



Presenting:

**Use of a DA Process to Develop a Petroleum
Upstream Fiscal and Regulatory Regime
by Tony Kenck**

DAAG Conference 2003

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Use of a DA Process to Develop a Petroleum Upstream Fiscal and Regulatory Regime

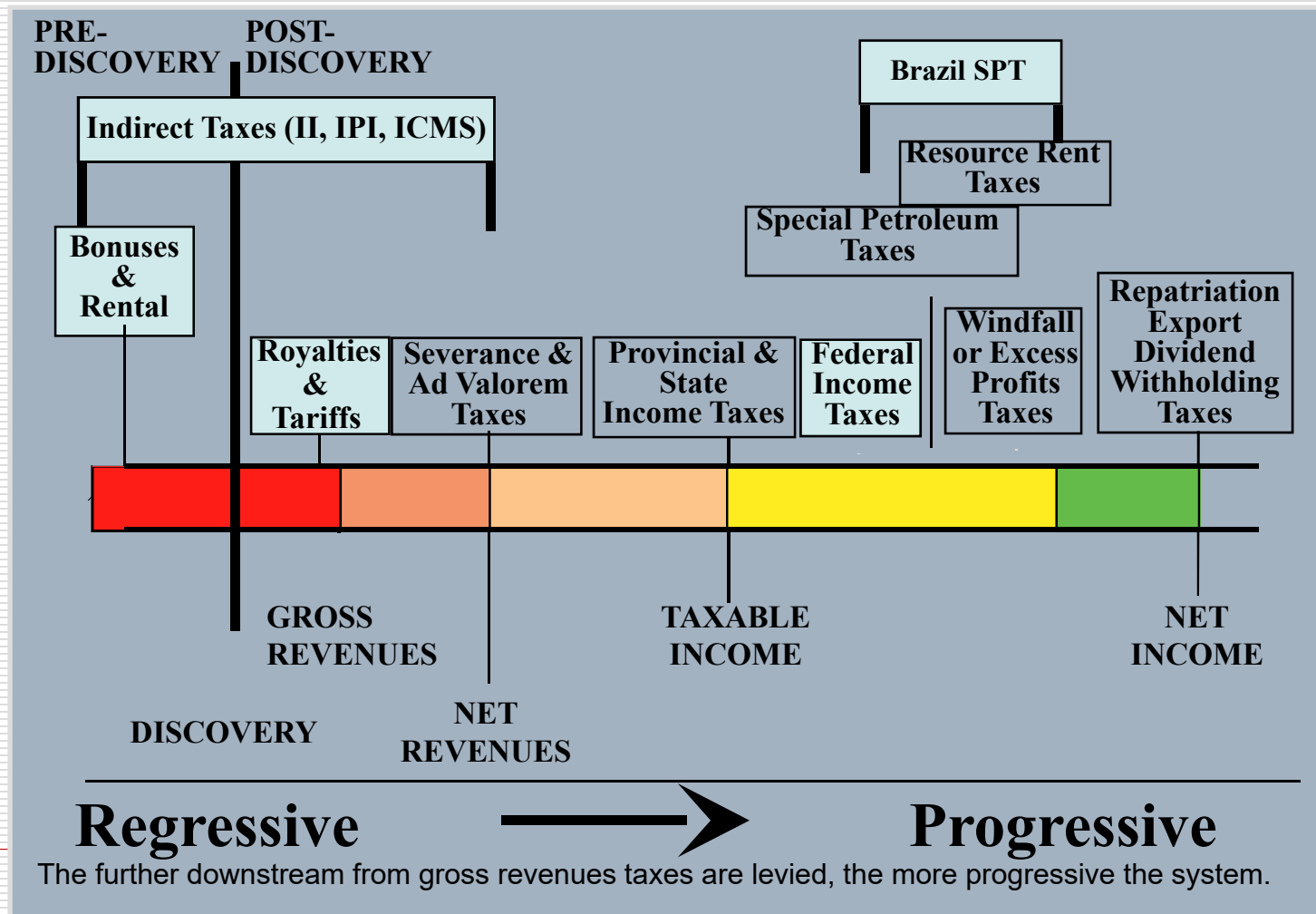
DA Process as a Model for
Government/Industry Collaboration

Tony Kenck
ChevronTexaco

How We Got To Where We Were

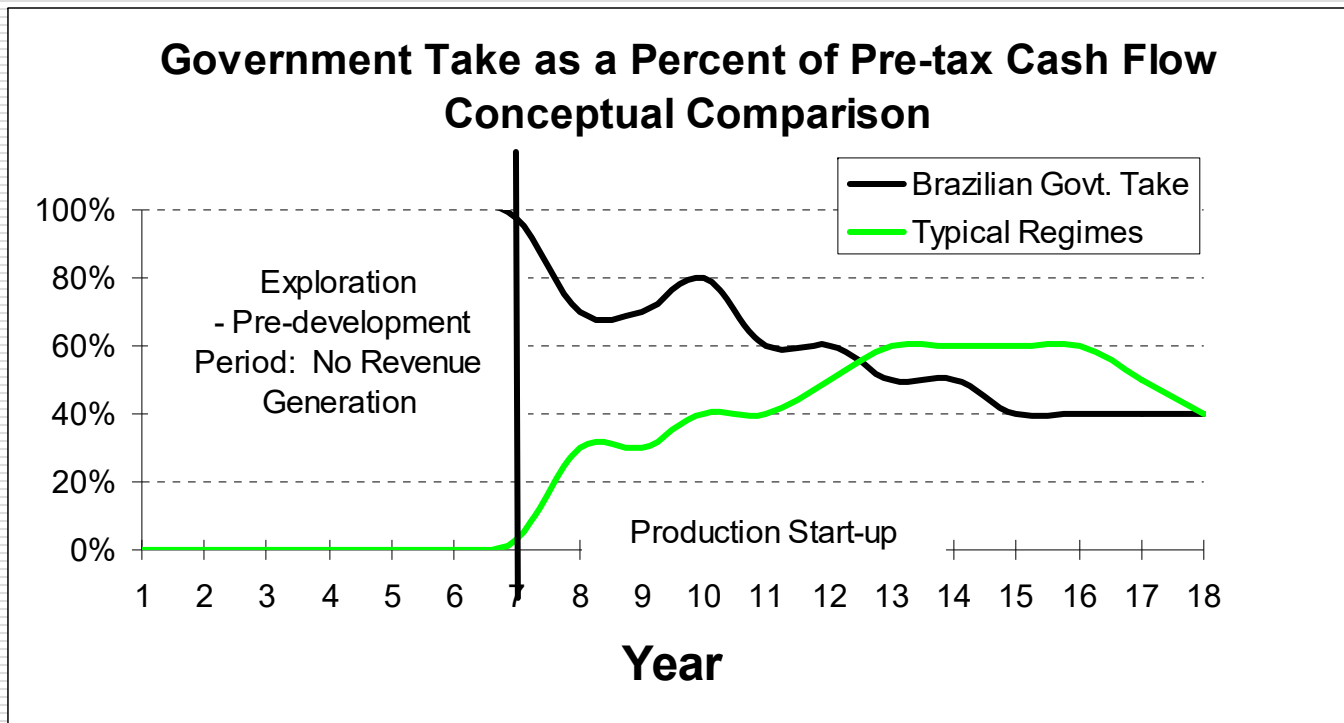
- ❑ Petrobras = State Oil Company
 - ❑ Brazil Flexibilization in 1996
 - ❑ Law established oil tax framework and ANP
 - Standard Royalty Tax plus...
 - ❑ “Indirect Taxes”
 - VAT plus import duties = 50%+ increase of capex
 - TAR
 - ❑ Regulations?
 - ❑ Not competitive, not economic
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Petroleum Tax Spectrum



Graphic adapted from [Petroleum Fiscal Systems and Production Sharing Contracts](#) by Daniel Johnston

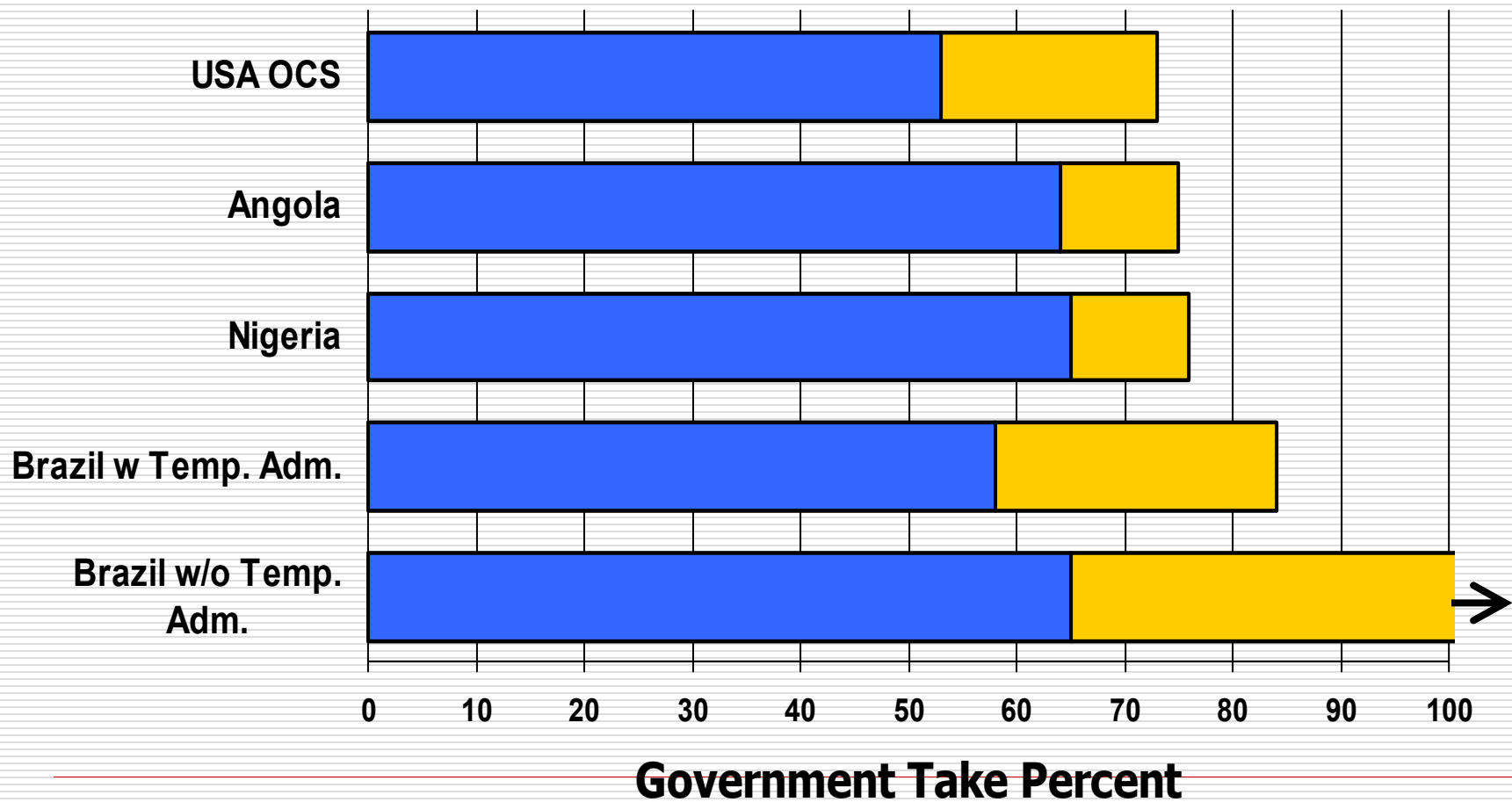
Conceptual Government Take Timing



Nominal And Real Government Take

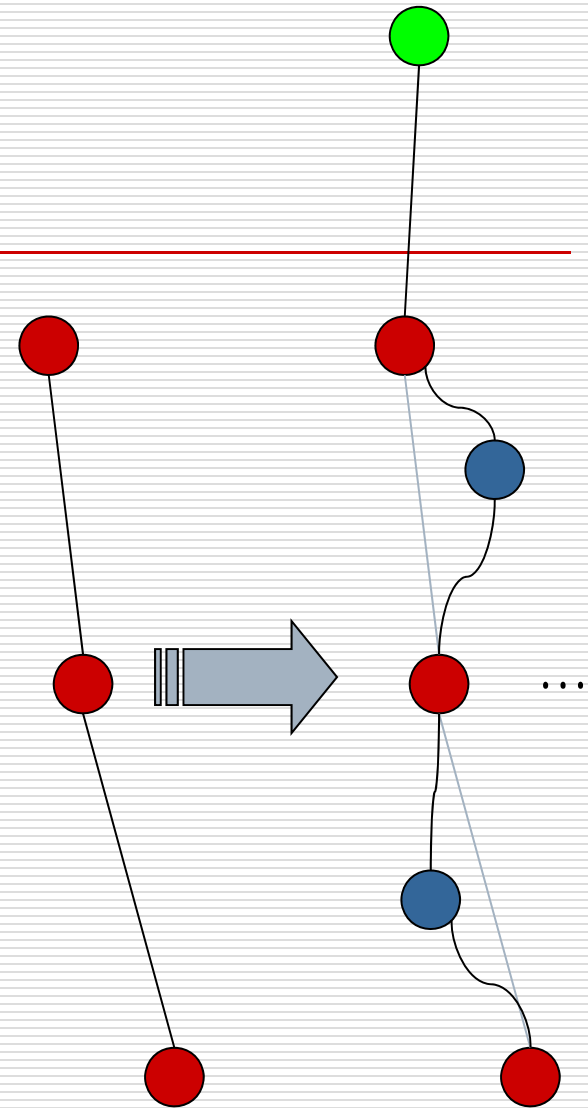
750 Million-barrel Oil Field, \$3.75/Bbl Development Cost, \$20/Bbl

Crude



Tax Legal Process

- Establish framework
- Layer in progressive details
- Scope (Frame) Issues



Industry Efforts

- Brazilian Institute of Petroleum (IBP)
 - Suggestions in 1997 to improve the fiscal terms within the framework
 - Then two studies
 - “Economist” Report
 - Macroeconomic study
 - Impact on petroleum specific terms and temporary import regime
 - Cultural challenges - Hofstede
-

Brazil Specific Issues

- ❑ Very deep water
 - ❑ Tendency to heavier crude oils
 - ❑ Perception that best areas are gone
 - ❑ Low exploration success rates
 - ❑ Perception of uncertainty/instability in fiscal regime
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Early 2000

- ❑ Bid round approaching
 - ❑ Temporary admissions expiration date was closing (relatively)
 - ❑ Brazilian businesses were flexing political muscle for increased local content
 - ❑ Time to take another run at a workable fiscal regime
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But...

- ❑ Oil Prices were high
 - ❑ The first few bid rounds had been declared successful
 - ❑ Less confrontational path, seeking to teach key people within ANP and IRS some of industry drivers
 - ❑ Blind alley after blind alley
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Finally...

- It became clear that there was little understanding by industry of the government drivers and vice versa
 - How to get the groups together?

 - I know... a framing session
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Purpose and Benefits

- Primary Purpose: To build a shared understanding of what a win-win-win fiscal regime looks like
 - Collateral Benefits
 - Networking
 - Education
 - Consensus/Trust
 - Understanding
-

Why now, why here?

- Early in the game—a chance to make a difference
 - Efforts in other countries are often confrontational
 - New approach
 - Recognize symbiotic relationship
 - Try to find solutions that benefit all parties
 - Set the global standard in arriving at a regime that works for all stakeholders
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What would it look like?

- ❑ What: Five Days
 - ❑ Who: Mid-level technically oriented people with influence. Federal, state, & local government, petroleum industry, local suppliers
 - ❑ Day one: Pre-meeting workshop—months before main workshop
 - ❑ Days 2 and 3 – presentation by interested groups
 - ❑ Days 4 and 5 – build frame, understand decision and risk interactions, map way forward
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What It Isn't

- ...not intended to be a rehashing of all the problems that petroleum companies have encountered in their Brazil efforts, nor is it meant to be a negotiation or formal crafting of policy. The meetings would be facilitated by disinterested professional facilitators who will ensure that discussion remains centered on the agreed upon agenda.
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Preliminary Agenda

Day One

- Petroleum industry basics
 - Geology
 - Development
 - Production
 - Downstream
 - Risk analysis
 - Economic analysis
 - Portfolio management
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Preliminary Agenda

□ Day Two

- Government Basics
 - Goal of Government in Brazil
 - Goals of Brazil's Petroleum Policy - Stewardship
 - Analytical methods used in arriving at policy decisions
 - Current Government Take Policy and Practice
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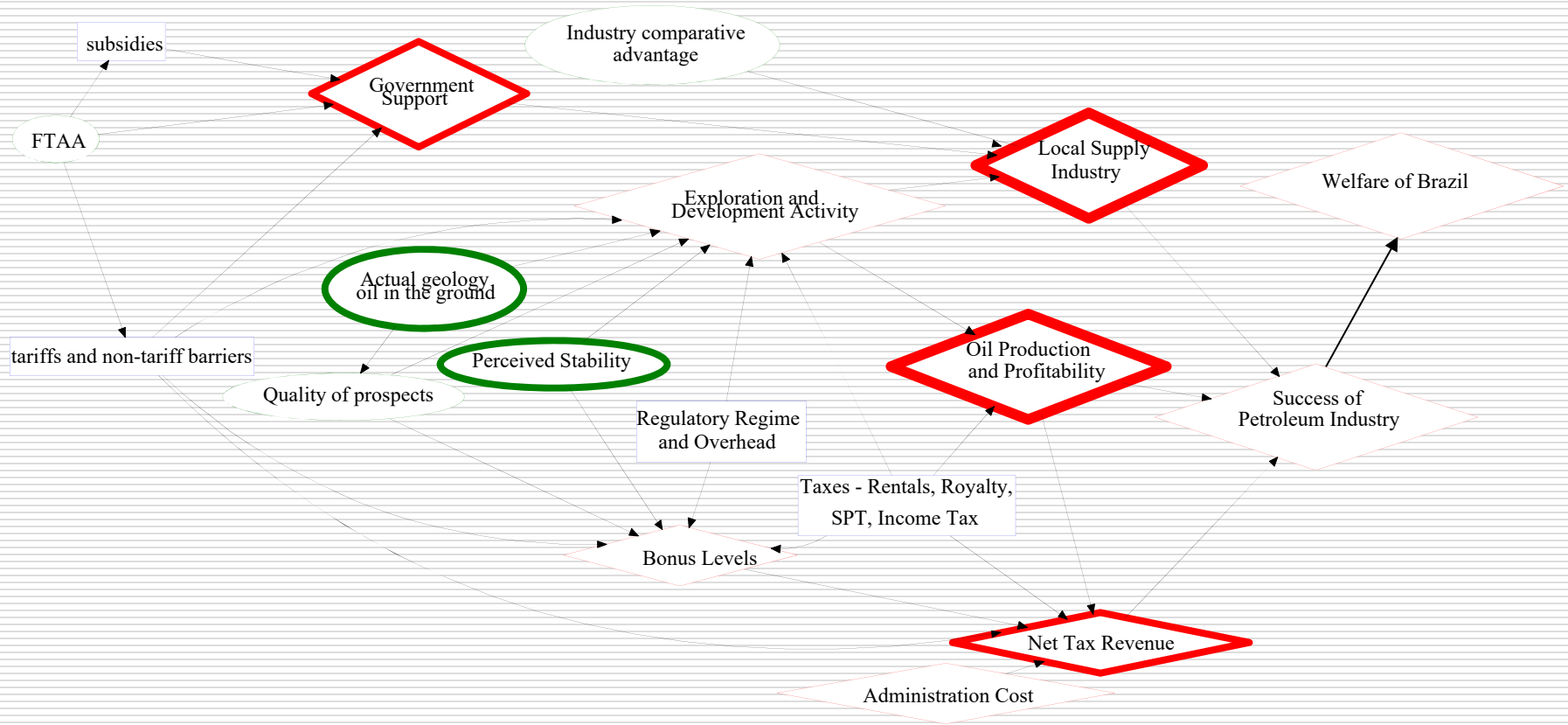
Preliminary Agenda

- Days Three and Four
 - Supply industry
 - International Macroeconomics
 - Decision Analysis Framework
 - Path Forward
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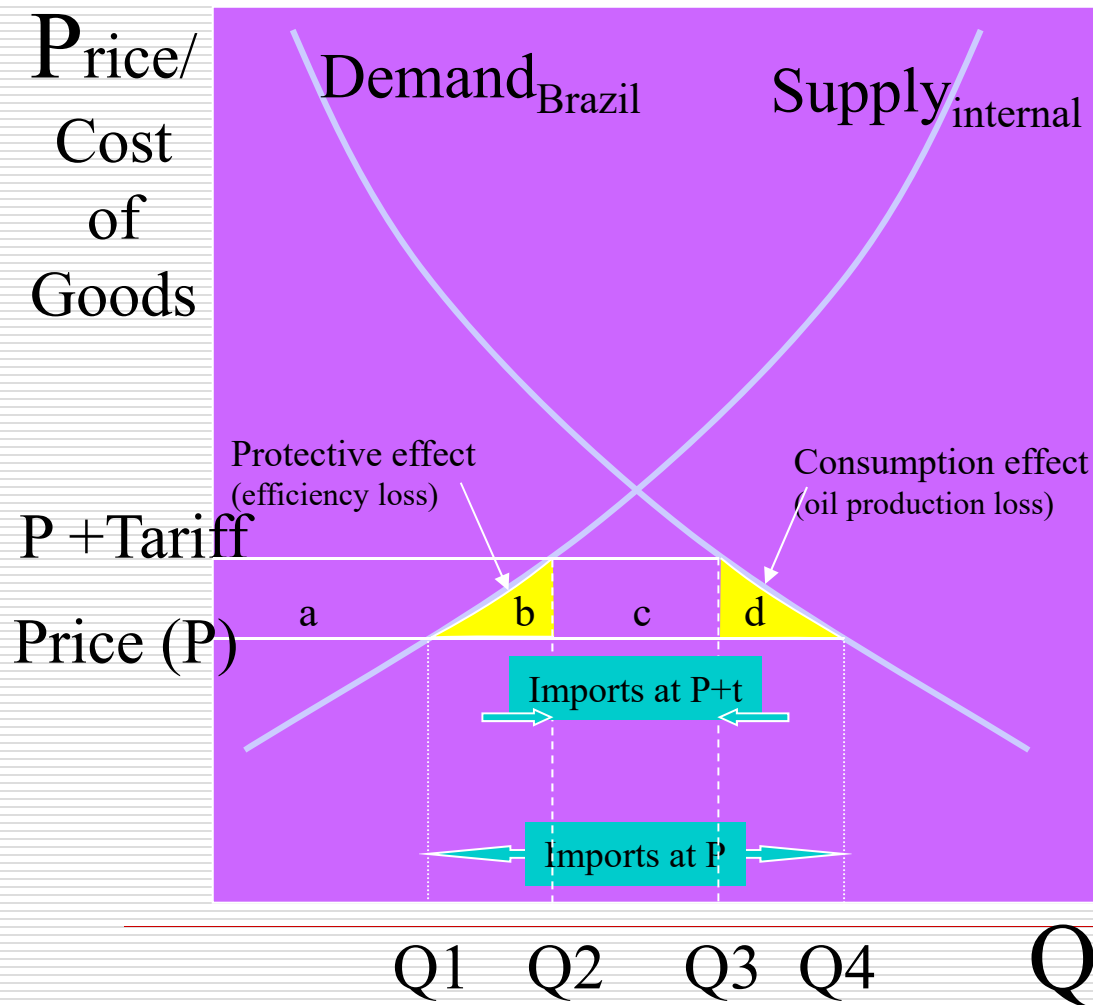
Vision

- ❑ The final two days would be spent building an influence diagram, discussing boundary conditions, mapping way forward
 - ❑ Future work would integrate the influence diagram and an established Brazil macroeconomic model to understand the range of outcomes
 - ❑ Build a communications package
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Example Influence Diagram



Macroeconomic Impact



Who wins and who loses

Consumer (oil cos.) loses - $(a+b+c+d)$

Local manufacturers gain a

Government gains c

Therefore, **Brazil** loses b and d.

Results

- ❑ Communication problems delayed the process
 - ❑ September 11
 - ❑ Merger and reprioritization
 - ❑ What has happened since?
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Key Learnings

- ❑ More time on the ground educating stakeholders on the process to make it more self-sustaining—bring in other companies in organizing efforts
 - ❑ Contact Brazilian DA experts early to give some local credibility to the effort (Informs database)
 - ❑ Would it have worked?
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Questions?

Abstract

Brazil opened its oil sector to international oil companies in the late 90s. The Brazilian tax system was not designed with the oil industry in mind, and was a labyrinth of fees, taxes, special interest representation, and fuzziness regarding division of tax authority between state, federal, and local government. The petroleum industry representative group, the IBP, tried to influence taxing authorities as the original law solidified into the actual regulations, and was somewhat successful. However, some huge hurdles remained, including potentially a 60% “investment tax.”

Through the IBP, we developed a process, based loosely on ChevronTexaco’s DA and business processes and proposed a joint industry-government workshop—essentially a framing session. Although the workshop never materialized, it was supported in several industry and government circles.

On the surface, this seemed like a useful approach to develop a joint understanding of the drivers of the involved parties, yet it never happened. What went wrong? Lessons learned include having a more permanent person on the ground trying to lay the groundwork as well as a stronger effort to educate the parties involved to facilitate progress with this approach.

Meeting Purpose

- To understand the points of view of the stakeholders of the Brazilian upstream, and to jointly build a model that demonstrates the impacts to Brazil of changes in the fiscal regime. The hope is that, with so many agencies having authority to impose taxes and regulations on the industry, decision makers would have access to a clear picture of the potential outcomes of their decisions. A successful outcome of this process would be the creation of a model that is used by decision makers to test potential consequences of proposed policy.
 - Collaboration and openness will be critical. The selected process will emphasize communication.
 - This effort is not intended to be a rehashing of all the problems that petroleum companies have encountered in their Brazil efforts, nor is it meant to be a negotiation or formal crafting of policy. The meetings would be facilitated by disinterested professional facilitators who will ensure that discussion remains centered on the agreed upon agenda.
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