qing Dynasty, which decided that the nature of petroleum law and policy formulated in China would be thoroughly
different from that adopted by the western countries. Oil fields have never been owned privately in China, and privately owned oil companies could not survive there. It was a principle in China prevailing for more than thousands of years in the feudalist society that all profitable mines and the mining industry belonged to the central government. By the time the Qing government proclaimed its petroleum policy in the early nineteenth century, its downfall was already unavoidable. The rulers of Qing government hoped the mining industry (including petroleum development) would soon bring huge economic benefit to consolidate their political power. As a political administration serving the imperial family, the government of the Qing Dynasty would naturally follow the example of the previous dynasties and claim that both oil resources and related mining right were owned by the empire.

In the mid-19th century, the Qing government launched a Westernization Movement and began to attach importance to the development of industry and introduce law evolved in the western style into China. The Qing dynasty's petroleum policy was a product of this Movement.

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8. To introduce technique of capitalist production, initiated by open minded bureaucrat in the latter half of the 19th century in order to preserve the feudal rule of the Qing government.
Before the Qing Dynasty came to assume power, there had been no civil or commercial laws governing China's industrial activities.\(^9\) The Qing government amended the industrial policy it had inherited to include the petroleum industry into the law.

The Qing dynasty had no distinct petroleum law. The development of petroleum industry was governed by a law entitled "The Official Regulations of Great Qing Dynasty on Mining Affairs" (hereafter "the Qing Regulations").\(^10\)

According to the law, petroleum mining came under the jurisdiction of the Agriculture, Industry and Commerce Ministry.\(^11\) Provincial mining affairs were governed by

\(^9\) "Opening the statute books published in China since the dawn of history until Qing Dynasty, only penal codes could be found. If hundred over hundred kinds of written law adopted in thousands of years of China's history were classified in the viewpoint of modern science of law, there would be no civil and commercial law, which were considered irrelevant compared to criminal law. That is an important feature of the Chinese legal system." Lin Jianhong, Fa Yu Zhong Guo She Hui (Law and Chinese Society) (Jinlin Province, China: Jilin Culture and History Publishing House, 1988) at 206, (my translation).

\(^10\) Promulgated under the imperial decree of Guangxu Emperor on the 13th of February, 1908. Da Qing Fa Gui Da Quan (Completed Collections of Laws and Regulations of Great Qing Dynasty), Book 6, Vol. 14 (Taibei, Taiwan: Kaozheng Publishing House, 1973) at 3076.

\(^11\) Ibid. Article 2.
The development of the petroleum industry was valued highly by the government of the Qing dynasty. The Qing Regulations classified all the mineral material into three types. Petroleum was classed as Type C, being treated in the same way as metallic minerals in the law. Such classification indicated that the exploitation of petroleum was very profitable and should be a government monopoly according to traditional Chinese political policy.

Under the Qing Regulations, landlords enjoyed rights to the surface of the land. Subsurface mineral deposits were the

12. Ibid. Article 3.
13. Ibid. Article 11.
14. In the Chinese feudal dynasties, which lasted for over a thousand years, all profitable mineral resources were run exclusively by the central government. This was an important traditional economic policy taken by all dynasties. Such a policy began with the Martial Emperor of the Han Dynasty (156-89 BC). At that time, the government exclusively possessed the trade of salt and iron. Factually, all the profitable mineral resources were monopolized by the government. Profit from such monopolies were major income for these dynasties. See Liu Xiuming, Xiong Cai Da Lue De Han Wu Di (Martial Emperor with Rare Gifts and Bold Strategy in the Han Dynasty) (Shanghai: Shanghai People's Publishing House, 1984) at 30-5.

See also Saeki Tomi, "The Salt and Chinese History" Vol V, N 11 Feb 1976 Shi Huo Monthly at 35. "Since the middle age of the Tang Dynasty (618-907), the (Chinese) government started to monopolize the trade of tea, salt spirits, iron and perfume. Such monopolies lasted until the late Qing Dynasty."

Because petroleum is a profitable mineral resources, according to China's traditional policy, the Qing government certainly would not relinquish control over it.
property of the state, and unauthorized petroleum recovery was not allowed.\textsuperscript{15}

The Qing Regulations provided that mining enterprises must apply for a licence to establish an oil company. The holder of a license was required to pay royalty on production to the government, and was also liable to taxation.\textsuperscript{16} The Qing government maintained an inflexible attitude in the enforcement of the state mining right, and stern punishment were prescribed for infringements of the law.\textsuperscript{17} In this way,

\begin{flushright}
\textsuperscript{15} "... Subsurface resources are vested in the State. Gold, silver, copper, iron, tin and other precious minerals are not allowed to be recovered without governmental permission.... Mineral rights are vested in the State. State-run, private or Sino-foreign joint venture mining companies shall hold licenses issued by the responsible Ministry before commencing mining." \textsuperscript{Ibid.} Article 14.
\end{flushright}

\begin{flushright}
\textsuperscript{16} \textit{Ibid.} Article 6.
\end{flushright}

\begin{flushright}
\textsuperscript{17} "Mining companies are not permitted to trade, exchange or mortgage mining properties privately. Any such infringement shall be punished under the law." \textsuperscript{Ibid.} Article 20.
\end{flushright}

"If the responsible authorities discover that a landowner has sold minerals extracted from his land without government authorization, the land shall be confiscated and the landowner shall be charged with the theft and sale of public property." \textsuperscript{Ibid.} Article 14.

As for the punishment, "In Ming (Ming Dynasty) and Ch'ing (Qing Dynasty) Law....Goods are assessed in terms of ounces of silver. Most serious was theft of goods entrusted to their care by supervisory or custodial officials. Theft of goods worth one ounce of silver or less was punished with a beating of 80 blows with the heavy stick and those worth 40 ounces nominally with decapitation (commuted in Ch'ing-Qing law to the exceptional punishment of punishment of penal servitude for 5 years). Next in order of serious were theft of public property by ordinary people...punishment started at a beating of 70 blows with the heavy stick in respect of goods worth 1 ounce of silver or less and ended with strangulation at 80
the Qing Regulations legislated the second legal basic right of the government with respect to hydrocarbons; recovery of petroleum was the exclusive privilege of the state.

The first well drilled using modern techniques was located in Taiwan Province and sunk in 1878.18 As soon as


18. At that time in North America, petroleum was extensively recovered for the purpose of power generation. The following quote describes the level of the development of the petroleum industry before the 20th century, which no doubt, stimulated the then Chinese government to search for oil resources.

"In the early nineteenth century, candles struggled against the gloom. More prosperous people could afford whale oil, and New Bedford flourished. Rock oil, scooped up from seepage, was famed for its medicinal properties but was too expensive to be used widely as an illuminant.

Edwin L. Drake, a colonel by courtesy but a man blessed with a simple, workable and original idea, brought more light. He copied the salt well driller's technique and deliberately drilled for rock oil which had polluted so many brine wells. It bubbled up by the barrel. And the kerosene lamp followed. It still illuminines more homes and huts around the world than electricity.

The history of oil can be grouped conveniently around the names of five men, who by design or accident marked after its period. Drake in 1859 found how to get oil out of the earth, by John D Rockefeller found how to get money out oil. Almost in the beginning of kerosene era there was Rochefeller....He built a towering fortune on Kerosene lamp and on lubricants. When the kerosene age began to sputter out, in this century, around the end of the nineteenth century, his marked position was so massive and impregnable that his fortune continue to mushroom, almost effortless, in the era that followed spindle top in 1901....For a half century the history of oil was also the personal history of John D. Rochefeller....His first investment in oil was made in 1862, only three years after Drake's discovery; in 1865 he had organized his first oil company; in 1870 he amalgamated this with the Harkness and Flagler plants and formed Standard Oil." Harvey O'Connor, The Empire of Oil (New York: Monthly Review Press, 1962) at 8-9.
the oil discovery was made, the Qing government immediately put the oil field under official control.\textsuperscript{19} In point of fact, no private oil companies were established during the time of the Qing dynasty, and the all petroleum exploration and production was directly undertaken and managed by the government.\textsuperscript{20}

To maintain their feudalist dictatorship, the Chinese emperors banned trade between China and foreign countries for centuries. When the door of China was forced open by imperialist powers in the nineteenth century, foreign investment was considered to be an economic encroachment upon China's sovereignty. Once the Qing Dynasty's glory was destroyed by the aggression of the imperialist countries, this government abhorred intrusions of the foreign capital and wished to be able to restrict foreign investment by law. The Qing government had not sufficient military forces to repulse the coming foreign invasion. It tried to repulse foreign intrusion into the economy by means of legislation. The Qing regulations restricted the activities of foreign investment in the exploitation of petroleum. The mains rules were as


follows:

1. Ownership of the Surface Land:

   Foreign companies were not allowed to become the owner of land where petroleum resources were located. In accordance with the Qing Regulations, foreign companies which jointly ventured with their Chinese equivalents to tap petroleum resources could only be granted a right to manage the mining business, and such right should be terminated as soon as the resources were depleted. Under law, foreign companies would not in any circumstances be allowed to own land from which the production oil was taking place.\(^{21}\)

2. Limitation of Investment:

   Foreign investments were limited to involvement in petroleum production. Because of its military defeat in the nineteenth century, the Qing government was forced to sign several unequal treaties with some imperialist countries. The contents of those unequal treaties contained the provisions allowing the foreign corporations to come to China to extract mineral deposits. The Qing government had to

\(^{21}\). *Supra*, note 10. Article 9.
accommodate companies established in the countries of the signatory powers, but wished to prevent any others from coming to China. The greater the number of foreign companies establishing in China, the greater the degree of humiliation experienced by the Qing government. Furthermore, the Qing government believed that foreign investors represented not only the impairment of China's sovereignty, but also constitute a threat to the political power of the Chinese government. Therefore, resisting foreign investment, no matter how inefficiently, was tantamount to the defence of the country in the eyes of the Qing government. In the eyes of the Chinese people, the Qing dynasty continues to bear the stigma of being the government which allowed foreign capital to exploit China's mineral deposits. This was one of the reasons why, when the PRC government decided to "open the door" after seventy years of foreign exclusion and invited foreign investment into China again, it dwelt at great length on provisions regarding national sovereignty in its offshore petroleum code. The PRC government was going to protect itself from being criticised as following in the steps of the Qing dynasty.

The Qing Regulations provided that only nationals of states which had signed the relevant treaties with the Chinese government were allowed to form a joint venture company with Chinese people to tap the petroleum resources. Foreigners of
states which had not signed treaties with China or which did not grant reciprocal rights to the Chinese people would not be allowed to exploit oil in China. Foreigners who did not abide by Chinese laws or foreigners who had a criminal record, foreign diplomats and foreign government employees, were not allowed to engage in oil mining.\(^{22}\)

3. Conclusion

The Qing dynasty conceived its petroleum policy and law in the final years of its power. By that time, China had been reduced to a semi-colonial country. The government was in political and economic trouble both at home and abroad, with the result that China's petroleum industry had no opportunity to develop.

The Qing government's petroleum law was somehow rudimentary. It did not wield much influence to the further development of China's petroleum industry. In formulating its mineral policy, the Qing government was motivated by the desire for quick success and instant benefit; it was not the first, nor was to it to be the last government to adopt such a short-sighted policy. Nevertheless, the Qing Regulations had put forward the basic legislative principles in running

China's petroleum industry, which has constituted the groundwork for future Chinese petroleum laws and policies. State ownership, state owned mining rights and safeguarding national economic sovereignty were the elementary legal principles laid down by the Qing government in its petroleum policy.

III. The Guomindang Government's Petroleum Law and Policy

China's petroleum industry took its first step towards development in the Qing Dynasty, but its foundation was laid under the Guomindang regime. The Guomindang government took the development of the petroleum industry more seriously than had the Qing dynasty, and made further progress with legislation.

Compared with the law governing the petroleum industry promulgated during the Qing Dynasty, the Guomindang government's petroleum law was a completely ideal statute. It was designed more rigorously as regards contents and more explicitly as regards the purpose. It not only further developed the legislative principles set down by the Qing government regarding the development of China's petroleum industry, but also established a series of new provisions to

23. See supra, note 7.
protect the petroleum resources, utilise private investments and provided for state participation in the exploitation of oil resources. A particularly estimable feature of the Guomindang government's oil law was the serious attention given to maintaining China's long-range interests in developing its petroleum industry. In handling foreign investments, the law showed itself to be an independent as well as a flexible political instrument of the Government. During Guomindang regime, China grew more expert in formulating its petroleum policy.

The Guomindang government successively promulgated two laws governing China's petroleum industry. The first was Provisional Regulations on the Exploration and Development of Kerosene (Petroleum) Mine (hereafter Provisional Regulations). The second one was the Mining Law (hereafter Mining Law), which was proclaimed two years after the Provisional Regulations. The Mining Law was the basic legislation governing the petroleum industry during the entire

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24. Promulgated by the ROC government in June of 1928 at the request of the Agriculture and Mining Ministry. Translation and Edition Division of National Legislative Council of the ROC edited, Zhong Hua Min Guo Fa Gui Hui Bian (Compilation of Laws and Regulations of The Republic of China), Volume 8, Book 6 (Shanghai, China: Zhonghua (China) Publishing House, 1934) at 266.

25. Adopted by the 88th meeting of National Legislative Council of the ROC on the 10th of May, 1930 and promulgated by the National Government on the 26th of May, 1930. Ibid. at 243.
period of Guomindang regime. The following sections offer a brief analysis of the Provisional Regulations and Mining Law respectively.

A. The Provisional Regulations

The Provisional regulations were tentative measures taken by the Guomindang government to manage its petroleum industry, remained in force for only two years. These rules were promulgated with the aim of obtaining maximum revenues for the government from the hydrocarbon production activities.

Two distinguishing features can be discerned in the Provisional Regulations; government control of activities, and the prohibition of foreign investment. Each will be examined in turn.

1. Government Control

The Guomindang government was not simply satisfied with maintaining the mining right of exploiting oil resources; it also wished ensure complete and direct management of the activities of the petroleum industry. The Provisional Regulations laid conspicuously emphasis on the government's intention to control the petroleum industry and promulgated
measures to bring this about. For instance, the law subjected oil companies to close official supervision. In this requirement can be seen a desire for a degree of control and involvement which presages the state-run oil companies, granted exclusive privileges by the government; such corporations were to be established worldwide in the decades following the end of the second world war.

The Provisional Regulations required that only two types of companies could apply for a license; those classified as an officially supervised oil company, or a company participating in a joint-ventured with the government. The government was entitled to place officials within either sort of company to exercise supervision over all aspects of management.26

Furthermore, the law give government the right to nationalize any licensed private oil company at any time. If this was considered necessary by Agriculture Mining Ministry considered necessary, nationalisation might be effected after submitting a report to the central government on the situation.27


27. Ibid. Article 2.
2. Banning Foreign Investment

The Provisional Regulations were drafted against the background of intensely national feelings as regards the involvement of foreign oil companies. Prohibiting foreign involvement of foreign oil involvement evidences the independent political stand of the Guomindang government at that time. This stance can be explained in several ways.

First, the income from exploitation of petroleum was an important financial resource of the Chinese government, which did not want foreign corporations to share this benefit. Second, there was a backlash against the policies of the Qing government. Due to weak political and military power, the Qing government had to accept the requirement by foreign countries to allow foreign enterprises to operate petroleum and other industries in China. The humiliating behaviour of the Qing government in the face of foreign demands now had a perhaps inevitable consequence. When the Guomindang government came into power, its first policy in this area was to prohibit foreign attempts to recover crude oil from China.

To demonstrate its patriotism, the Guomindang government resorted to the extreme measures in dealing with foreign
capital in the petroleum industry. The Provisional Regulations ruled out the possibility of foreign investment in China's petroleum industry. The law would penalize any violation of the provision. These measures were justified on the ground that they were in the best interests of China. Furthermore, moving against 'foreign economic plundering' demonstrated the political strength of the Guomindang government in contrast to the precursor of the Qing Dynasty government.

This policy was not without its costs. Foreign capital might have been utilised to promote the development of China's petroleum industry. But these consideration were overruled by reliance on the long-established principle of self-reliance and self-sufficiency. The Chinese people believed that without foreign interference China could develop and would continue to meet all its economic needs on its own. Besides, foreign political and economic invasions were bitterly resented by the Chinese people. These feeling influenced the actions of policy-makers accordingly. In the event, the closed door policy isolated China from the outside world and greatly hampered the progress of the Chinese society.\textsuperscript{28}

\textsuperscript{28} There was another reason for the Chinese governments, especially the governments in the feudal dynasties, to adopt a closed door policy. The past Chinese rulers were afraid that the incoming foreign influence would encourage the development of the capitalist elements in the Chinese society. The success of capitalism in China would jeopardize the feudalist dictatorship of the Chinese dynasties.
However, one result of these policies was that the Chinese petroleum industry was a domestic one for many years, before the participation of foreign investors in the late 1970s. The restriction was lifted - in appearance only - later, in the Mining Law.29

The restrictions on foreign participation meant that oil companies were to use 100% Chinese funds. Borrowing from abroad left the borrower open to confiscation of assets. Oil companies were not allowed to employ foreign staff, with the exception of technicians. The contract of the employment of foreign technician would be subject to the approval of the Agriculture and Mining Ministry.30

The Chinese petroleum industry expanded during Guomindang regime. Control of the sale of crude oil was a new concern of the government. The Guomindang government implemented a state restriction on the sale of petroleum. The Provisional Regulations provided that the government had the preferential right to purchase oil production. Contract for the sale of oil between Chinese oil companies and foreign traders were subject to the approval of the Agriculture and Mining

29. In spite the relevant provision in the Mining Law promulgated later on regarding the permit of the participation of foreign shares in China's state-run mining companies, foreign involvement in petroleum industry in the Guomindang's regime was not accepted in practice.

B. The Mining Law

The Mining Law proved to be of long duration and still applies in Taiwan. The promulgation of the Mining Law invalidated the Provisional Regulations. The leading provisions of Mining Law applicable to the petroleum industry were as follows:

(a) All petroleum deposits located within the territory of the Republic of China were owned by the state.\(^{32}\)

(b) The government enjoyed the preferential right to purchase produced petroleum, and the exportation of petroleum would be subject to the approval of the government.

(c) The government would establish reserved oil recovery zones if necessary.

(d) All oil fields would be run directly by the state. In the event that the government felt that it was

\(^{31}\) Ibid. Article 6.

\(^{32}\) Mining Law. Article 2. Supra, note 25.
not necessary for the state to run a particular oil field, a private oil companies might be allowed to lease that oil field. However, the lessee was not allowed to use foreign capital.\(^{33}\)

(e) If a private oil company leased an oil field from the government, the lease term would be no longer than twenty years. The term might be extended but renewal would not be more than another twenty years.

(f) The government would organise state-run companies to manage oil fields. Private and foreign interests\(^{34}\) should be allowed to participate the state-run oil company.\(^{35}\) State-run oil companies would be in the charge of the Agriculture and Mining Ministry.\(^{36}\)

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\(^{33}\) Ibid. Article 9.

\(^{34}\) Foreign shares might be claimed in the state-run mining companies; but the percentage of foreign shares shall be no more than 50%, the number of foreign directors should be no more than half of total number of directors and the chairman and general manager should be Chinese. Ibid. Article 5 and 50.

\(^{35}\) Ibid. Article 10 and 16.

\(^{36}\) Ibid. Article 48.
The Mining Law had three major objectives:

1. Establishing State - Run Oil Companies.

According to the Mining Law, petroleum industrial activities would be for the most part be operated directly by the state, and the government would rely on state-run oil companies as a principal means of recovering petroleum. The policy had a number of advantages for the government. First, the government could control the petroleum industry through state-run oil companies and directly manipulate the wealth created to support the national economy. Second, the government could access a pool of badly needed administrative managers and technicians trained in the oil companies, to assist with the development of other industries in China. Third, the government could readily adopt changes in policy as required by a given situation in order to better promote its development of the oil industry. The most important advantage of this policy was that the petroleum could be available for use in national defence.\footnote{37}

\footnote{37. This was one of the factors which influenced the development of petroleum policy in the United Kingdom in the early decades of this century.}
2. Measures to Protect Petroleum Resources.

The Mining Law stipulated two provisions to protect petroleum resources. The first was to set up reserved oil recovery zones. The second was to provide a fixed lease term for private oil companies during which they could recover oil.

These two provisions would effectively protect the petroleum resources and potentially increase the income of the government. When the state had insufficient capabilities to recover the oil resources in a promising area, the government was entitled to set up reserved zone to prevent the oil deposit from being damaged. The policy took the permanent interests of the country into account, which marked a significant difference from the former Chinese oil policy. The purpose of limiting the lease term of private oil companies was to preclude private enterprises from monopoly the oil resources, to exercise the government's positive dominion over the petroleum, and to ensure the maximum economic benefit to the state. Furthermore, since the law provided a limited lease term, private oil companies were under pressure to accelerate their exploration or production of oil, which would also be of help to China's economy.
3. Optimum Utilisation of Private and Foreign Investment

The Mining Law enabled Chinese oil companies to participate in the petroleum industry. In addition, the Mining Law also allowed foreign capital to be invested in the industry, thereby providing multiple economic forces to develop the petroleum industry. The Guomindang government's policy regarding foreign investments in the petroleum industry was to view foreign capital as a supplementary economic factor in support of the development of the industry. Foreign investors might participate in state-run oil companies under certain limitations and become a share holders of China's state-run oil companies.

The settled policy of the Guomindang government on foreign investment in the petroleum sector differed markedly from that of the Qing dynasty. The Qing government was forced to accept foreign investment, but the Guomindang government intended to utilize foreign capital in more focused way. The petroleum policy of the Guomindang government reflected an official desire to use foreign money to accelerate the development of China's petroleum industry. This consideration was similar to that of PRC's when it issued an invitation to foreign investment many years later.
C. Conclusion

The Mining Law was to govern the development of China's petroleum industry during the remaining years of the Guomindang regime. The law demonstrated an enhanced legislative proficiency in the government of the development of China's petroleum industry from this point on. The Mining Law was the vehicle whereby the Guomindang government brought about the promotion and development of the petroleum industry in China. The law laid down more concrete and pragmatic than Provisional Regulations. The general principle of the Guomindang government's petroleum policy was to increase the national economic forces and expand the strength of state-run oil companies to develop petroleum industry. This principle was well expressed in the Mining Law.

Notwithstanding the provisions of the Mining Law regarding possibilities for private Chinese and foreign participation, control of the petroleum industry remained firmly in the grasp of the Guomindang government. The regime gave serious consideration to the petroleum industry since petroleum was a very important material for the development of the economy, and also for national defence, and hence domestic and foreign politics. The Guomindang government did not allow
private or foreign capital to develop the petroleum industry independently of official control. Prior to the founding of PRC, state run oil companies were the rule in China.

The Guomindang government's petroleum policy underwent two stages of development. The first stage lasted until the World War Two. During this stage, the focus of policy remained on the economic value of the petroleum and the legislative objective was to protect national economic benefit and increase government revenue. Except for the legislation itself, the government did not offer special assistance to the petroleum industry.38

The second stage began at the breakout of World War Two. During this stage, the Guomindang government came to a full realisation of the importance of oil and gas to its military and politic affairs, and began to support its petroleum industry wholeheartedly. The development of the petroleum industry was now given top priority in the government's petroleum policy.

38. Between 1921-1929, some well known geologists surveyed the Yumen area, but the geological reports attributable to the surveys were then ignored by the government. It was only after WWII that actual development began. In fact, the Yumen Oil Field was the biggest development by the Guomindang government. See supra, note 20 at 10.
During the period of the Guomindang government, oil exploration had been limited, and had taken place mainly in Gansu Province, Shaanxi Province and Sichuan Province, where historical chronicles recorded oil discoveries in ancient times. The development of China's petroleum industry boomed during World War Two. During the Resistance War Against Japan, petroleum could not be imported from abroad. The Chinese government was pressed to produce as much oil as possible to meet national needs during the war. It was against such a background that the Yumen Oil Field, the biggest oil field discovered by the Guomindang government was found.\footnote{Located in Gansu Province, Yumen Oil field was developed in 1940. It was not only the biggest oil field in the Guomindang regime in China, but also one of the earliest developed non marine facies oil field in the world. The development of Yumen Oil Field greatly promoted the development of China's petroleum industry. Yumen Oil Field was an important base of China's petroleum industry. Petroleum produced from Yumen Oil field forcefully supported China's economic construction. Many of China's well know petroleum engineers, geologists and other technical staffs obtained were trained in Yumen Oil field. See supra, note 20 at 11. (my translation)} Between 1939 and 1948, the total oil output of Yumen Oil Field was 455 thousands tons, accounting for 72.3% of China's national oil production at that time.

After World War Two, China not only had the Yumen Oil Field but also took over some oil storage facilities and several oil refineries from the Japanese in the northeast of
China and Taiwan. In the year following the war, the extent of China's petroleum industry broadened to an unprecedented scale. This expanded industrial required a comprehensive policy to guide it. The Guomindang government's petroleum policy therefore began to stress the protection of the newly expanded petroleum industry, and to encourage the production of petrochemicals. The Guomindang government also wished to dislodge imported oil product from the Chinese oil market.

In 1945, the Guomindang government established China Oil Corporation, which was the first national oil company in China. The policy and experience of the Guomindang government anticipated the development of similar policies by the other developing countries. The legislative experiences of the Guomindang government in the development of the petroleum industry constituted valuable legacy to the current

40. "...over a long period of time, China's domestic oil market was controlled by foreign companies. Although this market was closed because of the breakout of Anti-Japanese War (World War Two), foreign oil companies wished to come back after the war. After World War Two, the provisional authorities appointed by the Chinese government to reorganise the Chinese petroleum industry strongly proposed that the future Chinese oil market should no longer be controlled by foreign companies and China's petroleum industry should be totally run by the Chinese government. This proposal was accepted by the Chinese government. Afterwards, the Chinese government established China Oil Corporation as a national oil company. China Oil Corporation was founded in July 1, 1946. Since then, China's petroleum industry and its relevant affairs in the Guomindang regime were in the charge of China Oil Corporation." (China Oil Corporation ceased to exist in Mainland China after the downfall of the Guomindang government) Supra, note 19 at 10, (my translation).
Chinese government.

Provisional Regulations and Mining Law were therefore important legal documents for the study of the evolution of China's petroleum law and policy. After the Guomindang government fled to Taiwan, mainland China did not promulgate a similar kind of law to govern its petroleum industry. The petroleum law formulated by the Guomindang government was well considered. The Guomindang government's petroleum law was evidence that China already had effective laws to protect and support its petroleum industry. Many of the legislative principles expressed by the Mining Law were absorbed by the legislators of the PRC government in the 1980s to develop China's petroleum industry.

IV. The PRC Government's Petroleum Policy

The idea that China is a country richly blessed with oil reserves was repeatedly suggested by many classic Chinese chronicles, which caused all the Chinese governments in history to truly believe that giant oil reservoirs were located somewhere in the national territory. Solving China's national energy problem once and for all through the discovery of huge crude oil reserves remained a dream for successive Chinese governments. The nationalization of China's petroleum industry, the organization of a state-run oil company and the
plan of absorbing private and foreign investment used to be the cardinal themes of petroleum laws and policies promulgated by the Qing dynasty and the Guomindang government. The fundamental purpose of all those petroleum policies was the discovery of sufficient oil to meet the demand of China's economy.

The PRC government's petroleum policy had the same target as the policies adopted by the two previous Chinese governments. With the beginning of the communist regime in Beijing in 1949, the oil industry in China entered a new stage of development. The new government was very conscious of the importance of this particular field of industry and placed great emphasis on it in economic planning. After the founding of the People's Republic of China, private and foreign enterprises disappeared from mainland China. The PRC government had to rely only on state action alone to develop the petroleum industry. While the petroleum law and policy of the Qing dynasty and the Guomindang government centred on how to harness the state, private and foreign capital in the development of the petroleum industry, the PRC's petroleum policy was centred on how to develop the petroleum industry by the state action alone. Because of its centralised political power, stronger than that of the Guomindang government and the Qing Dynasty, the PRC could mobilize all the active forces in China to reach its goal, and was thus in a better position to
secure the development of China's petroleum industry. The PRC government spared no efforts in the exploration for new sources of oil, and finally accomplished the purpose of building China into a major oil producing country.

As regards legislation, any review of the PRC government's petroleum policy must be divided into two historical periods. The first period covers from the 1950s to the 1970s. During this period, China developed its petroleum industry behind closed doors. The second period commenced in the 1980s. Since then, China has opened its doors to the investment of international capital through the implementation of the policies of economic reform. This required adjustment in petroleum policy. One result of this change in policy is that the Chinese government decided to invite foreign oil companies to help it to exploit its offshore oil resources. To meet this goal, some laws related to the petroleum industry and oil and gas operation had to be enacted at the outset. Since then, the development of the PRC's petroleum industry has been for the first time governed by a system of legislation.

The petroleum policy of the PRC will be examined in the two following sub-sections. The first concerns petroleum policy before the 1980s, and the second looks at the developments since then.
A. Petroleum Policy before the 1980s:

Before the 1980s, the PRC government's policy making procedure was quite different from that of western countries. The government's petroleum policy was not worked out through parliament and did not assume the form of laws, acts or regulations. The PRC government's petroleum policy was decided by the politburo and delivered in the form of administrative orders. Since any decisions regarding China's petroleum industry fell into the category of a state secret, it is rather difficult to trace the history of China's petroleum policy during this time. In addition to pervasive secrecy, the PRC government's policies were subject to frequent change, which increases the difficulty of doing comprehensive research on the topic. Understanding the PRC's petroleum policy must proceed through examining China's petroleum industrial activities.

The PRC government was aware that petroleum was the lifeblood of China's national economy and national defence. As soon as the PRC government unified mainland China, it placed the development of the petroleum industry on the most urgent agenda and did its best to support petroleum exploration and production. On the orders of the government, huge amounts of
money and personnel were committed to the exploration and development of oil fields. This strong government support of the petroleum industry is the key to understanding the PRC government's petroleum policy.

There are two notable features in the PRC's petroleum policy before the 1980s:

1. State Monopoly:

The Communist Party established the PRC as a socialist country. The government's general economic policy was to nationalise all the private enterprises. In 1956, the PRC government launched a political movement called the Socialist Transformation of the System of Ownership of the Means of Production⁴¹, with the result that all the private enterprises in mainland China were merged into state-run enterprises. Private capital as an economic force disappeared from China after this time. The objective of the petroleum laws and policies in the Qing dynasty and the Quomindang government - to monopolise the development of the petroleum industry - was easily achieved by the PRC government.

⁴¹ In the name of this movement, the PRC government had all the private enterprises annexed by the state-run enterprises. From then on, private enterprises were abolished in mainland China.
At the same time, the Chinese government had few diplomatic relations with western countries. It was impossible for international oil companies to enter China and work in the petroleum sector there.

In July of 1955, the Chinese government established the Ministry of Petroleum Industry and upgrade the level of the petroleum industry in China. Since then, China's petroleum industry has been under the direct leadership of the central government.\(^{42}\) The Ministry of Petroleum Industry managed all the oil fields in mainland China and the Chinese government had empowered it to enjoy the right of searching for and developing petroleum in China. China invested huge financial capital\(^{43}\) and mobilised enormous human resources\(^{44}\) to carry out the exploration for crude oil. With these investments,

\(^{42}\) Before 1955, China's petroleum industry was in the charge of the Ministry of Fuel Industry. Supra, note 20, at 23.

\(^{43}\) China's petroleum industry steadfastly focused on the exploration. During the period of the First Five Year Plan (1953-1957), the Chinese government allocated RMB 1.9 billion Yuan for the exploration of petroleum. The money made up of two third of the total state budget for the energy industry at the same period. Chen, Cheng-siang, Zhong Guo De Shi You Zi Yuan Ji Qi Fa Zhan (Petroleum Resources and Their Development in China) (Hongkong: the Chinese University of Hongkong, 1968) at 7.

\(^{44}\) For example, in 1952, according to the order of Chairman of the PRC government, a whole division of army soldiers were transferred to be oil workers. So were many more other army soldiers. Supra, note 20 at 2.
the development of China's petroleum industry then began to take off. During the following three decades, the Ministry of Petroleum Industry in Beijing commanded the management of the production of every oil field within the borders of China. This policy meant that the governments of oil-producing provinces had no right to participate in the exploitation of oil deposits, nor could they exercise any control over operations. This was an exclusively central government monopoly.

2. Self-reliance:

China is a very large country with a huge population and no other country in the world could be relied upon to help it to solve its energy problems. The Chinese government had to rely on itself to develop its petroleum industry.

Since the Opium War of 1840, China was reduced to a semi-colonial country. When the PRC government was set up, it denounced all the unequal treaties signed by the overthrown Chinese governments and abolished foreign concessions in China. The PRC government made China a politically independent country. In consequence, no foreign influence could survive in the PRC's petroleum industry.
In the 1950s, western countries placed an economic embargo on the PRC government due to the Cold War policy of the U.S. government. As a result, China could not import any advanced equipment or technology from foreign countries. In the 1960s, China suffered from a similar action taken by the Soviet Union. In the face of this international economic pressure, China closed its doors to undertake economic reconstruction. The hostile policy of foreign countries regarding the PRC was a crucial factor in the Chinese government's adoption of their self-reliance policy.

In practical term, China's self-reliance policy made a great contribution to the development of its petroleum industry. Almost all the large oil fields currently known were discovered and developed by Chinese geologists, engineers and other experts, without foreign assistance. In the 1950s, China discovered the Lenghu Oil Field in Qinghai Province and the Karamayi Oil Field in the Xinjiang Uigur Autonomous Region. Soon after, China discovered the Daqing Oil Field, which is the biggest oil field in northern China, and the Huabei Oil Field and Shengli Oil Fields in eastern China. In the 1963, China's petroleum industry achieved a significant goal when the Chinese government proudly declared that crude oil produced from China would meet its own basic demand.
The success created by the PRC government in the development of its petroleum industry was solely made due to state decisions and actions. In the process of the development of the petroleum industry, the Chinese government trained large numbers of technicians and manufactured all the required oil rigs, equipment and even oil refinery complexes. The PRC government did its utmost to cultivate the petroleum industry and it was eventually successful. The success of China's petroleum industry reinforced China's believe in its self-reliance policy with a result that this policy was applied nationwide to all the industries.

State monopolization and self-reliance in the development of the petroleum industry were the hallmarks of China's petroleum policy before the 1980s. Prior to the 1980s, China's petroleum policy played an important role in the development of its oil industry. However, China's prior petroleum policy had its limitations. Firstly, as a result of the central government's monopolization of China's petroleum industry, the provincial government had no role to play. One consequence of this was that the local government economy barely benefitted from the prosperity of the petroleum industry. Secondly, the total emphasis on self-reliance meant that advanced foreign technology or management experience, which could improve China's petroleum industry, were not being
used. Finally, there was no petroleum law in the PRC before 1980s. Without a petroleum law, China's petroleum industry could not be legally protected and its development could not be maintained at a permanent, steady and efficient level. Without a petroleum law, the Chinese public could not supervise the government's petroleum policy and could not defend their interests in the petroleum industry.

B. Petroleum Policy During the 1980s to the Present:

The essential difference between China's petroleum policy formulated prior to the economic reform of the 1980s and that formulated during and after that time was that the petroleum industry was no longer 'off limits' to international petroleum companies. This marked a significant new era for China's petroleum industry.

With the economic reform movement and open door policy, a dramatic change took place in China's oil and gas policy. The most significant change was that the Chinese government decided to open its continental shelf to international oil companies for the exploitation of petroleum. For this purpose, the Chinese government proclaimed a series of laws, regulations and detailed policies to govern development of China's offshore petroleum resources by means of domestic-

The Mineral Law is the fundamental law governing the tapping of oil resources in China. The only provision therein relevant directly to the petroleum industry is the reaffirmation that the ownership of mineral resources belongs

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45. Adopted at the regular session of the State Council of the PRC on Jan. 12, 1982; promulgated by the State Council of the PRC on Jan. 30, 1982.

46. Adopted at the 15th Meeting of the Standing Committee of the sixth National People's Congress, promulgated by the order No. 36 of the President of the People's Republic of China on March 19, 1986 and effective as of October 1, 1986.


48. "This Law must be observed in exploring and exploiting mineral resources within the territory of the People's Republic of China and in the sea areas under its jurisdiction." Mineral Law, Article 2:
to the state.\(^{49}\)

As a result of the general reform of China's economic policy, China's petroleum policy since the early 1980s became more complex. It can be divided into two parts. The first part applies to the onshore oil fields and all the other promising areas with good prospects of oil and natural gas. The policy for these areas remains the same as before: state monopoly and self-reliance. The second part applies to the offshore oil industry and the onshore frontier areas. The significant difference initiated by this policy is the invitation to foreign investors, and the possibility of cooperation with international oil companies in the exploration and development of the petroleum industry in offshore and frontier areas.

The petroleum laws and policy promulgated by the PRC government since the early 1980s were mainly designed to govern the Sino-foreign joint venture oil projects. Compared with the PRC government's petroleum policy prior to the 1980s, the present policy has two main difference:

\(^{49}\). "Mineral resources shall be owned by the state. The state ownership of mineral resources, either near the earth's surface or underground, shall not change with the ownership or right to the use of the land which the mineral resources are attached to." *Ibid.* Article 3.
1. The Establishment of New Management Mechanism:

International oil companies are encouraged to participate in the development of the petroleum industry in the ten southern provinces of China, but especially on China's continental shelf. To meet the new situation, the Ministry of the Petroleum Industry of the PRC was no longer the exclusive manager of China's petroleum industry. In 1982, the Chinese government established China National Offshore Oil Corporation (CNOOC), with a mandate to cooperate with foreign oil companies. To date, the development of China's petroleum industry has attracted dozens of international oil companies.

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50. Since its establishment, the Ministry of Petroleum Industry possessed two functions: the competent government authorities and the managing organs of the petroleum industry. In 1989, the Ministry of the Petroleum Industry converted into China Oil and Natural Gas Corporation. The competent authorities of the government over the petroleum industry is the Ministry of Energy at present.

Establishing a state-run oil corporation in China symbolised a turning point in the PRC's petroleum policy. This indicated that the Chinese government was going to end its rigid traditional government monopoly in the management of its petroleum industry and was ready to introduce fresh forces to reform its petroleum industry. This was the first concrete step taken after the issuing of China's offshore petroleum law.

2. The Participation of International Oil Companies:

Since the establishment of relevant laws permitting foreign oil companies to participate in China's offshore oil industry, self-reliance is no longer the only guiding principle of China's petroleum policy. The participation of international oil industry in China's exploitation of oil resources has affected the development of China's petroleum industry.

The PRC government's earlier oil policy, which was made and effected in an isolated environment, obstructed the further development of China's petroleum industry. To accelerate the modernization of this industry, China had to open its door to foreign investment. The Chinese government
was anxious to quicken the pace of the development of China's petroleum industry. It hoped that the utilization of international capital, advanced technology and scientific expertise could help it to achieve the purpose.

To open China's offshore petroleum industry to foreign investment was but a start in the reform of China's petroleum policy. The PRC government dared not ventured to deviate too far from the previous policy directions. Because of the aforesaid reasons, the current China's petroleum policy has the following characteristics:

(a) the state monopoly policy remains the basic policy as regards the development of major oil fields located on mainland China, and

(b) the joint venture policy is carried out in offshore oil industry and onshore frontier area.

In China's petroleum policy, self-reliance still remains as the dominating principle. However, the requirement of China's economic reform has made the Chinese government adopt

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52. At that time, a prevailing Chinese proverb was very popular among the senior Chinese government leaders, e.g. "feeling stones to go across the river (Mo Zhe Shi Tou Guo He)". To go across the river means to reform China's economy. Stones here refer to policies. The Chinese policy makers do not know which policy is firm and reliable for its economic reform.
a more and more flexible policy to develop its petroleum industry.

V. Conclusion

China evolved into a major oil producing country in the 1960s. The PRC government's accomplishment in the petroleum industry finally achieved what all the previous Chinese governments had only hoped to do. To some extend, the success of the PRC government's petroleum policy owes much to its predecessors' efforts and there is much in the PRC government's petroleum policy that is comparable with the policies of the Qing dynasty and the Guomindang government. When compared to other countries, China's petroleum policies are relatively unique. This is due, in large part to the reasons of historical convention, social economic development, domestic politics, international situations.

A conclusion may be drawn from the study of the evolution of China's petroleum law and policy. In China, the central government has closely controlled the development of the petroleum industry and at all times, the petroleum industry remains a servant of the government's general economic policy. The question whether to employ foreign investments in its petroleum industry has been a common theme of the last three
Chinese governments. Suffering many setbacks in the modern era, China keeps on improving its petroleum policy and law to promote the development of its petroleum industry. The petroleum policy formulated by the PRC government in the 1980s meant that the development of China's petroleum industry had started on a new path. When China began to shift its attentions to the outside world to develop its petroleum industry, it symbolised a remarkable advancement for China in the legislation of petroleum law.

China has commenced to break through the orthodox policy which hampered the development of its petroleum industry. The cooperation between China and international oil companies in the exploitation of petroleum resources will vitalise China's petroleum industry and lead it to a new realm. The change in China's petroleum policy has put China's petroleum industry to move forward from a new starting point.
Chapter Two

Policy and Laws Governing the Exploitation of Offshore Petroleum Resources in China

In keeping with the current of the time, ten years ago, the Chinese government struck out on a new path to develop its petroleum industry and opened its offshore territories to international petroleum companies. In order to attract foreign investment, the Chinese government promulgated its offshore petroleum law and other relevant laws applying to cooperative oil and gas activities in its offshore areas, and almost every foreign oil company was lured by the exciting hydrocarbon exploration prospects in the large expanse of Chinese waters.

China's offshore petroleum law was one of the more important legislative acts promulgated during 1980s in China. This law reflected general principles and official stands of the Chinese government regarding foreign investments. The establishment of such a law enabled many foreign oil companies to invest in China's offshore petroleum industry, which greatly promoted the development of this industry. In a way, China's offshore petroleum law pointed a new direction for the
Chinese government to develop its economy in future years. The study of China's offshore petroleum policy and law possesses a far reaching practical significance, going beyond hydrocarbons or even natural resources.

This chapter attempts to identify and analyze the policy and laws relevant to oil and gas activities in the Chinese offshore. To this end, the background, the legislative principle, context, and salient rules will be considered.

I. China's Rational for Inviting Foreign Exploitation of Its Offshore Petroleum

In the 1980s, a radical change of China's petroleum policy surprised the people who were interested in China's affairs in the western part of the world. In 1974, China's Minister of Foreign Trade stated that China "will never try to attract foreign capital to exploit domestic or foreign natural resources in conjunction with other countries."\(^{53}\) The above proclamation on behalf of the Chinese government impressed upon all the foreign legal experts on China's affairs at that time that China would stick to its self reliance policy to develop offshore petroleum industry.

However, before long, the Chinese government implemented an offshore petroleum policy which was comprehensively different from what it had pronounced. This fundamental change was initiated in 1978. It was in this year that China began to open its door to the foreign world. The Third Plenary Meeting of the Eleventh Congress of the Central Committee of the Communist Party of China made a decision to terminate its concentration on mass political movement and focused its policy on the development of the economy.\textsuperscript{54} In his government report of 1982, the Chinese premier announced to the Forth Meeting of the Fifth People's Congress that the Chinese government had decided to exploit offshore oil in cooperation with foreign countries on the basis of mutual benefit.\textsuperscript{55} From then on, China's continental area was legally opened to the international oil industries for tapping petroleum resources. The major international oil companies welcomed China's new petroleum policy, as is evidenced by the fact they rushed into

\textsuperscript{54} The meeting was held during December 18-22, 1978 in Beijing, which was considered as a milestone of China's modernization drive. Between 1966 and 1976, led by Mao Tsetung, Chairman of the Chinese Communist Party, a cultural revolution took place in China. This cultural revolution brought the development of China's economy to a stand-still and hurled the whole country into a political chaos. Following the death of Mao in 1976, new Chinese government leaders made a decision to end this cultural revolution and to shift the focus of the Chinese policies on the development of economy.

\textsuperscript{55} \textit{Supra}, note 20 at 176.
China to make bids for the exploration rights in China's offshore territories. Two questions arise at this point: why did the Chinese government substantially alter its prior petroleum policy and open its offshore area to foreign oil investments? Second, what was the objective of China's offshore petroleum policy?

Two reasons could be given for the promulgation of China's new offshore petroleum policy:

A. Energy Crisis

At the time, it was little known that China was facing a potential energy crisis at the end of the 1970s. China's oil output was 100 million tons in 1978, 106 million tons in 1979 and 105 million tons in 1980. No matter how hard the government tried, its oil production hovered around 100 million tons and refused to go up any further. Owing to the 10 years of fundamental political movements in previous years, beginning with the Cultural Revolution, China had paid no attention to the exploration of oil, and the available oil reserves were being rapidly consumed. If China could not promptly increase its proven oil reservoir on a large scale, it was very likely that the Chinese government would need to import crude oil again. It was at this time that the Chinese government initiated a large scale economic reform. Without
sufficient production of petroleum, China's new economic development plan would fail. The Chinese government need to expand the exploration and search for new oil resources to support its newly made economic policy. Since offshore China was considered to be a second Persian Gulf by geologists and the vast stretches of Chinese waters seemed extremely promising for oil discovery, the Chinese government expected an immediate benefit from recovery of oil there, and eventually determined on the exploitation of offshore oil deposits. At the beginning of 1980, the Chinese government formulated three policies to develop China's petroleum industry, the second one being to open its offshore area.\textsuperscript{56}

\textsuperscript{56}. In an officially published document named The Arrangement of National Economic Plan for 1979, China's National Planning Commission pointed out that the national economic plan for the petroleum industry was to strengthen the geological survey to increase oil reserves. For that objective the Chinese government then declared a new policy for the development of petroleum industry:

1. Contracting one hundred million tons of crude oil production to the Ministry of Petroleum Industry every year i.e. MOPI was only required to turn over one hundred million tons of oil annually to the state and was allowed to sell the excess of oil beyond the quota in the international oil market and retain the income at its disposal for the exploration and development of oil. In the meantime, the government would continue to allocate fund from state budget to the petroleum industry at the 1981's level.

2. Opening offshore continental shelf to international petroleum industries and inviting foreign bidders to explore China's offshore oil.

3. Granting the right to MOPI to import advanced foreign technology and equipment and borrow loans from international banks.

Because those policies broke through the boundary of long lasting self-reliance rules governing the petroleum industry, it was named "three pieces of important policy" by China's oil circles. See \textit{Ibid.} at 59.
B. The Requirement of the Economic Reforms

The development of China's onshore petroleum forced the Chinese government to develop its offshore oil reserves. For three decades since the founding of the PRC government, the petroleum industry provided endless funds and valuable energy for China's economic growth. The financial income turned over to the government from the petroleum industry gradually became a substantial part of China's national revenue. The foreign currency earned by exporting oil and oil products strongly supported China's modernization. The following are two tables demonstrating the importance of the petroleum industry to China's finance.
Table 1:
Percentage of State Revenue Contributed by the Petroleum Industry

<table>
<thead>
<tr>
<th>Period</th>
<th>Contributed Revenue from Petroleum Industry (100 million Yuan)</th>
<th>Percentage of State Revenue (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1953-1957</td>
<td>10.5</td>
<td>0.77</td>
</tr>
<tr>
<td>1958-1962</td>
<td>41.2</td>
<td>1.95</td>
</tr>
<tr>
<td>1963-1965</td>
<td>48.95</td>
<td>4</td>
</tr>
<tr>
<td>1966-1970</td>
<td>181.2</td>
<td>7.2</td>
</tr>
<tr>
<td>1971-1975</td>
<td>402.7</td>
<td>10.3</td>
</tr>
<tr>
<td>1976-1980</td>
<td>658.3</td>
<td>13.3</td>
</tr>
<tr>
<td>1981-1985</td>
<td>510.6</td>
<td>7.5</td>
</tr>
</tbody>
</table>

Table 2:
Percentage of State Exports Contributed by the Petroleum Industry

<table>
<thead>
<tr>
<th>Period</th>
<th>Total Petroleum Exports (100 million US$)</th>
<th>Percentage of State Export (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total Amt</td>
<td>Crude Oil</td>
</tr>
<tr>
<td>1961-1962</td>
<td>0.05</td>
<td>0.02</td>
</tr>
<tr>
<td>1963-1965</td>
<td>0.28</td>
<td>0.13</td>
</tr>
<tr>
<td>1966-1970</td>
<td>0.79</td>
<td>0.26</td>
</tr>
<tr>
<td>1971-1975</td>
<td>18.77</td>
<td>13.23</td>
</tr>
<tr>
<td>1976-1980</td>
<td>98.60</td>
<td>71.65</td>
</tr>
<tr>
<td>1981-1985</td>
<td>267.4</td>
<td>192.3</td>
</tr>
<tr>
<td>1961-1985</td>
<td>385.9</td>
<td>277.6</td>
</tr>
</tbody>
</table>

(The above tables are cited from China Today, Petroleum Industry, Vol.1, Chapter 5, pp 73)
To accomplish its plan for economic reform which was laid down in the late 1970s, the Chinese government needed to export more crude oil than before to increase its national revenues. Moreover, the expanding economy kept on consuming great amounts of oil.

Around the early 1970s, oil prices were skyrocketing because of the action taken by OPEC. Meanwhile, the U.K. and Norway had discovered tremendous oil reserves in the North Sea area, which attracted the interest of international petroleum companies to all the other undeveloped continental shelf areas in the world. The vast offshore territory of China certainly became a place which the international oil capital yearned for. Such a favourable situation was no doubt a factor influencing the Chinese government. The urgent need for oil and available foreign currency for the development of its economy made the exploitation of China's offshore oil resources an imperative concern of the Chinese government. The Chinese government pinned its hopes on the discovery of offshore oil fields. As a result, there would probably be no single issue so important to China in the 1980s as the development of its offshore oil. The offshore oil industry became the biggest project of Sino-foreign joint venture in China in that decade.
The Chinese government wished to be able to exploit its offshore oil as soon as possible, but it was short of the necessary funds and the requisite subsea oil recovery expertise. International oil companies also wish to be able to participate China's offshore oil industry. They have the financial funds, advanced equipment and expertise that China needed. The cooperative exploration of China's offshore oil resources would benefit both the Chinese government and international oil companies. It was therefore natural that the Chinese government would collaborate with foreign oil companies to tap its offshore oil resources.

The need to develop the petroleum industry and economic reform plan compelled the Chinese government to deviate its traditional state policy of self-reliance. Nevertheless, it did not move too far away from this principle. The areas designated for the development of the petroleum industry at that time were confined to the continental shelf.

Against such a background, the Chinese government worked out its offshore petroleum policy. China's rationale to invite foreign oil companies to explore its offshore petroleum resources was to absorb foreign capital and to use foreign technology in its petroleum industry so as to accelerate the development of China's economy. This was also the central
part of China's offshore petroleum policy and the legislative purpose of China's new petroleum law.

II. Main Provisions of PRC's First Mineral Resources Law

The decision made by the Chinese government to absorb foreign investments in order to develop China's offshore oil petroleum industry required it to formulate a series of relevant laws. These include the fundamental law governing the petroleum industry of offshore China - the Regulations of the People's Republic of China on the Exploitation of Offshore Petroleum Resources in Cooperation with Foreign Enterprises (referred to as 'the Regulations' hereafter). This was the first marine mineral code established since the founding of the PRC.

In a broad sense, the formulation of the Regulations was intended to safeguard China's sovereignty over its petroleum resources, maintain its economic interests and define norms for foreign investors in offshore China. The direct purpose of the Regulations was to maximize utilisation of foreign funds and advanced technology in developing China's offshore oil industry. The promulgation of the Regulations also met the

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57. Adopted at the regular session of the State Council of the PRC on January 12, 1982; promulgated by the State Council of the PRC on January 30, 1982.
requirements of foreign investors. They needed a firm commitment from the Chinese government in proper legal form to protect their interests before sinking their funds into oil ventures.

To serve the above legislative purposes, the Chinese government has formulated three basic principles to give effect to the Regulations. The first principle is that of permanent sovereignty over natural resources, as pronounced by the Charter of Economic Rights and Duties of States which was adopted by the General Assembly of the United Nations on December 12, 1974.58

58. In order to promote the establishment of new international economic order based on equality, sovereign equality, interdependence, common interest and cooperation among all nations, on December 12, 1974, the General Assembly of the United Nations adopted Charter of Economic Rights and Duties of States. The article 2 of the said Charter provides:

1. Every state has and shall freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities.

2. Each state has the right:
   (a). To regulate and exercise authorities over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities. No state shall be compelled to grant preferential treatment to foreign investment.
   (b). To regulate and supervise the activities of transnational cooperation and confirm with its national jurisdiction and take measures to ensure that such activities comply with its laws, rules and regulations and conform with its economic and social policies. Transnational corporation shall not intervene in the internal affairs of a host state. Every state should, with full regard for its sovereign right, co-operate with other state in the exercise of the right set forth in this subparagraph. Year Book of the United Nations Vol 28 (New York: United Nations 1974) at 381.
China has a history of being invaded and being oppressed by imperialist countries. In the past, due to the weakness and incompetence of the corrupt Qing dynasty, the Chinese government was forced to sign many treaties which humiliated the nation and forfeited its sovereignty to western countries. Because of damage to its national sovereignty, China changed from an independent country into a semi colonial country. During this phase, the Chinese nation was not treated with equality by other nations. The Chinese people witnessed how imperialists bullied China politically and economically. The issue of sovereignty remained a key political concern among the Chinese people. Because of the failure to defend China's sovereignty, the Qing dynasty was overthrown by the Chinese revolution.\textsuperscript{59} In World War Two, the entire Chinese nation was engaged in the Resistance War against Japan to defend China's sovereignty. the Anti-Japanese War lasted for fourteen years.\textsuperscript{60} These incidents of modern Chinese history were still fresh in the memory of the Chinese people. As a result, in their dealings with foreign countries, the Chinese people have a strong emotional need to safeguard their

\textsuperscript{59} After Opium War between China and Britain in 1840, the Qing government was forced to give up Hongkong to the U.K.. After Sino-Japanese War in 1895, China lost Taiwan Island. The Qing Dynasty was overthrown by the 1911 Revolution in China.

\textsuperscript{60} The resistance War against Japan in China started on september 18, 1931 and ended on August 15, 1945. The duration of the war was 14 years.
sovereignty. Therefore, to convince the Chinese people that the invitation of foreign investments to China would not damage China's interests, the Chinese government has to firmly express its attitude in the Regulations to safeguard China's permanent sovereignty over its natural resources during its cooperation with foreign enterprises to jointly recover petroleum deposits.

The issue of sovereignty is a common concern among host countries which invite foreign investors to tap their natural resources. China is a developing country that shares the common economic problems of fellow third world countries. To aid their economic construction, many other developing countries had already begun soliciting foreign investment long before China. These countries have accumulated certain experiences in handling foreign investment and in defending their sovereignty. If the Chinese government is determined to follow the examples of other developing countries to absorb foreign investments, it must assimilate their beneficial experiences and respect the favourable international practice. The acceptance of doctrine of permanent state sovereignty over natural resources settled the issue of sovereignty concerning host countries in their cooperation with foreign companies to develop their industries. It was a detailed lesson China on how to defend its sovereignty in a new situation. By the adoption of the principle of permanent state sovereignty over
natural resources, the concerns of the Chinese government regarding the sovereignty issue would be solved. Therefore, in establishing the Regulations, the above doctrine is the first principle to be observed.

The second principle is the rule of self reliance.

When expounding on China's policy regarding the invitation of foreign investment to China, the Chinese premier in his government report said: "connecting China with international market, expanding foreign trade, inviting advanced technology, utilizing foreign capital and developing all types of international economic and technical cooperation shall help China to overcome its shortcomings and build up its capacity of self-reliance." Self-reliance is a product of China's thousands of years of social economy and also an unforgettable lesson the Chinese government learned from bitter past experience. For centuries, the Chinese people suffered from the economic plunder of imperialist countries. They neither trusted nor wanted to rely on the help of foreign countries to tap its natural resources. Cooperation with foreign enterprises to explore China's offshore petroleum

resources symbolized a turning point of China's traditional policy and challenged China's inveterate conception of self-reliance.

In the early stages of China's offshore petroleum policy, the Chinese government questioned the feasibility of this policy. However, the Chinese government still used the policy as a tentative step in developing its petroleum industry. The Chinese government continue to debate the invitation of foreign oil companies to take part in its offshore petroleum industry. There is a vivid figurative description of China's offshore oil policy: "walking on two legs". "One leg" refers to the cooperation with foreign oil companies, "another leg" refers to the China's own force. For these reasons, the activities of the foreign oil companies would be restrained to a limited sphere. Economic reform and opening up to foreign investments has been a strong current in today's China, but the mainstay of China's general petroleum policy still remains self-reliance and the Chinese government would not deviate from it too much in its offshore petroleum policy.

The third principle is the principle of mutual benefit.

At the early phase of the official decision to absorb foreign investment to develop China's offshore oil industry, the Chinese government had set the tone for the joint venture.
In March of 1978, the central committee of the Chinese Communist Party and the State Council of the PRC authorized the Ministry for Petroleum Industry to establish commercial relations with foreign oil companies and create conditions to conduct cooperation with them. The MOPI was instructed to work with foreign partners on the basis of "independence, self-reliance, equality and mutual benefit".\(^{62}\)

The aim of foreign investors in offshore China was to make profit. The real bargain between the Chinese government and foreign investors lies in the exchange of oil resources for financial investment and technology. The Chinese government had to legislate in the Regulations to protect the legal right of foreign enterprises to obtain their deserved profits. Without the concrete provisions to ensure the justifiable right and interests of international oil companies, the plan of the Chinese government to invite foreign oil capital would not be able to come into being. To encourage foreign investors to develop China's offshore petroleum industry is another important objective of the Regulations. The regulations are required for the coordination of respective interests between China and foreign oil companies. So long as international oil companies could be certain that their interests in China's offshore petroleum industry would be protected, the prospect of tapping the vast

\(^{62}\) Supra, note 20 at 173.
oil reserves off China's coast would become the catalyst for increased cooperation between the Chinese government and major international oil companies. It was critical for the Regulations to handle economic benefits between China and foreign investors.

The Regulations mainly cover the following aspects:

A. Sovereignty and Ownership of Offshore Oil Resources.

The Regulations provide that all petroleum resources in international waters, the territorial sea and continental shelf of the People's Republic of China and in all sea areas within the limits of national jurisdiction over marine resources of the PRC are owned by China. In the above mentioned marine area, all buildings and structures set up and vessels operating to exploit petroleum as well as the corresponding on-shore oil (gas) terminals and bases, shall be under the Jurisdiction of the PRC.\textsuperscript{63}

These provisions confirmed China's sovereignty over its offshore petroleum resources and made all petroleum activities conducted in offshore China to comply with Chinese laws.

\textsuperscript{63} The Regulations. Supra, note 57. Article 2.
B. The Legal Position of Relevant Enterprises.

The Regulations provide that, on the premise of safeguarding national sovereignty and economic interests, foreign enterprises are allowed to participate in the cooperative exploitation of offshore petroleum resources of the PRC.

The investment of foreign enterprises participating in the cooperative exploitation of offshore petroleum resources, the profit due to them and their other legitimate rights and interests are protected by the Chinese government in accordance with the law. Meanwhile, all activities for the cooperative exploitation of offshore petroleum resources in China shall be subject to the laws, decrees and relevant provisions of China. All persons and enterprises taking part in petroleum operations shall be subject to the laws of China and shall accept inspection and supervision by the competent Chinese government authorities concerned. 64

64. Ibid. Article 1 and 3.
C. The Competent Authorities of the Chinese Government and the Exclusive Management Entity

The Ministry of Petroleum Industry shall be the competent authority in charge of the exploitation of offshore petroleum resources in cooperation with foreign enterprises.\(^{65}\) It shall determine the forms of cooperation, demarcate areas of cooperation, work out a plan for the exploitation of offshore oil in cooperation with foreign enterprises in accordance with long term state economic plans, formulate operation and management policies for cooperative exploitation of offshore oil and examine and approve the overall development program for offshore oil (gas) fields.

As a state corporation, China National Offshore Oil Corporation (CNOOC) has an exclusive right to explore for, develop, produce and market the petroleum within the zones of cooperation with foreign enterprises. Authorised by the Chinese government, CNOOC is entitled to call for bids and sign petroleum contracts to cooperate with foreign enterprises to exploit petroleum resources in the designated zones,\(^{65}\)

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\(^{65}\). The competent government authorities in charge of offshore oil industry is now the Ministry of Energy. The former Ministry of Petroleum Industry has converted into China National Oil and Gas Corporation.
surfaces areas and cooperative blocks.

The petroleum contracts and all documents signed by CNOOC for other technology and funds provided by the foreign enterprises are subject to approval by the Foreign Investment Commission of the PRC.\textsuperscript{66}

D. Basic Cooperative Patterns with Foreign Enterprises

Unless otherwise specified by the Ministry of Petroleum Industry or in a petroleum contract, the cooperation between China and foreign oil companies generally assumed the following forms:

(a) the foreign contractor shall be responsible for exploitation operation and bear all exploration risk.

(b) after a commercial oil (gas) field is discovered, both the foreign contractor and CNOOC shall provide the investment for its cooperative development and the foreign contractor shall be responsible for the

\textsuperscript{66}. The function of Foreign Investment Commission of the PRC has been performed by the Ministry of Foreign Economic Relation and Trade of the PRC (MOFERT). \textit{Supra}, note 63. Article 4,5 and 6.
development operations and productions.

(c) CNOOC shall take over the production operation when conditions permit as provided in the petroleum contract.

(d) the foreign contractor may recover its investment and expenses and receive remuneration out of the petroleum produced in accordance with the provisions of the petroleum contract.\(^67\)

After the foreign contractor's investment has been compensated as provided, the ownership of all assets purchased or built by the foreign contractor to exploit offshore oil shall belong to CNOOC.\(^68\)

E. Preferential Treatment to the Chinese Side

Foreign contractors shall give preference to employment of Chinese personnel, utilization of Chinese engineering design and Chinese services and purchase of Chinese made facilities.

\(^67\). \textit{Ibid}. Article 7.

\(^68\). \textit{Ibid}. Article 22.
In petroleum operation, the foreign contractor shall give preference to the employment of Chinese personnel.

Provided the terms are competitive, engineering design corporations of China shall have priority in entering into sub-contracts.

Chinese service includes geophysical prospecting, well drilling, diving, aircrafts, ships and oil bases.69

F. The Ownership of Information

Foreign contractors are required to provide information, reports and data obtained during the operation.

According to state sovereignty and international practice, in carrying out the petroleum contract, foreign contractors shall promptly and accurately report to CNOOC on the situation of petroleum operations and acquire complete and accurate data, records, samples, vouchers and other data with respect to various aspects of the petroleum operations and regularly submit to CNOOC necessary data and samples as well as various technological, economic, financial and

69. Ibid. Article 22, 12, 18, 20 and 21.
administrative reports.

The ownership of all the data, records, samples, vouchers and other original data obtained in the course of performing the petroleum operations shall vest in CNOOC. The utilization and transfer, donation, exchange, sale and publication of the aforementioned information and their export and transmission from China shall be subject to the Provision for the Control of Data promulgated by the Ministry of petroleum Industry.  

G. Other Requirements

All Chinese enterprises and foreign enterprises participating in the cooperative exploration of offshore petroleum resources shall pay taxes in accordance with the law and shall pay mining royalties. All employees of enterprises shall pay income tax.

The foreign contractor shall open a bank account in China.

Operators and sub-contractors shall comply with the relevant laws and provisions on environmental protection and safety in China.

70. Ibid. Article 13 and 23.
Any dispute arising between foreign and Chinese enterprises during cooperative exploitation of offshore petroleum resources shall be settled through friendly consultations. Otherwise arbitration may apply to the dispute by the arbitration body of the PRC or another arbitration body agreed to by the parties to the petroleum contract.\(^{71}\)

The Regulations are the legal foundation for the cooperation between China and foreign enterprises in the exploitation of oil in offshore China. They have full control over the key issues in offshore oil explorative and developmental operations. The Regulations has following major characteristics.

First, it outlined the cooperative method between China and foreign investors. Foreign investors' only right granted in the Regulations is to be able to obtain certain amount of crude oil after successful exploration, development and production of oil fields in China. Before having a successful commercial investment in offshore China, foreign oil companies have to take all the financial risks. The legal right of foreign investors will be protected by the Regulations, but their activities shall comply with laws of China.

\(^{71}\) Ibid. Article 8, 11 and 24.
Second, it is specified that the objective of cooperation between China and foreign investors is to develop China's national economy. The aim of the Chinese government to open its offshore areas to international oil industries was to expand China's capacity to develop its own economy and introduce advanced foreign technology. China wishes to make the best use of foreign funds and learn the required technology as soon as possible so that China will be able to command the exploitation of its offshore oil independently. Many provisions of the Regulations are stipulated to serve this purpose.

When a spokesman for the China National Offshore Oil Corporation officially talked to the press regarding the Regulations, he made a conclusive remark on the essence of the law:

"the Regulations have clearly provided that China enjoy the ownership and the jurisdictional right over the petroleum resources. The oil resources and the oil production produced from the contract areas belong to China. The location and the size of contract area and the cooperative partners shall be decided by China. When offshore oil fields go on stream, the fixed assets shall belong to China after foreign investors recover the investment. According to the provisions of the model petroleum contract, China shall take over the operation as soon as the conditions permit. All the important issues in the cooperation such as oil field developing plan shall be subject to the approval of the Chinese government. The Chinese government is entitled to participate in and supervise all the activities of cooperation. Petroleum bases must be located in China. Under the competitive conditions, China's goods, materials and services shall be
given priorities to be purchased and hired. The information and data obtained from the cooperation shall not be allowed to transfer, disclose, publish or sell without the permission of the Chinese government. In this way, China's sovereignty and interests shall not be infringed by the cooperative exploitation of offshore petroleum.  

The above was a precise summary of the Regulations.

III. Taxation and Royalty

The Chinese laws regarding taxation, royalty and customs duties which govern petroleum activities in offshore China are important components of China's offshore policy and law. Because those laws directly affect the net income of the Chinese government and the profit of foreign oil companies, both parties treat those laws seriously. The Chinese government expected to increase state revenue by levying more tax from the offshore oil activities. The foreign oil companies' investment policy in China was also affected by China's taxation laws. To balance China's own financial interests with those of foreign investors' is difficult.

Under the provisions of the Regulation, foreign enterprises operating in offshore China shall pay tax to the Chinese government according to the law.

The detailed laws regarding tax payment and royalties are also the concern of all the foreign investors in offshore China in the oil business.

To effectively handle the tax and royalty matters related to offshore oil industry, the Chinese government established the Offshore Oil Taxation Bureau in 1982. The headquarters of this bureau are based in Beijing and its branches have been set up in those areas where the China National Offshore Oil Corporation has established regional corporations, namely Shanghai, Tianjin, Guangzhou and Zhanjiang. Foreign enterprises shall pay their tax and royalties directly or through CNOOC to the Offshore Oil Taxation Bureau.

There are four relevant laws in China regarding the taxation and royalty payment of offshore oil activities.

(a) Foreign Investment Enterprise and Foreign Enterprise Tax Law of the People's Republic of China.\textsuperscript{73}

\textsuperscript{73} Adopted by the National Congress of the PRC on April 9, 1991 and effective from July 1, 1991.
(b) The Regulations on the Payment of Royalty for the Exploitation of Offshore Petroleum Resources.\(^74\)

(c) The Consolidated Industrial and Commercial Tax Regulations of the PRC.\(^75\)

(d) Rules Concerning the Levy and Exemption of Customs Duties and Consolidated Industrial and Commercial Tax on Imports and Exports for the Chinese-Foreign Co-operative Exploitation of Offshore Petroleum.\(^76\)

The following is the brief examination of laws regarding the foreign enterprises' income tax, foreign oil companies' royalty and the custom duties on imports and exports of Sino-foreign co-operative exploration of offshore petroleum.

\(^{74}\) Approved by the State Council of the PRC on December 5, 1988 and promulgated on January 1, 1989 under the Decree No. 1 of the Financial Ministry of the PRC.

\(^{75}\) Adopted in draft form by the Standing Committee of the National People's Congress on September 11, 1958 and promulgated on September 13, 1958. The law came into effect on the date of promulgation.

\(^{76}\) Approved on February 28, 1982 by the State Council and promulgated on April 1, 1982 by the General Administration of Customs and the Ministry of Finance of the PRC.
A. The Foreign Enterprises’ Income Tax

Under Foreign Investment Enterprise and Foreign Enterprise Tax Law (FIEFETL), all the foreign operators and contractors engaged in the exploration and development of natural resources on the Chinese continental shelf within the boundary of Chinese territory shall be taxpayers.\footnote{The term "foreign enterprise", as used in this law, refers to foreign companies, enterprises and other economic organizations that have establishments or sites in the PRC engaged in production or business operations, or that do not have such establishments or sites but nevertheless derive income from sources inside the PRC. FIEFETL. Supra, note 73. Article 2. As used in the preceding paragraph, the term "establishments or sites" primarily includes management establishments, - branches, offices, factories, places of extraction of natural resources, sites for contracted projects such as construction, installation, assembly or exploration projects, and sites for the furnishing of services (including consultancy services) for engineering and other projects. Implementing Rules of FIEFETL. Ibid. Article 3.}

The rate of the income tax shall be 30% of the taxable income plus the local income tax at the rate of 3% of the amount of taxable income.\footnote{Ibid. Article 5.}

Where enterprises engage in the cooperative exploration of petroleum, revenue shall be deemed to be derived when the
share of crude oil is received. The amount of the revenue so derived shall be calculated on the basis of a price that is adjusted periodically by reference to the international market price of crude oil of the same quality.\footnote{Ibid. Implementing Rules. Article 14.}

The geophysical prospecting and exploration expenses incurred by foreign oil companies operating in offshore China may be amortised in other contract areas owned by the same oil companies or in the future if the said companies terminated their operation for reasons such as the quantity of oil (gas) reserves.\footnote{"Reasonable geophysical prospecting and exploration expenses incurred by enterprises engaged in the exploitation of petroleum may be amortized by stages against the revenue derived from the oil (gas) fields that have already gone into commercial operation. The amortization period may not be shorter than one year." "If enterprise engaged in the exploration of petroleum have two or more contract areas, and operations in one or more of such areas are terminated for reasons such as the quantity of oil (gas) reserves, the reasonable geophysical prospecting and exploration expenses already incurred for such areas may by accumulated and treated as a capital expenditure, and amortized against the production revenue from the other areas." "If a foreign petroleum company terminates its operations in a contract area for reasons such as the quantity of oil (gas) reserves, and the company neither has successive contracts for exploitation of petroleum (gas) nor maintain in the People's Republic of China an operation and management establishment for the exploitation of petroleum (gas), such company shall be allowed to amortize its reasonable geophysical prospecting and exploration expenses with respect to the closed contract area against the production revenue the company earns from contract areas subsequently in its possession up to 10 years from the date of termination of the contract. The tax authorities must review and confirm the above situation and issue a certificate." the Implementing Rules of FIEFETL. Ibid. Article 48, 49 and 50.}
Before the promulgation of the FIEETL, the enterprises operating in offshore China were governed by The Income Tax Law of the PRC Concerning Joint Ventures with Chinese and Foreign Investment. As for the foreign oil companies engaged in the offshore China oil industry, the new law was more flexibly formulated than the previous one. The provisions regarding the amortization of geophysical prospecting and exploration expenses was an example.

B. The Consolidated Industrial and Commercial Tax

According to the Consolidated Industrial and Commercial Tax Regulations of the PRC (CICTR) and the Model Petroleum Contract prepared by CNOOC, 5% of the annual gross production of each oil field shall be used for payment of the consolidated industrial and commercial tax. The tax shall be paid in kind to the relevant authorities of the Chinese government through CNOOC. The CICT levied from crude oil produced by offshore oil fields is at the tax rate for "other industrial products" under the law. There is another tax rate

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81. Adopted at the Third Session of the Fifth National People's Congress, promulgated on September 10, 1980 and repealed at July 1, 1991.

for the production of mineral oil in accordance with this law. 5% of CICT applied to offshore oil production is a lenient taxation policy for the cooperation of exploiting offshore oil between China and foreign oil companies.

Besides, most offshore oil subcontractor services are subject to pay such tax at the rate of 3%.

"Basically, the CICT is a type of cascading turnover tax assessment on gross receipts arising from the sale or transfer of products. Tax liabilities arises at each level in distribution system and the tax is paid by the seller or transferor. In case of crude oil, the tax would be paid by the producer upon production. The tax is also applicable to purchases of foreign goods or imports." 85

C. Royalty Payment

The Finance Ministry of the PRC promulgated the Regulations on the Payment of Royalty for the Exploitation of Offshore Petroleum Resources (Royalty Regulations) on July 1, 1989, which was the first law governing foreign oil companies operating in China's offshore oil industry regarding royalty

83. According to the CICTR, the tax rate for mineral oil shall be 20%. See Ibid. the Table of Tax Rate for the Taxable Items attached to CICTR.

84. Ibid. Table of Tax Rate for Service Trades.

According to the previous policy, foreign oil companies should pay royalty to the Chinese government at the rate of 12.5% from the oil production for their annual output above the portion of 100 million tons. The Royalty Regulations adopted a new method to levy royalties from foreign oil companies.

Under the Royalty Regulations, royalty shall be exempted on the portion of the annual gross production of crude oil not exceeding one million metric tons; royalty rates for the portion of annual gross production of crude oil exceeding one million metric tons to one million and five hundred thousand metric tons shall be 4%, for the portion exceeding one million and five hundred tons to two million tons shall be 6%, for the portion exceeding two million tons to three million tons shall be 8%, for the portion exceeding three million tons to four million tons shall be 10%, and for the portion exceeding four million tons shall be 12.5%. The royalty rate for natural gas shall be zero for the annual gross production of natural gas not exceeding two billion cubic meters, 1% for the production exceeding two billion cubic meters to three billion cubic meters.
meters, 2% for the production exceeding three point five billion cubic meters to five hundred cubic meters and 3% for the production exceeding five hundred cubic meters.\textsuperscript{87}

Royalty for both crude oil and natural gas shall be paid in kind and be collected and administered by the tax authorities. Royalty for the cooperative oil and / or gas field with Chinese and foreign participation shall be first withheld by the operator of such oil / or gas field and handed over to CNOOC which will be responsible for the payment of the royalty.\textsuperscript{88}

In the past, the provisions regarding royalties were stipulated in the Model Petroleum Contract of CNOOC with a fixed rate of 12.5%. This rate would not be able to encourage the development of small or medium sized oil field. The royalty Regulations used a way of sliding scale to calculate the rate of royalty, which showed that the Chinese government became more flexible in formulating its offshore petroleum policy.

\textsuperscript{87} The Royalty Regulations. Article 3.

\textsuperscript{88} Ibid. Article 4 and 5.
D The Exemption of CICT and Customs Duties

According to Rules Concerning the Levy and Exemption of Customs Duties and Consolidated Industrial and Commercial Tax on Imports and Exports for the Chinese–Foreign Cooperative Exploitation of offshore petroleum (Customs Duties Rules), the following imported goods shall be exempt from duties and taxes:

(a) machinery, equipment, spare parts and materials verified and approved for the direct use in exploration and development.

(b) parts, components and materials verified and approved as necessary imports for manufacturing machinery and equipment in China for the exploitation of offshore petroleum.

(c) machinery and other engineering equipment, temporarily imported for exploration of petroleum and guaranteed to be re-exported by foreign contractors.
In addition to the above, crude oil received by foreign contractors in accordance with provisions of petroleum contracts shall be exempt from duties when it is exported.

China National Offshore Oil Corporation has been empowered to approve the importation of goods listed by Customs Duties Rules to be exempt from duties and taxes for the exploitation of offshore petroleum.

IV. Other Relevant Laws

Besides the above mentioned laws, to facilitate the cooperation between China and foreign oil companies, China has also promulgated some other relevant laws such as:

(a) The Law of the Territorial Sea and the Contiguous Zone of the People's Republic of China.\textsuperscript{89}

(b) Marine Environment Protection Law of the People's Republic of China.\textsuperscript{90}

\textsuperscript{89}. Adopted in the 24th meeting of the Standing Committee of the 7th People's Congress of the People's Republic of China on February 25, 1992.

\textsuperscript{90}. Adopted at the 24th meeting of the Standing Committee of the 5th National People's congress and promulgated by the order No 9 of the Standing Committee of the National People's
(c) The Regulations of the People's Republic of China on the Environment Protection and Management Concerning the Exploitation of Offshore Petroleum Resources.\(^91\)

(d) Marine Traffic Safety Law of the People's Republic of China.\(^92\)

(e) Provisional Regulations for Foreign Control of the People's Republic of China.\(^93\)

(f) Rules Governing Control over Inward and Outward Ocean Vessels, Goods for Purpose of Chinese-Foreign Cooperative Exploration of Offshore Petroleum and Personal Effects Belonging to

council on August, 1982 and effective as of March 1, 1983.

\(^91\). Promulgated by the State Council of the People's Republic of China on December 29, 1983.

\(^92\). Adopted at the 7th meeting of the Standing Committee of the 6th National People's Congress, promulgated by Order No. 7 of the President of the People's Republic of China on September 2, 1983 and effective as of January 1, 1984.

\(^93\). Adopted at the Regular Session of the State council on December 5, 1980 and promulgated by the State Council on December 18, 1980.
The legislative measures taken by the Chinese government not only provide solid legal protection and support to the cooperation between China and foreign oil companies in the exploitation of offshore oil activities in China, but also strongly promote the development of China's offshore oil industry. The establishment of those governing laws which apply to China's offshore petroleum industry demonstrated that China has had relatively comprehensive offshore petroleum legislations.

Among the offshore oil related laws listed in this section, the most significant ones are The Laws of the Territorial Sea and the Contiguous Zone of the PRC (Territorial Waters Law hereafter), the Marine Environment Protection Law of the PRC (Environment Law hereafter) and the Regulations of the PRC on the Environment Protection and Management concerning the Exploitation of the Petroleum Resources (Environment Regulations hereafter).

The Territorial Waters Law has demarcated the boundary of the Chinese territorial waters and explicitly pointed out through the legislation that Diaoyu Islands, Xisha Islands and

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Nansha Islands are the territory of China.\textsuperscript{95}

Japan and Korea have territorial disputes with China over the Diaoyu Islands and the demarcation of the continental shelf in the Yellow and East China Sea. Some southeast Asian countries such as Vietnam, the Philippines, Malaysia, Indonesia and Brunei have a territorial dispute over the Xisha (Paracel) and Nansha (Spratly) Islands in the South China Sea. Before the promulgation of the Territorial Waters Law, in spite of the provisions of the Regulations regarding China's sovereignty over its petroleum resources, the identification and the extent of China's continental shelf was a major problem concerning China's jurisdiction over its offshore resources, which hampered the development of China's offshore oil industry. The provisions of the Territorial Waters Law has clearly defined the boundary of China's territorial sea and its contiguous zone and declared the firm stand of the Chinese government to safeguard its marine sovereignty.

To be more effective in tapping China's offshore petroleum resources, the Chinese government has to attach importance to environmental protection while exploiting the

\textsuperscript{95} "The territorial land of the People's Republic of China comprises the mainland of the People's Republic of China and its offshore islands, Taiwan and all its attached islands including Diaoyu Islands, the Pinghu Islands, Dongsha Islands, Xisha Islands, Zhongsha Islands, Nansha Islands and all other islands which belong to the People's republic of China." The Territorial Law. Supra, note 89. Article 2.
oil reserves. It is critical to avoid marine pollution caused by offshore oil industrial operations carried out in China. The promulgations of the Environmental Law and the Environmental Regulations were vital measures to serve the above purpose. In particular, the Environmental Regulation was formulated for the offshore oil industry under the provision of the Environmental Law. It stipulated in detail regarding the issue of environmental protection related to the offshore petroleum industry.

There are three prominent characteristics of the Environmental Regulations:

(1) To safeguard China's sovereignty

Under article 2 of the Environmental Regulations, "these regulations apply to the enterprises, managing units, operators and individuals who are engaged in the exploration and development of petroleum in the offshore areas under the jurisdiction of the People's Republic of China and the fixed and movable platforms and other facilities used by them." This provision indicates that the execution of the Environmental Regulations is to exercise China's jurisdiction within its territorial waters.
(2) In conformity with the United Nations Convention on the Law of the Sea

The United Nations Convention on the Law of the Sea (Conventions hereafter) provides that States have the obligation to protect and preserve the marine environment.\(^{96}\)

Part XII of the Conventions requires all coastal states to establish national laws to protect maritime environment and prevent its internal sea from being polluted.\(^{97}\)

The establishment of the Environmental Regulations is also meant to address China's international obligations.

(3) Paying attention to preventing marine pollution.

When marine pollution produces a serious consequence, it will take a long time and huge amount of money to wipe it out. Therefore, the Environment Regulations give full expression with respect to prevention.


\(^{97}\) "States shall adopted laws and regulations to prevent, reduce and control pollution of the marine environment arising from activities in the area under taken by vessels, installations, structures and other devices flying their flag or their of their registry or operating under their authority, as the case may be." Ibid. article 209 at 74.
The Environmental Regulations provided that "when enterprises and operators work out an Overall Development Programme to develop an oil (gas) field, they shall at the same time prepare a Report evaluating its potential effect on the marine environment. This Report shall be submitted for approval by the Ministry for Protection of Urban and Rural Construction and Environment." According to the Environmental Regulations, this Report should be prepared in detail on how to prevent the damage caused by the offshore petroleum activities to natural marine environment, to marine resources and to other marine development activities. The Environmental Regulations also require that offshore petroleum operators have contingent capacities to prevent and control oil pollution in offshore areas and have a contingent plan prepared for dealing with the pollution incidents which occur as a consequence of their activities.

The Environmental Regulations put forward concrete legal protective measures in China's offshore oil development area. It is an indispensable law governing the offshore oil activities in China.


99. Article 6. Ibid.

100. Article 6. Ibid.
V. Conclusion

China's offshore petroleum industry plays an important role in the modernization of China's economy. The promulgation of the laws governing the cooperative offshore petroleum activities between China and its foreign partners provided protection to the investors. Without these laws, foreign enterprises would not go to offshore China. Normally, it is not difficult to adopt a petroleum law with the most favourable terms on the government's side and imposing all the most severe conditions on the oil companies. However, since the petroleum law is formulated to bring adequate income to the government as the result of petroleum operations, the terms of the law should be made acceptable to the oil companies. To enable foreign oil companies to be in offshore China, the Chinese government has stipulated provisions in the law to look after the interests of the foreign enterprises. In legislating the relevant laws, China consulted the historical experiences, the prevailing international practice and the economic situation. Its offshore petroleum laws were made according to the principle of international laws and China's national condition. Among the relevant laws, the Regulations of the People's Republic of China on the Cooperation with Foreign Enterprises to Exploitation of
Offshore Petroleum Resources is the commanding statute governing the development of China's offshore petroleum industry. It stipulated in detail the scope of activity for foreign oil companies and the cooperative patterns between China and international enterprises in offshore China. All the rest of the laws have created adequate conditions to further develop China's offshore petroleum industry. The legislative focus of the Chinese government was to protect its interest with respect to sovereignty, territory, economy, environment, taxation and economy. It is a collective feature of China's offshore petroleum laws that the Chinese government tries to maximize the potential benefit due to it in the offshore oil activities.

Most of the Chinese laws governing offshore activities were adopted between 1982 and 1985. At that time, international oil prices were very firm and the geophysical survey conducted in 1979 and 1980 in the vast untapped China sea predicted a promising prospect. The situation made plenty of international oil companies eager to go to China to recover oil. In the meantime, the Chinese government also wished to become rich overnight by opening its offshore areas. Such an environment affected the formulation of China's offshore petroleum law. Certain provisions of the Regulations were generally criticised by foreign investors as being rather harsh for foreign enterprises. For example, foreign oil
companies have to pay all the exploration costs and undertake the risk. But in the event that the exploration succeed, the Chinese side shall share the benefit. The downfall of oil prices happened in the middle of the 1980s was a tough test for China's offshore petroleum laws. It is likely that the Chinese government might take some measures to further encourage foreign investments in the offshore oil business. However, judging from the conditions producing these laws, the Chinese government will keep its present offshore petroleum laws both intact and valid as long as its door is open to international oil companies.
Chapter Three.

China National Offshore Oil Corporation and its Model
Petroleum Contract

I. Two Marked Traits in the Cooperation

The cooperation between China and international oil companies in the exploitation of China's offshore petroleum resources has two legal characteristics under current Chinese laws. One is that the activities of offshore oil industry in China are in the charge of China National offshore Oil Corporation. Another is that all the operations of foreign oil companies in offshore China are bound by the model petroleum contract prepared CNOOC.

A prevailing international practice contributed to the formation of these two characteristics.

As early as in 1962, the United Nations General Assembly adopted the following resolution:

"the right of people and nations to permanent sovereignty over their natural wealth and resources must be exercised in the interest of their national development and the
well-being of the people of the State concerned .... the exploration, development and disposition of such resources, as well as import of the foreign capital required for those purposes, should be in conformity with the rules and conditions which the peoples and nations consider to be necessary or desirable with regard to the authorization, restriction or prohibition of such activities .... international co-operation for the economic development of developing countries, whether in the form of public or private capital investments, exchange of goods and services, technical assistance, or exchanges of scientific information, shall be such as to further their independent national development and be based upon respect for their sovereignty over their natural wealth and resources."^{101}

This resolution is the famous doctrine of permanent sovereignty over natural resources, which has ensured that the petroleum resources of underdeveloped countries are theirs. This is an essential precondition to all current cooperation between resource rich countries and international oil companies. This doctrine helped many oil producing countries to enact new petroleum legislations and reformed traditional cooperative models adopted between oil producing countries and international oil companies in the past.^{102}


^{102}. " Up until 1945 (and for nearly two decades thereafter) the global environment worked to the advantage of the major multinationals. The structure of the industry, the substantial resources of the companies, which included capital, technology, and control over markets and sources of supply, and the power wielded by their home governments enabled them to acquire, and to maintain, dominance in the international petroleum system and give them an overwhelmingly stronger bargaining position in relation to the governments with which they had dealings.... While efforts were exerted to revise existing arrangements through negotiations, the end of fifties and the early sixties witnessed developments which
Later, the same principles were reaffirmed in the Declaration adopted at the Sixth Special Session of the UN General assembly (May 1974) and in the Charter of Economic Rights and Duties of States (December 1974).

It was not accidental that the Chinese government chose the 1980s to open its offshore areas. At that time, the international climate was much more favourable to oil producing countries. The doctrine of permanent sovereignty over natural resources was recognised as a basic principle of a new international economic order. It demonstrated in general to the Chinese government how to protect its national interests while dealing with foreign investment in the development of China's petroleum industry. By complying with


103. " Under the impact of major developments, significant changes had been taking place in relations between governments and transnational oil companies. The doctrine of permanent sovereignty over natural resources propounded in the UN General Assembly in the sixties gained heightened relevance in the context of the post-1973 global energy situation. The doctrine was recognised as a basic principle of a new international economic order by Declaration adopted as the Sixth Special Session of the UN General Assembly (May 1974) and in the Charter of Economic Rights and Duties of States (December 1974). Implicit in such recognition was the determination of governments to secure effective control over their resources, leading to fundamental policy reappraisals not only in the established oil-producing (OPEC) countries, but in the new producing countries, such as Britain and Norway." Ibid. at xi:
international practice and by following in the steps of fellow oil producing countries, China was likely to obtain a success in the development of its petroleum industry without any substantial loss. The cooperative arrangement which China conducted with foreign oil companies to develop its offshore petroleum industry seemed to be worthwhile.

Although self-reliance remained a guiding principle which the Chinese government used to formulate its petroleum policy, there has been another philosophy which in recent years has been advocated by radical Chinese government leaders to defy the traditional convention. This philosophy is known as "making foreign things serve China." Whenever the Chinese government wished to revise its old foreign policy, the philosophy would be used as an argument. As the application by other oil producing countries of the doctrine of permanent state sovereignty over the natural resources was exactly in line with the revised Chinese petroleum policy, the Chinese government absorbed all the useful essence from that doctrine in its offshore petroleum law.

It has been a universal trend in some oil producing countries that the greatest emphasis is placed on the sovereignty of the state over its petroleum resources. To

\[\textit{104}\] This is a popular proverb in China. The proverb used to be frequently quoted by Mao Tse-tung, late chairman of the Chinese Communist Party.
achieve this goal, many oil producing countries, take two measures:

(a) The establishment of national oil companies, and

(b) The adoption of new types of petroleum contracts such as joint venture, or service or production sharing agreements.¹⁰⁵

By establishing national oil companies, oil producing countries exercise effective control over their petroleum resources. National oil companies not only allow resource countries to prevent their sovereignty and economic interest from being infringed, but also enable them to receive the utmost financial returns to which they are due.

With petroleum activities being controlled by national oil companies, the new petroleum contracts proved to be reliable instruments to facilitate the resource country's objectives. Supported by the doctrine of state sovereignty over the natural resources, the new types of petroleum contracts which were represented by joint venture agreements,

¹⁰⁵ "The urge in the producing countries to excise control over the development of their petroleum resources and to reduce the market power of majors, as well as dependence on them, let them (a) to establish national oil companies (b) to grant exploration rights to new entrants in the field under new types of petroleum development arrangements" Supra, note 102 at 15.
replaced the old style concession agreement, which had previously existed. The new contracts put the producing countries in a superior position to negotiate with foreign parties and enabled them to derive greater benefit to serve the development of their economy. Unlike the old concession agreements, the new types of petroleum contracts normally result in foreign oil companies' enjoying fewer rights and having greater obligations than in the past. Generally, the new type of petroleum contract requires that foreign oil company supplies the initial investment, the needed technical knowledge and the necessary equipment in exchange for the right to participate in the exploitation of oil resources in the host countries.¹⁰⁶

By using national oil companies and the new type of petroleum contracts, countries are able to dominate the cooperative petroleum activities and their interests.

For the above reason, the establishment of a Chinese national offshore oil corporation and the preparation of a

¹⁰⁶ "The joint venture agreement pioneered as a new form of petroleum development arrangement by ENI, the Italian State Oil Corporation, was a response to the need felt by governments to share in the ownership and control over operations.... It is noteworthy, however, that although ownership of any petroleum discovered was joint and the operating companies was jointly owned, the entire risk capital for exploration was to be furnished by the foreign partner. In the event that no commercial discovery was made, the loss was to be exclusively borne by the foreign partner." Ibid. at 121.
model petroleum contract were two top priority task which had to occur before cooperation between China and foreign oil companies could take place in offshore oil activities.

The Regulations¹⁰⁷ provide that China National Offshore Oil Corporation (hereafter referred to as CNOOC) has the exclusive and overall responsibility for the exploration of the offshore petroleum resources of the People's Republic of China. In addition, CNOOC shall, by means of calling for bids and by means of signing petroleum contracts, cooperate with foreign enterprises to exploit petroleum resources in the identified offshore areas.¹⁰⁸

The Regulations also provided that CNOOC shall enter into petroleum contract so as to cooperate with foreign enterprises in the exploitation of offshore petroleum resources. The contract stipulates that the foreign enterprise shall provide the investment to carry out the initial exploration, be responsible for exploration operations and bear all exploration risks. In addition, the contract provides that after a commercial oil (gas) field is discovered, both the foreign companies and CNOOC shall jointly make the investment for its cooperative development, and the foreign companies


¹⁰⁸. Ibid. Article 5 and 6.
shall be responsible for all development operations and production until CNOOC takes over the production operations when conditions as set out in the petroleum contract are met. The foreign contractor, in accordance with the provisions of the petroleum contract, may recover its investment and receive remuneration out of the petroleum produced.¹⁰⁹

In the offshore cooperation between China and foreign oil companies, CNOOC is the incarnation of the Chinese government. When foreign enterprises negotiate with CNOOC, they are factually dealing with the Chinese government and vice versa. Without the agreement and the cooperation of CNOOC, foreign oil companies will not be able to take any action in China's offshore. According to the Regulation¹¹⁰, the petroleum contract formulated for China's offshore petroleum industry is a model contract. This contract is the most direct and effective law governing the activities of foreign oil companies which have won the right to explore for oil in offshore China. Almost all the most important provisions provided by China's offshore petroleum policy and laws, are contained in specific concrete articles and clauses in the model petroleum contract.¹¹¹

¹⁰⁹. Ibid. article 7.
¹¹⁰. Ibid.
¹¹¹ "The model contract is being used by the Chinese used as a basic legal framework. Because of its applicability to all foreign oil companies involved in offshore oil
II. Legal Nature of CNOOC

In the cooperative efforts between China and foreign oil companies, CNOOC occupies a vital position. Therefore, an understanding of the legal nature of CNOOC is important.

CNOOC was created on 15 February 1982. Headquartered in Beijing, CNOOC has four regional subsidiary corporations. The Bohai Oil Corporation, based in Tanggu, is responsible for the petroleum operation in the Bohai Gulf. The East Offshore Oil Corporation, based in Shanghai, is responsible for the operations in the East China Sea and the South Yellow Sea. The operation in the South China Sea to the east of 113°10' longitude, is the responsibility of the Nanhai East Oil Corporation, based in Guangdong. The operations in the western part of the South China Sea are the responsibility of the Nanhai West Oil Corporation which is located in Zhanjiang. Petroleum contracts between CNOOC and foreign oil companies are negotiated and signed in Beijing and carried out by CNOOC's subsidiaries respectively.

exploration, the contract function is similar to that of a legislative enactment." Loretta D. Rich, "American Oil Interests in China" (1983) 6 Loyola of Los Angeles International and Comparative Law Journal, 119 at 130.
The function of CNOOC is to implement the policy of the Chinese government regarding the cooperation with international oil companies. This includes calling for tenders, deciding the bidding blocks, signing petroleum contracts, forming joint venture service companies, participating in the management of the operation and supervising the activities of foreign oil companies in China. All the important plans or proposals concerning the implementation of petroleum contracts are subject to the examination and approval of CNOOC. According to the Regulations:\textsuperscript{112} CNOOC is a

"state corporation with the qualification of a juridical person which has the exclusive right to explore, develop, produce and market petroleum with the zone of cooperations with foreign enterprises."\textsuperscript{113}

Most of the officials of CNOOC, previously worked for the Ministry of Petroleum Industry of the PRC and hold official government titles. The organizational structure of CNOOC is based on that of other Chinese ministries. In the genealogy of China's central government, CNOOC's position is equal to that of a ministry and is under the direct leadership of the State Council of the PRC. It has the same power as other

\textsuperscript{112} Supra, note 107.

\textsuperscript{113} Ibid. Article 5.
ministries. At the level of the central government, it is entitled to communicate with all the other ministries and discuss their actions as equals. The presidents of CNOOC's regional corporations have the same official status as provincial governors. Under the Regulations\textsuperscript{114}, the operations of CNOOC will receive special consideration from both the central and provincial governments. CNOOC is truly an arm of the central Chinese government.

Although CNOOC has authority in the government, the legal nature of CNOOC has become a fundamental question in the minds of many executives of foreign oil companies.\textsuperscript{115} To ensure that their petroleum contracts signed with CNOOC are secure, international oil companies hope to see that CNOOC is legally recognised as a representative of the Chinese government or, alternatively, is acting under the express mandate of the government. The power conferred on China National Offshore Oil Corporation under Chinese law gives foreigners the impression that CNOOC represents the Chinese government. If

\textsuperscript{114}. Ibid.

\textsuperscript{115}. "In addition to these issues concerning particular terms, there is more fundamental question in the minds of many executives. This involves the mandate of CNOOC. Although Ministry of Petroleum officials have stated more than once that CNOOC has the full power to sign contracts and to fulfil obligations under the contracts, some oil companies are uneasy with the absence of an official statute that defines CNOOC's authority. Executives have reportedly reexpressed the view that they would consider a contract with the Chinese government more secure." Chris Brown, "Tough Terms for Offshore Oil", The China Business Review, July 1982 at 37.
CNOOC were acting on behalf of the Chinese government, the agreements concluded between CNOOC and foreign oil companies would be backed by the Chinese government. Therefore, the legal status of CNOOC is of great relevance to foreign oil companies. So far, however, some foreign oil companies have been unable to define the legal position of CNOOC under Chinese law, nor have they found the guarantees for enforcing their petroleum contracts.  

China's legislation permitting the exploration and development of its offshore petroleum resources is made up of two parts. One part is the offshore petroleum law which protects China's sovereignty over its petroleum resources on the continental shelf, while the other part is the international petroleum contract which is signed between the Chinese and foreign parties. When foreign oil companies are signing petroleum contracts with CNOOC, they generally have the mistaken belief that they are actually dealing with the Chinese government directly. In this way, they believe that the petroleum contract signed by CNOOC could be ranked as a state contract which, in nature, could be considered as a

116. ".... Ambiguity is another feature in Chinese legislation.... questions arise as to the ability of CNOOC and its subsidiaries to assume legal liability and the extent of such liability in case of litigation. Some oil companies have even expressed uneasiness about CNOOC's power to sign contract and to fulfil contractual obligations." Paul C. Yuan, "China's Offshore Oil Development Policy and Legislation: An Overall Analysis" (1988) Vol3, No2 International Journal of Estuarine and Coastal Law 101 at 135.
quasi-international treaty. Therefore, when any dispute happened regarding a petroleum contract, not only the Chinese law, but also international law could potentially be applied. In addition, it was believed that if CNOOC incurred a debt, the relevant department of the Chinese government would be liable for the debt. However, this is an entirely mistaken opinion.

CNOOC has a dual nature. Internally, it is a powerful government organisation in charge of China's offshore oil industry. For example, all the important acts and decrees regarding the offshore oil activities were basically drafted by CNOOC and then rubber stamped by the Chinese legislature. Externally, however, the legal status of CNOOC is only an enterprise as a legal person.¹¹⁷ Except for the Regulation, descriptions regarding CNOOC's legal position cannot be found in any other Chinese law.

In accordance with the Chinese law:

"A legal person shall have the following qualifications: (1) establishment in accordance with the law; (2) Possession of the necessary property or funds; (3) Possession of its own name, organization and premises; and (4) ability to independently bear civil liability."¹¹⁸

¹¹⁷. Supra, note 107. Article 5.

¹¹⁸. General Principles of the Civil Law of the People's Republic of China, Chapter III, Article 37, (Adopted at the Fourth Session of the Sixth National People's Congress,
CNOOC was established under the Regulations and its registered capital was 8,281.08 million Yuan of RMB in 1990\(^{119}\), and it therefore meets the first two requirements for being a legal person. In the public, CNOOC has no difference from other state run companies in China when dealing with foreign oil companies.

"A legal person shall be an organization that has capacity for civil right and capacity for civil conduct and independently enjoys civil rights and assumes civil obligations in accordance with the law.\(^{120}\)

In the cooperation between CNOOC and foreign oil companies, CNOOC has to be responsible for its own behaviour. The Chinese government has no responsibility for CNOOC's action. CNOOC's debt liability is limited to its registered capital and the competent authorities of the Chinese government will not undertake any responsibility for CNOOC's debt. There is another provision of the Chinese law indicating the legal position of CNOOC.

"Contract for .... Chinese - foreign cooperative exploitation and development of natural resources to be promulgated by Order No.37 of the President of the PRC on April 12, 1986 and effective as of January 1, 1987.\(^{119}\)


\(^{120}\). Supra, note 118. Article 36 and 48.
performed within the territory of the People's Republic of China shall be governed by the law of the People's Republic of China."^{121}

This further demonstrates that CNOOC does not have the capacity of a government ministry. Therefore, a petroleum contract signed by CNOOC is not a quasi-international treaty and is not subject to international law.

In the joint development of China's offshore oil resources with foreign oil companies, CNOOC is an enterprise having the qualification of a body corporate which bears limited liability. This is its legal nature.

Under the Chinese law, foreign oil companies will undertake the financial risk in the exploration stage during the contract term. When they are to sign petroleum contracts in China, they should know that they are not signing the contract with the Chinese government.

^{121}. Law of the People's Republic of China on Economic Contracts Involving Foreign Interest, Article 5, (adopted at the Tenth Session of the Standing Committee of the Sixth National People's Congress, promulgated by Order No. 22 of the President of the People's Republic of China on March 21, 1985, and effective as of July 1, 1985).
III. Salient Features of Model Petroleum Contract

The model petroleum contract of CNOOC is a gateway for foreign oil companies to exploit China's offshore petroleum resources.

According to the legal procedure provided for in China, any foreign oil companies interested in China's offshore oil are required to bid for their qualification. The winning bidders then shall be able to acquire a chance to negotiate and sign petroleum contracts with CNOOC. The blocks will not be awarded to foreign oil companies unless they have signed a petroleum contract with CNOOC, and the signed contract is approved by Chinese government. For all the foreign investors, this petroleum contract is a licence of concession for being entitled to enter offshore China for oil. The petroleum contract prepared for foreign investors is a model contract which allows limited room for contractors to bargain.

The model petroleum contract is an integral part of China's open door policy and determines the fate of foreign investors in offshore China. The intent of this session is to present a brief analysis on the dominant features of China's model petroleum contract (hereafter referred to as Contract).
A. General Feature:

Under the provision of the Contract:

(a) In the exploration period, Contractor shall raise and pay all the funds needed, be responsible for operation and undertake total exploration risk.\(^\text{122}\)

(b) In the event that any oil (gas) field is discovered within the Contract Area, the development cost shall be shared by CNOOC and Contractor in proportion to their participation interests. CNOOC shall participate fifty one of the share and Contractor forty nine.\(^\text{123}\)

(c) Contractor may recover its investment and cost and receive profit.\(^\text{124}\)

\(^{122}\) CNOOC, *Model Petroleum Contract for the Third Round of Bidding*, Article. 2.4.

\(^{123}\) Ibid. Article 12.1.1, 12.1.2.

\(^{124}\) Ibid. Article 13.
The oil produced from oil fields within Contract Area shall be allocated in the following sequence:

(a) Payment of government taxes and royalty.\(^{125}\)

(b) Recovery of production operation cost from the portion of "Cost Recovery Oil".\(^{126}\)

(c) Recovery of exploration cost and uncovered production operation cost from the proportion of "Cost Recovery Oil".\(^{127}\)

(d) Share of remainder oil. After the payment of government taxes, royalty and the recovery of the above mentioned cost, the remainder oil shall be divided into two portions. One portion belong to CNOOC as "Share Oil Of China Side". another portion shall be "Allocable Remainder Oil". The "Allocable Remainder Oil" shall be shared by CNOOC and Contractor in proportion to their respective participating interest.\(^{128}\)

\(^{125}\) Ibid. Article 13.2.1. and 13.2.2.

\(^{126}\) Ibid. Article. 13.2.2.2.

\(^{127}\) Ibid. Article 13.2.2.

\(^{128}\) Ibid. Article. 13.2.2.3., 13.2.3 and 13.2.4.
B. Contract Term:

The exploration period of Contract shall be seven years, beginning on the date of commencement of the implementation of Contract. This exploration period is normally divided into three phases. The first phase shall be three years. The second and third phases shall be two years respectively.\(^\text{129}\)

Subject to the approval of CNOOC, the exploration period may be extended to a reasonable period.\(^\text{130}\)

In the event a commercial oil (gas) field is discovered within the Contract Area, the production period shall be fifteen years\(^\text{131}\)

There is no specific time table for the development period, but the development period of any oil (gas) field within the Contract Area shall begin on the date of approval of the Overall Development Program (ODP) of the said oil (gas) field by the responsible authorities of the Chinese government and end on the date of the entire completion of the

\(^{129}\) Ibid. Article 4.1.

\(^{130}\) Ibid. Article 4.3.

\(^{131}\) Ibid. Article 4.3.
Development Operation set forth in the ODP.\textsuperscript{132}

In any event, the term of Contract shall not be beyond thirty years.\textsuperscript{133}

CNOOC does not wish the term of the Contract to be able to extend without limitation. Thirty years is an absolute deadline. Even if there are several oil (gas) fields on stream within the Contract Area, the Contract can not be valid for over thirty years.

C. Contract Area:

The Contract is different from conventional commercial contracts entered in China. It deals with China's natural resources and grants the concessions to foreign oil companies for the exploitation of petroleum. The objective of foreign oil companies to invest in offshore China is to acquire some promising blocks to drill for oil. As long as the Contract is signed between CNOOC and a foreign oil company, that company is entitled to enter the concession to carry out the operation of oil industry. In this sense, the Contract in fact is an equivalent to a licence of concession which is awarded to

\textsuperscript{132} Ibid. Article 4.6.

\textsuperscript{133} Ibid. Article 4.7.
foreign oil companies by the Chinese government. To sign a petroleum contract with CNOOC is the first legal step for foreign oil companies to start their petroleum activities in offshore China.

CNOOC is empowered by the Chinese government to award Contract Areas to foreign oil companies which have won the bid to work in China's offshore petroleum industry. As a state company, CNOOC functions as the official representative of the Chinese government in the activities of offshore oil exploitation. It is up to CNOOC to pick out qualified foreign partners to sign Contract and decided the location and the size of Contract Areas.

The Contract area is composed of basic blocks, which are designated in accordance with every ten minute of longitude. The size of each basic block is about three hundred square kilometres. However, the size of those blocks which are located in shallow water and which possess better geological exploration prospects is smaller than that of other blocks.

The Contract provides that no right is granted in favour of the Contractor to the surface area, subsea, sea bed, subsoil or any natural resources or aquatic resources other than petroleum existing there, and no right is granted to the Contractor for anything left on sea-bed within the Contract
D. Relinquishment of Contract Area:

(a) At the period of the first phase of the exploration period, Contractor shall relinquish twenty five percent of the Contract Area.  

(b) At the expiration of the second phase of exploration period, the Contractor shall relinquish another twenty five percent of the remaining Contract Area after deducting the Development Area and/or Production Area.  

(c) At the expiration of the last phase of exploration period, Contractor shall relinquish the remaining Contract area except any Development Area and/or Production Area.  

(d) At the expiration of the Production Period, any oil (gas) field within the Contract Area shall be

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134. Ibid. Article 2.
135. Ibid. Article 5.1.2.
136. Ibid. Article 5.1.2.
137. Ibid. Article 5.1.3.
relinquished to CNOOC. ¹³⁸

The Contract also provides that the relinquished area shall be made up of as few rectangles as possible so as to facilitate exploration operations.

Well known Doctrine of Relinquishment is applied here in Contract. ¹³⁹ The provisions regarding of relinquishment of explored Contract Area are critical clauses to the Chinese government. These provisions mean to maintain the sovereignty over the exploration area and the mineral resources for the Chinese government. The Contractors may be awarded a large block of offshore area at the starting stage of exploration, but it is not appropriate for them to hold that large block for a long period. The Chinese government requires foreign

¹³⁸  Ibid. Article 5.1.4.

¹³⁹ "The interest of the government in this phase (exploration phase) is clearly to secure rapid and thorough exploration. This phase may, perhaps, be regarded as the most critical, since the future development is premised upon success of this phase. An area in which there has been a good deal of innovation is that involving legal mechanisms designed to ensure more rapid and thorough exploration....Government have an interest in resuming, within a relatively short time, control over area where companies have carried out initial exploration operations and have not made any discovery, or have decided not to conduct further exploration: the more so, since there is evidence that subsequent exploration in area abandoned by a company, has led to significant discoveries being made. The mechanisms by which this interest is secured are relinquishment or area-reduction provisions, which may be contained in the general legislation or in the agreement, or both." Supra, note 102 at 112-3.
oil companies to relinquish part of exploration areas on the expiration of each contracted exploration period in order to avoid the waste of mining area, to strengthen its negotiation position and to safeguard its national sovereignty. In the consideration of the Chinese government, the provision of Area Relinquishment was very important. If the Contractor was awarded long exploration period in a large block, new oil companies would have no opportunities to enter the occupied area to explore for oil. It was not acceptable to the Chinese government to allow any foreign oil companies to monopolise a broad area for oil exploration.

E. Confidentiality

The Contract and all documents, information, data and reports related to the Petroleum Operation within the Contract Area shall be kept confidential. Confidential period shall be determined by CNOOC in accordance with relevant Chinese laws and regulations.¹⁴⁰

The Contract provides time limits for two kinds of confidentialities.

¹⁴⁰ Supra, note 122. Article 22.
If the responsible authorities of the Chinese government decide to award new acreage in sea to a new foreign oil companies, CNOOC may furnish:

(a) the original information and data held by CNOOC for over two years,

(b) the interpretation of original information and data held by CNOOC for over five years to the third parties.\(^{141}\)

F. Arbitration and Applicable Law:

According to the provisions of the Law of the People's Republic of China on Economic Contracts Involving Foreign Interest\(^{142}\), the Contract is governed by Chinese law. This is a legislative principle that the Chinese government will always adhere to. As for the arbitration the Chinese government took a flexible manner.

\(^{141}\) Ibid. Article 22.2.(a) and (b).

\(^{142}\) Supra, note 121.
On the subject of arbitration, the Contract provides:

(a) Any dispute on the performance or interpretation of the Contract shall be settled amicably through consultation.\textsuperscript{143}

(b) A dispute which has not settled through consultation shall be referred to arbitration conducted by the China International Economic and Trade Arbitration Commission according to arbitration proceeding rules.\textsuperscript{144}

(c) If the parties fail to reach an agreement on arbitration under Chinese rules, an ad hoc arbitration tribunal shall be established. The arbitration tribunal shall consist of three arbitrators. Each parties shall appoint an arbitrator and the third arbitrator shall be appointed by the two arbitrators. If the two arbitrators fail to appoint the third arbitrator, the third arbitrator shall be appointed by the Arbitration Institute of the Stockholm Chamber of

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{143} Supra, note 122, Article 26.1.
\item \textsuperscript{144} Ibid. Article 26.2.1.
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Commerce.\footnote{Ibid. Article 26.2.2. and 26.2.2.1.}

(d) The third arbitrator shall be a citizen of a country which has diplomatic relations with China and the home country of the Contractor and shall have no economic interest or relationship with the parties. The arbitration tribunal shall conduct the arbitration in accordance with the arbitration rules of the United Nations Commission on International Trade Law (UNCITRAL) of 1976. The place of arbitration shall be determined by the parties through consultation or by the wishes of majority of arbitrators.

On the subject of applicable law, the Contract provides:

(a) The validity, interpretation and implementation of the Contract shall be governed by the laws of the People's Republic of China. If there are no relevant provisions in Chinese laws to interpret of the Contract for the implementation, the principles of applicable laws widely used in petroleum resources countries which are acceptable to the parties shall be applicable.\footnote{Ibid. Article 28.1.}
(b) If a material change occurs to the Contractor's economic benefits after the effective date of the Contract due to the promulgation of new laws, decrees, rules and regulations or any amendment to the applicable laws, decrees, rules and regulations made by the government of the PRC, the Parties shall consult promptly and make necessary revision and adjustment to relevant provisions of the Contract in order to maintain the Contractor's normal economic benefits.

It might be the first time since the founding of the PRC that China's competent authorities gave up their normal stand that anything happening in China must apply Chinese laws or legal procedure. This action has set an example for the future similar cooperation between China and foreign countries.

G. Effectiveness and Termination:

The signed Contract shall be approved by the Ministry of Foreign Economic Relations and Trade of PRC. The date of such approval shall be the effective date of the Contract.\textsuperscript{147}

\textsuperscript{147}. \textit{Ibid.} Article 2.7.
The Contractor can terminate Contract under the following conditions:

(a) After the expiration of the first or second exploration period and prior to the exploration period without discovering any commercial oil (gas) field.\textsuperscript{148}

(b) [1] If there is only one oil (gas) field in production within the Contract Area, the Contract shall be terminated on the termination of the production of such field. [2] If there are more than two commercial oil (gas) fields in production, contract shall be terminated on termination of production period of the field with the latest termination date.\textsuperscript{149}

(c) At the end of the last day of the thirtieth year from the date of commencement of Contract.

\textsuperscript{148} Ibid. Article 6.3. and 27.4.2.

\textsuperscript{149} Ibid. Article 27.4.4.
H. Management Mechanism

The Contract contains elements of a joint management, which can be demonstrated by the management mechanism of the operation in the exploration and development of China's offshore petroleum resources.

According to Article 7.1 of the Contract, CNOOC and the Contractor shall establish the Joint Management Committee (JMC) within forty-five days from the date of commencement of implementation of the Contract.

The establishment of the JMC is an outstanding feature of Contract. By setting up the JMC, CNOOC will reach three goals.

(a) To put the operation of the Contractor under the direct supervision of Chinese authorities.

(b) To learn management experiences on offshore petroleum industrial operation from foreign partners.
(c) To conduct direct management with the Contractor over the Contract.

The JMC is formed by an equal number of representatives (one to three) appointed by CNOOC and the Contractor.\textsuperscript{150}

The function of the JMC is as follows:

(a) Review and examine the work program and budget proposed by the operator.

(b) Determine the commerciality of each trap on which a petroleum discovery has been made in accordance with the operator's appraisal report and report its decision to CNOOC for confirmation.

(c) Review and adopt the Overall Development Program and budget for each oil (gas) field.

(d) Approve or confirm substantial items of procurement and expenditure.

(e) Determine and announce the date of commercial production of each oil (gas) field within the

\textsuperscript{150} Ibid. Article 7.1.
Contract Area.

(f) Determine the type and scope of information and data provided to any third party and affiliate in relation to the petroleum industry of the PRC in accordance with the Provision of Ministry of Petroleum industry of the PRC for the Control of Data Concerning the Exploitation of Offshore Petroleum Resources in Cooperation with Foreign Enterprises.

(g) Demarcate boundaries of Development Area and Production Area of each oil (gas) field.

(h) Review and approve plans for transfer of production operation.

(i) Review and approve the insurance program proposed by operator and emergence procedures on safety and environmental protection.

(j) Review and approve personnel training programs.

(k) Discuss, review, decide and approve other matters that have been proposed by either party to the Contract or submitted by expert groups or the
(1) Review and examine matters required to be submitted to relevant authorities of the Chinese government and / or CNOOC.

In offshore China, foreign oil companies have been not given a free hand to carry out their operation. The Joint Management Committee is an entity ruling the operation and activities of foreign Contractors. Nearly every step taken by the Contractor regarding the exploitation operation shall be subject to the approval, review and examination of JMC. The JMC informs CNOOC about how the Contract is being implemented and therefore CNOOC can take quick action should any problems arise. JMC is a standing unit. By working with their foreign colleagues daily, the Chinese members can learn different experience in managing offshore petroleum industry directly and immediately. The Chinese government has jointly ventured with foreign oil companies in the exploitation of its offshore petroleum resources. After the discovery of an oil (gas) field, CNOOC claims 51 percent of interest. CNOOC also feels important to participate in the direct management in every aspect since the beginning of the implementation of the Contract. The Contract provisions regarding the JMC are set up for this purpose. The Chinese government won't allow the foreign Contractor to be able to do anything alone within the
Contract Area. China's sovereignty over natural resources enables the Chinese government to require foreign oil companies to agree to the establishment of the JMC. It is a special method worked out to maintain China's economic interests.

I. Features of Other Articles

There are some other special articles provided in the Contract in China's favour. For example:

(a) all assets purchased, installed and constructed under the work program and budget for each oil (gas) field within the Contract Area shall be owned by CNOOC at the expiration of production period;

(b) if conditions permit, CNOOC may take over the production operation of oil (gas) field within Contract Area;

(c) The overall Development Program of any oil (gas) field within Contract Area shall be subject to the approval of Chinese government;
(d) CNOOC shall have the right to assign professional representatives to the operator's administrative and technical department which are related to the petroleum operation;

(e) the Contractor has to give preference to the employment of Chinese personnel, goods and services;

(f) the ownership of all the data, records, samples, vouchers and other original data obtained in the course of performing the petroleum operation shall vest in CNOOC.

Besides, the Contractor shall pay CNOOC a nonrecoverable signature bonus of one million U.S. dollars.\textsuperscript{151}

J. Conclusion

In Chinese history, both sea area and mineral resources used to be forbidden fields to foreign countries. When the Chinese government decided to open its offshore to foreigners

\textsuperscript{151} Ibid. Article 17.1, 8.7, 11.4, 7.5, 15, 17 and 30.5.
for the exploitation of oil resources, its first concern was to safeguard China's national sovereignty. Therefore, the doctrine of sovereignty is given a full expression in the Contract.

In drafting the Contract, the general objective of the Chinese government regarding the cooperation with foreign force to exploit China's offshore petroleum resources was to utilize foreign capital, technology and experience to serve China. The emphasis should be given on the utilization of foreigners. There are two fundamental doctrines running through Contract:

(a) doctrine of safeguarding sovereignty,

(b) doctrine of utilizing foreign investment. Almost all the questions arising from the interpretation of Contract can find answers from using these two doctrines.

The Contract is not simply a lease of concession, nor a joint venture agreement nor a production sharing petroleum contract which created by southeast Asian countries such as Indonesia or Malaysia. It is a Chinese style creation. The formation of the Contract has absorbed advantages from prevailing international petroleum agreements to date.
Several conclusions can be made from Contract.

In the first place, it is a risk contract. Contractor shall solely undertake all the exploration risk.

In the second place, it is a joint management contract. CNOOC and the Contractor shall jointly manage the Contract from the beginning to the end.

In the third place, it is a joint venture contract. CNOOC and Contractor shall pool their investments in the production period.

In the fourth place, it is a production sharing contract. CNOOC and Contractor shall recover their investment cost and share the remainder oil.

In summary, the Contract is a combination of a risk petroleum contract, a joint venture petroleum contract and a production sharing petroleum contract. It is a legal creation that the Chinese government has been practising in its offshore petroleum industry. To maintain China's national

152. "The model contract incorporates aspects of the Indonesian, British, Brazilian, and Norwegian contract models. It contains elements of a joint venture and a production sharing agreement." See supra, note 111 at 130:
economic interests and to make best of foreign capital to serve China's economic construction are fixed general government policies of China. These policies have been well reflected by the Contract.

Having studied and summarized the petroleum contract models of other host countries with petroleum resources, China established its model petroleum contract. It is a crucial legal instrument governing the activities of foreign enterprises working in offshore China for oil. In its more than ten years of practice, the Contract has made contributions to the development of China's offshore oil industry. Although it will undergo repeated modification to meet changes according to the situation of China's petroleum industry, the current Contract will remain a landmark to show the foundation of China's legal framework in cooperation with foreign enterprises in the exploitation of offshore petroleum resources.

\[153\] See supra, note 51.
Chapter Four

A Comparative Study of the Offshore Oil and Gas Laws of the

U.K., Canada and China

"Oil companies from all over the world have crossed the seas to search for oil off the Chinese coastline. Seismic surveys are presently spider-webbing over 1,100,000 km² of ocean space. Speculation on what kind of production contract the oil companies will eventually sign has been unbridled. Attention has been focused upon the Brazilian, Indonesian, Algerian, and Norwegian "Models" as possible ways China may contract with the international oil companies."

___ What Kind of Contract Will China Accept?\textsuperscript{154}

More than ten years have elapsed since the Chinese government officially commenced its cooperation with foreign oil companies in 1982. It may now be the appropriate time for the Chinese government to reexamine its offshore petroleum law and policy. The factors that have been most influential in shaping the development of this branch of law and policy in China are:

(a) the urgent need for economic reform; and

(b) China's distinct historical tradition and social background.

In addition to these factors, worldwide practices and the legislative experiences of other states have also influenced Chinese policy. Petroleum is the foremost source of energy in the world. To promote the development of the petroleum industry, many countries have promulgated exclusive petroleum laws to regulate oil exploration and production. A brief comparative study of the offshore oil legislation and practice of other important oil-producing countries may yield valuable insights which can be used to evaluate the effectiveness of the Chinese offshore petroleum law and policy and to suggest possible legislative changes.

Three petroleum regimes of those of the U.K., Canada and China will be studied in this chapter:

I. Oil and Gas Law in the U.K.

Until the 1970s, the U.K. was a country poor in oil. In the mid-1950s, it developed some small onshore oil fields. In 1974, the annual oil output of U.K. was only 88 thousands
tons.\textsuperscript{155} With the exploration and development of the North Sea oil fields, however, the U.K. became a major oil-producing country. The success of the British state was one of the factors which encouraged the Chinese government to embark upon the recovery of petroleum resources in its offshore area. The Chinese government takes a continuing interest in the practice of the British offshore oil and gas industry. Any adjustment in British offshore petroleum policy usually attracts the attention of the Chinese government. Oil and gas law in the U.K. has set a precedent which could be studied by the Chinese government in formulating its own petroleum law. It is no surprise, therefore, that the contents of China's offshore petroleum laws are substantially similar to those of the United Kingdom.

A. The License System

British petroleum law rests is based on the Petroleum (Production) Act 1934 and the Continental Shelf Act 1964. The basic provision of oil and gas law in the U. K. is that all the petroleum resources located within the boundaries of the U.K. and its continental shelf are owned by the Crown.

Under U.K. law,

"The property in petroleum existing in its natural condition in strata in Great Britain is hereby vested in His Majesty, and His Majesty shall have the exclusive right of searching and boring for and getting such petroleum... Any rights exercisable by the United Kingdom outside territorial waters with respect to the sea bed and subsoil and their natural resources, except so far as they are exercisable in relation to coal, are hereby vested in Her Majesty."

The above statutes provide that the Crown is the owner of

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156. "The main elements of United Kingdom law on the production of oil and gas are to be found in the Petroleum (Production) Act 1934, the Continental Shelf Act 1964, the Mineral Workings (Offshore Installations) Act 1971, the Oil Taxation Act 1975 and the Petroleum and Submarine Pipe-lines Act 1975, and in the Petroleum (Production) Regulations 1976 made under the first of these statutes." T. Daintith at al, ed., United Kingdom Oil and Gas Law (London: Oyez Publishing Ltd, 1977) at 1.


petroleum resources located in the territory of the Kingdom and that it exercises sovereignty rights over the resources of the continental shelf in accordance with international laws. Only the Crown may give permission for the exploration and development of petroleum. Otherwise, such activities violate the exclusive proprietary rights of the Crown. Because the exploration and development of petroleum in Britain are mainly undertaken by private enterprises, a system of licenses was developed as the legal vehicle to govern the industrial activities aimed at tapping state-owned petroleum resources.

Thus, in the U.K. only license holders are entitled to drill for petroleum. Petroleum licenses are granted by the Secretary of State for Energy. According to the Petroleum (Production) Act 1934,

"section 2-(1) The [Secretary of State], on behalf of His Majesty, shall have power to grant to such persons as [he] thinks fit licenses to search and bore for and get petroleum. (2) Any such licence shall be granted for such condition (whether by royalty or otherwise) as the [Secretary of State] with the consent of Treasury may determine, and upon such other terms and conditions as the [Secretary of State] thinks fit. . . . 6-(1) The [Secretary of State] shall, before granting any license under this Act, make regulations prescribing—(a) the manner in which and the person by whom applications for licences under this Act may be made; (b) the fees to be paid on any such application; (c) the condition as to the size and shape of areas in respect of which license may be granted; (d) model clauses which shall, unless [he] thinks fit to modify or exclude them in any particular case, be incorporated in any such license." 159

159. Ibid. at 221-223.
Petroleum licenses are an integral part of U.K. oil and gas law. They have a dual nature. On the one hand, they are consensual contracts. When licensees reach agreements with the Crown, they have the right to explore and develop petroleum in a assigned block during a fixed term. In return, by way of consideration, they have to pay royalties and taxes to the government. On the other hand, these petroleum licenses are different from common commercial leases since they derive their authority directly from U.K. legislation and the British government sets their terms. The Secretary of State grants petroleum licences on behalf of Parliament. Thus, while the Secretary of State exercises power to regulate petroleum activities, the licensees's rights and obligations are also governed by the license provisions set by the British government as compulsory regulations. In addition, the British parliament can, by legislation, unilaterally alter the terms of existing seaward and landward petroleum production

\[160\] "... the license arrangements retain a strongly regulatory flavour, both by reason of the formal rules for the issue of licenses laid down at the instigation of Parliament, and by reason of the contents of the licences themselves, which must normally accord with model clauses regulating such matters as working methods, safety, pollution and training, and reserving to the Minister considerable powers of direction of the licensee's activities. Indeed, with the unilateral alteration of clauses in existing licenses by the Petroleum and Submarine Pipe-lines Act 1975 one might be tempted to say that the contractual character of the licences was pure fiction." Ibid. at 26.
licenses. There are of course political limits on the exercise of these rights.

To summarize, in Britain, the government uses the system of petroleum licenses to control the exploration and development of petroleum resources. The license system is a combination of both contract and governmental regulation.

B. Financial Requirement

The non-exclusive U.K. exploration license includes the possibility of drilling wells to a depth of 1,000 ft (330 meters).

The surface of the blocks in the exclusive production licenses is 100 sq miles (250 km$^2$). Duration of the license is 40 years. After 6 years, 50% of the area must be relinquished. The work obligation is negotiated before the license is granted.

The financial aspects of this legislation include the payment of a fixed-initial bonus of 200 pounds sterling for

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each of the first ten blocs and 5 pounds\textsuperscript{162} for each subsequent bloc. The surface duties amount to 25 pounds--per \( \text{km}^2 \) for the first six years, and 40 pounds for the seventh year; each following year the surface duty increases by 25 pounds to a maximum of 29 pounds per \( \text{km}^2 \) after seventeen years. The royalty is fixed at 12.5\% of the initial well head price based on the sale price. The corporation income tax is 40\% of the taxable income. An investment-credit of 30\% exists for fixed assets and intangible drilling expenditures. \textsuperscript{163}

The production of the British offshore petroleum industry has brought tremendous benefits to Britain, and maintenance of oil income remains a constant concern of the government. In order to attract more international oil companies to operate in its offshore petroleum industry, the taxes levied by the British government are not very high. The U.K. is the oldest and most seasoned capitalist country in the world; its government has expertise in manoeuvring economic incentives to motivate international petroleum companies. The Chinese government has been most impressed by the way in which British petroleum tax policy has contributed toward the development of offshore resources. The tax rates in China from the offshore

\textsuperscript{162} Pounds referred in this section means English pounds sterling.

petroleum industry are therefore structured similarly to those in the U.K..

C. State Participation

In its offshore petroleum industry, the British government asks oil companies to bid for the grant of petroleum licences. Before 1976, during the first to fourth round of license bidding, no state participation was officially required. British state corporations such as BGC (British Gas Corporation) and NCB (National Coal Board) might form consortia with other oil corporations to bid for petroleum licences. The British government encouraged the participation of the State corporations but its policy was one of "voluntary participation".164

After 1977, starting with its 5th round of bidding for petroleum licenses, the British government required oil investors in offshore oil areas to accept 51% state

164. "Such participation was on a formally equal footing with private enterprise, though in the informal published criteria for the allocation of licenses, in the 1965 and 1969 rounds, the participation of the NCB and BGC in the license consortium was made first a desideratum and, in certain of the 1969 allocations, an essential prerequisite for the grant of the license. These provisions induced certain private operators, among whom Gulf and Conoco were notable examples, to cooperate extensively with the State corporations." Supra, note 156 at 16.
participation. This shift in policy put the activities of international oil companies under strict governmental control and supervision. This enabled the British government to fully utilise foreign investment and gain access to foreign advanced technology and experience, while maintaining its sovereignty over its national resources. The most significant advantage for the U.K. in implementing a state participation policy was that it guaranteed governmental control over a large part of crude oil produced from the North Sea oil fields.

In fact, even before 1977, the British government had directly participated in the development of the petroleum industry in various ways. Even before the exploitation of its continental shelf, the British government, in its role as a 50\% "sleeping partner" in British Petroleum Plc (BP), shared the enormous profit of that giant private company. At the early stage of its offshore petroleum industry, the British government encouraged the two British state

\[165\] "The Government's announced aim was to ensure majority BNOC participation in existing licences covering fields with had been or would be proven commercial......With regard to future licences, ....such licenses will be granted only on the basis that BNOC or one of its subsidiaries (or possibly BGC) is from the outset a co-licensee with at least a 51 per cent interest." Ibid. at 16-17.

\[166\] This is not to say that there was no State participation in exploration and production activities prior to 1975. BP may be left to one side, ..... the government's shareholding in the firm has never dropped far below 50 per cent and confers a right of veto over Board decisions, .... " Ibid. at 16.
corporations, BGC and NCB, to form a consortium with foreign oil companies to join the offshore petroleum activity in the U.K.. As soon as the brilliant prospects of offshore oil resources were apparent, the British government organised a national oil corporation and required its direct participation in the industry through legislation.

Under the Petroleum and Submarine Pipe-lines Act 1975, the British government established the British National Oil Corporation (BNOC). The aim of the British government in setting up BNOC were:

(a) to secure for Britain the full benefit of its oil;

(b) to acquire information and expertise through participation in the councils of the oil companies;

(c) to secure national use of oil extracted in the U.K..

Subject to certain provisions of the Petroleum and Submarine Pipeline Act 1975, BNOC could act as the agent of the Crown. The British government pinned great hopes on BNOC,

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167. Ibid at 284.

168. Ibid. at 17.
and the Act empowered it

"... to perform for the government the services connected with petroleum at request.... to do anything required for the purpose of giving effect to agreements entered into by the Secretary of State with a view to securing participation by the government of the U.K., or by the Corporation, in activities connected with petroleum beneath controlled waters...." 169

However, the British policy for participating in its offshore petroleum industry did not provided the expected economic benefits. On the contrary, the state oil corporation grew to become a financial burden on the British government's budget. As a result, in the mid-1980s, the British government reduced its support to the state oil corporation. In practice, the British government eventually changed its policy of direct state participation in the offshore petroleum industry.

Under the Oil and Pipeline Act 1985, the role that BNOC played was greatly reduced.170 It could no longer be regarded as a servant or as an agent of Crown.171 The new


171. Under the Act, "The Agency shall have power (a) to enter into agreement for the carrying out on behalf of the Crown of activities with respect to petroleum, pipelines and storage installation held by or on behalf of the Crown; (b) to enter into such participation agreements as the Secretary of State may determine." Ibid. at 1880.
act stipulated that BNOC should not enjoy any status, privilege or immunity of the Crown. It was not to be exempt from any tax, duty, rate, levy or other charge whatsoever, whether general or local.\footnote{Ibid. at 1880.}

In 1988, the British government sold its BP shares, and BNOC was taken over by BP. Presently, the British government pursues a privatization policy regarding state run enterprises. State participation in the offshore petroleum industry is not part of current British government policy. With less government interference in the British offshore petroleum industry, the development of the industry tends to be more vigorous. Privatization may prove to be a sensible policy if it leads to greater innovation on the part of oil companies and increased economic benefits to the state.

At present, State participation has become a policy commonly adopted by most oil producing countries, including China. Many countries regard state participation as a means of safeguarding state sovereignty and as an effective method of protecting their economic interests.\footnote{In recent years the trend is toward greater participation of the state in petroleum resource development and that solely because the producer countries have perceived the need of controlling this critical resource in order to strengthen its economic and strategic position in the world arena. The concept of direct state participation in the development of petroleum resources has been widely accepted.} The flexible
manner of the British government in dealing with state participation in the offshore petroleum industry can be used as a different example for other countries in formulating their petroleum laws. The current Chinese offshore petroleum law was formulated ten years ago under the influence of the old political mode, and state participation has been considered a decisive principle in China's offshore petroleum law. In China, just as in Britain, the economic interests and the oil income from the offshore petroleum industry have become the primary concern of the government. Given the positive British legal experience in its offshore petroleum industry, it might be a useful exercise for the Chinese government to reexamine its state participation policy in order to accelerate the development of its offshore petroleum industry and to attract foreign oil companies.

and implemented in many parts of the world, and both developing and developed countries have enacted laws and acts that assure them of direct participation in the management of petroleum operations, including the power of determining the rate, price, and distribution of production sharing, or full state participation. Even the United States which has traditionally favoured the concession system is now beginning to explore options whereby the government would have an operating interest. The degree of success achieved by various systems as adopted by different countries varies greatly, and this in large measure 'reflects the petroleum potential and the bargaining strengths of the countries involved.' Paul C. Yuan, "China's Offshore Petroleum Resources Law--A Critical and Interpretative Analysis" (1982) Vol.16 No.2 The International Lawyer 647 at 653.

"The establishment of Statoil in Norway, and that of British National Oil Corporation, are in part influenced by the need to develop national capacities to deal more effectively with the multinational oil companies." Supra, note 102 at 65.
D. The Power of Secretary of State

The Secretary of State has enormous powers over oil activities in the U.K.. He is entitled to grant petroleum licenses to oil companies, modify provisions of model clauses of the licences and he can empower the State oil companies to act as agents of the Crown or the government. All important government polices regarding the petroleum industry in the U.K. must be shaped with the prior consent of the Secretary of State. The Secretary of the State acts as the representative of the Crown interest to control and supervise the development of the petroleum industry in the U.K.. This is another special feature of the legal system of the U.K.

E. Conclusion

The U. K. is a common law country. It was the earliest country in the world to become industrialised and to be engaged in the exploitation of offshore petroleum resources. In the long process of developing its industry, the British government accumulated abundant legal experiences which have been applied in establishing its petroleum legal system and policy.
In sum, the petroleum law of the U.K. has the following features:

(a) A petroleum license is used to be the contractual agreement as well as the law governing the petroleum activities.

(b) There is less government interference (no state participation).

(c) The discretion of the Secretary of State plays an influential role.

(d) Financial income from the petroleum industry remains as a major incentive to the government to adjust its petroleum policy frequently.

Generally speaking, economic goals drive adjustments to the petroleum law in the U.K.. The British government is good at deploying its tangible economic interest to stimulate foreign oil companies to invest in its offshore oil industry. The British government has underscored the importance of the taxation, royalty, and other financial incomes, which have been engendered by the development of its petroleum industry and have provided huge financial support to
that country. The most outstanding feature of the British oil and gas law is that profits from the petroleum industry are the paramount objective of the government policy.

Britain has accumulated experience over a long period of time in enacting and applying petroleum laws. It has developed these laws smoothly and flexibly in various national and international circumstances. From 1934 to the present time, the British Parliament has promulgated several statutes to regulate the petroleum industry according to changes in the factors affecting the development of the offshore petroleum industry. Although the British petroleum law has the main objective, as is the case in other states, of safeguarding its sovereignty and economic benefit, the British government has scarcely stuck to a fixed pattern in its cooperation with international oil companies. The British government's adept legal experiences have rejuvenated its petroleum industry and greatly benefited the country.

When the British government decided to tap the petroleum resources in the North Sea, it encountered the same difficulty as the Chinese government. The British government was also short of capital and advanced technical expertise. However, it established effective oil and gas laws to meet the requirements of offshore industrial development. The U.K. oil and gas law helped to attract foreign investments and turned
the U.K. into an important oil producing country. The recent wealth of the U.K. has been mainly brought about by the offshore petroleum industry. China is a country with a long coastline and a vast continental shelf. To reform its economy, the Chinese government wishes to develop its offshore petroleum industry. The legal experience of the British government regarding the offshore petroleum industry is worth studying by the Chinese government.

II. Oil and Gas Law In Canada

Canada is an important oil producing country in north America, whose oil reserves rank highly in the world. In Canada, proven oil reserves have been discovered mainly in the western provinces, Yukon Territory, Northwest Territories and the eastern offshore area. Alberta is an important oil province and 85% of Canada's oil output is produced there.\footnote{Supra, note 155 at 114.}

Both Canada and U.K. are common law countries, but their oil and gas laws are fundamentally different. In Canada, the ownership of oil resources remains a tough legal issue. Proprietors at various levels are all given exclusive rights to tap the country's petroleum resources. Therefore, the common law and the statutes in Canada governing petroleum

\footnote{Supra, note 155 at 114.}
activities are more intricate than those in U.K.. As far as petroleum activities on Canadian lands are concerned, the governing laws have been significantly influenced by U.S. law. On the continental shelf, the ownership of petroleum resources belongs to the federal government; the Canadian offshore petroleum industry is governed by Canadian federal statutes. According to the relevant agreements, petroleum activities carried out in the offshore area are managed by the Canadian government and the adjacent coastal provincial governments jointly.

Canadian petroleum law contrasts with that of the U.K. and China. It provides an alternative model that is worthy of study by the Chinese government.

A. Lease System

Unlike the British oil and gas law, the mineral rights for petroleum in Canada are not exclusively vested in the Crown. In Canada, the mineral right is enjoyed by the landlord, regardless of the landowner's title in Crown land or

175. "Canadian oil and gas law has been significantly influenced by U.S. law. The reason is that basic industry documents, particularly the freehold oil and gas lease, were developed first in the U.S. and subjected to U.S. juridical interpretation." A. R. Lucas and C. D. Hunt, Oil and Gas Law in Canada. (Toronto Calgary Vancouver: Carswell, 1990) at 1.
in private land. In Canada, anyone who wishes to possess the ownership of petroleum resources has to meet two conditions:

(a) to have the mineral right;

(b) to have the capacity to extract crude oil from the oil trap in the ground.

This difference in the legal practice between Canada and U.K. has explained the nature of the Canadian oil and gas laws and explains why that the fundamental legal vehicle governing the Canadian petroleum industry is the lease system rather than the license system.

The lease system was the result of private ownership. At common law in Canada, the ownership of petroleum resources located in private land is determined by the rule of capture.\(^{176}\) This rule was an active factor in the formation of Canadian oil and gas law. Originally, the petroleum

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\(^{176}\) "The rule of capture may be stated as follows: There is no liability for capturing oil and gas that drains from another's lands. The owner of a tract of land acquires title to the oil and gas that he produces from wells drilled thereon, though it may be proved that part of such oil and gas migrated from adjoining lands. The rule of capture is unusual as a rule of law because it is a rule of nonliability. It gives a mineral owner the shield of positive legal principle as he develops oil and gas resources from his lands." John S. Lowe, *Oil and Gas Law.* (St. Paul, Minn: West Publishing Co., 1988) at 9.
industry in Canada was governed by private law. Landlords not only own the surface right of the land, but also the underground mineral resources. Since crude oil, a migratory mineral, can flow underneath the land surface, the ownership of the petroleum resources in the strata does not explicitly belong to the landlord who has title to land through which oil resources flow. The rule of capture was defined to mean that the petroleum resources should be owned by the land owners who could physically possess it.

To obtain the mineral right, an oil developer had to negotiate or bargain with the landlord to sign a lease. The lease between an oil developer and a landlord was essentially the law governing the petroleum industry on the private land in the early times of Canada. Current Canadian oil and gas law is an extension of such private leases.

Oil companies must have two kinds of leases in hand before they are legally permitted to embark upon a prospective undertaking. One of them is an oil and gas lease, the other is a surface lease.

177. "Originally, oil and gas was almost entirely a private law field. Questions of ownership and rights under various industry agreements were the dominant concerns. More recently, however, and particularly in the last 15 years, public law issues in oil and gas law have become increasingly important." Supra, note 175, at 2.
The oil and gas lease is not a tenancy lease. It merely offers an exclusive right to recover subsurface oil resources. The lease is a critical legal instrument by which the landlord grants the mineral right to oil developers to carry out oil activities. If oil and gas are owned in situ, an oil and gas lease will turn oil developers into rich men overnight.

Apart from an oil and gas lease, oil companies also need to sign surface leases with the landlords in order to enter the leased land.

In Canada, surface rights and mineral rights are separately vested in the hands of landowners. The purpose of the statutes which protect the surface rights is to create a new interest for landowners. The operators of the petroleum industry have to pay compensation to the landowners for the right to enter the land where the mineral might be located. The surface right allows oil companies to use transportation and install the equipment to develop the oil production. To

178. "At common law, neither a life tenant nor a remainderman can develop oil and gas." Ibid. at 106.

179. "Historically, grants of mineral interests normally carried with them surface rights to the extent reasonably necessary to permit the mineral owner to enter, win, work and remove the minerals. However, the western provinces have by statute removed this surface right facet of the mineral estate." Ibid. at 86.
acquire surface rights, oil companies have to negotiate with landowners or their agents to reach agreement. The consent of the landowners is another indispensable condition for oil companies to start their work according to the law.\textsuperscript{180} To have a surface lease is another important legal procedure for oil companies to go through.

Both the oil and gas lease and the surface lease govern the activities of oil companies. Without these legal instruments, oil companies are not allowed to start their work. An oil and gas lease represents the commercial interest between the landowner and the oil company. The normal contents of a lease include the lease term, minimum work commitment, royalty, rent and etc. Since the creation of the lease is subject to negotiation between the oil company and the landowners, the terms of a lease can be reached in a flexible way according to the specific situation. An outstanding contrast between a Canadian oil and gas lease and a British oil and gas license is that the Canadian lease offers more flexibility to cover the commercial interests of the relevant parties. The oil and gas lease has become a feature of the Canadian oil and gas law. Petroleum activities in Canada are highly commercialized.

\textsuperscript{180} Ibid. at 90.
In the final analysis, the Canadian petroleum industry is based on private commercial activities and multiple ownership. The rule of capture reflects the capitalist doctrine of free competition. Private land ownership lays down a legal foundation for the Canadian petroleum industry. These two factors, capture and ownership, constitute the legal framework for Canadian oil and gas law. The purpose of Canadian oil and gas law is to promote private petroleum activities. The oil and gas lease system is a key to understanding the development of the Canadian petroleum industry. It is also the core of Canadian oil and gas law, reflecting the typical commercial deal in the capitalist world.

B. Legal Regime on the Provincial Crown Lands

Crown lands in Canada are owned by the governments at either the federal or provincial level. Both federal and provincial statutes have provisions governing the petroleum industry. In order to have an overall analysis of oil and gas law in Canada, a study of statues enacted respectively by relevant provinces and federal Canada to protect Crown interests in the development of the petroleum industry will be helpful.
In Canada, the provinces have mining laws that differ widely. A lease offered by a province is called a "Crown Lease". Currently, all the western provinces use a two-stage tenure system to govern the oil activities in Crown lands.

In the first stage, the oil developers have to apply for an exploration license. When the exploration leads to a commercial discovery, the licensee will be entitled to apply for an oil and gas lease. The exploration licence only grants the license holder the right to conduct the geophysical exploration for petroleum. The production rights for petroleum resources are subject to the oil and gas lease.

In Alberta, the term for an exploration licence is two to five years depending upon whether the location applied for is in the plains, northern or foothills area.\(^\text{181}\) The term of an oil and gas lease is 5 years.\(^\text{182}\)

In Saskatchewan, the exploration permit is for three years but may be extended for another two years, subject to the approval of the minister responsible. There is another exploration permit in Saskatchewan known as the drilling reservation, the term of which is one year. The term of an

\(^{181}\) Ibid. at 15.

\(^{182}\) Ibid. at 14-7.
oil and gas lease in Saskatchewan is five years. When an exploration permittee applies for an oil and gas lease, he has to relinquish forty to sixty per cent of permitted areas.183

In British Columbia, geophysical permits are classified as Class A, B, C, or D., depending upon the accessibility and the terrain of the location. The term of a geophysical permit is seven years. A qualified applicant may obtain an oil and gas lease lasting five to ten years.184

In Manitoba, oil companies have to apply for an exploration reservation, the term of which is three years. The term of an oil and gas lease in Manitoba is five years. Subject to an extension penalty, such a lease may be extended for a longer term.

As representatives of the Crown interests, ministers of all the above mentioned provincial governments have the right to grant exploration licences or oil and gas leases to qualified applicants. In the normal sequence of events, oil companies have to first complete their work commitment for the exploration. They will then be able to apply for oil and gas leases.

183. Ibid. at 17-9.
184. Ibid. at 19-21.
The advantage of the two stage tenure system in the western provinces in Canada is that it inspires oil companies to accelerate their work and create more opportunities to increase revenue to the local government. Generally speaking, the terms for exploration licences or oil and gas leases in the western provinces are not too long. Such a restricted time limit will press oil companies to work hard to look for oil and do their best to produce as much oil as they possible so as to create more royalties, land rent and tax revenue for the provincial governments. The entire purpose of the provincial system governing the petroleum industry in Crown lands is to extract the largest financial gains for the governments concerned.

C. Legal Regimes on Federal Land

The objective of the Canadian federal government's petroleum policy is "to have energy policies ensuring the best management of our resources for the general welfare of Canadians." 185 Because of the Arab oil embargo in the 1970s, the Canadian federal government attaches importance to the development of its own petroleum industry.

185. Ibid. at 43-4.
Petroleum activity on federal lands is subject to the Canada Petroleum Resources Act (CPRA) and the Oil and Gas Production and Conservation Act (OGPCA). The Canada Oil and Gas Lands Administration (COGLA) is the managing organ for the federal Crown petroleum interest.

Three kinds of tenure are effected in the federal lands to govern the petroleum industry.

(a) Exploration Licence (EL):

The terms and conditions of an EL may be agreed between the minister and the interest owner. The period of an EL may not exceed nine years.187

(b) Significant Discovery Licence (SDL):

Subject to the preliminary discovery of the first exploration well by the EL holder and the declaration of the minister, an EL holder may apply for a SDL. The term of a SDL is not specifically provided by the Law.

186. Ibid. at 51.

187. Ibid. at 54.
(c) Production Licence (PL):

When an EL and SDL holder makes a commercial discovery, he is entitled to a PL. The grant of a PL is also subject to the declaration by the minister as to the existence of the commercial discovery. The term of a PL is twenty-five years but an extension will be granted as long as petroleum is being produced commercially.\textsuperscript{188}

The EL and SDL permit oil companies to carry out the petroleum exploration on federal lands. The PL allows an oil company to have title to the petroleum produced in the licensed area.

Under OCPCA, a PL and a share therein can only be held by a company incorporated in Canada, a Canadian citizen or a permanent resident of Canada. Canadian ownership of the owner cannot be less than 50 per cent.\textsuperscript{189}

\textsuperscript{188} Ibid. At 55.

\textsuperscript{189} Ibid. at 56.
D. East Coast Offshore Oil and Gas Development

The east coast of Canada lies adjacent to the European North Sea area. The success of the petroleum industry in the North Sea stimulated the Canadian government to exploit its offshore petroleum resources. However, the long-standing jurisdictional dispute between the federal and provincial governments prevented the Canadian government from seizing the best chance.

It was not until the March 1984 that the question of ownership was finally decided by the Supreme Court of Canada, stating that rights over offshore resources were vested in the federal government.  

To manage the Canadian offshore petroleum industry, the federal government has reached two critical agreements with the relevant provincial governments, e.g.

[1] the Atlantic Accord of 1985 and


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These two Accords were designed to create management frameworks between the federal government and the Newfoundland and between the federal government and Nova Scotia respectively. The contents of these Accords include

(a) the establishment of funds to promote the development of the offshore petroleum industry, and

(b) the distribution of royalties, revenues and taxes accumulated from the petroleum activities between federal government and the two provinces.

Canadian-Newfoundland Offshore Petroleum Board (CNOPB) and the Canadian-Nova Scotia Offshore Petroleum Board (CNSOPB) are two policy-making organizations to be responsible for the petroleum industry in the Canadian offshore area.

The purpose of the Canadian offshore petroleum developing plan was to promote the development of the economy of the east coast area and to increase the employment opportunities. The Canadian federal government and the Provincial governments of Newfoundland and Nova Scotia all place their hopes in the development of the offshore petroleum industry. They expected that the development of the Canadian offshore petroleum industry would bring prosperity and economic benefit.
However, the long lasting legal dispute over the sovereignty of the territorial waters meant that Canada missed the best opportunity to develop its offshore industry. The downturn in world oil prices in the middle 1980s caused a recession in the offshore petroleum industry worldwide. So far there has been no striking achievement made by the Canadian offshore oil industry.

E. Conclusion

In general, oil and gas law in Canada has the following features:

(a) The lease system is the basic legal vehicle for facilitating the development of the petroleum industry.

(b) The relevant provinces have independent laws to govern the industry within their territories.

(c) The right of the federal government to manage the petroleum industry is confined to federal land and the Canadian offshore area.
(d) There are no state run oil companies.

In Canada, land titles decide crude oil mineral rights. Since lands are respectively owned by private landlords, provincial governments and the federal government, mineral rights of the petroleum resource vest in the hands of these land owners. To defend and coordinate the interests of various proprietors related to the petroleum industry, oil developers and the Canadian people, the Canadian legislatures at different levels promulgated a large number of statutes, which complicated Canadian oil and gas laws.

There are two significant features in Canadian oil and gas law.

First, the prevailing lease system in Canada covers the commercial interest between oil companies and landlords. In the Canadian petroleum industry, every petroleum lease represents a concrete law governing a related petroleum development project. Since the petroleum lease is established through negotiation, the lease holders have tried their best to protect their interests in the lease. Besides, the Canadian government has interfered little with private commercial interest in the petroleum industry. The practice of the oil and gas lease system exhibits the flexibility of
the Canadian oil and gas law.

Second, the Canadian government uses the federal and provincial laws to maintain the public interest.\textsuperscript{191} The Canadian oil and gas law emphasizes environmental protection, tax income and other benefits relevant to the public in the development of its petroleum industry. However, because of the two levels of legislative power in Canada, the complicated legal procedure, as well as the substantive law remains to be an obstruction to the efficient development of the petroleum industry. As a result, Canadian oil and gas law does not sound appealing to foreign investors.\textsuperscript{192}

\textsuperscript{191}. For example, the rule of capture encouraged oil developers to exploit the oil resources wildly and resulted in the damage to the Canadian ecological environment and the natural structure of the oil field. To balance the public and private interests regarding the petroleum industry, the Canadian legislatures promulgated regulations to restrict the rule of capture in term of well space, pooling, well licensing, production rate and so on. In this way, the Canadian petroleum industry will be developed to the advantage of the public. See supra, note 175 at 199-207.

\textsuperscript{192}. The territorial disputes over the Canadian offshore areas between the federal government and the coastal provinces are examples of the inefficiency of the Canadian petroleum industry. " ....the uncertain status in Canadian law of intergovernmental agreements means that the provisions of Accords are unlikely, in law, to prevent the federal government from amending the enabling statues without consulting the two provinces.... The issue of jurisdiction over territorial sea off Newfoundland is unresolved in the face of dormant appeal of the Newfoundland Reference; a federal decision to alter either regime on its own would undoubtedly bring the legal issues to fore again....Prior to the Accords, the existence of two sets of governing legislation administered by two levels of government sometimes created an almost untenable situation for offshore operators." Supra, note 190 at 43-57.
Canada has vast land and huge resources with a relatively small population and its economic environment is entirely different from that of China. It is not as anxious as China to absorb foreign investment to develop the petroleum industry so as to enable the economy to flourish. The petroleum policy of the Canadian government demonstrates a lack of enthusiasm in attracting foreign investment to develop its petroleum industry. Current Canadian oil and gas law seems to favour domestic oil enterprises to exploit its petroleum resources.

III. Legal Comparisons of Practices in the Offshore Petroleum Industry

A. Précis of China’s Offshore Petroleum Law

China's offshore petroleum industry is a domain where foreign oil companies function as top players. The major task of China's offshore petroleum law and policy is to control the cooperation between China and foreign oil companies.

China's offshore petroleum law and policy are marked by several outstanding features:
(a) Legal frame:

Foreign Investment Enterprise and Foreign Enterprise Tax Law of the PRC (FIEFETL)\textsuperscript{193} and Regulations of the PRC on the Exploration of Offshore Petroleum Resources in Cooperation with Foreign Enterprises (Regulations)\textsuperscript{194} are two statutes directly governing China's offshore petroleum industry.

China National Offshore Oil Corporation, a state company, has an exclusive right to run China's offshore petroleum industry.

A model petroleum contract formulated by China National Offshore Oil Corporation is a concrete legal instrument binding the operation of foreign oil companies working in offshore China.

(b) Legal features:

There are three main legal features: risky foreign investments, the oil production sharing model, and

\textsuperscript{193} Supra, note 73.

\textsuperscript{194} Supra, note 57.
Foreign investments in offshore China for the exploitation of petroleum resources are risky ventures. The investors will bear the risks associated with exploration.

With regards to the oil production sharing model, when a commercial oil field is discovered, the Chinese government is entitled to participate in up to 51% of shares.

The Model petroleum contract calls for the establishment of a Joint Management Commission (JMC) composed of representatives from CNOOC and the foreign company. The JMC will be chaired by a CNOOC representative and has the power to determine the commercial discovery of a oil field, approve major expenditures and decide other important issues.\textsuperscript{195}

(c) Other legal regulations:. The exploration term for foreign petroleum contract holders will be seven years, production

\textsuperscript{195} See supra, note 150.
term will be fifteen years and the entire contract term will be no more than thirty years.

Foreign oil companies are required to transfer to China the advanced technology which was used in offshore petroleum activities in China and give preference to the utilization of Chinese engineering designs, Chinese made facilities and the Chinese services.

Foreign oil companies will propose an "X" factor, based on which the profits produced from the contracted field will be split between CNOOC and the foreign contractors.¹⁹⁶

¹⁹⁶. The formula to split the oil output in China's offshore petroleum industry between foreign oil companies and the Chinese side is rather difficult. Among the output, 17.5% goes to the government (royalty and tax), 50% goes to the cost recovery. The remaining 32.5% will be divided into two portions by an "X" factor. One portion goes to CNOOC directly as share oil. Another portion will be split between CNOOC and foreign contractors by 51% and 49% respectively. The negotiation on the "X" factor is a crucial condition to entering the petroleum contract. See supra, note 122, article 13.
B. Comparison of Petroleum Laws

China is a socialist country with a long unique legal tradition. The laws of China are different in nature from those of the U.K. and Canada. Nevertheless, to narrow the economic gap between China and these countries, the Chinese government must understand the western legal tradition and learn from their advanced experience in legal practice. A brief comparative study of laws governing the development of the offshore petroleum industry in the U.K., Canada and China might be able to extend constructive suggestions to the Chinese government in developing its own offshore petroleum laws and policy.

The characteristics of the development of the Chinese economy are similar in many respects to those of other third world countries. Therefore, the Chinese government adopted the model comparable to those of the developing oil producing countries to tap its own petroleum resources. The legislative purpose of China's offshore petroleum law is to encourage foreign oil companies to invest in offshore petroleum industry so as to be able to obtain capital and technology. Since China's offshore petroleum industry was late to develop, the Chinese government lacked the necessary experience to manage
the industry. Compared to the U.K. and Canada, China was relatively unsophisticated in establishing its offshore petroleum law. It is not enough for China to simply have foreign investment and advanced technology introduced to develop its offshore petroleum industry. The Chinese government also needs to grasp the knowledge of legal practices applied in the development of offshore petroleum industry in all the developed countries including the U.K. and Canada, which will accelerate the speed of modernization of China's offshore petroleum industry.

There are abundant similarities between the oil and gas law in the U.K. and offshore China. The fundamental reason for the similarities is that the titles of the offshore petroleum resources in these two countries are both owned by the state.

(1) Both the statutes enacted in the U.K. and China underscore the country's respective sovereignty over their petroleum resources.

(2) The governments of both the U.K. and China directly control the exploitation of their respective offshore petroleum resources. In Britain, foreign oil companies are required to apply for licenses from the government in order to
acquire blocks in offshore area. In China, foreign oil companies must enter into model petroleum contracts in order to obtain the right to operate in the offshore areas. The petroleum license of the U.K. and the Chinese model petroleum contract serve the same purpose, namely, they govern the petroleum activities of foreign oil companies.

There are certain fundamental differences between oil and gas laws in the U.K. and China. The most conspicuous difference is that the British government's control in the offshore petroleum industry is far more flexible than that of the Chinese government. British petroleum law aims to increase government revenue from the petroleum industry. China's offshore petroleum law aims to enhance the entire level of China's economy and asks for foreign investors to make as much of a contribution as possible. This contrast between China and the U.K. demonstrates the different characteristics of their social economic structures. As a socialist country, the Chinese government exercises a planning economy. Traditional Chinese politics translated into the establishment of China's comparatively rigid offshore petroleum law and policy.

Canadian and Chinese petroleum laws belong to sharply different systems. The two countries share few commonalities
in their respective legal practice with regards to the petroleum industry. In Canada, the basic legal instruments governing the activities of oil companies are leases, which offer oil developers leverage to negotiate with petroleum resource owners. Both at common law and in accordance with the statutes of Canada, there are much fewer restrictions and requirements for foreign oil companies than in China. The Canadian federal government attaches much importance to the interests of the local people. Through the law and policy governing its offshore petroleum industry, the Canadian government has made efforts to increase local employment opportunities in the industry so as to prosper the local economy, which is a worthy example for the Chinese government. In China, all the benefits of the offshore petroleum industry belong exclusively to the central government. The Chinese government should take more of the provincial and local economic interests into account. However, in terms of the general public interest such as environmental and resources protection, both the Canadian and Chinese governments have shown due concerns respectively in their oil and gas laws. There is one weakness in the establishment of the oil and gas law in Canada. Since both provincial and federal governments in Canada have the legislative right, there is much disorder with regards to jurisdiction and applicability of laws.
The common law and statutes of Canada governing the petroleum industry bear close semblance to those of the U.S.A.. Large portions of the Canadian petroleum laws was enacted to cover litigation arising from legal interests. Foreign investors who intend to exploit petroleum resources in Canada must take serious steps to avoid pitfalls. In China, the likelihood of comparable litigation is far less. The target of China's offshore petroleum law is clearly focused on the immediate concerns of foreign petroleum-exploiting companies and the Chinese government. Compared to the oil and gas law of Canada, Chinese offshore petroleum law is more efficient in attracting investment from foreign oil companies.

In summation, the comparison of the legal practices in the U.K., Canada and China regarding the petroleum industry shows that the Chinese government has a long way to go in improving its offshore petroleum law and policy. Being a socialist country, China has long been used to relying on administrative orders to run its petroleum industry, thus accounting for the backward state of its economy.\(^{197}\) This

\(^{197}\) "... Another notable example is the review of the accident of Bohai No2. drilling rig. The accident happened in November 25, 1979. A drilling rig named Bohai No 2 which was owned by the Offshore Oil Exploration Bureau of the Ministry of the Petroleum Industry capsized in the Bohai Gulf. Seventy two crew members on the rig were killed. The economic loss arising directly from the accident was 37.35 million Chinese Yuan. The reason of this accident was that the leaders of the Ministry of Petroleum Industry ignored the regulations and
ideological position affected the establishment of China's offshore petroleum law. In China's offshore petroleum industry, the government exercises strict restrictions and frequent interferences even in minute matters. As well, the legislation of China's offshore petroleum law is based on the self reliance, which reflects a negative political stand in China. The petroleum laws of the U.K. and Canada are centred mainly on economic interests. These laws pay less attention to detail. It is in China's best interest that the Chinese government should prioritize economic interests in the formulation of its offshore petroleum law and policy.

Through the comparative study of oil and gas laws in the U.K. and Canada a common point can be discovered. The economic interests in the petroleum industry are the focus of forcefully issue orders to the operation.... According to the uncompleted statistics, between 1975 and 1979 before the accident of Bohai No.2, there were 1043 accidents in the working scope of the Offshore Oil Exploration Bureau. More than thirty accidents were serious and major, killing 105 people and heavily injuring 114. The Chinese procuratorial authorities never paid any attention to those accidents" (Before 1982, there was no China National Offshore Oil Corporation. Offshore petroleum industry then was in the charge of Offshore Oil Exploration Bureau). Zhang Xin, Zhong Guo Fa Zhi De Xian Zhuang Yu Gai Ge (China's Legal System and Its Reform) (Hongkong: Mingbao Pressing House, 1988) at 202 (my translation).

"The legal uncertainty is in fact a reflection of policy fluctuations which are inherent to Chinese politics. There is no separation of legislative, judicial and executive powers in China, nor a mechanism of "check and balance" to keep the government machinery healthy and sound. In China, the Communist Party controls the state machinery and wields absolute leadership over all spheres of government activities. Supra, note 116 at 135.
oil and gas legislation in these countries. In the U.K., it is apparent that the British Parliament continually revises its oil and gas law in accordance with the current situation of its petroleum economy. In Canada, despite the complicated legal framework, the profit-oriented petroleum lease system stimulates the development of the petroleum industry. Economic interests remain the essence of the petroleum laws in both the U.K. and Canada and continue to determine them.

In the process of China's economic reform the Chinese government cannot avoid emulating the western countries in the area of industrialization. Very soon, the economic and legal problems encountered by western countries will be met by the Chinese government. At present, the Chinese government is facing the task of re-examining its laws and policies. It will be a shortcut for the Chinese government in this examination to adopt the useful parts of western legal practices into Chinese laws.
Chapter Five

Concluding Remarks

I. Suggested Reform for China's Offshore Petroleum Law and Policy

For a long period of time, the Chinese government's general policy was founded on the principle of self-reliance, and this dominated policy on offshore petroleum law. Based on past performance, the Chinese government might have appeared to have been opposed to the profound involvement of foreign oil companies in its oil and gas industry. However, the offshore petroleum industry has been considered an exception. The development of this industry requires huge investment and relies on advanced technology; the Chinese government, unable to supply either, was therefore dependent on external factors. Without foreign investment, China could not have developed its offshore petroleum industry. As far as offshore petroleum law and policy is concerned, the legislative principle of the government is to utilise foreign capital and expertise. The Chinese government hoped that the development of its offshore petroleum industry could give a huge impetus to the
development of the economy. Having been isolated from the outside world for over thirty years\(^{198}\), the Chinese government lacks the legal experience to cooperate with foreign countries to develop its industry. The emerging legal regime for offshore petroleum needed to be tested in practice as circumstance changed and amended to meet the developmental needs of this industry.

The following proposals are therefore made.

(a) Revision of the basic government policy:

Shifting government stand from self-reliance to a more flexible policy. The self-reliance policy is a conservative policy, designed for an isolated agricultural country. This policy hinders the further progress of China's offshore petroleum industry and constitutes a hindrance to the absorption of necessary foreign assistance. China's offshore petroleum resources are so large, it is impossible to implement a self-reliance

\(^{198}\) The People's Republic of China was founded in 1949. Since then, the Chinese government has had no significant contact with the western countries. China promulgated its regulations on the cooperation with foreign enterprises in the exploitation of offshore petroleum resources in 1982, which symbolised China's formal invitation to foreign enterprises to its offshore petroleum industry, that is, over thirty years had passed.
policy in order to exploit them. The effective exploration of these resources would necessarily call for the attraction of foreign capital, technology and experience. To modernize its offshore petroleum industry, China needs extensive cooperation with the rest of the world in many aspects. The more China's offshore petroleum industry links with international petroleum industries, the narrower the economic gap between China and the industrialised countries will be. On this point, China should study the offshore petroleum policy of the British government.

(b) Reformation of the pattern of cooperation with foreign oil companies:

So far, China has one model petroleum contract, which limits the cooperative pattern between China and foreign oil companies. China's model petroleum contract was designed to invite major international oil companies and demands a relatively heavy work commitment. The interested foreign oil companies have little choice but to enter into such petroleum contracts if they want to develop the offshore petroleum industry in China. China could take more flexible measures
to encourage more foreign investors into its offshore petroleum industry. China National Offshore Oil Corporation might prepare different varieties of model contracts for interested foreign oil companies. In the new model petroleum contracts, foreign oil companies might be allowed to choose a proper pattern according to their capacities to cooperate with China. In this way, not only large international oil companies but smaller companies too could come to work in China's offshore petroleum industry.

(c) Underscoring the economic interests:

To a certain extent, China's model petroleum contract lacks flexibility. Since the leading objective of China's offshore petroleum law is to promote the country's economic interests, China's model petroleum contract might be modified in a way to underscore such a goal. China's model petroleum contract combines certain characteristics of both the British petroleum license and the Canadian petroleum lease. However, legal instruments for oil in the U.K. and Canada highlight the economic interests of the state. China might increase the provisions in its model
petroleum contract to pay more attention to its economic interest and reduce some concerns of less importance. This will be a way to turn China's model petroleum contract into a more effective and commercial one.

(d) Taking consideration of provincial interests:

Under the present political power structure, the national offshore petroleum industry is under the direct control of the central government. All the revenue which derives from the industry therefore benefits the central government and the relevant provincial governments have no share in it. If the Chinese central government allows provincial governments to participate in the development of its offshore petroleum industry and allows them to share the benefits, the development of China's offshore petroleum industry will become a common concern of the governments at two levels and gain more political support. The participation of China's provincial governments in the offshore petroleum industry may increase local income and employment opportunities, which will also promote China's economic reform as a whole. The central Chinese government might establish a law to allow
provincial governments to form oil companies and bid for the concessions in competition against foreign oil companies. The bidding provincial oil companies could therefore enjoy more rights than the foreign ones. They might issue stocks or securities and transfer the investment risk and benefit to shareholders. After having had the cooperation with foreign oil companies for more than ten years, China has mastered the technology to develop its offshore petroleum industry. What China currently mostly needs is financial investment. The financial participation of provincial governments might provide a new source of capital. At present, China's coastal provinces such as Guangdong Province and Fujian Province have strong economies. It would therefore not be difficult for those provincial governments to raise funds to invest in China's offshore petroleum industry. The policy initiative, however, remains in the hands of the central Chinese government. If the provincial governments could be mobilised by the central Chinese government through legislation, the provincial investments in the development of the offshore petroleum industry could become significant constructive factors.
II. Conclusion

Without a solid economic base, China will be unable to achieve an influential and stable political power base within the world community. To catch up with the economic level of the developed countries the Chinese government is endeavouring to industrialize China. Since the late 1970's, the Chinese government has been pursuing an extensive economic reform programme. The reform of China's economy is bound to evoke corresponding reforms within Chinese legal system.

In China's current reformed economy, the development of China's offshore petroleum industry continues to attract primary attention. During the last decade, the first tranche of large scale foreign investments in the Chinese offshore petroleum industry was made. Both the Chinese government and foreign investors are anxiously expecting the successful outcome of these efforts. However, that success depends to a great extent on the existence and administration of an effective offshore petroleum law; this is as important as adequate financial investment and advanced technology.

To promote the development of China's offshore petroleum industry, the Chinese government has to seriously review its
past experiences and incorporate the beneficial aspects of foreign legal practices. The constantly changing new economic situation always requires that the Chinese government review its offshore petroleum law from time to time. A sound offshore petroleum law is the foundation for a brilliant future for the development of China's offshore petroleum industry and will result in long-lasting benefit for the economy.
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