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Introduction

The oil and gas industry in Malaysia is a vital sector contributing significantly to the country's economy. With significant oil and gas reserves, Malaysia continues to attract substantial investments in exploration and production activities in this critical energy transition phase.[1]

Drilling rigs are strategic assets which are essential for the production of oil and gas reserves. The acquisition of drilling rigs involves intricate legal processes and regulatory compliance. Understanding the legal aspects of purchasing a drilling rig in Malaysia is essential for investors to ensure a smooth legal transaction.

Regulatory Framework

The supply and use of offshore vessels in the oil and gas industry in Malaysia are regulated by several statutes, *inter alia*, the Petroleum Development Act 1974 ("**PDA**"), the Environmental Quality Act 1974 ("**EQA**"), and the Merchant Shipping Ordinance 1952 ("**MSO**").[2]

While the PDA is the main piece of legislation for Malaysia's oil and gas sector and the EQA governs marine oil pollution, the MSO is the principal legislation governing the licensing and registration of all vessels in Malaysia.[3] Therefore, the acquisition process for a drilling rig mirrors that of a traditional vessel as they are governed by the same legislation.

Legal Due Diligence

Prior to acquiring a drilling rig in Malaysia, conducting thorough due diligence is imperative to evaluate the legal standing of the drilling rig. This process entails verifying the title of the rig to ensure accurate ownership, identifying the state flag of the rig, as well as being able to ascertain whether there are any encumbrances or maritime liens attached to the drilling rig.

The flag of a vessel indicates which jurisdiction the vessel is subject to.[4] All of these information are crucial especially to ascertain the structure for the payment of the purchase price, and to effect the transfer and registration of the title later on.

Moreover, ensuring that the rig and the seller comply with all the necessary regulatory requirements, including obtaining any licences or permits, is crucial to ensure a smooth transaction.

Structure of the Acquisition Transaction

The acquisition of a drilling rig can be structured in different ways, depending on the interests of the parties involved. Some common transactions are by i) acquiring the rig as a standalone asset; ii) purchasing an equity interest in the entity owning the drilling rig, thereby acquiring ownership over the rig; or iii) entering into a joint venture agreement to jointly own and operate the drilling rig with another entity. For the purposes of this article, we will be focusing specifically, on the acquisition of a drilling rig as a standalone asset via a sale and purchase agreement ("**SPA**").

Upon the conclusion of the due diligence, if the purchaser is satisfied with its findings, parties will initiate the drafting, discussion and subsequent reviews on the SPA.

The SPA will first lay out the description of the drilling rig. Generally, a description of the rig is given in relation to the following elements: name, IMO number, classification society/- class notation, year of build, the identity of the shipbuilder, flag, place of registration and gross and/or net tonnages. Following that, the SPA will also set out the payment structure that has been agreed upon by the seller and the buyer, and the mortgagees, if any.

It is pertinent to note that one of the most important clauses in the SPA would be the representations and warranties clauses. Both the buyer and seller typically make representations and warranties to protect their respective interests.

These representations and warranties include, but are not limited to, the seller affirming its legal title and ownership over the drilling rig and asserting that the rig is free from all encumbrances, maritime liens or claims by third parties. Most sales of drilling rigs take place when the rig is "off-hire"/"laid-up" but any existing drilling contracts would have to be disclosed by the seller. The seller also provides assurances regarding the condition of the rig, confirming that it complies with all applicable laws and regulations and is fit for its intended purpose. Additionally, the seller would warrant that all title documentation, including certificates of ownership, permits, and licences are valid.

Conversely, the buyer represents that they have a good legal standing to enter into the agreement and that the transaction will not violate any of its organisational documents or existing contractual obligations. The buyer will also warrant that it has the financial capacity to fulfil the transaction. The buyer may represent that they have conducted thorough legal due diligence on the rig and is aware of its condition, operational history, and any associated risks. Some sellers would insist on the sale to be on an “as is where is” basis.

These representations and warranties serve as a crucial safeguard for both parties, delineating responsibilities and mitigating any risks inherent in the transaction. By providing assurances regarding ownership, condition and legal compliance of the rig, the seller will instil confidence in the buyer, while the buyers commit to being transparent throughout the transaction. Ultimately, the clause fosters trust and accountability between the parties involved.

Following which, the parties will also agree on an intended time frame for the rig to be delivered and the location for delivery when risk and possession passes to the buyer. The location for the delivery of the vessel could be a specific anchorage or port, or a place elected by the seller within a specified geographical area.

If the seller wishes to avoid domestic sales taxes and seeks to deliver the vessel in international waters close to a port within the agreed-upon area, the buyer may negotiate a term requiring the seller to bear all additional costs incurred by the buyer in connection with such delivery.

Registration with the Marine Department

Upon the fulfilment of all the rights and obligations of both parties as provided in the SPA, the buyer will deliver to the seller a duly executed bill of sale in the form agreed by the buyer and seller. The bill of sale is a document which is used to prove and effect the transfer of legal and beneficial title in the vessel from the seller to the buyer. It should be noted that the bill of sale should be in the form of the state flag of the drilling rig.

Following the delivery of all the relevant documents from the buyer to the seller, the buyer can proceed to register the drilling rig with the Malaysian Marine Department. The buyer is able to register the drilling rig at either one (1) of the five (5) ports of registry[5] in Malaysia.

Conclusion

In conclusion, the acquisition of a drilling rig in Malaysia is a multifaceted endeavour that requires careful contractual considerations. Ultimately, a comprehensive understanding of the legal aspects and diligent adherence to regulatory compliance are essential for investors to execute a successful legal acquisition of a drilling rig in Malaysia, securing a strategic foothold in this dynamic oil and gas industry landscape which is projected to require increasing drilling rig services. Engaging experienced legal advisors and industry professionals is essential to navigate the legal aspects effectively and achieve a seamless transaction.

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1. In January 2024 PETRONAS awarded Production Sharing Contracts (PSCs) for six exploration blocks and one Discovered Resource Opportunities (DRO) cluster. The Malaysia Bid Round 2024 (MBR 2024) for five exploration blocks and five DRO clusters is open until 1 August 2024.
2. Philip Teoh, "*Malaysia Oil and Gas Industry: Guide To Offshore Vessels, Facilities and Law*" (Maritime Fairtrade, 23 January 2024) <https://maritimefairtrade.org/malaysia-oil-and-gas-industry-guide-to-offshore-vessels-facilities-and-law/>
3. ibid.
4. Aisyah Llewellyn, "Does a Ship's Flag Matter?" (The Diplomat, 3 April 2024). <https://thediplomat.com/2024/04/does-a-ships-flag-matter/>
5. Port Klang, Pulau Pinang, Kota Kinabalu, Kuching and Labuan (MISR).

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