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22 October 2013

Dear **REDACTED**,

**THE HYDROCARBONS (TEMPORARY MANAGEMENT SCHEME) REGULATIONS
2013: DECISION NOTICE IN RELATION TO THE APPLICATION OF A TEMPORARY
SCHEME**

1. Thank you for your letter of 23 July 2013 in response to the Preliminary Notice of 8 July 2013 (the "Preliminary Notice"). I am writing to set out the Secretary of State's decision as regards the application of a temporary scheme to those interests of the Iranian Oil Company UK Ltd ("IOC") listed below within the meaning of regulations 3 and 5 of the Hydrocarbons (Temporary Management Scheme) Regulations 2013 (the "Hydrocarbons Regulations"). The interests to which I refer are the interests of IOC in the following:
 - a. Licence P198, insofar as it relates to the Rhum Field (No. 347) lying to the east of 1 Degree 41 Minutes East;
 - b. the wells connected to the Rhum field, namely Well 3-29a/4, Well 3-29a/NF1 and Well 3-29a/SF1;
 - c. the flowlines and relief lines between these wells and the Rhum manifold and the pipelines to the Bruce platform, together with the associated chemical injection and hydraulic lines;
 - d. any control, production or safety equipment located at the Rhum field, along the lines mentioned in (c) from the Rhum field to the Bruce platform, or at the Bruce platform, including the control umbilical;
 - e. the contents of all lines in (c) and (d), including any petroleum;
 - f. any other pipeline or part of a pipeline in which IOC holds an interest, which enables petroleum from the Rhum field to be brought to shore or is related to the operation, production or safety of the Rhum field;

- g. entitlements to hydrocarbon products in the Frigg Pipeline System and the Forties Pipeline System and rights to make nominations in the Frigg or Forties systems;
- h. stocks and spares owned by the Rhum joint venture and held, either offshore or onshore, for any of the equipment in this list;
- i. technical studies, operating manuals, historical records and other intellectual property or confidential information developed for or by the Rhum joint venture;
- j. communications and IT software and hardware procured by or developed by the Rhum joint venture for use offshore and/or onshore; and
- k. all contractual rights in relation to the items above and in relation to the transport of hydrocarbons across the Bruce platform.

I refer to these collectively in this letter, for simplicity, as the “hydrocarbons interests”.

2. The Hydrocarbons Regulations allow the Secretary of State to apply a temporary scheme to the hydrocarbons interests of a listed person which holds a relevant licence where he is satisfied that this is necessary (i) to avoid or remediate environmental damage; or (ii) to prevent permanent destruction of the value of the relevant licence. IOC is a listed person for these purposes, having been listed in Annex IX of EU Regulation No. 267/2012 concerning restrictive measures against Iran as amended by No. 1263/2012 (the “EU Iran Sanctions Regulation”) in June 2013. IOC holds a relevant licence, in that it holds a licence granted under s2 of the Petroleum (Production) Act 1934 which was issued before IOC became a listed person, namely licence P198 issued to IOC and BP Exploration Operating Company Limited on 10 July 1972.
3. Following careful consideration of your representations, the Secretary of State remains satisfied that it is necessary to apply a temporary scheme to IOC’s hydrocarbons interests both (i) to avoid or remediate environmental damage, and in any event also to (ii) prevent permanent destruction of the value of the relevant licence. Accordingly, the Secretary of State has taken the decision to apply a temporary scheme to IOC’s hydrocarbons interests within the meaning of regulations 3 and 5 of the Hydrocarbons Regulations. The commencement date of the temporary scheme shall be the date of this Decision Notice and the temporary management period shall continue until the expiry of the licence on 16 March 2018, or until such earlier date as may be determined in accordance with regulation 26 of the Hydrocarbons Regulations.
4. The Secretary of State’s reasons for applying a temporary scheme are set out at Annex A. In your letter of 23 July 2013 in response to these reasons, you state at section (c) (“*Environmental damage / Permanent destruction of the value of the licence*”) that “IOC does not disagree that with the [Secretary of State’s] analysis that there is an increasing risk of environmental damage as time goes by without

production being resumed...[and] IOC does not disagree that there will be a permanent destruction of the value of the licence where there is no realistic prospect of commercial levels of production during the licence period". Nevertheless, you also set out in that letter your position with regards to certain of the aspects of the proposed temporary scheme, and in doing so made representations that such a scheme should not be applied. In deciding whether to apply a temporary scheme, these representations have been taken into account as set out below.

DECC responses to IOC representations in respect of Preliminary Notice of 8 July 2013

5. You state that you have been advised that the application of the temporary scheme could result in a deemed or indirect expropriation. The Hydrocarbons Regulations were introduced to ensure that, where a person listed in Annex IX to the EU Iran Sanctions Regulation has hydrocarbons interests by virtue of a petroleum licence, that a temporary scheme can be applied to avoid or remediate environmental damage or to prevent permanent destruction of the value of the restricted licence. As such, the Hydrocarbons Regulations are in the interests of both the public and the relevant licensee.
6. In applying the temporary scheme, our intention is to limit environmental risks and preserve the value of the licence; it is not to expropriate IOC's hydrocarbons interests. As set out below, the options for the Rhum field are limited, and the Secretary of State believes that the application of the scheme is proportionate to achieving these aims. Production at the Rhum field ceased in November 2010 in relation to sanctions against Iran, and IOC has not enjoyed the benefits of petroleum exploitation under the licence since that date. Therefore in practical terms the temporary scheme will not deprive IOC of the economic use of any of its rights under the licence. The scheme will not have any negative economic impact for IOC because, without the scheme, we do not foresee how production will resume prior to removal of current sanctions, which may or may not happen before the expiry of the licence on 16 March 2018. However, under the scheme the temporary manager may be able to restart production in order to limit environmental risks and preserve the value of the licence, and any monies from production will be paid into the temporary management account held by the Secretary of State on behalf of IOC in accordance with the Hydrocarbons Regulations. The temporary scheme will not affect ownership, as the licence, along with income from any production, will remain the property of IOC.
7. Further, the nature of the scheme is ephemeral: it will terminate at the latest on 16 March 2018 at the expiry of the licence and the application of the scheme will be periodically reviewed. The temporary scheme will be terminated earlier than that date if IOC ceases to be a listed person (within the meaning of the Hydrocarbons Regulations) or where the Secretary of State is satisfied that the scheme is no longer necessary to achieve the aims of avoiding or remediating environmental damage or preventing the permanent destruction of the value of the licence.

(a) Rationale for applying the scheme

8. You comment that no information has been provided on the form that a temporary scheme may take. The requirements that the Secretary of State must follow under a temporary scheme are set out in the Hydrocarbons Regulations, under which the Secretary of State can appoint agents to manage the interest in the petroleum licence. The Secretary of State and/or his agents will manage the interests of any licence in accordance with good management practice. Further details on the form that the temporary management scheme will take will be provided to you in due course.
9. As you point out in your letter, EU and US international sanctions against Iran provide a specific carve out for NICO's interest in the Shah Deniz field in Azerbaijan. You suggest that a similar carve out from international sanctions be implemented for the Rhum gas field in place of a proposed temporary management scheme. The Secretary of State believes that a carve out for Rhum would not be appropriate as (i) Article 43a of the EU regulations does not provide the UK with authorisation for a carve out; and (ii) the US sanctions against Iran do not provide the necessary carve out for Rhum.

(b) Scope of the scheme

10. You state that any temporary management scheme should be applied to the whole P198 licence and should include Block 15/13a (also known as the Hood discovery) **REDACTED** rather than only the Rhum field. In this instance, the Secretary of State does not believe it is appropriate to apply the temporary management scheme to the whole of the petroleum licence, as to include Block 15/13a **REDACTED** is not necessary (i) to avoid or remediate environmental damage, or (ii) to prevent permanent destruction of the value of the relevant licence.
11. As set out in Annex B, the Rhum field poses a potential environmental risk unless pressure at the Rhum reservoir can be reduced and the necessary remedial work undertaken using existing infrastructure, to make it stable. There are no significant safety concerns at Block 15/13a **REDACTED** that would suggest that environmental damage is likely to result if production is not initiated or resumed.
12. In October 2010, when BP ceased all commercial production activities at Rhum in response to concerns over international sanctions against Iran there had never been any commercial production by IOC at either Block 15/13a **REDACTED**. The existing infrastructure at block 15/13a currently consists of four wells; this includes one exploration well, 15/13-2, which is abandoned and three appraisal wells, of which 15/13A-4Z and 15/13a-7Z are abandoned and 15/13a-9 which is suspended. Unlike at Rhum, there are no production wells, associated infrastructure or pipeline at

15. It is noted that you do not disagree that (i) there is an increasing risk of environmental damage as time goes by without production being resumed; and (ii) there will be a permanent destruction of the value of the licence where there is no realistic prospect of commercial levels of production during the licence period.
16. It is also noted that you would welcome the resumption of production and that you believe that there are alternative means (i.e. carve out under international sanctions for Rhum) to achieve this.
17. As set out at paragraph 9 above in response to your section (a) *Rationale for applying the scheme*, the Secretary of State believes that a carve out in the Shah Deniz model cannot be achieved under EU legislation or international sanctions regimes and therefore the temporary management scheme model provides the most realistic prospect of restarting of production.

(b) Practical modalities of application of a temporary scheme

i. Temporary management activities

18. In your letter you state that regulation 8 of the Hydrocarbons Regulations provides that the Secretary of State may carry out temporary management activities and exercise any of the management powers to do so. You note that the Secretary of State may exercise the rights of a restricted person, must not dispose of that interest and you note that the Secretary of State may allow rights to continue to be exercised by IOC. It is therefore at the Secretary of State's discretion whether or not to take temporary management of an interest in a petroleum licence. Although it is correct that where a decision to take temporary management has been made, the interests in the petroleum licence cannot be disposed, it does not follow that temporary management can be awarded to IOC or that IOC can be consulted on management activities. As IOC is designated under EU sanctions against Iran and is subject to further international sanctions, if IOC is appointed as temporary manager or its views are taken into account in the day-to-day management of Rhum, there is a strong risk that this will be perceived as IOC having an active involvement in the management of the field. This is likely to result in third parties refusing to work at Rhum in case they be deemed in breach of international sanctions against Iran, which may make it impossible to carry out the works necessary at the field in order to render it safe. Appointing the Secretary of State or a third party as temporary manager of Rhum should result in third parties being willing to contract in order to bring Rhum back into production, and is therefore a viable means of avoiding or remediating environmental damage and of preventing the permanent destruction of the value of the licence.
19. As you may be aware, the Hydrocarbons Regulations set out details of information that must be provided to IOC and how often this will be provided under any temporary

24. You should note that the regulations set out that funds deposited in this account can be used to discharge liabilities of the restricted licence, a managed contract, a new contract and/or liabilities that the Secretary of State incurs in exercising management powers. Therefore, such payments may also be taken from the temporary management account to pay other liabilities.
25. Accordingly, the Secretary of State is satisfied that applying a temporary management scheme to the Rhum field is necessary to avoid or remediate environmental damage and to prevent the permanent destruction of the value of the licence.
26. Further details on the form of the temporary management scheme will be provided to IOC in due course.

Yours sincerely

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- j. REDACTED REDACTED REDACTED, notwithstanding the matters addressed in (b) and (c) there is still likely to be a permanent destruction of the value of the Rhum licence due to continued postponement of production. Re-starting production becomes less commercially viable the longer it is deferred and the total value available from production before the end of the licence is being continually eroded.
- k. The Secretary of State is satisfied, accordingly, that applying a temporary scheme is necessary to prevent permanent destruction of the licence value.