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Corruption: Are OSVs Exempt?
Will the offshore business avoid scandal?

The Economics of Local Content
A look at its place in a global market

Split Charters & New Law 13.043
The difficulty of dividing costs & earnings



WESTSHORE
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Westshore do Brasil, Cover image courtesy of Fairmount Marine.

Drilling & Production

The latest from Brazil

New tender for UDW drilling rigs

A new international ultra-deep water tender launched by Petrobras is on the market for chartering two different categories of drilling rigs. The first is for units able to work in 2,400 meters of water depth for three years and the second cover units for 2,000 meters water depth for five year contracts. The drilling rigs will be used in the pre-salt area of the transfer of rights.

FPSO confirmed

As mentioned in this publication's September edition and as the market has been expecting, the consortium Modec/Schahin has been awarded the construction of the FPSO for Tartaruga Mestiça and Tartaruga Verde fields, in Campos Basin. The unit will be capable of producing 150,000 boed and processing four million cbm of natural gas per day. The FPSO is scheduled for delivery in the third quarter of 2017.

Pipelay splash

French firm Technip is confirmed to provide Petrobras with 114 kilometers of flexible pipes, including gas lift, gas injection and gas export lines to be installed in Iracema North pre salt field in the Santos Basin. The company's new building center in Rio de Janeiro will be responsible for performing the engineering and project management. Technip is expected to start delivering the flexible pipes during the first half of 2015.

And the winner is...

According to ANP (National Agency of Petroleum) the FPSO Cidade de São Paulo, owned by the consortium Modec/Schahin and installed in the Sapinhoá field, is the unit with the largest oil production in Brazil with a total of 131.9 thousand of boed. In second place, the platform P-52, operating in the Roncador field, produces 131.1 thousand of boed, followed by the FPSO Cidade de Paraty which produces 130.4 thousand of boed in the Lula field. ANP released a list with all 20 FPSOs actually working for Petrobras and their respective production. More info at www.anp.gov.br

Leaving and coming to Brazil

After Petrobras released the drilling ship DPDS1 around 154 days before the conclusion of its contract, the state major and Paragon Offshore has agreed to swap out the unit for the semisubmersible MSS2 for a lower day rate of USD 273,000 as opposed to the USD 290,000 previously paid for the drillship. The DPDS1 will be transferred and stacked in the Gulf of Mexico awaiting new customers while the MSS2 will be on contract with the oil company by April 2016. The decision will benefit both companies at a time when Petrobras is looking for cutting costs and Paragon seeking new long term charters.

Headline News



Corruption: Are OSVs Exempt?

The market is overwhelmed by the unprecedented volume of corruption scandals investigations held for the last couple of months involving Petrobras contracts.

They are mainly triggered by a disastrous overpriced purchase of a US refinery (Pasadena) that led to a plea bargaining agreement with one former Petrobras Director which culminated in a tsunami of accusations in the Petrobras International, Services and Downstream Directorships. But what about OSVs?

Due to the plea bargaining agreement, many other corruption scandals and names have appeared leading to a much wider investigation as some of the denounced parties have also been making agreements with the justice, bringing more and more names to the scene.

The investigation is mainly based on an alleged formation of cartels, not by the suppliers as an economical

crime, but encouraged by Petrobras' own senior management in order to diminish competition then enabling "kickbacks" to Directors and political parties. The sums involved in the investigation have already reached dozens billions of Dollars and it has become one of the biggest corruption scandals ever.

There are presently two former Petrobras Directors and one former executive manager involved, where two of them have agreed to tell the justice all they know. Dozens of directors of renowned companies/suppliers were also arrested and the investigation is still on going with 39 people now facing charges but none of them are so far directly related to the OSV sector.

Many question whether such a cartel could have been formed and implemented in a sector where you have clear lowest price tenders.

Petrobras' OSV sector has always been very democratic and transparent, almost crystal clear, since the times

there were public meetings for each bidding process where any interested party could attend. It was a very cordial event where sealed envelopes were opened and anyone could have access to it. It was also a moment to have a public contact with the market players, competitors and Petrobras chartering department.

Petrobras used to issue national bidding processes (for Brazilian flag vessels, where all and any Brazilian ship-ping company could participate if interested) and whenever demand was still not covered, they would thereafter proceed to an International bid/invitation, where, in addition to Brazilian owners, any other interested Party could be invited, including shipbrokers and foreign owners. It had been like that for decades, until 2010, when Petrobras implemented its web based procurement portal namely "Petronect".

The public meetings were then discontinued and all proposals sent electronically via the portal. The market felt the difference and the coldness of the new procedure, which also limited the access for interested parties to witness the result of tenders personally.

On the contracts resulted from bids where corruption schemes are found to be a practice, there has been a historical movement to limit competition, to concentrate the ability and the right to offer on very few suppliers. Petrobras' simplified contracting mode (Decree 2.745) if misused can potentially enable this practice.

The simplified mode does away with the principles of the normal public tender of wide competition, unrestricted access to information and ample reach for all interested Parties.

Usually, a bid done through an "Invitation Letter" (one of the options in the simplified mode) gives each Petrobras contracting department the freedom to invite only who they feel is capable of performing the intended contract. Criteria are usually established to justify the receivers list, for example: proven track record in service, experience in Brazil, to be a Petrobras registered supplier, development of the local industry and healthy financial standing.

The conduct of Petrobras OSV Chartering department has always been exemplary, very impartial, and aiming

for transparency in the processes and negotiations. However, they have been systematically forced to go through some changes when it comes to the Bids receivers' list. The first big change is the use of Petronect itself, which meant the need for a login/password to access or even follow a bidding process.

The second one relates to shipbrokers: Petrobras management instructed that professional shipbrokers should no longer be directly invited to the International bids/ invitation. Despite its own high contracting pace, Petrobras argued that although shipbrokers have recognizably promoted competition on the tenders and intensely diversified their OSV fleet profile, it led to a higher frequency of problems, including vessels' "no shows". Shipbrokers have then still participated on the tenders, by either "registering" foreign Owners interested to render services to Petrobras, or supporting the already registered ones, but also through others willing to partner with foreign Companies to serve Petrobras.

In subsequent moves, Petrobras has implemented several criteria that a company should meet in order to be invited for OSV tenders. All these criteria depend on Petrobras' own judgment which does not help transparency. They include: being an EBN fully registered on the Petrobras supplier system (CRCC) which involves compliance to several of Petrobras' own requirements; the EBN must rank minimum 6.0 on an HSE excellence program (PEOTRAM) which was created and is judged by Petrobras. In addition the EBN must not have an operational score considered as "insufficient" by Petrobras; EBNs not only during the CRCC registration but also during each tender must comply with Petrobras specific and rigorous financial standing requirements

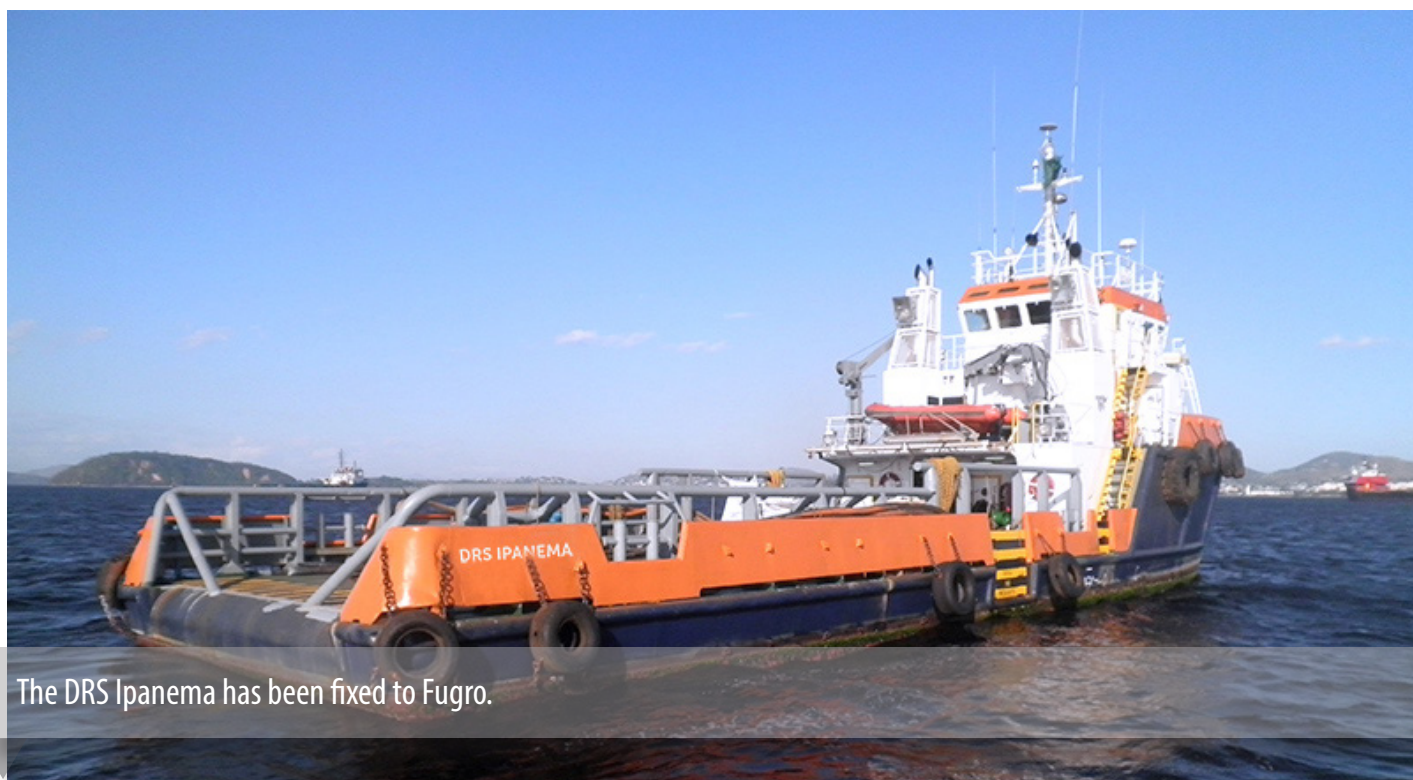
Around five years ago Petrobras chartering department could count on the free support of shipbrokers, increasing competition in a "free" market where any foreign owner and EBNs could freely offer on bidding processes.

The present scenario of increasing limitations on the number of suppliers and further barriers for new entrants, gives them a very challenging task in efforts to increase transparency, efficiency and keeping rates at international levels.



Vessel News

Chartering Activity



The DRS Ipanema has been fixed to Fugro.

DRACARES - Brazilian built and flagged DRS Ipanema has been fixed to Fugro 30 days firm plus options to assist on a survey for end users Petrobras and Repsol.

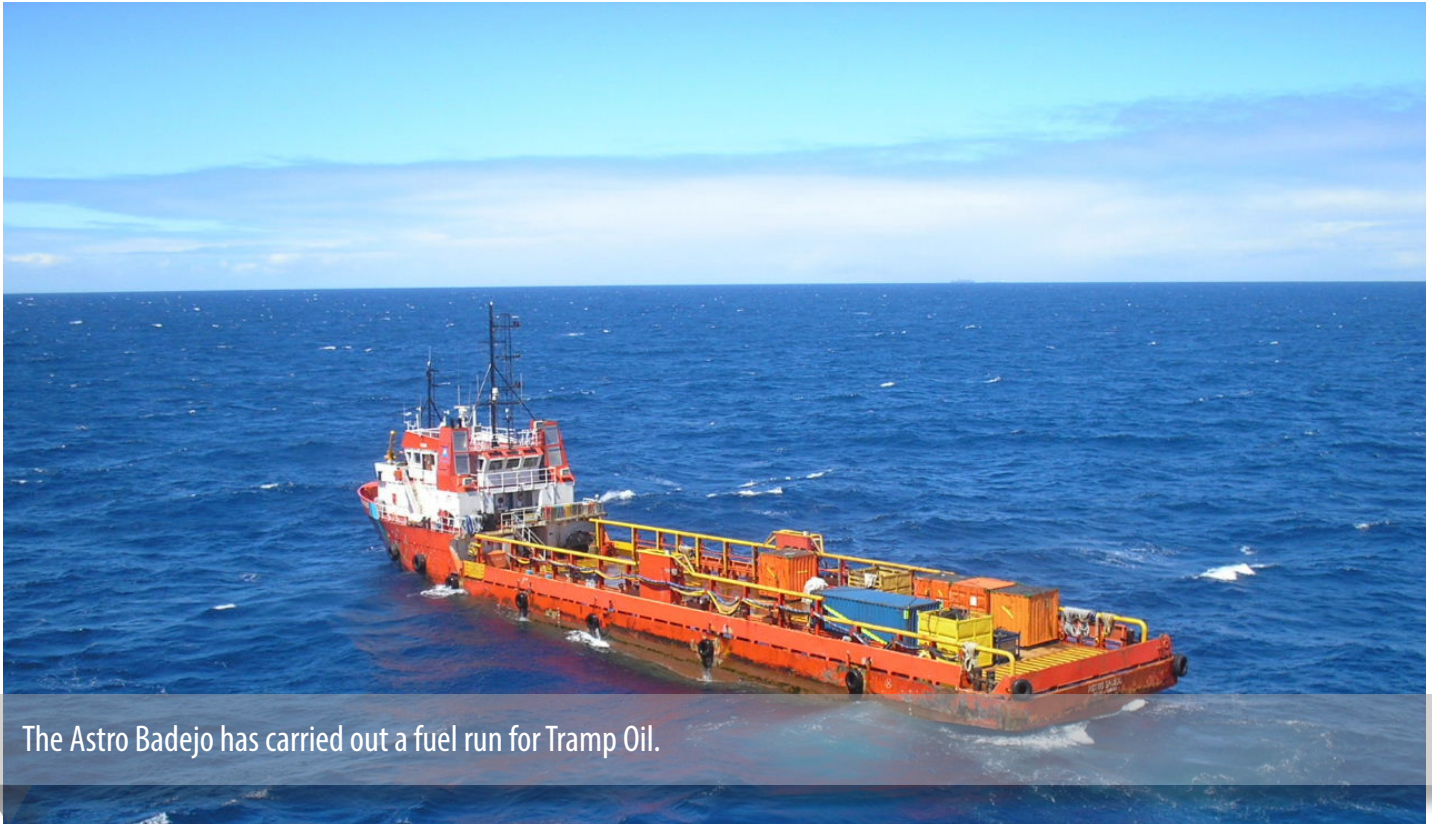
ECO TUG - Brazilian built and flagged OSRV Eco Octo has been fixed to Ocean Rig last month for one cargo run offshore to the Campos basin.

CHOUEST - Brazilian built and flagged PSV Santos Solution has been released by Shell. The vessel is now set to work in Colombia. Brazilian built and flagged AHTS Elizabeth C had previously been fixed for 18 days with HRT to assist on a well re-entry campaign, which has already concluded.

DEEP SEA SUPPLY - AHTS Sea Leopard has been fixed to OGP for a couple of weeks to assist on maintenance of their FPSO offloading hose and is now available in the spot market.

BRAVANTE - PSV Bravante VIII has arrived in Brazil after a successful journey from the Gulf of Mexico. The PSV Viking Thaumias is being released after her successful charter with Petrobras. The vessel will undergo modifications for her new charter with the oil major.

LABORDE - PSV Magnolia Mar has been fixed to OWBunker for one fuel run, and to another couple



The Astro Badejo has carried out a fuel run for Tramp Oil.

to Tramp Oil. Brazilian built and flagged LAB 152 is finishing her maintenance and is expected to be ready by December 20th.

ASTROMARITIMA - Brazilian built and flagged Astro Badejo has been fixed to Tramp Oil for one fuel run from late November. At the moment of writing the vessel is prompt available in Guanabara Bay.

DEEP SEA SUPPLY - Preparations for the Brazilian built and flagged DP2 PSV Sea Brasil are nearly concluded. The vessel is now set to enter her new contract shortly.

BRAVANTE - PSV Bravante VI is set to become available in Brazil right after Christmas on December 26th. The vessel has cleared customs and is ready to

work. Sister vessels Bravante V, VII and VIII are under negotiation for another charter.

STARNAV - PSV Starnav Aquarius to become available on December 18th after conclusion of her successful contract with Saipem for the end user Petrobras. The vessel will be then be prompt available.

OCEANPACT - OSRV Clarisse (300m3) and LH Antonio David are prompt available in

Guanabara Bay.

For updated online news and vessel positions please check our website and APP available for Android and iOS.

“Oceanpact’s OSRV Clarisse and the LH Antonio David are now prompt in Guanabara Bay.”

Operator Update

Brazilian Activity

A new Brazilian oil company?

Rumours of a plan for the union between HRT and OGpar are all over the market after the biggest shareholder of HRT, Nelson Tanure, has started talks with OGpar's creditors for a possible merger. If it happens, the deal could represent savings of over USD 400 thousand per day only on FPSOs chartering as it would be necessary for only one unit at both Tubarão Martelo and Polvo fields. It could also lead to the unitization of production in the area once HRT says that the fields are inter-connected, but OGpar disagrees. The negotiations have started and are subject to the approval of OGpar's creditors.

Cheaper oil worries the market

French Total may revise their investments in Brazil if the oil price persists in the range of USD 70 per barrel during the next two years. According to the company's president in Brazil, the price of the barrel of oil will determine if new drilling campaigns will be economically viable once the average of USD 80/barrel is the limit price for many projects, but also guaranteed that none of company's assets in the country are threatened. Total plans on investing between USD 400 to USD 500 million in Brazil next year.

Coming up...

Statoil may still announce this year the necessary investments for chartering a third platform for the Peregrino field in the Campos Basin. According to the company, the concept of engineering design is already defined and it is aiming for a fixed platform connect-

ed to the FPSO Peregrino. The project is only dependent on internal approvals. The first oil is planned for 2019.

Shell wins an ANP award

Anglo Dutch Shell has been awarded the ANP's Innovation Technology award due to the success of the project with wet Christmas trees design. The scheme was applied to the re-development of Bijupirá and Salema fields in the Campos Basin and implemented by FMC with Shell's supervision. The company was also nominated for the project of artificial elevation system in the Parque das Conchas field, in the Campos Basin.



Statoil

Inside Story



Brazilian policy sometimes seems like a throwback to 17th century France.

The Economics of Local Content

Modern day Brazilian policy seems to have a lot in common with the French 17th century economic mindset of Jean-Baptiste Colbert. But the notion that economic power can be enhanced by “selling more and buying less” is coming under strain.

The last 12 years of Lula and the first Dilma governments maintained development fundamentals for the ministries. As a result, the Brazilian agenda for the oil industry since 2002 has been to strengthen the local content. In a simplistic terms, the plan has been to produce more local goods, replacing foreign imports.

The strategy jointly followed by the Development and the Finance ministries, is anchored on the local production of oil rigs, FPSOs and offshore support vessels.

The problems arise when we look at how the government deals with their intentions. The production is “fictitiously” exported (in Portuguese called *exportação ficta*), a smart instrument from the government. While the goods are produced locally and remains in country, their full value at the conclusion of the ship-building is “exported”, thus added to the trade balance.

Although physically the unit never leaves the country (just part of the leasing contract will in the end). Here is



Too much focus on the trade balance is distorting the true Brazilian economic situation.

where things start to go wrong. If an economy is to be measured by its foreign trade balance, the United States of America would be broken.

The excess of governmental intervention in Colbert's time ended up suffocating the French. The consecutive years of fiscal renunciation and increased governmental expenditure could end up breaking the Brazilian economy (USD 15 billion expected deficit in 2014).

A focus on the trade balance alone ignores its effects on the balance of capital. Not generally but in most cases, if a developing economy imports less than it exports, it means the capital is finding better remuneration outside than investing locally.

To compensate for the better routing the capital finds (and capitalists will always and naturally pursue the best return), the government sponsors with the public Petrobras capital a pernicious local industry building at non-competitive cost. It spends badly and more, to supposedly export the goods (the economic results stimulates higher costs). Further, it mixes the Petrobras and the governmental budgets; like Mexico does with Pemex and Venezuela with PDVSA.

Whereas a better model might be how Norway deals with Statoil. In the Scandinavian country, the revenues generated by the royalties enter a sovereign fund, untouched by the parliament.

In Brazil's example, the revenues not even yet acquired are already committed in the governmental budget, the same that sponsors the doomed local content policy, the ships and platforms and the cycle that doubles costs continues

The recently named not yet confirmed new Brazilian Minister of Finance is a professional from the investment market.

The question is will he be able to change the scenario when surrounded by supposedly left fundamentalists? Or will the government learn from the recent crisis surrounding Petrobras and focus on reducing and improving cost and investment?

The initial signs do not look positive so far. On 11th December 2014 in the eye of the hurricane of the Petrobras scandal and the government announcing Petrobras will issue bonds worth USD 9 billion with guarantees from the government for a capital injection there has not been one single note about solving the excess expenses in refineries and shipbuilding. ■

"A better model might be how Norway deals with revenues generated from Statoil, where the royalties enter a sovereign fund."

Petrobras News

7th Newbuilding Round Awards

As mentioned in our July edition, Petrobras has finally released the awards on the 7th newbuilding round. Eleven OSVs were awarded contracts as described in the table below. Nine of the awards are for PSVs 4500 and two AHTSs 18000. So far the Renewal Program of Offshore Fleet has hired 121 OSVs, of which 34 are already in operation and 87 are under construction. Petrobras also confirmed that an 8th phase of the program is scheduled for the first quarter of 2015. Note that rates offered are subject to negotiations with Petrobras.

PSV 4500 A (fresh water)					
<i>Bidder</i>	<i>No of vessels</i>	<i>Period (years)</i>	<i>TDG</i>	<i>CDC</i>	<i>TT</i>
CBO TBN1	1	6	38,950.00	12,425.81	50,862.06
Chouest Hull 147	1	8	35,822.00	16,785.11	52,607.11
Chouest Hull 148	1	8	36,744.00	16,785.11	53,529.11
Chouest Hull 149	1	8	37,666.00	16,785.11	54,451.11
Chouest Hull 150	1	8	38,588.00	16,785.11	55,373.11

PSV 4500 B (fuel diesel oil)					
<i>Bidder</i>	<i>No of vessels</i>	<i>Period (years)</i>	<i>TDG</i>	<i>CDC</i>	<i>TT</i>
Chouest Hull 144	1	8	35,822.00	16,785.11	52,607.11
Chouest Hull 143	1	8	36,744.00	16,785.11	53,529.11
Chouest Hull 145	1	8	37,666.00	16,785.11	54,451.11
Chouest Hull 146	1	8	38,588.00	16,785.11	55,373.11

AHTS 18000					
<i>Bidder</i>	<i>No of vessels</i>	<i>Period (years)</i>	<i>TDG</i>	<i>CDC</i>	<i>TT</i>
CBO TBN 2&3	2	6	74,000.00	31,075.50	104,024.81

Requirements

Outstanding Requirements

Petrobras has recently issued the following requirements for local and foreign OSVs:

PSV 1500 E&P Nº 1685522148		
Type	Delivery	Period (Years)
PSV 1500 A Type	latest May 2015 or 120 days after award	4 + 4
PSV 1500 B Type	latest June 2015 or 120 days after award	2 + 2

PSV 3000/4500 (local flag or REB) E&P Nº: 1685545148		
Type	Delivery	Period (Years)
PSV 3000 A Type	Up to Jun 2015 or 120 days after contract award	2 + 2
PSV 3000 B Type	Up to Jun 2015 or 120 days after contract award	2 + 2
PSV 3000 C Type	Up to Jun 2015 or 120 days after contract award	4 + 4
PSV 3000 D Type	Up to Jun 2015 or 120 days after contract award	2 + 2
PSV 4500 A Type	Up to Jun 2015 or 120 days after contract award	2 + 2

AHTS 18000 ROV E&P Nº 1691980148		
Type	Delivery	Period (Years)
AHTS 18000 ROV	Up to April 2015 or 90 days after charter award	4 + 4

AHTS 18000 E&P Nº 1691982148		
Type	Delivery	Period (Years)
AHTS 18000 Type 1	Up to April 2015 or 90 days after award	2 + 2
AHTS 18000 Type 2	Up to July 2015 or 90 days after award	2 + 2
AHTS 18000 Type 3	Up to September 2015 or 90 days after award	2 + 2
AHTS 18000 ROV Type 4	Up to March 2015 or 90 days after award	2 + 2

Saving Millions

Since its creation in 2012, the Infralog (Logistics Infrastructure Optimization Program) has focused on projects related to offshore support bases and airports, natural gas processing and transportation of oil exports and refined products. The solutions adopted by Petrobras include adapting and expanding the capacity of pipelines serving refineries, as well as using existing ports and airports rather than building new support bases for its ship and helicopter operations. By the end of 2013, the Infralog program has managed to cut costs by about BRL 800 million. The goal is to save BRL 4 billion by December 2016.

Better Late Than Never

Petrobras has started transporting the hull of the FPSO P-66 to BrasFels shipyard in Angra dos Reis, where the topside integration will be performed. The unit is the first of the series of 8 “replicantes” to be built in Brazil and will have a capacity to produce 150 thousand of boed and to compress 6 million cbm of gas. The hull was originally planned to leave Rio Grande (ERG-1) shipyard last year but after several delays the company expects that it will arrive in Angra on December 18th. The P-66 will be installed in the Lula South field and its first oil is scheduled for 2016.

Look Ahead



Having contract splits in Brazil can be extremely tricky.

Split Charters & New Law 13.043

Having a foreign flag vessel chartered through two contracts or a contract split instead of one can be tricky in Brazil. It requires a lot of thought on the maths and fiscal analysis should be done over the two “halves” of the rate.

One share of the vessel charter contract may not be subject to withholding tax (if the owner’s domicile is not a tax haven) and the other share related to the services portion of the contract may have local taxes due.

It is only once this analysis of both shares is calculated can it be seen whether a shipowner is competitive enough to win in a tender and, moreover, if the net amount left is enough to continue the operations.

This scenario mainly affects Petrobras, taking into consideration that IOCs in Brazil usually only take national charter contracts with no overseas charter remittance.

Throughout the last tenders, Petrobras has been limiting the charter share to up to 80% of the daily rate, while some IOCs that also allow daily rate splits have

signed contracts with up to 90% of charter share. Nevertheless, the declaration of the federal law number 13,043 on November 13th, more specifically its Article 106, has amended the law number 9481/1997, which determines the IR (income tax) incidence over products and services, by limiting the charter split amount in OSV contracts, as well as rigs, drillships, etc. As of November 14th, the charter portion of any new OSV split contract must be limited to up to 65% of the contract value.

The law has also determined that, in order to precisely calculate the percentages, the share or shares of the daily rate in a foreign currency must be converted to Brazilian Reais using the PTAX (official average exchange rate according to Brazilian Central Bank) of the proposal presentation date to the charterer.

If the daily rate should be adjusted periodically, the split calculation should still consider the same PTAX of the proposal date. If the charter share exceeds 65%, the exceeding amount should be considered in IR calculations.

When the law was declared, at first the market thought it was applicable only to new contracts, not ongoing ones. Nonetheless, very recently Petrobras issued letters to owners whose contracts have an exceeding percentage of charter split, informing that as from January 2015 Petrobras shall withhold the income tax (15% or 25%) on the quota exceeding the percentages according to this law.

If owners have any pleadings on daily rate readjustment, they need to be sent along with valid and qualified documents that prove that it would be applicable. For example, a report prepared by an independent audit firm showing that the contracted party incurs an effective increase of costs, as well as other documents. Petrobras' analysis over these documents may take much longer than expected, while owners will face

more IR being withheld from January.

In addition to that this law does not offer a steady ground for owners trying to foresee future daily rates either, since this same law says that the Ministry of Finance can change this percentage limit anytime by adding or subtracting up to ten percent of the current 65%.

Even though all competitors will be in the same situation whichever limit is applicable, it may not reflect the reality of the costs share of a foreign vessel (paid directly abroad in dollars to the foreign owner) and would end up having to be compensated by part of the services share that is "neglected" by a set of taxes.

On the new Petrobras tenders, for example the PSV 1500, 3000, 4500 and AHTS 18000, the oil major is not taking a position or imposing limita-

tions of charter or services split portions taking this law in consideration, but is allowing shipowners to freely offer whichever split they feel applicable. This position may give room to different interpretations as well as bring some challenges.

As there is no limitation imposed by Petrobras on the charter portion, the question is will owners feel free to offer up to 99% for that split? Is it better to pay 15% of IR tax over the charter portion exceeding 65% instead of the taxes due over the services portion? Can Petrobras disqualify owners that may not offer according to the new law? Can contenders judge these bids as incorrect, protest and be heard by Petrobras?

It is still too early to see how exactly it will go as the regulation is new and no new tenders for OSVs have been finalized yet, so there is time for further clarification from both Petrobras and authorities. Due the volatility in the Brazilian legislation and taxation system this may not be the last chapter of this contract split limitation. ■

"It is still too early to see how the regulation will go as no new tenders for OSVs have been finalized."

É Isso Aí

Westshore do Brasil Cocktail Party

On December 3rd Westshore do Brasil had the pleasure to host its Cocktail party 2014 at Eça restaurant, in Rio de Janeiro. We are very thankful for the amazing time we had with our friends and customers and for all the great experience and achievements that we shared this year. We hope to keep collaborating with you next year!



Season's Greetings



“Westshore do Brasil would like to wish you all a Merry Christmas and a 2015 full of peace, prosperity and accomplishments”

Brazilian Wave Satisfaction Survey

Brazilian Wave's goal is to offer all readers high quality information and analysis on the Brazilian OSV market, in an accessible format. And so, in order to keep improving, we would like to hear your sincere thoughts on our magazine. Please click on the link below to access our Satisfaction Survey. The responses are completely anonymous and it will only take a couple of minutes. Thank you for your support.

Please click here: <https://www.quicksurveys.com/s/Ta95E>