



## Week in Review

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### 3 Crude Production Pact

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*Iran and Saudi Arabia come to an accord. [Read More](#)*

### Production Cuts

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*Russian majors aren't ready. [Read More](#)*

### 4 Foreign Ownership

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*Russia reverses decision on Bashneft. [Read More](#)*

### Turkish Stream

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*Deal may move ahead following World Energy Congress. [Read More](#)*

### Liquid Competition

---

*US LNG tries to compete in Turkey. [Read More](#)*

### 5 Rig Counts

---

*American shale in Permian Basin could bounce back. [Read More](#)*

### Hollywood's Take

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*Deepwater Horizon film paints event with black and white. [Read More](#)*

### Paris Agreement

---

*With EU ratification, climate change accord moves ahead. [Read More](#)*

### 6 Ratification

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*Russia holds back on COP 21. [Read More](#)*

### Cold Feet

---

*Decreased prices could mean cause Petronas to reconsider projects in Canada. [Read More](#)*

### Protestors Clash with Police

---

*Dakota Access Pipeline controversy escalates. [Read More](#)*

## Energy News Blog

### 2 Iran and Its New Petroleum Contract (IPC): A New Paper Drill

*– Alberto Perego*

*In order to attract pre-sanction levels of foreign investment, Iran has innovated new legal mechanism to attract foreign companies while protecting sovereign claim to their natural resources. ENERPO student Alberto Perego looks at the implications for Iran and foreign majors. [Read More](#)*



South Pars onshore facilities near Asaluyeh by Hamed Malekpour; Own work, CC BY 4.0



## Energy New Blog

### Iran and Its New Petroleum Contract (IPC): A New Paper Drill

– *Alberto Perego*

Iran has the largest gas reserves in the world, and the 4th largest oil reserves. Its current oil production capacity is around 3.6 million bbl/d, and it is no secret that with the sanctions lifted, Iran plans to increase production up to 5 million bbl/d. This is not an easy task in the context of oversupply in the international oil market. To achieve this goal, it is not enough to simply have low production costs of about US\$ 5-8 per barrel and easy extraction environment. At the current stage, the essential condition is advanced extraction technology and locked-in sales volumes. In order to guarantee these two conditions, Iran announced it has developed a special type of contract – the Iranian Petroleum Contract (IPC).

In Iran, the property of natural resources is severely regulated at a high juridical level. In fact, there is a constitutional provision banning private or foreign ownership of natural resources. Article 45 of the Iranian Constitution clearly states: “Public wealth and property, such as uncultivated or abandoned land, mineral deposits, seas, lakes, rivers and other public waterways, mountains, valleys, forests, marshlands, natural forests, unenclosed pastures, [...] shall be at the disposal of the Islamic government for it to utilize in accordance with the public interest. Law will specify detailed procedures for the utilization of each of the foregoing items.” This is a situation that often happens in oil producing countries, and usually to grant access to foreign capital and technologies in their markets, they adopt contracts known as Host Government Contracts.

So far, Iran used a system of buyback schemes to finance the exploration and development of its natural resources. These schemes are risk service contracts under which the contractor is paid with a portion of the hydrocarbons produced by employing its services. Pay-backs tend to have short time frames, and to be used for around five to seven years. At the end of the duration of the contract the developed field goes back to the National Iranian Oil Company (NIOC).

These contracts are not considered very comfortable tools by international oil companies (IOCs). The main complaints are that the buyback scheme proved to be too inflexible on several occasions, and that it granted limited returns. Moreover, this contract was designed in a way that made it difficult for IOCs to put a ceiling on their capital costs.

The IPC is intended as a fresh start in relations between NIOC and IOCs, as it proposes several innovative solutions especially interesting for the IOCs. Firstly, the IPC will have a longer duration of about 20-25 years. This will allow a much longer cost recovery period. Secondly, there will be a risk-reward element linked to the complexity of fields. Companies will be paid higher fees for very high risk projects on offshore fields, and lower fees for low-risk onshore fields.

While the two points mentioned above are favourable for the IOCs, there are also at least two provisions favourable for Iran, its NIOC and its other oil companies. The IPC is designed to take advantage of foreign companies’ marketing expertise and give Iran access to their supply network to find an export market, a crucial feature in this times of oil oversupply. Another advantage for NIOC and Iran is the fact that any dispute arising under the IPC will be subject to the exclusive jurisdiction of the Iranian courts. International companies may not feel too comfortable with this provision, and would probably prefer international arbitration, or international courts.

Whether this new juridical tool will successfully serve its purpose depends on many factors, from Iran keeping up its promises in nuclear matters to the willingness of the investors to put capitals in the oil markets in times of oil oversupply. However, the IPC is an interesting new contract and is definitely an important step forward for Iran to come back at pre-sanction levels of oil and gas production.

[Dave Forest, 2016. The Start of Something Big? Iran Changes Oil Contracts. OilPrice.com. 23 September, 2016.](#)

[Oil & Gas 360, 2016. New Iranian Oil Contracts Unlikely To Attract Big Oil. OilPrice.com. 10 August, 2016.](#)

[Dalga Khatinoglu, 2016. Tougher oil investment problems for Iran than 2 decades ago. Trend News Agency. 12 November, 2015.](#)

[Iranian Constitution English translation taken from the website of Alavi and Associates.](#)



## The Week in Review

### **OPEC Deal: Riyadh and Tehran Reached a Pact on Reducing Crude Oil Production**

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*As producing countries gather in Algiers for talks on September 28, Riyadh and Tehran reached a pact on reducing crude oil production. The exact numbers will be determined in November, but the September deal is still significant. It is the first time that this kind of agreement is announced since the 2008 crisis. The goal is to drop crude oil production to 32.5 million bbl/d (which has reached 33.47 million bbl/d in August). Should parties fail in reaching the agreement on November 30, that will be a disaster according to some OPEC sources. For two years, crude oil price has been tumbling. In June 2014, crude oil Brent price was US\$ 110 a barrel and fell down to \$30 a barrel at the beginning of 2016. Currently, the Brent price is just under \$50 a barrel. The major cause is the discovery of shale oil in the US and the recovery of Libya and Iran. As the sanctions on Iran were lifted, it had set a target output of 4 million bbl/d— roughly the level it pumped before oil sanctions were imposed in 2012 – and above the country’s current level of around 3.6 million bbl/d. This was the reason why Saudi Arabia first refused to freeze its oil production. However, if the oil price continues to drop, Riyadh will suffer a fiscal deficit equal to 13.5% of GDP this year. Indeed, 73% of revenues in Saudi Arabia are based on oil. IMF says the Saudis need oil close to \$67 a barrel to recover. The problem is pressing for all OPEC members.*

*[David Sheppard and Anjali Raval, 2016. Opec deal: How Riyadh and Tehran poured oil on troubled waters. Financial Times, 30 September, 2016.](#)*

### **Russian Oil Producing Companies Not Ready to Reduce Output**

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*At an informal meeting in Algeria on Wednesday night, OPEC agreed on a production limit in the range of 32.5-33 million bbl/d. The Russian Energy Minister announced that Russia is ready to consider participation in joint actions of OPEC and in October-November the Russian Federation will conduct the necessary consultations with OPEC. Heads of the two of the biggest oil producing companies in Russia, Gazprom Neft and Lukoil, expressed their views on the matter. On 30th September, Lukoil Chief Executive Vagit Alekperov said that Lukoil is not ready to reduce its oil outputs, but he agreed on the need of signing a protocol on stabilizing oil production between Russian oil producers. President of Gazprom Neft Alexander Dyukov during an interview to “Russia 24” also expressed concerns about cuts in production. He also explained that freezing production is technically possible, but it will lead to 5-10% decline in production. Lukoil and Gazprom Neft are the second and the fourth biggest oil company in Russia. They produced respectively about 707 million bbl and 482 million bbl in 2014. Their share of the market is enough to put pressure on the government. Other Russian oil producing companies haven’t yet expressed their readiness to reduce output, but controversy between producers and the government will put Russia in a difficult situation.*

*[Maria Kiselyova, Polina Devitt, Dmitry Solovyov. Russia’s Lukoil CEO Says Not Ready to Reduce Oil Output. Rigzone. September 28, 2016.](#)*

*[Ria Novosti, 2016. “Газпром нефть” заявила, что не готова снижать добычу сырья \[Gazprom Neft Announced that They Are Not Ready to Decrease Output\]. RIA Novosti. 1 October, 2016.](#)*



## **Russia, Bowing to Budget Pressures, Revives Oil Firm Sell-off**

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*It seems that Russia's budget shortfalls have forced them to reverse an August decision to suspend state sell-offs of key assets. The decision to allow for sale of a minority stake in Bashneft has potential to attract overseas buyers interested in the Russian market. "Russia said on Friday that it was resuming the shelved privatization of oil firm Bashneft, in a sign of how anxious the Kremlin is to raise money to fill holes in the budget left by the economic slump." This will raise about 1 trillion rubles by the end of the year if the deal goes through. A minority stake in Rosneft is also now up for grabs. All in all, it seems that Russia needs a stop-gap injection of money to make it through the next current year without eating up the rest of the sovereign wealth fund reserves.*

[\*Darya Korsunskaya, 2016. Russia, Bowing to Budget Pressures, Revives Oil Firm Sell-off. Investing.com. 30 September, 2016.\*](#)

## **Intergovernmental Agreement on Turkish Stream Expected Soont**

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*On Friday, September 30, the Russian Energy Minister Alexander Novak announced during an interview to Rossiya 24 TV channel that a draft for an intergovernmental agreement between Russia and Turkey on the Turkish Stream project is in progress and is expected to be agreed upon and signed on October 2016. Istanbul will host the World Energy Congress on October 10-12, and the Russian Government has instructed the Energy Ministry to prepare the draft before the event. This doesn't mean that the construction of the pipeline will start immediately. Gazprom still needs to obtain all of the required construction and survey permits for Turkish territorial waters. During the International Investment Forum Sochi-2016 on Friday, the Gazprom Deputy CEO Vitaly Markelov said that most of the permits for the Turkish Stream gas pipeline project have been already obtained, with the most important being the exploration permit. The Russian President Vladimir Putin is expected to pay an official visit to Turkey in October. The main focus of the visit will be the Turkish Stream project and we may expect the signing of the agreement which will assure the implementation of the project. Initially, Turkish Stream was conceived as an alternative to the "South Stream", which was supposed to supply gas to Europe, bypassing Ukraine as a gas transit state. However, at this stage Gazprom intends to construct only 2 of the planned 4 pipelines with overall capacity of 63 bcm. The current project consists of two pipelines, one of which will be to supply gas for the domestic needs of Turkey and the other is for the European market. Conformations by Brussels are yet to be obtained and there are no guarantees at this stage that Russia's gas will be allowed to enter the EU.*

[\*TASS, 2016. Draft intergovernmental agreement on Turkish Stream to be prepared by October 10. Russian News Agency TASS. 30 September, 2016.\*](#)

[\*Daily Sabah, 2016. Russian President Putin to visit Turkey in October. Daily Sabah. 28 September, 2016.\*](#)

## **Will US LNG Be Competition for Gazprom in Turkey?**

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*US LNG supplies were delivered to Europe for the third time early last week, Platts reports. The third shipment arrived in Turkey and the first two arrived to Portugal in April and Spain in the summer. Neither Portugal nor Spain are supplied by Gazprom, but the third shipment to Turkey is significant given that a large portion of Turkey's imports is from the Russian. This is despite deteriorating relations last year after a Russian fighter jet was shot down in Ankara. Earlier this year Turkey became Russia's third largest customer after Germany and Italy. Most US LNG shipments have been destined for South America, Central America, and the Caribbean, while others have gone to China, India, and the Middle East. Vladimir Debrentsov, BP's Head of Russia and CIS economics stated, "Russian gas production costs are very low, among the cheapest in the world. My thinking is that Gazprom will undercut US LNG."*

[\*Stuart Elliot, 2016. US LNG cargo Lands in Turkey, First Market with Direct Russian Competition. S&P Global Platts. 29 September, 2016.\*](#)



## **The Permian Basin's Future Impact on US Shale Output**

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*Throughout the past couple of years, low oil prices have reduced US oil production by one million barrels per day. The last production peak was registered in April 2015, and it consisted in a production of 9.7 million bbl/d. However, the Permian basin exploration and exploitation of oil and gas fields has proved to be immune even in times of barrel prices around the US\$ 40 mark. Today's oil market is still very concerned with overproduction, and even amid talks and declarations of an OPEC freeze the Permian basin outlook for 2016 shows a rebound in its rig count. In May the US rig count was at its lowest point with 404 rigs in total. At the end of September, the count was up to 511 rigs. Out of this 107 new rigs, 64 are located in the Permian basin. The reason behind this growth is what is called the 'the Permian hydrocarbon column'. The Permian basin is characterized by its stacked formations. This allows the companies to extract using fewer wells, and as a result to operate with lower breakeven costs. In these times of crisis of the oil businesses, the shale industry has been resilient, but it has suffered losses as well. Lots of shale companies are now relocating their assets and knowhow in West Texas. This new wave of investments meant a rising price for purchasing land in the region. Shale technology is improving fast and thanks to the production cut agreed upon on the 28th of September by OPEC the Permian basin is now possibly set for an even higher level of growth.*

[\*Nick Cunningham, 2016. Permian Could Lead U.S. Shale Output Higher. 29 September, 2016.\*](#)

## **"Deepwater Horizon" Film Fumbles with Facts**

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*The film "Deepwater Horizon" tells the story of the BP disaster in the Gulf of Mexico in 2010. The film does a terrific job of recreating the look and feel of the offshore oil industry: it shows the challenges of working in isolated and hostile conditions, but it also fumbles some key details. It tells only a partial version of the story in simplistic fashion, setting opposition between the heroes of Transocean, which owned and operated the Deepwater Horizon rig, and the villains, that being BP. In reality, employees of both companies were at fault. The screenplay does stick pretty closely to its source, the New York Times article on the rig's final hours, but the film deviates from the record; it does show Transocean in a better light and BP in a worse one. What is barely shown in the film is the "command confusion at a critical point in the emergency", which was highlighted by the US Coast Guard's report on the accident. Other criticisms of Transocean are also skated over or ignored. To find out what really happened one must read the reports from the Presidential Commission or the US Coast Guard's Marine Board of Investigation, or the findings of fact from Judge Carl Barbier in the main court case over the disaster. Overall what audiences can take away from the film, is the vivid sense of the extraordinary engineering feat that is deep-water drilling. In that aspect, "Deepwater Horizon" has to be judged as a success.*

[\*Ed Crooks, 2016. Deepwater Horizon film fumbles with facts. Financial Times. September 30, 2016.\*](#)

[\*David Barstow, David Rohde, Stephanie Saul, 2016. Deepwater Horizon's Final Hours. The New York Times. December 25, 2010.\*](#)

## **Climate Agreement Enters into Force**

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*The European Union has announced of its ratification of the Paris Agreement on Climate Change. Previously, the agreement was ratified by China, the US, Brazil, India, and more than 50 other countries. The agreement that enters into force ahead of schedule: it was expected that this would only happen after two or three years. In order for the agreement to enter into force, it was required that more than 55 countries responsible for more than 55% of global GHG emissions ratified it. With the EU ratification, these benchmarks were exceeded.*

[\*WWF, 2016. Парижское соглашение по климату вступает в силу \[Paris Climate Agreement Enters into Force\]. World Wildlife Fund. 5 October, 2016.\*](#)



## **What's Holding Russia Back from Ratifying the Paris Climate Agreement?**

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*Russia officially claims that it is “getting ready to ratify the Paris Agreement with regard to the subsequent implementation of procedures required by Russian law, including an overall assessment of socioeconomic issues of the ratification and the development of the relevant national legal framework”. However, there are factors that hold the country back in this process. Firstly, as noted by Angelina Davydova, an expert in international relations with the focus on climate change; there is a strong opposition from private businesses, predominantly coal and steel sectors. Secondly, there is a perception that Russia cannot allow itself an ambitious domestic climate policy for economic reasons. “Namely, there is lack of funding for emission reduction and energy efficiency measures,” the expert notes. As the treaty has come into force without Russian ratification, Russia’s role in the climate change accord becomes uncertain.*

[\*Ministry of Foreign Affairs, 2016. Comment by the Information and Press Department on the upcoming entry into force of the Paris Agreement on Climate Change. Ministry of Foreign Affairs, 6 October, 2016.\*](#)

[\*Angelina Davydova, 2016. What's holding Russia back from ratifying the Paris climate agreement? The Conversation, 27 September, 2016.\*](#)

## **Petronas Wins Approval for Canadian LNG Project, but Gets Skeptical About Costs**

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*After a long struggle the Malaysian state-owned Petronas group received the green light from the Canadian Government for a massive LNG terminal project in British Columbia, development of gas fields in Alberta, and a 900 km pipeline between the provinces. The win was not easy and approval was awarded only in addition to hundreds of conditions, most of them of environmental character, tangibly raising the overall project cost. Petronas may reconsider its participation in the project as costs in the energy markets have taken significant downward turns since it showed initial interest in the ambitious projects. Canada, for its own part, optimistically looks forward to 4,500 new jobs should the project go ahead as projected. Everyone is patiently waiting for Petronas’s next move.*

[\*Jeevan Vasegar, 2016. Petronas wins approval for Canadian LNG project. Financial Times, 28 September, 2016.\*](#)

## **Conflict over North Dakota Access Pipeline Escalates with 20+ Protesters Arrested**

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*The mass protests happening in opposition to the North Dakota Access pipeline have escalated with the arrests of more than 20 people at a pipeline construction site located in Morton County North Dakota. Police used “military-style” equipment and armored vehicles to arrest 21 protesters and charge them with various crimes, including criminal trespass on private property, possession of stolen property, and resisting arrest. Since protests began in early August, over 95 people have been arrested for opposing the further construction of the Dakota Access Pipeline. The Dakota Access Pipeline is four-state US\$ 3.7bln project intended to carry 570,000 bbl of crude oil per day from the Dakotas to Illinois. The local Standing Rock Sioux Tribe has always opposed the pipeline construction because they feel its location (less than half a mile from their reservation) would threaten their only source of water, the Missouri River, should an oil spill happen, and encroach upon cultural heritage sites. Since August, they have been joined by protesters from other tribes located across the continental U.S. in a show of solidarity and also by environmental activists, farmers, and landowners, who had their land confiscated by the governmental power of eminent domain to make room for the pipeline. Despite the challenges to construction posed by the protesters, the pipeline is estimated to be over 60% completed.*

[\*RT, 2016. ‘Military-style’ armed police arrest 20+ Dakota Access protesters. Russia Today, 29 September, 2016.\*](#)

[\*Nick Bernabe, 2016. Media Silent as Dakota Access Pipeline protests spread, construction blocked in Iowa. The Anti-Media.Org, 28 September, 2016.\*](#)



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