

## Bridging the GAP – Geopolitical Legal Due Diligence: The Impact of the Iran Crisis on M&A Transactions



### Executive Summary

- Geopolitical risks, particularly those associated with the Iran crisis and its far-reaching sanctions regimes, require an expansion of the scope of traditional legal due diligence to include a dedicated geopolitical dimension.
- As well as reviewing sanctions compliance and export controls, geopolitical legal due diligence involves analysing supply chain risks, FDI (foreign direct investment) screening requirements and political force majeure risks in the target company's key contracts.
- Even if the target company only has indirect ties to Iran, for example via suppliers, customers or business partners, this can pose considerable risks, particularly with regard to secondary sanctions imposed by the US government.
- The Iran crisis may also have a significant impact on the cost structure of energy-intensive target companies due to rising oil prices. This makes a company's ability to pass on costs to customers (also known as "pricing power") a central focus of geopolitical legal due diligence.
- The results of a geopolitical legal due diligence have a direct influence on purchase price mechanisms (earn-outs, MAC clauses), lists of warranties and the extent to which transactions can be covered by warranty and indemnity (W&I) insurance.
- Drafting forward-looking contracts that contain sanction-specific warranties, indemnity clauses and compliance covenants can help to allocate risks effectively and make transactions more secure.



## 1. Introduction

Even for seasoned transaction advisers, the speed and intensity with which the geopolitical landscape has shifted since early 2025 is unprecedented. In addition to the war in Ukraine, which is now in its fourth year, and the ongoing political instability in Europe, the current tensions surrounding Iran, which have now also spread across the entire Arabian Peninsula, have reached a new level of escalation. The war, coupled with Iran's increasing isolation from international trade and the stricter rounds of sanctions imposed by the EU and the USA, is creating a risk environment that extends far beyond the Middle East. Although a ceasefire was agreed between the USA, Israel and Iran on 8 April 2026, the immediate consequences of the conflict are already being felt on the energy markets. Each new report of further escalation in the Gulf is driving up oil prices, increasing production costs for countless European companies.

Following Donald Trump's inauguration as the 45th and 47th President of the United States and the political earthquake that ensued, we in Europe have been forced to relinquish the last shred of certainty that has underpinned economic prosperity, legal assurance and predictability in recent decades: the transatlantic partnership between the USA and Europe. The current US government's chaotic approach to customs policy is fuelling uncertainty, particularly for companies with strong ties to the US market, and this dynamic is only being exacerbated by the Iran crisis. The extraterritorial reach of US sanctions policy – specifically, the secondary sanctions imposed by the Office of Foreign Assets Control (OFAC), now also affects European companies without a direct presence in the USA.

It has rarely been more difficult to provide reliable valuations of companies and forecasts for business models in recent decades.

PEST analyses, a framework for systematically investigating the macroeconomic factors (political,

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<sup>1</sup> Aguilar, *Scanning the Business Environment*, 1967. Has since been further adapted into the acronym **PESTLE**, among others.

economic, social and technological) that impact strategic corporate management decisions and market entry analyses, have been widely used in academic circles for half a century<sup>1</sup>. Since the 1980s, states, associations of states, armed forces and security organisations have used the acronym VUCA (volatility, uncertainty, complexity, ambiguity), which is currently enjoying renewed popularity, in an attempt to describe dynamic environmental conditions<sup>2</sup>.

Following the period of low interest rates, tools that had previously been gathering dust in the transaction adviser's toolkit, such as MAC clauses, vendor loans, holdbacks, escrows and earn-out clauses, have been given a new lease of life and have become increasingly relevant. It is therefore time to look beyond these tried-and-tested mechanisms to another, increasingly critical area of focus: geopolitical legal due diligence, and our "Bridging the GAP" series is the perfect venue for exploring this in more detail.

## 2. What is geopolitical legal due diligence?

Traditional legal due diligence focuses on assessing the target company from a legal standpoint, taking into account its corporate structure, key contracts, employment relationships, intellectual property rights, legal disputes and regulatory compliance. This then provides the legal basis for determining the purchase price and structuring the list of warranties.

Geopolitical legal due diligence, however, goes beyond these traditional areas of review, systematically examining the extent to which the target company is exposed to geopolitical risks that could jeopardise its business activities, its valuation or the feasibility of the transaction itself. The following aspects are examined in particular detail:

**Sanctions compliance.** The central question is whether the target company maintains business relationships with sanctioned countries, persons or entities, either directly

<sup>2</sup> Bennis / Nannus, *Leaders: Strategies for Taking Charge*, 1985. Analysis model adopted in particular by the U.S. Army War College and the Bundeswehr Command and Staff College.



or through its supply, value or “activity” chains. Particular attention should be paid to the complex and sometimes divergent sanctions regimes of the EU and the USA. While the EU sanctions against Iran are governed by Regulation (EU) No. 267/2012, the US sanctions laid down in the OFAC regulations also cover non-US companies with ties to the USA (also referred to as secondary sanctions).

**Export controls and dual-use goods.** Companies that manufacture, distribute or export goods or technologies with potential military applications are particularly exposed. The corresponding regulatory framework comprising the Dual-Use Regulation (EU) 2021/821 and the German Foreign Trade and Payments Act (AWG) has come to play an increasingly important role in the context of the Iran crisis.

**Supply chain risks.** Geopolitical legal due diligence also involves checking whether the target company’s key suppliers or customers operate in regions subject to sanctions, trade restrictions or political instability. The same applies to intermediaries and distributors who may have indirect links to Iran.

**Investment controls and FDI screening.** In numerous jurisdictions, including Germany (Section 55 et seq. AWV), the EU (Screening Regulation (EU) 2019/452) and the USA (CFIUS), acquisitions of companies concerning sectors relevant to national security are subject to review under foreign trade law. These review criteria have been extended in direct response to the current heightened geopolitical situation.

**Political force majeure risks.** Finally, it must be verified whether any of the target company’s key contracts contain force majeure clauses covering geopolitical events such as war, sanctions or embargoes, and what the legal consequences of these might be. Unlike MAC clauses, which cover situations in which a transaction becomes less economically attractive for the buyer, force majeure clauses address cases in which it is no longer possible for contractual obligations to be met.

### 3. The Iran crisis as a benchmark

The current Iran crisis lends itself particularly well as a reference point for geopolitical legal due diligence, as it touches on almost all of the above-mentioned aspects simultaneously.

**Compliance country risks as early indicators.** One well-established and widely used standard reference work that stands out from the growing number of international risk indices is the Corruption Perceptions Index (CPI), which is published by the NGO Transparency International and now in its 31st edition. This “corruption barometer” measures the propensity for public sector corruption in 182 countries worldwide and shows a clear correlation with other comparable indices, such as the Fragile States Index (FSI), the Global Terrorism Index (GTI) and the Modern Slavery Index (MSI). The CPI is also used as a key parameter for the Basel AML Index. In the latest edition for 2025, released on 10 February 2026, Iran is ranked 153rd with just 23 out of 100 possible risk points. This is significantly lower than the regional average for the MENA region of 39 points and shows a clear negative trend when compared over a ten-year period<sup>3</sup>. It is crucial that such clear, publicly available risk statistics are reflected appropriately in transaction structures or factored into contract negotiations on a cost-oriented basis.

**EU and US sanctions regimes: Primary and secondary sanctions.** The sanctions regime imposed on Iran is one of the most complex in the world. At the EU level, Regulation (EU) No. 267/2012 prohibits, among other things, the supply of certain goods and technologies to Iran, access by Iranian banks to the European financial system and investments in certain sectors of the Iranian economy. The US Iran Sanctions Regulations (31 C.F.R. Part 560) go even further, imposing secondary sanctions on non-US persons and companies engaging in certain business activities connected to Iran. This creates a

<sup>3</sup> See also our GSK Update dated 11 February 2026 <https://gsk.de/en/the-new-transparency-international-corruption-perceptions-index-2025/>



regulatory dilemma for European companies, as the EU Blocking Regulation (Regulation (EC) No. 2271/96) prohibits EU companies from complying with US secondary sanctions. These conflicting regulations pose considerable challenges in transaction practice.

**Risks in the case of indirect ties to Iran.** Due diligence practice shows that it is rare for European companies to have direct business ties to Iran. The actual risks often lie in indirect relationships, such as with suppliers who source from Iran, end customers who re-export products to Iran, or business partners who appear on OFAC sanctions lists or are controlled by individuals on these lists. Uncovering these indirect relationships often requires a more in-depth examination than is typically provided in traditional legal due diligence.

**Implications under export control law.** Companies operating in sectors such as mechanical or chemical engineering, aerospace or IT must be subject to particularly thorough review. As the Iran crisis has progressed, the EU has repeatedly expanded the list of controlled goods and technologies. Geopolitical legal due diligence also covers the target company's internal compliance systems, such as internal compliance programmes (ICP) in accordance with the recommendations of the German Federal Office for Economic Affairs and Export Control or other precautions to avoid organisational culpability<sup>4</sup>.

**Oil price volatility and pricing power.** In addition to the sanctions and export control implications, the Iran crisis has a further, direct economic dimension in the form of its impact on global oil prices. Iran is one of the world's most important crude oil producers. Each tightening of sanctions, each blockade of the Strait of Hormuz and each military escalation in the Persian Gulf has caused oil prices to soar, and this trend is set to continue.

For target companies with energy-intensive business models in sectors such as chemical engineering, logistics, steel, plastics and transport, the key question in any geopolitical legal due diligence is to what extent increased

energy and raw material costs due to the crisis can be passed on to customers.

The due diligence should cover several levels:

The first step is to analyse whether any of the target company's key customer and supply contracts contain **price escalation clauses** that allow the company to pass on increased raw material and energy costs, either automatically or following negotiation with customers. In practice, there are various mechanisms for this, ranging from indexed **sliding-price clauses** which are linked to a reference price (e.g. Brent Crude or TTF gas price), to periodic **price review clauses** and unilateral price adjustment rights combined with a special right of termination for the customer. Pure **raw material cost clauses**, which are linked exclusively to the development of certain input prices, are also common practice in industrial contracts.

Another decisive factor is the **target company's market position**. Experience has shown that companies with a strong market position, a differentiated product range or long-term customer relationships are able to pass on cost increases more easily than companies operating in highly competitive markets with interchangeable products. This ability to pass on costs, also known as "**pricing power**", is a key factor in the valuation and sustainability of a company's business model under geopolitical stress. A target company whose margins shrink when oil prices rise because it cannot pass on cost increases to its customers, or can only do so with a considerable time lag, represents a significantly higher investment risk than a company with robust contractual price adjustment mechanisms.

Finally, it should also be verified whether the target company has **hedging strategies** in place to mitigate commodity price risks, at least temporarily (e.g. oil futures, swaps or long-term purchasing contracts with fixed price components). The absence of such hedging strategies, particularly if there are no contractual price adjustment mechanisms in place, can represent a significant earnings risk and must be reflected in the

<sup>4</sup> See Sections 30, 130 of the German Act on Regulatory Offences (OWiG)



company valuation and/or the purchase price mechanisms.

#### **Impact on valuation and purchase price mechanisms.**

The results of a geopolitical legal due diligence have a direct impact on the target company's valuation and the structuring of purchase price mechanisms. If sanction risks are identified during due diligence, this can lead to downward adjustments to the company's valuation or to the breakdown of negotiations. The implementation of an earn-out structure may also be motivated by political uncertainties and a lack of predictability. The same applies to the uncertainty surrounding the future development of energy costs and the extent to which any increases can be passed on to customers. If it is unclear whether the target company will be able to protect its margins under altered market conditions, an earn-out can cushion this uncertainty in the valuation. Including geopolitical events in MAC clauses can also help to allocate risks appropriately between signing and closing.

#### **Particular relevance for private equity investors.**

Geopolitical legal due diligence is particularly important for private equity investors with international LPs – especially from the USA, the UK or the Middle East. US-based LPs are directly subject to OFAC sanctions. This means that a portfolio company with links to Iran could pose both operational and fundraising-related risks. With institutional (co-)investors such as leading sovereign wealth funds, listed financial intermediaries and multilateral development banks becoming increasingly sensitive to ESG factors in their role as “lenders of last resort”, transparency about geopolitical risks during the investment process is essential. This is also relevant in the context of rising oil prices. Private equity investors who hold portfolio companies in energy-intensive sectors must recognise the pricing power of these companies as a key value driver – or value risk – and factor it into their investment decisions.

#### **4. Practical tips and recommendations for drafting contracts**

Similar to the dos and don'ts in our previous articles in the “Bridging the GAP” series, we provide specific recommendations for transaction practitioners below:

##### **Dos**

1. **Do consult sanctions experts at an early stage:** Geopolitical legal due diligence should not be left until the advanced DD process. Sanctions list screenings should be carried out in the pre-DD phase to identify any potential red flags, ideally with support from specialised compliance advisers.
2. **Do include geopolitical questions in the DD questionnaire:** The standard DD questionnaire should be amended to include specific questions on geopolitical aspects, for example: Are there direct or indirect business relationships with sanctioned countries? Are there any internal compliance systems in place? Have export control licences been granted? Have any violations been identified, or have any official enquiries been answered, in the past?
3. **Do include sanction-specific warranties and indemnities:** The list of warranties in the purchase agreement should include specific warranties on sanctions compliance – including assurances that there are no business relationships with sanctioned persons or entities and that the target company has a functioning compliance management system. In addition, specific indemnities should be agreed upon in the event that sanctions are subsequently found to have been breached.
4. **Do consider geopolitical aspects in MAC clauses:** In view of the current crisis, it should be examined whether the MAC clause explicitly covers geopolitical events, such as the imposition of new sanctions, the escalation of armed conflicts or the breakdown of trade relations. In an environment that is challenging for private equity/M&A transactions overall, MAC clauses can be a useful tool for reconciling the different interests of the contractual parties and allocating general risks



- appropriately. A MAC clause can also cover sudden rises in energy costs due to geopolitical escalations, provided it is worded broadly enough.
5. **Do agree on compliance covenants between signing and closing:** In the case of transactions involving a period between signing and closing, compliance covenants should be agreed that prohibit the target company from entering into any new business relationships with sanctioned persons or countries and require the immediate disclosure of any existing sanction-relevant business relationships.
  6. **Do check pricing power and mechanisms for passing on costs:** Geopolitical legal due diligence should include a systematic review of the target company's key customer and supply contracts to determine whether they contain price adjustment clauses that allow the company to pass on increased energy and raw material costs to its customers. The absence of such clauses should be taken into account when determining the purchase price. In addition, it is advisable to include warranties in the purchase agreement regarding the completeness and effectiveness of existing price adjustment mechanisms and hedging strategies.
  7. **Do check W&I insurance cover:** Warranty and indemnity (W&I) insurance policies generally exclude sanctions violations and their consequences from their scope of cover. In transactions without rights of recourse against the seller (non-recourse transactions), MAC clauses can therefore also be used to compensate for certain general W&I insurance exclusions, such as those relating to armed conflicts or nuclear and/or environmental disasters. Consulting with the W&I broker at an early stage regarding the scope of the sanctions-related exclusions is therefore essential.
2. **Don't consider individual sanctions regimes in isolation:** A review based solely on the EU sanctions lists does not provide a full picture. US secondary sanctions, UK sanctions and the sanctions regimes of other jurisdictions need to be examined cumulatively. The potential conflict between the EU Blocking Regulation and US secondary sanctions is a separate risk that must be addressed on a transaction-by-transaction basis.
  3. **Don't use generic warranties:** General compliance warranties (e.g. "The target company shall comply with all applicable laws") are insufficient when it comes to geopolitical risks. They lack the necessary specificity for effective risk allocation and provide no solid basis for effective enforcement.
  4. **Don't forget the fiscal and structural dimension:** Sanction-related reorganisations, such as withdrawal from certain markets or termination of business relationships, can also have significant tax implications.
  5. **Don't ignore oil price risks:** Against the backdrop of the Iran crisis, it is unrealistic to assume that energy prices will remain stable. Target companies without contractual price adjustment mechanisms or hedging strategies are particularly vulnerable to geopolitical cost pressures. This risk should not be overlooked in the valuation or when drafting the contracts.
  6. **Don't leave secondary sanction risks to the seller:** In situations where the target company falls under the buyer's operational management after closing, it must be ensured that the buyer's compliance obligations are also set out in the contracts – otherwise the buyer runs the risk of triggering sanction violations itself.

## Don'ts

1. **Don't underestimate the risk of sanctions:** Traditional due diligence often overlooks indirect ties to sanctioned persons or entities via supply chains, distributors or beneficial ownership.



## 5. Conclusion

The Iran crisis is a striking example of how geopolitical risks can extend beyond the remit of traditional legal due diligence. In an environment where political upheavals can lead to new sanctions packages, trade restrictions or regulatory intervention within days, dedicated geopolitical legal due diligence is not an optional extra, but a necessity for any diligent transaction adviser.

The results of a geopolitical due diligence have a direct impact on how a transaction is structured, from the determination of the purchase price and the formulation of earn-out and MAC clauses to insurance conditions under W&I policies and the target company's ability to pass on crisis-related cost increases to its customers, particularly in the energy sector.

Geopolitical legal due diligence is an increasingly indispensable tool in the transaction adviser's toolkit. This article aims to encourage a shift in perspective, moving away from viewing geopolitical risks as abstract background noise and towards integrating them systematically – i.e. at an early stage, on a regular basis and with a risk-based approach – into the due diligence process and drafting of contracts.

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## GSK M&A/Private Equity

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### Robert Korndörfer

Rechtsanwalt

Berlin

[robert.korndoerfer@gsk.de](mailto:robert.korndoerfer@gsk.de)

### Eric Mayer

Rechtsanwalt

Munich

[eric.mayer@gsk.de](mailto:eric.mayer@gsk.de)



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### GSK Stockmann

Rechtsanwälte Steuerberater Partnerschaftsgesellschaft mbB

#### BERLIN

Anton-Wilhelm-Amo-Str. 42  
10117 Berlin  
T +49 30 203907 - 0  
F +49 30 203907 - 44  
[berlin@gsk.de](mailto:berlin@gsk.de)

#### HEIDELBERG

Europaplatz 3  
69115 Heidelberg  
T +49 6221 4566 - 0  
F +49 6221 4566 - 44  
[heidelberg@gsk.de](mailto:heidelberg@gsk.de)

#### FRANKFURT/M.

Bockenheimer Landstr. 24  
60323 Frankfurt am Main  
T +49 69 710003 - 0  
F +49 69 710003 - 144  
[frankfurt@gsk.de](mailto:frankfurt@gsk.de)

#### MUNICH

Karl-Scharnagl-Ring 8  
80539 Munich  
T +49 89 288174 - 0  
F +49 89 288174 - 44  
[muenchen@gsk.de](mailto:muenchen@gsk.de)

#### HAMBURG

Neuer Wall 69  
20354 Hamburg  
T +49 40 369703-0  
F +49 40 369703-44  
[hamburg@gsk.de](mailto:hamburg@gsk.de)

---

#### LUXEMBOURG

GSK Stockmann SA  
44, Avenue John F. Kennedy  
L- 1855 Luxembourg  
T +352 271802 - 00  
F +352 271802 - 11  
[luxembourg@gsk-lux.com](mailto:luxembourg@gsk-lux.com)

---

#### LONDON

GSK Stockmann International  
Rechtsanwaltsgesellschaft mbH,  
London branch  
Queens House, 8-9 Queen Street  
London EC4N 1SP  
United Kingdom  
T +44 20 4512687-0  
[london@gsk-uk.com](mailto:london@gsk-uk.com)

Registered office: Munich  
Munich Local Court  
HRB 281930  
Managing directors:  
Dr. Mark Butt, York-Alexander  
von Massenbach