THE NEW IRANIAN PETROLEUM CONTRACT (IPC)

KEY TERMS

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OIL AND GAS

UPSTREAM

- Fourth largest oil reserves and the (second) largest gas reserves in the world
- Iran predicts exports to increase by 1,000,000 bpd by end of 2016/early 2017
- Over $150 billion will need to be invested in the oil and gas sector within the next five years
- Iranian Petroleum Contract to replace old buyback contract

PETROCHEMICALS

- Region’s second largest petrochemicals industry after the KSA
- Plentiful gas reserves to support expansion of the petrochemical industry
- Ambitions to be world’s largest methanol producer

OTHERS

- Potential LNG exports

CONCERNS WITH BUYBACK CONTRACT

Operator Risk	• National Iranian Oil Company (**NIOC**) usually became operator as of commercial production • Risk that NIOC produced insufficient hydrocarbons to allow cost recovery • Further risk that Remuneration Fee adjusted for not meeting production targets
Capital Costs Ceiling	• Cap determined at commencement of project based on estimated cost • Risk that cap was insufficient to cover costs incurred • Little tolerance to take into account potential or unforeseen costs • Only increases for Additional Works approved by NIOC
Further Restraints on Recovery	• Traditionally limited term - Extension of term with mutual agreement • Risk that production phase insufficient to allow cost recovery • No ability to recover costs after end of term • Certain costs only able to be amortized within fixed period • Contractor only entitled to a percentage (maximum 50%) of revenues to recover costs (Iranian law requirement)

CONCERNS WITH BUYBACK CONTRACT (CONTINUED)

Lack of Incentives	• Little upside for Contractor efficiencies or to develop riskier fields or fields that required more costs procedures • Limited transfer of technology and know-how
Local Content	• At least 51% of the value of the project to be contracted locally (Iranian law requirement) • Failure could lead to termination or reduction in Remuneration Fee
Reserves	• Hydrocarbons owned by State • No ability to book reserves

KEY TERMS OF IPC

Contractor	• Incorporated or unincorporated JV with Iranian entity
Term	• Exploration/appraisal – 4 years (plus 2 year extension) for exploration and 2 years for appraisal • Development and production – 20 years (plus 5 year extension for IOR/EOR) • Greater certainty regarding cost recovery and return on investment • Incentive for investors to make longer term investments and maximise field life
Operatorship	• Contractor during exploration/appraisal • Requirement to establish a joint operating company in Iran to operate field during development and production phases
Minimum production levels	• Production targets will exist • Consequences of failing to meet targets is unclear

KEY TERMS OF IPC (CONTINUED)

Cost recovery	• No cap on cost recovery • Some time constraints on recovery during development and production • Term may be extended to allow for additional cost recovery (subject to NIOC approval) • As with buyback contract, Contractor only entitled to a percentage (maximum 50%) of revenues to recover costs
Remuneration Fee	• $/bbl or $/scf • Fee will vary depending on “R-factor” and production rates • Adjustment mechanism based on market price (subject to cap)
Incentives	• Remuneration Fee will reflect exploration risk and field type • Incentives for IOR/EOR • Joint fields given priority

KEY TERMS OF IPC (CONTINUED)

Transfer of technology and know-how	• Express provisions to be included • Exact requirements and incentives are unclear
Local content requirements	• As with buyback contract, at least 51% to be contracted locally • Clear that Iranian government expects a greater percentage and will favour companies that aim to exceed the minimum requirements
Dispute resolution	• Arbitration with details (e.g. seat and rules) to be agreed by parties • Iranian Constitution requires political approval for submission to arbitration in certain circumstances
Reserves	• Unclear whether investors will be able to book reserves

SUMMARY

- Structure is similar to the buyback contract, but with some key changes
- Balance between attracting FDI and protecting Iran and the development of domestic oil and gas sector
- Certain provisions still remain unclear
- Despite “Implementation Day” occurring, certain sanctions still remain in place
- Risk of “Snapback” of sanctions - Not considered an FM event under IPC
- Other legal risks and limitations