

## New Regulatory Framework for Gas in Brazil



The new regulatory framework for the natural gas sector was approved this week by the houses of Congress and now goes forward for presidential sanction. Last Tuesday, March 16th, the House of Representatives concluded the analysis of the amendments presented by the Senate to the text previously approved, which is now proceeding to the last stage before the publication of the new law.

The industry, in its majority, considers the new framework as an advance to modernize the business environment and to move towards to a more international model attracting investments to the sector.

### **Legal, economic, social and political scenario**

The new regulatory framework for the natural gas sector is not a new subject under debate in Brazil. It has been part of the government, but there was not an effective advance until 2020.

Currently, the Federal Government is under great pressure to reduce the value of the gas cylinder in one hand, and to open the market to new players on the other hand; so the equation would result in the benefit of the real factors of offer and demand.

In 2019, Petrobras agreed with the Administrative Council for Economic Defense ("CADE"), through the Termination Agreement ("TCC"), to open the Brazilian gas market. At the time, the end of the gas pipeline monopoly was agreed upon, stimulating competition in the sector.

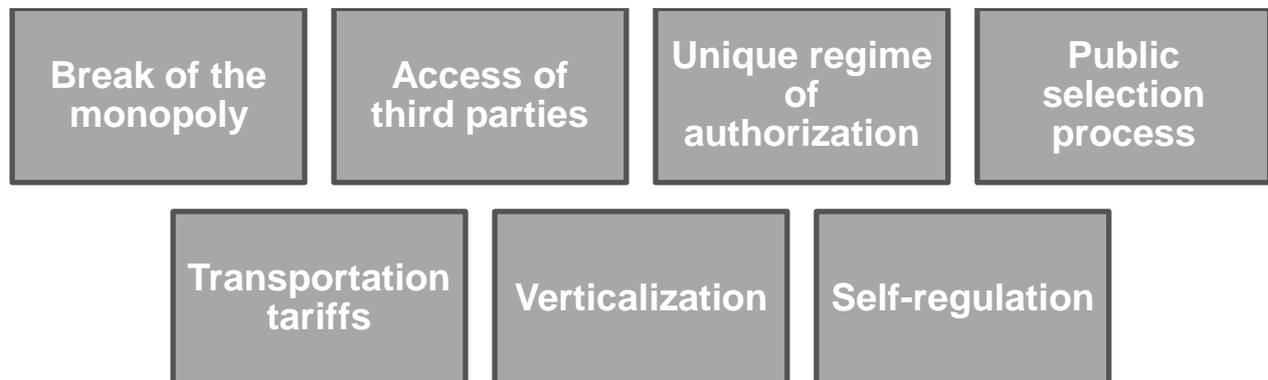
The new regulatory framework intends to break the monopoly – nowadays with Petrobras’ facilities – to attract billionaire investments to the sector, enforcing it to develop and lower the final costs to the consumer. The new law allows the access of new agents in the country and guarantees greater legal security for investments.

In summary, the new text guarantees access to essential infrastructure by market players and the opening of the market.

Also, the change in the concession regime was a point strongly advocated by the sector, since the current model, which determines the concession regime for new gas pipelines, hinders investments and limits the supply of natural gas, since bidding is required. The new framework establishes the regime of authorization, a model practiced worldwide.

## Important changes for the Brazilian natural gas market

With the new regulatory framework for the natural gas sector, we have assessed important changes to the current model practiced. Below are the most significant, mainly related to the opening of the market:



- **Breaks the monopoly** of natural gas production by equating the gas market with the free energy market, in which consumers can choose from whom they will buy the product. The gas distribution company continues to be operated by the state or concessionaire company, but the final product (gas) can be purchased from any other agent in the chain.
- Establishes the **access of third parties** to the gas pipelines and their respective assignment process, as well as delimits negotiated and non-discriminatory access to Liquefied Natural Gas ("LNG") terminals.
- The construction of pipelines will be under the unique regime of **authorization**, no longer under concession – this regime will apply to the construction, expansion, operation, and maintenance of the facilities. The sector's regulatory agency (National Agency for Petroleum, Natural Gas and Biofuels – “ANP” in Brazilian acronym) will have the authority to regulate the qualification of those interested in the authorization.

- If more than one agent is interested, ANP must hold a **public selection process** to choose the most advantageous project. The agency may also, at any time, conduct a selection process to identify carriers interested in the construction or expansion of a gas pipeline, if it is needed.
- Natural gas **transportation tariffs** will be proposed by the transporter and approved by the ANP, after a broad transparency process in public consultation with the sector.
- Establishes the **entry and exit model**, in which companies contract the capacity to inject (entry) and remove gas (exit) from the transportation pipelines. The transportation services will be offered under the entry and exit capacity contracting regime, with the permission for one to be contracted independently of the other.
- The possibilities for **revoking authorization** are: liquidation or bankruptcy; request by the authorized company; deactivation of the facility; or non-compliance with obligations, contracts, and regulations.
- The **verticalization** among the segments – exploration, development, production, importation, loading, and commercialization – is expressly forbidden. Therefore, any direct or indirect corporate relationship of control or coalition among the agents of the production chain is forbidden.
- Proposes **self-regulation** in the market.
- To avoid national shortages, establishes that transporters and shippers must prepare a **contingency plan** for the supply of gas.
- To maintain the national supply, provides that the ANP may **designate** another transporter to operate and maintain the facilities.
- It also allows the company to receive authorization from the ANP to a **underground natural gas stock**, at its own risk.

One of the points of divergence in the sector is the deverticalisation and independence among companies that distribute, transport, and produce natural gas.

On one hand, there is a defense of the competitiveness by keeping the gas supply chain independent, thus avoiding that one group controls all the supply chain necessary for the produced or imported gas to reach the consumer. The government, most associations of producers, transporters, and consumers of natural gas agree upon this.

On the other hand, the counter argument is that the Brazilian market has a limited gas infrastructure concentrated in a few regions and the verticalization of large companies helps to make investments in integrated projects feasible. Thus, it would be easier to expand the gas infrastructure available in the market.

## **Brief considerations on the legislative process and next steps of the new Law**

The original project was presented in 2013, but it only had relevant progress in 2020, when an urgency request for the matter was approved in the House of Representatives. The urgency requirement waives some procedural formalities, which can take the proposition directly to the Plenary, without going through the Committees.

Therefore, the Bill ("PL", in Brazilian Acronym) 6407/2013 was reported by Representative Laercio Oliveira (PP/SE) in the House of Representatives, a strong advocate of competition in the gas market. In September 2020, the Bill was assessed by the Plenary of the House, proceeding to the Reviewing process, in the Senate.

In a quick review by the Senate, PL 6407/2013 was reported by Senator Eduardo Braga (MDB-AM), an experienced Senator and former Minister of Mines and Energy in the second term of Dilma's government. Approved in December 2020, the matter returned to the Initiating House (House of Representatives) so that the amendments to the previously approved text could be considered.

Back in the House of Representatives, the text was definitively approved on March 16, 2021, also under the rapporteur of Representative Laercio Oliveira. In an agreement between parties, including the support of the Administration, all amendments made by the Senate were rejected. This agreement was reached due to the analysis that some points included by the Senate should be subject to future regulation (government decree) and should not be addressed by the Law. Besides of that, there were some insertions related to the electricity sector, which distorted the main purpose of the Law.

Thus, the text previously approved by the House of Representatives last year was sent for presidential sanction.

Now, the President has 15 days to either sanction the legislative proposal or veto it (fully or partially). Otherwise it is not customary for the President's Office to do so, if the 15 days deadline is missed, the consequence is a tacit sanction, i.e., the full original text from Congress will be enacted.

Another possibility is that some provisions may be vetoed at this stage, based on the analysis of the constitutional text or if it is against the public interest.

We expect to have the New Regulatory Framework for Gas published soon, enabling new investments in the sectors and opening up the market in a beneficial way.

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MJ Alves e Burle Advogados e Consultores – Advocacy Brasil (MJAB) is the first Brazilian law firm specialized in Advocacy. The firm advocates for organizations and companies on governmental matters in Brazilian Congress and Administration.

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