The sanctions regime against Russia and the effects on the offshore community

Few thought the political climate in the world would change as much as it did when watching the winter Olympics in Sotchi in February this year. Only a few months later, USA, EU and other neighbouring countries implemented the first sanctions against Russia – with further and extended restrictive measures over the summer.

On 12 September this year the latest EU council regulation entered into force, extending the scope of the sanctions significantly, especially within the fields of shipping and offshore. The petroleum and offshore sector is one of three sectors that form part of the so-called economic sanctions against Russia, which include measures targeting certain aspects of sectoral cooperation and exchanges with Russia. The other two are the defence and the finance sectors. In addition, there are two other categories of sanctions against Russia which include asset freezes against a list of identified people and entities, and restrictions for Crimea and Sevastopol (especially import, export and finance prohibitions/restrictions).

With this article I will focus on the restrictions affecting the offshore and petroleum sector, and try to give you a brief overview of the sanctions provisions that are relevant to the offshore community.

Latest extensions
With the latest and extended sanctions regulations, the EU has sought to prohibit key services necessary for deep water and arctic oil exploration and production and shale oil projects. These key services are specifically; drilling, well testing, logging and completion services and supply of specialised floating vessels, ref. Article 3a in Council Regulation 960/2014 of 8 September 2014 (entered into force on 12 September 2014). The USA has implemented a corresponding regulation.

The EU passed a new Council Regulation 4 December 2014, No 1290/2014. This Regulation makes necessary and sought after amendments and specifications to many of the provisions in the various EU sanctions regulations against Russia, as well as defining a number of terms use (including to the abovementioned Article 3a). It is to be expected that the Norwegian regulations will be amended accordingly. I will...
mention the amendments and definitions below where these are of relevance to content of this article. In Council decision No. 2014/659/CFSP of 8 September, the EU Council explained the political backdrop for the extended sanctions against Russia in the following way:

2. On 30 August 2014, the European Council condemned the increasing inflows of fighters and weapons from the territory of the Russian Federation into Eastern Ukraine and the aggression of Russian armed forces on Ukrainian soil.

4. In view of the gravity of the situation, the Council considers it appropriate to take further restrictive measures in response to Russia’s actions destabilising the situation in Ukraine.

7 In addition, the provision of services necessary for deep water oil exploration and production, arctic oil exploration and production or shale oil projects should be prohibited.

Unrest in the offshore community
The wording of the last of the aforementioned necessary key services, “supply of specialised floating vessels”, caused a massive anxiety and uncertainty in the offshore and shipping community. The wording is comprehensive in form and would, if the same wording were to be applied by the member states, have an impact on a wide range of service providers. It would be easy to interpret the wording, as it stands in Article 3a, to include vessels such as seismic vessels and a number of supply vessels.

It seems likely, however, that the EU legislators in Brussels did not fully consider the impact of such a wide term, and many jurisdictions with a presence in the offshore and shipping industry in Russia have decided to use their right to define the term more closely when implementing the council regulation into national legislation.

The Norwegian Foreign Minister, Børge Brende, announced on 23 September 2014 that the Norwegian government would also mirror the latest extensions in the sanctions regime against Russia made by the EU, and gave the following explanation (our translation):

“Despite extensive international pressure, Russia has not shown any willingness to change its behaviour, in defiance of international law in Ukraine. Norway will therefore implement...
equivalent enjoining of the sanctions rules passed by the EU on 12 September.

Norway has, since the start of the crisis in Ukraine, remained united with the EU and neighbouring states in a joined, international reaction to Russia’s defiance of international law. The new restrictive measures will be implemented in the Norwegian regulation shortly."

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Focusing on the Norwegian sanctions regulations

The Norwegian sanctions regulations against Russia are found in, “Forskrift om restriktive tiltak vedrørende handlinger som undergraver eller truer Ukrainas territorielle integritet, suverenitet, uavhengighet og stabilitet av 15. august 2014”, as amended on 10 October 2014.

It is worth noting that the sanctions provisions are given a wide application in Section 1, and apply, among others, to anyone on Norwegian territory, all Norwegian citizens irrespective of where they are in the world, all legal persons, and entities or organisations founded or incorporated pursuant to Norwegian legislation or who run a business wholly or partly in Norway. This would, for example, mean that (on a general level) a Norwegian company cannot avoid the Norwegian sanctions regulations simply by channelling an ownership or interest through foreign set ups if this does not change the ownership, interest or contractual link. Furthermore, a Norwegian citizen or company might be in breach of one or more of the sanctions provisions, if this person is hired on board a drilling rig as key personnel to perform the drilling operations.

The effect of one word

As expressively stated by the Foreign Minister, the mirroring of the EU sanctions regulations includes the abovementioned Article 3a, but, similarly to many other jurisdictions, Norway decided to specify and thereby narrow the wording when translating “supply of specialised floating vessels”. The wording used in the Norwegian provision cited below is “supply of specialised floating facility”.

The Norwegian provision equivalent to the abovementioned Article 3a in the Council Regulation, Section 17a, is almost identical to Article 3a and reads as follows (our translation):

Section 17a
Prohibition against providing certain services to be used in the oil industry

1. It shall be prohibited to provide, directly or indirectly, the following associated services necessary for deep water oil exploration and production, arctic oil exploration and production, or shale oil projects in Russia:
   (a) drilling
   (b) well testing
   (c) logging and completion services
   (d) supply of specialised floating facility.

2. The prohibitions in paragraph 1 shall be without prejudice to the execution of an obligation arising from a contract or a framework agreement concluded before 11 October 2014 or ancillary contracts necessary for the execution of such contracts.

3. The prohibition in paragraph 1 shall not apply where the services in question are necessary for the urgent prevention or mitigation of an event likely to have a serious and significant impact on human health and safety or the environment.

In other words; this provision applies to whoever is in the business, directly or indirectly, of the four specified “associated services”, in which all would be considered as necessary for deep water and Arctic oil exploration and production (as well as shale oil projects).

Important to note, and different from the American sanctions regulations, is that the prohibition against the four specified key services does not apply for the fulfilment of contractual obligations which follows from “a contract or framework agreement concluded before 11 October 2014 or ancillary contracts necessary for the execution of such contracts”, ref paragraph 2 as cited above. Whereas the American linked company Exxon had to stop all drilling operations in Russia following only a short grace period, Norwegian companies who would fall under the scope of Section 17a could continue obligations under contracts entered into before 11 October this year. This provision has obviously and considerably reduced the negative effects of the EU sanctions regulations.

Of the four services mentioned, the last of these is still the alternative where we face most questions. It is difficult to give a general statement in an article as regards which types of facilities would be included and which will not, as there are always borderline examples – when is a “facility” a “vessel” (falling outside the scope of litra d) and the other way around. However, it is useful to look at the definition of “facility” as provided in the Norwegian Petroleum Activities Act of 1996, Section 1-6 litra d (although it does not always provide you with the answer), which includes;

“…installation, plant and other equipment for petroleum activities, however not supply and support vessels or ships that transport petroleum in bulk. Facility also comprises pipeline and cable unless otherwise provided”. 
Norway decided to specify and thereby narrow the wording when translating “supply of specialised floating vessels”. The wording used in the Norwegian provision cited below is “supply of specialised floating facility”.

Offshore technologies
The individual supply of pipelines and cables would not be covered by Section 17a, but could easily be in breach of the provision in Section 17. Section 17 is part of the Norwegian regulation which entered into force on 15 August 2014, and prohibits export of certain technologies to be used in the Russian oil industry (ref Council Regulation 833/2014 of 31 July 2014). Pursuant to paragraph 1 in the provision, authorisation is required for

“...the sale, supply, transfer or export, directly or indirectly, of technologies as listed in Annex IV, whether or not originating in Norway, to any natural or legal person, entity or body in Russia or in any other country, if such equipment or technology is for use in Russia.”

The technologies included in Annex IV, please see the following link; https://lovdata.no, are suited to the oil industry for use in deep water and Arctic oil exploration and production and or shale oil projects in Russia. Pursuant to paragraph 4, there is an absolute ban on the Norwegian Foreign Ministry granting authorisation for “any sale, supply, transfer or export of the technologies included in Annex IV” if they have reasonable grounds to determine that such is intended for deep water and Arctic oil exploration and production or shale oil projects.

Similarly to Section 17a (2), however, the Foreign Ministry may nevertheless grant an authorisation “...where the export concerns the execution of an obligation arising from a contract or an agreement concluded before 16 August 2014”.

When dealing with Annex IV technologies, it is important to know that also technical assistance or brokering services in this regard, as well as the provision, manufacture, maintenance and use of these items – again directly or indirectly – when the assistance is for such technology used in Russia, would require authorisation from the Foreign Ministry. The same applies to financing or financial assistance (such as grants, loans and export credit insurance) related to such technologies. As with the technologies themselves, there is an absolute ban on granting authorisation to such assistance for contractual obligations entered into before 16 August this year, when the technology in question is to be used in projects regarding deep water or Arctic oil exploration and production or shale oil projects in Russia.

When a word is both a limitation and a solution
There is an interesting, and apparently not clearly reasoned, limitation in the regulations discussed above. All three sections, 17, 17a and 18, include – to varying degrees – the limitation in the terms “deep water” and “Arctic” oil exploration and production. In other words, where a sanction regulation is limited by these two words, any operations performed in oil fields in Russia which are neither Arctic nor deep water would be lawful.

Up until 4 December 2014, neither terms were defined or explained in any preparatory works to the regulation, nor in the EU Council Regulation or other guidelines. As the Foreign Ministry had announced, the EU Council has now passed a Council Regulation, No 1290/2014 of 4 December 2014, where the wordings of certain provisions are amended to include a specification of, among others, the two abovementioned terms, as well as a specification of shale oil production.

We expect the Norwegian government to implement the same specifications in the Norwegian sanctions provisions, but emphasise that there might be small differences. Both Section 17 and 17a will in that case have the following wording added to define “deep water”, “Arctic” and shale oil production, implementing the amendments to respectively Article 3 in Council Regulation 833/2014 and Article 3a in Council Regulation 960/2014:

(a) oil exploration and production in
(b) oil exploration and production in the offshore area north of the Arctic Circle; or
(c) projects that have the potential to produce oil from resources located in shale formations by way of hydraulic fracturing; it does not apply to exploration and production through shale formations to locate or extract oil from non-shale reservoirs.

Article 3a has also included a requirement for the service provider to notify the authorities within five working days of any activity performed which might be in breach of the provision. Also worth mentioning is the amendment whereby the EU Council has emphasised that all provisions regulating the offshore sector in Russia shall include Russia’s Exclusive Economic Zone and Continental Shelf.

Up until the specifications were introduced on 4 December, the term “Arctic” had not been subject to many questions, as there had been a common understanding that Arctic means any geographic area north of the Polar Circle. The definition of “deep water” to 150 metres or deeper, however, is somewhat surprising. 150 metres is in line with the definition set by the Americans, who defined “deep sea” to be 500 feet (about 152 metres). From a Norwegian and European offshore perspective, 150 metres is hardly characterised as “deep”, but it appears that the international uniform understanding has been important in this respect.

The above specifications mean that at least one Russian offshore area would not be included by the abovementioned sanctions provisions. The offshore area around the island of Sakhalin in East Russia is located south of the Polar circle. Furthermore, most or all of the oil fields in this area are located at depths of less than 152 metres, and would therefore not be considered as “deep sea exploration and production”. This effectively means that the Sakhalin area could be one of few Russian areas not affected by the sanctions, where performance of the key services could be done lawfully by a Norwegian company.

Criminal liability
One last point that needs mentioning is the authority under which the sanctions are given by the Norwegian Government. All non-military sanctions are given by the government pursuant to the Norwegian Sanctions Act of 27 April 2001, Lov om tverksettjing av internasjonale, ikke-militære tiltak i form av avbrot eller avgrensing av økonomiske eller anna sanktvern med tredjestater eller rørslar. This act also provides the criminal provisions which would apply if any person or legal entity was in breach of sanctions provisions issued by the government.

The maximum sentence/penalty is 3 years of imprisonment and/or fines for intentional breach or contributory breach, or a maximum of 6 months for negligent breach or contributory breach. For a company significant corporate penalties could be expected. It is worth noting that intentional evading of the law or otherwise unlawful transactions would be subject to a maximum sentence of 3 years of imprisonment and/or fines.