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Energy: Oil & Gas

Brazil: Law & Practice

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Tauil & Chequer Advogados in association with
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Law and Practice

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1. General Structure of Petroleum Ownership and Regulation

1.1 System of Petroleum Ownership

The Brazilian Constitution of 1988 provides that the Federal Government has ownership over the petroleum and mineral resources located in the subsoil, in the continental shelf and in the exclusive economic zone (ZEE) [Arts. 20 and 176]. Also, pursuant to the Brazilian Constitution, oil and natural gas exploration and production activities, refining, the importation and exportation of by-products, maritime transportation of crude oil or by-products and pipeline transportation of petroleum and natural gas are activities under the monopoly of the Federal Government [Art. 177].

However, the Federal Government can contract with state-owned or private entities to conduct the petroleum activities referred to above, subject to certain conditions set forth in the applicable laws.

The economic reforms in the early 1990s brought about an exception to the Federal Government monopoly over petroleum activities. After several years of monopoly over petroleum activities (exclusive to *Petróleo Brasileiro S.A.* – Petrobras since 1953), the government authorities concluded that keeping the Federal Government's monopoly on the exploration and production of oil and natural gas could be an obstacle to the development of the petroleum industry.

Thus, aiming to provide legal mechanisms to attract both domestic and international private capital to Brazil, the Brazilian Congress enacted Constitutional Amendment No. 9/95, which amended the first paragraph of Art. 177 of the Brazilian Constitution and allowed petroleum activities to be contracted by the Federal Government with state-owned or private entities (subject to certain conditions set forth in the applicable laws).

In this context, Law No. 9,478/97 (the Petroleum Law) was enacted and, among other provisions, implemented the concession regime for the award of E&P rights by the Federal Government in Brazil. A few years later, following the discoveries of huge oil reserves in ultra-deepwaters of the pre-salt layer in the Campos and Santos basins announced by Petrobras in 2007 and several discussions within the Federal Government and Congress about the best way to exploit those resources, Law No. 12,351/2010 (the Pre-Salt Law) introduced the production sharing regime in Brazil, which is applicable to areas located within the pre-salt areas (within the limits of a defined pre-salt polygon) and other strategic areas.

In addition, in the face of massive investments that Petrobras was required to make in the oil and gas sector, Law No.

12,276/2010 introduced the so-called Transfer of Rights (ToR), which defined a special capitalisation of Petrobras at the time and gave Petrobras (upon consideration) the right to produce up to five billion BOE (barrels of oil equivalent) in certain pre-salt areas.

1.2 Regulatory Bodies

Petroleum activities are regulated by the following main governmental bodies:

- the Ministry of Mines and Energy – *Ministério de Minas e Energia*;
- the National Council of Energy Policy – *Conselho Nacional de Política Energética*; and
- the National Agency of Petroleum, Natural Gas and Biofuels – *Agência Nacional do Petróleo, Gás Natural e Biocombustíveis*.

The Ministry of Mines and Energy

The Ministry of Mines and Energy (MME – www.mme.gov.br) was originally created by Law No. 3,782/1960 and then later recreated by means of Law No. 8,422/1992, which governs its organisational structure. The MME's main activities are focused on political co-ordination and interaction with its related entities.

The MME promotes and supervises the implementation of public policies in the following sectors:

- geology, mineral and energy resources;
- hydraulic energy;
- mining and metallurgy; and
- oil, fuel and electricity, including nuclear energy.

The National Council of Energy Policy

The National Council of Energy Policy (CNPE – www.mme.gov.br/web/guest/conselhos-e-comites/cnpe) was created by the Petroleum Law. It is a joint ministerial entity, presided over by the Minister of Mines and Energy and formed by representatives of other Ministries and relevant entities, such as the Energy Research Office (EPE).

The CNPE is a consulting body and assists the President of Brazil with recommendations and proposals regarding policies and guidelines for the energy sector. In general, it is responsible for promoting rational use of the energy resources in Brazil and ensuring the proper supply of energy throughout the country.

The attributions of the CNPE have been amplified under recent regulations. One of the main changes in this regard was brought by the Pre-Salt Law, which provides that the CNPE is entitled to

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define the blocks to be offered in bid rounds for the exploration and production of oil and natural gas.

The National Agency of Petroleum, Natural Gas and Biofuels

The National Agency of Petroleum, Natural Gas and Biofuels (ANP – www.anp.gov.br) is the regulatory agency for petroleum activities. It is connected to the MME and is part of the indirect public administration.

The ANP was created by the Petroleum Law and has the authority to regulate, intervene and oversee petroleum activities, including the creation of infra-legal rules (eg, the ANP resolutions), the institution of administrative proceedings and the application of the relevant penalties, the issuance of authorisations to companies that carry out the relevant regulated activities, and the promotion and disclosure of geological and geophysical studies related to petroleum activities, including official statistics on the national reservoirs and production.

The ANP is also authorised to promote and organise bid rounds for the award of E&P rights, and to execute concession contracts on behalf of the Federal Government. It must be pointed out that the attribution to execute production sharing contracts was granted to the MME, as a representative of the Federal Government, in accordance with the Pre-Salt Law. The ANP executes the sharing contracts as the regulatory body responsible for supervising petroleum activities.

1.3 National Oil or Gas Company

Brazil also has two state-owned companies related to E&P activities: Petrobras (<http://www.petrobras.com.br/pt/>) and Empresa Brasileira de Administração de Petróleo e Gás Natural – Pré-Sal Petróleo S.A. (PPSA – <https://www.presalpetroleo.gov.br/ppsa/default.php>).

Petrobras was created in 1953 by Law No. 2,004/1953, following a heavily nationalist debate over the most appropriate policy for oil and natural gas E&P activities in Brazil. Petrobras played the monopoly role in the Brazilian petroleum sector until the opening of the market in the late 1990s.

Before the creation of the ANP, Petrobras used to have regulatory attributions, such as the award of risk contracts to private entities and the distribution of royalties, which allowed a more direct intervention of the Federal Government in the sector. However, Petrobras no longer plays a regulatory role.

PPSA is a state-owned company linked to the MME, whose creation was authorised by Law No. 12,304/2010 and Decree No. 8,063/2013. Its main purposes are the management of the production sharing contracts – to which it is a party without

assuming liabilities – and the management and marketing of the Federal Government's share of oil and natural gas. The company also represents the Federal Government in connection with unitisation matters in pre-salt areas.

1.4 Principal Petroleum Law(s) and Regulations

The regulatory framework for the petroleum sector in Brazil encompasses two main laws: the Petroleum Law and the Pre-Salt Law.

The Petroleum Law was a major milestone for the petroleum sector in Brazil and implemented the concession regime for the award of E&P rights by the Federal Government. In this context, the Petroleum Law created the ANP and the CNPE (and defined their authorities), outlined the relevant bidding rules and procedures to be observed in the Bid Round and the main provisions of the Concession Contracts, and provided for the government's policy objectives towards the rational use of the country's energy resources.

In its turn, the Pre-Salt Law established an additional contractual regime – the production sharing regime – to fields located within Brazil's pre-salt areas and other strategic areas.

Among other substantial provisions and rules applicable to the production sharing regime, the Pre-Salt Law also gave Petrobras preferential rights to choose the areas in which the company intends to operate, and the relevant participating interest (with a minimum 30% participating interest).

The ToR (despite the debates towards its classification as another legal-fiscal regime) has been also put in place exclusively for Petrobras to allow for its capitalisation, formalised by means of Law No. 12,276/2010, as further detailed in **6.3 Unique or Interesting Aspects of the Petroleum Industry**.

2. Private Investment in Petroleum: Upstream

2.1 Forms of Allowed Private Investment in Upstream Interests

Both the concession regime (governed by the Petroleum Law) and the production sharing regime (governed by the Pre-Salt Law) allow for the acquisition of E&P rights by any company that meets certain requirements, as established by the ANP.

Such acquisitions may be direct (through participation in the bid rounds promoted by the ANP) or indirect (through the acquisition of participating interests in a concession contract or production sharing contract previously granted in a bid round),

subject to the approval of the ANP or the MME (the latter for production sharing contracts).

The concession regime has been in effect since 1997, pursuant to the Petroleum Law. Under the concession regime, a concessionaire will carry out E&P activities at its own risk and expense. Access to the bid rounds is open to any company that meets the legal, technical and financial requirements established by the ANP. Operators must undergo a qualification process to operate onshore or offshore (shallow and/or deep waters), depending on their prior operating experience. The criteria used by the ANP to determine the winning bidders are based on a formula that considers the amount of signature bonus (80%) and the minimum exploratory programme (20%). Local content is no longer a bidding criterion.

The concession contract is entered into by the ANP and the concessionaires. In addition to the payment of a signature bonus offered during the bid round, the concession contract determines the payment of the following:

- a retention fee that is proportional to the size of the concession area retained;
- royalties;
- special participation; and
- the payment for occupation or retention of an area (in the case of onshore blocks).

For the areas located within the pre-salt polygon and others that are considered strategic, the CNPE decides whether a bid round will be held or whether Petrobras will be hired directly (in order to preserve the national interest and achieve other energy policy objectives), in accordance with the Pre-Salt Law. In both cases, contracts are executed under the production sharing regime. Bid rounds will also be conducted by the ANP.

Under the production sharing regime, a contractor will also carry out E&P activities at its own risk and expense. In the case of a commercial discovery, the contractor will have the right to be reimbursed for properly incurred E&P costs (cost oil), and will receive a percentage of the profits generated by the project (profit oil). The contractor's share of project profits will be defined in the production sharing contract.

The cost oil is the share of production costs that the contractor is entitled to recover (in the case of a commercial discovery) for costs it incurred and investments it made during exploration, appraisal, development, production and abandonment activities. The terms, conditions and limitations of the cost oil will be detailed in the production sharing contract.

The profit oil is the share of production profits to be divided between the Federal Government and the contractor, and represents the difference between the total volume of production and the share of cost oil and royalties.

In addition to royalty payments, the production sharing regime also establishes the payment of a signature bonus. Unlike the concession regime, the value of a signature will be determined in advance by the relevant production sharing contract – it will not, however, be among the criteria used to determine the winners of a bid round. Rather, the criteria used by the ANP to determine winning bidders during the production sharing regime's bid rounds will be based exclusively on the highest share of profit oil offered by the competing companies to the Federal Government.

In addition to the main regimes mentioned above, so-called "risk contracts" are worth mentioning – they are no longer issued in Brazil but are still in force, pursuant to the provisions of the Petroleum Law.

Back in the 1950s, when Petrobras had a monopoly on the exploration, production and refining of Petroleum in Brazil, it used to enter into services contracts with a "risk clause" for the performance of E&P activities by third parties on its behalf.

The services provider under the risk contracts performed all the relevant activities for the exploration, appraisal and development of the oil fields (technical services), and supported all the necessary investments for the execution of the referred E&P activities (financial services) on behalf of Petrobras. By executing and costing the relevant E&P activities at its own risk, the services provider would only profit from the oil field if there was commercial production.

2.2 Issuing Upstream Licences/Obtaining Petroleum Rights

In order to acquire E&P rights in Brazil, either directly or indirectly, the interested companies must undergo a qualification process before the ANP to demonstrate their legal, technical and financial capacity to be a concessionaire or a contractor, pursuant to the applicable procedures and requirements set forth by the ANP.

The applicable rules for a direct acquisition are outlined in the Petroleum Law or the Pre-Salt Law, and detailed in the tender protocols of each relevant bid round. In the case of an indirect acquisition, the requirements set forth in the tender protocol of the most recent bid round carried by ANP must be met.

In a nutshell, the tender protocols of bid rounds detail the relevant phases of the bidding procedures, such as registration/

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expression of interest, qualification (legal, technical and financial), the submission of bid bond guarantees, public sessions for the placement of offers (bids), the payment of a signature bonus and the award of the contract.

In the concession regime, only an initial registration phase will take place, and the qualification process of the winning bidders occurs after the bid (offer) public session. In the bid rounds under the production sharing regime, the qualification process must occur before the bid (offer) public session, meaning that only those companies duly qualified as operators or non-operators are eligible to participate in the bid and place their offers (individually or in consortium).

In addition to the registration (or the qualification, in the production sharing regime), potential bidders must also pay the participation fees for the areas of their interest – to acquire the data package containing technical information on the offered areas.

Bidders whose registration (or qualification, in the production sharing regime) is approved by the ANP are eligible to place bids in the public session, as long as they provide bid bond guarantees in such amount and form, and within such term, as defined in the tender protocol. The bid bonds may be provided in the following categories:

- letter of credit;
- performance bond; and
- escrow account deposit (in the concession regime).

The bids placed in a specific public session will be ranked and the winning bidder will be announced (in the same public session).

If the winning bidder either is not qualified (in the case of the concession regime) or fails to execute the relevant contract, the bid bond guarantees will be enforced, as applicable, and the penalties provided for in the tender protocol are applied. In this case, the remaining classified bidders will be called to express their interest to meet the amount of the bid placed by the previous winning bidder.

Winning bidders must proceed with the following main steps towards the execution of the relevant contract:

- submit the proof of payment of the signature bonus, in accordance with the tender protocol;
- provide the ANP with financial guarantees for the minimum exploratory programme within the term established in the tender protocol; and

- provide the ANP with the performance guarantee, if necessary (applicable for operators only, if its technical qualification was based on the experience of its economic group).

The bidding process ends upon the execution of the contracts.

The assignment of an E&P contract – fully or partially – is allowed under Art. 29 of the Petroleum Law and Art. 31 of the Pre-Salt Law, provided that the assignee fulfils the technical, financial and legal requirements set forth by the ANP in the relevant E&P contract and the rules set forth in the tender protocol. The ANP's prior approval is required before the assignment can actually be effective. For production sharing contracts, the ANP will issue a recommendation to the MME, which is the governmental body entitled to approve the assignment. Production sharing contracts also provide that, in any case of assignment by any contractor, the right of first refusal of the other contractors must be observed.

2.3 Typical Fiscal Terms Under Upstream Licences/Leases

The Petroleum Law and Decree No. 2,705/1998 set forth that the exploration, development and production of petroleum are subject to the payment of the following government takes:

- a signature bonus (please see **2.2 Issuing Upstream Licences/Obtaining Petroleum Rights**);
- royalties;
- special participation; and
- payment for occupation or retention of an area (in the case of onshore blocks).

Under the concession regime, the basic rate for royalties is 10%, but this can be reduced by up to 5% depending on geological risks, expected production, and other relevant factors. On 1 July 2020, the CNPE published Resolution No. 04/2020, requesting the ANP to evaluate the relevant measures that would reduce royalties by up to 5% for fields granted to small or medium-sized oil companies.

Under the production sharing regime, royalties are levied at a rate of 15%. In both cases, the royalties will be calculated on the value of the production of oil and natural gas.

The special participation only applies to fields with large production volumes under the concession regime. The special participation is calculated based on the net revenue of the quarterly production of each field, after the deductions allowed by paragraph 1 of Art. 50 of the Petroleum Law (royalties, exploration investments, operating costs, depreciation and taxes), and the rates range from 0% to 40%.

The amounts to be paid as occupancy or withholding of the area, also payable only under the concession regime, are calculated in Brazilian Reals per km². They must be paid and adjusted annually, as of the date of execution of the concession contract.

2.4 Income or Profits Tax Regime Applicable to Upstream Operations

In addition to the government takes detailed in **2.3 Typical Fiscal Terms Under Upstream Licences/Leases**, companies engaged in the petroleum industry are also subject to the payment of Federal, State and Municipal taxes levied on different situations.

Brazilian companies are subject to corporate income taxes (IRPJ and CSLL) on their worldwide income. IRPJ is levied at a rate of 15%, with a surtax of 10% levied on the taxable income exceeding BRL240,000 a year, while CSLL is levied at a rate of 9%.

Brazilian companies may elect to pay IRPJ and CSLL on a deemed income determined by a percentage of gross revenues (Presumed Profit Methodology) or on their actual income adjusted by add-backs and exclusions determined by tax legislation (Actual Profit Methodology).

Brazilian companies engaged in the petroleum industry usually elect the Actual Profit Methodology because it is the method that allows losses to be carried forward indefinitely and to offset up to 30% of the taxable income of subsequent tax periods, and because it is mandatory for companies whose gross revenues in the previous calendar year exceed BRL78 million.

In addition to the taxes levied on income, revenues earned by Brazilian companies are subject to PIS/COFINS at a combined rate of either 3.65% for companies under the cumulative regime, or 9.25% for companies under the non-cumulative regime. The latter regime is mandatory for companies under the Actual Profit Methodology and allows the calculation of non-cumulative credits for certain inputs to be offset against PIS/COFINS amounts otherwise payable.

While dividends are exempt from income taxes, payments of other income, capital gains and earnings to beneficiaries domiciled overseas are subject to Withholding Income Tax (WHT) at rates ranging from 0% to 25%. The remittance of fees for the charter of FPSO and other vessels used in E&P activities may be subject to a 0% tax rate if certain requirements are met. Except for dividends, payments made to beneficiaries domiciled in tax haven jurisdictions are subject to WHT at a rate of 25%, regardless of their nature.

It should be noted that tax reforms are under discussion in the Brazilian Congress that could include a resumption of taxation on dividends.

Brazilian companies are also subject to taxes levied on the importation of services (WHT, PIS/COFINS-Importation, CIDE and ISS) and goods (II, IPI, PIS/COFINS-Importation, ICMS and AFRMM).

The importation of goods may benefit from Repetro-Sped, which is a new special tax and customs regime applicable to the importation of goods used in E&P activities. It is valid until 2040 and encompasses different regimes that may result in the suspension, proportional payment or exemption of federal taxes levied on the temporary or definitive importation of those goods.

Repetro-Sped also encompasses the so-called Repetro-Industrialização regime, which allows both the importation and the local acquisition of raw materials, intermediate products and packaging materials for the manufacturing of products to be used in E&P activities, with the suspension of federal taxes.

Although the State VAT tax (ICMS) is not regulated by Repetro-Sped legislation, ICMS Agreement No. 03/2018 grants a tax rate reduction to 3% for goods imported under Repetro-Sped on a definitive basis and the exemption of ICMS for goods imported on a temporary basis.

2.5 National Oil or Gas Companies

The most relevant national oil company with an operational role in Brazil is Petrobras, which is still responsible for the majority of petroleum produced in the country.

Petrobras played a monopoly role in the Brazilian oil sector until the industry was opened to other companies – including private foreign companies – in the late 1990s, as a result of Constitutional Amendment No. 09/1995 and the enactment of the Petroleum Law.

Since the opening of the market, Petrobras has been carrying out the economic activities related to its corporate purpose in free competition with other companies, in line with market conditions and other principles and guidelines set forth in the Petroleum Law – and also pursuant to Section 1 of Art. 3 of Petrobras' By-Laws.

Over the 23 years since the enactment of the Petroleum Law, Petrobras has been given no special rights in connection with E&P contract awards. However, the Pre-Salt Law gave Petrobras certain preferential rights to choose the areas in which it intends

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to operate, and the relevant participating interest (with a minimum 30% participating interest).

Decree No. 9,041/2017 further regulated the “preferential right” concept and provides that, counted from the publication of the CNPE resolution that sets forth technical and economic guidelines of the blocks to be offered/contracted under the production sharing regime, Petrobras will have 30 days to express its interest to participate as an operator, and to indicate the relevant blocks and the intended participating interest, which cannot be lower than 30%.

After Petrobras’ expression of interest, the CNPE presents to the President of the Republic the potential blocks to be operated by the company, indicating its minimum participation in the consortium (between a minimum of 30% and that indicated by Petrobras).

According to Decree No. 9,041/2017, if Petrobras opts not to exercise its preferential right, the blocks will be offered in the bid round, and Petrobras may participate on equal terms and conditions with the other bidding companies.

Furthermore, for Petrobras’ areas of interest, Decree No. 9,041/2017 benefits the company with a “pull out option”, allowing Petrobras to refuse to enter into a production sharing contract with another company or consortium declared as the winner of the bid round. The “pull out option” only applies in cases where the Federal Government’s profit oil percentage offered by another consortium is higher than the minimum percentage established in the tender protocol. In such cases, however, if the Federal Government’s profit oil offered by another consortium (winner) is equal to the minimum established in the tender protocol, Petrobras will be part of the consortium, jointly with the winning bidder.

It must be pointed out that, in the cases where Petrobras is not integrated into the consortium, the winning bidder must appoint the operator and the participating interest of each party to the consortium, as a necessary condition for the approval of the bidding results by the ANP.

2.6 Local Content Requirements Applicable to Upstream Operations

Local content requirements in Brazil correspond to a contractual obligation arising from the concession contract or the production sharing contract, which may vary in accordance with the tender protocol and the applicable rules of each bid round.

Compliance with local content requirements must be evidenced by the contractor or concessionaire through the submission of local content certificates to the ANP, which will run an audit

process in this regard. The certificates are issued by third-party certifying entities that are accredited by the ANP.

Upon assessment of the certificates, if the ANP verifies that the concessionaire or contractor has not complied with the relevant local content requirements, a penalty may apply, corresponding to the difference between the percentage achieved and the percentage actually committed to.

Historically, local content obligations have been encompassed in E&P contracts in Brazil ever since the first bid round under the concession regime, as they were originally bid criteria. However, at the beginning of 2017, the Federal Government started to implement several regulatory changes in the petroleum industry, including the removal of local content from the applicable bid criteria by means of CNPE Resolution No. 07/2017.

Moreover, in order to improve the attractiveness of the bid rounds, CNPE Resolution No. 07/2017 also reduced the minimum percentages of local content requirements (which were historically high) to be complied with by the concessionaire or contractor of offshore blocks, to the following:

- 18% in the exploration phase; and
- 25% (well construction), 40% (offloading systems) and 25% (offshore production rigs) in the production development phase.

As for onshore blocks, the CNPE established a global commitment of 50% in the exploration phase and 50% in the development phase.

This adjustment represented a significant reduction (50% on average) on local content requirements for the upcoming bid rounds at the time – it eventually contributed to the organization of General Bid Rounds 14-16 (under the concession regime), and the Pre-Salt Bid Rounds 2-6 under the production sharing regime, all of which were held in 2017-2019.

In 2018, further improvements were made under ANP Resolution No. 726/2018, which regulated the amendments to the local content clauses of concession contracts executed until and including the 13th Bid Round, and also established rules regarding exemptions (waivers), adjustments of percentage and transfers of local content excess regarding the concession contracts from the 7th to the 13th Bid Rounds.

2.7 Requirements for a Licence/Lease-Holder to Proceed to Development and Production

Please see 2.8 Other Key Terms of Each Type of Upstream Licence for a comprehensive analysis of the key terms of con-

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cession and production sharing contracts in Brazil, including the requirements to proceed to development and production.

2.8 Other Key Terms of Each Type of Upstream

Licence

E&P Phases

Concession and production sharing contracts in Brazil typically provide for two distinct phases:

- the exploration phase, which also comprises the appraisal of a discovery, if any; and
- the production phase.

During the exploration phase, concessionaires/contractors are obliged to perform all activities contemplated by the minimum exploratory programme, including conducting seismic works and drilling wells.

Concessionaires/contractors must provide the ANP with financial guarantees for the minimum exploratory programme within the term established in the tender protocol.

Failure to comply with the minimum exploration programme at the end of the exploration phase may result in the lawful termination of the contract, without prejudice to the enforcement of the financial guarantees for exploration activities and the application of penalties.

After performance of the minimum exploration programme and within the expected term for the exploration phase, concessionaires/contractors may do the following, after providing written notice to the ANP:

- propose a discovery appraisal plan and relinquish the remaining area;
- inform the ANP about the commercial feasibility of the discovery (declaration of commerciality), initiating the production phase;
- retain the areas in which postponement of the declaration of commerciality is applicable; or
- fully relinquish the concession area.

The ANP must be informed of any discovery of oil and/or natural gas in the concession area within 72 hours. If the company decides to proceed with the appraisal of a discovery, it must submit a discovery appraisal plan for the approval of the ANP.

Upon compliance with the discovery appraisal plan approved by the ANP, concessionaires/contractors may, at their sole discretion, submit the declaration of commerciality of the field, along with the final discovery appraisal report. Within 180 days of receiving a communication on the approval of the final dis-

covery appraisal report, concessionaires/contractors must also submit the development plan to the ANP, describing in detail the activities and investments to be made in its entire life cycle.

The production phase usually lasts up to 27 years for concession contracts, counted from the submission of the declaration of commerciality. A total contractual term of 35 years will apply for production sharing contracts.

The field must be relinquished to the ANP at the end of the production phase, in compliance with the applicable laws and regulations and the best practices of the oil industry.

Liability

Concessionaires/contractors may carry out oil and gas E&P activities either individually or through a consortium with other companies. Under a consortium agreement, a leader company must be appointed to be the operator. The other consortium members will be jointly and severally liable before the ANP and the Federal Government for the obligations undertaken under the relevant contracts.

Decommissioning and Abandonment

It is worth mentioning that concessionaires/contractors must also provide a decommissioning and abandonment guarantee as of the production start date, in an amount corresponding to the expected cost for the decommissioning and abandonment of the facilities in place. This guarantee may be issued in the form of a performance bond, a letter of credit, a provisioning fund, or other types of guarantees, at the ANP's discretion.

The amount of the decommissioning and abandonment guarantee for a development area or field must be reviewed at the request of the concessionaires/contractors or the ANP if there are any events that alter the cost of the abandonment and decommissioning of the relevant operations.

Entitlement, Domestic Supply Requirements and Export Rights

Concessionaires and contractors are entitled to sell or dispose of the petroleum produced. As a rule, concession contracts and production sharing contracts do not provide for restrictions on export rights.

However, the contracts provide for an exception in cases where the domestic supply of oil, natural gas or their by-products is put at risk (an "emergency situation"), in which case the ANP may determine that the concessionaire/contractor must limit its exports of petroleum. An emergency situation must be declared by the President of the Republic.

Termination Events

Concession and production sharing contracts provide for several termination events, which are divided into three categories:

- lawful termination;
- bilateral termination (upon mutual agreement between the parties, without prejudice to the performance of the obligations thereunder) and unilateral termination (at any time during the production phase, giving the ANP at least 180 days prior notice); and
- termination for default (failure of concessionaire/contractor to perform the contractual obligations within the term established by the ANP, or the occurrence of a judicial or extrajudicial reorganisation, if not evidenced to the ANP concessionaire/contractor's economic and financial capacity to fully meet all contractual and regulatory obligations).

In a lawful termination, the events will apply at the following points in time:

- at the end of the contractual term;
- upon completion of the exploration phase without performance of the minimum exploration programme;
- at the end of the exploration phase, if there has been no commercial discovery;
- if the concessionaire/contractor fully relinquishes the concession/contract area;
- if the concessionaire/contractor exercises its right to withdraw during the exploration phase;
- upon failure to deliver the development plan within the term established by the ANP;
- upon non-approval by the ANP of the development plan;
- upon refusal of the consortium members to execute, in whole or in part, the production unitisation agreement after the ANP's decision in this regard; or
- upon adjudication of bankruptcy or non-approval of any concessionaire/contractor's request for judicial reorganisation by the court.

Under any of the termination events set forth above, the concessionaire/contractor will not be entitled to any reimbursement. Upon termination, the concessionaire/contractor will be liable for losses and damages arising from their default and termination, paying all applicable indemnifications and compensations, as provided by the Brazilian law and the relevant contracts.

Dispute Resolution

Both the concession contract and the production sharing contract provide for arbitration as the main dispute resolution method, in accordance with the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL). The city of Rio de Janeiro, Brazil, will be the seat

of the arbitration and the place where the arbitration award is rendered.

On the merits, arbitrators will decide based on the Brazilian laws, and the arbitration proceeding will be in Portuguese. It is worth noting that there are already disputes in place against the ANP, which were based on the arbitration clause of the relevant contracts.

2.9 Requirements for Transfers of Interest in Upstream Licences

Both the Petroleum Law and the Pre-Salt Law allow for the assignment – in whole or in part – of the concession contracts and production sharing contracts, as long as the assignee (new concessionaire/contractor) meets the technical, economical and legal requirements set forth by the ANP in the relevant E&P contract and the rules set forth in the tender protocol (summarised in an Assignment Proceeding Manual published on the website). The ANP's prior and express approval (or recommendation for the approval of the MME, for production sharing contracts) is required before the assignment can actually be effective.

The assignment may materialise as an actual/direct assignment of participating interest from a concessionaire/contractor to another or, indirectly, by means of a corporate transaction. Thus, a change in control or a merger, amalgamation or other corporate transaction may trigger a need for the concessionaire/contractor to request the ANP's approval.

The assignment process is initiated upon the request of the assignor (concessionaires/contractors) by means of an application (filing) to be submitted to the ANP.

Upon the issuance of the technical opinions of the ANP's internal bodies and the opinion of the partnership proposal evaluating committee (CAPP), as well as the recommendation of the Attorney-General's Office of the Agency, the request will be submitted for the approval of the ANP's Board of Directors. The decision of the ANP's Board of Directors is issued by means of a Board Resolution, which will be published on the ANP's website and in the Official Gazette. For production sharing contracts, the ANP will issue a recommendation to the MME on the approval of the assignment.

Production sharing contracts also provide that, in any case of an assignment, the other contractors must be given the right of first refusal.

In addition to the ANP's approval, the transaction may also be subject to the approval of the Brazilian Antitrust Authority (CADE), if the gross revenues of the parties involved in the

transaction (and the relevant economic groups) meet certain thresholds established in Art. 88 of Law 12,529/2011, updated by Interministerial Ordinance No. 994/2012. The documentation to be submitted to the ANP in the context of the assignment process includes evidence of CADE's approval or a statement indicating that the transaction is not subject to CADE's approval.

ANP Resolution No. 785/2019, regarding the assignment of rights, consolidates the procedures towards the assignment of E&P contracts (previously established in several different documents) and improves the legal certainty of the related mechanisms. It provides that the assignment of rights will be effective as of the execution date of the amendment to the concession contract, which must take place within 30 days of the notification of the ANP's decision approving the assignment. The Resolution also allows the parties to choose a different date for such purposes, which must be after the execution date of the amendment to the E&P contract and within 60 days of the publication of the ANP's decision approving the assignment.

2.10 Legal or Regulatory Restrictions on Production Rates

There are no specific legal or regulatory restrictions on production rates.

3. Private Investment in Petroleum: Midstream/Downstream

3.1 Forms of Allowed Private Investment in Midstream/Downstream Operations

Petrobras still has a major role in the midstream/downstream sector, although such role has been reduced over the past few years as a result of actions taken by both the antitrust authorities and the Federal Government, which took substantive actions to reduce Petrobras's role and create a competitive regulatory framework for local midstream and downstream markets. As a result of those actions, Petrobras has undertaken a major asset divestment programme involving its midstream and downstream assets, and its de facto monopoly position in the refining business and its quasi de facto monopoly position in the pipeline transportation business have been diminished. In short, the applicable legislation does not restrict private investments nor create a statutory monopoly on refining, pipelines, transportation or the distribution and retail of fuels or lubricants.

However, private investors interested in carrying out midstream/downstream activities in Brazil must be authorised by or registered with the ANP. The nature of and requirements to seek those authorisations or registrations depend on the spe-

cific activity to be pursued, and must follow the existing public regulations issued by the ANP.

In the course of granting those authorisations or registrations, the ANP as a public body must limit itself to verifying fulfilment of the requirements set out in the existing legislation and regulation.

3.2 Rights and Terms of Access to Any Downstream Operation Run by a National Monopoly

There are no legal national monopolies in Brazil in relation to downstream operations. As noted in **3.1 Forms of Allowed Private Investment in Midstream/Downstream Operations**, Petrobras still holds a de facto monopoly position in the refining business.

However, those dominant market positions are currently under review by CADE and, as a result, in June 2019 and July 2019 Petrobras and CADE entered into agreements for the cessation of practices (TCCs), whereby Petrobras agreed to divest approximately 40% of its refining capacity in Brazil and to completely exit from gas pipeline transportation and gas distribution activities in Brazil. The planned outcome for those TCCs is in accordance with the Federal Government policies for the opening of the midstream and refining sectors in Brazil set by the CNPE in April 2019.

3.3 Issuing Downstream Licences

All licences for downstream activities must be granted by the ANP in the form of an authorisation to be issued by the ANP or a registration with the ANP.

Refining activities, including construction, the expansion of capacity and the operation of refineries, are subject to prior and express authorisation from the ANP, which is granted in a two-stage process:

- construction authorisation (construction, modification or expansion of capacity); and
- operation authorisation.

Companies that are interested in applying for refining-related authorisations must comply with the requirements of ANP Resolution No. 16/2010 (as amended by ANP Resolution No. 48/2014), ANP Technical Regulation No. 1/2010 and relevant attachments. The applicant must be a company existing and incorporated in Brazil.

Upon completion of the works relating to the construction authorisation, the applicant shall formally request the ANP to inspect the facilities. To obtain the authorisations, the company

must submit the relevant environmental licences, a specific fire safety certificate, and proof of ownership of the facilities or a lease agreement for a minimum period of five years to the ANP, among other documents and information.

The authorised refiner can only market refined products with distributors that are authorised to operate by the ANP. Such distributors shall exclusively market the refined products with retail carriers (TRR) and retailers of automotive fuels, liquefied petroleum gas (LPG) and aviation fuels.

Similar to refining activities, distribution is also subject to prior authorisation by the ANP following a process of staged application and the filing of documents as specified by ANP Resolution No. 58/2014.

Only companies that are incorporated in Brazil and whose business purpose is the distribution of fuels may be authorised by the ANP. Such companies must also have a minimum paid-in capital of BRL4.5 million (updated periodically by the ANP) and storage capacity of 750 m³ requirements.

The applicant must also own at least one storage facility or a participating interest percentage in “pooled” facilities that meet the minimum storage capacity.

It is important to highlight that the applicable law also establishes that the distributor’s share capital cannot be owned by the following entities:

- individuals/companies who have been shareholders or officers of companies that have negative credit records with the tax authorities (CADIN);
- companies that have had any ANP authorisation to operate in the market revoked in the past five years; or
- companies authorised by the ANP to operate as retailers (transport retailers and service stations).

Lastly, the retail sale of automotive fuels may only be exercised by companies incorporated in Brazil that are authorised by the ANP to sell automotive fuels, and that comply with the provisions set forth in ANP Resolution No. 41/2013.

Restrictions on the ownership of the retailer’s share capital apply to the following entities:

- individuals/companies who have been shareholders or officers of companies that have negative credit records with CADIN;
- companies that have had any ANP authorisation to operate in the market revoked in the past five years; and

- companies that are authorised by the ANP to operate as distributors of liquid fuels (prohibition of vertical integration).

In April 2019, the ANP issued ANP Resolution No. 784/2019, establishing new rules regarding the authorisation for operations of storage facilities of automotive liquid fuels, aviation fuels, solvents, basic and finished lubricant oils, LPG, fuel oil, illuminating kerosene and asphalts.

Such authorisation may only be granted to distributors, TRR, producers of finished lubricant oil, collectors of used or contaminated lubricant oil, and re-refiners of used or contaminated lubricant oil.

To obtain an operation authorisation for storage activities, the interested company must file certain documents listed in ANP Resolution No. 784/2019 before the ANP, per facility, such as:

- a request for operation authorisation signed by a legal representative with evidence of powers and identification;
- an operation licence issued by the relevant environmental authority; and
- evidence of possession of the area where the facilities are located, among other documents.

3.4 Typical Fiscal Terms and Commercial Arrangements for Midstream/Downstream Operations

Unlike upstream activities, midstream/downstream operations in Brazil are not granted or awarded by the Federal Government to a private investor. Any private investor that is eligible and capable of complying with the existing requirements may apply for an authorisation or registration with the ANP. Said application has no costs attached to it, and if it is accepted by the ANP, the applicant is not required to submit to any specific fiscal terms vis-à-vis the Federal Government.

The main transactional taxes applicable to midstream/downstream activities are PIS/COFINS, CIDE-Fuel and ICMS, which are detailed further in **3.5 Income or Profits Tax Regime Applicable to Midstream/Downstream Operations**.

3.5 Income or Profits Tax Regime Applicable to Midstream/Downstream Operations

Comments regarding IRPJ and CSLL made in **2.4 Income or Profits Tax Regime Applicable to Upstream Operations** also apply to midstream/downstream activities. The other key taxes are as follows:

- CIDE-Fuel, which is levied on the importation and trading of petroleum and its derivatives, natural gas and its deriva-

tives and alcohol ethyl fuel, due from the producer, importer and formulator at variable rates;

- PIS/COFINS – although the general aspects are detailed in **2.4 Income or Profits Tax Regime Applicable to Upstream Operations**, there are differentiated rates/regimes depending on the product and the specific activity segment of the taxpayer; currently, the taxation is concentrated at the level of the producers, importers and/or distributors (the so-called monophasic regime); and
- ICMS – transactions with fuels are usually subject to a “pre-payment” regime where the tax substitute (usually the producer/importer) advances the ICMS due on the next transactions of the production chain (ICMS-ST) up until the sale is made to the final consumer, based on statutory value-added margins.

The Special Regime of Incentives for the Development of Infrastructure (REIDI) may apply to projects related to the construction of infrastructure necessary for producing or processing natural gas and related pipelines. If so, such projects will be exempt from the PIS and COFINS normally levied on certain acquisitions used in pre-approved projects.

3.6 Special Rights for National Oil or Gas Companies

As per **3.2 Rights and Terms of Access to Any Downstream Operation Run by a National Monopoly**, there are no legal national monopolies in Brazil in relation to upstream/downstream activities. Also, there are no special rights for Petrobras (the national oil and gas company) or its subsidiaries in the Brazilian upstream/downstream sectors.

3.7 Local Content Requirements Applicable to Midstream/Downstream Operations

There are no mandatory local content requirements in connection with midstream/downstream activities in Brazil.

3.8 Other Key Terms of Each Type of Downstream Licence

Please see **3.3 Issuing Downstream Licences**.

3.9 Condemnation/Eminent Domain Rights

A cornerstone of the Brazilian Constitution is the protection of private property. Property rights in Brazil can be acquired by all ways admitted under Brazilian civil law, and eminent domain rights and condemnation are admitted in certain circumstances as an exception to the private property protection general regime.

Law No. 8,987/1995 (the Concessions Law) sets forth that only a public authority has eminent domain rights and in Brazil those rights translate as a power of certain public authorities to declare

a property (including real estate) to be of “public interest” for the execution of a public service or work.

Condemnation in Brazil must be carried out directly by a public authority or by a private party by means of a delegation of powers, in which case the private party will be the one liable to pay any third party(ies) the applicable financial compensation for the asset declared to be of public interest.

Regarding the expropriation of real estate properties or the establishment of an administrative servitude in a private property for the performance of petroleum activities in particular (eg, the implementation of refineries, natural gas processing, liquefaction or regasification units, storage terminals, pipelines, etc), the ANP has the authority to conduct the relevant processes and to declare any assets (including real estate) necessary for the execution of a certain public activity to be of public interest, as provided in the Petroleum Law and in Law No. 11,909/2009 (the Natural Gas Law).

ANP Resolution No. 44/2011 sets forth the applicable rules and requirements to be met by the parties interested in having a property declared by the ANP as public interest for the purposes of expropriation and/or the establishment of an administrative servitude.

3.10 Rules for Third-Party Access to Infrastructure

Both the Petroleum Law and the Natural Gas Law provide interested parties with third-party access rights to transportation pipelines and maritime terminals, except LNG terminals.

Third-party access to transportation pipelines is governed by ANP Resolution No. 11/16 (oil transportation pipelines) and ANP Resolution No. 35/12 (gas transportation pipelines).

Under the open access regime, a transporter must allow third parties non-discriminatory access to transportation facilities in exchange for adequate remuneration, calculated using criteria established by the ANP, taking into account any exclusivity rights held by the owner of the facility, if applicable.

The extension of third-party access rights to gas production off-loading pipelines, gas processing or treatment units and LNG terminals is currently under discussion in the Brazilian National Congress through Bill of Law No. 6,407/13, as amended by Bill of Law No. 6,102/2016.

Furthermore, under the TCC entered into between Petrobras and CADE in July 2019 for the cessation of certain practices by Petrobras in the Brazilian gas transportation sector, Petrobras committed to negotiate in good faith non-discriminatory access

for third parties to Petrobras' gas processing or treatment units, following certain guidelines set by CADE until the ANP issues specific regulation on the matter.

Considering that Petrobras is currently the owner of nearly 100% of the gas processing or treatment units in Brazil, this obligation imposed on Petrobras by CADE will be extremely relevant to increasing access and competitiveness in the gas transportation market in Brazil.

3.11 Restrictions on Product Sales into the Local Market

There are no restrictions on product sales into the local market in Brazil.

3.12 Laws and Regulations Governing Exports

In April 2019, the ANP published Resolution No. 777/2019, establishing a new framework for export activities of biofuels and petroleum and its by-products. Such resolution revoked more than 20 diplomas governing export activities, thus providing standard authorisation requirements and standardised administrative proceedings for both export and import licence applications.

3.13 Requirements for Transfers of Interest in Downstream Licences

The available downstream licences in Brazil are addressed under **3.3 Issuing Downstream Licences**. The transfer of downstream licences typically requires prior approval from the ANP, and shall be subject to the ability of the transferee to evidence their capacity to undertake the related downstream activity and to comply with the applicable regulatory requirements. Please see **3.3 Issuing Downstream Licences** for the applicable ANP Regulations for downstream activities where the relevant requirements shall be provided.

4. Foreign Investment

4.1 Foreign Investment Rules Applicable to Investments in Petroleum

Brazil's traditional position regarding the international foreign direct investment (FDI) system is usually a topic of significant discussion. Brazil is still not a major player when it comes to bilateral investment treaties and agreements (BITs) – although it signed 25 BITs between 1990 and 2014, none of them has yet entered into force. Beginning in 2015, Brazil accelerated the pace, signing BITs with several countries (Post-2015 BITs) and entering into a Protocol of Co-operation and Intra-MERCO-SUR Investment Facilitation (PCFI) with Argentina, Paraguay and Uruguay. Of these, only the BITs with Angola and Mexico

and the PCFI (only as it pertains to Uruguay) have entered into force.

Over the years, Brazil has implemented crucial domestic changes to create an appropriate climate for foreign investment, by adopting rules in favour of neutral dispute resolution and international commercial transactions, including the enactment of pro-arbitration legislation, international sales of goods, rules on the protection of property rights and free enterprise.

Brazil enacted a modern arbitration law in 1996 (Law No. 9,306/1996 – the Arbitration Law), which was not only declared constitutional by the Supreme Court in 2001, but was also amended in 2015. The amendments reinforced the cultivated pro-arbitration environment in the Brazilian legal system with specific changes, seeking only to clarify controversial issues and deal with matters that were not previously regulated (eg, that the Public Administration may use arbitration to resolve disputes). In addition, Brazil enacted a mediation law in 2015 (Law No. 13,140/2015) and has ratified relevant international conventions, such as the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention) in 2012 and the United Nations Convention on Contracts for the International Sale of Goods (CISG) in 2013. Furthermore, Brazil has passed several laws under which certain disputes with the State are subject to arbitration.

In the petroleum industry, arbitration has gained a prominent position in Brazil among public and private parties. For public parties, for instance, Art. 43, X, of the Petroleum Law states that one of the mandatory clauses in concession contracts for oil and gas exploration and production is “the rules for the resolution of disputes (...) including conciliation and international arbitration”. Moreover, Art. 29, XVIII, of the Pre-Salt Law states that one of the mandatory clauses in production sharing contracts is “the rules for the resolution of disputes, which may set forth conciliation and arbitration”. With regard to private contracts such as Joint Operating Agreements (JOA) and Farm-in (or Farm-out) agreements, arbitration clauses – as per the models provided by the Association of International Petroleum Negotiators (AIPN) – are used increasingly, and arbitration has become the main method for dispute resolution.

The adoption of arbitration by Brazilian law, especially in Brazilian oil and gas legislation, and its acceptance by local courts represent a great attraction for investors. The possibility of having disputes settled by an independent and impartial arbitral tribunal, whose award can be enforced in Brazil (following the ratification of the New York Convention), is considered a major advantage for foreign investors.

Under Brazilian domestic substantive law, the protection of foreign investment is included in the current legal-normative structure of Brazilian Public Administration. Pursuant to Art. 172 of the Brazilian Constitution, Public Administration should be zealous in meeting its responsibilities for the maintenance of foreign investment. The core provisions of the Brazilian Constitution also reflect these responsibilities, establishing the guaranteed right to private ownership of property and free enterprise (Art. 5, XXII, and 170).

5. Environmental, Health and Safety (EHS)

5.1 Principal Environmental Laws and Environmental Regulator(s)

The Brazilian Constitution provides for environmental protection (Art. 225), stating that every person has the right to an ecologically balanced environment.

Pursuant to the Brazilian Constitution, Federal authorities can pass general laws and regulations on environmental control, while States and municipalities can supplement Federal legislation on issues of local interest. Moreover, Art. 23 of the Brazilian Constitution ensures that all three administrative levels are responsible for the enforcement of environmental laws, so Federal, State and municipal environmental agencies are involved therein.

Complementary Law No. 140/2011 details the activities subject to environmental licensing by Federal, State and municipal environmental protection agencies, and co-ordinates the enforcement power of those agencies.

Law No. 6,938/1981 implements the National Environmental Policy Act (NEPA) and details the environmental authorities at the Federal, State and municipal levels. Among these authorities, it is worth mentioning the Federal Environmental Agency (IBAMA), the Federal Agency for Conservation Units (ICM-Bio), and State and municipal environmental agencies, which are responsible for the execution and enforcement of environmental laws at Federal, State and municipal levels.

The Brazilian Constitution provides for environmental liability in three different fields, which may be imposed against individuals or legal entities, as follows:

- civil liability, which is tied to the concepts of pollution and polluter, and is strict, joint and several, and unlimited. Strict liability means that no fault or wilful misconduct of the polluter needs to be evidenced in order to establish the obligation to repair or pay compensation for environmental

damage. Joint and several liability means that each polluter may be called to indemnify or recover the entire damage, provided that the right of contribution is secured;

- administrative liability, which subjects the violator of a legal provision to administrative sanctions described in the Environmental Crimes Act (ECA), in Federal Decree No. 6,514/08 and in other laws and regulations. Environmental administrative liability is enforced by the competent Federal, State or municipal environmental protection agency, through the application of auto-enforceable sanctions, which may include fines of up to BRL50 million; the suspension or cancellation of a registration/permit/authorisation; the restriction or suspension of tax benefits/incentives or credit from official institutions; and the prohibition to execute contracts with public authorities; and
- environmental criminal liability, which is also provided for in the ECA and establishes criminal sanctions applicable to activities deemed harmful to the environment. The determining element of accountability for the application of criminal sanctions is the existence of fault on the part of the agent that committed the crime (negligence, imprudence, malpractice or wilful misconduct). Liable parties may be sanctioned with fines, the rendering of community services, the restriction of rights and, in worst cases, imprisonment. Executive officers, directors, administrators, managers, etc, may also face environmental criminal liability along with companies.

Other laws and regulations are also important in the context of petroleum activities. At the Federal level, the following should be highlighted:

- Federal Law No. 9,966/2000 and Federal Decree No. 4,136/2002, which provide for pollution at sea, in line with the International Convention for the Prevention of Pollution from Ships (MARPOL) and other international conventions signed by Brazil regarding the matter;
- Federal Decree No. 8,437/2015, which defines the activities that are subject to Federal environmental licensing;
- Federal Law No. 9,985/2000 and Federal Decree No. 4,340/2002, which regulate the environmental compensation due from potentially polluting activities; and
- MMA Ordinance No. 422/2011, which defines and details the environmental licensing proceeding for offshore petroleum activities, among others.

5.2 Environmental Obligations for a Major Petroleum Project

Major petroleum projects require environmental licensing, through which the relevant environmental agency authorises the location, installation, operation and expansion (alteration) of the relevant projects and activities.

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The installation, operation or alteration of projects without proper and valid environmental licensing, or without complying with the conditions of the respective environmental licences, may subject transgressors to civil liability (in the case of environmental damage), administrative sanctions and criminal liability.

While IBAMA conducts environmental licensing for offshore E&P activities for conventional resources and onshore or offshore E&P activities for unconventional resources, State EPAs conduct the proceedings for onshore E&P activities for conventional resources and, as a general rule, for midstream and downstream activities.

MMA Ordinance No. 422/2011 governs the Federal environmental licensing of offshore E&P, and comprises the following:

- the Seismic Survey Licence, which authorises the execution of seismic data acquisition;
- the Drilling Operation Licence, which authorises the drilling of wells offshore;
- Preliminary, Installation and Operation Licences for the production and flow off of petroleum activities; and
- Preliminary, Installation and Operation Licences for extended well tests (EWTs).

The proceeding begins with a Term of Reference granted by IBAMA, which details the type of environmental study required. The type and level of detail of the study depend on the complexity of the project and the sensitivity of the area. More complex projects require an Environmental Impact Study, a Report on Environmental Impact (EIA/RIMA) and at least one public hearing.

Usually, before each bid round, the Ministry of Mines and Energy and the ANP convene with the Ministry of Environment and competent EPAs on the sensitivity of the field and the possibility of areas being subject to E&P activity.

As a final remark, the Brazilian Congress is currently discussing a General Law to govern the environmental licensing proceeding. Monitoring the development of such Bill of Law is recommended.

5.3 EHS Requirements Applicable to Offshore Development

Offshore development is subject to environmental licensing proceedings and compliance with several environmental laws on the management, control and reporting of incidents; please see **5.1 Principal Environmental Laws and Environmental Regulator(s)** and **5.2 Environmental Obligations for a Major Petroleum Project**.

It must be highlighted that the Petroleum Law appoints the ANP as the entity responsible for inspecting E&P activities, with the objective of preventing failures in the operational safety of relevant facilities and avoiding possible harm to life, the environment and property.

One of the main regulations concerning offshore facilities issued by the ANP in this regard is ANP Resolution No. 43/2007, which provides for the Operational Safety Regime and establishes the Technical Operational Safety Management System Regulation (SGSO Regulation).

In addition, ANP Resolution No. 41/2015 establishes the Subsea Systems Operational Safety Regime and the Technical Regulation of the Subsea System Operational Safety Management System (SGSS), which sets forth the requirements and minimum safety and operational standards, as well as the preservation of the environment.

From a labour law perspective, it must be pointed out that companies are legally required to implement both the Occupational Health Control Programme (PCMSO) and the Environmental Risks Prevention Programme (PPRA). Companies are also required to have an Internal Committee for Accidents Prevention (CIPA) and Specialised Services in Health and Safety (SESMT) for purposes of guaranteeing the safety of employees in the workplace and avoiding the occurrence of occupational diseases and labour accidents.

The Labour Office of the Ministry of Economy is the entity responsible for the issuance of the Normative Rules that will establish the main obligations to be complied with by companies regarding health and safety matters. For companies responsible for offshore activities, there is a specific Resolution under No. 37 regarding health and safety conditions to be complied with in the Brazilian territory.

5.4 Requirements for Decommissioning

The relevant procedures and costs for the decommissioning of any field are detailed in the development plan of each field, subject to approval by the ANP before the start of production. Once the development plan is approved, the concessionaire/contractor is bound to the decommissioning obligations and liabilities set forth in the approved plan, and such provisions must be revised periodically throughout the field's production phase by means of the annual work programmes and budgets. The concessionaire/contractor – or, jointly, the consortium members – is (are) responsible for the decommissioning liabilities of the field before the ANP.

It is important to note that the decommissioning obligations are subject to specific financial guarantees – in the form of

insurance, a letter of credit, a provisioning fund, or other forms accepted by the ANP – in an amount sufficient to cover all decommissioning activities, as provided in the field's development plan approved by the ANP.

ANP Resolution No. 817/2020 established guidelines, obligations and deadlines for the decommissioning of oil and gas production systems, including the content of the decommissioning programme and the final decommissioning report. This Resolution attempted to establish a more integrated approach between the different existing regulatory agencies that should be involved (ie, the ANP, environmental agencies, and the Navy), but this is still a work in progress.

5.5 Climate Change Laws

Brazil is a signatory of several international treaties, such as the Paris Agreement, which was ratified in 2017 and under which Brazil undertook to reduce its greenhouse gas emissions to 37% below the levels of 2005 by 2025 and to 47% below by 2030, through reaching a 45% share of renewable energy in the energy mix, increasing biofuel consumption, ethanol supply and bio-diesel content in the diesel blend, among other means.

In this context, Brazil enacted the National Policy on Climate Change Act (Law No. 12,187/2009), seeking to reduce GHG emissions, strengthen carbon capture initiatives and promote the recovery of degraded areas, among other objectives.

Brazil is also known for encouraging an increase of biofuels in its energy mix, having implemented several related mechanisms, such as the mandatory addition of biofuels to fossil fuels and incentives on tax, finances and credits. More recently, additional mechanisms were created by a new national biofuel policy, called "RenovaBio" (Law No. 13,576/2017).

5.6 Local Government Limits on Oil and Gas Development

In Brazil, exploration activities in the sedimentary basins have been carried out through two main conventional methods:

- in most cases, based on the occurrence of a porous and permeable deposit, protected by an effective "cap rock" and filled with hydrocarbon from "source rocks" (capable of generating oil and/or gas); and
- in less frequent situations, in naturally fractured reservoirs with production capacity.

In both cases, a fracturing process may be necessary to increase the flow area in the deposit, being the hydrocarbon conducted to the top of the well through induced fractures and considerably increasing the drainage area.

In Brazil, hydraulic fracturing operations in conventional petroleum formations in the Recôncavo basin have been common since the end of 1950, with about 6,000 operations carried out, such as the hydraulic fracturing campaign carried out by Petrobras in wells located at the Candeias and Dom João fields in 1959. To date, there is no indication, information or confirmation of environmental damage caused to aquifers resulting from these operations.

Based on the successes achieved by the United States in the production of petroleum through the direct fracturing of source rocks or low-permeability reservoirs (unconventional reservoirs), and due to the reduction of petroleum supply, price increases and the need for self-sufficiency, Brazil has tried to promote the use of such techniques to evaluate the potential of gas production in its onshore basins of Recôncavo, São Francisco and Paraná.

In this regard, the ANP published ANP Resolution No. 21/2014, which addresses the operational safety towards the protection of people and the environment while using hydraulic fracturing techniques in an unconventional reservoir.

Also, the ANP promoted the 12th Bid Round for the exploration and production of petroleum, offering 110 exploratory blocks in areas of New Technological Frontiers and Knowledge in the basins of Acre, Parecis, São Francisco, Paraná and Parnaíba, with the objective of attracting investments to regions that were still not well known from a geological standpoint or that had any technological challenges.

During the promotion of the 12th Bid Round, Non-Governmental Organisations initiated a campaign against hydraulic fracturing in unconventional reservoirs, highlighting alleged uncertainties arising from this activity. The campaign was also supported by the Prosecutor General Office, which proposed several Public Civil Actions in all States where the offered blocks were located. As a result, several preliminary injunctions were rendered, suspending the execution of the E&P contracts.

Several judicial decisions currently prohibit the ANP from offering exploratory blocks that demand hydraulic fracturing, and from authorising the use of these techniques by any concessionaire/contractor. Due to the legal uncertainty caused by judicial activism, environmental agencies are also not granting any environmental licence that authorises this kind of activity.

6. Miscellaneous

6.1 Unconventional Upstream Interests

Please see 5.5 Climate Change Laws.

6.2 Liquefied Natural Gas (LNG) Projects

The typical structures for LNG projects in Brazil are as follows:

- a structure where the imported LNG is regasified at a Floating, Storage and Regasification Unit (FSRU) terminal (FSRU Terminal); or
- a structure where the imported LNG is regasified at a regasification plant within a certain industrial site, in which case a special LNG pipeline may connect the storage facilities to the regasification plant (Onshore Regasification Terminal).

Both the FSRU Terminal and the Onshore Regasification Terminal are classified as an LNG Terminal, pursuant to the Natural Gas Law, the Gas Decree and ANP Resolution No. 50/2011, which establish that an LNG Terminal is a facility used for the liquefaction or import, discharge and regasification of LNG and the subsequent delivery of the natural gas to the gas pipeline network or other means of transport.

In general terms, the main permits required for the construction and operation of a LNG Terminal are environmental permits, port and maritime permits, and LNG and gas regulatory permits.

Regarding the LNG and gas regulatory permits in particular, ANP Resolution No. 52/2015 regulates the relevant authorisations for the construction and operation of LNG Terminals. Accordingly, such authorisations are granted by ANP in two phases: (i) construction authorisation; and (ii) operation authorisation.

In order to obtain the construction authorisation and the operation authorisation, the company or consortium of companies interested in the implementation of an LNG Terminal must primarily be registered as a “regulated agent”, through the submission of certain corporate documents to the ANP.

In short, most of the requirements imposed by the ANP for the issuance of the construction authorisation and the operation authorisation are related to technical information regarding the LNG Terminal, which must be in accordance with certain specific technical requirements set forth by the ANP and other technical bodies. The ANP will also require the applicable environmental, port and maritime permits for the LNG Terminal, which must be secured by interested parties for the construction and operation of such facilities.

6.3 Unique or Interesting Aspects of the Petroleum Industry

Both before and after the creation in 2010 of a production sharing regime for pre-salt areas, industry has questioned the need and wisdom for such change. Initially, pursuant to the Pre-Salt

Law, only Petrobras could operate pre-salt blocks. To address the concerns of foreign investors, the Pre-Salt Law was amended in November 2016 so as to allow companies other than Petrobras to operate in pre-salt areas, and to grant certain preferential rights to Petrobras regarding pre-salt operatorship.

At the tenth anniversary of the pre-salt regime, lacklustre performance teamed with industry satisfaction sent a clear signal to the Government that change was necessary. Accordingly, several legislative proposals are under consideration, the most promising of which is Bill of Law No. 3,178/2019, which would eliminate Petrobras’ preferential rights and permit the CNPE (advised by the ANP) to decide whether to apply the concession regime or the production sharing regime to Pre-Salt Bid Rounds.

Another interesting recent development is the unique “Transfer of Rights” (ToR). To increase Petrobras’ financial capacity to explore and produce the pre-salt reserves, Law No. 12,276/2010 introduced the ToR, which defined a special capitalisation of Petrobras at the time and assigned Petrobras (upon consideration and through direct contracting) the right to produce up to 5 billion BOE in certain pre-salt areas (more specifically, the areas of Búzios, Itapu, Sul de Sapinhoá, Atapu, Sul de Sururu, Norte de Sururu, Sul de Berbigão, Norte de Berbigão, Sul de Lula and Sépia – as currently defined).

As consideration, Petrobras paid BRL74,807,616,407 for the ToR, and the company’s capitalisation process amounted to BRL120 billion (representing the largest capitalisation in world history at the time).

As mandated by Law No. 12,276/2010, the Federal Government and Petrobras entered into a special E&P contract to govern the ToR (the ToR Agreement).

In addition to the 5 billion BOE that Petrobras has the right to produce, studies indicate the existence of a surplus volume of oil and gas ranging from 6 billion to 15 billion BOE in the ToR area (the ToR Surplus). In order to allow a bigger and more diversified presence of private investments in the petroleum sector in Brazil and to collect funds for the Federal Government, in November 2019 the ANP organised a specific bid round for the ToR Surplus (the ToR Bid Round). The ToR Bid Round was held under the production sharing regime and offered private companies the opportunity to jointly develop the ToR Surplus with Petrobras within the Atapu, Búzios, Itapu and Sépia areas (Santos Basin).

Under the ToR Bid Round, Petrobras acquired Itapu (100%) and a consortium formed by Petrobras (90%), CNOOC (5%) and CNODC (5%) acquired Búzios. There were no bids for

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the Atapu or S epia areas. The Federal Government collected approximately BRL70 billion in signature bonuses, in addition to its contractual share of profit oil from eventual production.

The ToR Bid Round winners will enter into both a production sharing contract and a “Co-participation Agreement” with Petrobras. These agreements will govern the joint operations for the development and production of petroleum in the relevant areas, and the compensation due to Petrobras for the investments it previously made in those areas.

Future ToR Bid Rounds will provide a unique opportunity for oil companies. In January 2020, the MME appointed PPSA as a representative of the Federal Government, to assess the surplus volumes of the unawarded areas (Atapu and S epia) and to assist in the negotiation with Petrobras regarding compensation reflecting prior investments made in the Atapu and S epia areas. The MME’s main goal is to provide adequate predictability and legal assurance for the interested companies to participate in the next ToR Bid Round – hopefully resolving investors’ concerns in a consistent and economically attractive manner.

6.4 Material Changes in Oil and Gas Law or Regulation

Following a period of five years with no offshore bid rounds between 2008 and 2013, in mid-2016 Brazil started to make significant adjustments to its regulatory framework, promoting a further opening of its petroleum industry.

The recent reforms in the petroleum industry resulted in several adjustments that took place in 2017-2020, such as:

- the change in the local content requirements (eg, reduction of percentages, exclusion of local content as a component of the offers);
- the enactment of ANP Resolution No. 785/2019 on the assignment of E&P Rights (including the provisions related to the upstream funding based on the reserve-based lending concept);
- the execution of the TCCs between Petrobras and CADE, under which Petrobras agrees to divest approximately 40%

of its refining capacity and to completely exit from gas pipeline transportation and gas distribution activities;

- the enactment of CNPE Resolution No. 16/2019, which established the guidelines for the new gas market;
- the ToR Surplus Bid Round, Concession Bid Rounds 14-16, and the Pre-Salt Bid Rounds 2-6, all of which were held in 2017-2019;
- the announcement of the upcoming Concession Bid Rounds 17-18 and Pre-Salt Bid Rounds 7-8;
- the first round (also known as “cycle”) of the Permanent Offer (allowing, through a differentiated bid mechanism, the development of relinquished fields and exploratory blocks that have not been awarded during past bid rounds, or that were relinquished); 33 blocks and 12 marginal areas were awarded in the first cycle;
- the announcement of the sale of certain midstream/downstream oil refining and gas assets owned by Petrobras (aimed at opening the gas market in Brazil);
- the Programme for the Revitalisation of Onshore Oil and Gas Exploration and Production Activities for 2020 (REATE 2020), which aims to stimulate competition at the national level and foster development at the local and regional levels; and
- the enactment of ANP Resolution No. 817/2020, which establishes guidelines, obligations and deadlines for the decommissioning of oil and gas production systems.

The Impact of COVID-19

ANP Resolution No. 815/2020 extended certain deadlines related to oil and natural gas exploration and production contracts. In parallel, ANP Resolution No. 816/2020 (as amended by ANP Resolution No. 820/2020) established procedures to be adopted by oil industry participants regulated by the ANP during the pandemic. The ANP will likely continue to take actions to minimise the impact of the pandemic on the oil and gas industry.

The pandemic has impacted the bid round schedule, with the ANP Board of Directors suspending concession regime Bid Round 17, which was planned for 2020. The production sharing regime Pre-Salt Bid Round 7 is also scheduled for 2020, but may also be postponed due to the pandemic.

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Taulil & Chequer Advogados in association with Mayer Brown is a full-service law firm, offering clients in-depth local knowledge combined with global reach. Founded in 1992, the firm has grown rapidly and today has approximately 160 lawyers in Rio de Janeiro, São Paulo and Brasília. In December 2009, Taulil & Chequer entered into a combination agreement with Mayer Brown and became “Taulil & Chequer in association with Mayer Brown (TCMB)”. The firms co-operate to provide clients with a unique combination of local strength and

global reach. T&C has a team of highly specialised lawyers in several areas of business law in Brazil, working on simple and routine operations through to the most complex and sophisticated. The firm offers clients the full range of legal services and has a particularly strong and long-standing presence in the energy, oil and gas, and infrastructure industries. It offers a full-service practice and legal advice to domestic and international clients, financial institutions and government agencies.

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