



Fiscal Regimes for Hydrocarbons Exploration and Production in Brazil

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ABSTRACT

The pre-salt oil province in Brazil was discovered in the Santos and Campos Sedimentary Basins in 2007, with reservoirs containing significant reserves of high quality oil and natural gas. Because of this occurrence, the Brazilian government began a discussion to adopt a new regulatory model for the new exploratory frontier, claiming the need to preserve the national interests in the exploitation of its energy resources. These incidents eventually led to the adoption of the Production Sharing Regime, which currently coexists with the Concession and Onerous Transfer of Rights models.

Under the given circumstances, this article seeks to present the current fiscal regimes for the exploration and production activities in Brazil, their particularities and scope of application, as well as to initiate a brief discussion on the advantages and disadvantages of the changes recently undertaken by the Brazilian government in its regulatory framework.

1. Introduction

It is commonly known that regulatory models and fiscal regimes adopted in different oil-producing countries strongly affect the attraction of domestic and foreign investments to the oil and natural gas industry. In different countries, there are several different forms of government participation paid by oil companies, as well as the definition of their respective collection aliquots.

Several regulation models in the oil and natural gas industry have been adopted in the various producing countries, some with just one tax regime while others are mixed, merging two or more tax regimes, always aimed at maximizing government revenues and the efficient appropriation of oil revenues.

Brazil has been a relevant oil producer since the 1990s and by the end of 2016, the country was the 15th largest country in terms of proved oil and reserves and also the 15th largest producing country in the world. With respect to natural gas, the country's respective global rankings are 34th and 35th (BP, 2017). More recently at the end of 2010, after the discovery of significant volumes of hydrocarbons in the subsoil of the Brazilian continental shelf, the federal government applied significant alterations to the regulatory model for hydrocarbon exploration and production activities. Thus, Brazil became a country with three different tax regimes for the oil and natural gas industry.

Under these circumstances, this article has the following objectives: to review the evolution of regulation in the oil and natural gas in Brazil during the last three decades, since the relaxation of the state monopoly in 1995, and presenting and commenting its current tax regimes.

2. Evolution of Exploration and Production Fiscal Regimes in Brazil

In 1998, the Petroleum Law reformed the Brazilian oil sector, establishing a new institutional and regulatory framework and determining, in addition, the relaxation of the state monopoly exercised by Petrobras (National Oil Company). This reform redefined the role of the State in the concession and promotion of oil and gas exploration and production activities, attracted significant foreign investments to the country and proved to be very well succeeded. Before that, several different tax regimes have taken place in Brazil, as shown in Table 1.

However, from 2007 onwards, twelve years after the relaxation of the state monopoly in Brazil, due to significant discoveries at the pre-salt layer, ANP, the government and industry stakeholders engaged in discussions to bring reforms and create a new regulatory framework that better reflected the exploration and production activities in these areas, with the purpose of ensuring the Brazilian State the appropriation of a higher percentage of the revenues obtained with the

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Table 1

Evolution of the Fiscal Regimes for Oil Exploration and Production Activities in Brazil. Source: As from Lucchesi (1998).

Period/Year	Fiscal Regime
1892 – 1896	First exploration activities took place in the City of Bofete, State of São Paulo by the farmer Eugênio Ferreira Camargo, who is considered the pioneer of oil research in Brazil.
Until 1938	Free initiative regime. Private enterprises, either domestic or foreign, could be freely applied to any petroleum activity in the country. Most of the foreign capital invested in the country came from companies set up following the breakup of Standard Oil and from Royal Dutch Shell.
1938 – Nationalization of all mineral wealth and other subsoil resources ^a	In accordance with federal law, all petroleum activities had to be mandatorily conducted by Brazilian companies and citizens.
1938 – Creation of CNP, marking a new phase of the petroleum history in Brazil	The Federal Government created the National Petroleum Council – CNP, whose main function was to evaluate the requests for oil deposits research. The decree that regulated CNP also stated that national fuel supply was a matter of public interest, and it further regulated the import, export, transportation, distribution and trading of oil fuel activities as well as the operation of the refining industry. Therefore, hydrocarbon deposits were considered as Union assets
1953 – Creation of Petrobras (NOC) and establishing of State monopoly over all exploration and production activities	The monopoly was to be exercised by the newly formed company and CNP, tasked with setting guidelines and monitoring the industry.
1963 – Expansion of the State monopoly	The State monopoly was expanded to cover import and export activities of oil and oil products.
1976 – Signature of the first Risk Agreements for Exploration and Production Activities	Petrobras and other Brazilian oil companies (Camargo Corrêa, Paulipetro, Azevedo Travassos and others) signed the first risk agreements for exploration and production activities with international companies (Exxon, Shell, Texaco, Total, Elf, Marathon, Conoco, Hispanoil, among others).
1988 – Promulgation of a New Federal Constitution	The Constitution of 1988 maintained State monopoly, the risk agreements were banned, with the exception of those whose operations that had already resulted in commercial discoveries.
1995 – Constitutional Amendment n° 9, relaxing the sector's monopoly grip exercised by Petrobras	The Amendment allowed the Union to contract private or public companies to undertake research, exploration, refining, import, export and transport activities of crude oil, natural gas and oil products from any origin.
1997 – The Constitutional Amendment n° 9 was ratified into Law n° 9478 on August 6 th 1997, known as the Petroleum Law and regulated by Presidential Decree n° 2455/98	The law regulated the execution of all activities listed above by private or public companies, and also asserted the fundamentals and objectives of the national energy policy, creating the National Council for Energy Policy – CNPE, the governmental organization responsible for setting policies for the country's energy sector. The law also created the National Agency of Petroleum, Natural Gas and Biofuels – ANP ^b , the federal institution responsible for the regulation and the monitoring of all activities in the oil and gas industry in Brazil.
1999 on – Zero Round and other Bidding Rounds for the concession of exploration blocks	Under the new institutional model, the Petroleum Law stated that the contracting of exploration and production activities would occur under a concession model, which must be preceded by bidding rounds promoted by ANP (Article 15, Paragraph 1, Decree n° 2455, 1997). ANP established which exploration areas would remain under Petrobras operation following through the Round regulation. By the end of 2015, ANP had promoted thirteen bidding rounds for the concession of exploration blocks.

^a Article 20 of the Federal Constitution determines that the Union owns the resources existing in the Brazilian subsoil. This article establishes that the Union will pass on part of the financial compensation arising from the production of oil and natural gas to the States and Municipalities. Federal Constitution, Art. 20. § 1 - The Federal, State and Municipalities, as well as to the organs of the direct administration of the Union, are assured, in accordance with the law, participation in the result of the exploration of oil or natural gas, of water resources for the generation of electric energy and other mineral resources in its territory, continental shelf, territorial sea or exclusive economic zone, or financial compensation for that exploration.

^b The ANP is a federal autarchy under a special regime related to the MME, but not subordinated to it. According to the law of its creation, it has administrative, financial and budgetary autonomy.

production of oil and natural gas.¹ These discussions resulted in the enactment of several federal laws specifically regulating the pre-salt province and distinct areas that could eventually be considered of strategic value for the Brazilian government.

3. Reserves and Petroleum Production in Brazil

By the end of 2016, the country had almost 13 billion barrels of proven oil reserves and natural gas reserves were equivalent to 637 billion cubic meters. Total natural gas production was almost 38 billion cubic meters (ANP, 2017). Figs. 1–3 and 4 show the evolution of oil and natural gas (onshore and offshore) total and proven national reserves,²

¹ Another reason was the need to develop an industrial policy, focusing on goods and services with high national content, however the discussion on this point is not part of the scope of this article.

² The reserves were evaluated in accordance with the criteria for the appropriation of

from 1997 to 2016, marking the evolution after the relaxation of the state monopoly.

Figs. 5 and 6 show the evolution of oil and natural gas production respectively, onshore and offshore, for the same period.

3.1. Hydrocarbons Production in the Pre Salt Fields

The increase in both oil production and natural gas production since 2013 has been a consequence of the start of production of pre-salt fields. The main reason for the growth in pre-salt production is the wells' high productivity, which is significantly higher than expected. In addition, the post-salt production from Campos Basin, the country's

(footnote continued)

reserves defined in the Technical Regulation contained in ANP Ordinance No. 09/2000 of the Superintendence of Development and Production, which establishes the guidelines for its estimation.

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