

How to counterbalance sanctions? On improving investment climate favourability under external limitations (some lessons from the history)

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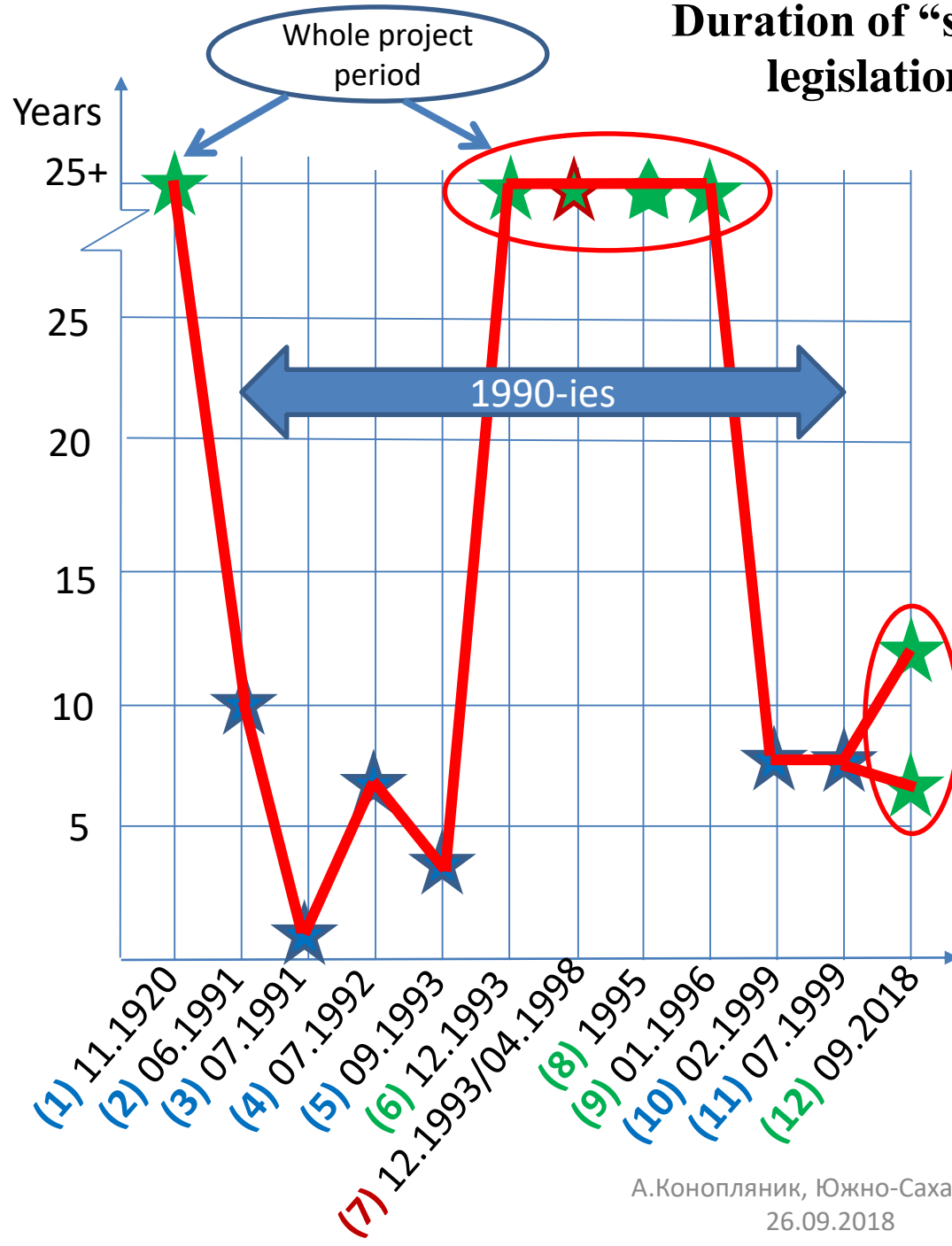
To counterbalance risks of tax fluctuations by legal stability

- How to counterbalance external limitations (sanctions)?
 - Counter-sanctions?
 - Increasing tax & other administrative pressure on domestic/home business?
 - Or to (compensatory) increase favourability of internal investment climate to expand pre-tax (taxable) base?
- Recent initiatives of the State aimed at retroactive confiscation of windfall profits of the companies who earned them in result of Rouble devaluation (so-called “devaluation profits” considered not to be “earned”) – seems to be element of the second route?:
 - September 2015: “Siluanov’s sickle” (ac. to K.Simonov) – regarding Oil & Gas companies => did not pass...
 - August 2018: “Belousov’s letter” – the same in regard to the companies beyond raw-material sector (to confiscate 500+ bln Rb from 14 companies; this time Siluanov did not support/ TV 12.09) =>
 - In result: draft law by Finance Ministry on Investment Protection & Stimulation Agreements (IPSA)

Finance Ministry draft law & stabilization clause

- Transformation of “tax confiscation” into self-imposed compulsory exchange: “conversion of accrued – and not paid - incremental taxes into investments” (list of projects is being prepared) +
- + state guarantees of stable conditions for their implementation (to counterbalance risks of tax fluctuations by legal stability) =>
- Finance Ministry draft law : standard agreement between Russian State and an Investor with the guarantees of stable conditions for implementation of his investments (Investment Protection & Stimulation Agreements - IPSA) =>
- Differentiated “stabilization clause” :
 - With CAPEX 3 bln RB and above Investor is guaranteed with stable tax and regulatory conditions for 6 years,
 - With possibility to extend “stabilization period” for another 6 years in case he will reinvest profits from the project in Russia,
 - With CAPEX 30 bln. Rb and above – for 12 years.
 - And dispute settlement procedures within civil law.
- The step in right direction (re stability). A necessary one. But whether it is enough?

Duration of “stabilization clauses” in Russian legislation through different periods



- (1) Lenin’s Decree on concessions (11.1920)
- (2) USSR Fundamentals of legislation on foreign Investments (06.1991)
- (3) Law on foreign investments in RSFSR (07.1991)
- (4) RF Gov’t Ordinance №1375 on JVs (07.1992)
- (5) RF Presidential Decree №1466 on work improvement with foreign investments (09.1993)
- (6) RF Presidential Decree №2285 on PSAs in subsoil use (12.1993)
- (7) Energy Charter Treaty (12.1993 / 04.1998)
- (8) Draft law on concessions (2nd version) (1995)
- (9) PSA Law (01.1996)
- (10) Law on investment activities in RF in the form of CAPEX (02.1999)
- (11) Law on foreign investments in RF (07.1999)
- (12) Draft law on investment protection & stimulation in RF (09.2018)

А.Конопляник, Южно-Сахалинск,
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-  International law
-  Public law
-  Civil law

This author's historical proposal: possible composition of investment regimes (investment matrix/menu) for Russian subsoil use (within "legal stability" - "tax favorability" axes)

1997: companies expressed willingness for 250 PSA projects in Russia (RF State Duma survey)

Key idea: to create competition between investment regimes for investor

General route for improvement investment attractiveness of Russian subsoil use

		Legal system	
		Administrative (public)	Civil
Tax treatment	General (common)	Licenses	Concessions
	Special (incl. individualized)	Licenses with allowances (differentiated licensing regime)	PSAs

Prirazlomnoye & Sakhalin-2 (1st phase) projects: Similar natural conditions & development technologies

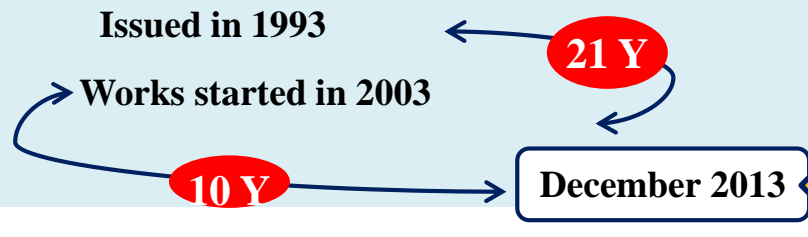
Parameters	Prirazlomnoye	Sakhalin-2 (1 st phase)
Location	Pechora Sea	Sakhalin offshore
Water depth	19-20 m	32 m
Distance from shore	60 km	16 km
Minimal temperature	Minus 48 degree Celsius	Minus 42-44 degree Celsius
Ice conditions	9-10 grades	9-10 grades
“Weather window” (no ice)	4 months	6 months
Platform: stationary gravity (artificial island)	Metal caisson 126x126m (produced in Severodvinsk)	Metal caisson 111x111m (produced in Komsomolsk-on-Amur)
Upper base (from secondary market)	Was first used in non-ice conditions (Hutton, UK North Sea), in result 90% modernization, cost overrun etc.	Was first used in ice conditions (Beaufort Sea), modernized in S.Korea
Number of well-slots	36	32

Source: А.Конопляник, Ю.Попова, Н.Трошина. «Двадцать лет топтания на месте. Преимущества Закона «О СРП», принятого 20 лет назад, так и не были востребованы в России». // «Нефть России», сентябрь 2016, №9, с.4-10 (часть 1); октябрь 2016, №10, с. 4-10 (часть 2).

Prirazlomnoye & Sakhalin-2 (1st phase) projects: different economic results

Prirazlomnoye field

License



One Russian company

Multiple attempts to create consortiums with foreign participation (to involve strategic & financial investors) failed

“Sakhalin-2” (1st phase): Piltun-Astokhskoye field

PSA



Consortium (combining competences)

Initially consortium of only foreign companies

In 2006 Gazprom entered (non-amicable merger), “learning curve” for Gazprom

Internal conflict of interests

Long internal conflict of interests inside Rosshelf (producers vs consumers of equipment, companies w/o experience of offshore E&P & w/o experience of producing equipment for offshore E&P)

Conflict of interests within consortium of foreign companies... (producers vs consumers of equipment, struggle for operatorship)

...was quickly & effectively settled

Long fight for tax concessions under licensing regime = **key obstacle/deterrent in project preparation for implementation**

Clear & predictable project economics & its stable legal base, fixed in/by PSA = **key trigger for quick & effective project preparation for implementation**

Reserve slides

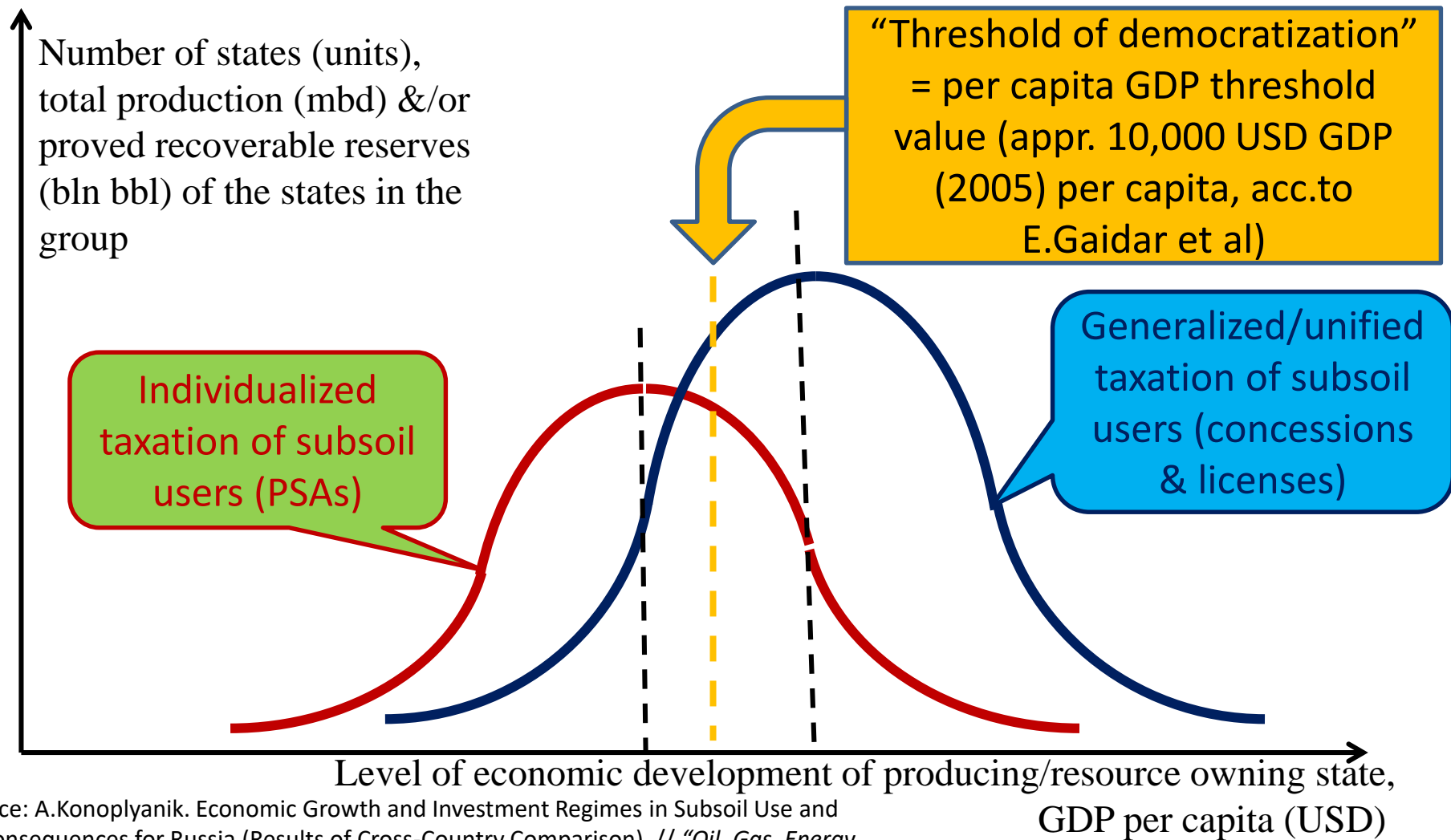
Summarized Data for Applied Regimes of Subsoil Use Worldwide, 2003 and 2009

-	2003		2009	
Number of analyzed countries, including	180		177	
countries that run commercial oil production, including those applying the subsoil regime of:		91		104
- tax plus royalty	113	45	111	55
- PSA	54	34	55	38
- both	13	12	11	11

Calculated using data of the Association of International Petroleum Negotiators (AIPN) and Barrows Co kindly furnished to the author by Mr. Gordon Barrows

Source: А.Конопляник. Средство от «правового вакуума». Уровень экономического и правового развития государства определяет выбор инвестиционных режимов в недропользовании. – «Нефть России», 2012, № 8, с.20-24; № 9, с.26-29, № 10, с.16-23.

Basic author's hypothesis (proved by calculations) – probable distribution of individualized & generalized tax systems of subsoil use worldwide dependent on the level of economic development of producing/resource owning state



Source: A.Konoplyanik. Economic Growth and Investment Regimes in Subsoil Use and its consequences for Russia (Results of Cross-Country Comparison). // “Oil, Gas, Energy Law Intelligence” (OGEL), July 2015, vol.13, Issue 4

Thank you for your attention!

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