inBrief

Doing Business in Iran: The Momentum Builds

By Shahram Safai | October 2016

Over the summer, several European blue chips, certain Fortune 500s and major Asian corporates accelerated their entry strategy for Iran. Some are investing in Iran pursuant to the Foreign Investment Promotion and Protection Act 2002 (“**FIPPA**”), which, amongst other things, provides a sovereign guarantee from the Iranian government. Once an investment has been approved and registered under FIPPA, the government of Iran would pay market value compensation if it is expropriated or nationalized. Also under FIPPA, all invested capital and resulting profit may be repatriated.

Furthermore, the US government has been active since early September in removing certain obstacles to doing business in Iran. In late September, the US government granted permission to two aviation giants to sell aircrafts to Iran. Boeing was granted permission to sell 80 planes and Airbus was granted permission to sell 17 of 112 planes (with permission for the sale of the remaining aircrafts to come shortly). In early October, the US Treasury Department confirmed that foreign banks including foreign banks owned by US banks, may process transactions denominated in US dollars or can maintain US dollar denominated accounts that involve Iran or persons ordinarily resident in Iran (so long as such transactions or accounts do not involve the US financial system or any US person).

The new Iran Petroleum Contract

Meanwhile, in Iran the recent approval of the new Iran Petroleum Contract (“**IPC**”) signals an exciting opportunity for potential foreign investors to enter Iran. Replacing the original “buyback” scheme, this new contract aims to attract foreign investment by establishing a framework for overseas companies to become involved in not only the exploration and development of Iranian oil fields but also in sharing in the resulting production.

Established in the 1990s, the buyback scheme attempted to find a middle ground between the need for foreign oil and gas investors and the restrictions on private (particularly foreign private) natural resource ownership. The buyback scheme contract covered field exploration and development, pursuant to which a contractor would be remunerated in the form of an allocation of the hydrocarbons produced in exchange for the provision of its services. The contractor would receive its remuneration over a relatively short time period - approximately five to seven years - following which the developed field would be surrendered to the National Iranian Oil Company (“**NIOC**”). The contract was based on a distinct work scope, with fixed capital costs (i.e. with the inability to recover any additional and unforeseen costs), fixed remuneration fee and fixed cost recovery period.

As such, it was unpopular due to its inflexibility and largely limited yields.

Features of the new Iran Petroleum Contract

The new IPC provides for an extended duration of involvement of the foreign investor in the project – approximately 20 to 25 years – thereby allowing investors a lengthier cost recovery period after the field first starts producing. It also allows investors to invest in higher risk onshore and offshore fields in return for payment of higher fees compared with the lower risk onshore fields. This would allow a company to add varying Iranian petroleum ventures to its portfolio based on its own risk-reward model.

The new IPC also proposes the creation of a joint venture between a foreign partner and NIOC (or a subsidiary of the NIOC) for the exploration, appraisal, development and now, the production of a field (clearly signifying the opportunity for increased profitability in such investments compared with the old buyback scheme contract which did not allow participation in profits from production).

The new IPC also envisages that there will be provisions for investors to include any revenues in their financial reporting, making it a potentially crucial incentive to foreign investors looking to increase profile and standing in the global market.

In addition, to appeal to foreign investors used to having some control over the way their business and joint ventures are conducted, the IPC will include an annual work program and budget which will require approval by a joint venture development committee. This is clearly an important change since under the old buyback scheme, any costs incurred in excess of the amount already fixed and agreed were irrecoverable, thus affecting profitability. Now, investors will have greater flexibility to agree a budget and method for approving and recovering any additional costs.

Ultimately, the new IPC provides investors with a greater degree of flexibility and the opportunity to negotiate better terms, allowing for increased returns and better profitability. Despite the perceived benefits, there is still the potential risk that the local joint venture party (i.e. NIOC or its subsidiary) may have more power to control the project. As it is likely that the foreign investor will be assuming the majority of the risk associated with such a project, a foreign investor should consider negotiating additional security in order to be better protected in terms of cost recovery and remuneration. ■

***

Given the increased influx of foreign corporates into Iran over the summer; the US Treasury Department's permission in late September to Boeing and Airbus to sell aircrafts to Iran; the US Treasury Department's confirmation that foreign banks may process US dollar transactions of persons in Iran so long as such transactions do not involve the US financial system or US persons; and the introduction of the more competitive and streamlined Iran Petroleum Contract, the expectation is that the momentum for doing business in Iran will increase at an even greater pace after the November US elections.

The Author

Shahram Safai
Partner
ssafai@afridi-angell.com
Tel: +971 4 330 3900

Shahram's practice consists of corporate law, real estate law, disputes, and advising on the legal aspects of doing business in Iran. He also advises on private equity and venture capital transactions. He heads the firm's Iran, real estate and venture capital teams and has been highly sought after by boards and shareholders for strategic legal advice. He is active in lobbying for, providing constructive feedback to and advising government organizations regarding regional laws and regulations pertaining to doing business, real estate and venture capital investment.

His Iran practice involves advising clients with respect to investments, joint ventures, as well as introduction to sector specific private and public entities in Iran. Such advice generally involves franchise and agency matters, build-operate-transfer transactions, regulatory compliance and strategies, foreign investment protection regimes, sanctions and anti-money laundering implications. Shahram is fluent in Farsi and he is a qualified solicitor in England and Wales and a member of the California State Bar. He is also a registered professional engineer.

Shahram's specific Iran related work has included advice relating to:

- Manufacturing sector joint ventures, commercial agency arrangements and local partner introduction.
- Onshore and Free zone entry advice, incorporation and liaison.
- Private equity transactions involving financial institutions.
- Build-operate-transfer arrangements related to the oil and gas sector.
- Hospitality industry legal and regulatory matters as well as related construction matters.

Shahram is described as "a cut above the rest with thorough knowledge, sharp analytical prowess, understanding of the industry, good relationships with government authorities and the best of communication skills" (Legal 500 EMEA). He is described as "quick, responsive and forthright" and a "Leader in [his] Field" (Chambers Global).

AFRIDI & ANGELL
LEGAL CONSULTANTS

Afridi & Angell

Founded in 1975, Afridi & Angell is one of the leading and most established full-service law firms in the UAE. The firm provides comprehensive legal advice and innovative business solutions in banking and finance; corporate and commercial law; dispute resolution; projects; construction and real estate; employment; energy; project finance; transport; as well as doing business in Iran, the UAE and the DIFC. We advise local and regional clients ranging in size and sophistication from start-ups to some of the region's largest public and private companies, governments and quasi-government institutions. We work extensively with entrepreneurs and investors from the region and beyond, and have attracted numerous international clients looking for the right counsel to protect and expand their interests.

Afridi & Angell is a selected member of top legal networks and associations, most notably Lex Mundi, the world's leading network of independent law firms, and World Services Group.

www.afridi-angell.com

Afridi & Angell's inBrief provides a brief overview and commentary on recent legal announcements and developments. Comments and opinions contained herein are general information only. They should not be regarded or relied upon as legal advice.

© 2016, Afridi & Angell