



Possible Alternatives to Improve the Efficiency of the Iranian Method of Buyback Transaction in Relation to the International Oil and Gas Contractual framework

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Registration Period: 01 October 2013 to 01 November 2017

Date of Submission: 15 February 2017

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Table of Abbreviation

APOC	Anglo-Persian Oil Company
AIOC	Renamed from the APOC to the Anglo-Iranian Oil Company in 1935
bl	Barrel
b/d	barrels per day
BOT	Build-Operate-Transfer
BOOT	build-own-operate-transfer
EIA	Energy Information Administration
FDI	Foreign Direct Investment
FIPPA	Foreign Investment Promotion and Protection Act
IEF	Iran Energy Focus
ILSA	Iran-Libya Sanctions Act
IOC	International Oil Company
IPC	Iranian Petroleum Contract
LAPFI	Law for the Attraction and Protection of Foreign Investment
NIOC	National Iranian Oil Company
NPCC	National Petroleum Construction Co
OIETAI	Organisation for Investment, Economic and Technical Assistance of Iran
OPEC	Organisation of Petroleum Exporting Countries
PSA	Production Sharing Agreement
WEC	World Energy Council
WTO	World Trade Organisation

Declaration

'Whilst registered as a candidate for the above degree, I have not been registered for any other research award. The results and conclusions embodied in this thesis are the work of the named candidate and have not been submitted for any other academic award'. This work consists of 78,788 words within 223 pages.

1. Statements of Aims

1.1 Acknowledgements

Fulfilling this PhD course has been the most challenging of my academic career and has been similar to a marathon attempt which required sufficient hard work to be carried out. I truly confess that I could not finish it without the support and co-operation of countless people during these three years. Firstly, I would like to give thanks to my first supervisor, Professor Maniruzzaman for his patience, kind advice, and secondly Mr. Joe Sekhon, my second supervisor, for supporting me to finish this research. I also have to express my appreciation to Dr. Khademan and Dr. Koosha for their constant motivation and encouragement during the most disheartening moments of this journey. Finally, my extensive thanks go out to everyone at the University of Portsmouth, particularly people in the School of Law and Business School, who assisted me through this venture. Obviously, I could not complete this process without the moral and practical aid of the respectful above mentioned people.

1.2 Abstract

Although the Iranian buyback contract has been widespread since 1989, this model has not been sufficiently and comprehensively analysed in academic works. Hence, this research offers a critical examination of the Iranian method of oil transactions, buyback, from distinctive perspectives in order to clarify the reasons behind the creation of the model, as well as applicable ways to modernise the mechanism. Initially, the work focuses on the development of the method of petroleum transactions in Iran from the early concessions,

the Nationalisation event, and the annulment of all agreements, due to the Revolution of 1979 in order to point out the reasons behind the adoption of such a harsh model by analysing the historical, political, geo-political, and legal concerns about Iranian buyback. Considering the Iranian buyback from such angles has crystallised that this harsh model is the outcome of the constant argument between the necessity of international investment and knowledge to develop the petroleum sector, from one side, and the weariness of International participation in oil industry, from the other side, due to the negative historical and political experience of Iranians towards foreign involvement in the oil sector. This research, by analysing the current practice of the model, has proven the fact that despite the long duration of exercising the Iranian buyback, it could not compete with other mechanisms in absorbing international investments which is the consequence of the unattractive features of the model, including the unnecessary preventive provisions. As a result, this study, based on the detailed examination of the model from the above-mentioned angles and comparative analysis of the other major international contractual mechanisms, firstly, highlights the necessity of improving the efficiency of the model, secondly, it selects the evolutionary rather than revolutionary approach towards the future of Iranian buyback, and finally offers applicable reforms to make the model more attractive. Consequently, this research concludes that although changes to the current Iranian contractual system will probably occur, a radical change to another method is a very remote possibility, as a result of the permissive historical, political and legal attitudes towards such radical changes. Thus, this study confirms the superiority of the evolutionary approach over revolutionary reform.

1.3 Aim and Objectives

The goal of this study is to offer a comprehensive understanding of the present Iranian contractual system used in petroleum transactions by critically examining the historical, political, geo-political and legal factors of Iranian buyback, in order to highlight the idea behind the creation of this model, and accordingly clarify the particular concerns of Iranian buyback. Following the detailed analysis of Iranian buyback and to answer the question of this research which is discovering the most applicable and effective way to increase the efficiency of the model, this study aims to propose the solution to make the model more attractive to absorb the foreign investment after removing the nuclear sanctions.

Accordingly, the main research question of this study is to determine the most effective and applicable approach among the evolutionary attitude and the radical shift towards the future of Iranian buyback, in other words, what approach can obtain a higher commercial efficiency for Iranians in petroleum deals with consideration of the current political and economic situation. In order to answer this question, this work has recognised the need to ask and answer other questions such as what are the reasons of introducing buyback, what are the main ideas behind buyback, its features and restrictions, and what approach can guarantee the effectiveness of proposed changes. To answer these questions, the legal analysis of the effective historical events in formation of the model, shortcomings of the model from both international and domestic sides, as well as comparative studies of the issue with other international common models of petroleum transactions will be provided to determine the most applicable and effective approach towards the future of the Iranian scheme of buyback with consideration for the historical, political, geo-political and legal concerns. The last objective in this study is analysing some case studies which have been carried out on the formation of the buyback mechanism with the aim of examining the applicability and the efficiency of the proposed reforms to the model when put in practice.

2. Literature Review

Basically, in the context of the Iranian buyback a precise and complete grasp of its mechanism, contractual foundation, and applicable views towards the model's future developments are crucial for the purpose of increasing the commercial efficiency of the method. Therefore, this work through providing a comprehensive grasp of Iranian buyback's legal mechanism will firstly explain its current situation for contractors, and also will enhance their level of capability to predict the prospect changes in Iran's oil sector. In addition, this research will serve the host state's interests via improving the model to make it more attractive in order to absorb international investments to Iran with no need to breach any historical, political, geopolitical and legal limitations existed in Iranian society and Iranian national laws. As a result, this study aims to fulfil these goals from a national and international perspective to ensure the interests of both parties in the contract for the aim of offering an adequately precise academic work.

2.1 Background and research context

The initial deals for the extraction of Iranian oil blocks begun in the 19th century. First agreements were fully dictated and controlled by foreign petroleum companies on the basis of concessionary deals¹ whereby the Iranian government's role in those projects and shares in the interests were considerably unimportant compared to the exclusive rights of the foreign companies in the deal². The public discontent towards the exploitative nature of the concessions resulted in the nationalization event of 1951 which changed the Iranian petroleum framework from concessionary deals to a contractual system such as PSA.³ The 1951 Petroleum Act acknowledged the wish to nationalisation of the natural resources by expressing that all activities regarding exploration, development and production have to be entirely operated by the NIOC to permanently preserve the ownership right on oil and gas reserves. Thus, this Act prohibited the government from engaging in any type of oil transaction that would permit the foreign sovereignty over natural assets including PSA⁴. However, following the removal of the nationalist government in 1953 via a British and American sponsored coup, the new government under the pressure of foreign powers began to implement the production sharing agreements model by ignoring the essence of the nationalisation event which resulted in public protests and impacted on the economic grievances of the people leading to the 1979 Islamic revolution. The Islamic government nullified all previous petroleum deals and on the basis of the new Constitution introduced the Iranian model of buyback whereby a foreign company supplies the required services and equipment for the discovery and development of the field, and will be compensated via selling the final product⁵. Therefore, the buyback agreement has become the key element of the Iranian oil industry which has been defended as an effective means to render an appropriate balance between national interests such as expanding exports and attracting foreign investment.⁶

2.2 Critical review of similar research studies

¹ Teimoury, 1., 'Asre Bikhbari ya Tarikhe Emtiyazat dar Iran' (History of concessions in Iran), Eghbal, Tehran, 1363(1984)p 25-32

² Fesharak, Fereidun, Development of Iranian Oil Industry, New York 1976 p.II-12

³ The chronological account of the nationalisation's unfolding is found in Benjamin Shwadran, 'The Anglo Iranian Oil Dispute 1948-1953', Middle Eastern Affairs, June-July, 1954, pp. 193-230.

⁴ NIOC, Brief History of Iran's Oil. p.3

⁵ Fashradgohar, N.'Seyri Dar Gharardadhaye Naftiye Iran', (A Survey On Iran's Oil Agreements).2002,Tehran.P.20-22

⁶ Makki, H., "Dr Mossadegh and his Historical Speeches", p. 46-52

Despite the long existence of the Iranian model of buyback, it has not been enough the topic of detailed research. Amid the limited studies on this subject the research carried out by Dr. Ule and Dr. Brexendorff⁷ is crucial, as this work provided the detailed critical analysis of Iranian buyback. However, a careful examination of the authors' examination of the current model's shortcomings exposes an obvious prejudice trend. While this research dealt with the government's relevant issues solely to highlight the foreign investor's objections, international oil companies' concerns are precisely discussed. As a result, hence foresee of the future development of the model necessitates the examination of government's complaints in addition to the international investors, the analysis provided by this author cannot enable the parties in buyback to predict the future changes of the model.⁸ On the contrary to the research of Ule and Brexendorff, this study for the purpose of ensuring the benefit of both parties in buyback via enabling them to predict the changes of model in future will equally consider the deficiencies of the model from the view of the national and international stakeholders to determine the accuracy of proposed reforms⁹.

Another weakness of the above mentioned research is the inappropriate balance between the examinations of the deficiency of the model and the legal issues. In other words, although this research precisely discussed the restrictions on Iranian Constitution and other relevant laws, it devoted inadequate attention to the process and formation of such laws¹⁰.

On the contrary, this work to respond its research question will point out the different obstacles against introduction of any new model including historical, political, geo-political and legal restrictions rather than simply suggesting the solution only on the basis of commercial purposes. Therefore, this study in order to create a real effect on the current legal environment of the Iranian buyback contracts will present an alternative according to the existing situation instead of proposing an inapplicable solution which has no influence from the practical point of view.

More importantly, an overview of this work demonstrates that the emphasis has been put on the immediate explanation and examination of the model rather than its origins and prospects. Although a comprehensive analysis of the current state of the buyback model are

⁷ Ule, C. and A. Brexendorff, Investing in the Oil and Gas Industry 2005: Mena.

⁸ Ule, C. and A. Brexendorff, Investing in the Oil and Gas Industry 2005: Mena

⁹ Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P20

¹⁰ *ibid*

provided in that work, especially in regards to foreign companies' concerns, it suffers from lack of consideration of the Iranian buyback from different angles, particularly historical, political and geo-political to accurately assess the present situation of the model, as well as predicting its future development, as the consideration of historical, political and geo-political events can determine both of these factors, and, crucially, can ensure the applicability of proposed solutions to increase the efficiency of the model. However, this study, unlike Ule's and Brexendorffs work, recognises the importance of providing such analysis as the basis for reaching its conclusions. Therefore, this work will be able to offer applicable and effective solutions for the future development of the model by understanding its historical, political and geo-political roots. Lack of such vital consideration led the Ule's and Brexendorffs research to propose an alternative system, merely based on commercial purposes which is not necessarily applicable within the current political, geo-political and legal environment of Iran, while, this study via providing the above-mentioned analysis will consider vital concerns such as negative historical experience of Iranians towards foreign involvement in the oil sector and the Constitutionally forbiddance of ownership of Iranian natural reserves by foreigners, which ensure the applicability of the proposed reforms by this work.

Unlike the Ule's and Brexendorffs study, which focus on the critical analysis of the current mechanism of buyback, the examination of several publications on the issue of Iranian oil agreements demonstrated that most of these works, despite concentrating on explaining of the background and current legislations concerning buyback agreements, suffer from providing sufficient analytical content, as well as failing to propose solutions for the future of the model. "Contract Laws"¹¹ and "A Survey on Iran's Oil Agreements"¹² are two examples of sole explanation of the related legislations and social facts summary with a lack of critical analysis¹³. Albeit above mentioned works are respected due to offering the related social data, these studies cannot, consequently, be useful in demonstrating the contemporary practice, as well as, Iranian buyback's deficiencies, because of their lack of analytical consideration of the model. Thus, these works are unable to propose the necessary reforms

¹¹ Rabiee, F, Hoghoogh-e-Gharardadha (Contract Laws) 1381, Tehran, Behnami

¹² Farshadgohar, N., A Survey on Iran's Oil Agreements. 2002, Economic Research Institute, Tehran

¹³ Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P 22

to improve the efficiency of the model. On the contrary, this study aims to offer solutions to make the Iranian buyback more attractive, and a detailed analysis of the current mechanism of the model including an examination of domestic and international factors, as well as a comparison with other methods used, in order to offer practical solutions to modernise the model and attract foreign investment after the removal of the nuclear related sanctions.

Unlike the Ule's and Brexendorffs study, the PhD thesis at Durham University, *A Critical Analysis of Iranian Buy-Back Transactions in the Context of International Petroleum Contractual Systems* 2008, conducted by Dr. Kakhki provided historical information, case studies, and proposed the solution for the future of the model. However, the work offered general historical information that in some points suffers from lack of critical analysis, moreover, the thesis simply described some cases, and did not explain the link between the theoretical analysis of the model and its practical review which accordingly cannot prove the applicability of proposed attitude regarding the future of Iranian buyback. The Dr. Khakhkii's work was concluded by suggesting the evolutionary approach which is a vague concept, and did not specifically addressed the applicable revisions with regard to defective provisions of the model. Nevertheless, this work instead of providing massive information on Iranian history and politics critically analyses only those historical and political fact that are crucially influenced on the Iranian present petroleum framework. This work examines cases in Iranian buyback to point out the problematic provisions and their effects in practice to create the link between the theoretical and practical study of the model for the purpose of great understanding of the model, moreover, this work attempted to utilize the cases to analyse their consequences with the current situation and needs of the model to ensure the applicability of proposed solutions. This work in final stage chose the evolutionary approach over the radical shift, however, it specifically suggests the applicable and effective reforms to defective provisions of Iranian buyback to convince the Iranian law makers to improve the model for the purpose of absorbing more foreign investment.

The recently published book, *Lex Petrolea and International Investment Law*, Nima Mersadi Tabari¹⁴, despite offering an extensive analysis of all methods of oil transactions in the Persian Gulf, suffers from a lack of comprehensive consideration of the Iranian buyback.

¹⁴ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*. 2016. Page 152-193

Although this book contains an examination of the Iranian buyback from historical, political and legal perspectives, it fails to provide any case studies in order to analyse the model from a practical view point. Thus, the work only focused on a substantive analysis of the model, whilst failed to offer a comprehensive examination of the model. Nevertheless, the distinguishing feature of this study is to provide an examination of case studies via considering the past projects of the Iranian oil fields which have been governed on the basis of Iranian buyback for the purpose of examining the applicability and efficiency of the proposed reforms by this work. Such analysis is vital from the point that this study focuses on offering an applicable and effective solutions instead of simply suggesting a hypothetical improvement which might not be applicable or effective in the current situation of the country. This book unlike the above mentioned thesis which provided the unnecessary general information on the sanctions instead of critically discussing the effect of them failed to offer crucial deliberation on international sanctions on Iranian oil sector¹⁵. Nevertheless, this work will examine the impacts of previous sanctions, as well as, analysing the effect of lifting the embargo in order to determine the needs to reach the ambitious plan of the country in boosting its production rate, thus, this work on the subject of Iranian model of buyback cannot be completed without critical consideration of these impacts which provides more clear image of the model from the both past and future perspective. Consequently, this work aims to comprehensively analyse the Iranian model of buyback from different angles to suggest practical reforms to modernise the model. Therefore, for the purpose of providing the full picture of the Iranian method of oil transactions, as well as ensuring the effectiveness of the proposed revisions, the historical, political, geo-political, legal and practical considerations of the model will be critically examined in the different chapters of this work.

2.3 Description of gaps in research literature

The successful negotiation of Iran with the five big powers plus Germany which resulted in the removal of nuclear sanctions increased the attention of issues related to Iran's economy and particularly the Iranian oil industry. Nevertheless, the Iranian buyback has not been comprehensively examined, despite being the key element of the Iranian oil sector, as this

¹⁵ ibid

method is not broadly practical among the other petroleum producers around the world. Therefore, the issue with the Iranian model of buyback is that it is becoming academically more valuable, due to the fact that Iran is actively attempting to obtain its previous position in the market after lifting of the sanctions and this will be examined in this research.

As the critical review of the similar researches¹⁶ in the last section demonstrated the existing gap in the studying of Iranian buyback is the lack of analytical consideration of the model from the historical and political views to show the origins of the model,¹⁷ offering the case studies, and proposing the applicable, effective and specific solutions to improve the model. Thus, this study will focus on providing such considerations to fill the gap via analysing the effective historical, political and geo-political events in the current practice, pervious cases and future development of the model, owing to the fact that without such considerations it is almost impossible to understand the core concept of the Iranian buyback, and more importantly to predict its future development with the aim of offering a more attractive version of the model. Moreover, offering such a critical examination will increase the effectiveness of the solutions that this study will propose in order to make the model more competitive. Noticeably, to avoid the descriptive feature of the history and politics, only relevant events that have legally influenced the Iranian model of buyback will be highlighted in order to grasp the framework of the model, point out the crucial concerns, and provide appropriate attention for critical factors within this research. In addition, such an analysis will be carried out in the light of both practical and academic literature to ensure the applicability of the proposed solutions. Accordingly, the present study fills this gap with the aim of modernising the model by offering a greater level of understanding of the Iranian buyback, which will serve the interests of the domestic party in petroleum deals via absorbing more foreign investments and subsequently obtaining more income, whilst also enables the foreign contractors to predict the future changes of the Iran's oil and gas legal framework. Both sides' understanding will be increased via enjoying a critical research rather than works with unnecessary general and irrelevant information on this subject. Thus, this study attempts to reach these goals by critically examining the relevant issues of buyback from different perspectives to demonstrate the origins of Iranian buyback and to

¹⁶ Ule, C. and A. Brexendorff, Investing in the Oil and Gas Industry 2005: Mena

¹⁷ Nima Mersadi Tabari, Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf. 2016.

predict the future development of the model as a unique tactic with regard to consideration of this topic. Noticeably, lack of this tactic in considering the Iranian buyback will lead to ambiguity in some features of buyback deals including the rationale behind such a model, the direction that the Iran's authorities' legislation will move, and the applicability and efficiency of any proposed reforms. Hence, this work aims to enhance the understanding of foreign investors regarding the model and increase their foreseeability of new reforms within the framework of the model after the removal of the nuclear sanctions.

2.4 Importance and contribution of the proposed research

Whilst the issue of Iranian buyback agreements seems to be a legal topic at the first glance, this study asserts that law and regulation cannot exist independently from history and politics.¹⁸ This relation in the case of Iranian buyback is even more significant, as many historical and political events have had a heavy influence on the adaption of the model, the foundation of the basis of the mechanism and the creation of its provisions. Therefore, understanding the core concept of Iranian buyback is impossible without considering such factors. Thus, this has demonstrated the importance of providing a brief examination of the relevant historical, political and geo-political events of the Iran's petroleum sector with the aim of identifying the root of Iranian buyback to grasp the issue from different angles. Moreover, social events on the Iranian model of buyback have had an undeniable effect on the future of the model by creating relevant disadvantages to the model which plays the main role in the selection of the future approach of the model¹⁹, as the effectiveness of potential reforms within the current framework of Iranian buyback is strongly dependent on those factors. Thus, a consideration of the core concept of the Iranian scheme of buyback and providing suggestions to improve it cannot be completed without an examination of these serious influences. Moreover, this study examines some previous buyback projects to show the adverse effects of unattractive provisions on the actual Iranian projects and to determine the efficiency of the reforms on the model in practice, such element will also enable the work to cover the model from both theoretical and practical views. Finally, this study in addition to drawing the general trend of the model, addresses the unattractive

¹⁸ Movahed, M.A., 'Nafta Ma va Masaele Hoghooghiye an', (Our Oil and its Related Legal Issues) Kharazmi, Tehran, 1353.p 67-74

¹⁹ Farshadgohar, N., A Survey on Iran's Oil Agreements. 2002, Economic Research Institute, Tehran

features of the model to specifically provide applicable and effective reforms for each of them.

Consequently, the above-mentioned analysis will enable this study to choose the applicable approach for improving the efficiency of the model via proposing the effective reforms that do not breach the historical and political barriers within Iranian society, which will result in a higher degree of certainty for the parties involved in buyback transactions, as they will be able to foresee the future development of buyback agreements.

3. Research Outline

Since the quality of a research's outcome undoubtedly correlates with the utilised process and the mechanism in the study, an accurate examination of these process and mechanisms is vital for the purpose of providing valid results²⁰. This is especially important in those studies which are based on the qualitative method, as the researcher is intended to produce "decision rule" through examining different ideas and information for the purpose of deciding which one optimally fits the facts at hand in the sense of efficiency and applicability²¹. This section will illuminate the procedure that such factor is adopted to the subject of Iranian model of buyback, and also to choose the most useful methodology, as there are various items which can effect on the social study's conclusion. Therefore, this work will use different research method in time of examining the various effective factors to maximize the quality of different carried out analysis in order to propose the valid outcome.

3.1 Research design and organisation

The international decision to remove the nuclear sanctions on the Iranian oil industry and the oil price fluctuation highlighted the issue of the Iranian stance on the oil market, as Iran intended to relocate its position amid other oil producing countries via absorbing more foreign investment. Therefore, to offer a detailed analysis of Iranian buyback for the aim of

²⁰ Robson, C. Real world research: a resource for social scientists and practitioner-researchers. 2002, .Blackwell Publishing, Oxford Pg.130

²¹ Sarantakos, Sotirios, 'Social Research', the MacMillan Press Ltd, London 1994. p. 6-7

undersetting all of its angles to propose the applicable reforms for the future of the model, this research is designed to critically discuss the historical, political, geo-political and legal considerations of buyback that have influenced the current practice of the model²². Such a comprehensive examination of the Iranian buyback from different perspectives which will be completed by scrutinising the case study via analysing some important carried out projects, will enable this work to offer suggestions to modernise the current model, so as to compete with other commonly used methods of oil transactions. For this purpose, this work consults various researches with different view, national and the international, and also refers to massive information from different sides, both the host state and IOCs, moreover it follows the news related to the Ministry of Oil, journals in both languages to ensure a completed examination of this complicated subject. Accordingly, this work which consists of five chapters will discuss the five areas related to the issue of Iranian buyback including the historical, political, geo-political, legal, critical and case study analysis. To carry out such a comprehensive study, the first chapter is concerned with an examination of the effective historical elements in shaping the present mechanism of buyback with particular focus on the concessionary deals as the first method of oil transactions in the pre-nationalisation era, to highlight the historical roots and concerns of the buyback. The second chapter considers the political and geo-political analysis of Iranian buyback via reference to the Nationalisation event, in order to examine the impact of such a vital event on the adoption of the buyback as the key element of the Iranian oil industry. The critical analysis of the existing mechanism of Iranian buyback from the legal aspect is addressed in the third chapter, which investigates the legal anatomy of the model in order to point out the shortcomings of the model as well as its legal limitations regarding any future change. The fourth chapter's emphasis is to review the criticisms of both international and domestic players, as well as a comparison of the Iranian model of buyback with other common mechanisms to highlight the deficiencies of the model and, more importantly, to employ the chosen approach in order to offer the applicable reforms to modernise the model with a consideration of historical, political, geo-political and legal concerns. The last chapter provides the dissection of Iranian buyback deals in practice by referring to some cases of contemporary Iranian oil transactions which allows the research to consider the buyback through the practical

²² Denzin, A. and Yvonna, S. *Collecting and interpreting qualitative materials* 2003, Sage Publishing, London

approach to examine the effectiveness of the chosen approach by this work, and accordingly to foresee the future development of the Iranian buyback agreements. Finally, the conclusion of the whole work will be drawn through reviewing the carried out analysis in the previous chapters for the purpose of answering the question of this research, which is to suggest the most applicable solution to make the Iranian model of buyback more attractive.

3.2 Confidentiality and ethics

The consideration of an ethical approval has been discussed with the 'Ethical Approval' Committee of the University of Portsmouth, and it was confirmed on 19th October 2015 that it was not required prior to, or as a part of, final submission. Therefore, no attempts have been made to collect any primary data without first obtaining a favourable ethical approval from the faculty ethics committee.

3.3 Methods and choice of analysis

Providing a valid conclusion is absolutely based on the process and the procedure that were applied in the research highlighting the importance of the examination of these procedural elements for the purpose of obtaining convincing conclusions. While it is unfeasible to list the different research methods in the structure of this research, this is vital to explain the general kinds of this study's methodologies²³.

Generally, social issues are not mutually exclusive, in other words, the standard research needs a limitless method of study to ensure that the work is not confined to a rigid hypotheses or requirements which would restrict the scope of the research²⁴. Following this guideline, this research is not aimed to reach a particular outcome via persuading the pre-designed data, nevertheless, it will propose the outcome that will be reached through the analysis of all relevant data. Moreover, this guideline clarifies that reaching a comprehensive grasp of the issue is not completed, unless, a precise analysis of the concept has been carried out from different angles. Therefore, this point is implemented in this

²³ Robson, C. Real world research: a resource for social scientists and practitioner-researchers. 2002, .Blackwell Publishing, Oxford Pg.135

²⁴ Sarantakos, Sotirios, 'Social Research', the MacMillan Press Ltd, London 1994. p. 7-9

study by the presence of only relevant events on the history, politics and geo-politics background of buyback. In addition, the limitless feature of the method of study necessitates the concept of interactions. This concept specifies that the target of this work is to clarify the foundation of the model, and subsequently to foresee its future foundation. Therefore, this research's focus, via following the guideline, is not only the historic or even the present form of the buyback, but also predicting the future development of the matter in question with an analysis of the historical and political events' influences on buyback²⁵ and to offer solutions to improve the efficiency of the model.

Social studies utilizes various methodologies in a single research, as social issues generally have various aspects which require utilising different types of research methods, in order to ensure that every element has been investigated by its most appropriate research method. Therefore, it is possible to use different research methods in a study including descriptive, analytical and theory creating method. However, it is notable that every research method in this study is used for a certain part of the paper and issue which, obviously, is not practical in other parts of the paper and issues. This mixed research method, quantitative, qualitative, analytical, and theory creating system is being called by Bryman as 'the mixed method approach'²⁶. Nevertheless, most of this work enjoys the analytical system even in the chapters of historical and political analysis which are descriptive in nature, therefore, the major research method is interpretative to prevent the common mistake of research methods which put the main emphasis on the descriptive method which plays as parallel when the study reaches the analytical part, as the sections of historical and political analysis are strongly linked and closely interconnected to the analytical examination of the buyback in other chapters. Subsequently, although this research acknowledges the priority of the mixed methods research, the main methodology in this work is qualitative research which refers to interpretive, comparative and an analytical method of research.

As alluded to above, the research will place emphasis on qualitative methods which will be conducted mainly through a documentary reviews and critical study of the Iranian buyback contracts. Applying a qualitative method in social researches has some advantages

²⁵ Denzin, A. and Yvonna, S. *Collecting and interpreting qualitative materials* 2003, Sage Publishing, London

²⁶ Bryman, A. *Social research methods* Oxford University Press, 2004 pg. 48

compared to the quantitative system such as research's openness and linking to reality.²⁷ Accordingly, the issue in question will be abided to the qualitative method, thus, it will take into account the necessity of the recognition of buyback agreements in both different stage of current situation, as well as those evidences that are guiding to the future position of the scheme such as historical, political and geo-political influences on the final product. Overall, in this study all essential elements (in both English and Persian) are in an effort to analyse the various theories to create a "decision rule"²⁸ by fulfilling the guidelines of the qualitative research method to examine all the effective historical, political and geo-political events in order to answer the question of this research.

3.4 Process of attaining conclusion

Following the consideration of the method of research chosen for the present study, it seems vital to discuss the mechanism that guides this research in proposing its outcome. In fact, the method of research is being employed to provide a definitive conclusion to the initial theoretical question of the work, however, the conclusion that this study arrived at may vary depending on the precise structure of the research method. Moreover, since the subject matter of this study is controversial, and accordingly can cause a serious disagreement between various parties, using a mechanism that demonstrates such contrast seems essential. As a result, this research utilizes the mechanism of examining of both parties' complaints, as well as a side-by-side analysis of various contractual issues to ensure both sides' concerns in the time of proposing the conclusion. In addition, showing the core concept of the issue that can guarantee objectivity, due to the analysis of two parties of the topic will be provided in this study, as this analysis offers improvements of the provisions if this seems vital to respond a party's compliant.

This study, via examining relevant information, will follow an approach that is consistent with the emphasis on contextual analysis which manifested itself in the decision to offer the chapters on the historical and political considerations of the model as the vital preliminary aspects which offers the conceptual analysis of present situation and future development of the model in the remainder of the work. Moreover, the inclusion of an initial and extensive

²⁷ Sarantakos, Sotirios, 'Social Research', the MacMillan Press Ltd, London 1994. p. 6-7

²⁸ Dooley, D. 'Social Research Methods', Prentice-Hall Inc. Englewood CliftS, 1984,USA, pg. 9/ A decision rule is a procedure that the researcher uses to decide whether to accept or reject the null hypothesis which is about applying the radical shift or evolutionary approach towards the future of Iranian buyback.

analysis of historical and political considerations of buyback prevents this work to solely concentrate on examining current situation of the model and its future development. The rest of the work is designed in a way to process the relevant general information prior to detailed examination in order to provide related facts²⁹ before beginning the contractual analysis. In addition, this study by ordering a logical structure in placing the related chapters and critical analysing and conducting a comparative examination of the model with other commonly used methods prior to employing the chosen approach regarding the future tendency of the model, attempts to point out the flaws of the current mechanism and more importantly, specifically provides the applicable reforms for them. Therefore, although this work does not focus on the chronological sequence, it seems logically appropriate to begin the work with a review of historical and political considerations of the issue before the study of flaws and possible alternatives for the future development of the model. Following such an analysis, the case study chapter for the aim of demonstrating the impact of historical, political, geo-political and legal items on the practice of Iranian model of buyback will provide cases of the provisions which are applied in past buyback projects to examine the efficiency of the proposed reforms. Finally, the conclusion of this work in the form of a short section will review the entire work for the purpose of offering the compromising solution to determine the future development of the Iranian buyback to provide the answer to the question of this research which is 'what is the most effective and applicable solution amongst the evolutionary attitude and radical shift for Iranian buyback'.

3.5 Expected Outcomes

This research examines the Iranian model of buyback from various outlooks, historical, political, geo-political, and legal, to determine the matter of whether an amendment of its terms or a superseded system would be more appropriate with regard to the different existing prohibitions.³⁰ Moreover, this work conducts the accurate consideration of the specific terms and conditions of buyback contracts from both domestic and international perspectives along with the comparison of the model with other mechanisms to analyse the

²⁹ Bryman, A. Social research methods Oxford University Press, 2004 pg. 50

³⁰ Rabiee, F., 'Hoghoogh-e-Gharardadha' (Contract Law), Tehran, 1381.p 43-52

current practice of Iranian buyback with a focus on its flaws and criticisms. In addition, a review of various oil field projects can define the effect of the perceived deficiencies of the model in reality and more importantly will show the possible influence of any reforms on the model. The outcome of such an analysis demonstrates that the method of a buyback agreement in Iran is based on the unnecessary preventive provisions which stem from the nationally supportive nature of the model rather than owing to the system itself³¹. Hence, the low efficiency of the model in consequence of such a feature, removal of nuclear embargo and Iranian ambitious plan to boost the production rate to develop its economy, highlights the necessity of offering more balanced version of the Iranian buyback³². Thus, the Iranian government is actively attempting to offer more attractive contracts on the basis of the buyback. Accordingly, this study is based on facts and findings and draws a conclusion which leads to the application of the evolutionary rather than the revolutionary reform of the current model of the buyback with no rejection of the existing legal framework, neither breaches any historical, political, geo-political, and legal barrier within the present structure. This is because of the fact that any radical change within the model will confront such barriers which would create a considerably high expense for the country to adopt the new mechanism, as it requires a fundamental change in the entire system, therefore, no justification will remain to shift to another model particularly with a consideration of Iran's time limit to return to the market. Moreover, despite the low efficiency of the model, it still has obtained some achievements during many years of its practice which demonstrates it has a capacity to be revised. Furthermore, the precedent in Iran in the introduction of four generations of buyback proves the applicability of the evolutionary approach, even though this study confirms the need to develop the scope of such reforms. Consequently, this work, in its conclusion will summarise the various areas that was analysed in different chapters of this study and highlights the fact that applying an evolutionary reform will make the model more attractive by addressing the related issues to national, as well as, international party, and also integrating the useful elements of other models without crossing the line drawn by historical, political and legal considerations.

³¹ Estelami, H. 'A Study of Iran's Responses to US Economic Sanctions' Middle East Review of International Affairs (MERIA) Journal, Volume 3, No.3, Sep. 1999

³² Mobaser, D., 'Kalbodshekafi Sarmayegozarihaye Sanate Naft, Beyeh Moteghabel, (Autopsy of the Oil Contract "Buy-Back")', collection of articles by et al, 2000, pg. 21

Chapter 1: Examination of effective historical concerns on Iranian buyback: Iranian Establishment of the petroleum contractual system Prior to Nationalisation Event

1.1 Introduction: The influence of economic mustiness of Iran and its challenge with dominant powers on formation of concessionary deals

The country of Iran which was economically a progressive country historically has lost its strong position since the 19th century³³. This is because Iran's political authorities refused to modernise the country to decrease the economic gap between Iran and other developed countries. Thus, Iran was not able to economically compete with the developed European countries. In fact, the leadership of the country was reluctant to carry out any modification that possibly could lead to change the political regime, thus, there was a lack of any attempt to modernise the country in the sense of economy and trade which resulted in the economic weakness of Iran in the 19th century³⁴. On the other hand, European economies, Britain and Russia, were in the middle of the Industrial Revolution which created a high level of competition between them, therefore, they needed more natural resources to develop their economy and win the competition³⁵. As a result, Iran as a country with a huge capacity of natural resources, as well as, a strategic position faced the challenge with the two great powers, Britain and Russia, in the early 19th century, as these two dominant countries took the advantages of their political and economic power to utilise Iran for boosting their own economy, as well as expanding their geo-political influence in Asia, mostly in India and China. In other words, Iran seemed to be a backyard for foreign companies coming from these great powers to actively compete with each other with the support of their governments, in employing the Iranian natural reserves via obtaining economic benefit privileges³⁶ in the form of concessions, as well as developing their geo-political influence in a strategic zone in the world. Therefore, Iran as a result of its oil and gas fields and its strategic position was crucially significant from the economic and the geo-political point of

³³ The Circle of Ancient Iranian Studies "Kanoon-Pazhooheshhay-Iran-Bastan ", affiliated with the School of Oriental and African Studies. Entry on Turkmanchai Treaty [<http://www-cais-soas.com/CAIS/Iran/torkmanchai.htm>]

³⁴ Muhlberger, op.cit., p.2

³⁵ F. KazemNia, "Story of Oil" [in Farsi], <<http://www.tebyan.net/index.aspx?pid=10893>> (January 18, 2010).

³⁶ Muhiberger:Steve', -History of Islamic civilization, Nipissing University 1999 [<http://www.nipissingu.ca/departement/history/MUHLBERGER/2805/LEADUP.HTM>] pg. 1

view of big powers, Britain and Russia, which resulted in their taking advantage of the economic weakness of the country and putting pressure on Iran to establish concessionary deals with unbalanced terms and an exploitative nature that created a negative historical experience towards foreign involvement in the oil sector and denied the national interest of Iran in petroleum deals. Accordingly, the economic weakness of Iran in the 19th century, because of poor economic strategy of Iranian authorities provided the basis for the special advantage of the big powers to challenge the country by extending their pressure on Iran to exploit the country to develop their economic and geo-political influence in the world to overcome their rivals and win the competition. The effects of this competition for Iran was the breaking down of the national economy, limiting the sovereignty of the Iranian state and increasing the poverty of the Iranian people³⁷, by granting unbalanced and exploitative concessions to foreign companies which denied the national interest of Iran in oil and gas deals. As will be discussed in this chapter the effects of the involvement of foreigners in the Iranian oil sector created the negative experience towards foreign participation in the Iranian oil industry and led to an ignoring of the national interest in petroleum deals which resulted in the introduction of the Iranian buyback with its extreme provisions. As a result, this chapter, which has been divided into two sub-chapters, aims to demonstrate the influence of historical events on the formation of the current model of buyback to show the reasons for the adoption of such a harsh model, and more importantly to highlight the historical concerns regarding the issue of buyback to ensure the applicability of reforms that will be proposed in the following chapters on the basis of the evolutionary approach to make the model more attractive after the removal of the nuclear sanctions without any clash with the historical, political and legal barriers in the current situation of Iran³⁸. Therefore, the first sub-chapter will examine the overview of the concessionary deals with some examples to illustrate the process of the creation of the negative attitude among Iranians towards foreign participation in the oil sector as the main historical reason which led to the adoption of the buyback, and the second sub-chapter is designed to analyse the influence of foreign pressure to establish the unbalanced concessions which resulted in

³⁷ Farshadgohar, N., "A survey on Iran's Oil Agreements". 2002, Tehran} P, 20-22

³⁸ Elwell-Sutton, L.P, *Persian Oil*. 1976 ed. 1955, London: Lawrence and Wishart Ltd, p. 10

ignoring the national interest of Iran in the petroleum deals which led to the nationally supportive features of the present buyback.

Carrying out such an analysis is vital to understanding the reasons for the introduction of this particular model; moreover, proposing the applicable alternative for the future of Iranian buyback to increase its efficiency is not possible without a careful consideration of the historical roots for the formation of the model. This is because of the fact that this study is aimed at providing solutions that are applicable in the current situation of Iran after the removal of the nuclear sanctions which highlights the essence of considering the historical concerns of the model. More importantly, offering such a consideration distinguishes this study over other studies regarding the topic of Iranian buyback, as the lack of the historical analysis in examining the issue of Iranian buyback is a significant gap that makes the examination incomplete, as the issue in question has crucial historical roots and also influences the current and the future mechanism of the Iranian method of buyback.

1.2 Overview of concessionary deals: Creation of negative historical experience of Iranians towards foreign involvement in oil industry

The 19th century's form of Iranian petroleum deals is an unpleasant memory in the history of Iranian petroleum agreements³⁹. In other words, Iran was under financial pressure and the government had to obtain income through awarding exclusive rights to foreigners to enjoy exploitation of Iranian energy reserves which was defined as concessionary deals. Nevertheless, the unfair terms of these concessions in favour of foreign companies, which resulted in the frustrating of the domestic party's rights to enter into any further commercial interaction, subsequently aggravated the feelings of resentment between Iranians towards foreigners. Accordingly, such concessions with unfair provisions and their exploitative nature which were granted as a result of the foreign force via Powerful countries (Britain and Russia) in consequence of Iran's weak policy and economy played the main role in the creation of public discontent towards foreigners. Moreover, as will be discussed in the next chapter, granting the unbalanced concessions led to the formation of

³⁹ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 152

the nationalisation movement which nationalised Iranian natural resources and introduced the Iranian model of buyback with unfriendly provisions for investors and a nationally protective framework. As a result, this sub-chapter will analyse some concessions granted to foreigners in four sections in order to firstly show the mechanism of the concessionary deals in the Iranian oil industry, secondly, to demonstrate the effect of such concessions on the introduction of buyback, and finally to provide the necessary facts to employ in the following chapters with the aim of offering applicable reforms which are not in contrary with the historical elements of Iran to make the buyback more attractive.

a) The Reuter concession: The most "extraordinary surrender"⁴⁰ concession

The Reuter concession is the first petroleum agreement in the Middle East which was signed on 25 July 1872 amid the English businessman, Reuter, and Iranian King Nasir al-Din Shah. This concession, which was based on the proposal of cash for a concession is highlighted because of the extensive scope of exploitation of Iranian natural resources that was granted to the foreign party⁴¹. Thus, it is identified as the most extraordinary surrender. In fact, while the Reuter concession initially monopolized of the building of train and bus stations, it extended to the enjoy jungles and all uncultured farms. In fact, based on the provisions of this concession, Reuter's agency was granted the exclusive right over all Iran's mineral resources for long duration, with exclusion of expensive rock such as gold and silver⁴². Therefore, as a result of the extensive granted rights to the company, Lord Curzon⁴³ pointed out that the deal as absolutely comprehensive and "extraordinary surrender"⁴⁴ deal granted from Iran in favour of international benefits. Moreover, Lord asserted that "the concession is an absolute profitable deal that a country is able to award to foreigners through leaving of ownership of the natural resources."⁴⁵ The concession was terminated after 15 months, owing to great internal public pressure and Russian objections, even though it left a lasting negative experience for Iranians to associate the contract with a foreign party and also an alarm for the peril of foreign exploitation of Iran's national resources. Accordingly, although the Reuter concession was prematurely terminated, it demonstrated the main elements of

⁴⁰ Curzon, George N., *Persia and Persian Question*, London 1892, Vol 1 p. 480

⁴¹ El well-Sutton, L.P., *Persian Oil* 1976 ed. 1955, London: Lawrence and Wishart Ltd, p. 11

⁴² *ibid*

⁴³ George Curzon, the eldest son of Baron Curzon, was born on 11th January .He was appointed foreign secretary in 1919 and died on 20th March 1925.

⁴⁴ Curzon, George N., *Persia and Persian Question*, London 1892, Vol 1 p. 480

⁴⁵ Rabiee, F., *op.cit.*, p.20

the concessions, including the unfair and unbalanced terms of concession in the form of ownership of almost all Iranian natural resources in exchange for cash, and more importantly the extremely long duration of the deal, in this case seventy years, which highlighted the exploitative nature of the concessions⁴⁶. Such features of the concessions resulted in the current provision of buyback regarding short contracts and a separation of granting the discovery rights from the development rights that will be considered by this work when offering the reforms on the basis of the evolutionary approach in order to ensure the effectiveness of the proposed revisions.

b) The Imperial bank of Persia concession: Modified version of the Reuter concession

Subsequent to the premature termination of the Reuter concession, the company had struggled for almost two decades to obtain another concessionary provision in order to enter the Iranian market. Accordingly, after a long negotiation between the parties to modify some of the terms and conditions of the Reuter Concession, this led to the foundation of the 'Imperial Bank of Persia'⁴⁷ in order to reactivate the Reuter Concession in a new form. The new agreement obliged the Reuter Company to make a payment of a million Francs at an annual interest of 16%, as a loan to the Iranian Government. In return, the Iranian Government would provide the necessary starting capital for the establishment of the Imperial Bank. Noticeably, the concessionary provision was included in fourteen articles and provided a monopoly over minting banknotes and more importantly an exclusive right under Article 11 to exploit all Iranian minerals, including oil.

Article 11 of the concession states that:

Minerals

“As the Imperial Bank declares that they are ready to exploit all of the natural minerals, everywhere in the country, immediately, the government will give a concession to this bank to exploit all minerals, including iron, copper, lead, coal, oil, and manganese; provided that the government had not granted this to others in the past. If the bank does not start to

⁴⁶ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*, (2016) p 154

⁴⁷ 54 Specifically Article 20 of the Concession, which dealt with the establishment of a bank, with the hope of preventing the dissolution of the Reuter Company.

exploit any particular resources within ten years from the time that the bank was established, the government would assume that they had abandoned their title to those minerals”⁴⁸.

Consequently, despite the long negotiations, after more than seventeen years, the Reuter Company could still compromise with the Iranian Government and resolve all conflicts over the concession in order to acquire new opportunities pertaining to the exploitation of Iran’s oil and gas resources⁴⁹. Therefore, although the scope of the new agreement was more limited compared to the original version, the Reuter Concession, it still contains features of an exploitative nature through its long duration and unbalanced considerations. Accordingly, this concession was the second deal in Iran’s oil history that formed the basis of the current Iranian buyback such as the nationally protective element of the present model which created many unnecessary restrictive provisions that limit the attractiveness of Iranian buyback.

c) The D’Arcy Concession: Inequality of parties’ considerations

The D’Arcy concession which was granted by the Iranian king, Mozaffar ad-Din Shah, to the British businessman William D’Arcy in 1901 resulting in the Middle East’s first huge oil field discovery. The concession required the foreign party to provide the value of £40,000 stocks to the King in exchange for obtaining the right to explore and develop vast areas in southwest Iran which led to the discovery of a huge oil reserve in the Masjid Soleiman region. In consequence of the high level of oil discovery in the field, the Anglo-Persian Oil Company was established, 1908, later becoming Britain Petroleum Company (BP) in 1954 to continue the operation of the Masjid Soleiman project⁵⁰. Thus, D’Arcy’s Company which owned all of the concession rights transferred them to the new APOC. The main elements of the D’Arcy concession, which point out its contradiction with the Iranian national interest by applying an unbalanced consideration of the Parties’ interests, can be found in the first Article which states that: “The Government of His Imperial Majesty the Shah grants to the concessionaire by these presents a special and exclusive privilege to search for, obtain, exploit, develop, render suitable for trade, Carry away and sell natural gas, petroleum,

⁴⁸ Zoghi, op.cit., p.59

⁴⁹ Farshadgozar, op.cit., p.39

⁵⁰NIOC, Brief History of Iran's Oil. p.3

asphalt and ozokerite⁵¹ throughout the whole extent of the Persian Empire for a term of sixty years as from the date of the signing”⁵².

As it has been mentioned, this article granted the exclusive right⁵³ to the foreign party to carry out a number of oil related activities such as exploration, production and export over a vast area of Iran’s southwest for the long length of sixty years in exchange for £50,000 worth of fully-paid shares⁵⁴ which resulted in to a vital limit for Iran over its sovereignty of natural resources. This article, in fact, highlights the inequality in the parties’ considerations, as whilst the foreign party could enjoy unlimited level of operations over the vast area for a period of 60 years, the Iranian side had limited rights, namely £50,000 in cash. Accordingly, the harshness of this concession’ provisions was similar to the Reuter Concession and led to the formation of some of the current mechanisms of buyback especially the terms regarding the granting of separate exploration and development rights, the NIOCs’ discretionary power to grant the development rights to every contractor that successfully finished the discovery stage, and the relatively short period of the contract. Therefore, this study, in dealing with the above-mentioned restrictive provisions for the purpose of proposing the proposed reforms will consider the cause of these provisions, and more importantly the special historical concerns regarding them.

d) The 1933 concession: The first attempt to balance the terms of the concession

Following the exploitative nature of the D’Arcy Concession, the Iranian government proposed some revisions in the concession in order to achieve more revenues from the deal by rendering a better balance between the parties’ interests. To prove the necessity of the modifications in the D’Arcy Concession the Iranian government required the company to provide a licensed expert to analyse the fiscal situation of AIPC and Iranian authority, due to the fact that the Company had breached important terms of the concession several times such as the secret deal between the Company and the British Admiralty to supply the fuel at a lower price. However, the Company refused to employ a chartered accountant, and subsequently denied any need to revise the concession. Therefore, the Iranian government

⁵¹A naturally occurring mineral wax and paraffin

⁵² *ibid.*, p. 63

⁵³ Despite being qualified to exclude several provinces in a subsequent Article

⁵⁴ *ibid.* p.33-34

concluded that the Iranian rights were being undermined by the application of the provisions of the D'Arcy Concession and proposed a new set of negotiations to establish a new deal⁵⁵. In the new set of negotiations the Iranian government proposed an arrangement containing possession of 20% of the Corporation's stocks, as well as owning 75% of the original concession area and also achieving acknowledgement of the host country's contractual privilege in entire activities of Corporation, and also in the case of the termination of concessional provision. However, the negotiations, as a result of the British governments' pressure by sending several warships to the Persian Gulf, was not successful and subsequently the case passed to the Security Council which led to the granting of another concession under the effect of deceit and duress, on the basis of all the previous exploitative and unbalanced terms and conditions. This is because the new concession was similar to the previous deals and awarded the Company the special privilege inside the zone defined via the deal to discover oil reserves and produce or treat in any other way which was beneficial in the sense of the petroleum trade for the period of seventy years⁵⁶. Moreover, the Company was allowed to conduct numerous logistical operations such as purchasing all necessary imports to satisfy the vital requests the workers with no need of obtain any licence or pay any custom duty⁵⁷. Therefore, under the new deal the foreign company enjoyed the exclusive right of a various range of activities including discovery, production and export over a vast area of Iran for a long period. Furthermore, this concession ignored the rights of Iran to require a licence and the payment of custom duties for the import of facilities to the country which led to a reduction in the revenue of the government⁵⁸. Accordingly, despite all the efforts of the Iranian government to grant a concession with more balanced terms to obtain more profits, above mentioned deal was concluded because of pressure in favour of British Governments' interests on the exploitative nature of the old concessions. Therefore, the Iranian government's attempts failed. The influence of this exploitative nature of the concessions on the current Iranian buyback was the formation of a model based on hostility against foreign contractors and the

⁵⁵ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 157

⁵⁶ Alavi op.cit., p 58

⁵⁷ *ibid.*,

⁵⁸ NIOC, *Brief History of Iran's Oil*. p.3

naturally supportive nature of the model for the government, which created an unfriendly environment for foreign investors in the Iranian oil industry⁵⁹.

Overall, analysing the four concessions in Iran's oil history in this section shows that the foreign companies, by using their government's support, took advantage of the lack of technology and investment in the Iranian oil sector as well as Iran's economic difficulties in order to establish agreements with unbalanced provisions and an exploitative nature for a long period of time. Such concessions, with the above-mentioned elements, created a negative attitude in Iran towards international participation in energy sector which led to nationalisation event in Iranian history of oil that will be examined in the second chapter of this work, and subsequently resulted in the introduction of the buyback model as the main method of oil transactions in Iran. Furthermore, the influence of the concessions in the formation of some of the provisions of the current buyback has been discussed in this section and it has been demonstrated that the applicability of reforms that this study will propose according to the evolutionary approach in the third and the fourth chapter of this study to make the model more attractive is dependent on considering such a historical analysis. Following the consideration of the concessions and their impact on the current mechanism of buyback by creating a negative attitude among Iranians towards the involvement of foreigners in the Iranian oil industry, the next sub-chapter will examine the effect of foreign pressure on the formation of the present form of buyback to highlight, and more importantly, consider the historical concerns when offering effective revisions to increase the efficiency of the model.

1.3 The influence of the foreign pressure on petroleum deals: Ignoring the Iranian national interest in oil and gas agreements

As has been demonstrated in the last sub-chapter, the exploitative nature of concessions resulting from the unbalanced terms of the deals created public discontent regarding foreign participation in the Iranian oil sector. The reason that the foreign parties imposed such unfair concessions on Iran was Iran's valuable resources that they intended to obtain with a greater share of profit than Iran as the host country. However, the occurrence of the two great World-Wars increased the value of Iran for western countries, due to its

⁵⁹ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 156

geographical position located amid Russia and Turkey⁶⁰, which resulted in the aim of employing Iran and its natural resources by the great powers in order to win the War. As a result, the period between the two great World-Wars, and more importantly the Second World War significantly influenced current Iranian petroleum framework by underestimating the national Iranian interest which led to the provisions of the present buyback. Therefore, this sub-chapter in three sections will concern the influence of significant historical events during the above-mentioned time period on the formation of the existing Iranian buyback, to highlight the reasons for introducing the current mechanism from a historical angle, and grasp the special historical concerns in Iranian society to ensure that the proposed reforms will not breach these historical concerns.

a) Development of the Northern Provinces oil fields: Iran's attempt to obtain more balanced deal by changing its concessionary party

Following Iran's failure to change the provisions of D'Arcy deal to acquire more beneficial contract with the British Company, as has been demonstrated in the last sub-chapter, the Iranian government under the influence of the Russian government decided to grant a concession to develop the oil fields located in the Northern Provinces of Iran. This concession, which was named the Khoshtaria concession⁶¹, was granted to a Georgian businessman in order to restrict the influence of the APOC in Iran's energy sector. In fact, as the Iranian government was disappointed in not being able to acquire a more balanced deal with the British company, it decided to shift to the Russian side to chase its goal to establish more fair petroleum deal. However, foreign pressure from the British side forced the Iranian government to invalidate⁶² the Khoshtaria concession, and accordingly the Anglo-Persian Oil Company took this opportunity to purchase the rights granted under the Khoshtaria concession, which was similar to the D'Arcy Concession on March 1922 in return of 90,000 English Pounds. Subsequently, NPOC was established as a branch of Anglo Persian Oil Company, with an initial capital of £3m and supervised by APOC directors to carry out the concession. Therefore, the attempts of the Iranian government to shift its concessionary party from Britain to Russia was not successful and, more importantly, Iran could not reach

⁶⁰ Malek, M., History of Iran, Iran Chamber Society. p. 10

⁶¹ Ghaffari, op.cit., p.45 "The full text of the concessions can be found in Foreign Relations, 1920, Vol. III, pp351-352"

⁶² ibid, p.45.

its aim to increase its revenue by enjoying a more balanced deal. As a result, the Iranian government began to negotiate with American oil companies, particularly the Standard Oil Company of New Jersey⁶³ for the purpose of developing the northern areas of Iran based on a satisfactory agreement⁶⁴. However, the main concern of the Standard Oil Company was the economic and financial influence of Britain on the Iranian oil industry, as the Anglo-Persian Company had obtained exclusive rights through various concessions to develop vast areas of northern and southern parts of Iran. Nevertheless, the negotiations between the Iranian government and the Standard Oil Company reached an agreement by the end of 1921, to replace⁶⁵ AOPC with the Standard Oil Company in the Khoshtaria concession in return of financial credit from America which could permit Iran's authority to stand out against Britain's and Russians' pressures⁶⁶. In response to this agreement Britain intended to resist the Standard Oil Company to nullify the deal by restricting the process of exporting oil from Iran, due to the fact that the Anglo-Persian Oil Company had the exclusive privilege⁶⁷ of delivering oil throughout Iran, which forced the Standard Oil Company to cooperate with APOC in order to export its products to the global oil markets. Therefore, following the strategy to avoid conflicts amid corporations, the Standard Oil Company annulled the agreement under pressure from the British company which resulted again in the failure of the Iranian government to change its concessionaire party to obtain a better petroleum deal. Accordingly, as a result of the nullification of this concession under the pressure of a foreign country, and after again failing to achieve a more balanced deal, the Iranian Parliament approved the granting of a concession to another giant American company, Sinclair Consolidated Oil Corporation, based on a fulfilment of two requirements. The first condition was an assurance of a \$10 million loan to Iran's government by the Sinclair Consolidated Oil Corporation in exchange for a concession for the development of the Northern oil fields⁶⁸, and the second condition concerned a prohibition to transfer or annul the concession.⁶⁹ Noticeably, these requirements highlighted the Iranian governments' intention to gain more revenues from oil concessions by the granting of more balanced

⁶³ Later to transform into the contemporary oil firm Standard

⁶⁴ Foreign Relations (FR) 1920, Vol. III, p.353

⁶⁵ US Senate, Oil Concession in Foreign Countries, Washington, 1924, p.94

⁶⁶ Ghaffari, M., Political Economy of Oil in Iran 2000, London: Institute of Islamic Studies.p.46

⁶⁷ibid, p.47

⁶⁸ Ghaffari, op.cit., p.48-49

⁶⁹ Foreign Relations, 1923, Vol. II p. 713

terms along with the exercise of a greater sovereign authority, as well as resisting against foreign pressure to impose unfair agreements. Although the Sinclair Consolidated Oil Corporation was not pleased with the new restrictive conditions, both the parties reached an agreement for operations in four of the five Northern provinces and the new concession proposal was then confirmed by the Iranian Parliament in June 1923. However, foreign pressure from the Russian side via forbiddance of oil transport⁷⁰ from the fields to the international oil markets forced the Sinclair Consolidated Oil Corporation to reject the Northern concessions⁷¹.

Accordingly, the Iranian government, in spite of its active attempts to obtain a more balanced concession by changing the concessionaire was unsuccessful as a result of the foreign pressure from the Great Powers, Britain and Russia, that prevented the Iranian government to reach its goal to increase its revenues from the concessions. Imposing such pressure, which resulted in undermining the interests of Iran in the petroleum deals, aggravated the negative attitude of Iranians towards foreign participation in the oil industry that resulted in the current framework of buyback through the formation of the idea of supporting the national interest of Iranians against the foreign party. This tendency, in the present mechanism of buyback, has been reflected in the provisions of the fixed rate of return, the cost estimation before the beginning of the project and insurance regulation. Applying such provisions are a direct consequence of foreign pressure that led to the inflexibility of the Iranian buyback and the subsequent unattractiveness of the model. This study, by considering the influence of the historical factors on the existing buyback will attempt to propose the necessary reforms based on the evolutionary approach that do not conflict with any historical concerns to ensure the applicability of the offered solutions to improve the model.

b) The influence of World War II on the Iranian oil and gas industry: Absolute control of foreigners over Iranian oil sector

⁷⁰ *ibid.* p.51

⁷¹ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 168

As has been mentioned in the last section, Iran possessed a vital position for foreign countries because of its geopolitical location, as well as its natural resources. The Great War Two occurrence significantly improved energy price, particularly oil and gas reserves for the Great Powers, as the Allies forces, operating in the Middle East and Europe, relied on Iranian oil fields to provide their needs to win the war. As a result, the Allies forces, the Soviet Union and Britain, captured all the Iranian oil-producing zones in 1941, for protecting petroleum reserves against Nazis troops. Thus, the Great Powers directly overcame the Iranian oil industry through military pressure. As a result of the Allied forces' domination of the Iranian oil sector, the main part of Iran's economy, a treaty was signed in 1942 between Iran and the Allies countries, Britain and the Soviet Union, promising military aid to fulfil the duty of defense, guaranteeing the respect to Iran's state independency, providing economic assistance and leaving Iran as soon as the Axis threat passed⁷². However, the Great Powers, Britain and the Soviet Union, did not leave Iran, as both Powers, through military pressure, intended to extend their occupation of the Iranian oil and gas resources by exaggerating the Axis threat⁷³. Accordingly, the Iranian budget was significantly reduced, as the country did not have any control of its natural resources, many European and Mediterranean markets became inaccessible and shipping capacity drastically fell. Thus, the country with a huge amount of natural reserves faced a horrible economic situation which led to famine and the dying of many Iranian people, despite Iran's neutrality in the War. As a result, the impact of World War II on Iran was losing the control of its own natural resources and an ignoring of its sovereignty which led to creation of one of the worst events in Iranian contemporary history.

c) The Effect of the Cold War on Iranian Oil sector: Applying the doctrine of the 'negative balance' in petroleum deals by Soviets and the 1947 Iranian Petroleum Act

Following the finishing of the Great World War Two, which resulted in foreign absolute control of Iranian oil industry, the Cold War affected Iran's oil sector. This is because of the importance of the oil industry's position in the boosting the international economy and

⁷² Madani, Seyed Jalal Din, *Tarikh Siyasi Moaser Iran*, (Modern History of Politics of Iran) p. 289

⁷³ Ghaffari, op.cit., p.50-52

finance prior and after war, as well as the raised oil consumption during the Cold War, Iran, with possession of a huge amount of oil and gas reserves, became an area of competing interests. In addition to British and Russian oil companies, American oil companies which used to have small shares in the region's oil market began to play a more active role⁷⁴ in the competition by investing, and subsequently obtaining oil concessions in the Iranian oil and gas industry. Therefore, the country's situation, particularly removal of foreign army, Britain and Russia, appears as a significant issue for Americans. Although the 1943 Agreement, Iran, Britain and Russia, obliged all foreign army to leave the country within 180 days, and it being confirmed at the Tehran conference of 1943 that the Great Powers were to recognise Iran's integrity and independency, this provision was not fulfilled by either Russia or Britain. This is because of the fact that Iran was in an important location for the Allied countries.

The Royal Dutch Shell proposed an agreement in 1943, to achieve a discovery right beyond the territory of Anglo Iranian Oil Company's operations. In 1944 Assistant People's Commissar for Foreign Affairs, requested oil concessions in the north of the country which were close to USSR. Furthermore, American oil companies with the support of Iran's King, Mohammed Reza Pahlavi, were also pursuing concessions in order to compete with the Russians. In response to all these proposals, Iran's Government insisted on avoiding granting any concessions during the Second World War in order to prevent any presumption that they were awarded under duress. In spite of this government policy, the domestic Communist Party in the Iranian Parliament claimed the concession in favor of the Soviet Union in northern parts to render a political balance with the oil concessions in the South of Iran which were granted to the British. However, this argument, 'negative balance'⁷⁵, was rejected by Parliament, and Dr Mosaddegh in particular. To avoid the promotion of this argument, a punishment was enacted of up to 8 years in prison in solitary confinement, to prevent all government employees from debating any concession with foreigners.

On the other hand, the Soviet Ambassador, who was in contact with Roosevelt and Churchill, suggested a concessions' proposal to aid Iran's economy, and expand the friendship between the two countries. Moreover, He promised to either terminate or revise the new petroleum law. In fact, this proposal was part of the Soviets' agenda to render a

⁷⁴ Eden (et al), "Energy Economics", p77. The US reign deposits. Painter, "Private Power and Public Policy", p 14

⁷⁵ Whereby no privilege are granted to one power that would require the giving of similar benefits to others.

balanced relationship between the Great Powers and also to utilise the north of Iran as a security zone against US and British influences. The request to counter balance the US and Britain with demands for concessions in northern Iran was insisted on by the Soviet Union when they informed the combination of Western powers against them. This presumption was perhaps importantly confirmed, due to the fact that Shell, the partially British-owned firm, with a number of US companies started to demand oil concessions in Iran. Accordingly, the Soviet reaction in this contest is, actually, against the Western powers, particularly US attempts, to gain an oil concession in north parts of Iran. Furthermore, Russian and American companies' competition to engage in oil concessions in the northern provinces of Iran is highlighted by the British consul, Claremont Skrine: "the efforts of Standard Vacuum and Shell to secure oil prospecting rights that changed the Russians in Persia from hot-war allies into cold-war rivals."⁷⁶

As a result of the increasing political pressure of the Soviets on the Iranian government, the negotiations in respect to a concession on northern parts of Iran was begun in Moscow, despite Parliament's prohibition to discuss any concession with foreigners. This negotiation resulted in an agreement with important concessions to the Soviet Union in 1946. Moreover, a combined oil corporation was founded to discover the blocks in northern provinces of Iran. The agreements' length was twenty-five years which could be easily extended if both parties wished to do so. This agreement contained certain novel features, in contrast with former concessions. While the Soviet Union owned 51% shares for 25 years, Iran's Government possessed 49% and more importantly incomes obtained from the oil projects were to be divided in accordance with the parties' shares. Additionally, the royalty payments were not mentioned in this concession and both parties agreed on a share basis division. It is worthy to note that the area of exploration was extremely vast, comprising all three Iranian northern provinces from the Soviet Union border to the Miyanduab city which is close to Turkish border⁷⁷.

In contrast to the pressure from the Soviets regarding the concessions, the Americans, who were in competition with the Soviet Union over the northern concession, supported the Iranian Parliaments' Act. The American Ambassador in Iran recognised and defended the

⁷⁶ Skrine C.A., "The World War in Iran", London, Constable, 1962, p.227

⁷⁷ Hurenty, op.cit., p.263

right of the Iranians to dispose of their own natural wealth⁷⁸. However, the British Government was willing to accept the granting of the oil concession in the northern parts of Iran to the Soviet Union. This was because the British Government was concerned about the forces of nationalism in the parliament and that this might result in the challenging of the Anglo-Iranian concession in the south of Iran, if the Iranian Government and Parliament rejected the USSR request regarding mutual operation of oil blocks in north of the country. Subsequent to Parliament's decision to not granting the concession to the Soviets, the British Ambassador in Iran, who was in favour of awarding the concession to the Soviets, suggested to the Prime Minister to deliberate the future prospect of negotiation with regard to granting of the concession to the Soviet Union⁷⁹. He suggested that the Government revise the draft to provide fairer terms rather than rejecting the Soviets proposal on the concession. Following the encouragement of the British Ambassador in Iran to grant the concession to the Soviets, a renegotiation occurred between Iran's Government and the Soviet Union.

The Prime Minister in particular, by utilising a policy of "positive equilibrium" with Britain, in order to persuade the Parliament to permit the renegotiation of the "unjust" 1933 Agreement with APOC, attempted to convince Parliament to grant a concession to the Soviet Union. However⁸⁰ a further Act, which was presented by the deputy of the Nationalist Party in Parliament, became a barrier to all his attempts. This Act, which was about preventing the government from issuing any further oil concessions to foreigners, was ratified on 22 October 1947. It contained important terms which will be highlighted in further details. Although this Bill nullified the former negotiations with the USSR regarding the oil concession in the northern provinces, it exempted the Prime Minister from the regulated punishment which was versus those officials that attempted to establish a petroleum deal with international company. The government was obliged to provide the facility to begin exploring the field in 60 months via its investment. However, this was permitted for employing international technician, in case of a lack of technical experts, only from "completely neutral countries".

⁷⁸ Sutton, "Persia Oil", p.117.

⁷⁹New York Times, 13 September 1947, p. 86-87

⁸⁰ The vote had the dramatic result of 102 votes to 2. op.cit., Sutton, p. 118

Based on this Bill, the Government was allowed to negotiate with the USSR only in regards to the sale of discovered oil and only by informing Parliament, in the case of Iranian companies extracting oil. Accordingly, this Act absolutely banned the Iranian Government from awarding any concessions or any partnership privilege to foreign powers or oil companies. It was concluded in regards to oil concessions in the south of Iran and the regime pledged to start consultations with the British Government, as well as putting all its efforts to defend the rights of the Iranian nation in all circumstances where they had been violated⁸¹. Therefore, this Act had vital and also clear implications for the future of AIOC. The main consequence of this Act, further to the preventive effect of this bill with regard to finalizing petroleum deals with international companies, as well as involvement in those deals, was instructing the government to put its effort for guaranteeing Iranian national ownership over natural assets, when they were diminished. The Soviet Ambassador in Iran described this Act as an obvious prejudicial trend against the Soviet Union. Additionally, the Soviet Union via the ratification of this Act realized the Iranian regimes' intention to completely govern the country's petroleum assets. The revival of national feeling in Iran was the driving force behind the ratification of the Act in Parliament, as the people realised the feasibility of obtaining their own rights by standing up for their demands. Considering the Soviet Union's failure to achieve the concession, they began to embargo the Iranian government by blocking the APOCs way to export oil to the global market, putting pressure on Iranian MPs and sending their army to Iran to defend their interests⁸².

Accordingly, examining this part of Iran's oil history in this sub-chapter showed that there was a foreign military pressure to overcome Iranian control over its natural resources and which ignored the national interest of Iranians in petroleum deals, aggravating the negative attitude of Iranians towards the involvement of foreigners in the Iranian oil industry⁸³. Such foreign military pressure ignored the national interest of Iranians by overcoming their control and this resulted in the provision of the current method of buyback through forbiddance of any ownership or control of Iranian natural resources by foreigners, that have been mentioned in the Iranian Constitution. This principle, which is the main basis of the Iranian buyback, has been designed to protect the interests of Iran in petroleum

⁸¹ USFR, 1946, Vol. 7, pp 560-561

⁸² Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 170

⁸³ Ghaffari, op.cit., p.53

agreements against foreign contractors, and resulted in the practice of the buyback instead of any other model allowing the ownership of the oil product by foreigners such as the Production Sharing Agreement model. Although this historical concern has created inflexibility and, subsequently, unattractiveness within the framework of the buyback, it has stemmed from one of the worst parts of Iranian history and its influence cannot be underestimated in the present method. Therefore, this study, on the basis of the evolutionary approach to make the model more attractive by offering reforms will consider this crucial historical concern to ensure the applicability of its offered solutions. More importantly, this historical concern proves the accuracy of the evolutionary approach chosen by this study rather than revolutionary tactics, as any shift to another model which requires the foreign ownership of natural resources will face this historical consideration and public discontent, as well as the legal barrier in the form of the constitutional prohibition. Therefore, the most accurate way to offer a more attractive version of the Iranian buyback after the removal of the nuclear sanctions is by applying an evolutionary approach by carrying out applicable reforms that do not breach any historical, political and legal barriers.

1.4 Conclusion: The impact of concessions and foreign pressure on current mechanism of buyback

In summary, examining the Iran's foundation of petroleum contractual system prior to event of Nationalization demonstrated that the economic weakness of Iran in the 19th century and the foreign powers' interest in employing Iranian natural resources via controlling Iran because of its strategic position led to the Great Powers, Britain and Russia, to force Iran to grant unbalanced and exploitative concessions⁸⁴. Such features of the concessions as have been mentioned in the first sub-chapter created the negative experience of Iranians regarding the involvement of foreigners in the Iranian oil industry⁸⁵. Moreover, as has been discussed in the second sub-chapter, this negative historical experience has been aggravated by foreign pressure to refuse any attempt by the Iranian government to make the terms of concession more balanced and led to an absolute control

⁸⁴ Hurenty, op.cit., p.263

⁸⁵ Sutton, "Persia Oil", p.119

of Iran and its resources during the Second World War, which resulted in ignoring the national interest of Iran in petroleum deals. Therefore, as this chapter showed, the influence of the negative experiences of Iranians towards foreign involvement in the oil sector, as well as foreign pressure to preserve the concessions, were the two main historical reasons for adapting the harsh model of Iranian buyback which banned any kind of international possession of petroleum products. Furthermore, the conducted analysis of Iranian buyback background in this chapter pointed out the roots of many current restrictive provisions of the buyback stemming from the nationally supportive nature of the model which are, in fact, a response to the unbalanced terms and policies of concessions such as the short duration of contract, fixed rate of return, separation of discovery rights from development rights, cost estimation prior to the beginning of the project and more importantly banning any control or ownership of oil products by foreigners. Therefore, this study highlighted that the restrictive terms of the model arose from the historical concerns that will be examined and the applicable reforms will be proposed in the following chapters based on the evolutionary approach with no breach of any historical, political and legal prohibitions. Additionally, this chapter pointed out that the adverse effects of exploitative concessions created the special historical concern regarding the foreign ownership of Iranian natural resources. Therefore, adapting any model that contains permission of ownership of Iranian oil and gas fields will be confronted with this historical concern. As a result, this study by considering this historical concern will employ the evolutionary approach by utilising applicable reforms that do not breach the above-mentioned historical concerns. Accordingly, providing the historical analysis of the Iranian buyback covered an important gap which was present in other researches, offers a more completed image of the model via illustrating its historical roots and ensures the applicability of the reforms that this study will propose in the next chapters of this work.

Following the examination of the historical elements of the Iranian buyback, which demonstrated the influence of concessions on the current mechanism of buyback by the creation of a negative attitude amongst Iranians towards foreigners working in the oil sector, the next chapter will show the public discontent resulting from the concessions and foreign pressure to the nationalisation of Iranian natural resources led to the introduction of the current buyback. In fact, this study will attempt to provide the political and geo-political examination of the Iranian buyback in order to scrutinise the Iranian petroleum legal

framework in the period after the nationalisation event for the purpose of highlighting the political and geo-political concerns of the Iranian buyback.

Chapter 2: Analysis of Political and Geo-political consideration of Iranian buyback: Iranian petroleum legal framework subsequent to the event of Nationalisation

2.1 Introduction: The Nationalisation event, the pathway between the public discontent regarding foreign participation in Iranian oil sector and introduction of Iranian buyback

As has been demonstrated in the last chapter, the unbalanced and exploitative nature of the concessions issued due to Iran's economic flaw, as well as pressure of the Great Powers created a negative attitude amongst Iranians towards the involvement of foreigners in the oil industry. The direct result of such public discontent which begun from the concerns of the government regarding the inequality of the parties' income led to the nationalisation of Iranian natural resources, which in turn led to the introduction of the Iranian buyback. The occurrence of the nationalisation event is heavily influenced by the former historical events that were examined in the last chapter, due to the fact that it was in essence a political rebellion against the economic and political situation of Iran after the Second World War, which was characterised by rampant poverty, financial inequalities and the incapability of the government to rule the country⁸⁶. Therefore, the 1951 Nationalisation event is an essential element of Iranian petroleum background that stemmed from the economic and political dissatisfaction of Iranians towards the foreign companies operating in Iranian energy sector, leading to the rise of national opposition.

Historically, the nationalist movement as will be discussed in this chapter in political and geo-political context, firstly obtained majority in Parliament, then formed a nationalist government in the 1950s and finally were removed via the 1953 British and American coup⁸⁷. However, this foreign interference which has been carried out for the purpose of controlling the economy and political structure of Iran, as well as ensuring the geo-political aims of the western powers against the Soviet Unions aggravated the attitude of Iranians towards foreigners operating in the oil sector, and subsequently founded the economic root

⁸⁶ Jerrold L. Walden, "The International Cartel in Iran: Private Power and the Public Interest," 11 *Journal of Public Law* 69 (1962).

⁸⁷ Mostafa Elm, *Oil, Power and Principle: Iran's Oil Nationalization and its Aftermath* (New York: Syracuse University Press, 1992).

of the 1979 Islamic Revolution which excluded foreigners from the Iranian oil industry by nullifying all petroleum deals and applying the current harsh model of buyback.

The main influence of the nationalisation event on the current method of oil transactions is shifting the framework of the Iranian oil and gas industry from concessionary deals to the contractual framework in the form of production sharing agreements, and service contracts⁸⁸. In other words, this is the first time in the entire history of Iran's oil and gas industry that Iranians recognised the value of ownership of their natural resources and attempted to change the unfair terms of the concessions and to balance the provisions⁸⁹. It is noteworthy that Iran, after the nationalisation of its oil industry in 1951, has experienced a number of methods of oil and gas agreements such as production sharing agreements and service contracts. However, the extensive disappointing experience of Iranians to equalise the unbalanced terms of concessions which always were confronted by the political pressure of the Great Powers resulted in preferring the harsh mechanism of buyback over other models such as PSA, as the mechanism of buyback can ensure preserving the ownership of Iranian natural resources against the Great Powers. Accordingly, the current Iranian method of oil transaction has been influenced by the event of the nationalisation as the pathway between the negative experience of Iranians regarding the international involvement within oil related operation, and also to introduce Iranian buyback following the 1979 Islamic Revolution. Thus, this milestone in the historical background of Iranian legal framework needs to be politically and geo-politically examined to ensure that this study provides the complete picture of the Iranian buyback, as well as offering the applicable reforms to increase the efficiency of the model on the basis of the evolutionary approach. For these aims, this chapter which has been divided into four sub-chapters, will offer the examination of the Iranian petroleum legal framework subsequent to the event of nationalisation to point out the political and geo-political concerns of buyback, and more importantly to highlight their impact on the formation of the present provisions of buyback to ensure the applicability of proposed reforms in the following chapters. The first sub-chapter reviews the concern of the Iranian parliament regarding the inequality of the income of the parties in petroleum deals as the basis for the establishing of the nationalist

⁸⁸ Nationalization Act, Iran National Parliament, (1951).

⁸⁹ Madani, Seyed Jalal Din, *Tarikh Siyasi Moaser Iran*, (Modern History of Politics of Iran) p. 299

movement, and it will show the roots of some of the existing provisions in the buyback such as the fixed rate of return. The second sub-chapter considers the nationalisation government in relation to the foreign pressure which led to the 1953 coup and the failure of Iran to enjoy the full ownership and control over their natural resources as the key element in the introduction of the buyback in 1979. The third sub-chapter is aimed at illustrating the impact of the nationalisation event on the experience of Iran in practicing the production sharing agreement model which will show the accuracy of applying the evolutionary approach that has been chosen by this work rather than a shift to any model consisting of the foreign ownership of oil products. The last sub-chapter will consider the effect of the nationalisation event on the formation of the 1979 Islamic Revolution as the first successful attempt in the entire history of the oil and gas industries in Iran that could stop foreign powers from exploiting the Iranian natural reserves by nullifying all previous petroleum deals and introducing the Iranian model of buyback, despite the high economic and financial costs for the country.

Consequently, the study in this chapter will provide a full analysis of the political and geo-political considerations of Iranian buyback. This is because of the fact that lack of such consideration is an important gap in similar researches and will deprive this study from demonstrating the roots of many present provisions of buyback. Thus, this analysis is crucially significant within grasping the model's mechanism. Moreover, by not providing such political and geo-political considerations, this will lead this study to offer an incomplete picture of the Iranian buyback which cannot be reliable for the aim of this work to offer the applicable solutions for making the model commercially more efficient in the third and the fourth chapter.

2.2 Iranian parliament's concern regarding the inequality of parties' income: Failure to reach an agreement, as a result of foreign political influences

As has been shown in the first chapter of this work, the exploitative nature and unbalanced terms of the concessions granted to foreigners are the main elements in the creation of the negative attitude amongst Iranians towards foreign involvement in the oil industry. Such features of the concessions resulted in a disagreement amid the Iran's regime and foreign

party which resulted in a re-negotiation of the provisions of the oil transactions with foreign parties⁹⁰. The main issue of the dispute was the inequality between revenues obtained by the national side and the foreign contractor from the oil project, owing to the fact that the Anglo-Iranian Oil Company's income from the project was greater than the Iranian government's royalty and tax income⁹¹. Moreover, from the international perspective the 'UN Resolution of Permanent Sovereignty over Natural Resources' which recognised the absolute freedom of countries freely for using the local assets and reserves in favour of local benefits supported the Iranian parliament in its attempt to obtain a more balanced deal. Article I of this movement declared that⁹²:

1. The right of peoples and nations to permanent sovereignty over their natural wealth and resources must be exercised in the interest of their national development and of the well-being of the people of the State concerned⁹³.
2. The exploration, development and disposition of such resources, as well as the import of the foreign capital required for these purposes, should be in conformity with the rules and conditions which the peoples and nations freely consider to be necessary or desirable with regard to the authorization, restriction or prohibition of such activities⁹⁴.
3. In cases where authorization is granted, the capital imported and the earnings on that capital shall be governed by the terms thereof, by the national legislation in force, and by international law. The profits derived must be shared in the proportions freely agreed upon, in each case, between the investors and the recipient State, due care being taken to ensure that there is no impairment, for any reason, of that State's sovereignty over its natural wealth and resources⁹⁵.
4. Nationalization, expropriation or requisitioning shall be based on grounds or reasons of public utility, security or the national interest which are recognized as overriding purely individual or private interests, both domestic and foreign. In such cases the owner shall be paid appropriate compensation, in accordance with the rules in force in the State taking

⁹⁰ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 150

⁹¹ Mostafa Elm, *Oil, Power and Principle: Iran's Oil Nationalization and its Aftermath* (New York: Syracuse University Press, 1992).

⁹² <http://www.ohchr.org/EN/ProfessionalInterest/Pages/NaturalResources.aspx>. General Assembly resolution 1803 (XVII) of 14 December 1962, "Permanent sovereignty over natural resources", p 2. Access on July2016

⁹³ *ibid*

⁹⁴ *ibid*

⁹⁵ *ibid*

such measures in the exercise of its sovereignty and in accordance with international law. In any case where the question of compensation gives rise to a controversy, the national jurisdiction of the State taking such measures shall be exhausted. However, upon agreement by sovereign States and other parties concerned, settlement of the dispute should be made through arbitration or international adjudication⁹⁶.

5. The free and beneficial exercise of the sovereignty of peoples and nations over their natural resources must be furthered by the mutual respect of States based on their sovereign equality⁹⁷.

6. International co-operation for the economic development of developing countries, whether in the form of public or private capital investments, exchange of goods and services⁹⁸, technical assistance, or exchange of scientific information, shall be such as to further their independent national development and shall be based upon respect for their sovereignty over their natural wealth and resources.

7. Violation of the rights of peoples and nations to sovereignty over their natural wealth and resources is contrary to the spirit and principles of the Charter of the United Nations and hinders the development of international co-operation and the maintenance of peace⁹⁹.

8. Foreign investment agreements freely entered into by or between sovereign States shall be observed in good faith; States and international organizations shall strictly and conscientiously respect the sovereignty of peoples and nations over their natural wealth and resources in accordance with the Charter and the principles set forth in the present resolution¹⁰⁰.

Thus, this movement can be identified as the main international element effecting the Iranian Parliament's decision to nationalise the Iranian natural resources, owing to the fact that the Parliament realised that the idea of nationalisation of oil and gas resources was internationally accepted, and more importantly, it could be defended. Therefore, the Iranian Parliament in its first step of claiming fairer deals, enacted the rider of 22 October

⁹⁶ http://legal.un.org/avl/ha/ga_1803/ga_1803.html General Assembly resolution 1803 (XVII) of 14 December 1962, "Permanent sovereignty over natural resources", p 2 July 2016

⁹⁷ *ibid*

⁹⁸ *ibid*

⁹⁹ *ibid*

¹⁰⁰ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*. 2016. Page 152-154

1947, obliging Iran's government to propose a re-negotiation with APOC in order to increase the income of the Iranian government. This rider expressed that: In situations when rights of Iranians with regard to local assets, either mineral or else, was weakened, especially regarding fields in south of Iran, regime must start defending, as well as to prepare to return such local rights, moreover, Parliament has to be informed regarding outcomes¹⁰¹. Subsequently, negotiations commenced in September 1948 amid Iran's regime and Anglo Iranian Oil Company which resulted in a number of offers from the company including the increasing of the royalty payment to the government¹⁰², as well as promoting the Company's tax payment to Iran's government. Nevertheless, this round of negotiations, despite all proposed provisions, could not result in an agreement, due to the fact that the Parliament has been informed by the Supplemental Agreement Committee¹⁰³, headed by Dr Mosaddeq, that a more favourable contract had been concluded amid Aramco and Saudi government¹⁰⁴ with profits being split 50/50 between the parties. As a result, the Anglo-Iranian Oil Company with the support of the British government threatened to sanction the Iranian oil and to ban Iran from British technicians, and they left the negotiations in order to force Iran to conclude the agreement which created the dissatisfaction between the Iranian side, the government and the Parliament, due to their failure to achieve a more balanced term of the petroleum deals¹⁰⁵.

Accordingly, despite offering the altered provisions from AIOC regarding the payments to the Iranian government, the parties did not reach an agreement, and the proposed agreement was still biased towards the foreign party following a policy of exploitation of Iranian natural resources through political influence and pressure. Thus, Iranian government could not establish a fairer deal through negotiations. Such adverse foreign political influences, as will be discussed in the next sub-chapter, exploited the Iranian natural reserves and aggravated Iranians' attitude towards involvement of foreigners. More importantly, the negative effect of this foreign political influence made the Iranian government determined in its position to remove foreigners from the oil industry by nationalising Iran's natural assets and practicing the Iranian model of buyback with its harsh

¹⁰¹ International Court of Justice, *op.cit.*, p. 273.

¹⁰² Zoghi, *op.cit.*, pg. 251-256

¹⁰³ Anglo-Iranian Oil Company, Annual Report and Accounts, 1949, pp. 11 ff.

¹⁰⁴ Zoghi, *op.cit.*, pg. 231-236

¹⁰⁵ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 170

provisions such as a fixed rate of return with the aim of protecting Iran's national interests against all foreign parties in petroleum deals.

2.3 The Nationalisation government in relation with interference of foreign powers: Main step to introduction of buyback

It has been demonstrated in the last sub-chapter that the foreign political influences on Iran to preserve the unbalanced terms of deals for the purposes of exploiting the Iranian natural resources aggravated the Iranians' attitude towards involvement of foreigners in the oil sector. Therefore, as the Iranian government's attempts to modify the concessions via negotiations failed, the nationalist government in 1952 decided to nationalise the Iranian natural assets to obtain a more balanced petroleum deal, and accordingly defend the national interest of Iranians. In fact, from a political point of view, the Nationalisation movement, and subsequently the Nationalist government can be identified as a powerful reaction towards the many years of unequal financial and legal relationships between Iran and the foreign parties. This reaction has been visualised in the framework of the Iranian model of buyback with its harsh provisions to protect the Iranian national interests against the foreign party's intention to exploit the Iranian natural resources. Therefore, the negative domestic experience towards foreigners involved in the oil sector which has stemmed from the exploitative nature of concessions and has been aggravated by foreign powers interference in favour of foreign companies resulted in the nationalisation of the oil and gas reserves which was the main step in the introduction of the current Iranian buyback. As a result, the detailed political and geo-political examination of oil nationalisation in Iran as the vital event will be offered in this sub-chapter. In addition to this consideration, this sub-chapter will attempt to point out the political and geo-political concerns in Iranian society towards any reform of the buyback in order to prevent any clash between the proposed alterations and those concerns.

Following the nationalisation movement in 1947-1951, the nationalisation law was drafted by the Oil Committee in 1951 which stated that: For the happiness and prosperity of the Iranian nation and for the purpose of securing world peace, it is hereby resolved that the oil industry through all parts of the country, without exception, be nationalized, that is to say,

all operation of exploration, extraction and exploitation shall be carried out by the government¹⁰⁶. Articles 2, 3 and 6 of this law can clarify the vital image of nationalisation law which are considered below¹⁰⁷:

Article 2 epitomised the legal basis of the nationalisation by requiring the Anglo-Iranian Oil Company to dispose and relocate its assets to the control of the Mixed Board which was constituted by both Iranians and British members. In fact, this article confirms the equality of the parties in the agreement which had been the aim of the country for many years. Article 3 appointed the National Iranian Oil Company as the main body in operation of the Iranian oil fields. This article is the key element for the current NIOCs' role in petroleum deals as the sole authorised party to participate in oil contracts. Article 6 of this law concerns the steady replacement of British technicians by domestic technicians, and also requiring foreign training for Iranian experts¹⁰⁸. This article has been reflected in the third generation of Iranian buyback via provisions related to the transfer of technology, as well as employing Iranian workers.

On the other hand, the British government in support of the Anglo-Iranian Oil Company sanctioned Iranian oil, blocked Iranian assets in the British currency and banned Iran from British technicians which resulted in dramatically diminishing Iran's oil production and subsequently led to the suffering of the Iranian economy. Moreover, for the purposes of protecting the economic interests in the Iranian oil sector, the British Government sued Iran in the International Court of Justice by claiming the illegality of the nationalisation law, as this law destroy its contractual benefits. Hence, the International Court of Justice issued an order to secure both parties' respective rights by interim measures¹⁰⁹. However, the Iranian Government rejected this order, as the Court's jurisdiction was not recognised in this action by the Government. In response to Iran's refusal, the British government brought its claim to the United Nations to compel Iran, within the United Nations framework, to respect the International Court of Justice's previous order for interim measures, as issued in 1951. In

¹⁰⁶ Iranian Embassy; -op.cit., p.2

¹⁰⁷ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 171

¹⁰⁸ International Court of Justice, op.cit, pp. 279-280

¹⁰⁹ Anglo-Iranian Oil Co., U.K. v. Iran, Judgment, 1952 I.C.J. 93 (July 22)

https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=3&cad=rja&uact=8&ved=0ahUKewiG9O3WoMfUAhVGbxQKHbqFCdwQFggYMAI&url=http%3A%2F%2Fwww.worldcourts.com%2Ficj%2Feng%2Fdecisions%2F1952.07.22_oil_co.htm&usg=AFQjCNG_8cKNbD3-V0w_RMhQpFmARglqOA/ p 93-103/ Access on July 2016

response, the Iranian government, represented by Dr Mosaddeq, argued that since the nationalisation of the Iranian oil and gas industry was a merely domestic matter, it was out of the International Court of Justice's jurisdiction, or that of any foreign state¹¹⁰. Subsequently, the Security Council ruled to review the claim only after the International Court of Justice's examination of the matter. Accordingly, the International Court of Justice commenced its session with regard to the Iran - United Kingdom disagreement in 1952 to deal with its jurisdiction and subsequently ruled that since the Court's jurisdiction was only limited to conventions and treaties, as was accepted by Iran in September 1932, and also that the 1933 Contract was a concessionary agreement to which the British Government was not a party to, it was accordingly held that the Court had no jurisdiction to enter into the matter referred to it by the British Government in 1951. Therefore, it concluded that the Court's previous order, the interim measures, ceased to have effect¹¹¹. Consequently, since the Iranian and the British government failed to reach a solution, the British Government blocked all Iranian payments in Sterling Pounds, and cancelled the permission for the exportation of vital materials to Iran for the operation of the oil industry in order to force the Iranian Government to change some of the terms of the nationalisation law. Such actions had a negative impact on the Iranian economy by decreasing the oil production, which was the basis of Iranian government's budget, and subsequently led to the Iranian Government facing a financial crisis in 1952. Therefore, the Iranian Prime Minister requested £40 million from AIOC, claiming that this amount was owed by the Company to Iran. In response, Truman and Churchill, through AIOCs' representatives, offered a proposal for dealing with the problem via providing access to Iranian oil to the global market, as well as granting \$10 million in aid¹¹² by the United States which was rejected by Iran on the grounds of inconsistency with the Nationalisation Law in 1947. As a result, the political relationship between Iran and the United Kingdom deteriorated. However, the US government was determined in resolving Iran's financial crisis, as the US government did not want Iran to possibly begin renegotiations with the Soviet Union which could be a potential threat for the US. Therefore, following the geo-political American's interests, the

¹¹⁰ shwadhan, op.-cit., p.212

¹¹¹ Anglo-Iranian Oil Co., U.K. v. Iran, Judgment, 1952 I.C.J. 93 (July 22)

https://www.google.co.uk/url?sa=t&rct=i&q=&esrc=s&source=web&cd=3&cad=rja&uact=8&ved=0ahUKewiG9O3WoMfUAhVGbxQKHbqFCdwQFggYMAI&url=http%3A%2F%2Fwww.worldcourts.com%2Fici%2Feng%2Fdecisions%2F1952.07.22_oil_co.htm&usg=AFQjCNG_8cKNbD3-V0w_RMhQpFmARglqOA/ p 93-103/ Access on May 2016

¹¹² W. Levy, op. cit., p. 95

United States Ambassador in Tehran, on behalf of the British government, transmitted a final offer to the Iranian government for consideration. It was proposed that¹¹³:

(a) The International Court of Justice would deal with the issue of Iran's counter-claims and compensation for the Company on the ground of loss of business.

(b) An American company would pay \$50 million in advance in exchange of purchasing \$122 million discounted price of Petroleum from Iran. Moreover, an international firm would be established, as one of the AIOC members, with the authority to negotiate with the Iranian Government for the export of refined and crude oil.

(c) Iran would be obliged to pay 24% of received petroleum revenues to the British government, before the settlement the compensation claim, and 24% via direct payments or petroleum transfers for a period of twenty years after resolving the compensation claim¹¹⁴.

In response, the Iranian Government rejected the new offer, due to its contradiction with the nationalisation law with expression of that this offer principally is the same with earlier British-American shared offer. In response to this refusal, the US government dismissed the Iranian Governments' appeal for financial aid. The US President, Eisenhower, stated that "so long as Iran could have access to funds derived from the sale of its oil products if a reasonable agreement were reached it would be unfair if the money of the American taxpayers were to be spent in Iran"¹¹⁵. Accordingly, this contention regarding the proposals truly demonstrates the mutual distrust of both side towards each other which resulted in a strong resistance among Iranians towards the involvement of foreigners in the energy sector that impeded compromises between Iran on the one side and the UK and US on the other¹¹⁶.

Following the failure of the nationalist government and the British government to reach an agreement, Britain planned a full-scale Coup d'état in order to undermine, and finally remove the nationalist government. Therefore, the British government attempted to gain support from Americans, as well as various conservative Iranian groups, such as officers in

¹¹³ Zoghi, op.cit., pg. 235

¹¹⁴ Madani, S.J., 'Tarikh Siyasie Moaser Iran' (The Modern Political History of Iran), Vol. 1, Daftare Entesharate Eslami; 1982: 28-6

¹¹⁵ ibid

¹¹⁶ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 171

the King's army, senior police and newspaper editors.¹¹⁷ As a result, the CIA and MI6, with the knowledge and support of the Iranian King, put in place the joint efforts to remove the nationalist government by attacking the Prime Minister's house (Dr.Mosaddeq), kidnapping several key officials and encouraging mobs to throw the country into disarray in order to weaken the government in 1953¹¹⁸. Subsequently, the Prime Minister (Dr.Mosaddeq) was arrested by the rebels and army, and the judicial system prisoned him in cell for 36 months, as well as house arrest for the remainder of his life. Accordingly, the British government, as a result of the 1953 Coup d'état, finally achieved its long term mission of removing the nationalist government which was a vital restraint for increasing British financial and political influence in Iran. In fact, the effect of the 1953 Coup d'état for the British government was removing the barrier which the nationalisation event created for foreign investment. Thus, Anglo-Iranian Oil Company could continue to obtain huge benefits by exploiting the Iranian natural resources by preserving the previous unbalanced concessions, and more importantly, the British government preserved Iranian natural resources from being used by the USSR. From other side, reason for Americans' participation at 1953 Coup d'état was their fear of losing Iran in favor of USSR as a result of the country's relation to USSR¹¹⁹. Therefore, this event ensured the geo-political interests of Americans by preventing the Soviet Union from promoting its power and influence over Iran.

Overall, it can be determined from the events at the time, as well as immediately afterward nationalisation occurrence that primary reason for the Coup was control of Iranian oil. This event, the overthrowing of the first democratically elected government by the Coup d'état of 1953, has had a deep impact on the Country, people and government, and aggravated the negative tendency throughout the country towards foreign parties. Moreover, the removal of the nationalist government highlighted the significant influence of the oil industry in all aspects of society, politics, and the economic sphere of Iran. Accordingly, the present strict view of buyback which contains a nationally supportive nature as reflected in the restrictive provisions such as granting the discovery and production rights separately, and forbiddance of ownership of any oil product by foreigners can be fully comprehended in the light of the Great Powers, Britain and American, role in this coup. Such political and geo-

¹¹⁷ Katoozian; H., 'Mosaddeq and the struggle for power in Iran', I.B. Tauris & Co Ltd, London 1990: 178

¹¹⁸ *ibid*: 182

¹¹⁹ Iran Chamber Society op. cit. [<http://www.iranchamber.com/history/coup53/coup53pl.php>]

political influences of the foreign countries on the current model of buyback confirm the existence of a mutually responsive relationship between Iran's politics and geo-political concerns and the Iranian oil industry which remains true until recently. Therefore, the political and geo-political examination of the relevant issues, particularly the event of the nationalisation of oil, regarding the Iranian buyback is significant for the aim of this study to ensure the applicability of the proposed solutions to attract foreign investors, as well as to protect the national interests of Iran in the petroleum deals¹²⁰.

Furthermore, it has been demonstrated in this sub-chapter that the nationalist government suffered from economic difficulties which finally led to the collapse of the government with the support of foreign countries. Therefore, applying a new method of oil transaction relaxed the Iranian public feeling, however it also led the Iranian government to struggle amid global powers, which was an important reason for its collapse. Therefore, it can be pointed out that the mechanism of buyback should ensure both parties interests, otherwise, it cannot attract foreign investment or protect national interests. Accordingly, this study by employing the evolutionary approach will attempt to offer applicable solutions to make the model more attractive by rendering a fine balance between the interests of both national and international parties in the buyback. Following the collapse of the nationalist government, the King appointed a new government that chose a new approach regarding petroleum deals, known as the production sharing agreement. The effect of the nationalisation event on the new method of oil transactions, as well as the consequences of the practice of this new model, PSA, will be examined in the next-sub chapter.

2.4 Effect of the nationalisation event on practice of Production Sharing Agreement model: Economic root of the 1979 Islamic Revolution and practice of buyback

As has been discussed in the last sub-chapter of this work, the negative attitude of Iranians towards foreigners, resulting from their interference in Iran's political and economic issues, motivated the Iranian people to support the nationalisation movement against foreign oil companies which led to the nationalisation of the Iranian petroleum sector. Nevertheless, nationalist government faced the financial difficulties stemming from their political views towards the involvement of foreigners in the oil industry, as well as the 1953 Coup d'état by

¹²⁰ Katoozian; H., 'Mosaddeq and the struggle for power in Iran', 1.B. Tauris & Co Ltd, London 1990: 18-

the CIA and MI6, with support of the Iranian King, resulted in the collapse of the first democratically elected government in Iran. Therefore, the King appointed a new Prime Minister, General Zahedi, to establish a new government which chose a new approach in relation to foreign oil companies by the formation of an international consortium with the cooperation of the NIOC based on the terms of the 1933 concession. However, the public and Parliaments' protests against the new agreement confirmed that "the government" ... cannot not ignore public feeling by denying the Nationalisation Act. Furthermore, it would be impossible to return Anglo Iranian oil Company for exclusively producing, refining and marketing¹²¹." Nevertheless, the Iranian Parliament, under the pressure from the government, passed the first Iranian oil bill which included the new participation formula to permit the involving of foreign investors to operate outside the consortium's defined area in return of sharing the ownership of the final product instead of sharing the revenues coming from selling the oil product in the buyback. This proposal was accepted by the major oil companies, as this offer seem well designed and suitable to guarantee the collaboration producing countries, due to the fact that foreign oil companies obtained more shares than NIOC and more importantly, the new method of payment minimised the risk of price fluctuations in the global oil market¹²². Therefore, the Iranian government began to practice the production sharing model in 1957, despite its contradiction to the idea of the nationalisation which resulted in increasing the revenue of the Iranian government, as well the adverse socio-economic impact on Iranian society. Accordingly, this sub-chapter aims at highlighting the influence of the nationalisation event on the experience of Iran in exercising the Production Sharing Agreement, to provide the basis for the comparison of PSA with the current buyback system in the fourth chapter, in order to grasp whether it can be an applicable alternative for the Iranian buyback. Moreover, this sub-chapter will discover the roots of some of the existing provisions in the buyback such as the fixed rate of return in order to identify the unnecessarily restrictive provisions which have to be revised to make the buyback more attractive. Finally, the present study in this sub-chapter, by offering the socio-economic analysis highlights the necessity of providing an economic plan for the Iranian government to minimise the adverse effect of boosting its petroleum revenues,

¹²¹ Alavi, op.cit., p .127-128

¹²² NIOC, Brief History of Iran's Oil.P7

particularly at the present time, as the Iranian government is actively encouraging foreign investments in order to increase its revenues after the removal of the nuclear sanctions¹²³. Following the reaction of the public and political parties to the return to the terms of the 1933 concession, the Iranian Parliament enacted the 1957 Petroleum Law, which included the new formula which authorised the National Iranian Oil Company, on behalf of Iran's government, to sign the miscellaneous contracts based on the sharing agreements. "... it was determined that whereas Iran's regime could obtain half the revenue for revenue tariff, fifty percentage of revenues received by exploration will belong to National Iranian Oil Company as a party ,... in fact the model is based on the theory of equal income in the contract... therefore, the result was equivalent partnership with the foreign company¹²⁴." Subsequently, in 1957, the first PSA was concluded amid National Iranian Oil Company and the Italian corporation, AGIP, which was a governmental company, to operate massive area , 23,000 kl, in southern part of the country for a period of 25 years which led to the establishment of a joint company. Based on the agreement, while the AGIP was obliged to pay \$22 million as the capital for explorations' activities, it enjoyed the compensation at 10% of yearly extracted barrel, and also taking advantage of an exemption from royalty payments. The second significant production sharing agreement based on the 1957 Petroleum Law was signed in June 1958 between NIOC and a subsidiary of Standard Oil of Indiana, the Pan American Petroleum Corporation, to operate the 18,600 kl in the south of Iran which resulted in establishment of Iranian Pan-American Oil company (IPAC) as a joint firm. This agreement obliged the IPAC to finance all exploration-related expenses in return for having 50 per cent of the final product¹²⁵. Accordingly, the Iranian Parliament, in order to increase the revenue of Iran from oil production by making the terms of petroleum deals more balanced, allowed the exercise of the PSA model as the only period within the history of the oil industry in Iran which created a special legal framework. This new legal framework, unlike the concessionary agreements, taxed Profits at the rate of 50 per cent, divided the profits and board of directors equally between the two parties, and obliged the foreign companies to provide all financial support for the oil exploration until the oil discovery reached commercial quantities which resulted in an exceeding of the revenue of

¹²³ Alavi, op.cit., p .129

¹²⁴ Alavi, op.cit., p. 142

¹²⁵ ibid p.144

the Iranian government by establishing more balanced contractual provisions. As a result, Iran could reach some of its aims within the movement of nationalisation of oil by shifting the concessions towards the more balanced contractual framework of PSA. However, ownership of the oil product by foreigners and the long duration of the contract, which are a part of the PSA model remained ignored political concerns. Consequently, the financial effect of the new legal framework for the Iranian government was a dramatic increase of its revenue from oilfield production, which in turn enabled the government to develop the country economically. Such a radical change in the methods of oil transactions, led to a boost in the income of the government, whilst also conflicting with the essence of the idea of nationalisation and socio-economically impacting on Iranian society via aggravating the inequality of wealth in the country. In fact, although the modernisation of the petroleum contractual framework of Iran increased the revenue of the Iranian government, the absence of an economic plan aggravated the imbalance of wealth within the society of Iran¹²⁶. Moreover, the huge income obtained from the oil revenues led to high inflation, social movement, and increased crimes in different department of the regime¹²⁷. More importantly, allowing the foreign oil companies to possess the oil product within the framework of PSA was protested by political parties in Parliament, as well as by Iranian people, due to its contradiction to the nationalisation law that forbid any kind of foreign ownership of the oil product. Hence, the obvious contradiction of PSA with the nationalisation law, as well as the widened gap between the industrial class and the traditional classes (bazaar) resulted in public discontent which ultimately culminated in the Islamic revolution of 1979¹²⁸ and the subsequent re-introduction of the Iranian buyback. Accordingly, the radical move towards the production sharing agreement mechanism by applying a revolutionary approach which contradicted the essence of nationalisation created the economic roots to the Islamic Revolution that began the practice of the Iranian buyback.

Overall, analysing the experience of the Production Sharing Agreement model in Iran in the present sub-chapter showed that although this model was an effective method in ensuring the interests of Iran via increasing the profits of the government, this study does not

¹²⁶ Madani, Seyed Jala al Din, *Tarikh siyasi moaser Iran*, (Modern History of Politics of Iran) p. 280-286

¹²⁷ Fateh, Mostafa "Panjah Sal Naft Iran" (50 years Iranian Oil) p. 350

¹²⁸ Banani Amin, "The Modernisation of Iran, 1921-1941", p. 35-41

recommend the shifting towards this model from the current buyback in the form of a revolutionary approach. This is because of the fact that the high price of such a shift, including the great changes in the Constitution, cannot justify the necessity of this action and more importantly the Iranian society from a political point of view will not tolerate such a radical change in favour of foreign oil companies. Moreover, the socioeconomic examination of this vital time in Iranian petroleum background demonstrates, particularly in this specific time that the government should bring the socio-economic effects of the increase in petroleum revenue after lifting of sanctions to its consideration. As has been showed in this sub-chapter, lack of such consideration will aggravate the economic inequality in Iranian society, which will create many social and economic difficulties for the society and the government. Therefore, disregarding the socioeconomic effect of boosting the country's economy will aggravate the wealth gap between different parts of the society which was the main foundation of peoples discontent that resulted in the 1979 Islamic Revolution and, subsequently, in the introduction of the buyback. The impact of such a great event in the history of Iran on the current model of buyback will be analysed in the next sub-chapter. The role of the Revolution on the creation of the existing provisions of buyback from the political and geo-political point of view, will be examined in order to ensure that the reforms that this study will propose on the basis of an evolutionary approach will not breach the political barriers in Iranian society.

2.5 The 1979 Islamic Revolution: Applying the Iranian model of buyback through annulment of all previous deals with foreign oil companies

As has been highlighted in the sub-chapter 2.4 ignoring the basis of the nationalisation law, the forbiddance of the ownership of oil products by foreigners, in practising the production sharing agreement model, as well as failings by the Iranian government in providing an economic plan for its increased income, created the political and economic roots of the 1979 Islamic Revolution by aggravating the negative experience of Iranians towards foreign involvement in the Iranian oil industry. This sub-chapter will consider the political and geo-political influence of the most recent event in the history of the oil industry in Iran, the 1979 Islamic Revolution, on employing the current method of oil transaction in Iran to demonstrate the political concerns of the Iranian model of buyback which will be considered at the time of proposing the reforms to modernise the model.

The distrust amid Iranians towards any involvement of foreigners in Iran particularly in the oil industry reached its peak during the occurrence of the 1979 Islamic revolution. In fact, the revolution was a response to many years of foreign interference and pressure in the political and economic spheres of Iran to exploit the Iranian natural resources¹²⁹. Therefore, by 1979 Revolution occurrence National Iranian Oil Company annulled all Iranian oil and gas deals that was included international party before the Revolution, on the legal basis of the decision of the Revolutionary Council on 7th January 1979, in relation to all Iranian contracts with foreign companies¹³⁰. This annulment resulted in the costly litigation regarding cancellation damages, stopping all exploration-related activities, and subsequently led to a huge loss of income for the country which was the result of excluding foreigners from the oil industry for the purpose of stopping their exploitation of Iranian natural resources. The economic disruptive effect of this annulment has been notified by the previous National Iranian Oil Company Manager, Seyed Mahdi Hoseyny:

‘termination of any contract can be potentially costly for Iran, owing to the fact that oil agreements contain numerous complicated terms that can be issue of dispute in arbitrational panel, and subsequently will lead to a favourable solution for the international contractor, due to the fact that the judicial system might not be are not specialised in energy matters, therefore, they will adhere the side that seem to be wronged¹³¹. Hence, as the effect of the annulment of petroleum deals for the foreign oil companies was a huge loss in revenue, they sued Iran’s government to procure a legal verdict against Iran in order to cover their loss which resulted in the courts’ decision to oblige Iran to pay compensation to companies based on the very optimistic predictions of their potential profits by recognition of the companies rights only to above-ground oil rather than underground deposits¹³². As a result, following the decision of the government to annual all previous oil deals, the Iranian version of the buyback became the key element of the Iranian petroleum legal framework. In fact, the most crucial influence of this annulment on the Iranian method of oil transactions was shifting the Iranian model of oil and gas contracts from the production sharing agreement model to the Iranian buyback with its harsher mechanisms

¹²⁹ Moosavi - Amini , op.cit., p.60

¹³⁰ Fesharatki op.cit., p. 13

¹³¹ Payvand News, 19th May 2005

¹³² Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 171

which is more in compliance with the essence of the nationalisation event through its implementation of prohibiting any ownership of any oil products by foreigners. Accordingly, the decision of the new Iranian government to nullify all previous petroleum deals, and applying the Iranian buyback was the first time in the history of oil in Iran that an Iranian government could practice a model to fulfil the essence of the nationalisation idea for the aim of protecting the Iranian natural resources. However, such decision resulted in a high financial and economic loss for the country.

Consequently, this sub-chapter illustrated that public discontent stemming from the nationalisation movement changed the model of oil transactions from the production sharing agreement to buyback, despite the expensive financial fines that early termination of the contracts brought on the country. In fact, ignoring the political concerns regarding the production sharing agreements was one of the vital items in creation of the economic roots of the 1979 Islamic Revolution, which resulted in the annulment of all previous oil deals, and subsequently shifting from the PSA to the buyback model that ensured the aims of nationalisation. Therefore, it is crucially important that this study considers the potential political and geo-political impacts of any reform before proposing such reform in order not to clash with any barriers in Iranian society, so as to ensure that the reform can be successfully applicable.

2.6 Conclusion: The applicability of the evolutionary approach toward the future of buyback from the political and geo-political point of view

With the aim of determining the accurate way to modernise the present model of buyback agreements in order to foresee the future development of the model, it seems essential to have a perception into the political and geo-political considerations of the model by analysing the Iranian petroleum legal framework subsequent to the event of nationalisation. This insight into the issue of buyback can comprehensively demonstrate the adverse effect of the political and economic pressure of the big powers on the formation of oil transaction in Iran¹³³. Thus, an analysis of the political and geo-political considerations of buyback within absolutely significant petroleum relevant occasions of Iranian oil background, 1951 nationalisation of oil and the 1979 Islamic Revolution, can provide the full picture of the

¹³³ Malek, M., History of Iran, Iran Chamber Society. p. 78

Iranian buyback. As a result, limiting the analysis of Iran's buyback agreements to the present situation, which is the vital gap in similar researches, will result in missing such vital issues within the Iranian oil industry, and accordingly will decrease the applicability of the solutions that this study will propose with the aim of making the model more competitive in future.

As the political and geo-political considerations of Iranian buyback demonstrated in this chapter, the nationalisation event is the key element in connecting the negative attitude of Iranians towards international participation with Iranian petroleum market and exercising Iranian model of buyback with its preventive provisions. Moreover, the nationalisation event is politically and geo-politically vital, as it changed the petroleum framework of Iran from concessionary deals to a contractual form which was a result of the Iranian people's recognition regarding the value of their natural resources¹³⁴. Although this event was a political rebellion to the many years of unbalanced and exploitative concessions and ended via foreign interference, it heavily influenced the establishment of the current buyback system following the 1979 Islamic Revolution.

This chapter showed that the root of some provisions of the present buyback such as transfer of technology and obligation of foreign companies to employ Iranian workers in oil projects can be found in the political and geo-political influences of the nationalisation event, as a lack of technology and expertise failed the nationalist government in reaching its aim to nationalise the whole process of oil production, and more importantly led the foreign powers to successfully carry out the coup. Furthermore, it has been shown in this chapter that the main political concern regarding the oil contracts in Iran is the issue of ownership of natural resources that has been illustrated in the current constitutional provisions which ban the ownership of natural resources by foreigners. This vital concern which has been denied via the production sharing agreement model created the public discontent and economic roots of the 1979 Islamic Revolution that excluded all foreigners from the Iranian oil sector by nullifying the previous petroleum deals and applying the Iranian buyback with its harsh and restrictive provisions. Accordingly, this study by providing the political and geo-political considerations of buyback demonstrated the applicability of the middle way between the current harsh model of buyback and the 19th century and early 20th

¹³⁴ Foreign Relations (FR) 1920, Vol. III, p.353-355

exploitative concessionary deals by reforming the unnecessarily restrictive provisions of buyback without granting the ownership rights to foreigners on the basis of the evolutionary approach that will be discussed in the third and the fourth chapters of this work. Employing such reforms are intended not to breach any historical, political and legal barriers and will protect the interests of both parties on buyback, and subsequently can absorb more foreign investment into Iranian oil sector at the present time after the removal of the nuclear sanctions. For this purpose, the following chapter will examine the legal anatomy of the Iranian buyback to highlight the deficiency of the model in order to propose the applicable reforms.

Chapter 3: The Legal Anatomy of the Iranian Buyback: Discovering the present practice of the model

3.1 Introduction: The adoption of Iranian model of buyback

As it has been shown in the last chapter nullifying all the previous petroleum deals following the 1979 revolution occurrence led to the foreigners' exclusion from Iranian energy sector and subsequently led to the great disruption of Iran's oil supply. Such actions to remove the foreign oil companies from the Iranian oil industry which stemmed from the event of nationalisation for the aim of nationalising the entire process of oil production to protect the national interest of Iranians caused replacing of Iranians' oil by its traditional importers with other regional sources such as Saudi Arabia and Kuwait¹³⁵. As a result, in order to increase the rate of oil production as the main source of income of the country and considering the prohibition of the Iranian Constitution regarding foreign ownership of the Iranian natural assets, the Iranian government adopted the buyback model as the compromising solution to attract the foreign investors to oil sector, as well as ensuring the Constitutional forbiddance of foreigners. In fact, the introduction of the buyback model was an effort for establishing a method of oil transaction that would attract foreign investment, even with low efficiency, while it preserves the state's right to permanent sovereignty over Iran's natural reserves through the prevention of the ownership of Iran's mineral wealth by foreigners¹³⁶. In spite of the less attractiveness of buyback compared to the Production Sharing Agreement model, offering this model could attract many oil companies to the Iranian oil industry, as contractors desire an alteration in framework of the contract for the benefit of favour of international petroleum corporation, and also, they fear that another oil company may sign the contract instead of them and enjoy the aforementioned alteration in the structure. Therefore, from the legal point of view, the adoption of the model of buyback has stemmed from the existing prohibition Iran's Constitution that avoids NIOC to conclude unbalanced deals in form of concessions to international petroleum corporation in order to protect the ownership of Iran's oil resources. As a result, the buyback financing model

¹³⁵ Bindemann, Kirsten, Oxford Energy Comment, The Middle East Invites Bids by Foreign Oil Companies, December 1999 [http://www.oxfordenergy.org/comment_prn.php?9912]

¹³⁶ Seyed Nasrollah Ebrahimi and Abdolhossein Shiravi, 'Exploration and Development of Iran's Oilfields through Buyback' (2006) 30 Natural Resources Forum: The Constitution of the Islamic Republic of Iran.

became the key element of the Iranian oil and gas transaction, due to the fact that the Iranian government recognised the buyback as an effective mechanism for protecting its sovereignty, as well as absorbing foreign investments.

The first experience of the country in foreign investment in area of petroleum part after Islamic revolution in the form of buyback was related to the agreement between NIOC and Total for the operation of Syry fields¹³⁷. In 1999, IOCs showed more attention to involvement in Iran's oil sector, NIOC offered 31 discovery and extraction schemes which were awarded to Statoil, OMV, Edison Gas, ONGC and Sinopec¹³⁸. Therefore, for the purpose of attracting more foreign investment Iran adopted numerous significant plans within time of the second and the third government in Iran for guaranteeing the safe petroleum contractual framework in favor of IOCs. The key alterations referred firstly to, passing legislation to enable IOCs to register a division within the territory of Iran, adaption of the new system of arbitrational settlement, and finally, an amendment to the law for permission to establish international financial institutes in determined area identified as FTZ in 1999. Nevertheless, the present practice of the Iranian buyback obliges the foreign contractor to provide necessary capital, structures, technology and services in exchange for the contractually pre-agreed rate, approximately 16-18 %, which is received through its worth to the equal amount of the product that was remained. Therefore, under the Iranian buyback agreement, the contractor is entitled to receive compensation from the National Iranian Oil Company through a share of the final product for the price of funding all investments. Thus, Iranian buyback agreements are categorised in a series of "risk service" contracts, as the foreign contractor bears the risk of financing the project, as well as the risk of the oil discovery.

Accordingly, since deliberating the core concept of the Iranian buyback from a legal point of view is significantly essential for the purpose of analysing the current mechanism and also foreseeing the future development of the model, this chapter is aimed at examining the legal anatomy of Iranian buyback. This analysis focuses on the legal concern of the model to determine the most effective alternative for the current mechanism, and also to highlight its

¹³⁷ Lucas Herrmann, Elaine Dunphy et al. 'Oil & Gas for Beginners—a Guide to the Oil & Gas Industry', in Global Markets Research, (London: Deutsche Bank (DB), 2010).

¹³⁸ Wood Mackenzie (2010), "Overview Iran." ; — (2009), "Iran - Country Overview."; Pierre Shammass (2001), "Iran: Review of Petroleum Developments and Assessments of the Oil and Gas Fields," Energy Exploration & Production 19, no. 2&3.

shortcomings from a legal point of view in order to deal with the applicable reforms in the next chapter. Hence, this chapter is comprised of three sub-chapters which are all designed to examine the core concept of the Iranian buyback via the consideration of the present legal function of Iranian buyback. For this aim, the first sub-chapter considers the structure of the Iranian buyback to precisely show the legal function of the model and accordingly will demonstrate the nationally supportive feature of the Iranian buyback against the foreign party, which burdens the high financial risk on the international side. The second sub-chapter deals with the different generation of buyback to evaluate the efforts that have been carried out to offer more balanced version of the model, and more importantly will prove the applicability of the evolutionary approach toward the future of the Iranian buyback which has been chosen by this study over the revolutionary approach to make the model more attractive. The issue of Iranian influential laws on buyback will be considered in the last sub-chapter for the purpose of analysing the effective laws on the current practice of Iranian buyback, in order to highlight the deficiency of the model from this perspective. Moreover, considering the influential laws of Iranian buyback enables this work to point out the legal concern of Iranian buyback which will be employed in the next chapter to suggest the applicable reforms.

Noticeably, missing the examination of legal aspects of Iranian buyback would be a vital gap in this study, and renders the offering of the full picture of the Iranian buyback as incomplete, which impedes this study to predict the future tendency of the model for the purpose of answering the research question of this study.

3.2 The Structure of the Iranian buyback: Bias mechanism in favour of NIOC

The reasons for adapting the buyback model in Iran, despite its harsh mechanism and less attractiveness compared to other models have been discussed in the second chapter of this study. It has been demonstrated in the previous two chapters that the negative historical experience of foreign involvement in the Iranian oil industry as a result of the unfair concessionary agreements led to the nationalisation of Iran's national resources and subsequently all agreements with foreigners were nullified after the Islamic revolution in

1979¹³⁹. Therefore, following the consideration of the roots of the introduction of the buyback this sub-chapter will attempt to examine the structure of the Iranian buyback in order to critically analyse the function of the model in question.

The service contract depends on the nature and level of exploration and production is an agreement between private company and the host government in order to provide particular services for the exchange of the agreed payment¹⁴⁰. Therefore, based on the service contract the international oil company is obliged to offer the host government the necessary facilities, services and information for the aim of developing the oil resources. As a result, the international oil company in this type of oil transactions has been known as a contractor or hire hand working for wages¹⁴¹. Accordingly, unlike the concessions, under the service contract the IOC is not the traditional concessionaire as he is a contractor for the host government that on his own risk performs the necessary activities for development of oil field when there is block discovery. Since based on the service contract the contractor is carrying out the activities on his own risk and will be rewarded only in the event of successful production, this model has been coldly accepted by IOCs. This kind of agreement was practiced for the first time in Latin America, Brazil in 1953 and Argentina in 1958, as the concessionary deals came to the end, as a result of establishment of many national oil companies, as well nationalizing countries' resources¹⁴². The service contract has been divided in to three categories: ¹⁴³

Pure Risk where the contractor is responsible for preparing the required information.

Technical where the contractor has to provide technical facilities.

Buyback where the contractor is enable to buy the final product with agreed discounted price.¹⁴⁴

Vitally, the Iranian buyback has been distinguished over other commonly used petroleum contractual systems, due to its particular provisions regarding the prohibition of direct ownership of the oil product by foreigners which is in line with the existing Iranian constitutional restrictions. Therefore, based on this constitutional prohibition, buyback is

¹³⁹ Manouchehr Takin, "Iran seeks large volume of capital investment to boost upstream action", Oil & Gas Journal, September 13, 1999, volume 97, issue 37.

¹⁴⁰ Peter Cameron, „Managing the politics of oil reforms: Lessons from Iraq“ (Keynote Address at the Oil and Gas in Federal Systems, March 4 2010, Washington DC)

¹⁴¹ Yi Junseog, „Merits and Demerits of the Different types of Petroleum Contracts“ www.knoc.co.kr/servlet/Download?num=6&fno=6. Accessed on 15th February 2017

¹⁴² ibid

¹⁴³ Ernest E. Smith, John S. Dzienkowski, „A Fifty-Year Perspective of World Petroleum Arrangements“ [1989] 24 Texas International Law Journal 13, p 40-42

¹⁴⁴ ibid

the only method of direct investment in the energy industry in Iran for foreign persons or companies. In fact, the buyback is a viable vehicle to justify the involvement of international corporations in the energy sector which also complied with the existing prohibition of the Iranian constitution as the previous president of Iran, Khatami, stated that 'Buyback agreement is the finest choice with consideration of the restrictions that the government is bounded by them'. Hence, the most significant features of the structure of the Iranian buyback is that the foreign party will not share any part of the final product generated in the field, whereas, it is obliged to provide the necessary capital and technical support¹⁴⁵. Hence, the structure of Iranian buyback is designed to protect the national interest of Iran in petroleum deals mainly through banning the foreign ownership of Iranian natural resources. Under the structure of this model the foreign party only acts as a contractor to conduct activities related to the engineering, procurement and construction of the project, and will not be granted the right to possess the petroleum blocks, while it will be compensated on the rate of pre-agreed income through the final product. The main structure of the Iranian buyback model is examined as follows¹⁴⁶:

- a) While the NIOC is banned from transferring any form of right directly or indirectly such as equity, concession and license, it preserves the absolute sovereignty rights over the Iranian resources under any and all circumstances¹⁴⁷.
- b) The IOC undertakes the responsibility of exploration and development activities in the allocated area to reach a rate of production contractually agreed by bearing the risk of no discovery in the field.
- c) The buyback contract consists of two sections: the first part is an agreement to conduct the discovery activities in certain oil fields and the latter is the production and oil sales agreement which are granted separately.
- d) The mutual accepted inspection agency will assess the quality of the materials and equipment used by the IOCs in their operation with binding effect on the parties.

¹⁴⁵ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 175

¹⁴⁶ Petroleum Iran, Iranian oil information portal (<http://www.petroleumiran.com/buy-back.html>) 1st September 2013

¹⁴⁷ Paydar West Field Asmari and Bangestan Reservoirs, National Iranian Oil Company, South Fields .Year 1999. P 3

e) NIOC shall compensate IOC in exchange for its investment and activities in the project in the form of crude oil or natural gas extracted from the same field when the project starts generating income¹⁴⁸.

f) At the final stage, the field will be hand over by the contractor to NIOC after concluding the production activities; however, the contractor is still in charge of providing technical assistance during the operation and production phases¹⁴⁹.

Therefore, based on the structure of the Iranian buyback agreement, although the contractors bear a variety of risks by signing the Iranian buyback agreement including discovery in exploration, inadequate products for the recovery purpose and overrunning the expenses beyond the budget limit¹⁵⁰, they will be compensated in the fixed rate of return payable in the form of crude oil which burdens another risk on the contractors. As a result, the structure of the Iranian buyback is unfairly biased in favour of the NIOC which creates an unattractiveness feature of the Iranian buyback, and subsequently discourages foreign investors from engaging in the Iranian oil sector, which is against the national interests of Iranians. However, this study suggests that offering a more balanced structure of Iranian buyback and considering the current legal and political prohibition can generate more financial incentives to absorb more foreign investment following the removal of the nuclear sanctions.

Consequently, this sub-chapter identified the main elements of the buyback's structure model which can support this study for the purpose of highlighting the unattractive provisions of buyback which create the deficiencies voiced from both the national and international party from the framework of the model such as a fixed rate of return, the short duration of buyback and the separation of the discovery rights from the development rights. Such deficiencies, which resulted from the nationally supportive nature of buyback, will generate a unsafe commercial environment for IOCs operating in Iranian fields and subsequently make the model unable to compete with other commonly used methods in Iran's neighbouring countries. Therefore, this work will employ this analysis to propose applicable reforms within the structure of the model in the next chapter to increase the

¹⁴⁸ Paydar West Field Asmari and Bangestan Reservoirs, National Iranian Oil Company, South Fields .Year 1999. P 4

¹⁴⁹ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 175

¹⁵⁰ Manouchehr Takin, "Iran seeks large volume of capital investment to boost upstream action", *Oil & Gas Journal*, September 13, 1999, volume 97, issue 37.

efficiency of the model by revising the terms to an unfixed rate of return, longer agreements and offering the discovery and production rights together to the contractor. Thus, as this study's strategy is firstly to highlight the unattractive elements of buyback and subsequently provides applicable solutions to reform them in the future development of the model, the next sub-chapter will examine the features of different generations of Iranian buyback to demonstrate the efforts which have been carried out to improve the model, and more importantly to analyse the impact of such efforts on making the buyback more attractive for the purposes of introducing the most applicable alternative to improving the Iranian buyback

3.3 Different generations of Iranian buyback: Inadequate attempts to improve the model

As was mentioned in the last chapter, the Iranian method of transaction is not as attractive as other types of petroleum contractual systems, due to the lack of financial incentives, and also containing restrictive provisions which make the Iranian buyback unable to compete with other models in attracting foreign investment¹⁵¹. Therefore, since the 1979 Islamic Revolution, Iran has issued four generations of buyback contracts which demonstrate the Iranian government's position to render the buyback more attractive for foreign investors, in order to develop the country's economic situation. In fact, these generations have been introduced because Iran realised two vital facts: Firstly, the model is not as attractive as other commonly used mechanisms in Iran's neighbouring countries such as Saudi Arabia, and secondly, the model has the potential to be revised in order to compete with other models in attracting investments. Therefore, there is no need to shift towards another model which has high historical, political and legal expenses. As a result, Iran during the past three decades, conservatively, has attempted to modify the model to respond to all grievances from both sides, as well as ensuring that the commercial environment will become continuously more beneficial to IOCs by proposing a different generation of the model. Therefore, this sub-chapter, following the examination of the structure of the Iranian buyback will analyse the different generations of the buyback to evaluate the progression of the model, and highlight other areas which need to be reformed to make the model more

¹⁵¹ Farshad Gohar, Naser, 'Seyri Dar Gharardadhaye Naftiye Iran', { A Survey On Iran's Oil Agreements) Tehran, 1381, pg 262

attractive. Consequently, this sub-chapter will critically review the four different generations of the model in question and subsequently, points out the required trend of reforming in the future in order to accelerate such revisions and to improve the Iranian buyback.

a) Table one: The First Generation of Iranian Buyback Agreement (1979-1989): Simple mechanism and low economic efficiency

Main Elements	Shortcomings
Fixed Rate of Return	Bearing all Risks on the Contractor
Extremely short length of the contract	Vague in Production stage
Allocating the Exploration and Developments activities in separated Phases and Contacts	Not attractive for IOCs

As has been shown in table 1, the initial group of Iranian buyback agreements were uncomplicated buyback deals amid National Iranian Oil Company as well as an international corporation. This category of buyback was included a pre-agreed rate of return in exchange of provided services by IOC as a contractor. More importantly, there was no guarantee under this generation for IOCs to be the developer of the field, even if they would have found a commercial oil field, as the right to discovery and production activities would be rewarded separately¹⁵². This approach led to a great dissatisfaction amongst IOCs, due to

¹⁵² "roonamayee az avalin gharardad-e finance-e dakheli," Danesh-e Naft, December 1, 2013, accessed: September 10, 2014, <http://www.daneshenaft.ir/cid/CMSContent/content/3887>.

the uncertainty caused regarding the recovering of operation costs and capital investments during the project exploration phase¹⁵³, as well as a lack of financial incentives for the contractor resulting from the short duration of the agreement¹⁵⁴. Accordingly, the first generation of buyback agreements burdened all risks on the contractor and de-motivated them from participating in the Iranian oil industry which subsequently resulted in a loss of national interest in Iran, as the model was not successful with competing with other neighbouring producers regarding the absorbing of foreign investment¹⁵⁵. As a result of such analysis the officials decided to carry out some reforms to increase the attractiveness of the model which led to the introduction of the second generation of the Iranian buyback contracts.

¹⁵³ Farshad Gohar, Naser, 'Seyri Dar Gharardadhave Naftiye Iran', { A Survey On Iran's Oil Agreements) Tehran, 1381, pg 264

¹⁵⁴ Reza Yeganehshakib, Iran's New Generation of Oil and Gas Contracts: Historical Mistrust and the Need for Foreign Investment, *Journal of Political Risk*

¹⁵⁵ Farshad Gohar, Naser, 'Seyri Dar Gharardadhave Naftiye Iran', { A Survey On Iran's Oil Agreements) Tehran, 1381, pg 264

b) Table two: The Second Generation of Iranian Buyback Agreement (1989-1995): Similar to the first Generation

Main Elements	Shortcomings
Fixed Rate of Return	Vague in Production stage
Considerably short length of the contract	Lack of financial incentivise
Allocating the Exploration and Developments activities in separated contacts and phases	Bearing all Risks on the Contractor
Allowing the Contactor to start development phase in the case of successful exploration with discretionary power of NIOC	Not attractive for IOCs

The second table showed that the second generation of the Iranian buyback agreements preserved the main elements of the first generation of contracts including a fixed rate of return, short duration, and granting the discovery rights and production rights in separated legal documents¹⁵⁶. However, the main difference between the first and the second generation stemmed from the fact that in the latter generation the contractors would be

¹⁵⁶ Reza Yeganehshakib, Iran's New Generation of Oil and Gas Contracts: Historical Mistrust and the Need for Foreign Investment, Journal of Political Risk

granted the development phase if they successfully finished the exploration phase. However, the NIOC was granted the discretionary power to award the second contract, therefore, practically, the two different phases of the operation would not be granted in the same contract and the NIOC enjoyed the right to decide to grant the second contract to any of the contractors¹⁵⁷. Hence, the contractor under the second generation was still under the risk of exclusion from the operation, even if the discovery had been successful. This provision, which has been reflected in the current model of the buyback, is one of the main sources of financial risk for the contractor. This study based on the evolutionary approach by reforming the provision of buyback without any clash with the present prohibition suggests amending provisions in order to remove the discretionary power of NIOC in granting the production phase, as well as obliging the NIOC to grant the rights of production and development to any contractor that successfully discovers the oil. Applying such reforms will change the restrictive provisions to a financial incentive that makes the shape of the model more attractive by removing the important risks in favour of the contractor with no clash with the barriers in the current legal atmosphere of Iran.

¹⁵⁷ Farshad Gohar, Naser, 'Seyri Dar Gharardadhave Naftiye Iran', { A Survey On Iran's Oil Agreements) Tehran, 1381, pg 266

c) Table three: The Third Generation of Iranian Buyback Agreement (1995-2010): More contractual obligations for IOC

Main Elements	Shortcomings
<p>Fixed Rate of Return</p> <p>Extremely short length of the contract</p> <p>Conducting both Exploration and Developments activities in one contract at the same time</p> <p>Obligation on providing the cost estimation before the beginning of the operation</p> <p>Including the technology transfer Provision</p>	<p>Lack of clearness in Production stage</p> <p>Lack of financial incentivise</p> <p>Bearing all Risks on the contractor</p> <p>Less attractive for IOCs compared to offered contracts in neighbouring countries</p>

This group of the buyback agreements, table 3, had some dissimilar features the previous generations, as it contained two important legal obligations for IOCs¹⁵⁸. The first one was providing the cost estimation at the beginning of the project which burdens a significant

¹⁵⁸ Petroleum Iran, [<http://www.petroleumiran.com/buy-back.html>] 21 51 May 2013

financial risk on the IOC¹⁵⁹, due to the fact that the expenses of the project may be changed during the operation, and accordingly will not be covered based on this provision. This obligation which has existed in the present model of buyback created a high level of risk for IOCs; however, this study on the basis of the evolutionary approach proposes that the cost estimation can be carried out as the project is running¹⁶⁰. This reform will remove a significant risk for IOCs and subsequently will improve the efficiency of the model in attracting foreign investment which is the aim of Iran after the removal of the sanctions. The latter new obligation in this generation is a transfer of technology which is in line with the main tendency in the Iranian buyback regarding achieving an absolute independency in oil and gas related activities. This tendency, which has been demonstrated in the second chapter of this work, stemmed from the nationalisation of Iranian natural resources and was subsequently reflected in this obligation. This study suggests the revision of this provision in order to change this legal provision with a financial incentive by awarding a tax reduction to any contractor that employs more Iranian workers and engages more with Iranian companies. This revision will ensure the goal of Iran in achieving the absolute independency in the oil industry via the transfer of technology, as well as not burdening any formal obligation on IOCs. Accordingly, the third generation does not only cover the shortcomings of the previous buyback models but also obliged the contractor to provide the cost estimation before the start of the project and transfer the technology. As a result, this generation of the Iranian buyback agreement, in line with the former generations, was not successful in competing with common contracts offered by Iran's neighbours in the field of petroleum in that time, due to the fact that it did not provide any financial incentives for IOCs.

¹⁵⁹ Atieh Bahar, Oil & Gas Market Overview (<http://www.atiehbahar.com/Resources/Oil&Gas.htm>) may 2013

¹⁶⁰ Reza Yeganehshakib, Iran's New Generation of Oil and Gas Contracts: Historical Mistrust and the Need for Foreign Investment, *Journal of Political Risk*

d) Table four: Fourth Iranian Buyback Agreement Generation (2010-2015): Limited reforms

Main Elements	Shortcomings
Fixed rate of return	Bureaucracy
Longer duration of contract through series of successive agreements	Lack of enough financial incentivises
Conducting the Exploration and Developments activities in separated contacts	Bearing most Risks on the Contractor
Priority of explorer contractor in granting the sales contracts with discretionary power of NIOC	Vague in Production stage
	Less attractive for IOCs compared to offered contracts in neighbouring countries

Following the short duration of the last three generations of the buyback model, the most recent generation, the fourth one, attempted to solve this shortcoming of buyback by offering a series of successive agreements which can be roughly 20 years¹⁶¹. This reform,

¹⁶¹ Reza Yeganehshakib, Iran's New Generation of Oil and Gas Contracts: Historical Mistrust and the Need for Foreign Investment, Journal of Political Risk

which has been applied in this version of buyback, might address this deficiency; however, it will aggravate the problem of long negotiations and bureaucracy which is a common complaint among the foreign contractors¹⁶². Therefore, this study, following the evolutionary approach towards buyback proposes the determination of the length of contract subsequent to carrying out the analysis of the volume of the field and the necessary operations to maximise the exploitation of the field. As a result, this solution which does not breach any prohibition, nor will not aggravate the problem of long negotiations and bureaucracy will ensure the benefit of both parties, as it motivates IOCs to employ its highest technology to maximise the exploitation of the field from the national side, and it will remove the risk of uncompensated expenses from the perspective of IOCs. However, under the most recent generation, as was the same as the prior contracts, the contractor is still under the risk of a fixed rate of return, separation of the discovery contract from the production contract and providing the cost estimation before the beginning of the project. Moreover, the fourth generation attempted to address the deficiency of the provision that grants the discretionary power to NIOC to award the development contract to another contractor as opposed to the contractor that successfully carries out the exploration project, which results in the creation of ambiguity and subsequently discourages the IOC in participating in the Iranian oil industry. However, this attempt, compared to the shortcomings of the buyback was considerably insufficient, as most of the shortcomings of the model have not been addressed in this version and this therefore requires more effort to improve the model.

Overall, this sub-chapter examined all the different generations of the Iranian buyback to evaluate the progression of the model and more importantly to assess the efficiency of the changes which have been applied to them. It has been demonstrated that the changes which have been carried out within the buyback is not sufficient to offer a more attractive version of the model. Therefore, the Iranian buyback needs more attempts to be improved in order to compete with other models in attracting foreign investments. The limited reforms that have been applied in different versions of the buyback cannot make the model more attractive, and subsequently Iran would not be able to reach its ambitious goal,

¹⁶² Atieh Bahar, Oil & Gas Market Overview (<http://www.atiehbahar.com/Resources/Oii&Gas.htm>) may 2013

particularly after the lifting of the nuclear sanctions. As a result, Iran is in dire need to conduct more serious reforms within the buyback based on the attitude of the country in the introduction of four versions of buyback which confirms the applicability of the evolutionary approach rather than a revolutionary attitude which potentially breaches historical, political and legal barriers in the current atmosphere of Iran after the removal of the sanctions. Following the consideration of the different generations of buyback and highlighting the Iranian official's strategy in revising the provisions of buyback rather than shifting to another model, the next sub-chapter will examine the effective Iranian laws on buyback in order to point out the shortcomings of the model from the legal point of view and proposes applicable solutions to continue the process of the buyback improvement considered in this sub-chapter.

3.4 The influential Iranian laws regarding buyback transactions: The need to provide clear and certain laws

The second chapter of this work demonstrated that following the 1979 Islamic Revolution the new government nullified all petroleum contracts with foreigners and subsequently replaced the production sharing agreement method by the Iranian model of buyback, as the new constitution banned any ownership of natural resources by foreigners. Thus, considering the prohibitions of the constitution regarding the possession of foreigners in the oil industry, as well as Iran's need for investment to develop its fields and its economy, the buyback model appeared to be the only compromising model to employ. Further to the existing prohibition of the constitution, different sets of regulations have been enacted by Parliament relating to the different issues of buyback which have influenced the current mechanism of the buyback. Therefore, it seems essential to examine the effective laws and their impacts on the model as the aim of this sub-chapter is to highlight the shortcomings of buyback stemming from the relevant laws and, more importantly, to propose applicable reforms to cover the deficiencies, and subsequently increase the efficiency of the model.

a) Iranian Constitution: Prohibition of foreign possession of local reserves

The Iranian Constitution is main legislation regarding the buyback topic which plays the main role in preserving the buyback as a key element of the Iranian oil industry by banning any type of foreign ownership of Iranian natural resources. This provision as has been explained in the last chapter and is a direct reaction to the many years of the exploitative

nature of the concessionary deals in Iran. Article 43 of the Constitution¹⁶³ in this regard expressed that the economy¹⁶⁴ of the revolutionary government will be according to following principles:

- ‘1. Preventing the supremacy of any foreign power regarding Iranian economic position.
2. Highlighting the growth of farming, as well as technological manufactures.
3. Minimising the dependency on foreign imports’¹⁶⁵.

In addition, under paragraph 2 of Article 44¹⁶⁶, the state sector of the economy encompass all large-scale "mother" industries and Iran's most economically significant minerals. Obviously, oil deposits are accurate examples of economically significant minerals which are controlled by the government. Article 45 more explicitly grants the authority of managing national public assets and reserves such as minerals to the government. This article states that: ‘Public wealth and property, such as mineral deposits, seas, oil and gas resources lakes, rivers ..., property of undetermined ownership..., shall be at the disposal of the Islamic government. Therefore, oil deposits belong to the nation, thus, any private possession of them including long exploiting of the energy sources has been prevented via such requirement’. This prohibition of the Iranian Constitution that forbids the energy sources to be possessed by non-Iranians, is an absolute prohibitive Article regarding energy law in the Iranian constitution. In fact, the existing prohibition in this article justifies the practice of buyback as a means of ensuring the sovereignty of the host state. It declares that conferring concessions to foreigners for the purpose of a company’s establishment dealing with trade, manufacturing, farming, technologies or petroleum field operation, is absolutely prohibited¹⁶⁷.

In summary, Iranian Constitution has had the most significant influence on the current type of Iranian buyback by forbidding any ownership, and control of Iranian natural assets and energy sources by non-Iranians which has led to the introduction of the Iranian buyback. Although such a Constitutional prevention has adverse effects on attracting foreign

¹⁶³ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=7&cad=rja&uact=8&sqi=2&ved=0ahUKEwi3r8XEmcfUAhVLbxQKHReEDlwQFghQMAY&url=http%3A%2F%2Fwww.wipo.int%2Fedocs%2Flexdocs%2Flaws%2Fen%2Fir%2Fir001en.pdf&usg=AFQjCNGJrq4Zf_gCPkWFaVhMLFcGadOZ_Yg/ p 13-14/ Access on March 2016

¹⁶⁴ Ute, Christian& Brexendorff, Alexander, 'Investing in the oil & gas Industry', Mena, 2005, P 12

¹⁶⁵ Nima Mersadi Tabari, Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf.(2016) p 177

¹⁶⁶ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=7&cad=rja&uact=8&sqi=2&ved=0ahUKEwi3r8XEmcfUAhVLbxQKHReEDlwQFghQMAY&url=http%3A%2F%2Fwww.wipo.int%2Fedocs%2Flexdocs%2Flaws%2Fen%2Fir%2Fir001en.pdf&usg=AFQjCNGJrq4Zf_gCPkWFaVhMLFcGadOZ_Yg/ p 13-14/ Access on November 2016

¹⁶⁷ [http://www.imnonline.com/imn/iran-info/Government/constitution.html]

investment into the Iranian oil industry, this study does not suggest any change in this provision because such a change would require a fundamental alteration in the Constitution. Moreover, the analysis carried out in the last chapters demonstrated the strong link between this restriction, and the historical, political, and geo-political considerations of the model which showed that the current political and legal atmosphere of Iran is not flexible enough to tolerate such a radical shift to another model. Therefore, choosing a revolutionary reform will have high expenses for the country which is not recommended by this work, particularly considering the time limit of Iran to return to the global oil market. As a result, the alternative that this study offers is based on the current situation of Iran for the future development of the model via applying the evolutionary approach by reforming the restrictive provisions of the model, as well as improving the model via integrating the advantageous provisions of other methods.

b) Iranian Petroleum Laws 1987.1997: Bureaucratic provisions of finalising a contractual deal

The second relevant law to the Iranian buyback is the Iranian Petroleum Law of 1987 and 1997. This law and its updated version in line with the idea of the buyback model which is explained in the Constitution, are ratified to manage the powers of NIOC and the government in concluding petroleum deals with foreign contractors.

Based on this legislation, the Iranian authority is responsible for observing entire petroleum connected activities such as exploration, production and drawing the foundation and responsibilities of the Petroleum Department within the government. As a result, the government has an absolute power over the oil industry in Iran. The updated Iranian Petroleum Law of 1997 permits the Petroleum Department or NIOC to form agreements with "local and foreign natural persons and legal entities". Therefore, to enter to Iranian oil market, a foreign company should partner up with an Iranian company, and also attain the endorsement of Iranian Ministry of Economy. The second term in this Legislation declares the ownership of entire energy resources by Iran's authority, as well as being controlled by the government and administered by the Ministry of Oil¹⁶⁸. Consequently, with regard to the prohibition of foreign ownership of natural resources, the international petroleum

¹⁶⁸ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 180

corporations will merely perform as suppliers of the projects, instead of main leaders. The part 5 of this legislation requires Ministry of Oil to achieve endorsement of Ministries' Assembly regarding all significant contracts to have legal effect¹⁶⁹. The Article declares that significant deal's outcome amid the petroleum department, and international petroleum corporations needs the confirmation of Ministries' Assembly on the basis of petroleum department application. More importantly, this article highlighted the legal limitations imposed by the Constitution; it proclaims that the any agreements settled amid petroleum department of Iran and another government sectors must be entirely in compliance with 77th principle of the Iranian Revolutionary Constitution. Accordingly, based on these provisions, the process of signing a buyback will take a long time, as a result of the unnecessary bureaucratic structure of the Iranian petroleum laws which will lead to a loss of commercial profits for both parties, and the wasting of time and energy¹⁷⁰. Therefore, this study, on the basis of the evolutionary approach highlights the need for an updated version of petroleum laws, with less bureaucratic provisions in order to accelerate the process of finalising buybacks, as well as ensuring the interests of Iranians by preventing a loss of commercial benefits.

c) The Foreign Investment Promotion and Protection Act (FIPPA): Ambiguity regarding the protection of foreign investment in buyback projects

As has been mentioned in the last sub-chapter, the Iranian buyback is a compromising solution to develop the Iranian oil industry by attracting foreign investment to the oil sector which is the main economic goal of Iran. Therefore, for the purpose of absorbing the international investors to the Iranian oil industry the issue of providing sufficient legal protection for foreign investment involved in Iranian buyback projects seems vital. Thus, this section aims to examine the existing legal protections for foreign investment in the legal framework of buyback.

Basically, FIPPA influenced via 1957 LAPFI that followed the same target to absorb and protecting international investments. The FIPPA that is the ruling legislation to international

¹⁶⁹ [www.alaviandassociates.com/documents/petroleum.pdf]

¹⁷⁰ Dunia P. Zongwe, Natural resources for national reconstruction: A new generation of investment contracts, Society of international economy law/ 2016 p 12

investments (FIPPA) including buyback contracts, was approved in 2002 by Parliament¹⁷¹, and is an improved form of the previous foreign investment law, owing to the fact that its definition of 'investment' has been extended, so as to contain a variety of different kind of investments including buyback, which were not represented within LAPFI¹⁷². As a result, the FIPPA widens the scope of the legal protection to, almost, all sorts of outside investments in Iran.¹⁷³ Therefore, many areas which were absent in the LAPFI, such as buyback deals and BOT arrangements can now enjoy legal protection based on the FIPPA.

FIPPA recognised the following relevant categories as foreign investments and accordingly, entitled to enjoy legal protection¹⁷⁴:

- Foreign currency
- Assets of a technological nature
- Equipment and extra portions
- Financial achievement presented to project funding

Per FIPPA the following benefits of being registered as an investor can be highlighted:

- Nationalizing would be only allowed in the time of chasing a local benefit, on the basis of based on lawful arrangements with no discrimination manner, while reasonable reimbursement in the time of before nationalizing has to be guaranteed for instruction's actual price.
- Regulations, including any benefits and exceptions, would affect foreign investors just the same as local participants.
- The local laws of Iran concerning travel of foreign employees would not apply for foreign investors.
- The investor is allowed to select a jurisdiction other than Iran for arbitration; in addition, disagreements between investors and the government are to be settled based on the terms agreed by the parties.
- Foreigner investors are allowed to annually remove their earnings in foreign currency or related goods¹⁷⁵.

¹⁷¹ <http://www.iran-embassy.org.uk/web/page/?jsession=&m=vp&i=58>

¹⁷² Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 182

¹⁷³ <http://www.irvl.net/newforeigninvest.htm>

¹⁷⁴: <http://www.irvl.net/newforeigninvest.htm>

¹⁷⁵ Ule, & Brexendorff, *op.cit.*, p. 14

Although the Foreign Investment Promotion and Protection Act is an improved form of the previous foreign investment law, it still suffers from a great vagueness in relation to the existing constitutional limitations regarding the involvement of a public authority in the arbitration process. This vagueness stems from the fact that the Iranian Constitution ruled that any involvement of a public authority in arbitration requires approval from the Parliament. As a result, based on this provision, the foreign contractor is only able to apply the provisions of the contract's arbitration if the participation of the public entity has already been confirmed by Parliament. Despite granting dispute-resolution procedures, FIIPPA gives significant discretion to Parliament, and subsequently this lead to greater doubts for foreign contractors concerning the security of their investments. Therefore, under the provision of the FIPPA, it is not clear that the right of the foreign contractor in a buyback project to access arbitration in the event of a dispute has been protected which accordingly creates a high level of confusion and, more importantly, a disincentive for the foreign party. The solution that this study suggests, based on the evolutionary approach towards the issue of buyback, is to cover this deficiency by applying a flexible interpretation of the constitutional provision to remove the discretionary power of Parliament and to change the approval requirement to the advisory view of the NIOC. Carrying out this reform, which does not breach any legal provision, will provide a strong protection for foreign contractors and subsequently will attract them to participate in the Iranian oil industry by removing the above mentioned ambiguity¹⁷⁶.

Further to the above-mentioned obscurity of FIPPA, this act has not clarified whether the direct investment in upstream oil projects are protected by this provision, even though FIPPA¹⁷⁷ provides a broad range of protection for foreign investments compared to the last foreign investment law (LAPFI). Article 2(d) of FIPPA¹⁷⁸ requires protection to be expanded into "Crude oil and natural gas" projects as in theses projects international investors might not directly fund the projects¹⁷⁹. Therefore, although downstream oil projects are under the scope of above mentioned shield because of circumstances of upstream projects that are

¹⁷⁶ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*.(2016) p 185

¹⁷⁷ www.investiniran.ir, accessed 24 October 2013

¹⁷⁸ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKEwi4gaPJmMfUAhXlBxQKHeo3Bb0QFggIMAA&url=http%3A%2F%2Fen.seo.ir%2FLoadFile.ashx%3FId%3DvYhWA31_23SNDIGmT8WVeQ%3D%3D&usg=AFQjCNERscyn4RzZeGwALx-tl2uwctH5g/ p 2/ Access on December 2016

¹⁷⁹ Ule & Brexendorff, *op.cit.*, p. 32

entirely different, as such projects require direct investment for oil exploring and findings which, accordingly, would lead to uncertainty in the foreign contract in this regard¹⁸⁰. Accordingly, the FIPPA provides legal protection for a certain limit of direct foreign investment into exploration¹⁸¹. However, it is still vague as to how FIPPA would protect upstream buyback projects, as the related provisions specifically reference downstream projects within this context¹⁸². The reform that this study proposes makes the model more attractive by removing this shortcoming and providing a more clear and precise legal provision of the FIPPA via including the upstream projects in this act in order to assure the foreign contractors that their investment is fully under the legal protection of the Iranian FIIPPA legislation. Such a reform, in accordance to evolutionary approach, does not breach any legal barriers in Iran and will motivate foreign investors to engage with the Iranian oil sector by offering a more attractive version of the buyback from a legal point of view¹⁸³.

d) Bilateral Investment Treaties: Vague process of dispute settlement body

In addition to FIPPA, Bilateral Investment Treaties (BITs) have effects on foreign investment in Iran, as according to the information on the OIETAI's website¹⁸⁴, Iran is presently member of fifty eight Bilateral Investment Treaties¹⁸⁵. The Bilateral Investment Treaties follow a number of goals such as motivating the trend of funds in different states¹⁸⁶, generating and upholding 'favourable circumstances to financial fund of a project in a state other than investors' country, as well as intensifying 'economic cooperation to the mutual benefit of' contracting parties. The legal provision of 'Fork in road clause'¹⁸⁷ is the main benefit of these agreements, which allows the claimant investor to select the place of judicial system in event of dispute. Therefore, investors are able to decide under which judicial system disagreement will be heard, which is crucial for outside investors in Iran because of the constitutional restrictions. However, Article 139 of the Constitution requires the

¹⁸⁰ Alexander Brexendorff et al., 'The Iranian Buy-Back Approach' (2009) 7 Oil, Gas & Energy Law Intelligence (OGEL) pg 9-10

¹⁸¹ Hooman Farnejad, 'How Competitive Is the Iranian Buy-Back Contracts in Comparison to Contractual Production Sharing Fiscal Systems?' (2005) OEG; pg 16

¹⁸² Ute & Brexendorff, op.cit.,p.32

¹⁸³ Dunia P. Zongwe, Natural resources for national reconstruction: A new generation of investment contracts, Society of international economy law/ 2016 p 27

¹⁸⁴ <http://investiniran.ir/investmenguide-treaties-en.html> accessed 19 November 2013.

¹⁸⁵ <http://icsid.worldbank.org/ICSID/FrontServlet> accessed 20 November 2013.

¹⁸⁶ <http://www.unctadxi.org/templates/docsearch.aspx?id%7794> accessed 19 November 2013.

¹⁸⁷ Schreuer, 'Travelling the BIT Route of Waiting Periods, Umbrella Clauses and Forks in the Road' (2004) The Journal of World Investment & Trade 231, 239-49.

confirmation of both the Ministries' Assembly, and Parliament for the involvement of all governmental bodies in any dispute resolution. As a result, there is a great confusion for foreign investors operating in the Iranian oil sector regarding choosing the forum for dispute resolution which creates an unattractive feature of the model¹⁸⁸. This study proposes a flexible interpretation to solve this confusion. As the BITs are confirmed by the Guardian Council of the Constitution, there is no need to apply Article 139 of the Constitution. Consequently, there is no need for any separate approval when disputes arise between NIOC and the foreign contractors. Thus, foreign investors can enjoy the flexibility to select a dispute settlement body¹⁸⁹.

Overall, this sub-chapter examined the impact of influential laws on the current mechanism of Iranian buyback, and accordingly demonstrated that the most applicable alternative for the future development of the model considering the current Constitutional prohibitions are employing the evolutionary approach rather than any shift to another model which allows the ownership of oil products by foreigners¹⁹⁰. More importantly, analysing the Petroleum Laws, FIPPA and BITs highlights the shortcomings of the Iranian governing law of buyback which stems from the vagueness of the Act, and also points out the applicability of the evolutionary approach to remove such deficiencies within the model that demotivate foreign investors, whereas clear and certain laws can attract foreign contractors. As such, laws provide an advantage to foreign contractors in order to understand the function of laws and to anticipate the methods by which the laws will protect their investment¹⁹¹. Moreover, enacting more clear and less vague laws will minimise the risk of investing in Iran's oil industry which is an important concern for foreign investors, as the contractor can estimate all probable legal situations during the operation of a project. Accordingly, for the sake of making the buyback more attractive Iran needs to enact, and revise the related laws, and the investment laws in particular, to provide more certainty and clearness, so that contractors can rely on those provisions and consider investing in Iran over other oil producing countries. In other words, Iran must guarantee the protection of international investors' capital operating within petroleum market enacting clear and specific provisions.

¹⁸⁸ Nima Mersadi Tabari, *Lex Petrolea and International Investment Law: Law and Practice in the Persian Gulf*, (2016) p 191

¹⁸⁹ Dunia P. Zongwe, *Natural resources for national reconstruction: A new generation of investment contracts*, Society of international economy law/ 2016 p 32

¹⁹⁰ Alexander Brexendorff et al., 'The Iranian Buy-Back Approach' (2009) 7 *Oil, Gas & Energy Law Intelligence (OGEL)* pg 9-10

¹⁹¹ Hooman Farnejad, 'How Competitive Is the Iranian Buy-Back Contracts in Comparison to Contractual Production Sharing Fiscal Systems?' (2005) *OGEL*; pg 16

This is the solution that this study proposes, in line with the evolutionary approach, in order to make the Iranian buyback more competitive, especially in times of price falls and when there is high competition amongst producers.

3.5 Conclusion: Inaccuracy of radical shift in future development of the model

Analysing the legal anatomy of the Iranian buyback in this chapter demonstrated the constitutional prohibitions regarding foreign possession of Iranian energy sources, as well as set out reasons for the adoption of the Iranian buyback via relevant laws' perspective. This model, which has stemmed from the idea of nationalising Iranian energy sources was in accordance with national interest protection application against foreign parties in petroleum deals. Such a nature in this chapter has been recognised as the root of many unnecessarily restrictive provisions in the current buyback, including a fixed rate of return, which created a significant financial risk for foreign contractors. Furthermore, examining the four generations of Iranian buyback proves the necessity of revising the model, an insufficiency of efforts that have been carried out for the aim of modernising the model, and more importantly the applicability of employing the evolutionary approach with a legal consideration of the buyback, and based on political realities to increase the efficiency of the model. Moreover, although a consideration of the effective laws on Iranian buyback illustrated that applying the revolutionary approach to shift towards any model that contains foreign ownership of oil products will be confronted by the constitutional prohibitions, there is a necessity to provide less ambiguous and more certain provisions in the related laws of Iranian buyback to minimise the legal risk for foreign contractors operating in Iranian oil fields. Hence, considering the legal anatomy of the buyback demonstrated the applicability of evolutionary reforms towards the future tendency of the model rather than any shift to another method. Consequently, this chapter by examining the Iranian buyback from a legal perspective showed the applicability and efficiency of choosing evolutionary reforms to revise the unattractive legal elements of the model, and accordingly make the model more competitive. Therefore, the fourth chapter of this study will utilise the analysed functions of the Iranian buyback to offer applicable reforms on the basis of the evolutionary approach that do not clash with any historical, political and legal concerns which have been considered in the first three chapters of this work.

Chapter 4: The Critical Dissection of Iranian Buyback: Employing the evolutionary approach

4.1 Introduction: The necessity of improving the Iranian buyback

A reduced worldwide economic growth, especially in China, an increase in the number of oil producers, such as the US and Brazil, and the failure of OPEC members to agree on a deduction of the rate of production resulted in an oversupply of oil in the global markets and subsequently resulted in declining the global price of petroleum production, as well creating a high level of competition amongst producers in the past five years. Moreover, the imposed EU, US and UN sanctions on Iran's oil industry, in order to restrict the nuclear programme of Iran, significantly lessened the rate of Iranian oil production as the main source of the Iranian budget, due to the fact that investing in the Iranian oil industry on the basis of an unattractive model of buyback would not have any business visibility for foreign oil companies after the sanctions¹⁹². Accordingly, during the past five years Iran's economy, and more particularly the Iranian oil industry, has suffered greatly, as a result of the above-mentioned facts which made the Iranian government determined to actively attempt to attract foreign investment to the oil industry by offering a more attractive version of the buyback following the successful lifting of the nuclear sanctions. Furthermore, the necessity of offering a more attractive model of the buyback even before the imposition of the nuclear sanctions has been proved in the last chapter via an analysis of the four generations of buyback¹⁹³, and more importantly the ineffectiveness of the employed reforms have been clarified, even though, such an analysis in the last chapter confirms the applicability of the evolutionary approach which has been chosen by this study regarding the future of the Iranian buyback.

As a result, considering the massive need for Iran to improve the efficiency of its methods of oil transaction¹⁹⁴ this chapter, following the recognition of the historical, political, geo-political and legal concerns of buyback in the last three chapters of this study, highlights the evolutionary reforms as the applicable alternative for the future development of the model

¹⁹² Payvand, 07/04/2010 [<http://www.payvand.com/news/01/jul/1013.html>]

¹⁹³ M. Bunter, The Iranian Buy Back Agreement, OGEL Journal, Dundee Vol. 3 - issue 1, March 2005, P 6-8

¹⁹⁴ Alexander Brexendorff et al., 'The Iranian Buy-Back Approach' (2009) 7 Oil, Gas & Energy Law Intelligence (OGEL), P 9

and it will attempt to employ such an approach in order to provide the applicable reforms within the framework of the Iranian buyback to improve the function of the Iranian buyback. This is the gap in many similar researches on the issue of Iranian buyback, as they only examine the current mechanism of buyback including its shortcomings, while this study recognises the consideration of the models' future tendencies as the final outcome of this work by offering a vast analysis of Iranian buyback. Therefore, this chapter, which is divided into eight sub-chapters, will highlight the deficiencies of the model from the perspective of both parties' criticisms in the first sub-chapter and more importantly will offer applicable reforms on the basis of the evolutionary approach to cover their concerns, and accordingly make the model more competitive. The second, third and fourth sub-chapters will highlight the shortcomings of the model by carrying out a critical comparison of the Iranian buyback with production sharing agreements, service contracts and the international scheme of buyback respectively. Moreover, these three sub-chapters are designed to integrate the advantageous provisions of the above-mentioned models to the Iranian buyback that do not breach historical, political and legal barriers in Iran's current situation to revise the unattractive provisions of the Iranian buyback. The fifth sub-chapter deals with the proposal of applying production sharing agreements for the northern oil fields of Iran to examine the applicability of this model in the current political and legal environment of Iran, and will clarify that any shift to another oil transaction method even regarding a specific geographical area will confront serious barriers in Iran. Thus, such a revolutionary approach will not be applicable, particularly considering the time constraints for Iran to return to a strong position in the global oil markets. The influence of international sanctions on the Iranian oil industry will be dealt with in the sixth sub-chapter, and the dire need to remedy the adverse effects of such sanctions by utilising the evolutionary approach will be discussed. The influence of the recent nuclear deal which led to the lifting of the sanctions on the Iranian oil industry will be reviewed in the seventh sub-chapter, and it will be shown that Iran cannot reach its ambitious plans to increase its oil production, unless serious reforms have been done within the current framework of the model. The sub-chapter eight offers the comparison of the present buyback with a new version and will highlight the efficiency of the carried out changes. The last sub-chapter will deal with the issue of asymmetric data with regard to the shift of NIOCs customers from the EU to India and China, and confirms the crucial need of Iran to establish a research institute within NIOC to

organise and analyse the information with the aim of accelerating the process of oil production.

4.2 Deficiencies of the Iranian Buyback Agreement: Criticisms of buyback from national and International party's perspective

The core concept of the Iranian buyback with its mechanism has been discussed in the last chapter of this work which demonstrated that the Iranian buyback's mechanism could not compete with other common models in the region. This is because of the fact that the production rate of Iran did not increase in competition with its neighbors such as Saudi Arabia and Iraq which led to Iran's position in OPEC as the third producer being replaced by Iraq¹⁹⁵. Therefore, the Iranian buyback is not as attractive as other commonly used methods amongst oil producing countries which comprises the main question of this study, namely to discover effective alternatives for the present model. It should be noted that the long period in which the buyback has operated in Iran as the key element within the Iranian oil contractual legal framework has brought plenty of criticisms from both sides, which can be examined as a relevant source in order to highlight the deficiencies of the model and to analyse in order to increase the efficiency of the model. As a result, for the purpose of focusing on the issue of improving the nature, and subsequently enhancing the efficiency of the Iranian buyback in attracting foreign investments, it is essential to devote special attention to the criticisms voiced by international oil companies, as well as domestic parties, especially in this significant period after the lifting of sanctions, and when Iran is in dire need of attracting foreign investments to successfully return to the global oil market¹⁹⁶. Accordingly, this sub-chapter will consider the criticisms received by both parties in three distinct sections, named as the criticisms stemming from the contractual framework of buyback, the political considerations and the incomplete provisions of the model in order to highlight the shortcomings of the model, and more importantly to propose applicable solutions based on the evolutionary approach in order to respond to their complaints and making the model more attractive.

¹⁹⁵ Farnejad H., Strategic Approach & Legal Implications of Investment in Geopolitically Sensitive Iran P 19-21

¹⁹⁶ M. Bunter, The Iranian Buy Back Agreement, OGEL Journal, Dundee Vol. 3 - issue 1, March 2005, P 6-8

4.2.1 Contractual framework of buyback: Unnecessary restrictive provisions

As has been analysed in the second chapter of this work, the exploitative nature of the concessions resulted in public discontent, nationalisation of the Iranian natural resources and subsequently the introduction of the buyback model which includes a harsh framework with restrictive provisions. In fact, the main tendency in the framework of the buyback is to support the national party against the foreign contractor which has been reflected in different provisions including the length of the contract, the cost estimation, fixed rate of return, distribution of the exploration and production stage, the registration of foreign companies in Iran, the regulation of insurance and employment and business preference regulations which all will be examined in this section. Therefore, this section will examine the deficiencies of the Iranian buyback in ten sub-sections to highlight the criticisms of both parties regarding the structure of buyback, and more importantly to offer applicable solutions to make the model more competitive by responding to the complaints of the parties.

a) Length of contract: Further risk for both parties' interests

As has been shown in the first chapter of this work, the long duration of the concessions which was in line with the exploitative nature of the concessions has played the main role in the short duration of the current buyback. Since the domestic party in the buyback contract intends to restrict its ownership responsibilities, the contract's length would be shorter than the scope of the required effort which is only about seven to ten years, including extra 60 months for the time of cover of fund. The risk to the limitation of the duration for IOCs is that the amount of extracted oil agreed on the contract may be broken in the event of an oil price fluctuation, before the IOC is fully compensated. Therefore, the short length of the contract has an important commercial risk for the international contractor of not being fully compensated for operating in Iranian oil fields¹⁹⁷.

¹⁹⁷ Iran Energy Data, Statistics and Analysis - Oil, Gas, Electricity, Coal. [<http://www.eia.doe.gov/emeu/cabs/iran/pdf.pdf>]

On the other hand, from the NIOC's perspective the short duration of buyback will raise the issue of the partial transferring of capital and technology for the proposed project, as the time limitation prevents NIOC from obtaining as much "new-tech" from the foreign partner as it should. In addition, the application of the "new tech" could have its greatest benefit for NOIC within time of declining stage operation which foreign partner had left the project¹⁹⁸. More importantly, the short length of the contract cannot offer any incentive to either NIOC or IOC for operating the high performance of the field as Statoil's Representative expressed that "some incentives are needed in buyback. If you do a good job you should be awarded and if you do a bad job there should be no more cooperation¹⁹⁹." Accordingly, the short duration of the buyback is one of the unnecessary restrictive provisions of buyback which acts against the interests of both the national and international party, and subsequently has been criticised from the perspective of both the domestic and foreign party, as they both intend to maximally exploit Iran's natural resources through selling product when the project is under maximum operation of the contractor. The solution which has been suggested by some researches to cover the shortcoming of the duration in buyback, and ensure that the contractor is fully compensated is by applying the term of 'carry over' which allow oil contractors to obtain more amount of product when the provisional quantity is not sufficient²⁰⁰. However, this solution will require extra negotiations in order to ensure that such provisions' existed in the contract which will increase the bureaucracy of establishing the buyback. Establishing a couple of following agreements for enabling IOCs for using the previous project assets for purpose of financing the latter contract is another solution to cover the limitation of the contractual duration, and create a financial incentive for both parties. However, this study by following the evolutionary approach claims that this component of buyback essentially needs to be revised, due to the fact that the principle of deals easiness is applicable for decreasing expenses, as well as required period of finalizing a petroleum deal. Consequently, the solution which present study offers in accordance to the evolutionary approach is increasing the duration of the buyback based on the carried out mutual geological studies of the field capacity, precise estimation of the required operation of the field, the reasonable time to maximizing the production rate and fully transferring of

¹⁹⁸ [www.petroenergyinfo.net/News View.aspx?GroupId=5&MnuId=6&NewsId=26603&Page= 1]

¹⁹⁹ [http://www.payvand.com/news/06/apr/1186.html]

²⁰⁰ Alexander Brexendorff et al., 'The Iranian Buy-Back Approach' (2009) 7 Oil, Gas & Energy Law Intelligence (OGEL), P 9

technology besides the contractor's proposal regarding the length of contract to determine the appropriate duration of each buyback agreement. Such scheme will motivate the contractor to utilise its highest technology and efforts to exceed the rate of production, as well as enable the national side to enjoy the complete transfer of technology. Noticeably, this reform, which will respond to the significant deficiency of the buyback by providing the required response for parties' criticism, will make the buyback more attractive with no clash with any current legal prohibitions in the political, legal and historical atmosphere of the country; moreover, it supports the interest of NIOC by providing adequate time for the aim of transferring the technology.

b) Cost estimation: No Financial vision

The basis of the buyback contracts requires the IOC to precisely document all costs and possible returns from the certain field, which will be subsequently utilised as the main source of evaluation of compensation²⁰¹. This provision which has been showed in the first two chapters of this work stemmed from the unbalanced terms of the concessions particularly regarding the income of the parties which results in a further unnecessary risk for the IOC. This is because of the fact that it is difficult for IOC to precisely predict a number of factors such as the required time for production, the extent of oil reserves, production expenses and productivity rates. Moreover, an additional risk will occur when the project costs are greater compared to original estimation which make petroleum corporations responsible for covering differences. Furthermore, events outside petroleum corporations' estimation including radical changes in oil prices may lead to the creation of serious difficulties for IOCs, as they are obliged to use a limited amount of oil in order to cover the expenditures and agreed return²⁰². Therefore, since the Iranian buyback contract did not take such commercial contingencies to the concern, it failed to apply the consistent arbitrational settlement that can motivate overseas participation. As a result, the provision regarding the necessity of the cost estimation before the beginning of the production activities burdens another risk on the contractor in the buyback agreement. In fact, the

²⁰¹ Maximilian Kuhn and Mohammadjavad Jannatifar, Foreign direct investment mechanisms and review of Iran's buy-back contracts: how far has Iran gone and how far may it go? *Journal of World Energy Law and Business*, 2012, Vol. 5, No. 3, P 221-222

²⁰² N. Mohammad, The New Face of Iranian Buyback Contract: Any hope for Foreign Investment? *OGEL Journal*, Dundee, Vol. 7 - issue 1 April 2009, P 12

strategy of the current buyback is regarding the cost estimation issue is applying closed capex which can be a great risk for contractors in the event of increasing the prices. However, this study for the purpose of removing such risk proposes the idea of open capex in order to allow the contractor to provide the cost estimation for every step of the production activity. Hence, the unnecessarily restrictive provisions of pre-cost estimation, which does not have any commercial point will be changed to a continuous cost estimation that can remove the risk in favour of the foreign contractor, as well as provide a more precise and realistic estimation for the NIOC with no breach of any legal prohibitions.

c) Fixed rate of return: Vulnerability of parties in the event of the oil price fluctuation

A fixed rate of return is an adverse policy in upstream operations from both parties' perspective, as it cannot contain the change of oil price which forces another risk on parties. This provision, similar to the provision of the cost estimation which has been shown in the second chapter, stems from the concern of Iranians to an unbalance in the profit of the parties in the concessionary deals which now creates a bias term against the foreign contractor. In fact, the result of applying this provision is that the IOCs may not use their highest techniques in facilitating further discoveries to improve the performance of the total returns from the field²⁰³, as the rate of return is the same at the end of the production activities. Moreover, the IOC argued that the negative movement of the oil market means that the fixed quantity of explored oil may not be adequate for repaying project costs and the agreed return rate²⁰⁴ which is the vital financial risk for the operator. However, unlike the IOC's claim, the NIOC asserts that there is no actual price risk on IOCs which discourages IOCs to improve the efficiency of the operation, owing to the fact that the NIOC's liability for price reduction will be drastic in the event of these radical changes occur, as the National Iranian Oil Company has to offer a higher quantity of oil to accomplish the reimbursement provision²⁰⁵. In fact, the fixed rate of return also creates a risk for the NIOC, particularly in the situation of the price fluctuation, as it has to compensate the contractor, even if it could not generate the income.

²⁰³ Farnejad H., Strategic Approach & Legal Implications of Investment in Geopolitically Sensitive Iran P 19-21

²⁰⁴ Usually 15-18 percent.

²⁰⁵ Iran Energy Data, Statistics and Analysis - Oil, Gas, Electricity, Coal.
[<http://www.eia.doe.gov/emeu/cabs/iran/pdf.pdf>]

The solution of the present study for this unattractive provision is enacting a flexible rate of return based on the potential production rate of the field, cost estimation of the contractor and the price of oil in the global market which can be integrated from the PSA model. In this scenario the flexible rate of return will be a more attractive provision for the foreign contractor, as well as ensuring the national interest of the NIOC by minimising the above-mentioned risks without breaching any legal, political and historical concerns.

d) Distribution of exploration and production stages: Lack of financial incentive

The exploration rights under the buyback depends on the commercial discovery. As has been mentioned in the third chapter, the legal framework of the Iranian buyback has been framed in favour of the national interest. Therefore, the exploration rights have been divided from the production rights in order to grant more bargaining power to the NIOC to select different contractors with more favourable conditions for different phases of the project. On the contrary, this provision includes a damaging effect for the Iranian side, as it creates longer negotiations and a higher level of bureaucracy for different phases with different contractors which will lead to a long delay in conducting the production activities which will result in a loss of benefits for both parties in the buyback. Although the priority of the contractor of the discovered block to conduct the development activities is recognised under the buyback, NIOC is able to reject the terms of the proposed offer, as it is not obliged to accept the IOC's request on the basis of its granted discretionary powers. The effect of this provision is demotivating foreign investors from participating in the Iranian oil industry, due to the fact that they are informed that they might be excluded from the project after the discovery phases. In fact, IOCs are not guaranteed any other further rights which acts to discourage IOCs from investing in the Iranian fields.²⁰⁶ The reform that this study suggests, based on the evolutionary approach, is changing this provision to oblige the NIOC to offer the production stage to any contractor that has made a larger discovery in the quickest time. Such a change does not breach any legal prohibitions, and will shift the unattractive term of the buyback to a financial incentive which serves the benefit of both parties in the contract, as the production activities will begin quicker.

²⁰⁶ N. Mohammad, The New Face of Iranian Buyback Contract: Any hope for Foreign Investment? OGEL Journal, Dundee, Vol. 7 - issue 1 April 2009, P 12

e) Registration of foreign companies in Iran: Bureaucratic processes

As has been mentioned in the second chapter of this work the main tendency in the formation of the Iranian buyback provision is defending the national interest of Iranians in petroleum deals which is the direct result of the exploitative concessions. Therefore, the Constitutional principle of Iran which deals with operation, as well as foreign business's registration has²⁰⁷ banned the registering, and conducting of foreign businesses inside the Iranian territory. This Article states that the establishment of companies or institutions for the purpose of trade, manufacturing, farming, technologies or energy sources discovery inside Iran by foreigners is absolutely forbidden. Therefore, the solution of non-Iranian businesses willing for operation within Iranian oil industry is to establish the firm beyond the country of Iran in order to consequently nominate an authorized branch inside Iranian borders for the only aim to conduct concluded deal with Iranian partner. However, a careful consideration of this constitutional prohibition demonstrates that the proposed solution to establish the firm beyond the Iranian territory for nominating an authorized branch inside Iranian borders will increase level of bureaucracy for any legal actions which is one of the undesired features of the Iranian buyback that results in a loss of commercial benefits for both parties in the buyback agreement, as it burdens unnecessary expenses on the parties, and also creates delays in the development of the project.

The reform that this study proposes is based on the evolutionary approach towards buyback and allows the foreign company to establish a branch in Iran, while it requires the foreign company to devote a certain percentage of the company's equity to the Iranian Government in return of enjoying the tax reduction. This is because of the fact that such flexible interpretation of the Constitution can be applied if the government has equity in the company, so that, the company will not be considered as a foreign entity. This solution does not clash with the above-mentioned Constitutional prohibitions, moreover, the government can observe the functions of the foreign company for the purpose of protecting the interests of Iranians, and more importantly, the level of bureaucracy in buyback projects will be significantly decreased, which is in the favour of both parties' interests.

²⁰⁷ http://www.oefre.unibe.ch/Maw/icl/irOOt_.html access on 2013

f) Regulation of insurance: Unfair obligation for foreign contractor

Basically, the high value of the structures and machinery being employed in oil and gas projects requires significant insurance protections in order to prevent uncompensated damage to the bundle of risks²⁰⁸. The Iranian buyback, regarding the issue of insurance focuses on local solutions provided under the wing of NIOC rather than foreign parties. This position which has been shown in the second chapter of this study stemmed from the nationalisation event that aimed to obtain the full independence of all oil and gas related activities via nationalising the entire process of oil exports. Article 12 of the Iranian buyback defines a general obligation for the contractor to preserve insurance coverage or, if it is easier, for NIOC to offer insurance coverage at the contractor's cost by stating that the contractor shall uphold insurance coverage in amounts needed, and NIOC can use choice of offering such coverage on IOC's expenses which will not be higher compared to price of market elsewhere²⁰⁹.

Accordingly, this provision is in line with the essence of the Iranian buyback which aims to serve the interest of Iranian insurance companies, and subsequently the national Iranian interest which can be in contrast with the benefits of foreign companies, as they might find a better deal offered by non-Iranian companies. In fact, such a bias provision towards the favor of NIOC makes the shape of the model unattractive to foreign contractors by burdening unfair obligations on them which creates a financial risk for the foreign party. The reform that this study suggests, according to the evolutionary approach is shifting this unfair obligation to a financial incentive such as offering tax reductions to any foreign contractor that signs the insurance contracts with Iranian insurers. As a result, applying this reform which does not breach any current legal prohibitions in Iran, can ensure the Iranian government's objective of supporting the national insurance companies; as well as changing this unattractive provision of the buyback to an attractive provision by removing the mentioned obligation and offering some financial incentives.

²⁰⁸ Ule, C and Brexendorff, A, op. cit., p 39-40

²⁰⁹ Mabadi, Legal Strategies in Upstream oil and gas contracts to attract Investment: Iran's case. LLM Dissertation. Faculty of Law. University of Shahid Beheshti. 2008

g) Employment and business preference regulation: Forcing the foreign contractor to employ Iranian workers

The lack of expertise and technology as has been discussed in the second chapter of this work were the two main reasons which resulted in the collapse of the Nationalist Government. Moreover, economy situation of the country are deeply related to global price of petroleum product, as well as government's capability of exporting them. Such oil domination negatively impacts on the country's economy, as development of other industries other than petroleum for the purpose of commercial weakness reduction is also dependent on the oil industry²¹⁰. Therefore, the issue of local content, and in particular providing sufficient expertise, has been reflected in the current mechanism of buyback by provisions regarding transferring the technical expertise from the foreign contractor to the Iranian workers. As a result, NIOC mandates particular employment ratios and preferences in order to conduct the transfer of technical expertise by 'on the job' training of Iranians together with foreign specialists. Article 13 of the Iranian buyback contract draft establishes a preference for the employment of Iranian nationals by foreign companies in projects related to the buyback contract which is aimed at benefiting Iranian workers, and subsequently the Iranian economy by reducing unemployment rates, and generating income for the country. Article 13.1 expresses that the IOCs must priorities the local workers to engage to the operation of projects, and also limiting non Iranian employment rate for jobs that experienced local workers do not existed²¹¹. Moreover, for employing foreign personnel in Iranian fields, the foreign company is obliged to show that a foreign worker contains special knowledge which do not existed within Iranian workers. As a result, the final goal of the article is ultimately substituting foreign personnel by Iranian employees. Further to the above mentioned provisions which are focused on employing Iranian people by foreign contractors, Article 24 relates to the business involvement of foreign parties with Iranian companies, especially regarding purchasing equipment by expressing that the contractor shall employ the service of Iranian companies in line with terms of highest utilisation of national products during operation activities regarding Iranian law²¹².

²¹⁰ Dominique Bruhn, Space for local content policies and strategies, Investment Law and Policy at the Columbia Centre on Sustainable Investment, 2016, p 23

²¹¹ Yelena Kalyuzhnova, LOCAL CONTENT: CONCEPTS, PERSPECTIVES AND ECONOMY, 2016, P 112

²¹² Farnejad H., Strategic Approach & Legal Implications of Investment in Geopolitically Sensitive Iran Pp 19-21 (Unpublished LL M Dissertation & PhD Progression submitted to CEPMLP, Dundee, 2006).

Accordingly, these above-mentioned provisions are intended to protect the national interest of Iranians in the concept of local content by employing Iranian workers, creating skilled technicians and engaging the national companies with foreign contractors. However, passing such legislation which favours the Iranian side in buyback contracts will not support the Iranian governments' objectives of developing the national economy, as this legislation will act to discourage the foreign contractors from investing in the Iranian oil industry by forcing them to fulfil such requirements²¹³. Therefore, the forcing nature of these provisions which is in contrary to the principle of party autonomy as the essence of any agreement, is an unattractive element of the Iranian buyback. This study offers to apply an evolutionary reform in this regard by awarding financial rewards for any contractor that employs Iranian people or carries out business with Iranian companies. This reform will remove the biased obligation of foreign contractors as a financial risk, and subsequently revise the unattractive feature of the above-mentioned provisions. Moreover, from the Iranian perspective, this reform will support the position of the Iranian government in its attempt to provide expert workers, boost the Iranian companies' businesses and subsequently develop the national economy via absorbing more foreign investment into the country.²¹⁴ Consequently, fulfilling such a change can make the model more competitive with other mechanisms in attracting investors by shifting the bias obligation to a financial incentive with no need to either shift towards another method or by breaching any legal and political prohibition.

h) Taxation of foreign entities: High level of confusion as a result of bureaucratic processes

Considering the buyback model as a method of financial transaction to develop a certain oil field shows the importance of examining the issue of taxation of foreign oil contractors in Iran. This is because of the fact that the topic of taxation is in the heart of every fiscal system which can determine the commercial viability of the contract. Thus, the high cost of oil production activities, as well as the IOC's intention to boost their revenue demonstrates the necessity of analysing the Iranian regime of taxation regarding foreign oil companies

²¹³ Economic Efficiency and Optimal Contractual Design of Oil Service Contracts: The Cases of Iran and Iraq Ghandi, Abbas. University of California, Davis, ProQuest Dissertations Publishing, 2013. P14

²¹⁴ Mabadi, Legal Strategies in Upstream oil and gas contracts to attract Investment: Iran's case. LLM Dissertation. Faculty of Law. University of Shahid Beheshti. 2008

which influences on the attractiveness of the Iranian buyback. Providing clear laws which include financial incentives for foreign contractors can make the model more attractive.

The main Iranian legislation which deals with the issue of taxation of foreign companies is the Iranian version of buyback. This legislation essentially stems from the Rules of Direct Taxation of 1989 as a major law to govern the process of taxation of all companies, partnership and legal entities. Generally, the Iranian tax regime will apply to the entire income of companies registered inside the country, as well as foreign companies' income if it is received from Iran or earned in Iran²¹⁵. However, for the aim of absorbing international investors to certain areas, including development of oil and gas fields, the Iranian taxation system provides some tax privileges such as exemption and deductions for foreign investments in mining, and other related activities which are mentioned in the relevant articles of the Iranian version of buyback.

Article 8.1 of the Iranian version of the buyback model explained that: All national company revenue tax and payment for Community Safety shall be paid via a Foreign Investors too; however, NIOC shall compensate a foreign contractor with an amount representing such charges²¹⁶.

Although compensating the contractor for losses imposed, as a result of local taxation, can act as a financial incentive for foreign contractors to invest in Iran's oil industry, it seems that the main reason for establishing such a mechanism is preventing public dissatisfaction with the foreigners' tax free regime, due to the fact that based on this mechanism, the government can propose that taxes are payable by the foreign company as well as domestic companies, while their eventual compensation will be difficult to notice. In fact, this article sets an unnecessarily long mechanism to deal with the issue of taxation which results in creating confusion for foreign contractors, and also increases the level of bureaucracy in the buyback. Moreover, this article undermines the national interest by exempting all foreign contractors working in the oil industry from taxation which is against the objectives of the Iranian government to boost its economy. Although the government should ensure some financial incentives in the fiscal system of the buyback, it does not necessarily mean that it should deny its primary task in regard to the nation. Therefore, this article which was

²¹⁵ Iran Export, <http://www.iran-export.com/invcli/taxation.htm> access on 2014

²¹⁶ Paydar West Field Asmari and Bangestan Reservoirs, National Iranian Oil Company, South Fields .Year 1999. P 17

intended to offer financial incentives to foreign investors by fully exempting them from paying tax caused some commercially unattractive result for both parties.

Article 8.2²¹⁷ placed limitations on the level of compensation to ensure that tax returns on activities conducted outside the country which did not have commercial benefits for Iran is not included in the compensation payable by NIOC. The article expresses that contractors are not allowed to cover tax charges, energy expenses, payments and charges on the revenue obtained beyond the country that have to be compensated via NIOC²¹⁸. This article has to be considered in line with the previous provision, as it is attempting to limit the general extent of the previous article's mechanism which is the result of the lack of a clear and specific law regarding foreign companies' taxation. Setting such provisions decrease the level of legal clarity which makes the model unattractive for foreign investors, as it causes confusion amongst them.

Article 25 of Iranian version of buyback rules that for the purpose of not bearing the contractor undue burden NIOC will pay for any custom duties on the import. Article 25.1 expresses that: Tools and stuff that do not existed inside the country can be delivered on the behalf of NIOC, and all import taxes duties that are conducted via the supplier should be compensated by NIOC as non-capital expenses. This principle, similar to article 8.1, provides an unnecessary mechanism to deal with custom duty. This mechanism, as has been mentioned above, is bureaucratic and vague which will disappoint foreign investors. Moreover, providing the privilege of custom duty exemption for foreign contractors, it seems completely in favour of the foreign party, while the government can wisely use it as a financial incentive for any company that deserves to enjoy this right²¹⁹.

Overall, the issue of taxation of foreign oil companies operating in Iranian fields seems to need more concern to reform, as the third oil producer country in OPEC suffers from lack of a clear, certain and specific law regarding the taxation of foreign entities working in its oil industry. Having analysed the relevant articles clarify the vague bureaucratic mechanism that has been created in conjunction with old civil law which certainly cannot respond the

²¹⁷ Article 8.2 sets a limit on the size of compensation by barring reimbursement for anything that is not "petroleum costs", as per Articles 22. 1-4. It remains to be seen whether this element of the Model Contract may be overwritten by future amendments of the Majlis

²¹⁸ Mohammad Reza Saber, Buyback Contracts in Upstream oil and gas sector and its legal effects, International commercial law PHD dissertation, Azad University, International Postgraduate Centre, 2007, Tehran

²¹⁹ Yelena Kalyuzhnova, LOCAL CONTENT: CONCEPTS, PERSPECTIVES AND ECONOMY, 2016, P 112

need of the country to boost the economy through encouraging the foreign investors to invest in Iran's fields²²⁰. As a result, the solution which this study offers, in line with the evolutionary approach is abolishing the taxing of foreign companies working in Iranian oil industry, due to the fact that it is fully paid back, thus, there is no point to tax them, and in addition, such abolishment will remove the bureaucratic procure of receiving and paying back the tax. Moreover, this work proves that it is possible to make a fine balance between the aims of Iran's government's, boosting the economy, and increasing the attractiveness of the model by removing the tax, and accordingly providing a financial incentive as has been discussed in the previous section.

i) Legal concerns regarding land and resources: Lack of any environmental concerns

Assuring the success of the development of the oil fields requires the interaction with the land being used in the operation. In other words, as the relevant activities to produce oil has to be carried out on the land via drilling wells, it seems essential to consider the governing law of buyback regarding the land which will be used in the operation. Noticeably, the more precise provisions in this regard can diminish the legal difficulty of foreign contractors for the operation of the field which subsequently will make the model more attractive²²¹.

Article 5 of the Iranian version of the buyback model²²² deals with such rights which are exercisable by NIOC to ensure that there is no limit for NIOC in using the land while the contract is in force. This right has been fully granted to NIOC, as all natural resources are nationalised. Thus, private ownership of them is illegal and NIOC is the only authorised entity that can manage the operation of the fields. The article states that 'NIOC should conduct all essential observation, administration, and use absolute rights for employing the contractual terms excluding those action which will stop or delay the conducting of the progress of the project'. Therefore, NIOC which has been granted the full right to use the land for the purpose of the operation of the field will authorise the foreign contractor by

²²⁰ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006 p 22

²²¹ Mabadi, Legal Strategies in Upstream oil and gas contracts to attract Investment: Iran's case. LLM Dissertation. Faculty of Law. University of Shahid Beheshti. 2008

²²² Paydar West Field Asmari and Bangestan Reservoirs, National Iranian Oil Company, South Fields .Year 1999. P 7

signing the buyback agreement to employ the land in order to develop the project²²³. This article by granting full permission to NIOC in using the land for the operation denies any concern to limit this right in the case of misusing the right such as damaging the land. Presumably, this article could limit or even deprive the NIOC's rights if any harmful activities happened with regard to the land. In fact, this article does not consider any environmental concerns relating to the employing of the land in operating the field such as constructing the instalments which can potentially have a harmful effect for the environment.

Article 6 of the Iranian version of buyback in an attempt to minimise the high risks of the foreign party allows them to make requests for aid from NIOC, and also obliges NIOC to fulfil them. Article 6.1 expresses that: 'Land and water that sensibly are essential for IOCs to develop the project should be supplied via NIOC, and placed at the disposal of the contractor. The purchase prices shall be either remunerated by NIOC or encompassed in the petroleum costs if paid by the contractor'²²⁴. Nevertheless, this article creates an ambiguous criteria of 'reasonability' in obligation to NIOC to provide aid for foreign contractors. This criteria is vague, as it may potentially be interpreted by NIOC to deny assistance if it is recognised as inconvenient. Therefore, this Article may only be seen as window-dressing in most instances, especially where helping would be expensive, even though the article explicitly defines NIOC's responsibilities for supplying supplementary resources in the form of land and water to the foreign investors.

The two articles illustrating the legal concerns about the land and necessary resources to operate the field are confusingly general and ambiguous which will lead to bureaucratic process, and subsequently disappoint the foreign investors. As a result, the features of these provisions are part of the unattractive elements of the Iranian buyback that has to be reformed for the purpose of encouraging the foreign investors after the lifting of the sanctions.

The solution for these unattractive elements of the model in compliance with the approach chosen in this study is providing the provisions with a higher level of clarity and novelty to respond to the increasing need of the model to have specific, certain and clear governing

²²³ S.N.Ebrahimi, A. Shiroui Khouzani, The Contractual Form of Iran's Buy-back Contracts in Comparison with Production Sharing and Service Contract, PEDEC, 2003 p12

²²⁴ Stern R., The Iranian petroleum Crisis and United States national security, proceedings of the National Academy of the United States of America, Vol. 104 No. 1 PNAS January 2, 2007 p45

laws. Regarding article 5, it should be changed to determine the limits of NIOC's right in using the land, and more importantly to consider the environmental concerns about the operation of the field. Moreover, removing the criteria of reasonability can make the provision more certain, as the intention of the article is to oblige NIOC to provide necessary aid for contractors to operate in the field.

j) Administration of field operation: Ambiguous process of substituting the chairman

Basically, bureaucracy is one of the undesired features of the Iranian buyback, practically with regard to managing the project. This feature which absorbs many criticisms from both sides can result into a loss of commercial benefits for both parties in the buyback agreement, as it burdens unnecessary expenses for parties and delays in developing the project. Therefore, providing clear, certain and precise governing laws can eliminate this deficiency, and encourage the investors to work in Iranian fields²²⁵.

Nevertheless, the solution offered by the Iranian version of buyback to minimise the effects of the bureaucracy, as well as avoiding conflicts is the creation of an overseeing body. Such an overseeing body which is created based on Article 17 is supposed to govern the arrangement of the Joint Management Committee which observes the development of projects. Article 17.1 expresses that the JMC includes 5 nominees from both sides, whereby NIOC shall perform as the head of Joint Management Committee for the first 12 months, afterwards, the head of Joint Management Committee should substitute yearly amid others. Accordingly, based on the above Article, NIOC is granted the supplementary bargaining power, as well as control of the project in the first year, however, as the chairmanship will substitute between participants, it encourages both participants to preserve the current environment of mutual cooperation.

Although this article was intended to deal with the undesired bureaucratic mechanism of the buyback in managing the project, it seems that the provisions failed to solve the problem, as the article is not clear about the process of substituting the chairman which can result into further disagreement between parties, and subsequently creates more

²²⁵ Dominique Bruhn, Space for local content policies and strategies, Investment Law and Policy at the Columbia Centre on Sustainable Investment, 2016, p 25

bureaucracy. This flaw stems from a lack of clarity in this process that needs to be revised through the evolutionary approach to enact clear, specific and certain governing laws which can make the model more attractive by minimising the effect of bureaucracy²²⁶. It is noteworthy that achieving the major aim of the new Iranian government to attract investment to develop its petroleum industry is not possible in the lack of a clear, fair and neutral legal provisions which are the foundation of every business model looking for investments. Therefore, Iran is in dire need to revise its governing law of buyback to make the model more attractive, as the country is under pressure of a price fall in oil, as well as high competition from oil producers in both the sense of economy and politics.

k) Issue of flexibility in the Iranian model of buyback: non-modernised legal framework as a result of the pre-arranged version of buyback

Flexibility is the main financial tool for generating an improved system which is intended to reconcile the conflicting interests of both the host government and the foreign investor by establishing and maintaining a long term plan agreement. Moreover, flexibility as a key element for stabilisation of the fiscal regime consists of a process of adapting the changes, as well as adjusting possible fluctuations in the system.²²⁷ Therefore, adaptability and capability of an adjustment in the regime is the criteria to assess its flexible mechanism. As a result, from the early concession periods, host governments and IOCs have been offering flexible mechanisms in petroleum contracts to avoid parties from the rigidity of renegotiating the terms and conditions of the contracts because of the inevitable changes in circumstances such as rising or falling unit costs, product prices and economic rent. The approaches applied by countries to adjust the fiscal regime in order to adapt to changing circumstances vary from a contractual system to another one based on the sort of model in operation, such as a concessionary mechanism, production sharing agreement, or service contract regime. However, regardless of the differences involved in regimes, all of them are following the same goal which is increasing the possibility of the profitability of the fields to convince IOCs at the exploration stage to apply a high performance that can result in a

²²⁶ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006 p25

²²⁷ Le Leuch, H., Contractual flexibility in new petroleum investment contracts in Petroleum Investment contracts, 97 (Bjeredik, N and Walde, T., eds. London: Graham & Totman, 1988). P. 94

commercially viable discovery. Therefore, financial incentives particularly in fiscal packages may guarantee additional bargaining power for the host government. Accordingly, the main feature of a stable fiscal regime is the capability of the regime to survive what is known as flexibility in fiscal policy²²⁸. The Iranian buyback model, in particular, from the perspective of IOCs is considered one of the toughest oil and gas arrangements in the petroleum industry. This outcome is the direct result of applying the out of date provisions which are based on the historical views of Iranians towards the issue of oil deals. Such provisions as offered as part of the fixed draft to govern the relationship of NIOC and the contractors are not flexible, create restrictions for IOCs and subsequently demotivate them from participating in the Iranian oil sector. Offering the pre-arranged and solid model of buyback to all IOCs operating in different fields of the Iranian oil sector is the main element of inflexibility of the Iranian buyback which results in discouraging the IOCs, as the proposed contract might not ensure their interests in petroleum deals and it can lead to the bureaucratic process of negotiation and arbitration which also results in a loss of the national party's interest because of the delay in the beginning of the field operation, even though offering the pre-arranged draft aims to protect the national interest of Iranians in petroleum deals²²⁹. Therefore, this study, in order to evaluate the level of the buyback's attraction, proposes that the terms of every buyback should be mutually arranged on the basis of a pre-study of the field capacity, the contractor's technical and financial situation, and the required activities to maximise the level of the production. This suggestion will ensure the flexibility of the model framework, minimise the potential future disputes, and subsequently offer the most attractive form of Iranian buyback which can compete with other used forms of petroleum agreements²³⁰.

Overall, this section considered the criticisms arising with regard to the contractual framework of buyback from both the domestic and international view. It has been clarified that although the above-mentioned provision's goal were protecting national side benefits, they act against the interests of the foreign party and also have an adverse influence on the Iranian side, as they all are unnecessarily restrictive which impede the aim of encouraging

²²⁸ N. Mohammad, The New Face of Iranian Buyback Contract: Any hope for Foreign Investment? OGEL Journal, Dundee, Vol. 7 - issue 1 April 2009, P 17

²²⁹ Mohammad Reza Saber, Buyback Contracts in Upstream oil and gas sector and its legal effects, International commercial law PHD dissertation, Azad University, International Postgraduate Centre, 2007, Tehran. P 30

²³⁰ Ibid p34

foreign investment into the country. Therefore, to protect the national interest of Iran in petroleum deals, as well as to reach the goal of Iran in increasing its rate of production after the lifting of the sanctions by attracting foreign investments, it is vital to modernise the buyback by reforming its provisions to make it more attractive. For the sake of this aim, this study has employed the evolutionary approach in order to revise the required terms of buyback that have been criticised from both sides in order to increase the efficiency of the model by responding to the criticisms. Further to the criticisms resulting from the contractual framework of buyback, the political considerations in Iran's political environment have created some shortcomings for the buyback that have resulted in a decrease of the level of international companies' participation in the Iranian oil industry which will be analysed in the following section of this sub-chapter.

4.2.2 The unstable political considerations: Lack of legal certainty

As has been clarified in the second chapter of this work the Iranian buyback is the product of the nationalisation movement which stemmed from political considerations. Therefore, it is defenseless regarding changes in politics' atmosphere which led to low rate of foreseeability in comparison with other petroleum models²³¹. The vulnerability of the Iranian buyback contracts has been created as a result of rapid changes in government policies, and legislation passed by Parliament which degrades the level of protection for IOC's legal and financial stance as has been analysed in the last chapter regarding the deficiencies of the FIPPA²³².

An example for adverse effect of rapid political changes on the buyback in the contemporary history of Iran is the shifting of power from the Reformists to the Conservatives which led to a great changes in the strategy of the country regarding the oil industry. While the Reformists supported foreign involvement in the oil industry, and subsequently many oil projects including South Pars were granted to international oil companies, the Conservatives limited the participation of foreigners in the oil industry, and

²³¹ Stern R., The Iranian petroleum Crisis and United States national security, proceedings of the National Academy of the United States of America, Vol. 104 No. 1 PNAS January 2, 2007

²³² [<http://www.uofaweb.ualberta.ca/chinainstitute/nav03.cfm?nav03=44161&nav02=43873&nav01=43092>]

consequently many oil projects were granted to domestic oil companies²³³. Accordingly, these inconsistent strategies regarding the oil industry have been created by different political considerations, and impose the burden of legal uncertainty regarding the buyback on international oil companies operating in the Iranian fields, as they are not able to either rely on the legal strategy of the Iranian government or foresee the tendency of the Iranian governing laws of buyback enacted by the Parliament. Moreover, this legal uncertainty resulting from the change in the political environment of Iran creates a great confusion for the contractual parties which necessitates extra negotiations that result in a loss of both parties' interests by delaying the operation of the project. Hence, this study on the basis of the evolutionary approach, and in order to prevent these adverse political effects on the model suggests that Iranian officials need to define the obligatory strategy to develop Iran's petroleum sector independent from political parties which includes the precise regulations regarding the Iranian buyback, and more importantly cannot be changed by different political parties in regards to their fundamentals. Applying this reform will remove a great deficiency of the model, respond to the criticisms of IOCs, and allow IOCs to rely on the Iranian petroleum legal system which will make the model more attractive. The last section of this sub-chapter will examine the adverse influence of the unclear legal obligations of the Iranian buyback on its efficiency, and will attempt to respond to this complaint by recommending a revision of the model.

4.2.3 Unclear legal obligations of buyback contract: Separate negotiations and more complicated bureaucracy

It has been demonstrated in the third chapter that the Iranian governing law of buyback suffers from a lack of certainty and clarity which burdens an important legal risk on the foreign contractor. In addition to the above-mentioned adverse effects of uncertain and unclear laws, they require conducting separate negotiations, due to several necessary provisions such as the protection provisions for IOCs, and the bidding process requirements do not exist within the default system of the buyback agreement. These issues which require additional negotiations will result in more bureaucracy, and slower progress in

²³³ [<http://www.payvand.com/news/06/apr/1186.html>]

regards to NIOC which is against the interests of the parties, as some of these decisions must be made in a speedy manner²³⁴. Therefore, as the terms of the buyback are inflexible, and subsequently cannot be changed based on the different circumstances, both parties have to predict change of circumstances which requires additional negotiations.²³⁵ Accordingly, the effect of the unclear legal provisions of buyback will be extensive negotiations, and a high level of bureaucracy which would result in a loss in the speed of finalising the deal, beginning the field operations, and subsequently overall economic efficiency. In particular, the Bangistan proposal via BP led to different offers including 16-25 years operation of the field instead of determined length of 60 months buyback draft. As a result, most oil companies in Iran agreed on the fact that "We would definitely prefer things to happen more quickly" however "Iran is a country with a complicated political and social structure with a lot of checks and balances²³⁶." This comment is a product of the redundant bureaucratic system which has been created by both NIOC and the Ministry of Oil, as they duplicate each other's work without the necessary responsibility and transparency. Consequently, this section highlights the importance of providing a comprehensive governing law to legally manage the parties' rights and obligations. However, as the Iranian governing law in this regard is incomplete and unclear, the attractiveness of the model decreases. This is because the unclear legal provisions prevent the foreign contractor from relying on the governing law, and subsequently forces both parties to conduct separate negotiations. This delay which is created by unnecessary negotiations and bureaucracy is harmful for the interests of both the national and international party, as it postpones the production of the field. The reform that this study advises after the lifting of the sanctions is to attract foreign investments in the oil industry by establishing a special institute which offers legal consultancy to NIOC in order to prepare clear, comprehensive and precise provisions to govern the buyback. Otherwise, the return of Iran to the global oil market with its current governing laws of the buyback will not be in the near future with especially because of the current high competition amongst oil producers.

In summary, this sub-chapter dealt with the criticisms of the Iranian buyback from both the national and international perspectives, and showed that they stemmed from the

²³⁴ M. Bunter, The Iranian Buy Back Agreement, OGEL Journal, Dundee Vol. 3 - issue 1, March 2005, P 6-8

²³⁵ *ibid*

²³⁶ According to Alan Stott, Iranian envoy of BG Group, an oil extraction company

contractual framework of the model, political considerations and the incomplete legal provisions of the model. Moreover, the consideration of the three sections of this sub-chapter demonstrated that although, as mentioned in the second chapter of this work, the buyback model has been designed to protect the interests of Iran, the existing criticisms from the national party proves the economic inefficiency of the model which requires necessary revisions of the Iranian buyback²³⁷. Further to analysing the deficiencies of the buyback, this sub-chapter offered solutions for the criticisms examining the effectiveness of the evolutionary approach in revising the existing method of transaction. In fact, this study proves the applicability and efficiency of the evolutionary approach as the future alternative in modernising the Iranian buyback without any clash with the current obstacles. Following the consideration of the parties' criticisms, and providing solutions for them, the critical comparison of the Iranian buyback with the Production Sharing Agreement mechanism which is offered in the next sub-chapter will complete the process of highlighting and reforming the shortcomings of the buyback with the aim of introducing a more attractive version of the buyback subsequent to the lifting of the sanctions.

4.3 Iranian Buyback in comparison with Production Sharing Agreement: No Commercial Viability but in compliance with the essence of nationalisation event

As the second chapter of this work discussed, the public discontent towards the concessionary contracts led to the nationalisation of Iranian natural resources, and subsequently the introduction of the current model of the Iranian buyback. Although the production sharing agreement model could cover the national interests of Iran in petroleum deals, during its short period of operation in the history of Iran's oil industry²³⁸, the strong public feeling against the ownership of the oil product by foreigners, which led to the nationalisation event, as well as the aggravation of the economic inequality between Iranians, which led to the 1979 Islamic Revolution, fundamentally changed the petroleum

²³⁷ Shahri, Nima Nasrollahi. "The Petroleum Legal Framework of Iran: History, Trends and the Way Forward." *China and Eurasia Forum Quarterly*, vol. 8, no. 1 2010

²³⁸ Momeni, F., 'Tarh haye Beyeh Moteghabel va Negaraniye Meli' (Buy-Bach Schemes and National Concern), *Neshat Newspaper*, February 1999

contractual scheme of the Iranian oil industry to the buyback²³⁹. Accordingly, as the Iranian buyback has been analysed from both parties' perspective in the last sub-chapter, and the necessary reforms have been prescribed, this sub-chapter will attempt to highlight the deficiencies of the model stemming from the critical comparison between the Iranian buyback and the Production Sharing Agreement mechanism in four sections in order to adopting the advantageous provisions of the PSA with the aim of making the Iranian buyback more attractive.

The production sharing agreement model and the Iranian buyback contract are clearly similar in certain aspects. In both types of legal arrangements, whilst the IOC is the contractor in charge of performing the operations according to the agreed terms of the contract, the host country conducts the management control of the project. Moreover, the host government maintains the entire possession to the discovery inside land during condition of operation. Nevertheless, it provides the IOC with a method for remunerated hydrocarbons as proven oil reserves. Under both sorts of arrangements the contractor is required to supply all necessary capital, equipment, technology and skills, as well as bearing the risk of discovery, as well as operation for each approved work program. Nevertheless, critical comparison of the two models also illustrates the differences between the Iranian buyback and the Production Sharing Agreement which are highlighted below:

a) Duration of contract: Inadequate period to maximise the operation of the field under buyback

As has been mentioned in the last sub-chapter the short duration of the Iranian buyback is a response to the long length of the concessions previously granted, and is designed to protect the national interests of Iran in petroleum deals²⁴⁰. This relatively short length which is about 5-8 years is not an adequate period within the international energy contractual framework, particularly regarding the operation of NG. However, the PSA by offering a long term agreement which is about 20-25 years provides more motivations to international oil

²³⁹ S.N.Ebrahimi, A. Shiroui Khouzani, The Contractual Form of Iran's Buy-back Contracts in Comparison with Production Sharing and Service Contract, PEDEC, 2003

²⁴⁰ Me. M., The Iranian Buyback Model and Its Efficiency in the International Petroleum Market - A Legal View, OGEL Journal, Dundee, Vol. 7 - issue 1, April 2009

companies for preparing for maximizing the field's lifetime²⁴¹. As has been demonstrated in the last sub-chapter, this restrictive provision of the Iranian buyback which is against the benefits of both parties can be reformed by increasing the length of the contract based on the pre study of the field and the estimated size of the discovered block. The reform that this study proposes, in accordance with the evolutionary approach, will present a more attractive form of the Iranian buyback to international oil companies.

b) Transfer of technological skills: High limitation for NIOC to achieve the latest technology

It was mentioned in the third chapter that the Iranian governments' position in regards to the buyback was the nationalisation of the whole process of field operations. As a result, the issue of transferring the technology in buyback agreements is crucially significant for Iran in its attempt to obtain absolute independency from foreign contractors, as the second chapter showed that the lack of technology after nationalisation in Iran was the main bargaining power of the foreign contractor to burden their conditions on Iran. On the contrary, to the great importance of such provisions from the Iranian view, the transfer of technology is subjected to a high limitation in Iranian buyback contracts. This limitation stems from the short duration of the buyback, as the length of the buyback is too short for the NIOC to achieve the latest technology of the foreign contractor. However, with a long duration of contract, the host country can enjoy the latest technology, management skills and immense expertise on the PSA agreements²⁴². Accordingly, increasing the duration of buyback does not only not damage the interests of Iran in the buyback, but also will provide more commercial benefits for the country by enabling the NIOC to obtain the technology from the foreign party, and make the model more attractive for the foreign investor. Moreover, this advantageous provision of the PSA that this study proposes to integrate within the terms of the current buyback is not in contradiction with any legal, political and historical concerns in Iranian society.

²⁴¹ Ibid

²⁴² A. Ghandi, C-Y Cynthia Lin. Oil and Gas Service Contracts around the World: A Review, Institute of Transportation Studies, University of California, March 14, 2014 P 4-6

c) Granting the right of discovery and production activities: Lack of financial incentives in buyback

This has been discussed in the last sub-chapter that the idea of separation of the exploration and production stages in the Iranian buyback is aimed to protect the national interests of Iran, while this provision only produces extra negotiation and bureaucracy with no commercial benefit for the Iranian side²⁴³. Moreover, this provision creates a high level of risk for the contractor under the Iranian buyback deal which results from the fact that the cost of discovery activities is relatively higher than production activities, and more importantly, the main profit of the oil and gas business is generated from the production phase, while the contractor in the Iranian buyback is only granted the exploration rights. In fact, while the contractor in Iranian buyback agreements are not guaranteed the development rights on discovered blocks, even though a preferential right for the field development is recognised for the contractor of the discovery phase, the original terms of PSA allows the discovery contractor to enjoy the rights to develop the discovered fields. Accordingly, the provisions of the Iranian buyback increase the level of risk posed on the contractor which leads to discouraging foreign investors from participating in the Iranian oil industry. Shifting this restrictive provision of the Iranian buyback to the PSA' strategy of granting both phases of exploration and production to the contractor that discovers the oil block is the applicable solution that this study suggests based on the evolutionary approach²⁴⁴. By applying this reform, Iran can change the restrictive provision to a financial incentive in order to motivate foreign contractors to employ its highest technologies and expertise in the discovery phase to explore the oil block. Moreover, such a reform will definitely make the scheme of the Iranian buyback more prepared to attract foreign investments.

d) Method of payment: Financial risk for both parties in buyback

As has been precisely examined in the last sub-chapter, the method of payment in the Iranian model of buyback is based on unchanged level revenue. Such payment method

²⁴³ Mohammad Reza Saber, Buyback Contracts in Upstream oil and gas sector and its legal effects, International commercial law PHD dissertation, Azad University, International Postgraduate Centre, 2007, Tehran.

²⁴⁴ Mabadi, Legal Strategies in Upstream oil and gas contracts to attract Investment: Iran's case. LLM Dissertation. Faculty of Law. University of Shahid Beheshti. 2008

payment discourages IOCs for increasing total returns from the block by discovering additional reserves, optimising production targets, and employing enhanced oil recovery, as its revenue has been fixed from the beginning of the project. Moreover, this method, regardless of bringing the global price of oil into its consideration, obliges the NIOC to compensate the contractor which is obviously against the interests of NIOC and subsequently the national interest of Iran, in the event of price fluctuation. In contradiction with the Iranian buyback, the unfixed rate of return in PSA which is based on quantity of the production provides a high incentive for the contractor to reach the highest performance of the project, as well as reducing the risk of price fluctuation for NIOC. Therefore, to cover this shortcoming of the Iranian buyback this study offers applying an unfixed rate of return which does not clash with any constraints in Iranian legal, political, and historical considerations, and more importantly will remove an important risk in favour of the NIOC. Furthermore, this reform, which has been proposed on the basis of the evolutionary approach by integrating advantageous provisions of other models will make the buyback more attractive.

e) Field ownership rights and dynamic profit maximization policy: Main restriction for Iranian buyback

The main reasons of choosing the buyback have been discussed in the last chapter, and it has been shown that the ownership of the discovered field is a significant concern in the Iranian oil history and legal framework²⁴⁵. This is because of the fact that the main support for the adoption of service contracts is the country's concern of preserving the sovereignty of natural resources, as service contracts allows countries to uphold field ownership, as well as produce crude ownership in most cases. Thus, countries choose service contracts as it permits them to employ the expertise of the IOC whilst they relinquish less control over the fields and the produced crude to the IOC. However, sovereignty concerns arise under production sharing agreements due to the fact that the IOCs are granted decision-making power in the operation of the exploration and development and the right to share the

²⁴⁵ Me. M., The Iranian Buyback Model and Its Efficiency in the International Petroleum Market - A Legal View, OGEL Journal, Dundee, Vol. 7 - Issue 1, April 2009

produced crude ownership with the host country²⁴⁶. The effect of giving up the host's right regarding its own local sources would be less power for the host government for observing IOS's operation which is occurred through regulative laws, and supervisory activities. On the other hand, although service contract may ensure sovereignty considerations, the structure is leading to massive potential losses in profit, particularly in case of Iranian model of buyback, as well as Iraqi technical service contract. Lack of flexible method to maximize the income resulted in loss for NOCs in Iranian system, as well as Iraqi model that results led to inadequate economic impact of service contract. Hence, the adoption of such measure can rise the commercial proficiency of the agreements which would be generally recommendable in Iranian, as well as Iraqi method of transaction.²⁴⁷ Nevertheless, it seems that the service contract fundamentally is tending to lose massive possible revenue even in the case of applying a flexible method to maximize the income of, due to the fact that exercising this strategy is not an adequate solution for shifting upshots efficient of the service agreement framework, albeit Ghandy and Linee in 2012 and Ghandy and Linee in 2014 demonstrated this resolution as an enough means for achieving more economically efficient consequences. This uncertainty regarding the proposed solution rose from the idea of maximizing the income through flexible method, as it involves continues ideal choices which requires the operators to update their choices according to ideal amount of oil, as well as the ideal scheme of extracting according to reserves estimation, necessary capital and operation cost and oil market price predictions. Yet, the existing service contract does not have the essential means of adopting the dynamic profit maximization objectives, owing to; the fixed IOCs' compensation regarding to extracted quantity within the agreement²⁴⁸. Specifically, under Iranian buyback contract, the international oil companies' compensation is depending on subsequent fixed scheme in contract during a certain period, thus, departing agreed production rate in the deal would be impossible under such requirements, albeit IOCs discover the ideal. The Iraqi system rules that compensation of international oil companies would count on the basis of attaining the manufacture goal within the manufacture structure with no function for choosing ideal manufacture rate. In contrast,

²⁴⁶ Momeni, F., 'Tarh haye Beyeh Moteghabel va Negaraniye Meli' (Buy-Bach Schemes and National Concern), Neshat Newspaper, February 1999

²⁴⁷ Ibid.

²⁴⁸ Mabadi, Legal Strategies in Upstream oil and gas contracts to attract Investment: Iran's case. LLM Dissertation. Faculty of Law. University of Shahid Beheshti. 2008

the IOC in production sharing agreement applies flexible method of maximizing the income in association with the state-owned oil companies, as IOC is granted decision making power and rights to ownership of the generated crude under production sharing agreement. However, considering the forbiddance of ownership of oil product by foreigners, this study based on the evolutionary approach proposes the application of the dynamic profit maximization policy through shifting from pre-fixed remuneration to unfixed rate of compensation in order to preserve the essence of buyback, the ownership of oil field by Iran, as well as avoiding the great loss of Iran through buyback²⁴⁹. This solution which does not breach any barriers in Iranian petroleum law shows that there is no need to choose the radical change towards the production sharing agreement model, while it is possible to integrate the advantageous provisions of other models to the Iranian buyback.

Overall, this sub-chapter offered the critical comparison of Iranian buyback contract and production sharing agreement with focus on their differences. This comparative analysis of these two models highlighted five advantageous provisions that can be integrated to the Iranian buyback's terms to cover the deficiencies of the model without breaching any legal, historical or political restrictions²⁵⁰. This is the result of applying the evolutionary approach that this study has chosen, due to the fact that the radical change in the contractual framework of Iranian oil industry through shifting towards another model on the basis of revolutionary approach is not possible in the current political, legal and historical atmosphere of Iran, moreover, such a radical change has an expensive price for the country which needs more time to be prepared. Subsequent to improving reforms proposed in this sub-chapter regarding the problematic features of Iranian buyback through integrating the advantageous terms of PSA, the next sub-chapter will provide the comparison of Iranian buyback with other common service contracts in different countries in order to more precisely improve the scheme of the model through reforming the restrictive provisions of Iranian buyback to make it more demanding from the perspective of foreign investors, as well as more beneficial for national party.

²⁴⁹ S. N. Ebrahimi, *LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995*, IQPC London, 27th Oct. 2006

²⁵⁰ *ibid*

4.4 Iranian buyback in comparison with service contracts: More restrictive provisions of Iranian buyback than other service contracts

As it has been clarified in the last chapter, the Iranian buyback is a type of service contract that foreign contractor is in charge of development of the field through providing necessary capital and technology, while the NIOC's responsibility is to observe the progression of operation and subsequently compensate the contractor. However, as the Iranian buyback is independent of service contract model as the commonly used kind of petroleum legal framework²⁵¹, the comparison of these three models which will be carried out in this sub-chapter in three sections can precisely point out the shortcomings of the model compared to Iraqi as well as Venezuelan service agreements. This analysis will provide the essential materials for this study to prepare the applicable solutions that can make the buyback more efficient.

The table categorised service contracts in Iran, Venezuela and Iraq based on the following three different elements²⁵²: Ownership right regarding the produced crude oil, capital cost regulation and operation rights of the developed fields.

Table 5: Iranian buyback in comparison with other service contracts

Iran	First Generation of Buyback signed in 1995	Second Generation of Buyback signed in 2004	Third Generation of Buyback signed in 2009	Iran's announcement for new plan for offering more attractive model in 2016
Venezuela	First round of Operational Service Agreements in 1991	Second Round of Operational Service Agreements	Third Round of Operational Service Agreements in 1997	Shifting the Service Agreement to joint company framework in 2006-7

²⁵¹ Me. M., The Iranian Buyback Model and Its Efficiency in the International Petroleum Market - A Legal View, OGEL Journal, Dundee, Vol. 7 - issue 1, April 2009

²⁵² A. Ghandi, C-Y Cynthia Lin. Oil and Gas Service Contracts around the World: A Review, Institute of Transportation Studies, University of California, March 14, 2014. P 8

Iraq	Producing Field Technical Service Contract in 2009	Development and Production Technical Service Contract in 2009	Third Round of Technical Service Contract in 2010	Fourth Round of Technical Service Contract in 2012
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a) Ownership right regarding the produced crude oil: Harsh position of Iranian buyback

As the second chapter of this work demonstrated the essence of nationalisation of Iranian oil was the idea of forbiddance of any foreign ownership on Iranian natural resources. This principle has been reflected in the Constitution of Islamic revolution and more importantly formatted the basis of Iranian model of buyback. While Iran and Iraq banned the foreign ownership of any petroleum product which is the main similarity between Iranian buyback and service contract mechanism, the service contract of Venezuela recognised IOCs right to share from product which can be known as the exclusive element in third round of Venezuela service agreement. As this position of Venezuelan service contract is more flexible than Iranian strategy, it is more attractive for foreign contractor. Moreover, this will remove the risk for NIOC in the event of price fluctuation. However, this study with consideration of the current legal, political and historical situation of Iran, and its time limit to return to its previous position in the international oil market, does not suggest such a radical change as the alternative for the future of the model. This is because of the fact that to apply such radical change, the provision of the Constitution needs to be amended, as well as the political atmosphere and public feelings need to be prepared to adopt such fundamental reform. As a result, this study based on its strategy to propose the applicable solution to modernise the buyback, focuses on the reforms with no clash with the existing barriers.

b) Capital cost estimation regulation: Unrealistic legal obligation on contractor operating in Iranian field

It has been discussed in the first sub-chapter of the present chapter that Iranian buyback following the conservative method in consequence of negative experience of foreign

involvement in oil industry burden an unrealistic legal obligation on contractor with no commercial viability which is the cost estimation before the beginning of the project. While this provision poses extra risk on international contractor, it is also against the national interest of Iranians, as this provision will postpone the beginning of operation, production activities, and subsequently will lead to loss of both parties' benefits. On the contrary to this term of Iranian buyback, the service contract method in both Iraq and Venezuela provide the flexibility for contractor to amend its cost estimation²⁵³ which results in to minimise the risk on IOC in this regard²⁵⁴.

The amendment that this study offers on the basis of evolutionary attitude is integrating this element of Iraqi and Venezuelan model to permit contractor to provide the cost estimation as the project is running which does not breach any constraints. Applying this reform will minimise the risk on contractor, increase the accuracy of the cost estimation for NIOC, accelerate the start of project, and consequently remove this unattractive provision of model in favour of foreign investor.

c) Operation rights of developed field: Monopolised right for NIOC's subsidiaries

Iranian buyback in line with its legal framework as it has been discussed in the third chapter is aimed to protect the national interest of Iranians against foreign contractors. On this basis, the Iranian buyback denied the rights of foreign contractor with regard to operation of the developed fields which is an important source of income for IOCs, whereas, under service contracts in Iraq and Venezuela the contractor is granted the right to operate the developed fields²⁵⁵ which is the financial incentive for foreign investors to participate in oil industry of Iraq and Venezuela. On the contrary, the Iranian model by monopolising this right to NIOC's subsidiaries creates a loss of an advantage for the contractor, as well as stabilises the monopoly market instead of competitive one which can be against the national interest of Iranians. As a result, in to remove this unnecessary risk to and make the model more competitive, this element of can be integrated to Iranian buyback to motivate the foreign investment to engage with Iranian oil industry, as well as to award any

²⁵³ A. Ghandi, C-Y Cynthia Lin. Oil and Gas Service Contracts around the World: A Review, Institute of Transportation Studies, University of California, March 14, 2014. P 10

²⁵⁴ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006

²⁵⁵ Ibid.

contractor that quicker reaches to the phase of production by utilising its highest technology²⁵⁶. Therefore, this reform that is not in contradiction with any prohibition in Iran towards modernising the buyback will change the shape of the model to more attractive version which is the ultimate aim of this study from analysing the Iranian buyback.

Overall, this sub-chapter offered the critical comparison of Iranian buyback with the service contract mechanism in Iraq and Venezuela through considering the three vital elements of three models. The comparative study of the service contracts in these two countries with Iranian model of buyback demonstrated that although service contract model in general is less attractive for foreign contractors than production sharing agreement, the Iranian model of buyback is considerably more restrictive than other two service contracts in Iraq and Venezuela.

This sub-chapter highlighted the shortcomings of Iranian buyback which resulted in to unattractiveness of the model. More importantly, this sub-chapter attempted to propose the applicable reforms through integrating the advantageous provisions of the service contracts in those two countries that do not breach any prohibition in the current situation of Iran for the aim of making the Iranian buyback more attractive. Based on this strategy, the next sub-chapter will deliberate the comparison of two method of buyback in Iran and in the world to more precisely, and in greater details consider the necessary reforms of Iranian buyback on the evolutionary reforms to increase its economic efficiency to encourage International investors.

4.5 Comparative analysis of the Iranian buyback agreement in the light of International model of buyback: Low economic efficiency of the Iranian buyback

Legal analysis of Iranian buyback in the last chapter has been clarified that the Iranian model of buyback has been formatted through employing some provisions of international buyback scheme for the aim of protecting the national interest of Iranians, as well as attracting foreign investment to the country²⁵⁷. However, the differences between the Iranian buyback model and International buyback stemmed from the fact that Iran's interpretation of buyback contract is established according to the specific legal, political and

²⁵⁶ Chilenye Nwapi , A SURVEY OF THE LITERATURE ON LOCAL CONTENT POLICIES IN THE OIL AND GAS INDUSTRY IN EAST AFRICA, the School of public policy, university of Calgary, Volume 9, 2016. p 15

²⁵⁷ ibid

historical atmosphere of the country which does not always conform entirely to the international schemes of the buyback. Therefore, subsequent to provide a broader comparative analysis of Iranian buyback model with other mechanisms such as PSA, as well as Service Agreements, it seems essential for conducting critical comparison amid Iranian buyback and international buyback scheme in order to highlight the weaknesses of the current method of oil transition in Iran which has created the unattractiveness features of the Iranian buyback, and more importantly to offer the applicable reforms to make the model more attractive for foreign investors²⁵⁸.

Noticeably, the contracts used for this comparison represent the general framework of such agreements. While the 1999 Paydar West Field Asmari and Bangestan Reservoirs licensing agreement²⁵⁹ with the South Fields section within NIOC is chosen as a sample of Iran's model, its international equivalent is the International Model Rules of Buyback Contracts drafted by the United Nations Economic Commission for Europe²⁶⁰. Accordingly, this sub-chapter will attempt to point out the deficiencies of Iranian buyback through considering the differences of two models in nine sections to offer the solutions for the aim of offering more attractive shape of Iranian buyback via adopting the more developed terms of the international scheme that are not in contrary with prohibitions in Iran.

a) Delimitation of services and responsibilities: Not applicability of Iranian buyback's approach in offering the specific terms of rights and obligations for all contractors

The first element of any contract is delimitation of services and obligations which outline the duties that each party is expected to carry out in the agreement. Therefore, the definition of the scope of each party's obligations is the heart of any agreement. Thus, it is essential to firstly deal with the examination of both the domestic and the International buyback provisions with regard to their delimitation of duties between the parties. Basically, contractual rights and obligation of parties in the primary agreement are clarified in the

²⁵⁸ S.N.Ebrahimi, A. Shiroui Khouzani, The Contractual Form of Iran's Buy-back Contracts in Comparison with Production Sharing and Service Contract, PEDEC, 2003

²⁵⁹ Ule, C. and Brexendroff, A. op.cit, p 39-40

²⁶⁰ The international model rules of buyback contracts drafted by the United Nations Economic Commission for Europe/
http://www.ierc.bia-bg.com/uploads/vtcontract/files/vtcontract_00743d3417d145769033e1b5c06e4113.pdf/ Access on June 2015

‘whereas clause’ of the international model of buyback. Thus, according to such clauses the parties agree to establish the buyback contract, and also a series of terms in the form of articles follows: Article 1.1 provides a course of dealing between parties by expressing that the seller will consent to buyer or initiate another party's offer, as per the contractual provisions, of the buyer's output resulting from the utilisation of the technology provided by the seller, as well as to accept the output upon delivery. Therefore, Article 1 defines the key element of the agreement which is establishing a valid condition for each party subject to following articles, thus, the condition of the seller is a pledge to buy products while the condition of the buyer is a pledge to sell goods. Moreover, identifying relating terms to description of quantity and quality of the products, and also creating rules during time of delivery in a contract is significantly vital for the purpose of illustrating parties’ rights and obligations. As a result, since the number of goods and services with regard to buyback is countless, the International contract deliberately remains it unclear in this area to provide maximum latitude for the parties in agreement to decide regarding the scope of obligations and services.

On the other hand, Article 2 of the Iranian buyback by offering a more specific list of rights and obligations such as risks of not finding oil in the drilled field the assignment of profits and the expanses restricted the choice of parties in negotiation to clarify the rights and obligations of each party²⁶¹. Article 2 stated that: "Contractor responsible to NIOC for operations and is to provide all capital, technology and skills necessary for the conduct of Development Operations for this Contract, and shall bear the Petroleum Costs required in carrying out Development Operations, and to recover such costs as provided in Clause 22 hereof, and bear the risks that sufficient production additional production of Crude Oil, and or Natural Gas may not be produced from the Contract Area in order to recover all such Petroleum Costs."²⁶² Although the specific division of duties in agreement might seem effective to reduce the potentiality of arbitration, however, considering the vast area of petroleum contractual framework it is a serious restriction on the party’s choice which can create the dispute. This is because of the fact that the terms of buyback agreement need to be changed on the basis of different fields of operation, risks and situation of the

²⁶¹ S.N.Ebrahimi, A. Shiroui Khouzani, *The Contractual Form of Iran’s Buy-back Contracts in Comparison with Production Sharing and Service Contract*, PEDEC, 2003

²⁶² *ibid*

contractors, thus, offering the specific division of duties and rights for all contractors operating in different fields with different situations seems not to be commercially and technically acceptable which will create disagreements, and subsequently unattractiveness for foreign investors. On this basis, this study suggests the integration of this attitude from the international mechanism to the Iranian version for the aim of increasing the efficiency of the model, and subsequently making the model more attractive with no clash with any barriers.

b) Provisions concerning the remuneration: The nationally supportive future of Iranian buyback

The last chapter showed that the Iranian buyback in consequence of the exploitative nature of concessions has been founded on the basis of protecting the interests of Iranians in petroleum agreements. Therefore, the main tendency in enacting the Iranian buyback's provisions is to be in favor of NIOC's benefits as the representative of Iranians in oil and gas contractual deals. The most important portion of an agreement is remuneration provisions, as they clarify the distribution of revenues and expenses, thus, a specific and clear set of provisions in this respect can impede disputes.

International scheme in essence is based on a doctrine of fair regarding contract which avoids the parties from unfairly possessing the advantage of the each other, due to potential situation which may lead to a grossly disproportionate level of bargaining power. This duty to deal fairly stemmed from the Convention of the United Nations regarding Contracts to the International Sale of Goods (CISG), particularly based on Article 55 CISG which obeys a general idea of good faith, and explicitly noted by Article 7(1) CISG²⁶³.

The main article in the international model of buyback regarding the remuneration issue is article five which declares the prices of the relevant product to the contract as follows:

(1) The value of the output will be evaluated at the end of the sub-contracts for by considering the commercial context in the relevant area of commerce at the time when the transaction happens²⁶⁴.

(2) The price of the on the general market and under competitive terms of distribution and compensation.

²⁶³ Notably the United Kingdom have not ratified this convention.

²⁶⁴ Article 55 of the United Nations Convention on Contracts for the International Sale of Goods, 1980.

(3) The comparable cost of items which depends on the extent of similarity dictated by the level of quality and other qualities, within the relevant area.

(4) The agreed commodity exchange rate when the sub-contract is finished.

Accordingly, the strategy of International scheme regarding the remunerations' provision prescribes the precise theme of fair and balanced dealing arrangements through the sovereignty of Article 5.

On the other hand, the position of the Iranian model is significantly different compared to the international agreement, due to the unique historical background of oil deals which led to dissimilar procedures from the sale of goods as planned in the International scheme.

Article 18.1 is the key provision of Iranian model regarding remunerations' issues which governs the Master Development Plan and Budget. Article 18.1 expresses that MDP should contain the operation structure, project chargers and main expenses to operate the field.²⁶⁵. As it has been mentioned in the first sub-chapter this article burden a significant commercial risk on the contractors by obliging them to provide the cost estimation before the beginning of the project which is serious complaints of IOCs, as they are liable for any inaccurate estimation.

Further important provision concerning the issue of remuneration in Iranian buyback is Article 22 which governs the cost recovery, remuneration fee, and ruled the fixed rate of return for the contractor. This issue which has been also analysed in the first sub-chapter is financially damaging for both parties, as the fixed rate of return is demotivating for contractor, and will lead to loss of benefit for NIOC in the event of fall of price of oil.

Accordingly, the Iranian version of the buyback arrangement in contrast to the international scheme of buyback chose the bias strategy on the issue of remuneration to defend the Iranian interests on petroleum deals which cannot ensure a fair balance between parities. The unattractiveness feature of Iranian buyback has stemmed from such provisions which damage the benefit of both parties in buyback, as they discourage foreign contractor to participate in the Iranian oil industry that results in to losing of Iran in competition with other oil producers in absorbing the foreign investment. However, as it has been discussed in the previous sub-chapters, this study based on the evolutionary approach proposes the

²⁶⁵ Shahri, Nima Nasrollahi. "The Petroleum Legal Framework of Iran: History, Trends and the Way Forward." *China and Eurasia Forum Quarterly*, vol. 8, no. 1 2010 p32

reform in the regulation of cost estimation as the project is running, as well as applying an unfixed rate of return according to consideration of the capacity of the field, the price of oil and the expenses of contractor²⁶⁶. Integrating such terms will make the Iranian buyback more balanced on the issue of remuneration which will lead to the more attractive version of Iranian buyback with no clash with the current briers as the aim of this study.

c) Arbitration and dispute procedure: Limitation on party autonomy in Iranian buyback's provision of arbitration

Following to the analysis of legal anatomy of Iranian buyback which carried out in the third chapter of this work, it has been clarified that the Iranian oil contractual legal framework suffers from the lack of certainty and clarity which resulted in to discouraging foreign investor, as they are not able to rely on such framework, neither foresee its future development. Moreover, the lack of certainty and clarity in provisions of Iranian buyback creates the confusion for parties, and subsequently requires extra negotiations leading to delay the project that is in loss of both parties in Iranian buyback. In particular, arbitration provisions are vital component of all legal frameworks, as they ensure the stability of the commercial relationship between contractual parties, as well as preventing the minor disputes to become the full-fledged disagreement. Nevertheless, even in the event of serious disagreement arbitration plays the main role in establishing a compromise between the conflicting participants rather than leading to nullification of agreement, due to the fact that resolving the dispute in an environment of cooperation rather than in an argumentative atmosphere of court will result into reduce of friction between sides.

The International arrangement in this respect broadly clarifies the principles of arbitration through the special procedures including the finality of decisions. Article 19 of the international model demonstrates this general approach by outlining the mechanism for parties for the purpose of settling any potential disputes. Based on article 19.1, any disputes arising from the contract which cannot be resolved through informal negotiation will be considered under arbitration procedure in accordance with an agreed number of arbitrators and rules upon by the parties to the contract. Therefore, the International model on the

²⁶⁶ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006 p 21

issue of arbitration focused on the intention of contractual participants rather than forcing on any certain arrangement by a higher authority or by the agreement itself. As a result, the means of dispute resolution, the identity and numbers of arbitrators, and the place of arbitration are all discretionary²⁶⁷.

In contrast to the International arrangements' position regarding arbitration which is so broad, the Iranian buyback is different with such general guidelines through specifying certain rules of arbitration. Article 32 of Iranian scheme concerns the dispute settlement, and arbitration by stating that all disagreements, debates and arguments resulting from the agreement or finishing or annulment must ultimately be solved via arbitration, beforehand three arbitrators. All decision of them are compulsory for both sides. More precisely, the Appendix D deals with details of arbitration course in the Iranian buyback.

Section 3 of Appendix D of this work expressed that the place of arbitration is negotiable via both sides involved in disagreement. If an arbitration panel could not reach the agreement upon the determining of last arbitrator, afterwards arbitral panel will be settled in Tehran, Iran, for solving the disagreement.

Section 4 concerns the vital subject of the identity of the arbitrators, as objectivity is challenging to find those belonging to the same country as the disputed parties. Section 4 states that each side will have the power of appointment for a single individual with the first two appointees then finding a third member to chair the group who shall not originate in either of the participants' states²⁶⁸.

Therefore, the Iranian model of arbitration procedure in buyback is aimed to resolve a dispute by concerning the details of the arbitration course which is in contrast with the perspective of International model of buyback. Although applying such policy will create the more structural course of arbitration, it results in to a high limitation on the party autonomy as the most important element of every contract which leads to generate the unnecessary restrictive provisions, and subsequently demotivates foreign contractor to engage Iranian oil industry²⁶⁹. The reform that this study proposes on the basis of evolutionary approach is integrating the provision of arbitration from the international model to the Iranian buyback

²⁶⁷ Me. M., The Iranian Buyback Model and Its Efficiency in the International Petroleum Market - A Legal View, OGEL Journal, Dundee, Vol. 7 - issue 1, April 2009

²⁶⁸ Me. M., The Iranian Buyback Model and Its Efficiency in the International Petroleum Market - A Legal View, OGEL Journal, Dundee, Vol. 7 - issue 1, April 2009

²⁶⁹ Dominique Bruhn, Space for local content policies and strategies, Investment Law and Policy at the Columbia Centre on Sustainable Investment, 2016, p 25

model to ensure the freedom of choice of parties in buyback to agree on the details of arbitration course, and more importantly to award any contractor that chooses Iran, and Iranian law in the arbitration course as a financial incentive to ensure the interest of Iranians in arbitration course. Applying such reforms will change this legally binding provision to financially incentive term which does not only breach any barrier but also modernises the Iranian model of buyback.

d) The applicable law of contract: Little space for party's choice of law

A further significant issue related to dispute with regard to the terms of buyback is the governing law, as different jurisdictions have different sets of rules for considering the remedial subjects, assessing the validity of contract and interpreting of the contractual terms.

While Under Article 18 of the international model the guiding jurisdiction is the one defined within the contract, the Iranian version of the model explicitly clarified the set of rules to govern the agreement, and accordingly leaves little space to exploitative interpretation. For the purpose of falling the contractor's activities within the jurisdiction of domestic judicial system, Iranian buyback, in Article 7.2, prescribes that 'a branch of foreign company shall be restarted in Iran to ensure such legal coverage. In line with establishing judicial jurisdiction by registration of a branch of company the Article 3.1 clearly expresses the legal system by which the contract should be performed. Article 3.1 declares that agreement will be ruled and conducted based on the Iranian law', therefore, it defines the Iran's law as main governor of agreement, and subsequently eliminates any problems that may arise from issues of jurisdiction²⁷⁰.

Consequently, whereas the international model in the issue of governing law grants the full discretionary power to parties by relying on the related terms of contract to determine the choice of law, Iranian buyback through the registration of company's branch in Iran forces parties to follow the domestic law, even though, it provides legal certainty, as well as resolving any dispute over indicating the choice of law, nevertheless, it limit parties' autonomy in the contract. Imposing such a limit on the parties' choice of law decreases the attractiveness of the model, as a result, this work suggests to apply the related provision of

²⁷⁰ Article 16.2 of the international model rules of buyback contracts drafted by the United Nations Economic Commission for Europe/
http://www.ierc.bia-bg.com/uploads/vtcontract/files/vtcontract_00743d3417d145769033e1b5c06e4113.pdf p 14/ Access on June 2016

international buyback, as well as, providing financial incentives such as tax reduction for those foreign contractors which choose Iranian law of buyback as the choice of law. This solution will remove the above-mentioned restriction to absorb more investments, and also will motivate foreigners to choose Iranian buyback law.

e) Termination of the agreement: Lack of relevant provision in Iranian buyback

As it has been pointed out in the last chapter the legal framework of Iranian buyback needs to include more provisions to govern the related issues to the buyback. This is because of the fact that non-existence of the relevant legal issues to buyback will require extra negotiations which results in to postpone the beginning of the project as one of the foreign party's' complaint, and subsequently leads to loss of both parties' benefit. The issue of termination of an agreement as the last resort solution, subsequent to the failure of other choices including negotiation, and preliminary arbitration is a significant subject that has been ignored in the Iranian version of buyback²⁷¹. Thus, containing of such provisions seems essential in order to ensure legal certainty in the contingency that termination does become necessary.

While the International model concerns this issue in deep, there is no such provisions are existed in the Iranian equivalent. Article 16.1 of the international model rules that if the original contract is terminated before any changes in the technological, and logistics material, the contract will be nullified. Moreover, Article 16.2 stated that within this agreement, the seller's responsibilities will:

(A) Be considered as finished even in cases where one of the sub-contracts is subsequently terminated, as long as such an event occurs not as the result of the seller's actions.

(B) Will not be considered as satisfactorily concluded if any sub-contract is subsequently terminated, no matter the reasons. In such situation the seller is obliged to conclude additional sub-contracts which would be equivalent to the value of the original contracts that have been terminated. Therefore, Article 16.2 elucidates what will occur in respect to the seller's other duties, if the buyback contract or part thereof be terminated, moreover, it

²⁷¹ Mohammad Reza Saber, Buyback Contracts in Upstream oil and gas sector and its legal effects, International commercial law PHD dissertation, Azad University, International Postgraduate Centre, 2007, Tehran. P 12

ensures that both sides know their positions if the contract be terminated by either side²⁷². As a result, the position under the International agreement regarding the topic of termination of the contract is clear and precise which results in less legal confusion of parties, and more certainty of the governing law of the contract that makes the model more favorable for both parties from the legal point of view, as they can legally foresee their contractual actions.

In contrast to the international scheme, the Iranian model does not include specific provisions regarding termination of contract, thus, the dispute is supposed to be resolved by arbitration, with the extent of compensation or loss of assets according on the stage of operation. Nevertheless, the lack of such provisions may create significant level of confusion, legal action and untrustworthy for future business relationships in the case that termination is seeking by one of the parties, due to changed circumstances. Accordingly, it is a crucial shortcoming of the Iranian form of buyback that no contingency scenarios are expected for cases where termination is seeking, whereas this issue has been illustrated specifically in the International version. This deficiency which led to create confusion, long negotiation and bureaucracy will act to make the Iranian buyback unattractive through burdening a legal risk on contractor, due to the fact that IOC cannot rely on the framework of the model in the event of dispute²⁷³. The reform that this study proposes based on above-mentioned comparison is applying the evolutionary approach through establishing the special institute inside NIOC to provide the legal consultancy in order to update, and improve the provision of the governing law of Iranian buyback²⁷⁴. Applying such reform will offer a more reliable legal framework to foreign contractor, and subsequently will encourage the foreign investors to participate the Iranian oil industry through removing the above-mentioned risk, moreover, this reform from the national view will increase the quality, and reputation of Iranian legal framework amid other oil producers countries with no clash with any existing barriers in Iran.

²⁷² Farnejad H., Strategic Approach & Legal Implications of Investment in Geopolitically Sensitive Iran Pp 19-21 (Unpublished LL M Dissertation & PhD Progression submitted to CEPMLP, Dundee, 2006). P 8

²⁷³ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006 p 34

²⁷⁴ *ibid*

f) Issue of time schedules for operation activities: Non-existence of relevant provision, as a result of overruling the issue of contractual duration

Since responsibilities and remuneration are related to the performance of obligations within certain time frames, issues of time schedules appears significantly crucial in a highly structured contractual atmosphere. Such issue is even more important in the concept of buyback product-oriented origin of the model which requires more attention to the time frames within which such goods supposed to be manufactured.

Article 10 of the International model rules the vital issue of the schedules for carrying out the obligations under the contract. Noteworthy, failure to follow the time schedules for contractual responsibilities may result in to penalties against the breaching party through remedies clarified on Article 14. Article 10.2 defines the practicing a detailed time plan by clarifying the completion of number of commitments at different time frames and stages. Article 10.5 expressed that adequate Implementing Agreements to cover the whole of the seller's buyback responsibility as agreed under paragraph 4.1 above, shall be established via a fixed date negotiated between the parties. Moreover, Article 9 emphasises that the conditions for the supply of the product including the time scale and the location shall be negotiated in each distinct phase of the operation. Accordingly, based on mentioned articles, international model place the main emphasis on timely deliveries of the goods concerned, as well as the consequences of late delivery, thus, the issue of length of the actual contract is less being focused. In contrast to the international version of buyback, Iranian model put all its focus on the duration of contracts, as it is discussed from the view of criticisms of buyback and the sight of comparison of the Production Sharing Agreements model in the first and second sub-chapter respectively, and accordingly does not pay attention to the issue of time schedules for operation activities, even though this is a vital issue in the contract that can lead to many ambiguity and commercial loss of parties. Consequently, lack of such attention in Iranian buyback demonstrates the difference between Iranian oil contracts and the International model, due to specific concerns of dealing in oil²⁷⁵.

²⁷⁵ Chilenye Nwapi , A SURVEY OF THE LITERATURE ON LOCAL CONTENT POLICIES IN THE OIL AND GAS INDUSTRY IN EAST AFRICA, the School of public policy, university of Calgary, Volume 9, 2016. p 17

This study in line with the evolutionary approach suggests that the issue of schedules for operation activities needs to be included in Iranian governing law of buyback based on considering the length of contract, estimated capacity of the field and the necessary operation to reach the highest production rate. Such provision can increase the clarity of Iranian buyback model, ensures the benefit of both parties in contract by avoiding any extra negotiation which will lead to create a more attractive version of Iranian buyback

g) Assignment Clauses: discretionary power in favour of NICO

The assignment clause is a significant clause which decides whether to allow the parties to assign their contractual rights or commitments either wholly or partially to another party other than existing. Existence such rules are vital as lack of assignment provisions may create confusion and administrative delays. Both the International and the Iranian scheme are included certain provisions to determine the situation of transferring the role of a party to an alternative commercial entity.

Such clauses are drawn in Article A 6.1 of international contract which expresses that the seller shall not have the right to assign his rights and responsibilities without obtaining consent from the buyer in the form of a clear agreement in writing, while, such accord shall not be unreasonably suspended. Therefore, the seller is able to assign his contractual responsibilities to another party if he first informs the buyer regarding his purposes, while the buyer can only refuse where the seller's performance would be unreasonable, in particular where the assignment would adversely affect the other party's interests.

In contrast to international model, the subject of assignment the Iranian scheme includes only sparse attention which led to leaving less opportunities and protections for assignment to the buyer. Article 27.1 of Iranian buyback expresses that all task via supplier requires previous agreement with NIOC which would be accepted or rejected during one month after receiving via NIOC of notice that such a plan is intended. Noticeably, the NIOC has full discretionary power to either accept or reject the assignment without any requirement of the decision being 'reasonable', as is the case with the International scheme. Accordingly, this Article moves the balance in favour of the NIOC which does not seem fair, due to there is no restriction placed on the exercise of this power, moreover, it is doubtful that even applying arbitration could resolve the issue, as any refusal would be within the framework of the contract. Such granted discretionary power will generate unnecessary restriction for

forging contractor with no commercial benefit got the national party²⁷⁶. Therefore, this study for the aim of increasing the commercial efficiency proposes the integration of this provision from international model which is not in contrary to any barrier in Iranian law. This integration can motivate foreign investors to join the Iranian oil sector, as they have the right to apply assignment clauses if they need to do so.

h) Re-Sale destinations: Exorbitant liberal view of Iranian buyback

The resale of output to a third party is an additional way of achieving revenue through buyback transaction; however, political or commercial concerns may result into parties decision to restrict the destination of such transactions which is provided in Article 7 of International contract²⁷⁷. Article 7.1 expresses that the seller or any other legally empowered party obtains the right to resell the product within the territory defined by clause 7.2 below:

(A) 7.2 the region will include all nations.

(B) 7.2 the region will contain all nations indicated within the appendix for the certain types of goods.

(C) 7.2 the area shall comprise the seller-land.

Based on Article 7.3 the product cannot be resold anywhere but inside the defined area without divided contract from the buyer.

Article 7.4 prescribes that the parties will follow the commitments above without seeking to actively market the products anywhere but within the authorised regions.

Accordingly, this clause will affect the value of the contract, as if the seller intends to resell the products , he may be restricted by Article7, while the wider the seller's discretion on whom he can sell to, the greater profit in the contract and, therefore, the contract itself will be more valuable. Nevertheless, apart from the existing exception in Article (A) 7.2, the seller is not permitted to offer outputs in the market beyond the agreed territory, unless the written accord from the buyer is obtained, thus, this clause grants the buyer the power to have control over the seller's potential income in a market other than agreed one.

²⁷⁶ Chilenye Nwapi , A SURVEY OF THE LITERATURE ON LOCAL CONTENT POLICIES IN THE OIL AND GAS INDUSTRY IN EAST AFRICA, the School of public policy, university of Calgary, Volume 9, 2016. p 17

²⁷⁷ Me. M., The Iranian Buyback Model and Its Efficiency in the International Petroleum Market - A Legal View, OGEL Journal, Dundee, Vol. 7 - issue 1, April 2009

In contrast to the limiting rules on the issue of reselling the output generated through buyback in the International model, the Iranian version follows an entirely liberal position by not restricting the target of resale. Therefore, such liberal approach may provide opportunities for generating income from the oil sale beyond the original territory of contract. Although this provision is attractive for foreign investor, such exorbitant liberal view is in contrast with the essence of the mechanism to protect the national interest of Iranians in petroleum deals, as it is possible that the country in some circumstances may need to ban the reselling of product. Therefore, this work on the basis of evolutionary approach prescribes that the Iranian governing law of buyback should integrate the International provision of reselling the oil product in order to make the balance between the preserving the national interest and absorbing foreign investments.

i) The conformity of final product under the contract: Lack of any criteria in Iranian buyback

Since buyback model can be used to conduct oil extraction, as well as variety of other production processes, the issue of conformity of final product under the deal becomes significant, even though the main obligation of the contractor in buyback agreement is achieving the production target. This because of the fact that the certain rules to assess the final product can prevent any dispute which will lead to loss of both parties' benefit and delays the project. As a result, an extensive part in the International model is devoted to prescribe quantity, quality and delivery times of the output involved. Article 2 attempts to identify specific criteria for assessing the product under the contract. Under Article 2.2, the seller commits to the availability of the prescribed product based on the timetable set out in Article 10. Moreover, according to Article 3.1, the product will have the pre-agreed attributes, be of the agreed amount and also correspond to the sub-contracts created for their purchase, known as "implementing contracts". In fact, these are fairly standard terms of contracts which implied by legislation in jurisdictions such as the United Kingdoms' SGA 1979²⁷⁸. Therefore, deliberation of pertinent provisions in the International version demonstrates that this contractual area is significantly more precise than the arbitration

²⁷⁸ Shahri, Nima Nasrollahi. "The Petroleum Legal Framework of Iran: History, Trends and the Way Forward." China and Eurasia Forum Quarterly, vol. 8, no. 1 2010

section which is resulted to greater reliability but less flexibility. Accordingly, conformity of goods to the standard desired is a fairly common sense requirement, the level of scrutiny arranged by the International scheme seems to be proper, whereas under the Iranian version, no emphasis is placed on the issue of output conformity in the oil contract which illustrate an important comparative disadvantage in Iranian buyback. This disadvantage potentially will create the dispute between the parties, and subsequently demotivates the foreign investors. This study proposes the integration of this provision of International buyback to Iranian version, as it ensures the benefit of both parties through minimising the disagreement, and accordingly exceeding the production activities, moreover, such an integration will not breach any barriers in Iranian buyback, thus, it is applicable on the basis of the evolutionary attitude.

Overall, this sub-chapter considered the nine vital issues in Iranian and International mechanism of buyback through providing the critical comparison of the two models. This comparative analysis has been carried out to evaluate the efficiency of Iranian buyback's provisions to point out its deficiencies, and more importantly to offer the necessary applicable solutions for the aim of making the Iranian buyback more competitive via integrating the advantageous terms of the international buyback²⁷⁹. Accordingly, it has been demonstrated that the Iranian version of buyback, as a result of unnecessary restrictive provisions, ambiguous terms and lack of certainty in its governing law has considerably lower efficiency in comparison with the international scheme with regard to absorbing foreign investment²⁸⁰. As a result, this study in this sub-chapter offered applicable reforms through highlighting the more attractive provisions of the International model of buyback compared to their Iranian version to revise the mentioned shortcomings of Iranian buyback for the final aim of Iran to absorb more foreign investment in its oil industry. The next sub-chapter in line of chasing the most appropriate solutions for the future development of the model as the main question of this research will examine the applicability of the production sharing agreement for the particular region of the country in the current legal, political and economic environment of Iran.

²⁷⁹ Economic Efficiency and Optimal Contractual Design of Oil Service Contracts: The Cases of Iran and Iraq Ghandi, Abbas. University of California, Davis, ProQuest Dissertations Publishing, 2013. P13

²⁸⁰ *ibid*

4.6 Introduction of Production Sharing Agreement for Caspian Sea: Inapplicability of the proposed model

As it has been mentioned in the second chapter of this work the production sharing agreement has been practiced in Iran for short period of time which increased the income of the government in petroleum dealings. However, allowing the ownership of oil product by foreigners which was on the basis of PSA model confronted with the essence of the nationalisation event that resulted in to introduction of buyback with restrictive provisions following the 1979 Islamic revolution²⁸¹. Further to this previous experience of Iran in applying the PSA, recently, this model has been supported amid some Iranian officials; however, there has been confusion among them regarding the concept of PSAs, as there is the trend for mixing the concept of PSA, and straight possession of oil recourse. As already mentioned in the last chapter the straight possession, and exclusive right over Iranian natural assets have been forbidden by the Iranian Constitution, while PSA necessarily does not require²⁸² the ownership of mineral reserves²⁸³, therefore, there would be no Constitutional prohibition on PSA model that does not include transfer of any reserves²⁸⁴. As a result, this issue has been debating in the Petroleum Ministry and parliament to consider the possibility of adoption of PSA for the Caspian block, due to higher risk of field's discovery, as well as the high competition between Iran's neighbors such as Azerbaijan and Turkmenistan²⁸⁵. The investment department of national Iranian oil company proposed the high cost of the operation as barrier that would confront foreign companies, therefore, Iran was examining possibility of moving towards to PSA for the Caspian offshore. However, Gholamhossein Nozari, the previous Iranian oil minister rejected application of PSA regarding the north of Iran by identifying PSA model is as old-fashioned type of petroleum deal for the country. He clarified that the modified version of Iranian buyback can provide adequate incentives for investors. These conflicting statements highlighted the Iran's internal dispute regarding Iranian model of petroleum contracts, thus, it is expectable that any effort for adoption of PSA which may be recognised as a constitutionally prohibited

²⁸¹ S.N.Ebrahimi, A. Shiroui Khouzani, *The Contractual Form of Iran's Buy-back Contracts in Comparison with Production Sharing and Service Contract*, PEDEC, 2003 p 13

²⁸² Zhiguo Gao, 'International Petroleum Contracts; Current Trends and New Directions' (1994) p 123

²⁸³ Kirsten Bindemann, 'Production Sharing Agreements: An Economic Analysis, Oxford Institute for Energy Studies' (1999), at p. 85. Ernest

²⁸⁴ E. Smith, 'From Concessions to Service Contracts' (1992) 27 *Tulsa Law Journal* 493, 522

²⁸⁵ Alexander Brexendorff et al., 'The Iranian Buy-Back Approach' (2009) 7 *Oil, Gas & Energy Law Intelligence (OGEL)*, P 11-14

would take even greater political obstacles, as well as longer duration. Therefore, while some officials proposed the PSA without granting any ownership rights to the foreigners, other voices still support efforts to amend the current mechanism which have been continued for more than 10 years to provide incentives for investors. However, the Caspian would seem as a clear exception to the buyback model, as the offshore operations' expenses would be higher than onshore fields, thus, investors may not fund the project if they solely bear the risk of operation, therefore, this has been asked all the time to enjoy more friendly provisions for investors. Moreover, Iran has been faced the high competition with the neighbours contest, as they have proceeded with Caspian developments²⁸⁶. Hence, it has been argued that PSA shall be exercised merely in Caspian province, and not in for Southern part blocks of the country, however, the limitation scope of PSA to Caspian sea would generate a greater opposition, due to it can be deduced as the admission of insufficiency of Iran's government selected model. Therefore, in order to justify this exclusion regarding the Iranian typical method of petroleum transaction, the government needs to demonstrate a sense of urgency on the Caspian block which requires longer time, and more legal and political efforts in the current situation of high competition on Caspian Sea oil fields; thus, it cannot be an applicable solution, owing to political obstacles towards any shift to PSA, as well as, lack of any legal preparation to adopt, and justify radical change to the production sharing agreement model²⁸⁷. Accordingly, the special situation of the Caspian Sea oil fields that has been examined in the current sub-chapter proves the accuracy, and the necessity of applying the evolutionary reforms to modernise the model through rendering changes in order to make the buyback more attractive for foreign contractor through minimising commercial risks, and creating more financial incentives. Such a view which has been chosen by this study is applicable in the current political and legal framework of Iran, as it does not breach any obstacles, and more importantly does not have high legal and political expenses for the country, particularly following the successful nuclear negotiation which led to lifting the sanctions. Such sanctions which suffered Iranian economy had terrifying effect on Iran's oil sector that will be discussed in the next sub-chapter.

²⁸⁶ Maximilian Kuhn and Mohammadjavad Jannatifar, Foreign direct investment mechanisms and review of Iran's buy-back contracts: how far has Iran gone and how far may it go? *Journal of World Energy Law and Business*, 2012, Vol. 5, No. 3, P 223-227

²⁸⁷ Heiss, M. A. 'National Interests and International Concerns', *Journal of Iranian Research and Analysis*. Vol. 16, No.2 November 2012 p 8

4.7 The International sanctions on Iranian oil sector: Harmful economy effect for the country

Following the successful nuclear deal, and subsequently removing the sanctions in 2016, it seems essential for goal of present research to analyse sanctions' effects on Iran's economy with particular reference to oil sector. This analysis is significant to prove the unattractive feature of Iranian model of buyback, and its role in aggravating the impact of sanctions. Moreover, this sub-chapter will show the necessity, and applicability of improving the model from the economy and national security point of view in order to suggest the probable future developments in this area.

The United States has practiced economic sanctions against other countries in order to enforce its foreign policy demands, and pursuing certain objectives in such countries. Such sanctions have been carried out via other methods, such as pressure exerted through global entities including the UNSC and EU. Thus, the US through utilising diplomatic forces, and methods of coercion attempted to promote objectives it sets to achieve, such as deterring access to nuclear, biological and chemical weapons in different countries, especially in the Persian Gulf states, as they are of particular attraction to the United States, due to their abundance of natural resources. In Iran however, since the Islamic Republic has come into power, US demands and coercion through indirect means have not gone unchallenged. Initiated by President Carter in 1979, sanctions and other similar measures have continued, taking shape in various forms, till the present date²⁸⁸. The US for the purpose of preventing countries from concluding a business deal with Iran has equipped itself with variety of means including Iran-Libya Sanctions Act (ILSA), 1996, Iran Sanctions Act (ISA), 2006, and comprehensive sanctions in 2012.²⁸⁹ Moreover, the US utilised other legal powers to enforce secondary sanctions such as foreign-owned companies with access to the American market may be found culpable if conduct business with individuals, firms or governments with alleged terrorism links. Companies affected by such measures include banking groups

²⁸⁸ Institute for International Economics, Case Studies in Sanctions and Terrorism Case 84-1 US v. Iran, 2001 [www.iie.com/research/topics/sanctions/iran.pdf]

²⁸⁹ Estelami, H. 'A Study of Iran's Responses to US Economic Sanctions' Middle East Review of International Affairs (MERIA) Journal, Volume 3, No.3, Sep. 2015

in particular, such as ABN Amro, UBS Bank of Switzerland, HSBC and Credit Suisse, who all curtailed business operations within Iran on the basis of the above legislation²⁹⁰.

Historically, US sanctions have started from November 1979, after removing the Shah regime where President Carter subsequently froze all Iran's assets in America. President Reagan in 1987 initiated the sanctions with the passing of the Iran-Iraq Arms Non-Proliferation Act in 1992 which banned the exports of commercial arms sale, nuclear technology, missile technology, and sales of dual-use items. In 1995 Senator D'Amato presented the Comprehensive Iran Sanctions Act, followed by the Iran Foreign Sanctions Act which was named by himself as the Iran-Libya Sanctions Act. This Act penalises any American company investing in Iran and Libya, regardless of the amount, as well as, those foreign corporations that fund projects with greater worth than 20 million US Dollar within oil and gas relevant sector. Moreover, based on this Act the US President was granted the right to impose up to two of following six sanctions: the imposition of a maximum of \$10 million by all US financial institutions as a loan ceiling, restriction on US trade assistance, prohibition of company's imports and services in the US, the withdrawal or denial of licences approving the trading capacity of the company and prohibition from acting as a primary dealer of US treasury bonds. Noticeably, this Act, which was known as ILSA, was extended and changed in 20 September 2006 to the Iran Sanctions Act, because of terminating sanctions on Libya. The new Act was designed to stop Iran's progress in the field of nuclear programme, and also to deter its available funds granted to terrorist organisations, made effective through Executive Order 12957, prohibition of American investment in the petroleum and the Executive Order 12959 regarding the forbiddance of investment and trade with Iran in any manner or form, issued in 1995²⁹¹. In fact, such legislation was aimed to limit the amount of investment in Iran by enforcing companies to follow the rules in order not to negate access into the American market. The House of Bill 6198 in December 2011 extended the ISA until 31 December 2016. Moreover, it restricted sales of WMD technology or other advanced weaponry to Iran, and provided for the

²⁹⁰ Schott Jeffrey J. The Iran and Libya Sanctions Act of 1996: Results to Date, Institute for International Economics. [<http://www.petersoninstitute.org/publications/papers/paper.cfm?ResearchID=285>] date of access: 5th November 2006

²⁹¹ The Iran Foreign Sanctions Act- S.I228, Hearing before the committee on Banking, Housing, and Urban Affairs Washington, 2 Editions, October. 1995, pp. 24-48

prevention of money laundering by terrorists, and criminal groups²⁹². In 2012 following the huge progress of Iran in its nuclear programme the US Treasury Department have attempted to negotiate a military strike in order to coerce Europe and Russia to expand the Iranian economic sanctions in order to increase effectiveness, and to halt Iran's nuclear programme. In fact, the US was intended to enforce Security Council sanctions against Iranian government via means of a wide-reaching travel ban, and by restricting the government's capacity to conduct business outside its territory. Moreover, US officials have also endeavored to force International banks to take other measures to block Iranian nuclear advances²⁹³. As a result, the US government could convince the European Union and the United Nation Security Council to provide comprehensive sanctions regarding Iranian oil sector, and bank transactions in order to stop Iran to develop its progress in nuclear field. Such sanctions were designed to deprive Iran from the International oil market to minimise the country's economy scope. Therefore, any Americans or International company or bank which deals with Iran in the field of petroleum industry, and bank transaction would be harshly penalised, and subsequently being embargoed, for instance Amro had been fined \$80 million for not issuing a full report in its dealing with the Iranian Bank, Melli, HSBC, Credit Suisse and Commerz bank A.G. have halted dollar transactions²⁹⁴. On the other hand, the US Sanctions on Iran have adverse impact on the US economy both directly and indirectly. This is because of the fact such sanctions resulted into financial loss for US through decreasing the bilateral trades which calculated on the basis of total GDP's of the primary participants in the country's economy, namely, Germany, France, Italy, China and South Korea, shows that they amount to roughly \$12 trillion. Iranian imports from its trading partners amounted to an estimate of \$4.3 billion, in 2006, and further increased in 2009, where its imports rose from \$12.7 to \$21.2 billion by 2010, according to data collected by the Central Bank of Iran.²⁹⁵ Moreover, in exchange, \$7.1 billion of services and goods, by Iran's major trading partners, assuming fixed percentage shares of the trading

²⁹² Ibid p 57

²⁹³ Ibid p 63

²⁹⁴ Senate Hearing, The Comprehensive Iranian Sanctions Act of 1995 - S. 277 (1995, p. 24).

²⁹⁵ Cooper and Sanger, 'A rift emerges over US policy toward Iran', The International Herald Tribune, June 15, 2007 [<http://www.ihb.com/articles/2007/06/15/news/iran.php?page=2>]

partners, was imported to Iran²⁹⁶. Assuming instead that Iran would have imported such an amount in dollars, then subsequently the United States is losing \$6.2 billion every year, in the form of exports because of its embargo. Research conducted at the Institute for International Economics demonstrates the effect of the sanctions on jobs, wages and trade within the US. American exports to the twenty six states being affected by trade measures, in 1995, diminished to a threshold of \$19 billion below the expected level²⁹⁷. The loss of such exports would invariably lead to a figure of 200,000 of job reduction, and cause the loss of up to a billion dollars in salary bonuses alone for American employees, thus, many US companies have expressed regret towards the sanctions, which have the effect of denying them access to Iran's energy fields, unlike their non-US counterparts²⁹⁸. Accordingly, the sanctions have also had repercussions on the US economy, costing the US billions of dollars per annum, and increasing unemployment amongst American workers, who, as a result of the sanctions, lost their jobs, ²⁹⁹however, since the US economy is larger than Iran's economy, and more importantly, unlike Iran, the US economy is not based on oil industry, the effect of sanctions for Iran was seriously more terrifying than US for instance collapsing of the Iranian currency, thereby decreasing the value of exports which led to suffer non-oil exports in particular, as their value has lessened by 75%, exacerbating the state of the foreign-exchange debt³⁰⁰.

Iran has used to be a major player in the global oil markets and is one of the largest oil producer and exporter amongst the OPEC countries. During the last decade, Iran on average exported roughly 2.5 million barrels a day. In 2010, however, oil prices has risen four times the price a decade ago, to about \$60 per barrel of oil, and as a result, Iranian oil exports have increased to more than \$46 billion in 2012, from a meagre \$15 billion in 1995, thus, Iran received an increased amount of \$30 billion, more than that which it obtained twenty years ago³⁰¹. This rising of price expanded Iran's economy in order to widen and fasten its

²⁹⁶ Congressional Research Service (CRS) Report for Congress, The Iran Sanction Act (ISA), Kenneth Katzman, [http://www.fas.org/spp/crs/row/RS20871.pdt]

²⁹⁷ Torbat, A.E., 'Impacts of the US Trade and Financial Sanctions on Iran' 407, (2015)

²⁹⁸ World Bank News Release No. 2000/352/S {May 2010}.

²⁹⁹ The Independent on Sunday, UK hanks caught in Iran sanctions probe, 5th February 2008, [http://news.independent.co.uk/business/news/article343200.ece]

³⁰⁰ Odone, Toby, 'Iran: A Test Case in Opening Its Oil Fields to Foreign Investment in the Slow Way', paper presented at the Institute for Global Management & Research, George Washington University, DC (October 2007).

³⁰¹ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKewijvqm3sMfUAhUEPQKHVa-ARAQFggIMAA&url=http%3A%2F%2Fwww.cnb.com%2F2017%2F04%2F06%2Freuters-america-iran-struggles-to-expand-oil-exports-as-sea-storage-cleared.html&usg=AFQjCNHQuC8P_N84uaBEhd7K0FpDbBSEw/ Interview with Iran's oil minister / Access on July 2016

nuclear progress. Therefore, the US has tried to apply stricter policy in order to demean the power of Iranian adventurism, through sanctions and diplomatic measures. Damage done to the Iranian economy due to the global embargo has been created mainly because of lack of investment which they have caused. In fact, Iran would have been able to sign more beneficial contract with greater feasibility of success and security without sanctions³⁰². This is because of the fact that sanctions aimed to force Iran into contracts that were far from ideal for the country, and was further coerced in funding itself through various sources at a high price, as a result of US manipulation of foreign aid and financing. Therefore, the dominant impact of sanctions has been a dramatic reduction in the funds that Iran has needed for the development of its oil projects. Owing to the highly capital nature of the oil businesses in Iran, a lot of investment is required for the developing of such an industry³⁰³. A lot of the national Iranian oil companies, such as onshore oil fields, have been in dire need of re-structuring and re-development, as a result of the Persian Gulf War, additionally, Iran in the past faced the necessity of developing several of its untapped fields. Such development work needed capital which Iran lacked, and which, due to the sanctions, was unable to receive in the form of debt or loans. Thus, the IOC's cost on the development of buyback projects resulted into debt for Iran that more financial difficulty creates for the country as IOCs have to be rewarded for all their investment as well as extra costs undergone in the process. Sanctions effectively restricted Iran's negotiating powers in petroleum deals, and subsequently faced Iran with situation that had to offer high rates of return for investment as an incentive to investment. Therefore, Iran had to drop the originally proposed 10%, and offered on average between 15% to 18% rates of return to foreign investors, for instance the South Pars and the Sirri oilfields, both signed with very high rates of return, and close to those demanded by the oil companies themselves³⁰⁴. Such excessive charges can be used to calculate the cost of such projects to Iran³⁰⁵. More importantly, the unattractive nature of Iranian buyback with its restrictive provisions

³⁰² Ibid.

³⁰³ The Iran Foreign Sanctions Act- S.1228, Hearing before the committee on Banking, Housing, and Urban Affairs Washington, 2 Editions, October. 1995, pp. 25-47

³⁰⁴ Schott Jeffrey J. The Iran and Libya Sanctions Act of 1996: Results to Date, Institute for International Economics. [<http://www.petersoninstitute.org/publications/papers/paper.cfm?ResearchID=285>] date of access: 5th November 2006 p 12

³⁰⁵ Takin Manouchehr, Working with Sanctions, Trade Controls & Political Risk 03, Case Study: Iran, Centre for Global Energy Studies p 13

aggravated the effect of international sanction by discouraging the foreign contractors to invest in Iranian oil industry. Therefore, the International sanctions undoubtedly negatively impacted Iran's economy, and its oil sector in particular, via minimising the fund received by Iranian government; as well as diminishing the negotiating powers in petroleum deals for Iran, thereby generating less appealing terms for the country, as it strove to offer better incentives for companies abroad. Consequently, sanctions decreased the rate of Iranian extraction of petroleum from average four million barrels each day until 800,000 barrels which effectively has harm Iran's economy. Such terrifying economy effects can justify Iran's ambitious plan to boost its production rate after sanctions, and more importantly highlighted the necessity of modernising the model of Iranian buyback in order to remedy the adverse effects of sanctions. Considering the time limit of Iran to return to the market, the historical, political and legal considerations of the country, and the efficiency of the evolutionary approach this study suggests improving the terms, features and functions of the current method for the aim of proposing more attractive version of Iranian buyback rather than shifting to any other model which can potentially faces serious prohibitions³⁰⁶. Furthermore, from the geo-political point of view since modernising the current model will engage more number of IOCs to Iran's oil industry which have mutual interests with Iran's government, can help Iran to resist more effectively against potential future sanctions, thus, such improvements within the model will also ensure the national security of the country. As it has been mentioned in the beginning of this sub-chapter, the sanctions on Iranian oil industry have been removed in 2016 following the successful nuclear deal. This vital historical event which led to conclude the many years' dispute between Iran and western countries has some important influences on the current model of oil transaction which will be examined in the next sub-chapter.

4.8 The Implications of the Nuclear Deal on Iranian buyback transaction: Ambitious plan of Iran to return to the pervious portion via boosting the production rate

The necessity of reforms to make the Iranian buyback more competitive has been shown in different sub-chapters of this chapter. However, imposing the embargo on Iranian

³⁰⁶ ibid

the market for the purpose of offering necessary, and applicable reforms to make the buyback more attractive through employing the evolutionary approach.

a) The potential amount of production: Hard way for Iranian oil industry after removing sanctions

The first concern in issue of implication of nuclear deal on Iranian oil industry is the amount of additional oil that Iran can offer to global market after concluding the deal, and subsequently removing the sanctions. While it seems that Iran can supplement its current production of 800,000 barrels to bring an additional 800,000 barrels of crude oil within a year, the Iranian Oil Minister Bijan Zangeneh, in June 2015, predicted that Iran can immediately raise oil exports by 500,000 after removing sanctions, and subsequently produce a total of 4MNB within the three months. Achieving this level of export would inevitably require foreign investment in addition to releasing the Iranian frozen assets including 30 million barrels on floating storage. However, if Iran struggles to find a market for these barrels, the lifting of sanctions will not make them any more attractive to international buyers, as they may consider that the contents can damage refinery equipment³¹¹. Noticeably, despite of lifting of major sanctions on Iranian oil industry, U.S. restrictions on some kind of investments would still remain which would inhibit European investment, as well as Americans. Nevertheless, many international oil companies would be prepared to navigate difficult legal and political environments of Iran oil industry including the ideological and national opposition to foreign investment in Iranian petroleum market. Consequently, although the nuclear sanctions have been removed, Iranian government has hard way to reach its plan, as many internal and international obstacles are still existed. Accordingly, to reach the huge target of Iran to produce 5MNB/D by 2020, Iran significantly needs to have a clear strategy to compete with other oil producers countries to attract foreign investment to the Iranian oil industry. This is because of the fact that removing the sanctions itself cannot attract the investors to Iran; due to the fact that Iranian buyback as it has been mentioned in the third sub-chapter is not as favourable as other commonly used mechanism in oil dealings. Therefore, this fact proves the necessity of applying some

³¹¹ The Workshop Report , The Geopolitics of Energy Project ,The Energy Implications of a Nuclear Deal between the P5+1 and Iran , Cambridge, Massachusetts 23-24 2015, Belfer Center for Science and International Affairs | Harvard Kennedy School, Meghan L. O'Sullivan, Director, 17 July 2105, P 4-9

reforms within the current model of buyback with consideration of time limit for Iran to return to the global oil market which is the approach that this study has chosen as the evolutionary attitude to increase the efficiency of the model in attracting foreign investment with no clash with any current prohibition that can require long time, and serious legal and political preparation.

b) The low price of oil: More challenging situation for Iran to re-join the global oil market

The second topic on analysing the possible implications of the new deal on Iranian oil industry is influence of the low price of oil on returning of Iran to the global oil market. Economically, this is atrocious time for Iran to re-join the international energy markets, due to the fact that Iran should attempt to re-develop its oil sector at a time when prices are low, and global opportunities are limited³¹². Furthermore, the main response of the market of Brent crude oil to the JCPOA was dropping, as the agreed deal means the returning of a producer with great opportunities to the global oil market, therefore, returning of Iran to the market can reduce the global oil price, while Iranian inventories are stocked around 40 million bl in storage on tankers ready to be exported after lifting of sanctions through agreement in the inspections the JCPOA³¹³. Accordingly, while Iran is actively attempting to “surge” oil onto the market to develop its economic situation, the low price of oil will have adverse effect on returning Iran, as the less revenue will be acquired by the government compared to the time when Iran left the market. The impact of low price of oil necessitates applying serious reforms within the framework of the buyback to attract more foreign investments in oil sector, as the low price of oil is a demotivating element for foreign investors to participate the oil industry, therefore, as it has been mentioned in different sub-chapters of this chapter Iran needs to offer more flexible terms of buyback through utilising the evolutionary approach to renew its oil sector.

c) The regional effect of the new deal on OPEC: Geo-political influence of returning of Iran to the market

³¹² <https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=7&cad=rja&uact=8&sqi=2&ved=0ahUKEwj38sHG74DRAhUjOsAKHaE2A14QFgg-MAY&url=http%3A%2F%2Fwww.bbc.com%2Fnews%2Fworld-middle-east-33521655&usg=AFQjCNES8mron5mTcvQ9lRgViyy2UpX3wg&sig2=WKqzddMgUgODfe3dSlow9Q&bvm=bv.142059868,d.bGg> access on may 2016

³¹³ Ibid,

The last concern regarding the implication of the new deal on Iranian oil industry is consideration of OPEC re-action to returning its pervious second largest producer to the international market. Basically, the response of OPEC to return of Iran to global oil markets is critical, owing to the fact that Iran's former market share has rapidly become the market share of rival producers such as Saudi Arabia which pumped a record 10.6 million bl a day in June 2015³¹⁴. Although the additional amount of crude oil that Iran will provide to market realistically does not appear to be sufficient to create a change in the current scheme of OPEC, Iran's producer neighbors are still unlikely to return to a more cooperative approach to the oil market by restoration of the quota system within OPEC which can lead to the price war between OPEC members. More importantly, from the geo-political point of view, the current conflicts in the region, war in Yemen and Syria, has been aggravated the regional competition between Iran and Saudi Arabia. As a result, following the geopolitical competition, Saudi Arabia as the largest oil producer in OPEC will attempt to put pressure on Iran through resisting any change in quota system within OPEC in order to not allow Iran to achieve more income. Moreover, growing the new radical group called ISIS which threats the security of the Middle Eastern countries, and subsequently burdens finical pressure on them, as well as low price of oil in the global market will encourage all OPEC members, particularly Saudi Arabia to stand against any alterations leading to decrease their rate of production. As a result, the new form of geo-political competition in the region is likely to be happen, due to the fact that the countries may attempt to develop cross border fields which can result in to further tension and even conflict³¹⁵. Accordingly, the returning of Iran to the international energy market requires changes in the current rate of production of OPEC members which has the adverse effect on their interests, therefore, the OPEC members that already are struggling to the political problems, and low price of oil will be discontent to return of Iran to the market. Consequently, in such a harsh geo-political situation this study based on the evolutionary approach highlighted the fact that Iran has to employ effective reforms as they are demonstrated in above-mentioned sub-chapters to offer more

³¹⁴ <https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=17&cad=rja&uact=8&sqi=2&ved=0ahUKewj38sHG74DRAhUjOsAKHaE2A14QFghpMBA&url=http%3A%2F%2Fapps.washingtonpost.com%2Fg%2Fdocuments%2Fworld%2Ffull-text-of-the-iran-nuclear-deal%2F1651%2F&usg=AFQjCNEuwZ3KXoCINZVCKT7W89CRoJahw&sig2=xsnDObwSKIjbfMbJCMC5A&bvm=bv.142059868,d.bGg> access on may 2016

³¹⁵ The Workshop Report , The Geopolitics of Energy Project ,The Energy Implications of a Nuclear Deal between the P5+1 and Iran , Cambridge, Massachusetts 23-24 2015, Belfer Center for Science and International Affairs | Harvard Kennedy School, Meghan L. O'Sullivan, Director, 17 July 2105, P 8-9

attractive version of buyback to overcome the political and economy barriers within the OPEC to re-join the global oil market³¹⁶.

Overall, as it has been shown in this sub-chapter the new deal can provide a great chance for both Iranian and International contractors to establish commercial viable agreements through granting an opportunity for development of Iran's oil and gas fields, as well as higher income for IOCs. However, it is noteworthy that the solely removing the sanctions cannot cover all deficiencies of Iranian buyback to absorb the foreign investments which highlights the crucial necessity of required reforms in the current Iranian model of buyback. The consideration of the implications of nuclear deal, and removing the sanctions on Iranian oil sector from technical, economic and geo-political aspects which have been discussed in this sub-chapter pointed out that Iran is facing serious obstacles namely technical difficulties, low price of oil and discontent of OPEC members to return the country to the global oil market via increasing its rate of production. Such concerns emphasised that the framework of buyback has to become more flexible, and modernised through reforming its terms on the basis of evolutionary approach that does not clash with any current barriers.

4.9 The Overview of IPC in comparison with the present buyback: Great but not enough forwards steps

Following the successful nuclear negotiation, and subsequently removing the harsh sanctions which have been discussed in details in the past sub-chapter, the new Iranian government announced that Iran will offer the more attractive version of buyback with more financial incentives, and less restrictive provisions. This is because of the fact that the existing contractual scheme is not as attractive as other regional producers which prevents foreign investors to take equity stakes in Iranian companies or book reserves. Thus, the new

³¹⁶ <https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=17&cad=rja&uact=8&sqi=2&ved=0ahUKewj38sHG74DRAhUjOsAKHaE2A14QFghpMBA&url=http%3A%2F%2Fapps.washingtonpost.com%2Fg%2Fdocuments%2Fworld%2Ffull-text-of-the-iran-nuclear-deal%2F1651%2F&usg=AFQjCNEuwZ3KXoCINZVCCKT7W89CRoJahw&sig2=xsnDObwSKijbFMbJCMC5A&bvm=bv.142059868,d.bGg> / access on may 2016

Iranian government have realised that in order to attract the estimated rate of foreign investment, the terms of current financing method shall be made considerably more relaxing.³¹⁷ As a result, the international oil and gas companies began to prepare with great interest to consider the proposal of Iranian government regarding new contractual structure to govern the operation of foreign investors in the Iranian oil and gas industry, thus, many international oil companies have already visited Tehran including Shell, Eni, German and British trade delegation for the purpose of anticipation of more favorable investment terms³¹⁸. Therefore, the Iranian government truly realised that solely removing the sanctions cannot satisfy all Iran's needs to absorb foreign investments, as the industry situation, and price of oil compared to earlier than imposing sanctions have been changed which highlights the crucial necessity of required reforms in current Iranian model of buyback. However, the failure of Iranian government to obtain early economic gains in the energy sector, as well as the Conservative Party's opposition regarding the new terms of buyback led to challenges of applicability of new model of buyback, and subsequently the durability of the nuclear agreement. Moreover, the serious debate between the Government, and the Parliament regarding the necessity of Parliament, and the Security Council ratification of the new version of buyback, as well as, reaching the presidency election in the next year delayed the process of practicing the new generation of buyback, and subsequently created the huge uncertainty with regard to applicability of the model. As a result, exercising the new version of buyback depends on the political view of the next Government, thus, this fact highlights the influence of political issues on Iran's energy industry which has been historically existed, and discussed in the second chapter. Therefore, this sub-chapter is aimed to compare the new version of buyback with current method in order to analyse the efficiency of new provisions in attracting the foreign investors, moreover, the following table will demonstrate the differences of two versions³¹⁹.

³¹⁷ <https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=7&cad=rja&uact=8&sqi=2&ved=0ahUKEwj38sHG74DRAhUjOsAKHaE2A14QFgg-MAY&url=http%3A%2F%2Fwww.bbc.com%2Fnews%2Fworld-middle-east-33521655&usg=AFQjCNES8mron5mTcvQ9IRgViy2UpX3wg&sig2=WKqzddMgUgODfe3dSlow9Q&bvm=bv.142059868,d.bGg> access on may 2016

³¹⁸ Iranian nuclear deal - new opportunities in the oil and gas sector, July 17 2015, First access on 30 August 2015 http://www.cms-lawnow.com/ealerts/2015/07/iranian-nuclear-deal--new-opportunities-in-the-oil-and-gas-sector?cc_lang=en

³¹⁹ <https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=2&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFgggMAE&url=http%3A%2F%2Finfo.vedomosti.ru%2Fevents%2Fmaterial%2F19563%2F%25D0%25AD%25D0%25B4%25D0%25B4%25D0%25B8%25D1%2581%25D0%25BE%25D0%25BD%25D0%25B0%25D0%25BD%25D0%25B3%25D0%25BB.pdf&usg=AFQjCNF5vWQeJekfQcGFOqeRI4-OZ1fMw&sig2=8eUmamQONNSvVFomaSspeg&bvm=bv.142059868,d.bGg> / Access June 2016

The value of the generated oil in Iran before the sanction was about \$100 billion through the buyback which was a massive growth compared to \$40 billion generated in the past twenty years³²⁰, however, Iran still desires foreign investment for development of its petroleum industry, particularly in exploration phases which need enormous investment³²¹, as well as, to finish several exploration fields that their probability of success is almost 70% such as the Karoon province (Azadigan, Dar-Khoveen and Yaaran) which is capable to generate 2,000,000 b/d during 60 months, while the current production rate is 700,000 barrels per day. Therefore, it was estimated by the Iranian Oil Minister that Iran requires minimum \$40 billion for increasing the oil generation of 4,600,000 b/d³²², thus, the country is extremely concerned for absorbing international investment for modernising the petroleum productions, and also growing amount of petroleum production as Hassan Rohani, the new president of Iran, highlighted at the 44th World Economic Forum in Davos, Switzerland in January 2014, present situation of Iran's petroleum industry, its necessity for foreign investment³²³, and subsequently invited international oil companies to invest within Iranian petroleum projects by announcing the Iranian government's purpose to offer the more flexible version of buyback³²⁴. Thus, He, the current president of Iran Hassan Rohani, pointed out the most significant elements within the future category in Iranian buyback which are below:

Abolishing all fiscal as well as practical barriers with consideration of the borders of the common global legal framework in order to develop the relationship between the country and other International petroleum corporations.

Offering more attractive agreements for IOCs as an incentive for cooperation with the country within the discovery as well as operation activities

³²⁰ <http://www.mehrnews.com/TextVersionDetail/2305867>. access on May 2014

³²¹ Ibid

³²² www.bbc.co.uk/persian/business/2014/05/140509_zangane_oil_iran.shtml Page 2 of 203. access on May 2014

³²³ "Vijegi-haye Nasl-e Jadid-e Gharardad-haye Nafti-e Iran," Pars News, January 24, 2014, accessed February 28, 2014, <http://www.parsnews.com/>

³²⁴ Christian Campbell, *Legal Aspects of Doing Business in the Middle East* 2009, (np: Yorkhill Law Publishing, 2009), 4-5; "pishbini-e saderat-e naft-e Iran be Oroopa va Amrika," Fars News Agency, August 29, 2014, accessed: October 11, 2014, <http://www.farsnews.com/newstext.php?nn=13930607000299>.

Conveying new knowledge to the country's oil sector for growing national skills, in order to enable domestic corporations to contribute to IOCs within international petroleum market, as well as industry³²⁵.

Accordingly, the Iranian Oil Minister, Bijan Namdar Zanganeh, emphasized that the major aims of these contacts are encouraging the foreign investments, as well as, transferring the newest technologies in oil and gas upstream operations³²⁶. Moreover, the department of reviewing agreements within NIOC stated that, "Signing the win-win contracts" would be the NIOC's preference regarding defending the "national interests of the country"³²⁷, moreover it has been pointed out that such agreements are not established to recognise the "ownership right" in favour of for international companies³²⁸. Thus, applicability of any radical change towards another model containing the permission of foreign ownership of oil product such PSA has been rejected, while the strategy of the new government is practicing the evolutionary approach in order to increase the efficiency of the buyback³²⁹. On this basis, the new version of Iranian buyback with its changed terms has been debated amid Iranian officials³³⁰.

As an consultant of Iranian petroleum department dealing with creating the new transaction method, Mehdi Hosseini, has proposed the flexible fee method to guarantee the profitability of buyback for foreign contractor even in the event of fluctuations in the oil price that will lead to decreasing the associated degrees of risk of compensation for the IOCs in a buyback project, while the method of payment in the current model of buyback is

³²⁵ "Vijegi-haye Nasl-e Jadid-e Gharardad-haye Nafti-e Iran," Pars News, January 24, 2014, accessed February 28, 2014, <http://www.parsnews.com/>

³²⁶ "mehvar-e barnameh-haye nafti negah be daroun ast," Shana: Iranian Oil Ministry Petro Energy Information Network, March 6, 2014, accessed: June 6, 2014, <http://www.shana.ir/fa/newsagency/213440>

³²⁷ "7 Vijegi-ye Gharardad-haye Jadid-e Nafti," Mehr News Agency, June 7, 2014, accessed: 8/30/14. <http://www.mehrnews.com/TextVersionDetail/2305867>.

³²⁸ "mayadin-e moshtarak olaviyyat-e avval dar gharardad-haye jaded-e nafti," Ilina News, February 24, 2014, accessed: July 4, 2014, http://www.ilina.ir/news/print_news.cfm?id=148281.

³²⁹ IPC vs PSA <http://iranpetroleumcontract.com/what-makes-ipcs-different-to-buy-backs-2/> Access on 06.1.2016

³³⁰ Zangemeh Interview, ALmanitor <http://www.al-monitor.com/pulse/originals/2014/02/iran-oil-contract-sanctions-energy-nuclear.html/> Access on 28.3.2016

fixed which has been discussed in the second sub-chapter that bears the risk of incomplete compensation for IOCs, as well as, the risk of non-profitability of the project for NIOC³³¹.

Although, the new version of buyback similar to the current method does not grant the discovery and exploration right at the same contract, as Mehdi Hosseini highlighted the prioritisation of the discoverer contractor to conduct the entire development operations of the field has been confirmed in this new scheme³³². Therefore, the new version in this regard does not have any particular novelty other than prioritisation right, unless, the new version proposes some financial incentives for discoverer contractors such tax reduction in order to motivate them to employ their highest technology and efforts to find oil, thus, this provision needs to be more revised, otherwise, it is still an unattractive terms of Iranian buyback. In contrast with this element of the above-mentioned provision the new scheme changed the common rule of Iranian buyback's generation via granting another opportunity to conduct further exploration, if the contractor fails to find a commercial-scale reservoir³³³, while, in other generations of buyback the agreement would be automatically nulled, if a company was not successful in discovering oil after an exploration phase. Accordingly, this new element of the discovery right provisions will decrease the high risk of oil discovering for foreign partners operating in Iranian energy fields, and subsequently can offer a more attractive feature of Iranian buyback for the aim of absorbing foreign investment³³⁴.

The new version includes a novelty regarding the cost estimation issue as it has been defined in the last sub-chapters as a significant risk for foreign contractor in buyback, owing to the fact that the price of operation in time of concluding the agreement might be vary from the time of actual operation. While in the current method the contractor is obliged to provide the cost estimation of the entire operation in the beginning of contractual negotiation, based on the new scheme, the Iranian oil ministry annually evaluates necessary

³³¹ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=4&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFgg3MAM&url=http%3A%2F%2Fwww.shlegal.com%2Fnews-insights%2Firan-petroleum-contract&usg=AFQjCNHodQhnWQuLwV5U57zHefng6k8yyA&sig2=uv_HIEbo6RWRVS8Yk1INmw&bvm=bv.142059868,d.bGg/ Access July 2016

³³² Seyyed Payam Bathayee, "haq e tarjih-e foroush-e naft baraye peymankaran," Fars News Agency, December 8, 2011, <http://www.farsnews.com/printable.php?nn=13900717000285>; "Minister: Iran's New Oil Contracts More Attractive to Int'l Investors," Tasnim News Agency, February 22, 2014, accessed: August 12, 2014, <http://www.tasnimnews.com/English/Home/Single/291220>.

³³³ Sara Vakhshouri, "Iran offers new terms for oil contracts," Al-Monitor, February 26, 2014, accessed: March 20, 2014, <http://www.al-monitor.com/pulse/originals/2014/02/iran-oil-contract-sanctions-energy-nuclear.html#>.

³³⁴ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=6&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFgg3MAU&url=http%3A%2F%2Fwww.clydeco.com%2Fblog%2Fenergy%2Farticle%2Firan-council-of-ministers-ratifies-ipc-terms&usg=AFQjCNE1kEAgoOsehefZwl3DviygCpO35g&sig2=K_ZviSuYkl6J03IjSeQ0Kw&bvm=bv.142059868,d.bGg/ Access September 2016

expenses, and preserve outcome for supplier by reviewing the reservoirs condition, so as, the contractor may be awarded if He can decrease the development costs. Although this is an improvement in the provision of the cost estimation to minimise the risk on the contractor, as conducting the annual cost estimation for the oil ministry might be sometimes hard because of lack of enough data, and technical experience which will lead to the bureaucratic process of finalising the contract, thus, this study proposes the flexible cost estimation obligation on the beginning of the project with capacity of annually being updated³³⁵. Accordingly, this solution will minimise the risk for IOC, and also does not lead to any further bureaucratic process of establishing a buyback contract³³⁶.

Basically the duration of the buyback contract as it is showed in this chapter is a crucial criticisms of IOCs which also affected the national interest of Iranians in petroleum deals³³⁷. The short duration of buyback which stems from the negative historical experience of concessions will be ended earlier than maximising the field production, thus, it is vital risks for IOCs as it is unclear that they can compensate their costs by the end of the contract. While the current buyback duration is 5-7 years with the capacity of extending the duration which leads to the bureaucratic process of negotiation, the new version proposes the duration of 20-25 years which seems more practical in oil and gas industry³³⁸. This change which does not breach any barriers, can attract more foreign investors, as it ensures the profitability of the project, moreover, it will defend the national interest of Iranians in oil and gas deals, owing to the fact that the IOCs have enough time for maximising the field production, and conducting the provisions of transferring the technology³³⁹.

³³⁵ Economic Efficiency and Optimal Contractual Design of Oil Service Contracts: The Cases of Iran and Iraq Ghandi, Abbas. University of California, Davis, ProQuest Dissertations Publishing, 2013. P17

³³⁶ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=5&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFggxMAQ&url=http%3A%2F%2Ftheiranproject.com%2Fblog%2Ftag%2Firan-petroleum-contract-ipc%2F&usg=AFQjCNG_4UrMTbDAvxl2CQ90LMVczl7pGQ&sig2=7aulNspOBXCmUKafXYN5Pg&bvm=bv.142059868,d.bGg/ Access August 2016

³³⁷ <https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=10&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFghPMAk&url=http%3A%2F%2Fwww.upstreamonline.com%2Flive%2F1179665%2Firan-hoping-for-ipc-endgame&usg=AFQjCNFC8HLZi6AS0E8MatAiFO7ybP850A&sig2=00 ViSJoZphR8wyRmvxLEw&bvm=bv.142059868,d.bGg/> Access June 2016

³³⁸ [https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=8&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFghEMAc&url=http%3A%2F%2Fen.mehrnews.com%2Ftag%2Firan%2BPetroleum%2BContract%2B\(IPC\)&usg=AFQjCNFTDyLGrPWTU5doYesjGQBRdzSCDA&sig2=CUY0WfOYCsk9nsweZLmqQA&bvm=bv.142059868,d.bGg/](https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=8&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFghEMAc&url=http%3A%2F%2Fen.mehrnews.com%2Ftag%2Firan%2BPetroleum%2BContract%2B(IPC)&usg=AFQjCNFTDyLGrPWTU5doYesjGQBRdzSCDA&sig2=CUY0WfOYCsk9nsweZLmqQA&bvm=bv.142059868,d.bGg/) Access August 2016

³³⁹ What Makes IPC Different to Buy-Backs? Iran Petroleum Contract - Project IPC <http://iranpetroleumcontract.com/> Access on 12.4.2016

In current buyback agreement the contractors are required to pay for all exploration costs and recover their investment from any production at a pre-arranged rate of return. The Capex set fixed as per agreed MDP with NIOC within 18-24 month from contract date which bears a high risk on IOCs, as they are obliged to possess the Capex in the beginning of the project. However, in contrast with Capex ceiling in the current model, the new Iranian buyback contract includes the JV will create the master development plan and has provisions to allow changes in Capex if needed such as a yearly budget and mid-range work-plan that have to be developed and approved by the JV. Therefore, as a result of this change, the risk of providing the Capex will be minimised, as it has to be dealt by JV which has more flexibility than Capex ceiling, thus, it removed a restrictive feature of buyback with no clash of any prohibition³⁴⁰.

The issue of geographical differences in oil and gas related activities is significant from the point that it is the main element in estimation of the cost of discovery and exploration phases, and subsequently the revenue of parties in an agreement. While such a vital topic is being left in the current buyback which bears high risk for those contractors working in more geographically complex field, as they have to employ more capital and efforts with the same reward with contractors operating in less complex field. However, the new scheme has this novelty to consider the complexity factor in order to assess the contractors' reward. Based on the IPC new terms, risk-reward element is connected to the complexity of fields which ensures to pay companies higher fees for 'very high risk' on- and offshore fields compared with 'low-risk onshore'. This new provision will attract more foreign investment through taking to account the issue of geographical differences in order to ensure the full compensation of the IOCs working in high risk fields³⁴¹.

Basically, the high civil risk of area where the oil and gas activities are being operating resulted in to considering the issue of civil responsibilities in petroleum legal framework. This is because of the fact that such activities may produce dangerous situations for the entire city such as fire, different sort of pollutions, disruption of water and harmful effects

³⁴⁰ Economic Efficiency and Optimal Contractual Design of Oil Service Contracts: The Cases of Iran and Iraq Ghandi, Abbas. University of California, Davis, ProQuest Dissertations Publishing, 2013. P18

³⁴¹ Iran's Oil and Gas Insights, Ambitions, Challenges and Opportunities Iran Petroleum Contract - Project IPC <http://iranpetroleumcontract.com/> Access on 10.5.2016

for the environment. However, the current buyback left aside the issue of corporate civil responsibilities which has been shown in the last sub-chapter as an important gap in its governing law³⁴². As a result, this gap led to ignoring the rights of oil field's citizens in Iran which is against the core concept of Iranian buyback to protect the national interest of Iranians in petroleum deals. In contrast, based on the new version of buyback IOCs are expected to undertake civil, and other social projects such as building hospitals, water tank and electricity system in oil-producing regions. Although this is a significant improvement in Iranian buyback in favor of Iranian citizens, it will bear another obligation on IOCs which is not in comply with the aim of IPC to provide the more flexible provisions to attract foreign investors. Therefore, this study in order to ensure the rights of oil field's citizens, as well as not to bear another obligation on IOCs proposes that IPC could determine certain financial incentives such as tax reduction for those contractors that carry out the cooperate civil responsibilities. Therefore, as this approach will award the IOCs efforts regarding the above mentioned issue does not create another contractual duty for IOCs which may be seem to be an unattractive provision, and will protect the interest of Iranians, oil fields citizens in particular. The second deficiency of this new provision is lack of consideration of environmental concerns such as pollution, decommissioning and any change to the field's ecosystem. Lack of this vital topic in both current and the new Iranian buyback, IPC, will undermine the rights of Iranians in petroleum deals, as some of such issues have to be arranged in the beginning of the operation, moreover, ignoring the environmental concerns in oil and gas operations will results in to destroying the environment which has serious social effect such as force movement³⁴³. Therefore, this study based on the evolutionary approach highlights the necessity of more comprehensive, and up-to-date model of buyback to ensure the issue of environmental concerns as a mutual responsibility of NIOC and IOCs³⁴⁴.

³⁴² https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=6&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFgg3MAU&url=http%3A%2F%2Fwww.clydeco.com%2Fblog%2Fenergy%2Farticle%2Firan-council-of-ministers-ratifies-ipc-terms&usq=AFQjCNE1kEAgOsehefZwl3DviygCpO35g&sig2=K_ZvlSuYkl6J03lJSeQ0Kw&bvm=bv.142059868,d.bGg/ /Access June 2016

³⁴³ Iran's Oil and Gas Insights, Ambitions, Challenges and Opportunities Iran Petroleum Contract - Project IPC <http://iranpetroleumcontract.com/> Access on 10.5.2016

³⁴⁴ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=10&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFghPMak&url=http%3A%2F%2Fwww.upstreamonline.com%2Flive%2F1179665%2Firan-hoping-for-ipc-endgame&usq=AFQjCNFC8HLZi6AS0E8MatAiFO7ybP850A&sig2=00_ViSJoZphR8wyRmvxLEw&bvm=bv.142059868,d.bGg/ Access June 2016

The subject of local content is vitally crucial in Iranian buyback, as this model is based on the idea of protecting the Iranian interest against IOCs. The local content in the current buyback is a part of the restrictive provision which only allows IOCs to cooperate with Iranian oil companies, thus, this provision created a restriction for IOCs, as they are required to cooperate with certain companies which could not be commercially beneficial for them. However, the IPC chooses the more flexible approach in this regard through permitting IOCs to cooperate with Iranian foreign JVs, even though, the first priority is cooperation with Iranian companies³⁴⁵. Albeit, this new provision is more flexible than the present provision of buyback, it still restricts the IOCs' choice to choose their commercial partner which led to discourage the foreign investor. As a result, on the basis of the evolutionary approach this work proposes to award contractors which work with Iranian companies, so as, this provision does not limit the IOCs' party autonomy in the contract.

Table 6: The current Iranian buyback compared to IPC³⁴⁶

³⁴⁵ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006 p 28 -35

³⁴⁶ What Makes IPC Different to Buy-Backs? Iran Petroleum Contract - Project IPC <http://iranpetroleumcontract.com/> Access on 12.4.2016

Terms of Contract	Current buyback	New Version of buyback , IPC
Ownership right	NO	NO
Method of Payment	Pre agreed/ fixed	Flexible/ Unfixed
Discovery and Exploration right	Separated	Separated with more flexibility
Cost estimation	To be conducted in the beginning by the contractor	To be annually provided by Ministry of Oil
Duration	5-7 years with No reserves booking for the IOC	20-25 years
Capex	Capex ceiling; Entire risks on IOCs	JV plan
Geographical differences	Not being considered	Taken into consideration through risk-reward element
Corporate responsibility civil	No provision	Being considered
Local content	Obligatory and Strict	Obligatory but More flexible

This sub-chapter compared the provisions of the current buyback with the new scheme of Iranian buyback named as the IPC. It has been shown that despite of all criticisms against Iranian buyback, the new reforms in buyback may be considered as great forward step for ensuring of more progressiveness, and flexibility in the model. The main attempt for the above-mentioned aim is combination of the unfixed rate of return with recognition of responsibility for NIOC to restore the IOC's margin by supplying more oil from other projects when IOC's rate of return of a buyback project is affected, as a result of falling the world oil price. This is considered as the obligation of Iranian government which distinguishes Iranian buyback with other buyback in Venezuela and Algeria³⁴⁷. Therefore, the element of offering more oil production to the IOCs in the event of declining the oil price is a significant element for ensuring flexibility of the regime which can, subsequently strengthen the bargaining power of NIOC in future energy, especially after the removing the sanctions³⁴⁸. Thus, this new deal can provide a great chance for both Iranian and International contractors to establish commercial viable agreements by lifting sanctions, and subsequently grant an opportunity for development of Iran's oil and gas fields, as well as higher income for IOCs³⁴⁹. Consequently, such an attitude within the government confirms the applicability of proposed solution of this study for the goal of making the model more attractive through applying the evolutionary approach with no need to breach of any laws or shifting to another model³⁵⁰.

However, despite of effective changes regarding applying more flexible requirements about cost estimation, duration, capex, graphical differences, SCR, and local content, the comparative analysis of two versions has been clarified that the Iranian buyback is in dire need to enjoy a comprehensive and up to-date governing law which is independent of political parties. Moreover, the issue of bureaucracy and providing financial incentives and

³⁴⁷ Ibid P 19

³⁴⁸ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=6&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFgg3MAU&url=http%3A%2F%2Fwww.clydeco.com%2Fblog%2Fenergy%2Farticle%2Firan-council-of-ministers-ratifies-ipc-terms&usq=AfQjCNE1kEAgOsehefZwl3DviygCpO35g&sig2=K_ZviSuYkl6J03IjSeQ0Kw&bvm=bv.142059868,d.bGg /Access September 2016

³⁴⁹ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006 p 40 -45

³⁵⁰ Dunia P. Zongwe, Natural resources for national reconstruction: A new generation of investment contracts, Society of international economy law/ 2016

environmental concerns have not been considered in IPC, even though, this study dealt with them in the second sub-chapter, and proposed solutions³⁵¹. Furthermore, the IPC suffers from establishment of an academic research institute to collect and organise the related data in order to diminish the cost of discovery, and accelerate the process of maximising the production rate³⁵². Finally, the different view of political parties towards the IPC, the serious debate between parliament and the government regarding the need to ratify the IPC, and the future presidential election provide great doubt with regard to the applicability of the IPC which plays a main role in creating confusion, and subsequently unattractiveness feature of buyback. Other than the framework of the model, the structure of NIOC should be upgraded in order to ensure the capability of absorbing foreign investments after removing the sanctions which will be discussed in the next sub-chapter.

4.10 Issue of asymmetric data with regard to the shift of NIOCs customers from EU to India and China: The crucial need to establish a research institute within NIOC to organise and analyse the information

Following the comparison of the current buyback with IPC which led to prove the necessity and applicability of the evolutionary approach towards the future of the model with grater changes, analysing the structure of NIOC as the main body of Iranian government in petroleum deals seems essential for the aim of Iran to maximise the rate of production through absorbing foreign investments. Such analysis is important from the point that some criticisms which have been dealt in the past sub-chapters arise from the structure of the NIOC. Therefore, this study to provide the full image of Iranian buyback will offer the consideration of NIOCs structure with regard to the issue of asymmetric data³⁵³.

The technical insight of IOCs regarding oil fields' features in many cases is more than the state government. However, it does not mean that they have complicated technical data

³⁵¹ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=5&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFggxMAQ&url=http%3A%2F%2Ftheiranproject.com%2Fblog%2Ftag%2Firan-petroleum-contract-ipc%2F&usg=AFQjCNG_4UrMTbDAvxl2CQ90LMVczl7pGQ&sig2=7aulNspOBXCmUKafXYN5Pg&bvm=bv.142059868,d.bGg/ Access August 2016

³⁵² <https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=2&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFggxMAE&url=http%3A%2F%2Finfo.vedomosti.ru%2Fevents%2Fmaterial%2F19563%2F%25D0%25AD%25D0%25B4%25D0%25B4%25D0%25B8%25D1%2581%25D0%25BE%25D0%25BD%25D0%25B0%25D0%25BD%25D0%25B3%25D0%25BB.pdf&usg=AFQjCNGF5vWQeJekfQcGFOqerI4-OZ1fMw&sig2=8eUmamQ0NNSvVFOMaSSpeg&bvm=bv.142059868,d.bGg/> Access June 2016

³⁵³ S.G. Hassantash, Buy-Back Contracts and Asymmetric Information, OGEL Journal, Dundee, Vol. 7 - issue 1 April 2009. P 2

that state government do not possess, it rather highlighted that IOCs have more practical experience, and information system compared to the host government. This is because of the fact that IOCs have been operating in different countries with similar features. Since the operation of oil field contains a lot of risks and uncertainties, experience is essential to utility the newest technology and framework for increasing the oil recovery of the project. Accordingly, although, it seems that NIOC's data should be more than IOC's, however, as the NIOC's data are not centralised, organised and converted into information, they would not serve the benefit of the NIOC in petroleum arrangements³⁵⁴. Therefore, proper collection, processed data and updated information are the main strengths of international companies compared to NIOCs which suffers from existed problem in the analysable and useful information. Moreover, from the legal point of view since IOCs have concluded numerous kinds of contracts with various countries, political systems and domestic rules, they possess great experience regarding solving contractual issues, as well as finding solutions to settle down the disputes. Therefore, IOCs can enjoy such experiences in order to raise the capability of establishing new contracts; however, for NIOC it requires extensive legal studies to gain information in mentioned areas which needs to worldwide investigation of the oil lawsuits and claims. Although this deficiency cannot absolutely be resolved, it is definitely eliminable to a large extent, as there is no need for inaccessible technology to gather an inclusive database of the country's petroleum resources and its development movement. Such a purpose can be achieved through the organisational, and management adjustments of NIOC, as vital information of IOC's success and failure in using new technologies on various oil fields around the worlds is certainly demonstrable. Therefore, it would certainly be possible for National Iranian Oil Company to collect database regarding the global petroleum resources by using expert personnel³⁵⁵.

Furthermore, the recent changes in oil market such as self-sufficiency of America which can be a large and trustable exporter of oil to EU, utilising the new technology of shield oil in European countries such as Poland, and the increasing need of developing countries such as China and India towards oil to accelerate their economy will steadily change the buyer of Iranian oil from EU to Asia, additionally, although all companies may be familiar with related

³⁵⁴ Ibid P5

³⁵⁵ N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006

technology, the practical result of the operation is not recognised to all of them, particularly for new entries in Iranian oil sector, Chinese and Indian oil companies. Therefore, in this scenario the importance of having an institute for NIOC to generate such information is absolutely clear for Iran, as NIOC can enter into contractual negotiations with IOCs which have not worked in Iran in a more dominant position through achieving technical and financial information on IOCs, especially considering the fact that the number of companies that cooperate with Iranian government is not much³⁵⁶. As a result, although gathering information on status of projects, level of investments, financial condition and new investment opportunities of an international company is certainly difficult, it is not impossible, as it enables NIOC to update its current data which facilitates the cooperation with new partners such as Indian and Chinese oil companies³⁵⁷. Consequently, this study highlights the dire need of NIOC to have an institute to provide the symmetric information, as NIOC in negotiations with IOCs can protect the Iranian national interest in better way, thus, Iranian research institute should gather and centralised the data of Iranian fields, as well as, financial ,technical and legal data of IOCs.

4.11 Conclusion: The dire need of Iran in applying the necessary reforms after lifting the sanctions

The economic inefficiency of the Iranian model of buyback, as well as the adverse economic situation of the oil business in the world require the Iranian government to consider the dire need of improving its method of oil transactions. Moreover, the harmful effect of sanctions on Iranian oil industry which suffered the economy of Iran emphasised the urgency of such reforms within the mechanism of buyback, as the current practice of the model aggravated the adverse influence of sanctions³⁵⁸. As it has been discussed in first three chapters the historical, political and legal considerations of buyback demonstrated that the most applicable alternative to absorb more foreign investment following the lifting the sanctions is applying the evolutionary approach, as any shift to another contractual framework will

³⁵⁶ S.G. Hassantash, Buy-Back Contracts and Asymmetric Information, OGEL Journal, Dundee, Vol. 7 - issue 1 April 2009. P 6

³⁵⁷ Ibid P7

³⁵⁸ https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=4&cad=rja&uact=8&ved=0ahUKEwiQttuM8oDRAhVhL8AKHSRyCGYQFggsMAM&url=http%3A%2F%2Fwww.shlegal.com%2Fnews-insights%2Firan-petroleum-contract&usg=AFQjCNHodQhnWQulwV5U57zHefng6k8yyA&sig2=uv_HIEbo6RWRVS8Yk1INmw&bvm=bv.142059868,d.bGg/ Access July 2016

confront with serious historical, political and legal barriers. Moreover, examination of the four generations of Iranian buyback proved the applicability of such approach which has been practiced by Iranian government, even though, this study emphasised on the inadequacy of applied reforms within the buyback. Therefore, based on these carried out analyses this chapter employed the evolutionary approach to improve the Iranian buyback considering all discovered historical, political and legal concerns. This chapter through examining the criticisms received by both parties in buyback highlighted the shortcomings of buyback arising from the nationally supportive nature of the model, and proved the necessity of having balance between interests of both parties through changing the legally binding provisions to financially incentives terms, providing the independent legal framework, and certain governing law for the model. Furthermore, critical comparisons of Iranian buyback with production sharing agreements, service contracts and international version of buyback showed that many restrictive features of Iranian buyback can be revised through integrating the developed terms of above-mentioned mechanisms with no clash with any prohibition which will improve the efficiency of the model such as provisions related to duration of contract, transfer of technology, method of payment, arbitration and termination of agreement³⁵⁹. Therefore, it is possible to integrate certain aspects of other financing scheme to elevate the current version of Iranian buyback, due to the fact that the Constitutional prohibition of PSAs or other service contracts do not determine that their essential parts are unmatchable to existing buyback's structure which has been applied in this chapter.

The consideration of practicing the production sharing agreement in Iran illustrated the inapplicability of employing revolutionary approach because of the historical, political and legal barriers that have been resulted from concessionary deals and the nationalisation event. Finally, this chapter demonstrated the fact that merely removing the sanctions is not adequate for Iranian governments to reach its aim to renew Iran's oil industry, as well as to return to its previous position in the global oil market, thus, carrying out serious reforms within the present model of buyback is essentially required as they have been prescribed in

³⁵⁹ Economic Efficiency and Optimal Contractual Design of Oil Service Contracts: The Cases of Iran and Iraq Ghandi, Abbas. University of California, Davis, ProQuest Dissertations Publishing, 2013. P19

this study. Accordingly, following the analysis of Iranian buyback from historical, political and legal angles in the past three chapters it has been highlighted in this chapter that Iran considering its ambitious plan, as well as the situation of market is in dire need to carry out reforms to make the buyback more attractive, thus, this chapter employed the evolutionary approach to propose reforms that they can modernise the model with no clash with any constraints introduced in previous chapters. However, following this substantive analysis of the buyback it seems vital to examine the practical procedure of Iranian buyback in the next chapter in the form of considering some oil projects. Such consideration which is missed in many studies will provide the practical analysis of Iranian buyback for the aim of illustrating the restrictive provisions of buyback, and more importantly to point out the effect of applying evolutionary reforms on the model from the practical point of view.

Chapter 5: The Case study on Iranian Buyback: The examination of the evolutionary approach from the practical point of view

5.1 Introduction: Function of Buyback in Practice

Following the introduction of buyback after occurrence of the 1979 Islamic revolution Iran concluded limited number of contracts with foreign contractors to develop its oil fields. However, realising the inefficiency of the model to reach the country's economy's aims resulted in re-evaluation of buyback in the early 1990s³⁶⁰, and accordingly beginning the introduction of four generations of buyback which have been discussed in the third chapter of this study. Therefore, such inefficiency highlighted the fact that Iranian government is not able to be isolated from petroleum global contractual framework, as well as the country's need to access the overseas technical and financial investment. As a result, Iranian government in consequence of poor economy situation endeavored to improve the terms of buyback with consideration of the Constitutional prohibitions which this study proposed it as the evolutionary approach towards the future of Iranian buyback, thus, Iranian government began to offer more attractive version of buyback to govern its projects in order to accelerate the establishing of buyback contracts to develop the Iranian oil fields³⁶¹. Accordingly, following the substantive analysis of Iranian buyback carried out in the last three chapters from historical, political and legal perspectives this chapter will consider the practical examination of Iranian buyback through analysing four oil field projects. In fact, this chapter which is divided into four sub-chapters will highlight the effect of unattractive features of buyback which have been discussed in details in the third and the fourth chapter of this work on low efficiency of the current function of model on the past projects from the practical view, and more importantly will point out the practical influence of carrying out the proposed reforms in the last chapter based on the evolutionary approach on the future mechanism of Iranian buyback.

Providing the practical consideration of Iranian buyback which has been missed in many studies on the issue of Iranian buyback will enable this work to offer the fully understanding

³⁶⁰Shahri, Nima Nasrollahi. "The Petroleum Legal Framework of Iran: History, Trends and the Way Forward." *China and Eurasia Forum Quarterly*, vol. 8, no. 1 2010 p 46

³⁶¹ Economic Efficiency and Optimal Contractual Design of Oil Service Contracts: The Cases of Iran and Iraq Ghandi, Abbas. University of California, Davis, ProQuest Dissertations Publishing, 2013. P23

of the function of buyback in order to foresee the future development of the model. Such consideration will prove the necessity, and applicability of applying vital reforms within the framework of the model on the basis of evolutionary approach to modernise mechanism the model in this particular time after the removing the nuclear sanctions, and low price of oil in the market.

Accordingly, for above-mentioned aims the first sub-chapter will consider the Bangsetan project, and will show the practical effect of unnecessarily restrictive provisions of Iranian buyback on demotivating the both domestic and international contractor, as well as the influence of carrying out the proposed reforms in the last chapter from the practical view. The second sub-chapter via examining the Azadegan project deals with the impact of offering an attractive version of buyback on resisting against the foreign sanctions, and accordingly will prove the efficiency of applying the evolutionary reforms in future practice of the model. The serious need of the county to carry out some reforms within the buyback will be scrutinised in the third sub-chapter through considering the adverse effects of the high competition in the oil market, former sanctions and unstable governmental policy toward foreign involvement in oil industry which have been extracted from concerning the Southpars project. Analysing the Yadavaran project in the last sub-chapter will demonstrate the effect of unattractive method of oil transaction on aggravating the consequence of nuclear sanction on Iranian oil industry, and subsequently will show the Iranian government conservative position in applying some limited reforms within the model which highlights the accuracy of chosen solutions of this study to apply the evolutionary approach rather than shifting to any model³⁶².

5.2 The Bangestan oil field project³⁶³: Consequence of unattractiveness of the model on NIOCs' decision to replace the foreign contractor by the domestic oil company

The Bangestan field, around Ahwaz within Khoozestan region, is a large oil block. This contract concluded between NIOC and PIDC³⁶⁴ with value of \$900 million that predicted of massive production level, 80,000 and 110,000 b/d; however, this contract terminated in the early stages, as the two parties rapidly fell into dispute. PIDC claimed the non-verification of

³⁶² Mohammad Reza Saber, Buyback Contracts in Upstream oil and gas sector and its legal effects, International commercial law PHD dissertation, Azad University, International Postgraduate Centre, 2007, Tehran.

³⁶³ Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P218

³⁶⁴ Petrol Iran Development Company

the project as the reason to create the dispute, while NIOC proposed the difference amid of preservation, as well as operation structure with what has already been agreed upon as the key element for finishing the deal³⁶⁵. This sub-chapter in the following section is aimed to demonstrate the deficiency of the model from practical point of view to emphasis the necessity and efficiency of the applying the solutions that this study have offered based on the evolutionary approach.

a) Unnecessarily restrictive provisions of buyback: The main reason of the dispute

Basically, most of Iranian oil fields including the Bangestan field are suffering from the drop in production, as a result of ageing the wells which increases the cost, and the time of operation. Therefore, NIOC focused on finding a solution for this problem, as well as to increase generated b/d of Bangestan field. For this purpose, NIOC began to negotiate with foreign oil companies including BP, Shell, Total and Eni regarding the operation of the Bangestan oil field which led the companies to submit bids for the 3 phases of Bangestan, however, NIOC refused to accept their bids, since the plan was included different stages within the length 15 to 20 years, while NIOC offered 3 to 5 years contract for only one phase of the field. Therefore, as it has been mentioned in the last chapter, the unnecessary restrictive provisions of Iranian buyback mainly resulting from short duration of the contract, and separation of different phases of the operation demotivated the foreign contractors to establish the deal with NIOC. In fact, they were reluctant to invest in Iranian oil fields for such short periods, owing to the fact that the operation seems to remained uncompleted in such considerably small period particularly with technical difficulties arising from ageing the wells, thus, they refused to fund such expensive projects that contains such high commercial risk³⁶⁶. Due to their failure to reach an agreement, NIOC was forced to consider the establishing of the deal with the national oil companies, thus, NIOC quickly concluded the deal with Petroleum Iran Development Company. However, the restrictive provisions of Iranian buyback as mentioned in the case of foreign oil companies created the dispute between NIOC and PIDC which resulted in to early termination of the deal.

³⁶⁵ This is &S direct a translation as possible from an article, published on the Naft Nevis website at [[http://naftnevis.com/?m=2005 10&page=2](http://naftnevis.com/?m=2005%2010&page=2) from October 2005

³⁶⁶ Mabadi, Legal Strategies in Upstream oil and gas contracts to attract Investment: Iran's case. LLM Dissertation. Faculty of Law. University of Shahid Beheshti. 2008

Accordingly, as it has been discussed in the fourth chapter of this work the unnecessarily restrictive provisions of Iranian buyback stemming from the legal framework of the model demotivated the both national and international contractor, and subsequently failed the parties to reach an agreement. In order to revise these unattractive provisions of buyback for the aim of absorbing more foreign investment in oil industry after removing the nuclear sanctions this study based on the evolutionary approach proposed the applicable reforms in the last chapter that do not breach any barrier in Iran. This study regarding the issue of short duration of buyback suggests that the necessary duration of every contract should be determined after precise estimation of capacity of the field, and necessary operation activities to maximise the rate of production. Applying such a change which does not breach any legal, political and historical barriers ensures the interest of both parties in maximising the production rate, as well as avoids the negative experience of Iranians regarding the long duration of the concessions to exploit the Iranian natural resources³⁶⁷. Moreover, this study as proposed in the last chapter regarding the separation of granting the discovery right from development right suggests that the NIOC should be obliged to grant the development right to the contractor that successfully finished the discovery phase. This reform that does not confront any constraints will change the unnecessarily restrictive provision of buyback to the financial incentive which ensure the benefit of both parties, as in this scenario the foreign contractor is motivated to quickly start the production phase which is in favour of NICO as well.

5.3 Development of Azadegan field³⁶⁸: Japanese Investment in Iranian oil sector despite of American pressure

Azadegan field, in southern part of Iran, around Iraqi edge, is Iranian biggest oil field with estimation of 27 billion b/d. Following complex discussions with Japanese, they promised for 4 billion dollar during 36 months which led both governments to establish a 3 billion dollar deal to operate the field³⁶⁹. This sub-chapter in succeeding part is aimed for

³⁶⁷ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006. P 42

³⁶⁸ Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P 218

³⁶⁹ Iran Daily Economic Focus, 13/09/2013 [<http://irandaily.ir/1385/2659/html/focus.htm>]

considering efficiency of offering more attractive version of buyback based on the proposed solutions of this study in the fourth chapter of this work.

a) American pressure to terminate the deal: The influence of commercially beneficial deal for foreign contractor

The American pressure on Japanese government was announced by the English newspaper ³⁷⁰ for terminating the oil agreement with Iranians in order to minimize the revenue of the country because of the US goal to stop the Iran's nuclear program. However, since Japanese's petroleum industry was massively dependent upon receiving Middle Eastern oil³⁷¹, such dependency secured the oil agreement amid Iranians and Japanese. In fact, Japan signed the contract, despite the pressure from the US, as its economy needed Iran as the reliable supplier to provide petroleum for Japan industry. Moreover, NIOC proclaimed that this project was interesting for Japanese, as Iranian experts conducted special discovery analysis, as well as field's research³⁷². Therefore, Japan had a particular interest in developing of this field to operate the project as the contractor. On the other hand, NIOC was also motivated to grant the contract to Japan, as the corporation contains absolutely positive reputation in operating the petroleum fields during the history, especially within period of the Persian Gulf War³⁷³. Furthermore, NIOC was chasing to provide an opportunity for national Iranian companies to display themselves at the international level³⁷⁴.

Overall, this deal was concluded despite the foreign pressure, US in particular, as it was beneficial for both parties. It demonstrated the fact that if a contract is commercially vital for forging investors; they do sign the contract to operate in the field, even if in the event of pressure from other powerful countries. The signing of this project by Japan despite the American pressure showed that if Iran can make the current model of buyback more attractive by removing the unnecessarily restrictive provisions of buyback, and creating financial incentives as they have been demonstrated in the last chapter of this work, foreign contractors will be willing to work in Iran's field, particularly in this present time after

³⁷⁰ Financial Times, 01/07/2003[<http://search.ft.com/ftArticle?queryText=iranian+project+japan&y=O&aje=true&x=O&id=030701002529>] Financial Times Newspaper

³⁷¹ Agency for Natural Resources and Energy: the official website of the government of Japan, 26th June 2007, [http://www.enecho.meti.go.jp/english/policy/oil/fundamental_view.html]

³⁷² Iran Daily Economic Focus, 13/09/2012 [<http://irandaily.ir/1385/2659/htm/focus.html>]

³⁷³ Ibid

³⁷⁴ Peyvand Iran's News, 10/09/06 [<http://www.payvand.com/news/06/oct/1089.html>]

removing the nuclear sanctions. Therefore, this case proves the Iranian oil industry with no need to shift to another model can absorb more foreign investment via carrying out the evolutionary reforms, as this method, as has been discovered in the last chapter, will create financial incentives, and accordingly will offer more commercially beneficial deal to IOCs.

5.4 South Pars project³⁷⁵: Offering more flexible terms for foreign investors, as a result of high competition between Iran and Qatar

A discovered block in the Southern part of with estimation of eventual production of 100,000 bp/d³⁷⁶ of crude oil which was supposed to be shared by Iran and Qatar. The high capacity of the field, as well as the competition with Qatar motivated Iranian government to accelerate the negotiation with contractors through minimising the bureaucracy, and offering more flexible terms of buyback, as NIOC announce the Iranian government willingness to conclude the agreement regarding the project until May 2003 which resulted in creation of special interest amid foreign large oil companies such as Total, Gazprom, BP and Malaysia's Petronas. Therefore, the government's intention to quickly develop the South Pars field resulted in establishing the several contracts with foreign oil companies for operation of the field. The two following sections will examine the case from practical point of view in order to demonstrate the efficiency of reforms that this study on the basis of evolutionary approach proposed in the last chapter regarding the shortcomings of buyback to make the model more attractive.

a) The US bilateral sanction regarding the deal: Impact of offering more flexible terms of buyback

While Iran was determined to attract foreign investors to participate the operation of the field, US sanctions appeared to inhibit some foreign contractors to participate the Iran's energy industry. The US attempted to avoid the foreign contractors to invest in Iranian oil sector through applying the American bilateral embargo, 1996, which used to deter several European, Japanese and Australian energy companies from undertaking development

³⁷⁵ Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P 220

³⁷⁶ Alexander's Gas and Oil Connections, 31110/2012 [<http://www.gasandoil.com/goc/discover/dix24883.htm>]

projects in Iran³⁷⁷. Nevertheless, the situation was distinguishing in this project, owing to the fact that the tendency of the government was in favor of foreign involvement in oil industry, as a result of high competition with Qatar. Therefore, NIOC began to offer more flexible terms of buyback such as minimising the length of negotiation and bureaucracy, and technical consultancy in order to attract foreign investors to the south pars project. As a result, several large oil companies such as Total, Lukoil and Petronas, despite the US sanctions established the buyback with Iran for development of South Pars field. Accordingly, as it has been mentioned in the last sub-chapter establishing this project showed the fact that the more attractive version of Iranian buyback can absorb more foreign investment even in the event of foreign imposing sanctions which confirms the efficiency of the evolutionary reforms, in the last chapter, rather than the revolutionary approach towards the future tendency of the model. Moreover, this case has been highlighted the fact that the contractors operating in Iran challenges the US sanctions on Iranian oil industry, as the terms of buyback were more flexible for them, thus, approves the accuracy of this study's proposal to apply the evolutionary approach, as NIOC could resist the imposing sanctions of US through offering more favorable terms by reforming the current provisions of buyback without any clash with legal or social prohibitions³⁷⁸. Hence, these facts prove the accuracy, applicability and efficiency of employing the evolutionary approach rather than shifting to another model on the basis of the revolutionary approach which will be legally, historically and politically confronted in the current situation of Iran, therefore, there is no need to move towards the revolutionary approach which confronts many barriers as it has been discussed in the last chapters of this study.

b) The Change in Iran's governmental policy: Instability of buyback tendency towards foreign involvement

Following the initial South Pars contract, NIOC in the light of shifting the government to Conservative party began to progressively tighten the flexible terms that offered to other developers³⁷⁹. This change in the policy of NIOC towards foreign involvement in oil industry

³⁷⁷ Farnejad H., Strategic Approach & Legal Implications of Investment in Geopolitically Sensitive Iran Pp 19-21 (Unpublished LL M Dissertation & PhD Progression submitted to CEPMLP, Dundee, 2006). P 37

³⁷⁸ Koenraad Van Brabant, 'Can Sanctions Be Smarter? The Current Debate: Report on a Conference Held in London 16-17 December 1998' (May 1999), first accessed 18/06/2012 [www.odihpn.org/documents/sanconf.pdf]

³⁷⁹ Yielding a reported internal rate of return of 16-18 percent

has been stemmed from the fact that the Conservative party supports the desirability of foreign contractor's involvement in energy industry which places in the heart of the political debate between Iranian "conservatives" and "reformists". Applying such a policy by the new government, as well as the US sanctions to impede investment in the Iranian energy sector resulted in to hinder the foreign contractors, and subsequently minimise the role of them in Iran's oil industry. Therefore, many foreign oil companies left the contracts which were subsequently granted to the domestic contractors. Accordingly, as it has been mentioned in the last chapter the Iranian model of buyback needs to have certain and clear provisions of governing law that are independent from the policy of the different governments in order to be stable in the event of changing the government. Such change as it has been considered in the last chapter on the basis of evolutionary approach does not breach any barrier, and more importantly will remove the financial risk of changing the attitude towards foreign contractor³⁸⁰.

Accordingly, this case illustrated the existence of political concerns, until recent, regarding foreign involvement in oil sector which highlights the applicability of evolutionary reforms rather than revolutionary changes, as the Iranian political atmosphere will resist against such radical alteration. Moreover, offering more flexible terms of buyback in this project which enabled NIOC to resist the imposing sanctions of US through preserving the foreign contractors confirmed the proposal of this study to introduce the evolutionary approach as the future alternative of the model³⁸¹. More importantly, this project emphasised the influence of changing the government on attitude of buyback foreign involvement in oil industry which requires, as it has been discussed in the previous chapter, Iran to revise its petroleum governing law to provide more certain and less ambiguous provisions with independency from different political wings. Clearly, offering such a law with above mentioned elements can play vital roles in attracting foreign investors to Iran, as they enjoy the possibilities of understanding, and predicting the law of the country through ensuring the stability of attitude in buyback in the event of changing the governments.

³⁸⁰ Mabadi, Legal Strategies in Upstream oil and gas contracts to attract Investment: Iran's case. LLM Dissertation. Faculty of Law. University of Shahid Beheshti. 2008

³⁸¹ S. N. Ebrahimi, LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995, IQPC London, 27th Oct. 2006. P 47

5.5 The Yadavaran Oil Field³⁸²: The influence of unattractive model of buyback on aggravating the nuclear sanctions' impact on Iranian oil industry

The Yadavaran field, in Khuzestan province, is originally comprised of two former fields which are Koushk and Hosseinieh. Following finding the connection between the two above-mentioned fields, the both fields was renamed as the Yadavaran field with estimated capacity of 18 billion b/d measured to be recoverable³⁸³. Iran began to negotiate a contract with Sinopec and the Chinese company which was predicted to begin in 2009³⁸⁴. Accordingly, this case is vital from the point that it established in the time that the US and EU aggravated the nuclear sanctions in order to minimise the income of the Iranian government from petroleum deals to force the country to stop its nuclear plan, therefore, the Iranian government had to offer more attractive version of buyback to preserve the foreign contractor working in Iranian oil industry for the purpose of increasing its revenue from petroleum deals. This sub-chapter will consider the influence of offering more attractive version of buyback from the practical point of view which can confirm the efficiency of reforms that have been offered by this study on the basis of evolutionary approach.

a) Offering more flexible terms with no clash with any barrier: The only applicable solution for current mechanism of buyback

Imposing the nuclear sanctions on Iranian oil industry from UN, US and EU to stop Iran to develop its nuclear plan considerably reduced the rate of oil production from Iranian field. In fact, this imposed sanction which combined with unattractive mechanism of Iranian buyback resulted in to exclusion of many oil companies from Iranian oil sector which decreased the revenue of Iranian government, and considerably damaged the economy of Iran. Such event brought the Iranian government to the conclusion that the buyback is in dire need of reform to increase the income of the country through absorbing foreign investment³⁸⁵. Therefore, Iranian government decided to offer more flexible model of

³⁸² Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P 222

³⁸³ Accessed 26/06/2014 [<http://www.answers.com/topic/yadavaran-field>]

³⁸⁴ Rigzone; -02/04/2014 [<http://www.rigzone.com/news7article.asp?ii=id=44623>]

³⁸⁵ P. Dittrick, Yadavaran Buyback Contract Signals Better Iranian Terms, OEGJ Journal, Dundee, Vol. 7 - issue 1 April 2009

buyback through increasing the rate of return, prolonging the duration of contract and more flexibility regarding the obligation of providing the cost estimation prior to the beginning of the project. Noticeably, Iranian government offered all these reforms to preserve its revenue from petroleum deals as the main income of the country. Accordingly, these reforms truly addressed some of criticisms that have been examined in last chapter which can act as financial incentives for foreign contractors through minimising the commercial risk of operating in Iranian fields³⁸⁶.

Overall, as it has been shown in this project, some vital changes have been applied within the structure of the model to modernise its mechanism which were effective in preserving the interest in some IOCs to continue their operation in Iran³⁸⁷. Although this fact confirms the efficiency and applicability of the evolutionary approach, this study as it has been mentioned in the last chapter emphasised the necessity of developing the extent of more serious improvements within the framework of Iranian buyback to reach the Iran's ambitious economy plan.

5.6 Conclusion: The Practical influence of applying the evolutionary approach regarding the future development of Iranian buyback

Basically, present research key goal is to provide comprehensive consideration of Iranian buyback from various perspectives in order to propose applicable alternative to increase the efficiency of the model. Achieving such goal is not possible without offering the substantive analysis of Iranian buyback which have been provided in the first four chapters of this study along with examining the practical aspect of the model through considering function of the previous projects. In fact this is the distinguishing feature of this work to offer the practical study of Iranian buyback in this chapter for the aim of showing the adverse effect of unattractive features of the model, as well as demonstrating the potential influence of applying the evolutionary reforms, as they have been considered in the last chapter, on the future development of Iranian version of buyback.

This chapter from the practical point of view emphasised the necessity of utilising applicable reforms regarding the Iranian method of transaction, as a result of high competition of Iran

³⁸⁶ *ibid*

³⁸⁷ S. N. Ebrahimi, *LOCAL CONTENT ISSUES IN IRANIAN BUY-BACK CONTRACTS As Experienced by Law and Practice since 1995*, IQPC London, 27th Oct. 2006 p 51

with other regional producer, as well as the deficiencies of the model including the unnecessary restrictive provisions such as short duration of contract which deterred many international and domestic oil companies from undertaking petroleum projects in Iranian oil fields that could be improved via employing reforms that have been proposed in the last chapter on the basis of the evolutionary approach with no need to either shift to any other model or breach any barrier in Iran. Moreover, this chapter showed that offering more flexible terms of buyback through applying some reforms could attract the foreign contractors even in the event of sanctions against the country which highlights the applicability of chosen solution of this study to apply the evolutionary approach which was also taken by the Iranian government, as it has been pointed out since the unattractive version of buyback aggravated the adverse effect of nuclear sanctions, the Iranian government had to apply some limited changes in the model.

As a result, this chapter confirmed that some efforts have been carried out to make Iranian buyback model more attractive, however as it has been suggested in the last chapter the extent of reforms must be developed to other unattractive elements of the model including political and legal barriers. Accordingly, ensuring such reforms by Iranian government, firstly, proved the fact that Iran understood the necessity of applying some changes within the mechanism of buyback, and more importantly it confirms the applicability of the evolutionary reforms towards the future of buyback, thus, since the analysis of Iranian buyback from different angles demonstrated the applicability and efficiency of the evolutionary approach as the future alternative of the model, the examination of the model through practical sight in this chapter showed an applicability, as well as effectiveness of such solution. Moreover, present case study indicated that despite all deficiencies considered in the present and the past chapters regarding the model, they did not prevent foreign investment in Iranian oil fields, in fact, whilst the buyback contract is not sufficiently attractive method to for developing the petroleum industry, it has reached to few important achievement in absorbing investments. Thus, such success confirmed the applicability of required reforms within the model on the basis of the evolutionary approach rather than shifting to another method, as this shifting certainly will face historical, political and legal barriers which has high expenses for the country, especially with consideration of the time limit for Iran to return to the global market after lifting the nuclear sanctions. Therefore, despite of all changes applied in above-mentioned projects, the Iranian buyback still has

high capacity to being modified to compete with commonly used models in the world in attracting foreign investors. Accordingly, based on examination of Iranian buyback from practical point of view in this chapter the most applicable solution in the current situation for Iran towards the future of buyback is to continue more serious reforms that have been proposed in the fourth chapter of this work in order to create more flexibility and financial incentives, as well as removing, and minimising the restrictive terms and financial risks within the buyback. As a result, the main attitude in this study towards the future of buyback is employing the evolutionary approach through utilising the applicable reforms that do not breach any historical, political and legal barriers for the aim of absorbing more foreign investment in order to develop the Iranian oil industry. Consequently, following the analysis of Iranian buyback from substantive and practical point of view, and more importantly proposed reforms, the short review of the entire thesis will be offered to respond the question of this research by combining the historical, political, geo-political, legal and practical examination to draw the final conclusion of this work in proposing the most applicable alternative to make the Iranian method of transaction more attractive for foreign contractors.

6. Conclusion: The superiority of the evolutionary approach over the revolutionary attitude as the future alternative of Iranian buyback

Iran as a country with a large amount of natural resources and significant political role in the region has been actively chasing solutions to revitalise the country's economy situation through increasing its oil production rate. However, some historical, political, geo-political and legal concerns that have been examined in this work restricted Iranian government to reach its aim to increase the rate of oil production. The main barrier which has been stemmed from the historical, political, geo-political concerns is the Constitutional limitations on oil contracts that forbid any ownership or control of foreigners over Iranian natural resources. Such restriction which has been based on the idea of nationalisation of Iranian oil and gas reserves resulted in the introduction of buyback agreements with its restrictive provisions, as the only permitted mechanism to circumvent the legal prohibitions, as well as attracting foreign investment. However, many years of practicing Iranian buyback demonstrated its low economy efficiency compared to other commonly used models such as production sharing agreement, even though, Iran has offered four generations of buyback. As a result, this study chooses the issue of the possible ways of making the Iranian buyback more attractive as the research question, and attempted to reply this question by offering five chapters to examine the Iranian buyback from different aspects in order to ensure the applicability and effectivity of the alternative that will be offered for the future of the model. More importantly, this study recognised some gaps in the similar researches on the issue of Iranian buyback including lack of historical, geo-political, political examination, and also failure to provide the solutions to modernise the Iranian buyback following the critical analysis of the model that all have been offered in this work. Therefore, this study proposed the comprehensive analysis of Iranian buyback through five chapters for the aim of suggesting the applicable reforms to make the model more attractive. As a result, having considered the relevant subjects to the topic of Iranian buyback contract in details in previous chapters, this section is designed to review issues that have been previously analysed in

former chapters of this study to conclude this work by replying the research question of this thesis which is possible solution to make the Iranian buyback more attractive.

Examining the historical concern of Iranian buyback demonstrated that the foreign powers took the advantage of the poor economy situation of Iran in the 19th century, and imposed the exploitative concessions with unbalanced terms on Iran, as the country was in dire need of obtaining income. Such features of concession as the main Iranian method of oil transactions in Pre-Nationalisation era created the negative attitude of Iranian regarding the involvement of foreigners in oil industry; moreover, this attitude has been aggravated following the foreign pressure to impede the effort of Iranian government to make the terms of concessions more balanced which led to invade of Iran, and controlling its resources during the Second World War. Therefore, consideration of the historical elements of Iranian buyback showed that the negative experience of Iranians towards foreign involvement in oil sector resulting from the exploitative concessions, as well as ignoring the national interest of Iranians in petroleum deals stemming from foreign pressure to preserve the terms of concessions are the two major historical reasons of introduction of Iranian buyback which prohibited any kind of ownership of foreigners over oil product as the main historical concern of Iranian buyback. As a result, based on the historical examination of Iranian buyback carried out in the first chapter, shifting to any model that allows the foreign ownership of Iranian oil and gas fields will be confronted with this historical concern, thus, it demonstrates the superiority of applying the evolutionary approach through utilising the applicable reforms which has been chosen by this study. Accordingly, this study covered an important gap in other researches which is lack of providing the historical analysis of the Iranian buyback. This consideration is a vital issue, as understanding the reasons of adopting such a harsh model, and foreseeing its future development will be impossible without examining the historical concern of Iranian buyback.

Political and geo-political analysis of Iranian buyback demonstrated the formation of transferring the public discontent resulting from the exploitative concessions to the nationalisation of Iranian oil and gas reserves. In fact, the nationalisation event which led to adoption of buyback was the response of Iranians towards foreign involvement in oil sector, due to the fact that Iranian people recognised the value of their natural resources. As a result, this event changed the petroleum legal framework of Iran from concessionary deals to contractual system in order to protect the national interest of Iranians in petroleum

transactions that is the core trend in current model of Iranian buyback, and created some unnecessary restrictive provisions such as transfer of technology and obligation of foreign companies to employ Iranian worker in oil project. However, following the removal of the Nationalist Government through foreign coup, Iran under pressure of great powers began to exercise the production sharing agreement model which denied the main idea of nationalisation via allowing the foreign ownership of oil and gas resources. Such a radical shift resulted in to public discontent, and generated the economic root of the 1979 Islamic Revolution that nullified all the pervious petroleum deals, and applied the Iranian buyback with its harsh and restrictive provisions. Therefore, the political and geo-political consideration of Iranian buyback highlighted the strong concern against any model that permits the ownership of oil product by foreigners, thus, it showed the superiority of the evolutionary approach from the political and geo-political perspective that has been selected by this study as the effective alternative. Consequently, examining the Iranian buyback from the political and geo-political point of view within two absolute significant petroleum relevant occasions of Iranian petroleum contractual background, 1951 Nationalisation and 1979 Islamic Revolution, provided more completed image of the Iranian buyback which has been missed in many similar researches on the topic of Iranian buyback. Lack of such analysis leads to an inconclusive study on Iranian buyback, as the issue in question has strongly attached to the political and geo-political events, moreover, it will decrease the applicability of the alternative that this study proposes for the aim of increasing the efficiency of the model, due to the fact that it might breach the political and geo-political concerns.

The legal analysis of the Iranian buyback explained the idea behind the adoption of the Iranian model of buyback from the legal view. This examination demonstrated that the Iranian buyback is a compromising solution to follow the Constitutional prohibition regarding the foreign ownership of Iranian petroleum sector, and meeting need of country to absorb foreign investment to the oil sector as the main source of income for Iranian government, therefore, the buyback model is the only possible way for Iranian government to govern its oil transactions. However, the nationally supportive nature of Iranian buyback resulting from the idea of the nationalisation event created significant financial risks on foreign contractors through ruling many unnecessary restrictive provisions such as fixed rate of return. Therefore, a serious necessity is existed for Iran to improve the terms of buyback

which has been reflexed via offering four generations of buyback that illustrates the applicability of the evolutionary approach with regard to the Iranian buyback. More importantly, although the Iranian model of oil transaction is in dire need to be modernised, it does not mean every change within the current model can be applicable, as utilising any mechanism that includes the ownership of Iranian oil by foreigners will be rejected on the basis of the Iranian Constitutional prohibition. As a result, examination of Iranian buyback from legal point of view determined the superiority of the evolutionary approach through employing the applicable reforms which has been chosen by this study to make the model more competitive with other common methods of oil transactions. Accordingly, providing the autopsy of the core concept of the Iranian buyback from the legal perspective is essential from the point that such analysis highlighted the unattractive features of the model through clarifying the present practice of Iranian buyback. Therefore, lack of such consideration is in contrary with the goal of this work to offer the comprehensive understanding of Iranian buyback from different angles; moreover, it will deprive this study from precisely proposing the applicable reforms to improve the problematic provisions of buyback with no clash with any historical, political and legal concerns in the current environment of Iran after removing the nuclear sanctions.

The critical dissection of Iranian buyback dealt with the effectiveness and applicability of the evolutionary approach towards the future of Iranian buyback. For this aim, examination of the criticisms received by both parties in buyback highlighted the unnecessary restrictive provisions of the model which have been precisely revised on the basis of the evolutionary attitude via rendering a balance between the interests of both parties in buyback, changing the legally binding provisions to financially incentives terms, and providing the independent legal framework with certain governing law for the model within the Iranian oil legal framework. In addition, critical comparison of Iranian buyback with other internationally common methods of oil transactions indicates that many unattractive features of Iranian buyback can be revised by integrating the developed terms of other mechanisms which do not breach any prohibitions in the present situation of Iranian petroleum framework such as provisions related to transfer of technology, method of payment, arbitration and termination of agreement. Therefore, the critical dissection of Iranian buyback firstly pointed out the shortcomings of Iranian buyback, and in the next stage employed the evolutionary approach regarding the future of the model in order to examine the

effectiveness and applicability of such attitude for the purpose of modernising of the model. In other words, subsequent to illustrating the applicability of the evolutionary approach in historical, political, geo-political and legal consideration of the model the critical dissection of Iranian buyback proved the effectiveness of such attitude via reforming the unattractive elements of the model which showed the superiority of the evolutionary approach regarding the future of Iranian model of buyback. Consequently, many similar researches on the issue of Iranian buyback merely examined the current mechanism of buyback including its deficiencies, and subsequently failed to provide solutions to improve the efficiency of the model, while the main goal of this study to provide the examination of Iranian buyback from different angles for the aim of offering applicable alternative to make the model more competitive as the final outcome of this work. The consideration of Iranian buyback from the practical perspective examined the function of buyback in governing of some projects of Iranian oil industry in order to analyse the effect of unattractive elements of the model on its efficiency, and also foreseeing the future trend of Iranian buyback for the purpose of offering the applicable and effective alternative. The analysis of the four Iranian projects established in the framework of buyback demonstrated the harmful effect of the unattractive features of buyback including the unnecessary restrictive provisions, inflexible mechanism, and lack of certain, clear and independent governing law of model in demotivating the foreign investors to participate the Iranian oil sector. More importantly, consideration of Iranian buyback from practical view showed the applicability and efficiency of carrying out the evolutionary approach rather than the revolutionary one, due to the fact that despite limiting scope of changes that have been carried out to make Iranian buyback model more attractive in analysed projects, such limited changes were effective in absorbing foreign investment, thus, employing the evolutionary approach in order to utilise more serious reforms can make the model more attractive with no need to shift to any other method. Therefore, the examination of Iranian buyback from practical perspective demonstrated the superiority of the evolutionary approach through providing the efficiency and applicability of such approach in practice. Accordingly, offering the consideration of Iranian buyback from practical outlook through analysing some projects which is a vital gap in many studies on the issue of Iranian buyback enables this work to examine the efficiency and applicability of proposed reforms in this study regarding the future of the model. Lack of such analysis will result in to incomplete understanding of the function of buyback, as

well as the great doubt regarding the efficiency of proposed reforms in practice of the model.

Consequently, this work has provided detailed examination of Iranian buyback from different perspectives in order to comprehensively analyse the Iranian model of buyback for the purpose of offering the applicable alternative that can make the model more attractive. As a result, this study considered the Iranian buyback from historical, political, geo-political and legal points of view, and, more importantly, suggested solutions to improve the efficiency of the buyback. Further than the substantive analysis of the model, examining the practical aspect of the model through considering the previous projects has been carried out to determine the efficiency of the chosen method, the evolutionary approach, to modernise the buyback. Consequently, both substantive and practical analysis of Iranian buyback carried out in this work demonstrates the efficiency and applicability of the evolutionary approach rather than any radical shift on the basis of the revolutionary attitude, thus, this study has proven the superiority of the evolutionary reforms over radical change in the present Iranian oil industry, even though, the scope of this approach has to be developed to enable the model to compete with other model in attracting investors.

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8. Appendix

1. Definition of Iranian Buyback from the Council of Ministers Perspective

According to the part five of Article 85 of the Iranian Third Development Plan, a joint proposal submitted by the Ministry of Economic Affairs and the Iranian Central Bank with regard to the Regulations of Buyback contracts³⁸⁸.

Consequently, the Council of Ministers issued a decree, which included a number of provisions to define the precise nature of the Iranian Buyback arrangements³⁸⁹. They are as follow:

Article Two of the decree explained the basic nature of the agreements by stating that:

Buyback transactions apply to the transaction methods whereby the investor is responsible to provide the investment needed for all or a part of the project to the fund required equipment and services. This contains all financial facilities such as capital, services and intermediate goods needs for the operation, construction, development and enhancement of production or services units. The facilities will be compensated by exportation of goods and services acquired by the investment.

Article Three specified that the "Law Concerning Attraction and Protection of Foreign Investment" would regulate all benefits achieved through Buyback transactions. Subsequently, this law requires guarantees against confiscation and nationalisation of both

³⁸⁸ Central Bank of the Islamic Republic of Iran

³⁸⁹ The Decree was signed by the First Deputy President Hassan Habibi on 29th January 2001

property and funds, as well as granting of supplementary protections against sudden changes in export laws.

Article Five rules the situation when the implementation of contracts on the "export of mutually agreed upon goods and services", being obstructed by any changes in laws and regulations and subsequently, led to the non-fulfilment of the "Investments Receivers' commitments". This Article certifies that: The matured instalments shall be paid to the beneficiary in accordance with the same foreign exchange stated in the pertinent contracts and in compliance with the regulations of the Law Concerning Attraction and Protection of Foreign Investment³⁹⁰.

In order to ensure the fulfilment of the investors commitments, the Article Six is authorised the Investment Receiver to export all output from a single factory, manufacturing organisation/company. The Article Seven clarifies that the relevant domestic authority would indicate the rate of repayment. For the purpose of facilitating the export of the goods or services within the framework of all pertinent regulations, this Article provides that the Organisation for Investment, Economic and Technical Assistance of Iran is in charge of notifying the Customs, Export Advancement Centre, Central Bank and the managing bank. Under Articles Eight and Nine, some protections are guaranteed in favour of the investors such as exemption of foreign exchange from any duties, as well as no obligation to return the earnings to Iran³⁹¹.

Based on the Article Thirteen, any changes to the contract which may affect the financial commitments of the parties are restricted. In this regard, the Article determined that:

Any amendment, alteration or extension of the contract which may cause changes in the financial commitments of the contracting parties, shall be permitted only after the declaration of opinion of the Organisation for Investment, Economic and Technical Assistance of Iran and ratification of the related Ministry and the independent organisation.

Article Fourteen of the decree requires forming a committee board in order to facilitate the procedure of resolving problematic issues, as well as accelerating the process of buyback operations. This board is comprised of representatives from the Ministries of Economic Affairs, Commerce, and Foreign Affairs, the Management and Planning Organisation, the

³⁹⁰ Petroleum Iran, about Buy-back agreements, (<http://www.petroleumiran.com/buy-back.html>) 18th November 2013

³⁹¹ *ibid*

Central Bank, the Iranian Chamber of Commerce and Industries and Mines. The aim of the board is adopting measures to pursue reports on the conduction of all buy-back projects, examining arose issues, and more importantly, proposing solutions to resolve any problems or difficulties for in the event of specific disagreement³⁹².

2. Terms and Conditions of Iranian Buyback

Before defining the terms and conditions of Iranian buyback, the terminology of the contract should be clarified for the purpose of providing the deep understanding of the legal feature of per side performance in agreement. They are as follows:

- **The Supplier:** It can either be a natural or legal entity, which is responsible for funding the project, as well as transferring the expertise and the technology to the NIOC.
- **The Buyer:** The Buyer in the Iranian Buyback agreements is national Iranian oil company that works with authorization of Iran's Oil Ministry Oil. While NIOC obliged to compensate the supplier by sharing the end product, it receives the abovementioned services and the technology.
- **Capital Costs:** It refers to the necessary capital to fund all the direct expenditures of the project which is covered by the supplier, such as building and engineering the structures, purchasing and installing the major equipment, and service-provider fees³⁹³.
- **Non Capital Costs:** This type of cost is comprised the indirect expenses in operation of the development phase which are not categorized in the capital costs classification, such as custom duties, training the personnel and paying taxes³⁹⁴.
- **Cost Recovery:** Based on the Iranian Buyback, while the foreign party is charged with developmental operations, both financially and technically, it enjoys the reimbursement in the form of petroleum output.
- **Operating Costs:** It consists of all typical expenditures connected to petroleum production, labour force maintenance, conducting repairs, and providing vital equipment, including pipes, storage tools, drilling machinery and platforms.

³⁹² Petroleum Iran, 21/02/2014 [<http://www.petroleumiran.com/buy-back.html>]

³⁹³ Mobaser et al, op.cit., pg. 54

³⁹⁴ Rabiee, Faranak, 'Hoghoogh-e-Gharardadha', (Contract Law), Tehran 1391, pg 76

- **Petroleum Costs:** Petroleum Costs are embodied those expenditures which are payable by the supplier and mostly defined within the contractual documents pertaining to field³⁹⁵.

- **Development Operations:** It is known as conduction operated by the supplier in order to develop the certain block as well as assessing its capacity. This conduction could contain the following activities³⁹⁶:

- I. Development of wells, including drilling and any other operations with the aim of enhancing the quantity of oil being acquired.

- II. Building the installation of drilling platforms, implementation and any other required articles for purposes of extraction, processing, and delivering oil to the market.

- III. Providing accommodation, health care facilities, education area and administrative centre for the personnel³⁹⁷.

- **Exploration Expenditure:** Generally, it represents all expenses created as a result of exploration activities related to the particular oil field.

- I. All implements and machineries which are necessary for the act of exploration of oil field.

- II. Logistical costs which are consisting of property rent charges, labour and fuel and reparation.

- III. The provision concerning the education of the Iranian personnel to prepare qualified technical staff for the final aim of returning the field to the Iranian authorities.

- IV. Costs stemming from the preserving of the original environmental condition, as well as the avoidance of pollution resulting by the operations³⁹⁸.

- V. Customs duty payments regarding imported equipment and supplies which are required for the conduction of oil operations.

- **Development Phase:** It specifies the scheduled time while the supplier exploits the oil field based on the development frame.

- **Effective Date:** It is the date which the contract commences to the force according to agreed provisions and conditions.

- **Master Development plan:** MDP is an illustration for forthcoming issue of the oil field operation. It is designed to describe the accurate conduction of the field including

³⁹⁵ Ibid.

³⁹⁶ Petroleum Iran, Iranian oil information portal (<http://www.petroleumiran.com/buy-back.html>) 21st September 2013

³⁹⁷ Farshad Gohar, Naser, 'Seyri Dar Gharardadhave Naftiye Iran', { A Survey On Iran's Oil Agreements) Tehran, 1391, pg 262

³⁹⁸ Mobaser, op.cit., pg.56

requirements for the platforms' structural integrity, and a detailed time scale for the structure stages, the route for the pipe network, and contingency plans for emergencies³⁹⁹.

- Maximum Effective level: It clarifies the most probable amount of generated product with regard to prevention from loss of oil pressure and any physical damage to the field⁴⁰⁰.

3. International Model of Buyback Contract⁴⁰¹

Buyback contract

Between

X (The individual's name or identity of company)	Address of office/Town/Country(Land)
Y (The individual's name or identity of company)	Address of office/Town/Country(Land)

Whereas

Under a Primary Contract dated----- (hereinafter the "Primary Contract") and the Technical Assistance Contract dated---- (hereinafter the "technical assistance contract"), X has sold to Y, and Y has purchased from X, under the terms and conditions set forth in the primary contract and the technical assistance contract, the machinery and equipment and patents

³⁹⁹ Rabiee, op.cit., pg 76

⁴⁰⁰ Mobaser, op.cit., pg. 54

⁴⁰¹ This part is begin borrowed from Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P 267

and know-how and technical assistance specified therein (hereinafter "the equipment technology"), to manufacture---- (hereinafter "the products") in Y -land.

By way of buy-back, and under the terms and conditions set forth in this contract, Y agrees to sell to X, and X agrees to purchase from Y, products as specified herein.

Now, therefore, the parties to this contract agree as follows:

Article 1: The buyback commitment

1.1 X hereby agrees to buy (or cause the purchase) from Y, under the terms and conditions set forth in this contract, products manufactured by Y using the equipment/ technology sold by X, and take delivery of the said products.

1.2 Y hereby agrees to sell to X (or to his assignee (as defined below in Article 6)), under the terms and conditions set forth in this Contract, such Products, and to accept the purchase by X of such Products as buy-back within the framework of this Contract.

Article 2: The products

2.1 The assortment of products to be sold and purchased under this contract is agreed upon by the parties in accordance with the provision of article 10 below.

2.2. Y hereby warrants that sufficient products of the agreed assortment will be available at the times specified in article 10 of this contract.

Article 3: Conformity of the products

3.1 The products to be delivered shall correspond to the specifications and quality agreed upon in the primary contract, and must be of the quantity and assortment required by the individual purchase contracts (hereinafter "implementing contract(s) to be concluded within the framework of this contract between Y or his assignee (as defined below in article 6) in his capacity of seller of the products (hereinafter "the implementing seller" , and X, or his assignee (as defined below in Article 6) in his capacity of buyer of the products (hereinafter "the implementing buyer"

3.2 The products must be contained or packaged in the manner required by the respective implementing contract.

Article 4: Total value of the buy-back commitment

4.1. During the term of this Contract X shall purchase from Y Products for the value of either

(A)----- Or

(B) Not less than-----per cent (---%) of the total-----price of the primary contract as specified in Article X of the contract, plus not less than ---- per cent (----%)of the total price of the technical assistance invoiced in accordance with Article X of the technical assistance contract.

4.2. The value of each of the implementing contracts to be applied against X's buyback commitment under this contract shall be---- value of the respective Implementing contract.

4.3. The value of each of the implementing contracts, if invoiced in a currency other than the currency in which X's buyback commitment is set forth here above, shall be applied against X's commitment at the exchange rate quoted by the central bank of----- at the date of the invoice issued in respect of such implementing contract.

Article 5: The price of the products will be either:

(A) 5.1The prices of the Products offered under this Contract shall correspond to

(1) The price generally charged at the time of the conclusion of the respective implementing contract for such products under comparable circumstances in the trade concerned⁴⁰².

(2) The fair average market value of the products in the territory (as defined below in pare. 7.1) under competitive terms of delivery and payment.

(3) The prices of competing products, of essentially similar specifications and quality standards than those of the products, in the territory (as defined below in pare. 7.1) under competitive terms of delivery and payment.

⁴⁰² Article 55 of the United Nations Convention on Contracts for the International Sale of Goods 1980.

(4) The quotation of the product at the ---- exchange on the date when the respective implementing contract is concluded.

(B) 5.1 The prices of the products shall be agreed upon from case-to-case by respective implementing seller and implementing buyer of the products;

(C) 5.1 X and the assignee(s) shall be granted most-favoured-customer conditions in the territory with regard to the products.

5.2. The prices of the products shall be quoted and paid for in----

Article 6: Assignment

(A) 6.1 X shall not be entitled to assign its buy-back undertaking under this Contract, either as a whole, or any part of it, to any other entity without the express written consent of Y.

Such consent shall not be unreasonably withheld.

(B) 6.1 X may assign the whole, or a part, of its buy-back undertaking under this contract, to any third party

6.2 In the event that X (hereinafter "the assignor") shall assign any part of its buy-back commitment under this contract to a third party (hereinafter "the assignee")

(A) All rights and obligations of the assignor under this contract with regard to the assigned part shall terminate at the time when the assignment contract between the assignor and the assignee becomes effective, and the respective rights and obligations shall be vested in the said assignee; provided that in the said agreement the assignee assumes all the obligations of the assignor agreed upon in this contract with regard to the part so assigned

(B) The assignor shall remain responsible, jointly and severally with the assignee, for the fulfilment of all of its obligations agreed upon in this contract.

6.3. X agrees to include in its agreement with any assignee appropriate provisions whereby the assignee commits itself to be bound by this contract with regard to the assigned part of the buyback commitment, as if this contract had originally been executed by the assignee. In consideration for the said commitment, Y agrees to be bound by this contract against the

respective assignee, with regard to the assigned part of the buy-back commitment, as if this contract had originally been executed with the assignee.

6.4. In the event that a party shall assign any part of its buy-back obligations under this contract to an assignee· it must give notice to the other party of the assignment. If the notice is not received by the "other party within a reasonable time after the assignment, the party will be liable for the damages resulting from such non-receipt.

Article 7:Re-sale of the products

7.1. X or its assignee(s) shall have the right to re-sell the products in the territory agreed upon below in paragraph 7.2 (hereinafter "the territory").

(A) 7 .2. The territory shall include all countries in the world.

(B) 7.2. The territory shall include the countries set forth in appendix with respect to each of the products or product groups mentioned therein.

(C). X-land

7.3. The products shall not be re-sold outside the territory without the written consent of Y.

7.4. It is agreed by the parties hereto that the restrictions set forth in paragraphs 7.2 and 7.3 above shall be construed as undertakings from the part of X or the Assignee, to refrain from actively putting the products in the market outside the territory.

Article 8: Reference

Each implementing contract as may be entered into by a party or its Assignee in accordance with the terms of this contract, must explicitly refer to this contract and state that the said implementing contract is made in fulfilment hereof. The parties agree to include m their agreements with any assignee appropriate provisions to that effect.

Article 9: Terms of delivery

Unless otherwise agreed in the individual implementing contracts, the terms of delivery of the products will-----

Article 10: Time schedules for performance

10.1. Deliveries of the products by Y will commence ----days/months after the completion of the performance test and acceptance of the equipment/technology under the primary contract and the technical assistance contract.

10.2. It is presently estimated that the buy-back commitment agreed upon in article 4 above will be fulfilled according to the following schedule:

10.3. Actual quantities and assortments of products to be delivered will be negotiated and agreed upon in the individual implementing contracts to be concluded not later than days/months before the beginning of each year/quarter/month with regard to the said year/quarter/month.

10.4. When actual quantities and assortments are agreed upon, X's remaining buyback commitment and X's own needs for products and prevailing market conditions in the territory for the various assortments of the products will be taken into consideration. It is agreed, however, that, until the total buyback commitment has been fulfilled, the value of products to be sold by Y and bought by X each calendar year will be at least---- and not more than-----.

10.5. Sufficient Implementing Contracts to cover the whole of X's buyback obligation as agreed under paragraph 4.1 above, must be concluded by----

Article 11: Lack of conformity

11.1. X must examine the products delivered to him within as short a period as is practicable in the circumstances.

11.2. X loses the right to rely on a lack of conformity of the products if it does not give notice to Y specifying the nature of the lack of conformity within----after it has discovered or ought to have discovered it.

11.3. Further rights and obligations of the parties with regard to the lack of conformity of the products will be governed.

(A) By the provision of the law applicable to this contract.

(B) By the provision of the guarantee conditions attached to this contract as appendix (), and by the provisions of the law applicable to this contract.

Article 12: Payment of the products

12.1. The Products shall be paid for in the currency agreed upon in paragraph 5.2 above, and in the manner set forth in paragraph 12.2 below.

12.2. Each delivery of the products shall be paid against the original documents set forth in paragraph 12.3 below.

(A) Through direct bank transfer to the bank account in Y land of the implementing seller of the respective products.

(B) Through an irrevocable and transferable letter of credit, allowing partial and trans-shipments, to be opened in the amount of the respective implementing contract at the latest----days after the signing of the said contract, in the respective implementing seller's favour, and to be confirmed by the bank in Y land designated by the said implementing seller, such letter of credit to be valid for a period of-----days/weeks/months after the agreed date of delivery of the respective products.

12.3. The products/letter of credit shall be payable against the following documents:

12.4. The Implementing Buyer shall bear all exchange and bank charges as well as any other costs, including the confirmation charges of Letters of Credit but excluding the charges of the

Bank of Y -land for transferring the funds to the Implementing Seller's account.

Article 13: Monitoring the performance

13.1. Both X and Y shall keep records on all implementing contracts concluded within the framework of this contract. Each such record (hereinafter "the evidence account") shall be in the form set forth in appendix () to this contract.

13.2. The evidence accounts maintained by X and Y shall be compared and agreed by the parties through exchanges of letters on a quarterly basis during the term of this contract, the first occasion being no later than-----

13.3. X and Y hereby agree that the evidence accounts, compared and agreed in accordance with paragraph 13.2 above, shall constitute final and conclusive evidence as to the performance of their obligations under this contract.

Article 14: Liability

14.1. In the event that X's buy-back commitment, agreed upon in this contract, has not been fully performed by the date mentioned in paragraph 10.5 above, X shall, upon written demand by Y remit to Y as agreed and liquidated damages-----percent-----%) of the value of the products yet to be purchased under paragraph 4.1 hereof.

14.2. Notwithstanding the provisions of paragraph 14.1 above, X shall not be obligated to make any payment mentioned therein insofar as the lack of performance of X's buy-back commitment is due to the failure of the implementing seller to deliver products of the quality, price or cumulative value specified in Articles 3, 5 and 10, respectively, of this contract.

14.3. If the lack of performance of X's buy-back commitment is due to the reasons set forth in paragraph 14.2, Y shall, upon written demand by X, remit to X as agreed and liquidated damages-----percent-----% of the value of the products yet to be purchased under paragraph 4.1.

14.4. As guarantee for the due performance of its obligations under this article 14 X shall issue to Y a bank guarantee, acceptable to Y, for the sum of .The bank guarantee shall be essentially of the form and contents as set forth in appendix () attached to this contract.

14.5. As a guarantee for the due performance of its obligation under this article 14 Y shall issue to X a bank guarantee, acceptable to X, for the sum of----The bank guarantee shall be essentially of the form and contents as set forth in appendix () attached to this contract.

14.6. The payment by the respective party of the agreed and liquidated damages, set forth in paragraphs 14.1 and 14.3 above, shall be in full and final settlement of all claims that the

other party may have against the first party arising out of or in connection with the breach by the first party of his obligations under this contract.

Article 15: Relief

15.1. A party is not liable for a failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that it could not reasonably be expected to take the impediment into account at the time of the conclusion of the contract or to have avoided or overcome the impediment or its consequences.

15.2. Exemption under this article 15 shall be available to the affected party for the period during which the impediment prevents it from fulfilling his obligations under this contract. If the effect of the impediment lasts for more----than months, each party shall be entitled to terminate this contract upon written notice to the other, and neither party shall be liable to the other for any expenses or losses thereby incurred.

15.3. The party who fails to perform must give notice to the other party of the impediment and its effects on his ability to perform. If the notice is not received by the other party within a reasonable time after the party who fails to perform knew or ought to have known of the impediment, he is liable for damages resulting from such non-receipt.

15.4. A party may not rely on a failure of the other party to perform, to the extent that such failure was caused by the first party's act or omission⁴⁰³.

Article 16: The effect of the termination of the primary contract of the implementing contracts

16.1 In the event that the primary contract should subsequently be terminated without the equipment/technology having been transferred and accepted, this contract shall become automatically null and void and with no effect.

16.2 For the purposes of this contract, X's buy-back commitment, agreed upon herein, or a respective part thereof, as the case may be:

⁴⁰³ Articles 79 and 80 of the United Nations Convention on Contracts for the International Sale of Goods 1980.

(A) Shall be deemed fulfilled even if any implementing contract should later be terminated, through no fault on the part of X, for whatever reason.

(B) Shall not be deemed fulfilled insofar as any implementing contract should later be terminated, irrespective of the grounds for which the implementing contract was terminated. In this case X shall be obligated to conclude (a) fresh implementing contract(s) corresponding to the value of the terminated implementing contract(s) such fresh implementing contracts to be then carried out in accordance with the provisions of this contract.

Article 17: Prior commitments, effective date, amendments, and governing language

17.1. Except as otherwise expressly provided in this contract, this contract supersedes and invalidates all other commitments or representations which may have been made by X and Y either orally or in writing prior to the date of signature of this contract.

17.2. This contract shall come into effect only upon the entering into force of the primary contract and upon the signing of this contract by both parties and upon the approval of this contract by the competent authorities and/or financial institutions in Y land and/or X land. Y shall immediately notify X and X shall immediately notify Y by cable or telex of such approval, and the date of such notification, the latest of such notifications shall be the date on which this contract comes into effect. Unless the approvals are obtained within----- days/months from the signing of this contract, it shall be considered null and void and with no effect.

17.3. Amendments to this contract will be effective only if they are made in writing and signed by legally authorized representatives of the parties, and if approved by the competent authorities and/or financial institutions in Y land and X land.

17.4. The -----text of this Contract is the governing text

Article 18: Applicable law

This contract shall for all purposes be governed by, and construed in accordance with, the law of

Article 19: Settlement of disputes

19.1. All disputes or differences which may arise between the parties out of or in connection with this Contract, and which cannot be settled amicably shall be subject to arbitration by---
- arbitrator(s) under the rules of----

19.2. The award of the arbitrator(s) shall be final and binding on the parties.

19.3. The arbitration proceedings shall be conducted in the----language.

19.4. The place of arbitration shall be-----

4. Overview of the Iranian Buyback Contract⁴⁰⁴

(Paydar West Field Asmari and Bangestan Reservoirs)
National Iranian Oil Company, South Fields (Year 1999)

Article 2-Scope of service

Contractor responsible to N.I.O.C. for operations and is to provide all capital, technology and skills necessary for the conduct of Development Operations for this Contract, and shall bear the Petroleum Costs required in carrying out Development Operations, and to recover such costs as provided in Clause 22 hereof, and bear the risks that sufficient production additional production of Crude Oil, and or Natural Gas may not be produced from the Contract Area in order to recover all such Petroleum Costs.

Article 3 -Term (Duration)

3.1. N .I.O.C. hereby authorizes Contractor to conduct development Operations in the end of the Development Phase in (To Be Negotiated) field. The conclusion of the Development

⁴⁰⁴ This part is being borrowed from Kakhki, Mohammad Mehdi Hedayati (2008) A critical analysis of Iranian buy-back transactions in the context of international petroleum contractual systems, Durham theses, Durham University. P 270

Phase, under the Master Development Plan, for (To Be Negotiated) Field is (To Be Negotiated) months, unless extended by mutual agreement.

3.3. This Contract shall commence on the Effective Date, and shall continue through the Development Phase and thereafter until Contractor has recovered all Petroleum Costs and remuneration fee in accordance with Clause 22 ... which period shall not exceed (To Be Negotiated) years from the date on which ... Field has commenced first/additional production, unless extended by agreement.

Article 5- Rights of NIOC

N.I.O.C. shall exercise all necessary control and supervision and has all rights to utilise the Contract Area for purposes not related to this Contract, except that such usage shall not prevent or hinder the carrying out of the Development Operations within the Field. N.I.O.C.s rights include inter alia:

(c) - Insurance

N.I.O.C. has the option to provide any legally required insurance coverage of materials and equipment, pursuant to 12.

Article 6- NIOC Assistance

6.1 Land and water reasonably required by Contractor for the purpose of Development

Operations shall be acquired by the N.I.O.C. and put at the disposal of Contractor. The purchase prices shall be either paid by N.I.O.C. or included in the Petroleum Costs if paid by Contractor.

Article 7 - Rights and Obligations of Contractor

7.2 Contractor shall register a branch office in Iran for the purpose of following and complying with local laws.

Article 8 - Levies, Charges, Fees and Taxes

8.1 Any Iranian corporate income tax, Social Security Charges, or other levies imposed are payable by Contractor and an amount representing such charge shall be compensated by the N.I.O.C. to Contractor.

8.2 Contractor shall not be entitled to recover as Petroleum Costs

, and taxes charges, fees and levies upon its income levied outside of Iran nor any taxes, charges, fees and taxes of any nature that are paid directly by N.I.O.C.

Article 11 -Fixtures and Installations

11.2 - Ownership of Assets - All lands and assets acquired by the Contractor shall be the property of N.I.O.C., except for machinery and equipment imported on a temporary basis pursuant to provisions of clause 25 hereof.

Article 12 - Liability and Insurance

12.1 - Insurance - Contractor shall maintain insurance coverage in amounts required and N.I.O.C. may exercise the option to provide, at the Contractor cost, such coverage at rates not greater than market rates elsewhere.

Article 13 - Local Employment and Training

13.1 Contractor shall give priority to Iranian citizens in employment, or personnel to carry out the Development Operations, limiting the employment of foreign personnel to only positions where qualified Iranian citizens are not available. In regards to the requirements set out in the above Article, it can be added that the foreign company is obligated to prove that a non-Iranian employee has skills that are not available on the domestic employment market. Additionally, it is mandatory for training to be provided to Iranians with the purpose of eventually substituting the foreign worker. A further requirement is that the foreign employer must, on a mandatory basis, donate a sum of money that is a certain percentage of the foreign worker's pay (which must be at least IR 560.00 (about US\$70), as of 2001)). With regard to the expatriate employees' legal status, they must acquire a work permit from the Department for Employment of Expatriates at the Ministry of Labour and Social Affairs (MLSA), as well as a simultaneously applied-for, one-year duration, renewable residence permit. If the company wishes to terminate their employment, they must navigate a

complicated process, including a permission to terminate from the Labour Boards, which rarely favours the employer in their judgements.

Article 16- Operator ship

16.1 N.I.O.C. shall be the operator for all facilities, immediately after commissioning and start up.

Article 17- Joint Management Committee

17.1 Joint Management Committee ("JMC") of five representatives from each party. N.I.O.C. shall function as the JMC Chairman until the end of the first year, and thereafter JMC chairmanship shall alternate between members annually.

Article 18 - Master Development Plan and Budget

18.1 Master Development Plan, including Work Programs and Budgets for the Development Phase I attached as Appendix "[...]". Capital Costs shall be equal to or less than (To be Negotiated) for the field to carry out the Development Operation, expended over (To Be Negotiated) years from effective date in the manner set out in more detail in Appendix "X". First or additional production in the field is projected to occur within (To Be Negotiated) months after the Effective Date.

The amount in Sub-Clause 18.1 shall be the contract ceiling, which shall not be increased.

Article 22 -Cost Recovery and Remuneration Fee

22.1 Contractor shall recover Petroleum cost, together with bank charges from the month the expenditure occurred at a rate equal to LffiOR plus/minus (To Be Negotiated) percent.

22.3 Remuneration Fee- In addition to the Capital Costs, Non-Capital Costs, Bank Charges thereon and Operating Costs, Contractor shall be entitled to a remuneration fee of (To Be Negotiated) US Dollars to be paid commencing the first month following the date of first/additional production from the field as follows: (To Be Negotiated) In case of any changes required and approved by JMC in order to achieve the objectives of the Development Operations set forth in the original Master Development plan Contractor shall only be entitled to recover the additional related capital costs, resulting from all such

approved changes up to the ceiling amount pursuant to clause 18.1 and subject to clause 18.3. In such case the Remuneration Fee shall remain fixed and unchanged.

22.4 - Payment in Oil - Petroleum costs and the remuneration fee shall be paid to the Contractor. Oil/gas out of (To Be Negotiated) percent of the product produced from the field and delivered to Contractor pursuant to the crude oil/gas sales agreement. In the event that the petroleum Cost and Remuneration Fee are not fully paid during the Amortization Period, Contractor shall be entitled to receive Crude oil/Gas produced from the field as a result of Development Operation carried out by Contractor, pursuant to the Long Term Sales Agreement, until such Petroleum Costs and Remuneration fees are recovered, or the term expires pursuant to clause 3.3.

Article 24- Use of National Companies and Equipment

Contractor shall use the service of Iranian firms for the provisions of maximum utilization of Iranian content of the project with due regard to the laws of Iran.

Article 25- Exports and Imports (Customs)

25.1. Materials and equipment are not available in Iran shall be imported in the name of N.I.O.C. Any customs duties shall be paid by the Contractor and shall be reimbursed as non-capital costs.

Article 27 -Assignment

27.1 Any assignment by Contractor shall require the prior written consent of N.I.O.C., and which shall be granted or refused within thirty days of receipt by N.I.O.C. of notice from Contractor that it intends to make such an assignment.

Article 31 -Governing Law

Contract governed, interpreted by the laws of Iran.

Article 32 -Arbitration

Any dispute, controversy or claim arising out of or relating to this contract or the breach, termination or invalidity thereof, shall be finally settled by arbitration before three arbitrators. Any award of the arbitrators shall be final and binding on the parties. Either

party may seek execution of the award in any court having jurisdiction over the party against whom execution is sought.

APPENDIX "A" -Description of the Contract Area

APPENDIX "B"- Accounting Procedure

APPENDIX "C" - Long Term Crude Sales Agreement

Quantity

JMC under the Service Contract shall advise Seller (N.I.O.C.) and Buyer (Contractor) of the recoverable costs to be due to Buyer of the recoverable costs to be due to Buyer and the Service Contract (Service Contract Fees) during the next Quarter. Based upon the forecasted Service Contract Fees due to Buyer, Buyer shall furnish to Seller a statement of the volume of Crude Oil to be lifted in the lifting Quarter in order to compensate Buyer for the forecasted Service Contract Fees.

Payment

The Proceeds receivable by Seller under this Agreement shall be used to reduce the amounts owed to Buyer by Seller under the Service Contract and therefore no payments to Seller are required to pay Seller not post letters of credit or other guarantees of payment, relative to such deliveries, except as to any Crude Oil that Buyer may purchase from Seller in excess of amounts owed to Buyer under the Service Contract.

APPENDIX "D" -Agreement on Procedure for Arbitration

3 - The place of arbitration shall be agreed upon by the parties to the dispute. In the event that an arbitration site cannot be agreed upon prior to the appointment of a third arbitrator, then the arbitral tribunal shall, as its first act, convene in Tehran, Iran, to decide upon the site of arbitration.

4 - Each party shall appoint an arbitrator, and two arbitrators so appointed shall appoint a third arbitrator who shall act as chairman of the tribunal whom shall be from a country other than those of which the Parties are nationals.

11 -Referral of matters on dispute to arbitration by either party, shall if necessary to subject to the obtaining of the approvals of the appropriate authorities of the parties concerned.