

# IRAN SANCTIONS – IMPACT ON THE OFFSHORE ENERGY SECTOR



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**Other articles in this Standard Bulletin have examined a number of the prohibitions that are included in the various UN, EU and US sanctions against Iran. In this article, we consider the offshore energy sector and the application of the raft of sanctions regimes to a specific case study.**

## INTRODUCTION

One of the main aims of the US and EU sanctions programmes is to restrict Iran's ability to develop its oil and gas industry and, in particular, its ability to produce refined petroleum products. Given this focus, it is important for all individuals who are involved in this sector, and who may deal with Iranian interests, to obtain comprehensive legal advice regarding the impact of the various sanctions regimes on their business.

While the UN sanctions do not have any specific impact on the offshore energy sector, a number of the prohibitions that are included in the US sanctions and EU sanctions legislation do have a specific impact on the offshore energy sector, and some of these are considered in the following hypothetical scenario.

In addition to the points that are made below, there are likely to be concerns about the inherent commercial risks of any transaction that is in any way connected with Iran. These will include concerns about the availability of insurance, the mechanism for payment and the impact on other projects and aspects of the business if other counterparties prefer not to be associated with Iran.

The best approach, as in all situations where the sanctions against Iran may apply, is to be vigilant, to conduct detailed and thorough due diligence about the project and your counterparties, and to provide full information to the relevant authorities if you have any concerns.

## CASE STUDY – FACTS

Caspian Oil Pte Ltd is a Singaporean company that owns a number of assets, including a drill ship and a small tanker. Caspian Oil is the wholly owned subsidiary of a US company, and its director is a US national. Caspian Oil has been collaborating with a German company, Exploration and Drilling Services GmbH, which owns a fleet of geophysical survey ships (with all of the equipment on board), as well as extensive equipment and material onshore in Iran (including computers and software to analyse the data that they have collected, spare drilling equipment, plus reserves of drilling mud, hydrocarbon crackers, etc.).

Caspian Oil Pte Ltd has been operating for a number of years in Iran, exploring and developing Iranian oil reserves in the Caspian Sea, pursuant to a licence from the Iranian government. Acting together with Exploration and Drilling Services, it has collected abundant data about potential fields, has drilled some exploratory wells and had just started full-scale drilling (under contract to an Iranian state-owned company) when the US and EU sanctions came into force.

## CASE STUDY – RELEVANT SANCTIONS REGIMES

Caspian Oil's American director, as well as its US parent company, will be subject to the full range of US sanctions. In addition, the US Comprehensive Iran Sanctions Accountability and Divestment Act (CISADA) will apply directly to Caspian Oil to the extent that it does business with Iran's petroleum sector. The sanctions have direct effect (in that they apply to the person who has committed the prohibited act), and also indirect effect (in that they apply to any person who owns or controls that person, and also to any person who is owned or controlled by that person). The sanctions apply where the person has actual knowledge, or should have known, about the relevant conduct, circumstance or result.

EU Regulation No. 961/2010 (the Regulation) will apply to Exploration and Drilling Services GmbH, which is a German company. The Regulation includes a specific defence where the persons involved did not know, and had no reasonable cause to suspect, that their actions would infringe the prohibitions in the Regulation.

## CASE STUDY – APPLICATION OF THE SANCTIONS REGIMES TO THE FACTS

CISADA includes a prohibition on making an investment (or a series of investments) that directly and significantly contributes to the enhancement of Iran's ability to develop petroleum resources. Investment is defined to include entry into a contract that includes responsibility for the development of petroleum resources located in Iran; therefore, continuation of the drilling contract would be a breach of CISADA.

Consequently, Caspian Oil immediately contacted the relevant authorities and provided them with full details of their drilling programme. Caspian Oil agreed to suspend drilling operations and, as a result, the authorities agreed not to take any action in respect of the drilling programme. In our discussions to date with the US authorities, they have made clear their strong preference that companies that are engaged in conduct that is potentially subject to the sanctions should engage in a dialogue with the US authorities, so that the company can stop the sanctionable activity, without the need for further action to be taken, by way of investigation and possible prosecution.

Having terminated the drilling contract, Caspian Oil was asked by the Iranian contractor whether it would sell the tanker, or alternatively the cargo of crude oil on board, by way of compensation for the early termination of the drilling contract. Caspian Oil may not sell the tanker, as CISADA prohibits the sale to Iran of goods (etc.) that could directly and significantly contribute to the enhancement of Iran's ability to import refined petroleum products, and goods specifically include ships.

However, CISADA only prohibits the sale to Iran of refined petroleum products (defined as diesel, gasoline, jet fuel (including naphtha-type and kerosene-type jet fuel), and aviation gasoline), so Caspian Oil

would be permitted to sell the cargo of crude oil to an Iranian person or entity. Caspian Oil would, of course, need to check that the Iranian contractor is not on any of the restricted persons lists, before agreeing to sell the cargo. It may also face difficulties in persuading a US bank to process the sale proceeds if these are in US dollars.

Following Caspian Oil's decision to suspend drilling operations in Iran, Exploration and Drilling Services is considering winding up its own operations from Iran. It is wondering whether it may sell the geophysical survey ship, as well as the equipment and materials that are onshore in Iran, to an Iranian company. It is also considering simply handing over the geophysical data, computers and software to another Iranian company, rather than having to remove these. Finally, it is considering providing consultancy services to a third Iranian company that is now likely to oversee development of the wells, in return for an annual fee of €50,000.

All three of these proposals are likely to fall foul of EU Regulation No. 961/2010. Firstly, the Regulation prohibits the sale of key equipment or technology directly or indirectly to any Iranian person, entity or body or for use in Iran. The key equipment or technology is outlined in Annex VI to the Regulation and relates to the oil and gas industry in Iran (specifically in relation to exploration, production, refining and liquefaction). It includes physical equipment (such as the geophysical survey ship and any sampling and testing equipment), as well as materials (such as drilling mud).

Secondly, the Regulation also prohibits the supply and transfer of equipment, which includes software and technology, both of which are vaguely defined. Simply leaving equipment behind arguably falls within either supply or transfer (as these terms are intended to relate to something other than sales).

Thirdly, the Regulation prohibits the provision of technical assistance. Unlike the first two prohibitions discussed above, an authorisation can be obtained to provide technical assistance that would otherwise be prohibited. However, it is unlikely that Exploration and Drilling Services will actually receive payment for its technical assistance, as the rules in the Regulation that permit authorisation of transfers from an Iranian entity that have a value of €40,000 or more will not apply where the transfer of funds would contribute to the prohibited activities.

#### SUMMARY

It will be clear from the above that there are a number of wide-ranging prohibitions that will apply where a US or EU person is dealing with counterparties involved in Iran's oil and gas industry. Detailed legal advice will be required on the facts of each case. In addition, as indicated above, the best approach, as in all situations where the sanctions against Iran may apply, is to be vigilant, to conduct detailed and thorough due diligence about the project and your counterparties, and to provide full information to the relevant authorities if you have any concerns.

## IRAN – PRACTICAL ISSUES



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The various sources of the Iranian sanctions – from the UN, US and EU (and subsequently UK) – have created a complicated regime of rules that have wide-reaching effects on owners, charterers and insurers of ships. Whilst there is no outright ban on doing business with any Iranian party, to do such business is obviously more difficult as a result of the sanctions. There are additional legal and logistical considerations at several points of the shipping transaction, from entering the contract, its execution and, of course, payment.

This article briefly sets out some key steps that owners can take when dealing with an Iranian entity to avoid falling foul of the sanctions. It also offers some practical tips to assist when doing business with Iranian charterers.

Essentially, the sanctions target two main categories: prohibited goods and prohibited parties. As a result, any owner dealing with an Iranian charterer (before and during the charterparty's existence) must check whether the charterer is on the most recent list of prohibited persons, or intends to carry any prohibited cargo. These cautionary checks must also be applied to any potential sub-charterers.

In general, when dealing with Iranian entities, it is essential that owners are diligent and knowledgeable about all of the parties involved in the shipping transaction and check all of the goods when loaded (and keep records of these checks). This is often not so easy in practice!

As well as these checks, it would be wise for owners in contractual relationships with Iranian charterers to write to them and to set out the main terms of the sanctions and their obligations under them, as well as providing copies of the prohibited goods and persons lists. It would also be worthwhile to point out specifically the risks of that charterer dealing with other third parties.

As well as exercising sufficient caution, owners can protect themselves further with additional wording in the charterparty itself (which would also have to be incorporated into any sub-charter). Such wording would expressly provide a mechanism to deal with a situation when orders are given by the charterer that would breach the sanctions. BIMCO does have a standard form of wording, which could be adapted if necessary.

Having manoeuvred these tricky areas, there is then the crucial aspect of getting paid, which is complicated by the position taken by some EU banks and by prohibitions on dealing with certain Iranian banks, as well as transferring over a certain amount to Iranian entities. There are some ways around this; for example, in the UK, there are certain licensing exemptions in place whereby a recipient of funds from a prohibited Iranian bank can apply for a licence from HM Treasury in advance of payment. Otherwise, it may be a case of having to look to other ways of receiving payment, for example, via a different non-designated source. Parties, of course, need to be careful in situations where there has been corporate restructuring to in effect "get round" the sanctions. In such circumstances, whilst there may not appear to be a problem at a first glance, this could still amount to a breach of the sanctions.

Practically, therefore, it is clear that the sanctions create many impediments to dealing with Iranian entities, and although it is not impossible, diligence is constantly required throughout those dealings to avoid potential penalties.