

**Vietnam's Petroleum Sector:
Technical Assistance for the Revision of the
Existing Legal and Regulatory Framework**

December 2003

Joint UNDP/World Bank Energy Sector Management Assistance Programme
(ESMAP)

Contents

Acknowledgments	vii
Abbreviations and Acronyms	ix
Units of Measure	ix
Preface	xi
Executive Summary.....	1
1. Vietnam's Upstream Oil and Gas Sector.....	7
Oil Production.....	7
Gas Production	7
Gas Transmission.....	8
Exploration in Vietnam	8
2. Structure of Petroleum Legal and Regulatory Regimes – International Experience.....	11
Petroleum Law – Best Practice	12
State Property in Petroleum.....	13
Competent Authority	13
Conduct of Petroleum Operations	14
Petroleum Agreements	14
Regulations	15
Qualifications, Duties, and Rights of Rights Holder or Contractor.....	15
Taxation of Profits	16
Other Taxes, Duties, and Exchange Controls	16
Fiscal Stabilization	16
Environmental and Social Assessments	17
Natural Gas Development	17
Decrees/Regulations.....	18
Competent Authority	18
Petroleum Licensing	18
Petroleum Operations	18
Petroleum Agreements	19

	Fiscal and Financial Regime.....	19
	Assignment of rights	19
	Land use.....	19
	Environmental and Social Protection	20
	Model Contract.....	20
3.	Major Recommendations	21
	Project Objective.....	21
	Recommendations	21
	Major Recommendation 1: Make Fiscal Terms Simpler and More Competitive ..22	
	General Concept of Simplifying Fiscal Terms	22
	Increase the Cost Recovery Limit.....	23
	Competing Countries	23
	Price Movements	23
	Shallow Water Areas and Profitable Fields	24
	Competitive Corporate Income Tax.....	24
	Competitive Tax Rate	24
	Removal of Ring Fencing	25
	International Practice.....	25
	Exploration Incentive.....	26
	Status of Recommendations Regarding a Simpler Fiscal System	26
	The Cost Recovery Limit	26
	Competitive Corporate Income Tax.....	27
	Ring Fencing.....	27
	Major Recommendation 2: Make the Production-Sharing Contract the Principal Form of Petroleum Contract.....	27
	Joint Ventures in the Petroleum Industry	28
	Status of Recommendations Regarding the Production-Sharing Contract.....	29
	Major Recommendation 3: Facilitate Gas Marketing Opportunities	29
	Status of Recommendations Regarding Facilitating Gas Marketing Opportunities	30
	Major Recommendation 4: Separate Regulatory Functions: Policy, Regulatory, and Petroleum Rights Management	30

Introduction	30
Recommendation: Establishment of SPMA	32
Status of Recommendations Regarding Separation of Regulatory Functions.....	32
Major Recommendation 5: Use a Simpler Bidding Process.....	33
Role of SPMA in the Bidding Process.....	33
Bidding on Work Units	33
Bidding Modes	34
Bidding Criteria.....	34
Status of Recommendations Regarding Simpler Bidding Process.....	34
Major Recommendation 6: Consider Price- and Production-Sensitive Royalties.....	35
Royalties for Crude Oil and Natural Gas	35
Status of Recommendations Regarding Price- and Production-Sensitive Royalties.....	35
4. Other Recommendations	37
5. Conclusions and Next Steps for Vietnam's Upstream Petroleum Regime ...	39
Conclusions.....	39
Next Steps.....	40
Model Contract.....	40
Downstream Gas Regime.....	40
Appendix A: Steering Committee and Working Group Members and Members of the Project Team.....	43
Appendix B: International Practice Regarding Consolidation of Corporate Income Tax.....	45
Appendix C: Separation of Regulatory Functions.....	47
Appendix D: Proposal for Price- and Production-Sensitive Oil and Gas Royalties.....	51
Appendix E: Work Units—An Example	61
Annex 1: Revised Petroleum Law (Unofficial Translation).....	65
General Provisions.....	65
Annex 2: Revised Petroleum Decree (Unofficial Translation).....	77
Annex 3: Prime Minister's Decision No. 216 of 7 November 1998.....	99
List of Figures:	
Figure 1.1: Exploration in Vietnam, 1989 - 2001.....	9

List of Tables :

Table C.2: Petroleum Rights Management	48
Table C.3: Technical Regulation	49
Table C.4: Fiscal Terms and Financial Monitoring.....	50
Table D.1: Production Royalty - Oil	52
Table D.2: Price Royalty - Oil	52
Table D.3: Production Royalty - Gas	53
Table D4: Price Royalty - Gas	53
Table D.5a: Overview of Competitive Situation of Vietnam, Rate of Return Based on Constant 1998 Dollars – Oil	56
Table D.5b: Overview of Competitive Situation of Vietnam, Rate of Return Based on Constant 1998 Dollars - Gas	57
Table D.6a: Overview of Competitive Situation of Vietnam, Undiscounted Government Take in Constant 1998 Dollars (Includes Participation) - Oil.....	58
Table D.6b: Overview of Competitive Situation of Vietnam, Undiscounted Government Take in Constant 1998 Dollars (Includes Participation) - Gas	59
Table D.7: Profit Oil Rates	60
Table D.8: Profit Gas Rates.....	60

Acknowledgments

This report was prepared by the ESMAP project team under the guidance of Bent Svensson. The project team was comprised of Bent Svensson (team leader); Anil Malhotra, Nguyet Anh Pham; and William T. Onorato (all World Bank), Pedro van Meurs (Van Meurs & Associates, Ltd.), and Jay Park (Macleod Dixon), consultants. Ms. Esther Petrilli from COCPO provided desktop support while Ms. Marjorie K. Araya from ESMAP supervised the printing, distribution and dissemination of this report.

Abbreviations and Acronyms

EMV	Risk adjusted rate of return
ESMAP	Joint UNDP/World Bank Energy Sector Management Assistance Programme
EVN	Electricity of Vietnam
MOF	Ministry of Finance
MOSTE	Ministry of Science, Technology, and Environment
MPI	Ministry of Planning and Investment
NOC	National oil company
OGSMB	Oil and Gas State Management Body
ONGC	Oil and Natural Gas Corporation (India)
OOG	Office of Government
PVN	PetroVietnam
SPMA	State Petroleum Management Authority
VAT	Value-added tax

Units of Measure

Bcm	Billion cubic meters
Bopd	Barrels of oil per day
Mcf	Thousand cubic feet
Mmbtu	Million British thermal units
Tcf	Trillion cubic feet

Preface

At the request of the government of the Socialist Republic of Vietnam, the World Bank and the Energy Sector Management Assistance Program (ESMAP) have provided advice on a number of issues in the petroleum sector.

In late 1998, international oil prices fell to their lowest level in a decade and the government of Vietnam and PetroVietnam requested technical assistance from ESMAP to evaluate the upstream petroleum fiscal system and compare its competitiveness with that of other countries to analyze whether Vietnam's oil contracts are following international best practice. The request also included an evaluation of options for more flexible gas terms in production-sharing contracts and fiscal incentives for oil and gas development of economically marginal fields. The analyses were prepared in 1999 and later published under the title Petroleum Fiscal Systems and Policies for Fluctuating Oil Prices in Vietnam (February 2001).

A rebound in international oil prices resolved the issues specifically related to oil prices, but the government intended to modernize its Petroleum Law to make it a modern legal framework for petroleum activities and to attract investments in the sector. To address these issues, a decision by the prime minister on June 14, 1999, established a steering committee and a working group for revision and supplementation of the Petroleum Law.

The Office of the Government requested technical assistance from ESMAP for revision of the Petroleum Law. The current report summarizes recommended revisions to Vietnam's petroleum legal and regulatory framework under the project "Technical Assistance for the Revision of the Existing Legal and Regulatory Framework for Vietnam's Petroleum Sector."

The work on the Petroleum Law and its related Decree took place from October 1999 to September 2000. The amendments to the Petroleum Law were passed in June 2000. The Revised Petroleum Decree was passed in September 2000.

The project team made recommendations Vietnam's petroleum regime into a stable legal and regulatory framework for the petroleum sector, one that would attract investment in exploration and development of hydrocarbons in an environment of increasing competition for scarce investment resources. The recommendations are based on international best practice that has been successfully employed in other countries.

The recommendations are described in detail in this report. The report also describes the extent to which the recommendations were adopted by the government of Vietnam in the Revised Petroleum Law and Revised Petroleum Decree that were enacted in 2000 and outlines the next steps that Vietnam should take to meet its goal of establishing a stable

legal and regulatory framework for the petroleum sector that will attract investment in exploration and development of hydrocarbons.

Following the revision of the Petroleum Law, a project under separate funding has assisted the government of Vietnam in the development of a regulatory framework for the downstream gas sector in 2001 and 2002. There is currently no regulatory framework or law in place for regulation of the downstream gas sector in Vietnam. A separate report will describe this work.

Members of the Steering Committee, Working Group and the project team are listed in Appendix A. Mission members have expressed their appreciation for the cooperation, assistance, and hospitality provided by the Oil and Gas Department at the Office of the Government, the Steering Committee and Working Group for Revision and Supplement of the Petroleum Law, and all participating agencies during the course of these missions.

Executive Summary

1. The oil and gas potential of Vietnam's continental shelf remains relatively unexplored compared with that of its neighbors, including China, Indonesia, Malaysia, and Thailand. A number of factors affect the decision to undertake petroleum investments: geology, geography, geopolitics, and investment climate. Host governments cannot control the first three factors. However, they do control the investment climate, and the legal and contractual framework and the petroleum fiscal system are key factors to be considered in the competition among governments for access to investment capital.

2. Despite intense efforts to attract international oil companies to explore the country's sedimentary basins, including incentive terms contained in a 1998 decision of the prime minister, drilling activity has remained modest in recent years. The government requested technical assistance from ESMAP for revision of its petroleum legal regime so that it might become a modern legal and regulatory framework for the petroleum sector and attract foreign investment to develop its hydrocarbon reserves.¹

3. The project team evaluated and identified international best practice in the areas of petroleum regimes to develop its recommendations to Vietnam. They recommended strengthening of the legal, regulatory, and contractual framework based on three cornerstones: the Petroleum Law, the Regulations (or, as they are called in Vietnam, the Decrees), and a Model Contract based on production-sharing agreements. Recommendations were provided to the government of Vietnam in a series of meetings, workshops, and reports.

4. Some of these recommendations were adopted in the amendments to the Petroleum Law of Vietnam that were passed on June 9, 2000 (the Petroleum Law of Vietnam, as so amended, is referred to as the Revised Petroleum Law). Others were adopted in the Revised Petroleum Decree of September 2000. A translation of the Revised Petroleum Law is attached as Annex 1, and a translation of the Revised Petroleum Decree is attached as Annex 2.

5. The major recommendations made by The project team to the government of Vietnam can be grouped under six headings:

1. Make fiscal terms simpler and more competitive.
2. Make the production-sharing contract the principal form of petroleum contract.
3. Facilitate gas marketing opportunities.
4. Separate regulatory functions: policy, regulatory, and petroleum rights management.
5. Use a simpler bidding process.

¹ A decision by the prime minister of Vietnam on June 14, 1999, established a steering committee and a working group for revision and supplementation of Vietnam's Petroleum Law.

6. Consider price- and production-sensitive royalties.

Following is a brief explanation of each of these recommendations and the treatment of these recommendations under the Revised Petroleum Law and the Revised Petroleum Decree.

Make Fiscal Terms Simpler and More Competitive

6. In Vietnam, awarding a petroleum contract takes considerable time. This is a significant disincentive to foreign investment in the Vietnamese petroleum sector. The acreage award process is because too many of the fiscal terms are open for negotiation. The project team recommended simplifying the fiscal terms. Simplification can best be achieved by fixing most of the provisions in the Petroleum Law and the Petroleum Decree and making them nonnegotiable. It also recommended making only the "profit oil" and the "profit gas" share a negotiable item, although it would be possible to negotiate on two or three fiscal factors without making the petroleum fiscal regime unduly complicated.

7. For the nonnegotiable items, the project team recommended that the cost recovery limit of 70 percent be applied to all petroleum contracts entered into by the government of Vietnam. This would make Vietnam's regime competitive with those of its neighbors and permit petroleum development to occur under a wider range of petroleum prices. A more competitive corporate income tax was also recommended for petroleum activities, including the reduction of Vietnam's 50 percent rate to the international average of approximately 32 percent. The Petroleum Law should also be adjusted to make all petroleum contracts subject to the corporate income tax law of general application. Finally, it was recommended that Vietnam's corporate income tax not be determined on a "ring-fenced" basis; rather, tax should be calculated on a consolidated basis, as is the case in most other countries.

8. The first two recommendations were adopted by the government of Vietnam in the Revised Petroleum Law and the Revised Petroleum Decree, although with some variations that permit their discretionary application by the government. The recommendation regarding calculation of income tax on a consolidated basis was not adopted.

Make the Production-Sharing Contract the Principal Form of Petroleum Contract

9. Currently, Vietnam has signed 37 production-sharing contracts, which is the most commonly used form of contract with foreign investors (an exception is the Bach Ho [White Tiger] joint venture contract). The project team recommended that Vietnam make production-sharing contracts the principal form of petroleum contract, rather than joint ventures, joint operating companies, or other possible arrangements.

Facilitate Gas Marketing Opportunities

10. The project team recommended that Vietnam adopt a retention period of 10 years for significant natural gas discoveries. This would permit companies to build exploration programs aimed at building gas reserves in case gas was found and would increase the attractiveness of exploration. It would also be consistent with modern international practice for petroleum regimes.

11. In the Revised Petroleum Law, the government of Vietnam adopted a barely adequate maximum extension period of seven years for significant natural gas discoveries. The government also reserved the discretion to shorten this period if the contractor is not pursuing development in a manner satisfactory to the government.

Separate Regulatory Functions

12. The project team recommended that the regulatory functions for Vietnam's petroleum regime be divided into three parts: policy functions, regulatory functions, and petroleum rights management functions. It was recommended that as prescribed in the Petroleum Law, the state petroleum management authority should be established in accordance with the Law on the Organization of the Government to assume the state management of petroleum operations, which includes these functions. It was also recommended that an agency be established to perform the regulatory and petroleum rights management functions and that the government continues to perform the policy functions. These recommendations would mean that PetroVietnam's function would be to manage and administer its business relationships with foreign investors under its petroleum contracts.

13. The Revised Petroleum Decree contains provisions that provide further details regarding the establishment of a state body for the management of the petroleum sector: the Oil and Gas State Management Body (OGSMB) to perform technical regulation of the petroleum regime and to act as a secretariat to the prime minister and the Ministry of Planning and Investment in connection with petroleum rights management and policy matters.

Use a Simpler Bidding Process

14. The project team recommended that the bidding for petroleum contracts in Vietnam occur through a competitive bidding process that uses a single bidding criterion. It was also recommended that Vietnam adopt the concept of bidding on the basis of work units, which is being used increasingly in other countries.

15. A Draft Bidding Decree that the mission reviewed contained some movement toward international competitive bidding and reduced the number of bidding criteria, but still left some discretion to the authorities.

16. The government has indicated that it prefers production-sharing contracts, but neither the Revised Petroleum Law nor the Revised Petroleum Decree makes this

preference clear. It is recommended that the government develop a single Model Contract, a production-sharing contract, for use in future bidding rounds.

Put in Place Price- and Production-Sensitive Royalties

17. Vietnam's royalties are not price-sensitive, which can discourage the development of small fields. The project team recommended that Vietnam make its royalties sensitive to price and production. This would enhance petroleum economics for smaller fields and in periods of low-price environments. This recommendation was not adopted in the Revised Petroleum Law or the Revised Petroleum Decree.

Other Recommendations

18. The project team made a number of minor recommendations to the government of Vietnam in the course of the development of the Revised Petroleum Law and the Revised Petroleum Decree, some of which were adopted.

Conclusions and Next Steps

19. The project team recommended that its major suggested changes appear in the Petroleum Law in order to establish petroleum development incentives with the greatest degree of certainty. However, some of the changes were not accepted as part of the revision to the Petroleum Law. The project team then urged the inclusion of provisions adopting these recommendations in the Petroleum Decree, where possible.

20. Where these changes were not adopted in the Petroleum Decree, the option remains that some can be adopted when Vietnam commences the preparation of the Model Contract implementing the Revised Petroleum Law and the Revised Petroleum Decree. In many cases the recommendations were adopted in a manner that continues to allow the government of Vietnam administrative discretion on whether the recommendations will be implemented in specific cases. This may result in a failure to establish a more transparent system with a sufficient degree of comfort and certainty on the part of international investors in the improvement of Vietnam's petroleum regime. Some of that uncertainty could be eliminated by the establishment of a Model Contract that would be the basis for the bidding of petroleum contract awards. The government of Vietnam has not yet commenced the preparation of a Model Contract. This is the next step in developing a modern legal framework in Vietnam to encourage upstream petroleum activities and to attract investments in the sector.

21. The project team pointed out that the total fiscal package as reflected in the Revised Petroleum Law and the Revised Petroleum Decree is not materially better than, and in certain respects is inferior to, that of Decision 216 of the prime minister (Annex 3). From November 1998, when Decision 216 was put into effect, until the Revised Petroleum Law passed in June 2000, no petroleum contracts had been signed under its incentive terms. Although there has been an increase in 2000 and 2001, The project team is concerned that the fiscal revisions contained in the Revised Petroleum Law and the Revised Petroleum Decree will not be sufficient to attract sustained

investment in oil and gas exploration and production. If it is Vietnam's goal to obtain additional investment in oil and gas exploration, then the remaining features of Vietnam's petroleum regime must contain real and substantive improvements.

22. Another important step in the development of Vietnam's petroleum regime would be the creation of a legal and regulatory framework for downstream gas transmission and gas distribution in Vietnam. As the government of Vietnam undertakes the first major gas utilization program based on private investment in infrastructure and gas supplies from its offshore sector, there is a need to create the framework for private participation in the transmission and distribution of gas to industrial parks, industries, and commercial customers as well as power plants. An added benefit of encouraging gas development is that the resulting interest in gas exploration and development in Vietnam may lead to the discovery of additional crude oil reserves. The government of Vietnam is currently pursuing the establishment of a legal and regulatory framework for gas transmission and distribution, and this effort is to be encouraged.

1

Vietnam's Upstream Oil and Gas Sector

1.1 The oil and gas potential of Vietnam's continental shelf remains relatively unexplored compared with that of its neighbors, including China, Indonesia, Malaysia, and Thailand. PetroVietnam, the state oil company of Vietnam, has made intense efforts to attract international oil companies to explore the country's sedimentary basins, but drilling activity has remained modest, despite recent efforts by the government of Vietnam to create further incentives for the exploration of petroleum in the country. Vietnam's oil and gas resources can help attract foreign investment and meet future energy demand. Crude oil exports are already the country's largest foreign exchange earner, and natural gas reserves provide an environmentally clean way to meet domestic energy needs and could lead to exports.

Oil Production

1.2 Most hydrocarbon production in Vietnam comes from the Bach Ho (White Tiger) field, which is operated by Vietsovpetro. Other sources of oil production in the Cuu Long Basin are the Rang Dong, Rong, and Ruby fields; Dai Hung in the Nam Con Son Basin; and a small structure in the southwest continental shelf basin. Bach Ho was brought onstream in 1986 and is 120 kilometers offshore. Oil production in Vietnam in 2002 was an average of 342,000 barrels per day, with 1.5 billion cubic meters (bcm) of associated gas per year.

Gas Production

1.3 Production from the Lan Tay and Lan Do fields in the Nam Con Son Basin started in late 2002. An average production of 2.7 bcm per year is planned from these fields. This first gas development will be governed by contracts between the producers (BP, PetroVietnam, and ONGC) and the main buyer of gas, EVN (the state company, Electricity of Vietnam), and the government. More gas discoveries have been made both in the same basin and in the offshore area southwest of the Ca Mau province, and there are plans to expand the gas market. A distribution pipeline to Ho Chi Minh City

is also planned. As most of the gas discoveries are still at an early stage of appraisal, there is uncertainty in the resource estimates².

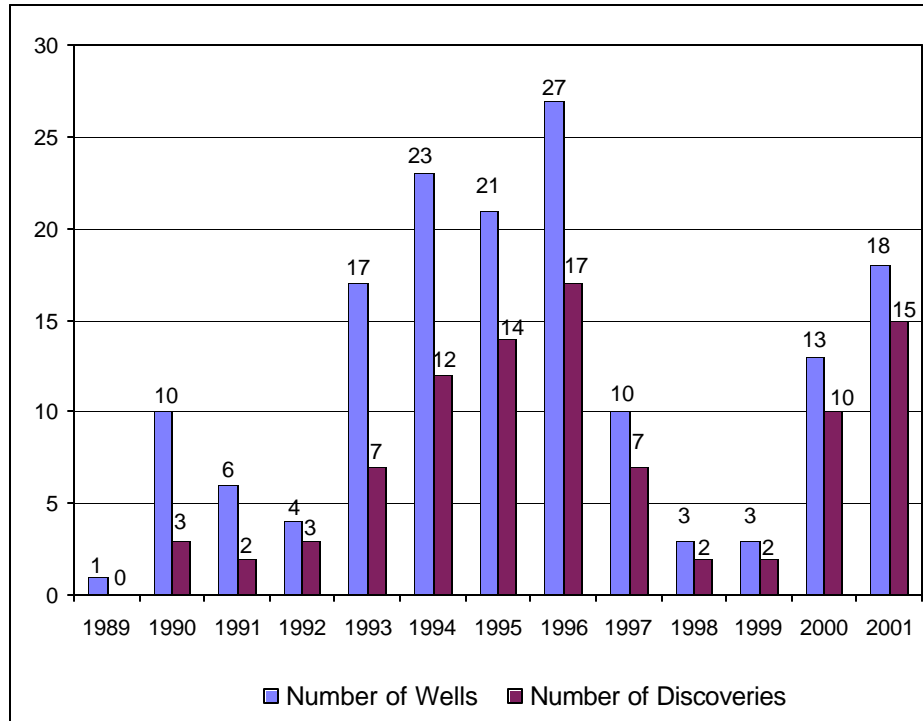
Gas Transmission

1.4 The existing gas pipelines consist of the Bach Ho pipeline, owned by PetroVietnam, with a transportation capacity of 2 bcm/year, to deliver associated gas from the Bach Ho field for power generation. Another pipeline, with a transportation capacity of 1.5 bcm/year, started to transmit associated gas from Rang Dong field to Bach Ho in 2002. Gas in excess of the pipeline capacity from the field and satellite fields is being flared. The 370-kilometer offshore Nam Con Son pipeline was commissioned in late 2002 to transport the gas from the Nam Con Son fields to the Phu My area 30 kilometers from the landing point, where a gas distribution center will deliver the gas to a number of power stations and a fertilizer plant. PetroVietnam is the primary owner of the pipeline transporting the gas onshore (PetroVietnam 51 percent, BP 33 percent, and ConocoPhillips 16 percent), which is defined as a regional pipeline, meaning that there is third-party access to excess capacity.

Exploration in Vietnam

1.5 Vietnam has signed 37 production-sharing contracts, seven joint operating/joint venture contracts, and one business corporation contract in total. Currently, 19 contracts are in operation. In recent years, the number of additional signed petroleum contracts has declined.

² Vietnam's total natural gas reserves are estimated to be 417 bcm (*Fuelling Vietnam's Development: New Challenges for the Energy Sector* World Bank, 1998).

Figure 1.1: Exploration in Vietnam, 1989 - 2001

1.6 The chart shows a declining trend in exploration from 1996 to 1999. Although some recovery took place in 2000 and 2001 when oil prices recovered from a low in 1998-99, the chart highlights the need to evaluate the legal and contractual framework and fiscal terms for oil and gas exploration and production. A number of factors affect the decision process that investors undertake in petroleum investments: geology, geography, geopolitics, and investment climate. Host governments cannot control the first three factors. However, they do control the investment climate, and the legal and contractual framework and the petroleum fiscal system are key factors in the competition among governments for access to investment capital. Therefore, to fulfill the promise of its oil and gas resources, Vietnam must provide the right framework for private sector development. Fiscal incentives—such as acceptable fiscal terms in production-sharing contracts—are needed to encourage hydrocarbon exploration and production. A strong contractual framework and an efficient, transparent system to oversee contracts and award acreage for exploration are needed. Gas pricing policy must be made clear and consistent, and it must include special provision for marginal fields.

1.7 When considering investing in Vietnam, international oil companies compare investment in that country with opportunities worldwide. In the case of natural gas which is dependent on regional and local markets, particular comparison may be made with investments in other Southeast Asian countries. Although some of these countries have much larger gas reserves and markets, Vietnam will still be able to attract investment for gas developments if the investment climate is right.

1.8 Still, Vietnam needs to develop competitive policies and fiscal terms to make itself attractive relative to countries with similar investment opportunities. To that end, in November 1998 the government announced Decision 216 of the prime minister, which improved fiscal incentives—including tax breaks—to encourage foreign investments in exploration in high-cost and technologically difficult areas.

1.9 An earlier report made the following conclusions about Vietnam's typical contractual terms³:

- Vietnam deals effectively with variations in economic conditions resulting from water depth.
- Vietnam deals ineffectively with field sizes, essentially creating a situation where small fields remain uneconomical.
- Vietnam does not deal specifically with variations in economic conditions.
- Vietnam deals well with high oil prices but does not deal effectively with low oil prices, so oil fields quickly become uneconomical when oil prices are low.

³ *Petroleum Fiscal Issues and Policies for Fluctuating Oil Prices in Vietnam*, ESMAP Report no. 236/01, February 2001.

2

Structure of Petroleum Legal and Regulatory Regimes – International Experience

2.1 Since the 1980s Vietnam has developed a variety of contractual models to explore and develop its petroleum resources. The first concept was a joint venture on the basis of which the Vietsovpetro agreement was established. PetroVietnam then developed standard terms for production-sharing contracts. Under such contracts the corporate income tax and other taxes are covered by PetroVietnam's share of profit oil and profit gas—that is, PetroVietnam pays the taxes on behalf of the contractor under such "tax-included" contracts. These contracts are negotiated individually, so contract terms vary. The 1993 Petroleum Law requires contractors to pay certain taxes and royalties. The terms for contracts negotiated under this Law are similar to those for tax-included contracts. With the breakout of the taxes, PetroVietnam's share of profit oil and profit gas was reduced to achieve the same government take. Taxes are calculated on a ring-fenced basis—that is, separately for each contract, even in cases where a contractor has several contracts—in the same manner as the profit oil share.

2.2 Most production-sharing agreements in Vietnam were formulated with a view toward exploring and developing oil production, and in most cases they do not adequately address natural gas production. Gas clauses are negotiated every time a new field goes onstream. The long-term development of the gas industry will be slowed if lengthy negotiations are needed every time a new field goes onstream, and investors will demand higher returns because of the uncertainty.

2.3 The main purposes of a petroleum legislative framework are to provide the basic context for and the rules governing petroleum operations in the host country; to regulate them as they are carried out by domestic, foreign, and international enterprises; and to define the principal administrative, economic, and fiscal guidelines for investment activity in the sector. The three essential elements of such a framework are the Petroleum Law, the Regulations (or, as they are called in Vietnam, the Decrees), and the Model Contract.

2.4 Vietnam's preexisting petroleum legislative regime contains two of the three necessary components. Vietnam's Petroleum Law was introduced in July 1993. It contains the legislative provisions granting petroleum rights, establishing royalty and

participation rights, and regulating activities in the petroleum sector. It also proposes the existence of Decrees and Model Contracts that contain more detail regarding the exploration and production of petroleum. Vietnam passed a Petroleum Decree in December 1996 that implements the provisions of the Petroleum Law of 1993. However, no Model Contract has been established yet, although a number of drafts exist. Finally, some aspects of Vietnam's petroleum regime are contained in a decision of the prime minister, Decision 216, dated November 7, 1998, which establishes fiscal and commercial terms for certain incentive blocks.

2.5 This chapter draws on international best practice and experience and argues that the cornerstone of effective petroleum legislative frameworks for exploration and production operations is a short but thorough, broad, generic Petroleum Law, complemented by enabling decrees and one or several variants of a Model Contract. Such frameworks provide both the host government and international oil company investors with a clear legal and contractual context within which to negotiate exploration and production arrangements that are mutually advantageous and develop the petroleum resources of the host government. In addition to the Petroleum Law, the Regulations, and the Model Contract(s), the fiscal and tax aspects of a complete petroleum legislative framework may either be detailed in the Petroleum Law itself or be separately set out in tax legislation. Other legislation pertaining to matters such as foreign investment is also part of the relevant legal and regulatory regime.

Petroleum Law – Best Practice

2.6 The core rationale behind the preference for a brief but thorough Petroleum Law is that it is meant to cover all essential concepts required in a modern, enabling Petroleum Law while not "setting them in concrete" through an unnecessary level of detail. In this legislative scheme, such detail is reserved for subsidiary instruments such as the enabling Decrees or Regulations and the Model Contract, which should not be required to be submitted to the legislature for amendment or change.

2.7 In addition, the best approach, whenever possible, is to package the legal, contractual, and fiscal regime for petroleum operations into a self-contained, coherent legislative framework consistent with the overall legal system of the host government and with any applicable principles of international law. This is a great incentive to attracting significant foreign investment into the sector. Where an international oil company is studying potential exploration and production investments in candidate countries, given relatively equal petroleum prospectivity, it will normally opt for the state that already has such a coherent regime in place for petroleum operations. International oil companies prefer such a coherent regime over a patchy legislative framework that requires piecing together provisions from the Petroleum Law and other necessarily related and relevant laws, such as those on foreign investment, taxation, land use, and the environment.

2.8 The essential elements of a recommended Petroleum Law format include provisions that address all of the following elements (2.9–2.26).

State Property in Petroleum

2.9 Through this provision the state asserts and confirms that all petroleum lying within its jurisdiction, both onshore and offshore—including offshore areas where it exercises exclusive economic interest over such resources—is the exclusive property of the state. Any provisions to the contrary in other laws or rights granted or vested thereunder in derogation of same are expressly superseded by this provision in the Petroleum Law. This approach is completely consistent with applicable international standards and established practice on the topic.

Competent Authority

2.10 The Petroleum Law should clearly identify a single government agency (or Competent Authority, which is the term used in this report) vested with the exclusive mandate to implement government policy in this area of petroleum development. The Competent Authority represents the state in negotiating and contracting with foreign investors and in regulating and administering, from a technical compliance viewpoint, the implementation of contracts once they have been signed. Ideally, the Competent Authority should be named in the Petroleum Law, so that potential investors will know who will be their single point of contact with the government. This body usually has responsibility for administration and regulation of petroleum exploration, development, and production. However, policy-setting functions remain the responsibility of the government or the relevant ministry.

2.11 Often, however, the state of petroleum development in a given host country will produce variants of this basic approach. This is particularly true at the extreme ends of the scale, where the host country is either a developed petroleum province or a neophyte to the sector. In the former case, it is likely that the state has already created a national oil company (NOC) with some degree of experience and responsibility. The state may also have vested the NOC with exclusive authority over the sector as the de facto Competent Authority, allowing it to allocate acreage by direct negotiation or tender, while itself retaining or competing for such acreage; contract on behalf of the state with the selected licensees or participate as state partner in joint ventures; and administer the petroleum contract and act as technical liaison for the state with the licensee. This development path is not recommended. Rather, a separate Competent Authority should hold the state's patrimony in its petroleum resources, conduct competitive bidding and/or direct negotiations, and ultimately issue licenses to successful bidders. The Competent Authority should contract on behalf of the state, not the NOC. The NOC should not have authority both to allocate acreage to potential licensees and to compete for it itself. This would be a strong disincentive to desired foreign investment. Assuming, however, that the Competent Authority, within or adjunct to the applicable ministry, was the licensing authority for the state, the NOC would have the important role of managing and administering its business relationships with foreign investors under its petroleum contracts (which are the usual commercial activities of an oil and gas company), carrying out the state's commercial functions within the sector, but not its sovereign and regulatory functions as well.

2.12 Where the state is completely new to the petroleum sector, often there is neither a central ministry with either responsibility for or expertise in petroleum operations nor an NOC. More likely, if petroleum is addressed at all in a legal context, it is addressed in an outdated minerals or mining law. Thus, aside from the need for a modern legislative framework for petroleum development, there will be the need to create a Competent Authority with adequate expertise and responsibility. This will require institutional strengthening and consensus. Rather than a competition between relevant ministries—such as geology, environment, trade, and finance—it is often expedient in such case, as an interim solution, to constitute the Competent Authority as an interministerial council with full authority to license, contract, and supervise petroleum operations. Concurrently, expertise can be developed through experience, training, and participation, ultimately leading to the creation of a true separate Competent Authority with the requisite staff and mandate.

Conduct of Petroleum Operations

2.13 This essential provision has a twofold purpose. First, it is meant to ensure that petroleum operations are conducted only under a duly issued permit or license from the Competent Authority, in such form and on such terms as are prescribed in the Petroleum Law, the Regulations, and, where applicable, a Petroleum Agreement, the terms of which must be consistent with the enumerated requirements thereof in both the Petroleum Law and the Regulations. Second, it is intended to give the state the maximum possible flexibility as regards its means of conducting petroleum operations. This may be through a state authority, such as an NOC; through a private entity, such as an incorporated joint venture; or in any other manner that it may deem appropriate—all within the bounds of established international norms and standards to attract foreign investment to a known and conducive setting in the sector.

Petroleum Agreements

2.14 Under this provision of the Petroleum Law, the concept and outline contents of a Model Contract are introduced. It authorizes the Competent Authority to have prepared and made available Model Contracts to potential applicants as the state's starting point for the negotiation of an exploration and production Petroleum Agreement. In some Petroleum Laws, a copy or copies of a Model Contract(s) is appended to the law as an exhibit. This would enact the Model Contract format as part of the Petroleum Law. It is preferable, however, not to follow this course. One must weigh the desirability of enacting a detailed, not easily changed or revised Model Contract with the force of law against merely identifying its essential, minimum provisions in the Petroleum Law—thus establishing their legal basis—but leaving full details and negotiable points to the Model Contract as a flexible instrument, subsidiary in position to the Petroleum Law. The latter course is recommended. The Petroleum Law should be couched in terms of permissive, minimal contents of a Model Contract, without legislating the provisions in detail. This is the "generic" aspect of such a Petroleum Law, which provides only the legal underpinnings and thereby leaves the state with maximum negotiating options.

2.15 Also to be covered in this section of the Petroleum Law are the Competent Authority's primary roles in negotiating and concluding Petroleum Agreements; directly

or indirectly supervising petroleum operations under Petroleum Agreements; revoking or suspending Petroleum Agreements for cause, after due notice to the rights holder and a reasonable period for it to effect a cure; granting nonexclusive prospecting permits for the purpose of obtaining information on hydrocarbon endowment; and, depending on how the Petroleum Law is meant to interface with the state's mining law, if any, granting mining permits for areas that are already the location of petroleum operations, provided, however, that the former does not interfere with the latter.

Regulations

2.16 As earlier stated, Regulations should be subsidiary instruments to the Petroleum Law and should not themselves be enacted as law. Rather, this section of the Petroleum Law should expressly authorize the Competent Authority to make Regulations from time to time, consistent with the policy and objectives of the Petroleum Law. This gives the regime the great advantage of flexibility, allowing for changes to be made quickly in response to developments, without the need for a protracted and often nonexpert legislative process. However, regulations and any amendments thereto should never be inconsistent with the Petroleum Law.

2.17 For greatest clarity, the Petroleum Law should bring forward into its text for summary mention the general areas in which the Competent Authority may make Regulations. These will be dealt with in greater detail below. The Petroleum Law should also give the Competent Authority broad authority to make any other Regulations that it considers necessary to put into effect the provisions and policy objectives of the Petroleum Law.

Qualifications, Duties, and Rights of Rights Holder or Contractor

2.18 First, it must be made clear in the Petroleum Law that Petroleum Agreements shall be concluded only with applicants who have the requisite financial resources, technical competence, and professional skills necessary to fulfill their obligations fully under such agreements.

2.19 The principal duties of a rights holder under a Petroleum Agreement should be enumerated in the Petroleum Law and then amplified in the Petroleum Agreement itself. In the Petroleum Law, the rights holder's duties to be specifically mentioned, and replicated as terms in all Petroleum Agreements, include reporting the discovery of any petroleum to the Competent Authority; presenting the Competent Authority in a timely fashion with a development plan for commercial petroleum discoveries and promptly taking all reasonable steps to develop and produce the discovery; conducting all petroleum operations in accordance with good international petroleum industry practice, including measures to promote conservation, safety, and environmental protection; and indemnifying the Competent Authority against all claims made by third parties in respect of injury, damage, or loss caused by or resulting from any operations carried out by the rights holder or its subcontractors under a Petroleum Agreement.

2.20 In return, the rights holder under a Petroleum Agreement should be accorded certain guaranteed rights in the Petroleum Law, some of which are necessarily

amplified in the Petroleum Agreement itself. The fundamental right is the exclusive right to carry out petroleum operations within the area covered by the Petroleum Agreement, for the time period(s) specified therein, subject to the provisions of the Petroleum Agreement. Separate procedures involving further governmental discretion—such as the granting of a license or the conversion of a "prospecting or exploration license" into a "production license," as is prevalent in civil law-based Petroleum Laws—are inadvisable, unless they are mere formalities, the validity of which is dependent upon the Petroleum Agreement. Any feasibility studies, expert evaluations, or requisite governmental approvals of a proposed arrangement should, thus, be obtained internally by the Competent Authority prior to the signing of the Petroleum Agreement.

Taxation of Profits

2.21 The tax/fiscal aspects of a complete petroleum exploration and production legislative framework may either be detailed in the Petroleum Law itself or separately set out in a companion Petroleum Revenue Code. The choice is often dictated by the depth and complexity with which the host government wishes to treat this topic. Normal practice, however, would be to establish the essential elements of the applicable regime in the Petroleum Law in such a way that the potential investor may easily gain a full understanding of the applicable tax regime; compute, without excessive uncertainty, the amount of taxes to be paid under such fiscal package; and consider such a fiscal package—taking into account the contractual arrangements—as reasonably competitive with other, similar worldwide investment opportunities.

Other Taxes, Duties, and Exchange Controls

2.22 While import and export taxes and duties are part of the overall fiscal package, practice is quite clear as to their relationship and applicability to petroleum operations. Most Petroleum Laws and Petroleum Agreements specify that rights holders, and those contractors and subcontractors working for them, are free to import and export supplies and equipment authorized under the Petroleum Agreement for petroleum operations, free of customs duties and taxes of any type. Expatriate employees of these parties receive the same treatment for their household goods and personal effects. To ensure that these exemptions do not become a mechanism to circumvent the state's regular import controls, any item(s) so imported are made subject to the applicable duties and taxes if they are later sold within the host government for any purpose. Equally, these exemptions from taxes and duties do not automatically exempt the rights holder from obtaining import and export licenses for the goods involved, if applicable. Such licenses permit the state both to consider the validity of the exemption on each item to which it applies and to enforce collections when a sale later occurs within its territory.

Fiscal Stabilization

2.23 After a Petroleum Agreement has been concluded, as an additional element of the total fiscal package, the investor should be secured where possible from the adverse economic effects of certain new statutes, regulations, and laws. One way this may be achieved in both the Petroleum Law and the Petroleum Agreement is by using certain limited stabilization or renegotiation provisions. These provisions would mitigate

the effects of any new enactments that either increase the burdens on rights holders or reduce their original rights and economic benefits. As a further qualification, they would not apply to new laws imposing safety, conservation, or environmental restraints, upon which the state must be free to act to protect the public interest. In such cases, newly enacted legislation will apply fully to the rights holder, although this provision may be subject to a requirement in the Petroleum Law for the Competent Authority, acting for the state, to negotiate in good faith amendments to the Petroleum Agreement that would compensate the rights holder for the resulting increased economic burden.

Environmental and Social Assessments

2.24 Although there is today a keen awareness worldwide of the need for diligent environmental protection and preservation, international practice in the petroleum sector has lagged behind in this regard. Petroleum Law often fails to adequately address the topic, and there is no substantial backup position in comprehensive and modern laws on environmental protection and conservation in most host countries. Most frequently, the topic has been left to a broad and bland obligation in both the Petroleum Law and the Model Contract that the rights holder or contractor is required to “conduct all petroleum operations in a diligent, conscientious and workmanlike manner in accordance with generally accepted standards of the international petroleum industry designed to achieve efficient and safe exploration and production of petroleum.” Some provisions have gone further, requiring that all necessary measures be taken for conservation, safety of life and property, crops, fishing and fisheries, navigation, protection of the environment, prevention of pollution, and safety and health of personnel. While being a reasonable beginning, these provisions were still inadequate.

2.25 Established practice today is to include a more comprehensive obligation for environmental protection and safety in the Petroleum Law and then to provide more detail on specific actions and requirements in both the Regulations and the Model Contract/Petroleum Agreement. Almost without exception, these details include a requirement for an environmental assessment study and an environmental management plan to be carried out prior to the commencement of petroleum operations as well as a social impact assessment. There is, however, a possibility of thereby creating a significant short-term financial disincentive. Equally, in line with the premise that legislative regimes for petroleum development should be self-contained, coherent legislative frameworks in and of themselves, it is not recommended to make petroleum operations generally subject to any broad, comprehensive, non-petroleum-specific environmental protection law, if extant, except to the extent that its principles are applicable to specific sector practices.

Natural Gas Development

2.26 Particularly in areas that are known or expected to have gas resources, it is advisable for the Petroleum Law to provide for special incentives and priorities to encourage the development of natural gas. Petroleum Laws often do not make adequate provision for the economic development of natural gas. Enlightened modern Petroleum Laws have specially tailored gas development and commercialization provisions to

encourage positive action on gas discoveries because of the long lead time required to build up the market and infrastructure. These include provisions to allow the rights holder a longer development or retention period to conduct a market feasibility study and optionally to develop natural gas jointly with the state in a negotiated joint venture. Price negotiations for gas also take longer because the value of the gas depends on the size of the local market and its value in that market.

Decrees/Regulations

2.27 The second essential component of successful petroleum legislative frameworks for exploration and development are the Regulations to the Petroleum Law. The Petroleum Law should authorize the Competent Authority expressly to make Regulations, from time to time, providing the detail and procedures by which to implement the policy and objectives of the Petroleum Law, by reference to specific, enabling provisions thereof. The Regulations are subsidiary instruments to the Petroleum Law, not intended for legislative consideration or enactment. The benefit of this practice is that maximum flexibility is maintained, allowing for timely response to any current developments that would require changes in the Regulations. The safeguard, always, is that the Regulations, and any changes thereto, should never be inconsistent with the policy, objectives, or letter of the Petroleum Law.

2.28 Consistent with the types of legislative formats discussed here, the Regulations to the type of Petroleum Law will follow the Petroleum Law's format, adding the detail necessary to effectuate the intent of its enabling provisions. This may be quite extensive or not, depending on many factors. Regardless of length or brevity, however, particular attention and elaboration in the Regulations should always be given to the following core items (2.29–2.36).

Competent Authority

2.29 In the event that the Petroleum Law does not itself identify the single government entity or agency that will act as the Competent Authority, the Regulations should do so. The policy advantage of such an approach is flexibility. The concept of the Competent Authority must be established by law, but its identity may be more readily changed by Regulation in response to evolving circumstances and growing or shifting expertise within government.

Petroleum Licensing

2.30 As the Petroleum Law establishes both that the state exclusively owns all petroleum within its territories and that it may conduct operations through any entity or in any manner to develop such petroleum, including the licensing of its exclusive right to qualified applicants under a Petroleum Agreement, the Regulations must detail the methods by which such licensing may be accomplished.

Petroleum Operations

2.31 Under this heading, the Regulations should address specific requirements to be met in carrying out petroleum operations under a Petroleum Agreement.

Petroleum Agreements

2.32 Some Petroleum Laws have attempted to legislate in detail the entire content of what must be included in a Petroleum Agreement. Alternatively, some Regulations go into extensive detail, in lieu of legislating it in the Petroleum Law. The former option is definitely not recommended; the latter is normally counterproductive. As earlier noted, it is better to have the Petroleum Law enact the core concepts of the legislative, contractual, and fiscal regime—in broad outline but not in detail—and for the Regulations to elaborate such core concepts as necessary. The contents of the proposed Petroleum Agreement—consistent with the essential requirements set out in both the Petroleum Law and Regulations—would, ideally, be contained in a Model Contract(s), which, as a subsidiary, nonenacted instrument(s), would be the starting point for the state's negotiations of Petroleum Agreements.

Fiscal and Financial Regime

2.33 Regardless of the complexity of the final fiscal regime chosen, its essential elements should be set out generically in the Petroleum Law and then treated with more specific detail in the Regulations. The advantage, as mentioned, of such an approach is the flexibility of being able to easily change particular rates and percentages in response to evolving circumstances, consistent always, however, with the principles and guidelines established in the Petroleum Law and individually agreed upon in Petroleum Agreements.

Assignment of rights

2.34 As a rights holder under a Petroleum Agreement may subsequently wish to transfer or assign all or a portion of its rights thereunder—to its own affiliate, another member of its consortium (if applicable), or a third party—the Regulations must address such a process expressly.

Land use

2.35 The Petroleum Law must guarantee the rights holder necessary access to both public and private lands for carrying out petroleum operations. The practice is for the Regulations to require the Competent Authority to deliver to the rights holder, at the time of its signing the Petroleum Agreement, all licenses and permits of every nature required under existing legislation for the conduct of petroleum operations, including those that allow the rights holder reasonable use of public and private lands, roads, means of communication, water, and minerals for such purpose. Where privately owned land is to be so encumbered, the practice is for the Regulations to require good faith negotiations by the rights holder with the owner(s) thereof and payment of just compensation thereto if voluntary agreement is reached. Failing voluntary agreement, the Regulations should empower the Competent Authority to institute proceedings under the applicable land law for the state taking of such lands—either temporarily or permanently—on behalf of the rights holder, subject to the rights holder paying both the adjudicated just compensation to the landowner and the administrative costs to the Competent Authority that it incurred by having undertaken and conducted such proceedings.

Environmental and Social Protection

2.36 Evolving practice on this topic is to amplify the obligation for environmental and social protection in the Petroleum Law with specific details and required actions in both the Regulations and the Model Contract. The Regulations may be as detailed as necessary, but in the process of establishing norms of conduct, they should focus on the following broad principles:

- Minimizing ecological damage;
 - Avoiding waste of petroleum and its production environment;
- Preventing pollution and waste of land and structures, fresh water resources, crops, and marine and animal life;
- Ensuring emergency cleanup obligations and procedures;
- Restoring the environment at the conclusion of petroleum operations; and
- Evaluating the social impact of petroleum operations.
 - The Regulations should also require the investor to prepare an environmental management plan.

Model Contract

2.37 The final essential component of successful petroleum legislative frameworks is one or several variants of a Model Contract. A state is best served by having its own contractual format from which to commence negotiations of Petroleum Agreements. The Model Contract(s) should be included in the bid tender package, requiring applicants to identify any exceptions thereto as part of their bid.

3

Major Recommendations

Project Objective

3.1 The focus of the technical assistance was to make recommendations aimed at revising and supplementing the existing Vietnam Petroleum Law and Decree to create a stable legal and regulatory framework for the petroleum sector that would last for a number of years, providing confidence for investors and enabling Vietnam to attract investment for exploration and development of hydrocarbons in an increasingly competitive environment.

Recommendations

3.2 The project team's recommendations were based on international best practice on a number of subjects related to petroleum legislation and fiscal systems. The major recommendations, outlined below, constituted the basis for the advice provided by the project team during the project.

3.3 The project team identified certain major areas where Vietnam's petroleum regime contains disincentives or hurdles for development and foreign investment compared with those in other countries throughout the world. The international best practice in these areas was identified and developed as a set of recommendations that were suitable to the current and expected petroleum resources, development, finances, and capabilities of Vietnam.

3.4 To establish petroleum development incentives with the greatest degree of certainty, the project team recommended that these changes appear in the Petroleum Law. However, some of the changes were not accepted as part of the revision to the Petroleum Law. The project team then urged the inclusion of provisions adopting these recommendations in the Petroleum Decree, where possible. It is also possible for some of these recommendations to be adopted when Vietnam commences the preparation of the Model Contract implementing the Revised Petroleum Law and Petroleum Decree.

3.5 The major recommendations of the project team can be grouped under the following six headings:

1. Make fiscal terms simpler and more competitive.
2. Make the production-sharing contract the principal form of petroleum contract.
3. Facilitate gas marketing opportunities.
4. Separate regulatory functions: policy, regulatory, and petroleum rights management.
5. Use a simpler bidding process.
6. Consider price- and production-sensitive royalties.

These recommendations are discussed below.

Major Recommendation 1: Make Fiscal Terms Simpler and More Competitive

General Concept of Simplifying Fiscal Terms

3.6 In Vietnam, awarding a petroleum contract takes considerable time. Some international oil companies have indicated that it takes as long as four years to negotiate a petroleum contract. This is a significant disincentive to foreign investment in the Vietnamese petroleum sector. Apart from the influence of factors that the government cannot control (such as geology), the acreage award process is slow largely because too many fiscal terms are open for negotiation. In the course of negotiating a petroleum contract in Vietnam, the parties will negotiate the cost oil share, profit oil share, calculation of profit for tax purposes, royalty, participation of PetroVietnam, and other matters. This situation creates lengthy negotiations and results in numerous variations among individual contracts, making them difficult to administer as a group. The project team recommended simplifying the fiscal terms.

3.7 Simplification can best be achieved by fixing most of the provisions in the Petroleum Law and Decree and making them nonnegotiable. It was recommended to make only the profit oil and profit gas share a negotiable item, although it would be possible to have negotiations on two or three fiscal factors without making the regime unduly complicated.

3.8 Analyses of the petroleum fiscal system should be based on the government take—that is, the government total revenues from petroleum development, if any, and from profit oil or gas, taxes, and duties. Appendix D shows calculations of the government take under different assumptions about the petroleum fiscal system, including the recommendations in this chapter.

3.9 The fixing of certain fiscal terms does not mean that the government of Vietnam is reducing the possible government take that can be obtained at the upper end of the scale. By introducing a fiscal system in which only profit oil and profit gas sharing is negotiable or biddable, Vietnam may still be able to conclude contracts with a government take of 80 percent (see Appendix D, which shows calculations of the Government take based on a variety of approaches to the petroleum fiscal system, including the recommendations in this chapter).

3.10 An important step in fixing the fiscal terms is defining the minimum fiscal terms. The minimum fiscal terms should be sufficiently low to permit economic operations in high-cost and difficult areas and under low oil and gas prices. They should be fixed at a level that permits viable petroleum operations in all of Vietnam's main petroleum basins. In previous discussions with the government of Vietnam, the project team had evaluated the terms and conditions of Decision 216 of the prime minister and concluded that these terms are appropriate for the economically marginal areas in Vietnam and to permit operations over a wide range of prices and costs.⁴ Therefore, it is recommended that the minimum fiscal conditions for all activities in Vietnam be based on the fiscal features of Decision 216.

Increase the Cost Recovery Limit

3.11 Article 6 of Decision 216 establishes a cost recovery limit of 70 percent for cost oil and cost gas in incentive blocks. This article applies to only "marginal fields." It is recommended that this higher-cost recovery limit be applied to all petroleum contracts. There are several reasons for this recommendation (3.12–3.16).

Competing Countries

3.12 Fixing the cost limit at 70 percent would be an essential step to make Vietnam competitive with its neighbors. Typical cost limits in South and Southeast Asia are as follows:

Bangladesh	50 percent
Cambodia	70 percent
China	60 to 62.5 percent
India	No limit (100 percent)
Indonesia	85 percent (due to "first tranche petroleum" provisions)
Malaysia	50 to 75 percent
Myanmar	40 percent
Pakistan	85 percent
Philippines	70 percent

A cost recovery limit of 70 percent would be near the average limit applied in the region and would be competitive with that of other countries.

Price Movements

3.13 Currently, some of the production-sharing contracts have cost limits as low as 35 percent. These cost limits are based on a share of the gross production. The costs that can be recovered, therefore, depend very much on the price level of the oil or gas. For instance, in the case of oil developments, the cost recovery limit under an oil price of US\$10 per barrel would be US\$3.50 per barrel based on a limit of 35 percent. This amount is available to recover operating costs, capital costs, and certain taxes and duties paid to government. Typical offshore costs range between US\$4 and US\$9 per barrel for operating plus capital costs. Therefore, in a situation with low oil prices and a

⁴ *Petroleum Fiscal Issues and Policies for Fluctuating Oil Prices in Vietnam*, ESMAP Report no. 236/01, February 2001.

cost limit of US\$3.50 per barrel, even costs under the most profitable fields cannot be fully recovered. This makes the development of these fields uneconomical under low price levels.

3.14 A cost limit of 70 percent would provide cost recovery of US\$7 per barrel assuming a low oil price of US\$10 per barrel. As long as the oil price does not fall below US\$13 per barrel, the costs could reasonably be recovered from a wide variety of offshore fields in the typical offshore cost range US\$4-9 per barrel.

3.15 It is likely that oil prices will continue to fluctuate. Vietnam's fiscal terms should be competitive at a broad range of prices to avoid having most of its offshore activities uneconomical during periods of low oil prices. A policy that provides a relatively high cost recovery limit under all contracts would therefore be attractive for investors in a number of circumstances and would ensure that the entire offshore of Vietnam would be reasonably economical under a wide variety of price scenarios.

Shallow Water Areas and Profitable Fields

3.16 A high cost limit does not mean that Vietnam would have a low government take on profitable fields in shallow water. The profit oil and profit gas rates could be raised to ensure a high government take from such fields. The effect, however, of the higher cost limit is that investors would recover their investments somewhat faster, which would encourage exploration. In combination with the removal of the ring fencing for corporate income tax, this would create a system whereby companies can quickly recover their investment and reinvest the profits in incremental exploration and production in Vietnam. This is precisely the overall concept that is required to increase the level of activities offshore in Vietnam.

Competitive Corporate Income Tax

3.17 The project team suggested that rather profound changes in corporate income tax be implemented in the Petroleum Law. The overall objective of these changes is to make the overall tax provisions more attractive to investment.

Competitive Tax Rate

3.18 Many countries' international corporate income tax rates are lower than Vietnam's 50 percent rate. The international average is about 32 percent:

Brazil	25 percent
Norway	28 percent
Argentina	30 percent
United Kingdom	31 percent
China	33 percent
United States	35 percent
Australia	36 percent
Pakistan	40 percent (cap)
Malaysia	40 percent
Indonesia	48 percent
Thailand	50 percent

Decision 216 reduced the corporate income tax rate for petroleum activities in incentive areas from 50 percent to 32 percent. The Petroleum Law should be adjusted to make all petroleum contracts subject to the corporate income tax law of general application, with the law determining how to calculate the taxes. This would introduce nonnegotiable corporate income tax terms, and the Petroleum Law and the implementing Decree would have only limited provisions on how to calculate the corporate income tax.

3.19 The main consequence of this recommendation is that the tax regime would no longer be an item for negotiation in petroleum development. The general tax rate of 32 percent is recommended to provide a tax rate of general applicability at a level similar to other countries. To send the right signal about policy change and to attract new investors, the tax changes should be included in the tax law or the Revised Petroleum Law rather than in individually negotiated contracts. Whether a tax rate of 32 percent or 50 percent applies or whether special tax exemptions should be granted will no longer be an issue. In addition, the tax will be determined completely independently from production sharing.

3.20 Currently, the definition of "recoverable" and "nonrecoverable" costs under the production-sharing provisions is negotiated in each contract, resulting in different tax calculations for each contract. Vietnam's fiscal regime would be simpler if all operators calculated their tax in the same way for every production-sharing contract, as is the case in other jurisdictions.

3.21 The administration of the corporate income tax would also be simplified because all calculations would be carried out in the same manner for all new contracts. There would be no exceptions or special treatment. A simple single tax administration could deal with all petroleum contracts.

Removal of Ring Fencing

3.22 An important method to encourage investment in petroleum exploration is to eliminate what is sometimes referred to as a "ring fence" tax calculation—a term meaning that income and expenses within an imaginary ring fence surrounding each contract area cannot affect or be affected by income and expenses outside that area. The following is an explanation of this issue (3.23–3.27).

International Practice

3.23 In almost all countries, corporate income tax is a tax on the profits of the corporation. Most petroleum corporations carry out exploration and production in many different contract areas in the same country. The international practice is that the corporate income tax is based on the results of all the contract areas combined. In other words, a corporation submits only one corporate income tax return for all its operations.

3.24 The practice of calculating the corporate income tax on the consolidated results is common in many countries, including the United States, Canada, all major Latin American countries, all European countries, and most countries of Asia and Africa.

Appendix B shows the international practice on this important aspect of the tax/fiscal regime.

3.25 Vietnamese corporate income tax law also permits, in principle, the calculation of the corporate income tax on a consolidated basis. However, in Vietnam the situation is complicated by the fact that foreign investment licenses are required for foreign operations and corporate income tax needs to be calculated for each license separately in accordance with the Law on Foreign Investment. The practical result has been that in Vietnam the corporate income tax is being calculated on the income of the "contractor" for each "contract area." If a contractor has more than one contract area, income tax is calculated separately for each contract area.

Exploration Incentive

3.26 Ring-fence calculations of corporate income tax create a disincentive for exploration. This disincentive relates to exploration contracts where exploration operations are not successful. Under the Vietnamese ring-fence system, the related expenditures cannot be deducted from the consolidated corporate income tax. If exploration is unsuccessful in a contract area, the tax calculation results in a loss. Since there is no income from the area, the loss cannot be deducted. In a consolidated tax regime, exploration expenditures can be deducted from any income earned by the corporation in other contracts. This lowers the tax payments. Taxable income is automatically lowered in the case of unsuccessful exploration under a consolidated system, so the companies receive a tax benefit, making exploration much more attractive. This has a considerable impact on exploration decisions. It also makes it much more attractive to reinvest in further exploration in Vietnam once income from the first discovery has been established.

3.27 In most petroleum-producing countries, petroleum companies have already established production and income. Therefore, reinvestment in exploration in such countries is being stimulated through the consolidated tax system. If Vietnam does not adopt the same system, it will remain at a serious competitive disadvantage relative to most other countries.

Status of Recommendations Regarding a Simpler Fiscal System

3.28 The amendments to the Petroleum Law and the Revised Petroleum Decree show significant progress toward simpler and more competitive fiscal terms. However, there is little improvement from the terms of Decision 216, and some of the suggestions of the project team were not adopted in the manner recommended, and a degree of administrative discretion remains, which reduces the likelihood that some of the improved fiscal terms will be available in all cases.

The Cost Recovery Limit

3.29 The cost oil/gas limit in the Revised Petroleum Law is now stated to be a negotiated percentage of "up to" 70 percent. This is an improvement, but the failure to fix the cost recovery limit for all operations means that the ability of the new Petroleum Law to attract investment will depend on how the government implements it and how

individual petroleum contracts are negotiated. The amendments also include the wording "until the full recovery" (in Article 25A), which is not clear.

Competitive Corporate Income Tax

3.30 The recommended 32 percent corporate income tax is adopted in the Revised Petroleum Law, but only for blocks under incentive schemes. This is an improvement, but the failure to establish this lower corporate income tax rate for all operations in Vietnam means that the ability of the new Petroleum Law to attract investment will depend upon the extent to which the government defines incentive blocks on a broad basis. A recommendation that the Petroleum Decree specify the incentive blocks as being those not explored to date was not accepted.

Ring Fencing

3.31 The issue of consolidating corporate tax calculation to eliminate ring fencing was not included in the revised law. This may have a significant negative impact on the willingness of investors to reinvest in oil and gas operations in Vietnam. Vietnam is one of very few countries where the tax consequences of reinvestment are so unattractive. Eliminating ring fencing could stimulate oil and gas exploration and production and help to provide a sustainable level of activity.

Major Recommendation 2: Make the Production-Sharing Contract the Principal Form of Petroleum Contract

3.32 The Petroleum Law discusses the possibility of using any type of petroleum contract in Vietnam: production-sharing agreement, joint venture, or some other arrangement. Many developing countries have adopted the production-sharing contract as the standard model for oil and gas development. In Vietnam, 37 production-sharing contracts have been signed, although Vietsovpetro is operating the largest producing field (Bach Ho) under a joint venture enterprise as envisioned by the Law on Foreign Investment.

3.33 The project team recommended that the Petroleum Law establish the production-sharing contract as the principal form of contract because:

- It is widely accepted by oil and gas companies operating in other countries with state-owned enterprises;
- It works well in the context of a petroleum regime with a state oil company such as PetroVietnam;
- It does not require the type of capital investment on the part of PetroVietnam in the way that a joint venture would;
- It establishes a simple operating structure, with fewer layers of management, which is desirable to attract international oil and gas companies, yet also provides a good measure of control to the host

government through PetroVietnam participation on the Management Committee; and

- It balances the interests of the host government with the interests of international oil and gas companies.

3.34 Another advantage of the production-sharing contract is that it is the best common oil and gas industry host government contract that fits within Vietnam's legal structure for foreign investment. The Law on Foreign Investment describes in Article 4 the forms in which investment by foreigners may occur:

“Article 4: Foreign investors may invest in Vietnam in the following forms:

1. Business cooperation under a business cooperation contract;
2. Joint venture enterprises;
3. Enterprises with 100 percent foreign invested capital.”

Article 5 goes on to describe the forms of business cooperation that are possible: “Two or more parties may enter into business cooperation under a business cooperation contract such as *profit-sharing or product-sharing production cooperation* and other business cooperation forms.”

3.35 The Law on Foreign Investment in Vietnam defines "business cooperation contract" and "joint venture enterprise" as follows:

- "Business cooperation contract" means a document signed by two or more parties for carrying out investment activities without establishing a legal person.
- "Joint venture enterprise" means an enterprise established in Vietnam through the cooperation between two or more parties under a joint venture contract or an agreement signed by the Government of the Socialist Republic of Vietnam or between an enterprise with foreign invested capital and a Vietnamese enterprise or between a joint venture enterprise and a foreign investor under a joint venture contract.

Joint Ventures in the Petroleum Industry

3.36 The provisions of the Law on Foreign Investment describe a joint venture enterprise as involving the establishment of a limited liability company with the status of a legal person. Each party to the joint venture enterprise must then contribute capital to this entity. While this form of joint venture enterprise is not uncommon, joint ventures as they are referred to in the petroleum industry do not involve the creation of a separate entity. In an oil and gas "joint venture," each participant owns an undivided interest in the joint property as cotenant. The participants share the profits or production resulting from the joint operations. No separate legal entity is created. The details of this relationship are set forth in an agreement commonly referred to as a "joint operating agreement."

3.37 The Law on Foreign Investment discusses such a relationship when it describes a business cooperation contract, which the law says could include profit

sharing, product sharing, or some other kind of arrangement that does not involve establishing a legal person.

3.38 Based on workshops with government officials and other stakeholders as well as other discussions with the Ministry of Planning and Investment, it was understood that there have been difficulties in implementing the concept of the joint venture enterprise in petroleum operations.

3.39 For these reasons and the others identified in the bulleted list above, it was recommended that a Model Contract based on a production-sharing contract be developed. This is the form that has been most frequently used in Vietnam and is preferred by most international oil and gas companies.

Status of Recommendations Regarding the Production-Sharing Contract

3.40 We understand that the government of Vietnam intends to prefer the use of a production-sharing contract for its petroleum contracts. The Office of Government advised that this is indicated by the production-sharing contract being the first form of petroleum contract listed in Article 20 in the Petroleum Decree. The project team does not consider this an adequate way to indicate this preference. The preference should be highlighted further in the Decree and by the issuance of only one Model Contract that adopts the form of a production-sharing contract.

3.41 The Revised Petroleum Law and the Revised Petroleum Decree propose that the prime minister or the parties to the petroleum contract may approve the use of a contract form other than the Model Contract in certain circumstances. The project team recommended that the Petroleum Decree describe the situations in which a contract form other than the Model Contract may be appropriately used. These may include stating that the activities to be conducted pursuant to the petroleum contract are restricted to development and production operations, reconnaissance surveys, or other operations that do not include exploration through drilling operations; or stating that a treaty or agreement between the state of Vietnam and a foreign government requires the use of a petroleum joint-venture enterprise.

Major Recommendation 3: Facilitate Gas Marketing Opportunities

3.42 Vietnam's petroleum basins appear to be relatively likely to contain gas. However, there is currently little infrastructure for the production, transportation, and marketing of natural gas in Vietnam. Accordingly, any gas discoveries will require significant capital investment, and there may be long delays before facilities and markets are in place. This may require extension of the period provided under a petroleum contract for the commencement of production.

3.43 For these reasons, the project team recommended that the Revised Petroleum Law include the concept of a "significant discovery"—a discovery that is not yet commercially viable because of the lack of markets, pipelines, or processing facilities. The discovery might become commercial once markets are available or pipelines or processing facilities are in place. The concept of a significant discovery is being introduced gradually around the world in view of the realization that natural gas discoveries can be developed only in conjunction with downstream market development.

3.44 Bangladesh, Pakistan, Canada, and Bolivia all include the possibility for such "significant discoveries" in their contracts and/or legislation. Canada permits the company to hold on "indefinitely" to a significant discovery until the minister decides that the discovery is commercially viable. Bolivia and Pakistan permit a 10-year retention period. Bangladesh permits a five-year retention period.

3.45 The Revised Petroleum Law should permit contractors to declare a significant discovery. This provision would entitle the contractor to keep such discovery for a retention period. It is recommended that a petroleum contract include a provision for a retention period with respect to a significant discovery until such discovery is commercially viable as a result of available transportation and processing facilities and markets. The duration of the petroleum contract with respect to such significant discovery shall be extended by the retention period.

3.46 A maximum retention period should be defined in the Decree. A period of 10 years or longer may be the appropriate retention period, which would be automatically added to the duration of the contract for the respective discovery. In the case of Vietnam, using a 10-year retention period would benefit exploration.

3.47 In view of the emerging gas markets in Asia, oil and gas companies need to know that, in case they discover gas, they have reasonable retention periods to build exploration programs and infrastructure to permit gas to be commercially exploited. This increases the attractiveness of oil and gas exploration.

3.48 The change in the upstream provisions of the Petroleum Law should be matched by new downstream legislative measures that would make it easier for private investors to develop gas markets in Vietnam, in particular in the power sector, which is the main market.

Status of Recommendations Regarding Facilitating Gas Marketing Opportunities

3.49 The recommendation that the Petroleum Law and Decree adopt the concept of an extended time period for development of gas discoveries has been adopted in the amendments to the Petroleum Law. However, the amendments allow for a maximum extension period of only seven years. Also, the amendments appear to give the government the discretion not to provide for the last two years of the seven-year extension, if the contractor delays or displays a lack of goodwill in reaching the agreement on a gas purchase and sale contract (Annex 2, Decree, Article 26) in a manner satisfactory to the government. This adds a disproportionate degree of discretion that does not appear in the significant discovery provisions in other countries

Major Recommendation 4: Separate Regulatory Functions: Policy, Regulatory, and Petroleum Rights Management

Introduction

3.50 In many countries, state-owned companies have regulatory and policy functions in addition to their operational functions. The role of national oil companies

(NOCs) in the management of petroleum operations worldwide is changing. As a country's petroleum experience develops, the NOC should evolve from regulator of activities to investor in petroleum operations. This is desirable because where an NOC is both a participant in petroleum operations and the regulator of them, there are some inherent conflicts of interest. This has been a matter of concern to international oil companies and to host governments. The many roles of PetroVietnam should also be separated and performed by different arms of the government of Vietnam. The project team recommended that the policy and regulatory tasks of PetroVietnam be separated from its commercial role.

3.51 Today, PetroVietnam supervises the contractors operating under petroleum contracts in Vietnam. If PetroVietnam wanted to conduct its own petroleum operations in the future in competition with foreign investors, there would be an inherent conflict of interest.

3.52 Chapter VI of the Petroleum Law states that the State Petroleum Management Authority (SPMA) shall be established in accordance with the Law on the Organization of the Government to assume the state management of petroleum operations, which includes a number of policy functions, regulatory functions, and petroleum rights management functions. PetroVietnam has in fact been delegated most of these management roles of the sector that the Petroleum Law proposes to be performed by the government of Vietnam, including the roles of the SPMA. The petroleum experience of Vietnam has evolved sufficiently for the government to follow the trend involving the separation of state management of petroleum activities. The Petroleum Law establishes a number of different state management roles, which can be separated into three categories: policy functions, petroleum rights management functions, and regulatory functions.

- *Policy functions:* Making decisions on strategies, plans, and policies for the development of the petroleum industry; issuing regulations with respect to the management of petroleum operations; making decisions on policies and forms of cooperation with foreign entities; and establishing policies to promote or restrict petroleum export to protect the interests of the state of Vietnam.
- *Petroleum rights management functions:* Designating and delimiting blocks or acreage for petroleum exploration and production; and approving petroleum contracts.
- *Regulatory functions:* Monitoring and giving instruction and guidance to relevant authorities and localities in carrying out activities related to petroleum operations; resolving issues related to the right to conduct petroleum operations and adjudicating any violation of this law; and monitoring, inspecting, and supervising petroleum operations.

3.53 It was recommended that approving Model Contracts and determining bidding procedures and results be added to the list of functions of the SPMA.

Recommendation: Establishment of SPMA

3.54 The Petroleum Law already discusses in Article 39 the establishment of an authority, the SPMA, that would perform some of the functions of state management. This authority has not in fact been established. It was recommended that the government of Vietnam create this authority to assume the petroleum rights management and regulatory functions of state management of petroleum operations identified in the Petroleum Law.

3.55 The policy functions of state management should not rest with the SPMA. These functions should be performed by appropriate ministries in the government. The World Bank has previously recommended the creation of a National Energy Policy Council that would have overall responsibility for establishing Vietnam's energy policies. If such an authority is created, it is recommended that the upstream petroleum policy functions described above be added to its responsibilities.

3.56 These recommendations do not mean that PetroVietnam will cease to have an important role in petroleum operations. PetroVietnam will continue to have the important role of managing and administering its business relationships with foreign investors under its petroleum contracts, whether they are production-sharing contracts, profit-sharing contracts in the form of joint operating agreements, or some other business relationships. These are the usual commercial activities of an oil and gas company.

3.57 The government of Vietnam may hesitate to add to its bureaucratic structure by creating yet another government agency. However, the establishment of the SPMA is already proposed in the Petroleum Law, and there are strong policy reasons to implement what the Petroleum Law prescribes. Also, many of these functions are already being performed by PetroVietnam, meaning that no new government activities are being recommended. With respect to the cost to the government of establishing this authority, the project team recommended the possible creation of a levy on the petroleum industry to pay for the operational costs of the SPMA. There is considerable international precedent for such a levy. Given that some of these functions are currently being performed by PetroVietnam without compensation, having an SPMA in place may even reduce overall government cost.

Status of Recommendations Regarding Separation of Regulatory Functions

3.58 While the amendments to the Petroleum Law do not establish or change the tasks and responsibilities of the SPMA, the Revised Petroleum Decree contains provisions that provide further details regarding the establishment of a state body for the management of the petroleum sector: the Oil and Gas State Management Body (OGSMB).

3.59 The Revised Petroleum Decree provides that the main function of the OGSMB will be technical regulation. In the area of rights management, the OGSMB will act as a secretariat to the prime minister and the Ministry of Planning and Investment (MPI). Essentially, rights management functions are given to the prime minister. The OGSMB is called upon to organize the bidding process, but all decisions concerning rights are made by the prime minister, and MPI is the key agency for appraising bidding results. The OGSMB also plays a secretariat role in the area of petroleum policy, as

stated briefly in the Petroleum Decree. The OGSMB may draft petroleum strategies and plans, but the decree clearly says that the government will decide strategies, policies, and plans.

3.60 The Petroleum Decree clarifies, at least in outline, the functions that will be undertaken by the respective state organizations. The five tables in Appendix C summarize all the articles of the decree, according to the main functions to be undertaken by each government agency. The decree specifies that the main functions of the OGSMB will be technical regulation, as is shown in Table C.3.

3.61 In the area of rights management (Table C.2), the OGSMB will act as a secretariat to the prime minister and MPI. Essentially, rights management functions are given to the prime minister. The OGSMB is called upon to organize the bidding process, but all decisions concerning rights are made by the prime minister, and MPI is the key agency for appraising bidding results.

3.62 The OGSMB also plays a secretariat role in the area of petroleum policy, as stated briefly in the decree, and shown in Table C.1. The OGSMB may draft petroleum strategies and plans, but the decree clearly says that the government will decide strategies, policies, and plans.

3.63 An important improvement in the Revised Petroleum Decree is that explicit conflicts of interest between PetroVietnam and the OGSMB have been eliminated.

3.64 Generally, the concentration of technical regulation in OGSMB, rights management in the prime minister's office, petroleum policy in OGSMB as advisor to the government, and economic regulation through licenses in MPI appears to be a viable and practical solution for Vietnam.

Major Recommendation 5: Use a Simpler Bidding Process

Role of SPMA in the Bidding Process

3.65 The project team recommended that the bidding and issuance of petroleum contracts be governed by the SPMA.

Bidding on Work Units

3.66 The project team suggests to consider the use of the concept of "work units" rather than the minimum financial and work commitment as the method describing the work obligation of a contractor in the bidding process. A number of jurisdictions around the world (including Bolivia, Canada, and Pakistan) have adopted this method of bidding, one that does not require identifying the kind of work that must be done for the proposed work program under petroleum concessions. Bidders make a commitment to perform a quantity of work that is denominated in work units. These work units can be credited by the performance of different kinds of exploration work, including two-dimensional seismic work, three-dimensional seismic work, and the drilling of exploration wells.

3.67 The work units concept offers a number of advantages. First, it provides a simple method for comparing bids that are to be evaluated in whole or in part based on the work commitment. Each bid can be evaluated based on the total number of work units committed to be performed by the bidder. In some cases, the host government establishes a minimum number of work units that must be performed, and bids are evaluated based on the bidder's willingness to perform work in excess of the minimum. Second, it provides flexibility for the contractor to select the kind of work program suitable for the exploration area during petroleum operations. The contractor is not required to commit to a specific work program before gathering sufficient information about the exploration area. Third, it eliminates the need to conduct careful audits of the amount of exploration expenditures that are required where the work commitment is denominated in dollars. It is much easier to ascertain that the contractor has performed a certain quantity of work when it is described in kilometers of seismic acquired or meters drilled than it is to ascertain that dollars are wisely spent.

3.68 Appendix E offers an example of the concept of work units.

Bidding Modes

3.69 The project team recommended that bidding for petroleum contracts in Vietnam occur on the basis of an international competitive bidding process to the greatest extent possible. If selective or bilateral negotiation occurs without reasonable justification, it may adversely affect the oil industry's perception of Vietnam as a place where open and transparent bidding is used.

Bidding Criteria

3.70 A major area of complaint from foreign investors is the slow negotiation of block awards in Vietnam. Therefore the first major recommendation above was that Vietnam decide upon—that is, make non-negotiable--most fiscal term provisions (including cost recovery level and participation share) of its petroleum contracts. The objective of this recommendation is to reduce the number of variables to be negotiated with bidders. The project team believes that the ideal situation for Vietnam would be to use only one or two bidding criteria when offering petroleum contracts. Bidding systems that operate in this way are easy to administer and transparent to the bidders. The greater the number of bid criteria, the greater the difficulty in determining the best bid and the greater the likelihood that the bidding process will be delayed and may appear to be less transparent.

Status of Recommendations Regarding Simpler Bidding Process

3.71 A Draft Bidding Decree reviewed by the project team⁵ contained some movement toward international competitive bidding and reduced the number of bidding criteria to two. The prime minister, however, can still introduce additional criteria, and no single body has been given the responsibility to oversee the bidding process, negotiations, and issuance of contracts. The amendments to the Petroleum Law suggest that the prime minister be allowed to approve petroleum contracts on a selective or

⁵ Later issued as Decree no. 34/2002/ND-CP, July 6, 2001.

bilateral negotiation basis in certain circumstances. It was recommended that either the Bidding Regulation or the Revised Petroleum Decree specify the situations in which selective or bilateral negotiations (as opposed to bidding) would be appropriate. This recommendation has not been adopted. The Revised Petroleum Decree specifies that the OGSMB will organize the bidding process, the prime minister will decide on appointment of bidders, and MPI will appraise the bidding results. This process is set forth in the Revised Petroleum Decree in Annex 2.

Major Recommendation 6: Consider Price- and Production-Sensitive Royalties

Royalties for Crude Oil and Natural Gas

3.72 Vietnam's royalty for oil is not price-sensitive, which can be a disincentive for the development of small fields. A royalty is a "front-end loaded" form of fiscal recovery mechanism that requires an operator to pay the same proportion of production regardless of the profitability of the field. The project team recommended that Vietnam make two changes to the royalty scale for oil that would (i) make the scale sensitive to price, and (ii) enhance the economics of small fields.

3.73 The royalties can be made sensitive to price by simply splitting them into two components: a production-based royalty scale and a price-based royalty scale. The total royalty rate is the rate based on production plus the rate based on price.

3.74 The details of the recommended royalty rates and the economic analysis of these recommendations are in Appendix D.

Status of Recommendations Regarding Price- and Production- Sensitive Royalties

3.75 The recommendation regarding royalty revisions was not adopted in the Petroleum Law or the Petroleum Decree. However, the first step of the royalty scale was reduced to stimulate marginal oil fields (see Article 32 of the law). The impact of this change, however, on the overall economics of oil and gas investment in Vietnam would be minimal. For up to 5 million cubic meters per day, no royalties would be paid.

4

Other Recommendations

4.1 The project team made a number of other recommendations to the government of Vietnam.

4.2 *Exports without Export Permit.* The project team recommended that the government of Vietnam allow exports of petroleum without an export permit in suitable circumstances. This recommendation was adopted in the Revised Petroleum Law, where Article 28(1)(g) (see Annex 1) allows the export of a contractor's petroleum share to be determined in the petroleum contract without the need for an export permit. This is a highly desirable change that will comfort potential investors once such contractual provisions are established.

4.3 *Foreign Exchange Availability.* Investors want to know that they will be able to obtain foreign exchange for any revenues they earn in local currency and that they will have the right to retain abroad the proceeds of their petroleum sales (subject always to fulfilling their royalty and tax obligations). Article 41 of the Revised Petroleum Decree appears to address these needs in part by proposing the exchange of Vietnamese dong into foreign currency, but this is permitted only for "important projects." The right to retain abroad any revenues of offshore sales is not specifically addressed.

4.4 *Grandfathering of Previous Contracts.* The project team recommended that previous contracts be "grandfathered" for any amendments in the revisions to the Petroleum Law. This grandfathering was not part of the recommendations that were adopted. However, most of the key provisions that would require grandfathering (changes to income tax and royalties, for example) either were not adopted by the government or were adopted in such a way that grandfathering of previous contracts is unnecessary (for example, the reduced income tax rate is to apply to only incentive areas).

- The following recommendations were not adopted:

4.5 *Value Added Tax.* The project team recommended that petroleum sales be "zero-rated" for value added tax (VAT) purposes rather than exempted, to ensure that VAT input refunds are available to oil and gas investors.

4.6 *Reconnaissance License.* A reconnaissance license permits a company to carry out geophysical, geochemical, or geological surveys that do not involve the drilling

of petroleum wells. The purpose of the surveys is to gather information. Surveys are typically carried out by specialized geophysical companies that sell the information to oil companies. The reconnaissance license usually includes the obligation to provide the government with a copy of the information. The information is useful for the government's planning of bidding rounds, and the availability of the information may raise the oil industry's interest in specific prospects. The project team recommended that the government of Vietnam allow for the granting of reconnaissance licenses.

4.7 *Block Size Restrictions.* The project team recommended that the size of blocks be restricted to ensure that no operator would have access to an excessively large part of Vietnam's offshore area. The current law restricts the number of blocks that can be awarded, but not their size.

4.8 *Flexible Abandonment Procedures.* Article 13 of the Petroleum Law states that upon the termination of petroleum operations, the facilities need to be abandoned and the areas need to be cleared. The abandonment process, however, is an ongoing one, and The project team recommended that the Petroleum Law should reflect this fact. Typically, in an oil or gas field, certain wells are abandoned while others are being drilled. Every time a facility, well, or area is no longer of use, it should be properly abandoned. The contractor should not wait until the termination of the petroleum operations.

4.9 *Development Plan.* The Petroleum Law did not propose the possibility of granting a petroleum contract for development only. It is likely that this will be required in the future. First, important gas discoveries could be relinquished by companies that are not interested in following up on such discoveries. After a number of years, such discoveries sometimes become of interest. In this case, a petroleum contract could be offered just for the development of the discovery. Second, in a number of cases petroleum contracts may still be in commercial production upon the termination of a contract after 25 or 30 years. In this case, the area could revert to PetroVietnam. However, the government might grant the area again on the basis of a bidding round for ongoing production and development. In this case, a petroleum contract could be issued that proposes development activities only. Therefore, the project team recommended the inclusion of the ability to grant a petroleum contract just for the development and production of an oil or gas field without the need for an exploration period.

5

Conclusions and Next Steps for Vietnam's Upstream Petroleum Regime

Conclusions

5.1 Vietnam's amended petroleum regime, including the Revised Petroleum Law and the Revised Petroleum Decree, contains many of the features of a modern legal and regulatory petroleum framework. The right of the state to petroleum is affirmed, the authority of the government to regulate petroleum matters is established, and a competent regulatory authority is created. Vietnam's petroleum regime establishes a role for the state oil company, PetroVietnam, that is not dissimilar from that of other petroleum-producing nations, although in practice, PetroVietnam's extensive powers and controls are more comparable to nations where petroleum activities are regulated by the state oil company rather than the government. This situation may change with the implementing of the Oil and Gas State Management Body.

5.2 The Revised Petroleum Law and the Revised Petroleum Decree took a number of steps in the direction of establishing a modern legal and fiscal framework for petroleum in Vietnam. However, the project team pointed out that the total fiscal package as reflected in the Revised Petroleum Law and the Revised Petroleum Decree is not materially better than, and in certain respects is inferior to, that of Decision 216 of the prime minister. From November 1998, when Decision 216 was put into effect, until the Revised Petroleum Law passed in June 2000, no petroleum contracts were signed under its incentive terms. Although there has been an increase in 2000 and 2001, the project team is concerned that the fiscal revisions in the Revised Petroleum Law and the Revised Petroleum Decree will not be sufficient to attract sustained investment in oil and gas exploration and production. To realize Vietnam's goal to obtain additional investment in oil and gas exploration, the remaining features of Vietnam's petroleum regime must contain real and substantive improvements.

Next Steps

Model Contract

5.3 As described in Chapter 3, the petroleum regime of a country is established in three components: Petroleum Law, Regulations, and Model Contract. The project team recommended that the major suggested changes that were not accepted as part of the Revised Petroleum Law be included in the revision of the Petroleum Decree, where possible.

5.4 The third component of an upstream petroleum regime is a Model Contract. The project team has recommended that Vietnam create a Model Contract in the form of a production-sharing contract to indicate that this is the preferred type of contract. The lack of Model Contract at present is a significant source of delay and a potential lack of transparency associated with the bidding and granting of petroleum rights in Vietnam. It is recommended that Vietnam prepare a Model Contract for use in future bidding rounds as a next step in developing a modern legal framework for upstream petroleum activities.

5.5 This project did not include the preparation of Model Contracts. However, the recommendations made by the team in the Petroleum Law and the Petroleum Decree would suggest that the basic tax/fiscal terms under a production-sharing agreement would be:

1. The applicable royalties;
2. The corporate income tax of 32 percent;
3. The production-sharing agreement with a cost recovery limit of 70 percent and a profit oil and profit gas share to be determined;
4. The 15 percent participation right of PetroVietnam;
5. The export tax;
6. The remittance tax, which would be 5 percent for marginal fields pursuant to Decision 216; and
7. Other applicable taxes.

5.6 In principle, these basic terms could be quite attractive to investors, depending, of course, on how the profit oil and profit gas shares are being determined. Also, this fiscal package would lend itself very well to bid situations where sliding scale profit oil and profit gas shares would be the subject of bidding.

5.7 The limited progress made in the Revised Petroleum Law and the Revised Petroleum Decree can be further advanced by the development of a Model Contract that adopts a production-sharing regime. The government of Vietnam should be encouraged to pursue this step.

Downstream Gas Regime

5.8 Another important step in the development of Vietnam's petroleum regime would be the creation of a legal and regulatory framework for downstream gas transmission and gas distribution in Vietnam. As the government of Vietnam undertakes

the first major gas utilization program based on private investment in infrastructure and gas supplies from its offshore sector, there is a need to create the framework for private participation in the transmission and the distribution of gas to industrial parks, industries, and commercial customers as well as power plants. The framework should set the policy objectives for development, competition, and performance of the downstream gas sector, setting criteria for granting licenses and defining the pricing methodologies and access terms for pipelines and distribution systems and the rights and obligations of the license holders in the sector. The framework should also include provisions to establish a regulator. An added benefit of encouraging gas development is that the resulting interest in gas exploration and development in Vietnam may lead to the discovery of additional crude oil reserves. The government of Vietnam is currently pursuing the establishment of a legal and regulatory framework for gas transmission and distribution, and this effort is to be encouraged.

Appendix A

Steering Committee and Working Group Members and Members of the Project Team

Steering Committee and Working Group members included:

Steering Committee on Revision of The Petroleum Law

1. Mr. Nguyen Ton, Deputy Head, Office of Government, Chairman
2. Mr. Ha Hung Cuong, Vice Minister of Justice, Vice Chairman
3. Mr. Vu Huy Hoang, Vice Minister of Planning and Investment, member
4. Ms. Le Thi Bang Tam, Vice Minister of Finance, member
5. Mr. Ho Sy Thoang, Chairman of Executive Board, Petrovietnam, member
6. Mr. Ngo Thuong San, General Director, Petrovietnam, member
7. Mr. Tran Van Giao, Acting Director of Petroleum Department, Office of Government, member, secretary

List of Members of The Inter-Ministerial Working Group on Revision of The Petroleum Law

1. Mr. Tran Van Giao, Acting Director of the Petroleum Department, Office of Government, Chief
2. Mr. Ngo Van Sang, Deputy Director of the Petroleum Department, Office of Government, Deputy Chief
3. Mr. Dinh Dung Sy, expert, Legislation Department, Office of Government
4. Mr. Tran Van Binh, law expert, Press and Communication Center, Office of Government
5. Mr. Nguyen Phuoc Hiep, Deputy Director, International Legislation and Cooperation Department, Ministry of Justice
6. Ms. Vu Tuyet Mai, expert, Legislation and Foreign Investment Promotion Department, Ministry of Planning and Investment
7. Mr. Phan Van Hien, Chief, Foreign Investment Division, External Finance Department, Ministry of Finance
8. Mr. Nguyen Hung Lan, Deputy Chief, International Cooperation Division, Petrovietnam
9. Mr. Do Chi Hieu, member, Executive Board, Petrovietnam

10. Mr. Phan Ngoc Cu, Sr. expert, Petroleum Department, Office of Government
11. Mr. Nguyen Quang Hinh, expert. Petroleum Department, Office of Government
12. Mr. Le Quang Vinh, expert, Petroleum Department, Office of Government
13. Mr. Bui Quyet, expert of Petroleum Department, Office of Government, secretary
14. Ms. Nguyen Quynh Mai, expert, Petroleum Department, Office of Government, secretary

The project team was comprised of Bent Svensson (team leader); Anil Malhotra, Nguyet Anh Pham; and William T. Onorato (all World Bank), Pedro van Meurs (Van Meurs & Associates, Ltd.), and Jay Park (Macleod Dixon), consultants.

A roundtable on gas sector policy was held October 19–20, 2000, in Hanoi. Although the roundtable was not directly related to or funded under the ESMAP project, oil and gas sector regulation was discussed in relation to the amendments and the Revised Petroleum Decree. The World Bank team at the workshop included Peter Eglington and David Aron, consultants.

Appendix B

International Practice Regarding Consolidation of Corporate Income Tax

Countries that do not permit consolidation for corporate income tax purposes

Generally, the countries that do not permit such consolidation are Algeria, Azerbaijan, Benin, Cambodia, Cameroon, Indonesia, Malaysia, Myanmar, and Vietnam.

In other countries, the state oil companies pay taxes on behalf of the foreign investors--that is, tax is included in the profit oil share and consolidation is not relevant. These countries include Bangladesh, Côte d'Ivoire, Egypt, Gabon, Oman, the Philippines, Sudan, Syria, and Yemen.

Countries that permit consolidation for corporate income tax purposes

Many countries permit consolidation for corporate income tax purposes. They are Albania, Angola, Argentina, Australia, Austria, Barbados, Belize, Bolivia, Brazil, Brunei, Canada, the Central African Republic, Chad, Chile, China, Colombia, Congo, Denmark, Ecuador, Equatorial Guinea, France, Germany, Ghana, Greece, Greenland, Guatemala, Guinea, Hungary, Italy, Japan, Kazakhstan, Korea, Liberia, Madagascar, Mali, Morocco, Mozambique, Namibia, Nepal, the Netherlands, New Zealand, Nigeria, Norway, Pakistan, Papua New Guinea, Peru, Poland, Portugal, Romania, Russia, Senegal, South Africa, Spain, Switzerland, Tanzania, Thailand, Trinidad and Tobago, Turkey, Turkmenistan, the United Kingdom, the United States, Uruguay, Venezuela, and Zaire.

Countries that permit consolidation of exploration losses against any activity or field

Finally, two countries permit consolidation of exploration losses against any activity or field. They are India and Tunisia.

Appendix C

Separation of Regulatory Functions

The October 2000 Revised Petroleum Decree clarified the functions that will be undertaken by the respective state organizations. The following five tables summarize all articles of the decree, according to the main functions to be undertaken by each government agency. The main functions are:

- Petroleum policy
- Petroleum rights management
- Technical regulation
- Fiscal terms and financial monitoring
- OtherTable C.1: Petroleum Policy

<i>Prime Minister</i>	<i>MPI</i>	<i>Oil and Gas State Management Body</i>	<i>Government</i>	<i>Petro Vietnam</i>
		Art. 65.1, 2, 3, 4 Draft legal documents, draft petroleum strategies and planning for government, draft development plans and important projects, draft and submit to government policies for encouraging investment projects	Art. 64.1 Issue legal documents and decide strategies, policies, and plans	

Note. MPI = Ministry of Planning and Investment.

Table C.2: Petroleum Rights Management

<i>Prime Minister</i>	<i>MPI</i>	<i>Oil and Gas State Management Body</i>	<i>Others</i>	<i>PetroVietnam</i>
Art. 3. Decide on PVN development plan when PVN acts alone	Art. 25. Extend prospecting and exploration stage, on request	Art. 23. Organize bidding according to bidding regulations issued by government, but where only one partner participates or in other special cases, propose to prime minister the appointment of bidders		Art. 3. May do petroleum activity alone or with partners, and all activity will include PVN; when acts alone it must submit plans to prime minister
Art. 23. Decide on appointment of bidders	Art. 66.1. Appraise bidding results and submit to prime minister for approval; appraise and grant or adjust investment licenses; submit to prime minister for permission to transfer rights and obligations in contracts	Art. 65.5. Submit to prime minister for decision appointment of bidders for petroleum contracts		Art. 29. Receive payments from contractor in event of incomplete work commitments
Art. 26. Extend retention of contract area when gas discovered, on request				Art. 33. Receive reports on output, oil and gas quality, own use, flaring, for each well, from contractors
Art. 27. Decide special cases of force majeure				Art. 35 and Art. 36. Prepare unitization plans where fields extend beyond boundary of contracts
Art. 31. Decide on field development plans submitted by OGSMB (or by PVN under Article 3)				
Art. 35 and Art. 36. Approve unitization plans where fields extend beyond boundary of contracts				
Art. 64.2. Issue lists of blocks, determine and adjust boundaries of blocks, approve petroleum contracts, decide on transfer of rights, consider and decide on appointment of bidders				

Note. MPI = Ministry of Planning and Investment; OGSMB = Oil and Gas State Management Body; PVN = PetroVietnam.

Table C.3: Technical Regulation

<i>Prime Minister</i>	<i>MPI</i>	<i>Oil and Gas State Management Body</i>	<i>Others</i>	<i>PetroVietnam</i>
Art. 11. Define offshore safety zones in special cases		Art. 5. Receive plans for exploration and development (for on-submission to government for approval, Art. 65.3)	Art. 6–10. Contractors must use Vietnamese safety and environmental standards; submit to competent state bodies environment, safety control, and contingency plan;	Art. 12. Receive reports from contractors of other natural resources discovered while drilling
Art. 31. Approve development plans		Art. 11. Define onshore safety zones	Art. 11. Offshore safety zones are defined by decree.	Art. 17. Send reports to OGSMB
		Art. 15. Receive plans for dismantling works	Other ministries are called upon as required, such as labor, MOSTE, construction, and others.	Art. 31. Receive results of discovery from contractor
		Art. 17. Receive reports from PVN on annual and long-term plans, quarterly and annual summary reports on performance and results, reports on implementation of economic and/or technical projects, reports on important events and incidents, and other reports at request of OGSMB		
		Art. 18. Receive reports from contractors, per regulations of OGSMB		
		Art. 30. Receive plans for early development, and approval		
		Art. 31. Receive results of discovery from contractor; receive contractors and PVN deposit reports and field development plans, for on-submission for approval by prime minister; if plans approved and field not developed, OGSMB entitled to recover the field		
		Art. 34. Control flaring of associated gas through use of permits		
		Art. 65.6 Examine, inspect, and supervise petroleum activities		
		Art. 66.2 Coordinate as required with other agencies and People's Committees		
		Art. 67. Carry out inspections and issue decisions		
		Art. 68. Suspend activities, in view of hazards (function of investment team)		
		Art. 69. Receive suspensions from contractors		
		Art. 71. Impose penalties for violations, including failure to notify OGSMB of discovery of other natural resources		
		Art. 72. Handle violations and decide on levels of fines (function of OGSMB head)		

Note. MPI = Ministry of Planning and Investment; OGSMB = Oil and Gas State Management Body; PVN = PetroVietnam; MOSTE = Ministry of Science, Technology and Environment

Table C.4: Fiscal Terms and Financial Monitoring

<i>Prime Minister</i>	<i>MPI</i>	<i>Oil and Gas State Management Body</i>	<i>Others</i>	<i>PetroVietnam</i>
Art. 52. Decide specific cases of tax exemptions	Art. 57. Issue list of equipment and machinery for basis of import tax exemptions (54) and value added tax (55) Art. 63. Receive annual financial statements of contractors	Art. 63. Receive annual financial statements of contractors	Important involvement also from OOG and MOF in design of fiscal terms	Advise government

Note. MPI = Ministry of Planning and Investment; OOG = Office of Government; MOF = Ministry of Finance

Appendix D

Proposal for Price- and Production-Sensitive Oil and Gas Royalties

Vietnam's royalty scale for oil is not price-sensitive, which can be a disincentive for the development of small fields. A royalty is a "front end-loaded" fiscal recovery mechanism that requires an operator to pay the same proportion of production regardless of the profitability of the field. The project team recommended that Vietnam make two changes to the royalty scale for oil to (i) make the scale sensitive to price and (ii) enhance the economics of small fields.

The royalties can be made price-sensitive by splitting them into two components: a production-based royalty scale and a price-based royalty scale. The total royalty rate is the rate based on production plus the rate based on price.

The following royalty scales are recommended.

Crude Oil Royalty

The recommended royalty on crude oil is calculated on the incremental basis of the actual net aggregate production of crude oil during a taxable period (one month) based on the daily average production of crude oil from the entire contract area. The royalty is the sum of the production royalty and the price royalty, as established below.

The production royalty for a month is the royalty determined on the basis of production rate of crude oil for that month, as follows:

Table D.1: Production Royalty - Oil

<i>Crude Oil Production from the Petroleum Contract for the Month</i>	<i>Production Royalty Rate -Onshore and Offshore</i>	<i>Production Royalty Rate - Offshore</i>
	<i><200 m Water Depth (%)</i>	<i>³200 m Water Depth (%)</i>
Rate applicable on first 10,000 bopd	0	0
Rate applicable on next 40,000 bopd (to 50,000 bopd)	3	1
Rate applicable on next 25,000 bopd (to 75,000 bopd)	5	3
Rate applicable on next 25,000 bopd (to 100,000 bopd)	10	5
Rate applicable on next 50,000 bopd (to 150,000 bopd)	15	10
Rate applicable on production over 150,000 bopd	20	15

Note. bopd = Barrels of oil per day

The price royalty for a month is the royalty determined based on the price of crude oil for that month, as follows:

Table D.2: Price Royalty - Oil

<i>Crude Oil Price in the Month (US\$)</i>	<i>Price Royalty Rate— Onshore and Offshore</i>	<i>Price Royalty Rate — Offshore</i>
	<i><200 m Water Depth (%)</i>	<i>³200 m Water Depth (%)</i>
12.00 per barrel or less	0	0
12.01–15.00 per barrel	1	1
15.01–18.00 per barrel	2	2
18.01–21.00 per barrel	3	3
21.01–24.00 per barrel	4	4
Over 24.00 per barrel	5	5

Natural Gas Royalty

The recommended royalty on natural gas is calculated on the incremental basis of the actual net aggregate production of natural gas during a taxable period (one month) based on the daily average production of natural gas from the entire contract area. The royalty is the sum of the production royalty and the price royalty, as established below.

The production royalty for a month is the royalty determined on the basis of production rate of natural gas for that month, as follows:

Table D.3: Production Royalty - Gas

<i>Natural Gas Production from the Petroleum Contract for the Month</i>	<i>Production Royalty Rate—Onshore and Offshore <200 m Water Depth (%)</i>	<i>Production Royalty Rate—Offshore ≥200 m Water Depth (%)</i>
On the first 3 million m ³ /day	0	0
On the next 3 million m ³ /day (to 6 million m ³ /day)	5	3
On the next 3 million m ³ /day (to 9 million m ³ /day)	8	5
On over 9 million m ³ /day	10	8

The price royalty for a month is the royalty determined on the basis of the price of natural gas for that month, as follows:

Table D4: Price Royalty - Gas

<i>Natural Gas Price in the Month (US\$)</i>	<i>Price Royalty Rate—Onshore and Offshore <200 m Water Depth (%)</i>	<i>Price Royalty Rate Offshore ≥200 m Water Depth (%)</i>
1.20 per MMBtu and below	0	0
1.21–1.50 per MMBtu	1	1
1.51–1.80 per MMBtu	2	2
1.81–2.10 per MMBtu	3	3
2.11–2.40 per MMBtu	4	4
Over 2.40 per MMBtu	5	5

Note. MMBtu = Million British Thermal Units

In no case would the amount of natural gas royalty paid for one month exceed 10 percent of the natural gas produced in that month.

The government of Vietnam may reduce the royalties described above for a field when (i) the field cannot produce natural gas in paying quantities without a reduction in royalties; (ii) a producing field is nearing the end of its economic life, and royalty reductions are necessary to permit continued production in paying quantities; or (iii) processing and transportation costs (both capital and operating) cannot be recovered without a reduction in royalties.

If royalties are reduced for a field and there is more than one field in the subject contract area, the total royalties shall be prorated downward based on the proportion of the fields that are subject to royalty reduction compared to the total production from the contract area.

Economic Analysis

Tables D.5 and D.6 provide an economic analysis of the various proposals for price- and production-sensitive oil and gas royalties.

Oil Cases

Table D.5 illustrates the impact on the contractor's rate of return for oil and gas. Three fiscal regimes are presented:

Option 1. "No incentives". This means 50 percent corporate income tax and maximum 35 percent cost limit for annual recovery of capital and operational expenditure against petroleum revenue, royalty, and other fiscal terms as defined in the Petroleum Law of 1993.

Option 2. "32–70". This means a 32 percent corporate income tax and a 70 percent cost limit.

Option 3. "32–70, new roy". This means 32 percent corporate income tax, a 70 percent cost limit, and the proposed scales for royalties.

Tables D.5 and D.6 also compare Vietnam's prospects with those of other important offshore areas, including China, the Gulf of Mexico (United States), Indonesia, Norway, Thailand, and the United Kingdom.⁶

A "no government" case is included in the analysis to evaluate underlying economic conditions in Vietnam. This case offers the same prospects as the others but does not involve contractors making any payments to government. The risk-adjusted real rate of return of the no-government case is a very attractive 22.7 percent even at US\$12 per barrel. The three cases (or options) are calibrated on achieving a 13.2 percent risk-adjusted rate of return at US\$20 per barrel. To calibrate the cases to the same rate of return, the profit oil shares are adjusted for each of the cases. Table D.7 shows how the profit oil shares are substantially higher for Option 2 and higher again for Option 3.

The adjustment of the profit oil scales underscores an important point: having a lower corporate income tax rate, cost limit, and royalties does not imply a reduced overall government take. Table D.6 shows the implications for the government take of the proposed royalties. It shows that the risked government take at US\$20 per barrel is essentially the same. This is because the more lenient tax regime, cost limit, and royalties are compensated by tougher profit oil shares.

Therefore, adopting the project team's proposals with respect to the corporate income tax rate, cost limit, and royalties does not necessarily mean a loss of government take. The project team proposes, on the contrary, that the profit oil scales be determined by bidding. In the project team's proposal, the market decides the level of overall government take.

⁶ For more fiscal analysis of the petroleum system, see *ESMAP: Petroleum Fiscal Systems and Policies for Fluctuating Oil Prices in Vietnam*. ESMAP Report no. 236/01. 2001

However, tables D.5 and D.6 show that the overall behavior of the fiscal system is much more flexible than that of the existing Vietnam fiscal regime. Under Option 3, the small fields are much more profitable than under Option 1. Also, under lower prices, the oil prospect maintains its profitability better. Option 3 behaves very much like the flexible system of Thailand. This means that Vietnam will be able to compete better regionally in case of marginal fields or low oil prices.

Gas Cases

Table D.5 also illustrates the comparisons for gas. Three fiscal regimes are presented:

Option 1. “*No incentives*”. This means a 50 percent corporate income tax and a 50 percent cost limit.

Option 2. “*32–70*”. This means a 32 percent corporate income tax and a 70 percent cost limit.

Option 3. “*32–70, new roy*”. This means a 32 percent corporate income tax, a 70 percent cost limit, and the proposed scales for royalties.

Table D.8 shows the profit gas shares that were calibrated at a 13.6 percent risked rate of return for a price of US\$2 per mmbtu.

The existing Vietnam fiscal regime for gas has a cost gas limit of 50 percent. Therefore, an increase to 70 percent does not create a strong effect. At the same time, the recommended new royalty regime for gas is somewhat tougher than the existing regime. Therefore, the combined effect of a 70 percent cost gas limit and tougher royalties is a fiscal system that behaves very much like the current system, except that it is not as vulnerable when prices are lower, and the economics of marginal small fields are slightly better.

Table D.5a: Overview of Competitive Situation of Vietnam, Rate of Return Based on Constant 1998 Dollars – Oil

<i>Price level (US\$/BBL)</i>	20	20	20	20	16	16	16	16	12	12	12	12
<i>Field Size (Million barrels of oil)</i>	50	150	300	EMV	50	150	300	EMV	50	150	300	EMV
	Rate of Return, Oil (%)											
“No government”	37.70	46.30	49.20	38.00	29.10	37.90	41.10	31.20	18.40	27.70	31.50	22.70
Vietnam, “no incentives”	14.40	19.20	20.10	13.20	9.30	14.60	15.80	9.40	2.90	8.70	10.50	4.60
Vietnam, “32–70”	16.30	19.30	19.20	13.20	11.20	14.80	15.10	9.50	4.80	9.30	10.10	4.90
Vietnam, “32–70, new roy”	17.10	19.30	18.60	13.20	12.20	15.10	14.90	9.70	6.30	10.00	10.30	5.50
Thailand—Gulf	16.20	17.30	17.50	13.70	12.60	14.30	14.60	10.90	7.30	10.60	11.20	7.40
China—offshore	24.00	30.80	32.50	22.80	17.80	24.70	26.70	18.10	10.00	17.30	19.70	12.20
Indonesia—incentive terms	11.30	17.20	19.90	12.80	7.70	13.20	15.90	9.50	3.60	8.60	11.20	5.60
United Kingdom—offshore	29.90	37.80	40.70	30.70	22.50	30.50	33.80	24.70	13.50	21.90	25.50	17.50
Norway	13.20	19.30	21.50	14.90	9.00	15.00	17.40	11.20	4.70	10.30	12.60	7.10
U.S.—Gulf Of Mexico <400 m	22.70	30.10	33.30	21.40	16.40	23.80	27.20	16.60	8.30	16.10	19.70	10.50

Note. BBL = Barrels; EMV = risk-adjusted rate of return

Table D.5b: Overview of Competitive Situation of Vietnam, Rate of Return Based on Constant 1998 Dollars - Gas

<i>Price level (US\$/Mcf)</i>	2.00	2.00	2.00	2.00	1.60	1.60	1.60	1.60	1.20	1.20	1.20	1.20
<i>Field Size</i>	0.5 TCF	1 TCF	2 TCF	EMV	0.5 TCF	1 TCF	2 TCF	EMV	0.5 TCF	1 TCF	2 TCF	EMV
	Rate of Return, Gas (%)											
<i>Vietnam, no incentives</i>	13.70	22.60	23.60	13.60	8.20	16.90	18.40	9.50	1.50	10.30	12.60	4.60
<i>Vietnam, 32–70</i>	13.90	22.70	23.40	13.60	8.40	17.10	18.40	9.60	2.20	10.40	12.60	4.70
<i>Vietnam, 32–70, new roy</i>	14.10	22.60	23.20	13.60	8.70	17.20	18.40	9.70	2.60	10.80	12.90	5.10

Note. EMV = risk-adjusted rate of return; Mcf = Thousand Cubic Feet; TCF = Trillion Cubic Feet

Table D.6a: Overview of Competitive Situation of Vietnam, Undiscounted Government Take in Constant 1998 Dollars (Includes Participation) – Oil

<i>Price level (US\$/BBL)</i>	20	20	20	20	16	16	16	16	12	12	12	12
<i>Field Size (Million barrels of oil)</i>	50	150	300	EMV	50	150	300	EMV	50	150	300	EMV
Undiscounted Government take, Oil (%)												
“No government”	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Vietnam, “no incentives”	75.30	76.10	78.40	79.30	78.90	77.30	79.20	81.50	89.30	81.00	81.10	87.20
Vietnam, “32–70”	71.00	76.30	80.20	79.50	73.60	77.40	81.10	81.60	81.10	80.00	82.90	86.60
Vietnam, “32–70, new roy”	68.90	76.10	81.00	79.40	70.30	76.70	81.40	81.10	74.40	78.00	82.30	84.70
Thailand—Gulf	71.40	79.70	82.80	81.10	69.90	78.00	81.60	80.20	70.70	75.90	80.00	80.10
China—offshore	72.30	73.20	75.00	74.60	73.10	73.50	75.30	75.30	75.60	74.30	75.80	76.90
Indonesia—incentive terms	81.00	80.60	80.40	82.10	82.10	81.00	80.60	83.10	85.10	81.90	81.00	85.30
United Kingdom—offshore	32.70	31.80	31.60	32.40	33.50	32.10	31.80	33.00	35.80	32.80	32.20	34.30
Norway	85.70	84.70	84.60	85.70	86.60	84.80	84.70	86.30	87.90	84.90	84.70	87.20
U.S.—Gulf of Mexico <400 m	49.10	49.00	48.70	51.20	52.40	50.70	49.90	53.80	61.50	54.30	52.40	59.70

Note. BBL = Barrels; EMV = risk-adjusted rate of return

Table D.6b: Overview of Competitive Situation of Vietnam, Undiscounted Government Take in Constant 1998 Dollars (Includes Participation) - Gas

<i>Price level (US\$/Mcf)</i>	<i>2.00</i>	<i>2.00</i>	<i>2.00</i>	<i>2.00</i>	<i>1.60</i>	<i>1.60</i>	<i>1.60</i>	<i>1.60</i>	<i>1.20</i>	<i>1.20</i>	<i>1.20</i>	<i>1.20</i>
<i>Field Size</i>	<i>0.5 TCF</i>	<i>1 TCF</i>	<i>2 TCF</i>	<i>EMV</i>	<i>0.5 TCF</i>	<i>1 TCF</i>	<i>2 TCF</i>	<i>EMV</i>	<i>0.5 TCF</i>	<i>1 TCF</i>	<i>2 TCF</i>	<i>EMV</i>
Undiscounted Government take, Gas (%)												
Vietnam, “no incentives”	64.60	64.60	67.20	68.20	67.60	65.00	67.60	70.20	85.80	66.50	68.40	76.70
Vietnam, “32–70”	64.60	64.90	68.30	68.70	66.50	65.30	68.50	70.50	78.10	66.70	69.30	76.00
Vietnam, “32–70, new roy”	63.40	64.20	67.80	68.00	64.90	64.30	67.80	69.50	73.70	64.50	67.70	73.70

Note. EMV = risk-adjusted rate of return; Mcf = Thousand Cubic Feet; TCF = Trillion Cubic Feet

Table D.7: Profit Oil Rates

<i>Options for fiscal regime</i>	<i>“No Incentives” (%)</i>	<i>“32–70” (%)</i>	<i>“32–70, New Roy” (%)</i>
Up to 10,000 bopd	20	25	25
10,001–25,000 bopd	30	55	58
25,001–50,000 bopd	45	65	68
50,001–75,000 bopd	50	70	75
Over 75,000 bopd	60	75	80

Note. bopd = Barrels of oil per day

Table D.8: Profit Gas Rates

<i>Options for fiscal regime</i>	<i>“No Incentives” (%)</i>	<i>“32–70” (%)</i>	<i>“32–70, New Roy” (%)</i>
Up to 3 million m ³ /day	25	45	40
3–6 million m ³ /day	35	54	51
6–9 million m ³ /day	45	64	61
9–12 million m ³ /day	55	70	72
12–15 million m ³ /day	65	75	75
Over 15 million m ³ /day	70	80	80

Appendix E

Work Units—An Example

This appendix offers an example of the concept of work units described in chapter 3. The appendix is meant to illustrate the concept, based on a model contract.

Interpretation

"Work unit" means a unit of work for the purpose of determining compliance with the minimum commitment under the petroleum contract.

Work Units

The work that qualifies for work units is new two-dimensional and three-dimensional seismic surveys and exploration wells carried out during the exploration period in a contract area. Any work carried out as an appraisal program or as part of the development of a commercial discovery shall not qualify for work units.

A well exploring a deeper horizon that is drilled into a reservoir that has previously been identified by a discovery in the contract area qualifies for work units only to the extent that it is drilled below the base of the deepest formation of that discovery. Any such well shall qualify for the number of work units that are applicable to the depth below the deepest discovered reservoir of that discovery.

The value of one work unit is US\$10,000. This amount shall be adjusted for inflation after January 1 of each calendar year in accordance with the changes in U.S. consumer prices shown in *International Financial Statistics*, a publication of the International Monetary Fund (or such other publication of the International Monetary Fund as may replace it), with the dollar amounts expressed in the petroleum contract being deemed to be expressed in US\$2000, in accordance with the following formula:

$$A_n = A_a \times \left(\frac{CPI_{Jn}}{CPI_{J00}} \right)$$

where:

A_n means the new amount as adjusted by the procedure;
 A_a means the amount stipulated in the petroleum contract;

CPI_{Jn} means the index for U.S. consumer prices for the month of July previous to the January 1 date under consideration; and

CPI_{J00} means the index for U.S. consumer prices for the month of July 2000.

The following equivalency applies to equate work that has been carried out with work units⁷:

a. Two-dimensional seismic surveys

One line kilometer of two-dimensional seismic surveys that has been acquired, processed, interpreted, and mapped: 0.3 work units

b. Three-dimensional seismic surveys

One square kilometer of three-dimensional seismic surveys that has been acquired, processed, interpreted, and mapped: 2.0 work units

c. One exploration well having a depth as shown below⁸:

<i>Well Depth (Meters)</i>	<i>Work Units</i>
1,000	300
2,000	550
3,000	1,000
4,000	1,800
5,000	3,200
6,000	5,800

For well depths intermediate to the ones indicated in Article c, the work units shall be determined on the basis of linear interpolation. For well depths deeper than 6,000 meters, three work units shall be added for each additional meter drilled.

The following work does not qualify for work units:

- (i) Work carried out prior to the effective date;
- (ii) Work carried out after the termination of the exploration period;
- (iii) Work carried out outside the Contract Area;

⁷ The list is by way of example only and is not necessarily recommended.

⁸ Consider a different scale of work units for onshore and offshore wells, and for wells in deep and shallow water.

- (iv) Work not carried out in accordance with an approved work program;
- (v) Work not qualifying as petroleum operations under the petroleum contract; and
- (vi) The portion of any well depth for which no well logs was obtained as a result of blowouts, other accidents, or drilling problems.

The work in order to earn work units shall be considered completed where:

- (b) The State Petroleum Management Authority has received satisfactory proof from the holder of the petroleum contract that the work has been executed; and
- (c) The State Petroleum Management Authority has received the minimum required information pursuant to a petroleum contract.

The contractor is free to define the work that qualifies for work units.⁹ [subject to the approval of the work program by the Management Committee]

Work units cannot be transferred from one contract area to another and work units can be carried forward subject to the provisions of an agreement.

Minimum Commitment

The minimum number of work units required under a petroleum contract (the "minimum commitment") is as follows:¹⁰

The State Petroleum Management Authority may at any time, but not during a bidding round, increase the minimum commitment for all or any part of Vietnam, as well as establish principles for apportionment for contract areas partially within and outside such areas, and after having increased the minimum commitment, decrease this amount but not below the values established in this decree. Any change in the minimum commitment shall not affect the obligations of a contractor to perform the minimum work provided for in a petroleum contract issued prior to the change in the minimum commitment.

⁹ Insert the words "subject to the approval of the work program by the Management Committee" at the end of this sentence if the Model Contract proposes a management committee that approves work programs.

¹⁰ Insert here provisions regarding minimum work commitments, denominated in work units, as appropriate

Annex 1

Revised Petroleum Law (Unofficial Translation^{*})

Petroleum Law

Amendments to the Petroleum Law passed on June 9, 2000 are indicated in italics

In order to effectively conserve, exploit and utilize Petroleum resources for the development of the national economy and the promotion of cooperation with foreign countries;

Pursuant to Articles 17, 29 and 84 of the 1992 Constitution of the Socialist Republic of Vietnam:

This Law governs Petroleum exploration and production activities carried out within the territory, the exclusive economic zone and the continental shelf of the Socialist Republic of Vietnam.

Chapter I

General Provisions

Article 1 All the Petroleum existing in the subsoil of the land, islands, internal waters, territorial sea, exclusive economic zone and continental shelf of the Socialist Republic of Vietnam is the property of the Vietnamese people under the sole space management of the State of Vietnam.

Article 2 The State of Vietnam encourages Vietnamese and foreign organizations and individuals to invest capital and technology to conduct Petroleum Operations on the basis of respect for the independence, sovereignty, territorial integrity and national security of Vietnam and in compliance with Vietnamese law.

^{*} This English translation of the Petroleum Law is an unofficial translation provided for informational purposes only. All questions of interpretation must be resolved by reference to the official Vietnamese text.

The State of Vietnam protects ownership rights with respect to the capital investments, assets and other lawful rights of Vietnamese and foreign organizations and individuals conducting Petroleum Operations in Vietnam.

Article 2a *Petroleum activities must comply with the provisions of the Petroleum Law and other relevant provisions of Vietnamese law. In case of any discrepancy between the provisions of the Petroleum Law and other provisions of Vietnamese law on the same specific matter related to petroleum activities, the Petroleum Law's provisions shall apply. In cases where the Petroleum Law and other Vietnamese legislation have not prescribed a specific matter related to petroleum activities, the parties signing a petroleum contract may agree on the application of international laws and/or international practices in petroleum activities or foreign petroleum laws provided that such international laws, international practices or foreign laws are not contrary to fundamental principles of Vietnamese law.*

Article 3 As used in this Law, the following terms shall have the following meanings:

"Petroleum" means crude oil, natural gas, and hydrocarbons whether in natural liquid, gaseous, solid or semi-solid state, including sulphur and other similar substances associated with hydrocarbons except coal, shale, bitumen or other minerals from which oil can be extracted.

"Crude Oil" means hydrocarbon in natural liquid state, asphalt, ozokerite and liquid hydrocarbons obtained by distillation or extraction of Natural Gas.

"Natural Gas" means hydrocarbons in gaseous state produced from wells, including wet gas, dry gas, wellhead gas and residue gas after the extraction of liquid hydrocarbons from wet gas.

"Petroleum Operations" mean activities in exploration, field development, and production of Petroleum, including services directly related to or supporting such activities.

"Petroleum Contract" means a written agreement entered into by and between the Vietnam Oil and Gas Corporation and any organization or individual to carry out Petroleum Operations.

"Petroleum Services" mean activities conducted by Sub-Contractors related to exploration, field development and production of Petroleum.

"Block" means an area delimited by geographical coordinates, designated for the exploration and production of Petroleum.

"Contractor" means any Vietnamese or foreign organization or individual who is permitted to conduct Petroleum Operations under a Petroleum Contract.

"Sub-Contractor" means any Vietnamese or foreign organization or individual who enters into a Contract with a Contractor or Petroleum Joint Venture Enterprise to render Petroleum Services.

"Petroleum Joint Venture Enterprise" means a joint venture enterprise established under a Petroleum Contract or Treaty entered into by and between the Government of Vietnam and a foreign government.

Executors (Operators) are organizations and/or individuals representing the parties to a petroleum contract and executing activities within the authorized scope.

Petroleum investment promotion projects are projects conducting petroleum activities in deep-water and offshore areas and areas with exceptionally difficult geographical and geological conditions according to the list of blocks decided by the Prime Minister.

Chapter II

Petroleum Operations

Article 4 An organization or individual conducting Petroleum Operations shall utilize advanced technology and comply with Vietnamese law regarding the protection of natural resources and the environment, and the safety of person and property.

Article 5 An organization or individual conducting Petroleum Operations shall have a plan for environmental protection, take all measures to prevent pollution, promptly eliminate sources of pollution, and be responsible for remedying all consequences of pollution.

Article 6 An organization or individual conducting Petroleum Operations shall establish a safety zone around an installation servicing Petroleum Operations in compliance with regulations of the Government of Vietnam.

Article 7 An organization or individual conducting Petroleum Operations shall obtain and maintain insurance for facilities and installations servicing Petroleum Operations, environmental insurance and other forms of insurance in compliance with Vietnamese law and in accordance with international practices of the petroleum industry.

Article 8 The exploration acreage covered by a Petroleum Contract shall be determined based upon the blocks delimited by the Government of Vietnam.

Article 9 Petroleum Operations shall not be conducted in any areas declared by the State of Vietnam to be off-limits or provisionally off-limits for reasons of national defense, national security or public interest.

In the event any Petroleum Operations that have been permitted are prohibited or temporarily prohibited, the Government of Vietnam shall make appropriate settlement for the damages to organizations or individuals resulting from such prohibition or temporary prohibition.

Article 10 The Government of Vietnam permits an organization or individual to conduct scientific research, exploration for and production of minerals and natural resources other than Petroleum in the area covered by a Petroleum Contract in compliance with Vietnamese law. These operations shall not hinder or be detrimental to Petroleum Operations.

Article 11 All the samples, cores, data and information acquired during the conduct of Petroleum Operations are the property of the State of Vietnam. The handling and utilization of such samples, cores, data and information shall comply with Vietnamese law.

Article 12 An organization or individual conducting Petroleum Operations is permitted to install and operate and maintain fixed installations and equipment servicing Petroleum Operations; to construct and use transport routes, pipelines, and warehouses for the purpose of transporting and storing Petroleum in compliance with Vietnamese law.

The ownership of the above installations and equipment shall belong to the State of Vietnam from the date agreed upon by the parties to a Petroleum Contract.

Article 13 Upon the termination of Petroleum Operations, the organization or individual shall clear the used acreage and remove fixed installations and equipment at the request of State management authorities having jurisdiction.

Article 14 The Vietnam Oil and Gas Corporation (known in its international dealings as "PETROVIETNAM") is a State-owned business enterprise founded by the Government of Vietnam to conduct Petroleum Operations and enter into Petroleum Contracts with organizations and individuals for the conduct of Petroleum Operations in accordance with this Law.

Chapter III

Petroleum Contract

Article 15 *A petroleum contract may be signed in the form of production-sharing contract, joint-venture contract or other contractual forms.*

A petroleum contract must be in conformity with the model contract issued by the Vietnamese Government with the following principal contents:

- 1. Legal status of organizations and/or individuals that shall jointly sign the contract.*
- 2. The contract's object(s).*
- 3. The area delimitation and the time schedule for returning the contractual area.*
- 4. The contract's duration.*
- 5. Conditions for termination of the contract ahead of time or for the extension of the contract.*
- 6. Commitments on working tempo and financial investment.*
- 7. Rights and obligations of the contractual parties.*
- 8. The recovery of investment capital, determination and distribution of profits, the host country's right over fixed assets after the capital recovery and the contract termination.*
- 9. Conditions for the assignment of rights and/or obligations of the contractual parties, the right of the Vietnam Oil and Gas Corporation to contribute investment capital.*

10. *Commitments on training and priority given to the employment of Vietnamese laborers and the use of Vietnamese services.*
11. *Responsibilities to protect the environment and ensure safety while conducting petroleum activities.*
12. *Methods of settling disputes which may arise from the contract and applicable laws.*

In addition to provisions and clauses stipulated in the model contract, the contractual parties may agree on other provisions and clauses, which must not be contrary to this Law's provisions and other relevant provisions of Vietnamese law.

The parties to a petroleum contract may agree to nominate a party from among them to act as the executor or hire an executor or establish a joint-execution company according to the Vietnamese Government's regulations. In cases where they obtain the Prime Minister's consent the parties to the petroleum contract may agree not to apply the model contract, but the contract to be signed must contain the principal contents prescribed in this Article.

Article 16 *Organizations and/or individuals wishing to sign petroleum contracts shall have to go through bidding under the specific regulations on bidding for projects on petroleum prospection, exploration and exploitation, promulgated by the Vietnamese Government. In special cases, the Prime Minister may appoint bidders in order to select partners for signing petroleum contracts.*

Article 17 *The term of a petroleum contract shall not exceed twenty-five (25) years, of which the prospection and exploration period shall not exceed five (5) years.*

For petroleum investment promotion projects and natural gas prospection, exploration and exploitation projects, the term of petroleum contracts shall not exceed thirty (30) years, of which prospection and exploration period shall not exceed seven (7) years.

The validity of a Petroleum Contract and validity of exploration period may be extended, but not exceeding five (5) years for Petroleum contract and two (2) years for exploration period.

If discovering gas with commercial value, while lacking the consumption market as well as conditions on pipelines and suitable treatment facilities, contractors may retain the areas where gas is found. The duration of retention of such an area shall not exceed five (5) years and may, in special cases, be extended for two (2) more years. Pending the consumption market and the conditions on pipelines and suitable treatment facilities, the contractors shall have to proceed with the work already committed in the petroleum contracts.

*In **force majeure** circumstances or other special cases, the parties to a petroleum contract may agree upon the mode of temporary cessation of the exercise and performance of a number of rights and obligations specified in the petroleum contract. The temporary cessation period due to **force majeure** circumstances shall last till the disappearance of such **force majeure** events. The temporary cessation period in other special cases shall be specified by the Vietnamese Government, but it must not exceed three (3) years.*

*The extended prospection and exploration period, the period of retention of the area where gas with commercial value is found and the period of temporary cessation of the exercise and performance of a number of rights and obligations in a petroleum contract in **force majeure** circumstances or in other special cases shall not be counted into the term of such petroleum contract.*

A petroleum contract may be terminated ahead of time provided that the contractor has fulfilled its committed obligations and such termination is agreed upon by the contractual parties.

Article 18 *The prospection and exploration area for a petroleum contract shall not cover more than two (2) blocks. In special cases, the Vietnamese Government may permit a prospection and exploration area for a petroleum contract to cover more than two (2) blocks.*

Article 19 *The contractors shall have to return the prospection and exploration areas according to the Vietnamese Government's regulations. Areas where temporary cessation agreements are effected according to provisions of Article 17 of this Law shall not be returned within temporary suspension periods.*

Article 20 The Contractor and the Vietnam Oil and Gas Corporation shall agree in a Petroleum Contract upon work program and minimum commitments on financial investment during the exploration period.

Article 21 Upon discovering Petroleum, the Contractor and the Vietnam Oil and Gas Corporation shall submit a report and provide all the required information about such discovery to State management authorities having jurisdiction.

In case a commercial discovery is made, the Contractor shall proceed immediately with an appraisal program, prepare a reserves evaluation report, and a field development and production scheme to submit to State management authorities having jurisdiction for approval.

Article 22 The language of the Petroleum Contract signed with foreign organizations, individuals and the documents attached thereto shall be the Vietnamese language and a commonly used foreign language as may be agreed upon by the Vietnam Oil and Gas Corporation and such organizations and/or individuals. Both the Vietnamese version and the foreign language version are equally authentic.

Article 23 A Petroleum Contract shall take effect upon the approval of the Government of Vietnam.

Article 24 Any total or partial assignment of a Petroleum Contract by the parties to the Contract shall only be effective after it is approved by the Government of Vietnam.

The Vietnam Oil and Gas Corporation shall have the preemptive right to acquire the Petroleum Contract or portion thereof subject to assignment of interest.

Article 25 The Vietnam Oil and Gas Corporation shall have the right to participate in capital investment under a Petroleum Contract. Its share of capital investment, terms of participation, reimbursement of expenses incurred by Contractor, and operating

agreement shall be provided in the Petroleum Contract in accordance with international practices of the Petroleum industry.

Article 25a *The parties to a petroleum contract may agree upon a level of recovery of expenses for petroleum prospection, exploration, field development and exploitation, of up to seventy percent (70%) of the annual petroleum output for petroleum investment promotion projects, and up to fifty percent (50%) for other projects, until the full recovery.*

Article 26 A Contractor is entitled to enter into Petroleum Service contracts with preference given to a Vietnamese organization or individual.

Vietnam will undertake flight service or enter into a joint venture contract with a foreign company providing flight service in support of Petroleum Operations.

Article 27 *Dispute arising from petroleum contracts must be first of all settled through negotiations and conciliation. In cases where negotiations and/or conciliation fail, if the disputing parties are Vietnamese organizations and individuals, the dispute shall be settled at a Vietnamese arbitration or court according to provisions of Vietnamese law. If one disputing party is a foreign organization or individual, the dispute shall be settled by mode stated in the petroleum contract. If the parties agree to settle their dispute at an international arbitration, the third country's arbitration or an arbitration chosen by themselves, such dispute shall be settled according to the procedures of such arbitration.*

Chapter IV

Rights and Obligations of Contractors

Article 28

1. A contractor shall have the following rights:
 - a) *To enjoy preferences and guarantees provided for by the Vietnamese law;*
 - b) *To use samples, data and information which have been obtained for conducting petroleum activities;*
 - c) *To recruit laborers to perform work of the petroleum contract on the basis of preferential employment of Vietnamese laborers;*
 - d) *To hire sub-contractor(s) according to provisions of this Law and in conformity with international practices of the petroleum industry;*
 - e) *To be exempted from import tax and export tax according to provisions of Article 34 of this Law;*
 - f) *To own its petroleum portion after fulfilling the financial obligations toward the Vietnamese State;*
 - g) *To export its petroleum portion as agreed upon in the petroleum contract without having to apply for export permit;*

- h) To recover its investment capital as agreed upon in the petroleum contract.*
2. *Contractors being foreign organizations or individuals shall be entitled to open accounts in Vietnam and abroad, to transfer abroad income from the sale of petroleum that is part of recovered expenses, profits and other lawful revenues earned in the course of petroleum activities.*
 3. *Contractors that are foreign organizations or individuals shall be entitled to buy foreign currencies at commercial banks to meet requirements of current transactions and other permitted transactions according to provisions of the legislation on foreign currency balance ensured for important projects.*

Article 29 *Sub-contractors shall enjoy rights prescribed at Points a and c, Clause 1, Article 28 and Article 34 of this Law. Sub-contractors being foreign organizations and individuals shall be entitled to transfer abroad their recovered expenses and profits earned in the course of petroleum service activities.*

Article 30 *A contractor shall have the following obligations:*

1. *To comply with the Vietnamese law;*
2. *To fulfill its commitments inscribed in the petroleum contracts;*
3. *To pay taxes and fees as prescribed by the Vietnamese law;*
4. *To transfer technologies, to train and employ Vietnamese officials and workers, and to ensure laborers' interests;*
5. *To apply measures for environmental protection and ensuring of safety in petroleum activities;*
6. *To report petroleum activities to the competent State management agency(ies) and the Vietnam Oil and Gas Corporation;*
7. *To supply necessary documents to inspection delegations;*
8. *To remove and dismantle installations, equipment and facilities upon the termination of petroleum activities at the request of the competent State management agency(ies);*
9. *To sell on the Vietnamese market a portion of crude oil under its ownership at the international competitive price at the Vietnamese Government's request and sell natural gas on the basis of agreements in gas development and exploitation projects.*

Article 31 *Sub-contractors shall have the obligations stipulated in Items 1, 2, 3, 4, 5 and 7 of Article 30 of this Law.*

Chapter V

Royalty, Taxes and Fees

Article 32 Organizations and individuals that exploit petroleum must pay natural resources tax. Natural resources tax shall be calculated according to the actual exploitation output in the taxation period for each petroleum contract. Natural resources tax rate for crude oil shall be set at between four percent (4%) and twenty-five percent (25%). Natural resources tax rate for natural gas shall be set at between zero percent (0%) and ten percent (10%). The Vietnamese Government shall prescribe specific tax rates within tax rate bracket stipulated in this Article depending on the geographical, economic and technical conditions of petroleum fields and crude oil or natural gas output.

Article 33 Organizations and individuals that conduct the petroleum prospection, exploration and exploitation shall have to pay enterprise income tax at the tax rate of fifty percent (50%). Organizations and individuals that conduct the petroleum prospection, exploration and exploitation at petroleum investment promotion projects shall have to pay enterprise income tax at the tax rate of thirty-two percent (32%). Organizations and individuals that conduct the petroleum prospection, exploration and exploitation may be exempted from enterprise income tax for a maximum period of two (2) subsequent years. The exemption or reduction of enterprise income tax shall be provided for by the Vietnamese Government. Profits for reinvestment shall not be subject to reimbursement of enterprise income tax.

Article 34 Organizations and individuals that conduct the petroleum activities shall have to pay export tax and import tax according to provisions of the Law on Export Tax and Import Tax.

Equipment, machinery, spare parts and specialized Supplies necessary for petroleum activities which cannot be produced at home, shall be exempt from import tax. Goods temporarily imported for re-export in service of petroleum activities shall be exempt from export tax and import tax. Petroleum portion that is part of natural resources tax of the State (royalty) shall not be subject to export tax.

Article 35 In addition to taxes prescribed in Articles 32, 33 and 34 of this Law, organizations and individuals that conduct the petroleum activities shall have to pay other taxes, rental for the use of land surface and fees prescribed by the Vietnamese law. In cases where any changes in provisions of Vietnamese law cause damage to the interests or organizations and individuals that conduct the petroleum activities, the State shall take measures to adequately settle the interests of such organizations and individuals according to provisions of the Law on Foreign Investment in Vietnam. Equipment, machinery, spare parts, specialized transport means and supplies which need to be imported to conduct the prospection, exploration and field development activities, which cannot be produced at home, shall not be subject to value added tax. Foreign organizations and individuals that conduct petroleum activities shall have to pay tax on transfer of profits abroad according to provisions of the Law on Foreign Investment in Vietnam.

A foreign organization or individual conducting Petroleum Operations shall pay a profit transfer tax in accordance with the Law on Foreign Investment in Vietnam.

Article 36 Employees of Vietnamese and foreign nationality working for Contractors, Petroleum Joint Venture Enterprises and Sub-Contractors shall pay personal income tax as stipulated by Vietnamese law.

Article 37 As may be agreed in a Petroleum Contract, royalty and all other taxes payable by a Contractor or Petroleum Joint Venture Enterprise may be included in the share of production of the Vietnam Oil and Gas Corporation, provided that the Vietnam Oil and Gas Corporation undertakes to pay such royalty and taxes on behalf of the Contractor or Petroleum Joint Venture Enterprise.

Chapter VI

State Management of Petroleum Operations

Article 38 The State management of Petroleum Operations shall include:

1. Making decisions on strategies, plans and policies for the development of the Petroleum industry;
2. Issuing regulations with respect to the management of Petroleum Operations;
3. Monitoring, inspecting and supervising Petroleum Operations;
4. Designating and delimiting blocks or acreage for Petroleum exploration and production;
5. Making decisions on policies and forms of cooperation with foreign entities;
6. Approving Petroleum Contracts;
7. Establishing policies to promote or to restrict Petroleum exports to protect the interest of the State while taking into account Contractors' interest;
8. Monitoring, giving instructions and guidance to relevant authorities and localities in carrying out activities related to Petroleum Operations;
9. Resolving issues related to the right to conduct Petroleum Operations, and adjudicating any violations of this Law.

Article 39 The Government of Vietnam shall solely exercise the State management of Petroleum Operations.

The State Petroleum management authority shall be established in accordance with the Law on the Organization of the Government to assume the State management of Petroleum Operations.

Ministries and other State authorities shall carry out the State management of Petroleum Operations in accordance with their respective functions, powers and responsibilities.

Chapter VII

Inspection of Petroleum Operations

Article 40 Inspection of Petroleum Operations forms a specialized inspection in the Petroleum Industry with a view to ensuring compliance with the provisions of this Law and regulations, technical procedures, specifications and rules; to conserving Petroleum resources, protecting the environment, enforcing safety rules, and fulfilling obligations to the State of Vietnam by organizations and individuals conducting Petroleum Operations.

Article 41 The State Petroleum Management Authority shall establish and organize the implementation of the inspection function regarding Petroleum Operations.

In conducting the inspection of Petroleum Operations, the inspection team shall have the right:

1. To ask/request relevant organizations and individuals to provide documents and clarify issues relevant to the inspection;
2. To take measures for on-site technical verification;
3. To suspend or make recommendations to State authorities having jurisdiction to suspend Petroleum Operations that may cause accidents or serious damage to life and/or property, petroleum resources and pollution;
4. To adjudicate any violations of this Law within its jurisdiction or make recommendations regarding the adjudication of violations to State authorities having jurisdiction.

Article 42 An organization or individual conducting Petroleum Operations shall facilitate the inspection team in carrying out its duties and shall strictly observe all decisions made by the inspection team.

Any organization or individual shall have the right to appeal decisions of the inspection team as stipulated by Vietnamese law.

Chapter VIII

Adjudication of Violations

Article 43 Any organization or individual violating any provision of this Law shall be subject to warning and/or fine and/or confiscation of its facilities or other administrative sanctions depending on the severity of its violations.

Any individual whose violation also constitutes a crime shall be prosecuted in accordance with Vietnamese law.

Article 44 Any organization or individual conducting Petroleum Operations that cause damage to Petroleum resources, other natural resources and the environment or property of State, such organization or individual shall be liable for compensation for such damage in accordance with Vietnamese law.

Article 45 Any organization or individual who illegally obstructs Petroleum Operations shall be prosecuted for its violations in accordance with Vietnamese law.

Article 46 Organizations and individuals shall have the right to appeal any decisions made on adjudication of violations as stipulated by Vietnamese law.

Chapter IX

Implementation Provisions

Article 47 This Law and other provisions of Vietnamese law shall also apply to:

1. All installations, structures, facilities and equipment used for the purpose of Petroleum Operations in the exclusive economic zone and/or on the continental shelf of the Socialist Republic of Vietnam.
2. Installation, structures, facilities and equipment owned by Vietnamese organizations and/or individuals for the purpose of Petroleum Operations on the basis of cooperation with foreign entities in areas not under the jurisdiction of the Socialist Republic of Vietnam.

Article 48 The Government of Vietnam shall protect the economic interest of the parties to Treaties and Petroleum Contracts approved by the Government of Vietnam prior to the effective date of this Law.

Article 49 *In cases where an international treaty which Vietnam has signed or acceded to contains provisions different from those of this Law, such international treaty's provisions shall apply.*

Article 50 All prior regulations that are inconsistent with this Law are hereby abrogated. The Government of Vietnam shall provide Regulations for the implementation of this Law.

Article 51 *This Law takes effect on July 1st 2000. The Government shall amend and supplement documents detailing the implementation of the Petroleum Law to make them consistent with this Law.*

This Law was passed on June 9, 2000 by the Xth National Assembly of the Socialist Republic of Vietnam at its 7th session.

Annex 2

Revised Petroleum Decree (Unofficial Translation¹¹)

DECREE No. 48/2000/ND-CP DATED
12 SEPTEMBER 2000 OF GOVERNMENT
DETAILING THE IMPLEMENTATION OF THE
PETROLEUM LAW

THE GOVERNMENT

- Pursuant to the 30th September 1992 Law on Organization of the Government;
- Pursuant to the Petroleum Law of 6 July 1993;
- Pursuant to the 9th June 2000 Law Amending and Supplementing a Number of Articles of the Petroleum Law;
- At the proposal of the Minister - Chairman of the office of the Government,

DECREES:

Chapter I

GENERAL PROVISIONS

Article 1. Scope of regulation

This Decree details the implementation of the Petroleum Law passed on 6 July 1993 by the IXth National Assembly of the Socialist Republic of Vietnam and the Law Amending and Supplementing a Number of Articles of the Petroleum Law passed on 9th June 2000 by the 10th National Assembly of the Socialist Republic of Vietnam (hereinafter referred to collectively as the Petroleum Law).

¹¹ This English translation of the Petroleum Decree is an unofficial translation provided for informational purposes only. All questions of interpretation must be resolved by reference to the official Vietnamese text.

Article 2. Objects of application

This Decree applies to the activities of prospecting, exploring oil and gas, developing oil and gas fields and producing oil and gas, including processing, gathering, storing and transporting oil and gas from the production areas to the point of delivery and the petroleum service activities in the inland, islands, internal waters, territorial waters, economic exclusive zones and continental shelf of the Socialist Republic of Vietnam, as well as on projects means and facilities in service of petroleum activities as provided for in Article 47 of the Petroleum Law.

Article 3. Subjects entitled to carry out petroleum activities

Organizations and individuals entitled to carry out petroleum activities include:

1. Vietnam Oil and Gas Corporation;
2. Other State enterprises set up under the Law on State Enterprises;
3. Enterprises set up under the Enterprises Law;
4. Foreign-invested enterprises in Vietnam;
5. Foreign organizations and individuals making direct investments in Vietnam;
6. Overseas Vietnamese making investments in Vietnam.

Organizations and individuals defined in Clauses 2, 3, 4, 5 and 6 of this Article may conduct petroleum activities on the basis of petroleum contracts signed with the Vietnam Oil and Gas Corporation.

In case arbitrarily conducting petroleum activities, Vietnam Oil and Gas Corporation shall have to draw up plans to submit them to the Prime Minister for approval and have to abide by the provisions of the Petroleum Law, the State Enterprises Law, this Decree as well as other relevant provisions of Vietnamese laws.

Article 4. Term definition

In this Decree, the following terms shall be understood as follows:

1. "Fixed works" are works built and installed fixedly and used in service of petroleum activities.
2. "Contractual area" is the area determined on the basis of prospection and exploration blocks as agreed upon in the petroleum contracts or the remaining area after the return of area.
3. "Point of delivery" is the place agreed upon in the petroleum contract where the oil and gas ownership is transferred to the parties to the petroleum contract.
4. "Fair transaction contract" is the transaction contract between the buyer and the seller in the market relationship, excluding internal sale and purchase contracts of a company, between Governments, between Governmental organizations, or any transaction and exchange affected by irregular trade relations.

5. "Associated gas" is hydrocarbon in gaseous form, which is separated in the course of crude oil exploitation and processing.
6. "Field development" is the process of preparing and investing in the project construction, exploitation drilling, and equipment installation in order to put oil and gas fields into production as from the time such fields are declared having commercial value.
7. "Net oil and gas production" is the output of oil and gas exploited and retained from the contractual area and measured at the point of delivery.

Chapter II

PETROLEUM ACTIVITIES

Article 5. Project and Work programs

1. Organizations and individuals, when conducting oil and gas prospection, exploration and production activities must draw up conceptual plans, detailed plans for such activities, and submit them to the oil and gas State Management Body for consideration and approval. The time limit for consideration and approval shall not exceed sixty (60) days for a conceptual plan and thirty (30) days for detailed plan from the date of receiving such plans.
2. Organizations and individuals, when conducting oil and gas prospection, exploration and production activities, shall have to draw up annual work program corresponding to each period in conformity with the commitments in the petroleum contracts regarding the time limit, work contents, financing and send them to the Vietnam Oil and Gas Corporation for agreement on the implementation thereof.

Article 6. Applicable standards

In the conduct of petroleum activities, organizations and individuals shall have to apply relevant Vietnamese standards on safety, environment, techniques and technologies. In case of unavailability of the Vietnamese standards, the organizations and individuals carrying out petroleum activities may apply the standards defined in the international agreements, which Vietnam has acceded to or signed. The application of other standards must be permitted by the Ministry of Science, Technology and Environment.

Article 7. Documents on environment and safety

Organizations and individuals, before conducting oil and gas prospection, exploration and production activities, shall have to compile and submit to the competent State Management Bodies the following documents:

- The report on environmental impact assessment;
- The safety control program and the risk evaluation enclosed with measures to mitigate incidents and damages;
- The emergency response plans, including technical solutions and the utilization of means and equipments to overcome the incidents.

Article 8. Requirements on environment protection and safety

Organizations and individuals conducting oil and gas prospection, exploration and production activities shall have to perform the tasks to protect the environment and ensure the safety as follows:

1. Setting up safety zones and maintain safety signals for petroleum facilities, machinery and equipments as provided for in Article 11 of this Decree;
2. Applying safety measures according to the approved safety control program;
3. Implementing monitoring programs of environment changes, realizing environment protection plans, pollution prevention measures and overcoming consequences of incidents which caused environmental pollution according to the provisions of the environment protection legislation;
4. Minimizing adverse impacts or negative consequences on environment such as soil, water, forest and/or air pollution, causing harms to the flora and fauna systems, causing ecological imbalance or badly affecting the human environment;
5. Updating data and finalizing the report on risk evaluation, the report on implementation of emergency response plans;
6. Fully recording incidents and accidents which have occurred;
7. Issuing emergency notices and promptly applying remedial measures in case of accidents or incidents;
8. Applying measures to ensure labor safety.

Article 9. Responsibilities when incidents occur

Organizations and individuals conducting petroleum activities shall be held legally responsible for the human, material and environmental damage as well as for cleaning up and restoring the environment which has been directly or indirectly caused by petroleum activities.

Article 10. Requirements on natural resources preservation

Organizations and individuals conducting oil and gas prospection, exploration and production activities must abide by the regulations on preservation of natural resources as well as petroleum resources and produce oil and gas with the optimum recovery coefficients suitable to international practices in the oil and gas industry.

Article 11. Oil and gas safety zones

The safety zone for offshore drilling and exploiting works is five hundred meters (500m) outwards from the outmost edge of the works or from the anchoring position for floating facilities with the exception of special cases as decided by the Prime Minister. Within two (2) nautical miles from the outmost edge of the works, means and vessels are not allowed to anchor. Unauthorized persons are prohibited from infiltrating into the safety zones, except for special cases as may be decided by the Prime Minister. The safety zone around the oil and gas prospection, exploration and production works in land shall be defined by the oil and gas State Management Body, depending on the geographical and social conditions of the places where petroleum activities are carried out.

Article 12. Regulations on drilling

While conducting the drillings, organizations and individuals shall observe the following regulations:

1. Drilling shall be in accordance with the approved designs or approved altered designs;
2. Not carrying out drillings outside the contractual areas;
3. All documents and specimen collected in the course of drilling shall be retained and submitted to the Vietnam Oil and Gas Corporation;
4. Promptly notifying Vietnam Oil and Gas Corporation of other natural resources discovered while drilling.

Organizations and individuals conducting petroleum activities shall also have to abide by other provisions of the current regulations.

Article 13. Regulations on oil and gas production

Organizations and individuals producing oil and gas shall have to abide by the current regulations on oil and gas production, strictly comply with the contents of the conceptual plans as well as the field development plans, which have already been approved; apply advanced technical measures and use advanced equipment for optimum oil and gas recovery without causing harms to the earth's substrata the ecological environment and the field safety.

Article 14. Right to use equipment and means

The Vietnamese Government has the right to use equipments and means in service of petroleum activities, including pipelines and depots being managed and used by organizations or individuals conducting petroleum activities, provided that they shall not obstruct petroleum activities and not increase the costs for contractors.

Article 15. Obligation to dismantle works

Organizations and individuals conducting oil and gas prospection, exploration and production activities must draw up programs, plans and cost estimates for the dismantlement of fixed works in service of oil and gas prospection, exploration and production activities and submit them to the oil and gas State Management Body for approval. The dismantling expenses shall be calculated into the costs of oil and gas recovery. At the request of the oil and gas State Management Body, organizations and individuals carrying out oil and gas prospection, exploration and production activities may not dismantle or may dismantle only part of the above-said fixed works.

Article 16. Petroleum insurance

Organizations and individuals carrying out petroleum activities shall have to buy insurance in accordance with the provisions of Vietnamese law and international practices in the oil and gas industry, particularly insurance for the facilities in service of petroleum activities, environmental pollution insurance, human life insurance, property insurance and the third party's civil liability insurance. Insurance bought at Vietnamese insurance companies is encouraged.

Article 17. Vietnam Oil and Gas Corporation's responsibility to report

The Vietnam Oil and Gas Corporation shall have to forward to the oil and gas State Management Body the following documents:

1. Annual and long-term work program and plans on petroleum activities;
2. Quarterly and annual summary reports on the work performance and results of the petroleum activities;
3. The reports on implementation of economic and/or technical projects for petroleum activities;
4. Reports on important events and incidents related to petroleum activities;

Other reports at the request of the oil and gas State Management Body. The time limit and content for each type of document shall be stipulated by the oil and gas State Management Body.

Article 18. Information supply

Contractors shall have to fully supply information, data and reports on petroleum activities according to regulations of the oil and gas State Management Body. The competent State Management Bodies may request contractors to supply information and reports when necessary, in accordance with their respective State management functions.

Article 19. Keeping information confidential

Reports and information must be kept confidential according to the provisions of Vietnamese law; Organizations and individuals conducting petroleum activities may use and must archive in Vietnam the original documents, specimen and reports; may temporarily export for re-import such documents and specimen according to the regulations of competent State Bodies.

Chapter III

PETROLEUM CONTRACTS

Article 20. Forms of petroleum contract

Petroleum contracts shall be signed in the following forms:

- Production-sharing contracts;
- Joint operation contracts;
- Joint-venture contracts.

Besides the above contractual forms, the Vietnam Oil and Gas Corporation and partners may opt for other contractual forms.

Article 21. Operator

The nomination or hiring of the Operator shall be agreed upon in the petroleum contract or made in a separate document. The scope of authorized operation shall be agreed upon by contractual parties in the petroleum contract or document on nomination or

hiring of the Operator. The Operator may represent the contractual parties to conduct oil and gas prospecting, exploration and production activities, exercise the rights and perform the obligations within the scope of authorization under the agreement on nomination or hiring of operators, and abide by other relevant provisions of Vietnamese laws.

Article 22. Joint Operating Company

A Joint Operation Company is established to represent the contractual parties to conduct oil and gas prospecting, exploration and production activities; exercise the rights and perform the obligations within the scope of authorization under the agreement on joint operation, and abide by other relevant provisions of Vietnamese law. The Joint Operating Companies have their own seals, may open accounts, recruit labor, sign economic contracts and conduct other activities as authorized. The Ministry of Planning and Investment shall prescribe the organization and operation of the Joint Operating Companies.

Article 23. Bidding for blocks

The oil and gas State Management Body shall organize block bidding according to the regulations on bidding for oil and gas prospecting, exploration and production blocks, issued by the Vietnamese Government. Where only one partner participates in bidding or in other special cases, the Prime Minister shall decide the appointment of bidders at the proposal of the oil and gas State Management Body.

Article 24. Prospecting and exploration stage

The prospecting and exploration stage defined in Article 17 of the Petroleum Law may be divided into short phases. The time limits of short phases shall be agreed upon by the contractual parties.

Article 25. Extension of the prospecting and exploration stage

Where the prospecting and exploration stage expires while the contractors have not yet fulfilled their work programs, the time limit of the prospecting and exploration stage may be extended according to the provisions in Article 17 of the Petroleum Law. The contractors and the Vietnam Oil and Gas Corporation must submit the documents stating clearly the reasons for the extension to the Ministry of Planning and Investment for consideration and approval before the end of the prospecting and exploration stage.

Article 26. Retaining areas where gas is discovered

The gas discovery of commercial value as stipulated in Article 17 of the Petroleum Law means the gas discovery where, through the reserve evaluation and preliminary assessment by the contractors, the investment in exploitation shall yield results. The contractors and the Vietnam Oil and Gas Corporation shall have to compile documents stating clearly the reasons therefore and the proposed duration for temporary retaining of the areas where gas is discovered and submit them to the Prime Minister for consideration and decision. If the duration for retaining the area where gas is discovered has prolonged for up to five (5) years and the contractor still fails to find the gas outlets, the Prime Minister may permit further extension for two (2) more years at the request of the contractor and the Vietnam Oil and Gas Corporation. Where the contractor deliberately delays or lacks goodwill in reaching the agreement on the gas

purchase and sale contract, the permission of retaining the area with gas discovery may be suspended or may not be considered for extension.

Article 27. Temporarily ceasing the exercise of a number of rights and obligations in the petroleum contracts

1. Temporary cessation in case of force majeure.

Parties to a petroleum contract may agree upon the mode of temporary cessation of exercising a number of rights and obligations in the petroleum contract in case of force majeure circumstances under the provisions in Article 17 of the Petroleum Law. The force majeure events shall be agreed upon by the contractual parties in the petroleum contract. Where the force majeure circumstance ends but its consequences have not yet been overcome, the continuation of the temporary cessation of exercising a number of rights and obligations in the petroleum contract shall be considered and decided by the Prime Minister.

2. Temporary cessation in special cases.

Special cases of temporary cessation of exercising a number of rights and obligations in petroleum contracts under the provisions in Article 17 of the Petroleum Law mean cases of temporary cessation for national defense, security or other special reasons. The Prime Minister shall consider and decide case by case at the proposal of the contractors and the Vietnam Oil and Gas Corporation.

Article 28. Return of prospection and exploration areas

The contractors shall have to return the prospection and exploration areas under the following regulations:

1. Not less than 20% of the initial contractual area shall be returned by the end of each small phase of prospection - and exploration.
2. The entire remaining- contractual area shall be returned after the end of the prospection and exploration stage, excluding areas under reserve appraisal, field development or oil and gas production areas and the areas retained under the provisions of Article 17 of the Petroleum Law.

Contractors may voluntarily return areas at any time during the prospection and exploration stage. The voluntarily returned areas shall be subtracted from the obligation to return areas. The voluntarily returned areas shall not reduce the obligations already committed in the petroleum contracts. The returned areas must create simple geometric form. Fixed works must be dismantled from the returned areas under the provisions in Article 15 of this Decree.

Article 29. Work commitments

Contractors and Vietnam Oil and Gas Corporation must reach an agreement on work programs in the prospection and exploration stage with minimum commitments regarding the geophysics survey volume, number of drilled wells volume and other integrated studies as well as commitments regarding training, recruitment and technology transfer. The cost estimates for the above-mentioned minimum work commitment shall be considered the minimum financial commitment. A contractor shall be considered as having fulfilled the minimum financial commitment when the minimum work commitments have already been fulfilled. Where contractor asks for the termination of the petroleum contract but have not yet fulfilled the minimum work commitments, they shall have to return to the Vietnam Oil and Gas Corporation a sum of money corresponding to the work volume committed to perform but not yet completed which is calculated according to the minimum financial commitment.

Article 30. Early production

During the prospection and exploration stage, if the contractors conduct early production in the contractual areas, they shall have to submit to the oil and gas State Management Body the Early Production Plans for approval as stipulated by the Petroleum Law and this Degree.

Article 31. Work to be done after discovery of oil and gas

After discovering oil and gas contractors shall have to promptly notify and report on the study results, evaluation and relevant documents to the oil and gas State Management Body and Vietnam Oil and Gas Corporation. Contractors and Vietnam Oil and Gas Corporation shall have to reach an agreement in the petroleum contracts on the terms regarding criteria to determine fields of commercial value, time limit for submitting the field reserve appraisal programs, outline plan and field development plans.

Contractors shall have to notify the reserve appraisal results to the Vietnam Oil and Gas Corporation. If the appraisal results show that the field is of commercial value, the contractors are entitled to declare commercial discovery. Contractors and Vietnam Oil and Gas Corporation shall have to submit to the oil and gas State Management Body the reserve report and the field development plans for submission to the Prime Minister for approval. After the field development plan is approved, if the contractors fail to proceed with the field development and oil and gas production according to the time limit prescribed in the written approval, the oil and gas State Management Body is entitled to recover the fields.

Article 32. Using petroleum for production activities

In the course oil and gas production, contractors may use oil and gas exploited from the contractual areas for prospection, exploration and production activities at the levels suitable to the international practices in the petroleum industry.

Article 33. Periodical reports

In the course of oil and gas production, contractors shall have to submit periodical reports on exploitation output, constituents and percentage of oil and gas exploited from each field, each production subject to the Vietnam Oil and Gas Corporation. The above-

mentioned reports must also include information on oil and gas volume used in service of exploration and production, the volume of oil and gas lost or burned off.

Article 34. Using associated gas

Contractors may use associated gas produced in the contractual areas as fuel in services of petroleum activities at fields or for reinjection into wells. Associated gas shall be burned off only when so permitted by the oil and gas State Management Body. The Vietnamese Government shall be entitled to use free of charge the associated gas, which the contractors intend to burn off if this does not obstruct the contractors activities. In that case, the contractors shall have to facilitate such usage.

Article 35. Oil and gas field stretching beyond the contractual areas

Where oil and gas fields stretch beyond the contractual areas to blocks neither opened to bidding nor having bidders appointed, Vietnam Oil and Gas Corporation and the contractors shall agree to draw up projects for joint exploitation of the entire field and submit them to the Prime Minister for approval.

Article 36. Field unitisation

Where an oil and gas field of the contractual areas stretches into the areas of blocks already opened to bidding, or having bidders already appointed or with petroleum contracts already signed, the concerned parties shall agree to draw up the projects for joint exploitation of the entire field and submit them to the Prime Minister for approval.

Chapter IV

RIGHTS AND OBLIGATIONS OF ORGANIZATIONS AND INDIVIDUALS CONDUCTING PETROLEUM ACTIVITIES

Article 37. Right to sign contracts in service of petroleum activities

Organizations and individuals conducting oil and gas prospection, exploration and production activities shall have the right to sign, in service of petroleum activities, goods purchase and sale contracts, petroleum service contracts with subcontractors or with other organizations and individuals. Contractors and subcontractors shall have to prioritize the purchase of goods made and supplied by Vietnam, prioritize the signing of service contracts with Vietnamese organizations and/or individuals on the principle of ensuring the competitiveness in prices and quality.

Article 38. Regimes towards laborers

Contractors must work out the labor rules, wage scales, regime of bonus and allowance payment and other regimes for the laborers in conformity with the provisions of Vietnamese legislation on labor, taking into account international practices in the petroleum industry; payroll tables, and the annual plans for labor recruitment and training.

Article 39. Recruitment and signing of labor contracts

Foreign organizations and individuals conducting petroleum activities must prioritize the employment of Vietnamese laborers and may recruit foreigners to perform the jobs

which Vietnamese laborers remain unable to undertake, but have to channel funding and work out plans for training so that Vietnamese laborers can soon replace the foreigners. The labor recruitment must comply with the provisions of Vietnamese legislation on labor. Foreign organizations and individuals conducting petroleum activities may directly recruit and sign labor contracts with persons who have work permits.

Article 40. Rights to open accounts and buy foreign currencies

1. Contractors that are foreign organizations or individuals may open accounts in Vietnam and overseas. When opening accounts overseas, the contractors shall have to register them with Vietnam State Bank.
2. After fulfilling the tax obligations under the provisions of Vietnamese law, the contractors that are foreign organizations or individuals may transfer or retain abroad their income from the sale of oil and gas related to recovery costs, their profits and other lawful incomes in the course of petroleum activities.
3. Contractors that are foreign organizations or individuals may buy foreign currencies at commercial banks or credit institutions licensed to trade in foreign currencies in Vietnam to satisfy the requirements of current transactions or other licensed transactions under the provisions of Vietnamese legislation on foreign exchange management.

Article 41. Ensuring the balance of foreign currencies

1. Important projects ensured with foreign currency balance are oil and gas production projects of contractors that or foreign organizations or individuals, with all or part of oil and gas being sold on the Vietnamese market in service of particularly important projects invested under the Vietnamese Government's programs, and projects with oil and gas sold at the request of the Vietnamese Government as provided for in Clause 9 of Article 30 of the Petroleum Law.
2. The foreign currency amounts balanced by the Vietnamese Government under the provisions in Clause 1 of this Article are the foreign currency deficit amounts after the contractors that are foreign organizations or individuals have bought at commercial banks and credit institutions licensed to trade in foreign currencies in Vietnam, which however must not exceed the amounts of Vietnam dong earned by the contractors from the sale of oil and gas on the Vietnamese market.
3. The conversion of Vietnam Dong into freely convertible foreign currency(ies) shall be made at the exchange rates of the commercial banks announced at the time of conversion.

Article 42. The duty to sell crude oil on the Vietnamese market

In emergency cases, at the request of the Vietnamese Government, the contractors have the duty to sell a part of the crude oil under their ownership on the Vietnamese market. The crude oil volume to be sold on the Vietnamese market at the request of the Vietnamese Government is determined as a percentage (%) between the crude oil volume under such contractors' ownership and the total crude oil volume owned by all contractors producing oil and gas in Vietnam. The price of crude oil sold at the request

of the Vietnamese Government is the selling price at the international competitive price.

Article 43. Rights and obligations of joint-venture enterprises

Where a petroleum contract is signed in form of joint-venture contract, the joint-venture enterprises may enjoy rights and perform obligations agreed upon in the joint-venture contract, and the rights and obligations of the contractors are stipulated in this Chapter and the corresponding provisions of the Law on Foreign Investment in Vietnam.

Chapter V

PROVISIONS ON TAXATION AND FINANCE

Article 44. Royalty on crude oil

Organizations and individuals producing crude oil shall have to pay a royalty. The royalty on crude oil shall be determined on the incremental basis of the actual net aggregate production of crude oil exploited in each tax payment period calculated according to the daily average crude oil output from the entire contractual area. The index of the royalty on crude oil is stipulated as follows:

Exploitation output	Investment encouragement project	Other project
Up to 20,000 barrels/day	4%	6%
Over 20,000 to 50,000 barrels/day	6%	8%
Over 50,000 to 75,000 barrels/day	8%	10%
Over 75,000 to 100,000 barrels/day	10%	15%
Over 100,000 to 150,000 barrels/day	15%	20%
Over 150,000 barrels/day	20%	25%

Article 45. Royalty on natural gas

Organizations and individuals conducting production of natural gas shall have to pay a royalty.

The royalty on natural gas shall be determined on the incremental basis of the actual net aggregate production of natural gas exploited in each tax payment period, calculated according to the daily average gas output from the entire contractual area. The index of royalty on natural gas is stipulated as follows:

Exploitation output	Investment encouragement project	Other project
Up to 5 million m ³ /day	0%	0%
Over 5 million m ³ to 10 million m ³ /day	3%	5%
Over 10 million m ³ /day	6%	10%

Article 46. Royalty calculation prices

The price for calculation of royalty on crude oil is the average selling price of crude oil at the point of delivery under the fair transaction contracts in the tax payment period. The price for calculation of royalty on natural gas is the selling price under the fair transaction contract at the point of delivery in the tax payment period. Where crude oil or gas is not sold under the fair transaction contract, the price for royalty calculation shall be determined by the Ministry of Finance on the basis of the market price, taking into account the oil or gas quality, location and other relevant factors.

Article 47. Royalty payment mode

The royalty shall be paid in oil and/or gas, or in cash, or partly in cash and partly in oil and/or gas at the option of the tax agency. The tax agency shall notify organizations and individuals conducting oil and/or gas production 6 months in advance of the mode of royalty payment whether in cash or in oil and/or gas.

The royalty shall be temporarily paid monthly and settled quarterly. In case the royalty is collected in oil and/or gas, the tax payment location shall be the point of delivery. Where the tax agency request the royalty be paid at other location, the taxpayers shall be entitled to subtract the transport expenses and other direct expenses and costs arising from the change of tax payment location from the royalty amount to be paid.

Article 48. Enterprise income tax

Organizations and individuals conducting oil and gas prospection, exploration and production shall have to pay enterprise income tax. The bases for calculation of enterprise income tax shall be the total taxable income in the tax payment period and the tax rates prescribed in Article 33 of the Petroleum Law. The total taxable income shall include the income from the oil and gas prospection, exploration and production activities and other incomes. The income from oil and gas prospection, exploration and production activities is equal to the turnover minus the expenses related to oil and gas prospection, exploration and production activities in the tax payment period as prescribed in Articles 49 and 50 of this Decree. Other income shall include:

1. Difference between security purchase and sale;
2. Income from property ownership and property use rights;
3. Proceeds from assignment;
4. Earnings from deposits, capital lending;
5. Difference from foreign currency sale;
6. Recovery of bad debts which had been written off from accounting books;

7. Collection of payable debts whose creditors can not be identified;
8. Income from other turnovers related to oil and gas prospection, exploration and production activities after subtracting the expenses for creation of such income;
9. Other incomes.

Article 49. Turnover

Turnover from oil and gas prospection, exploration and production activities, which serves as a basis for determination of the income liable to enterprise income tax is the total value of oil and gas sold under a fair transaction contract. Where oil and/or gas is not sold according to the fair transaction contract, the turnover used for determination of income liable to enterprise income tax shall be determined by the way of multiplying the sold oil and/or gas volume by the price set by the Ministry of Finance according to the provisions in Article 46 of this Decree.

Article 50. Expenses subtracted for determination of income liable to enterprise income tax

The expenses to be subtracted for determination of income liable to enterprise income tax shall include:

1. Expenses permitted to be recovered under the agreement in the petroleum contracts;
2. Royalty;
3. Export tax;
4. Petroleum bonuses agreed upon in the petroleum contract;
5. Contributions as financial support for social and charity purposes.

Article 51. Expenses not to be calculated into recoverable expenses

The expenses not to be calculated into recoverable expenses shall include:

1. Costs and expenses incurred prior to the effectiveness of the petroleum contracts, except for the special cases as agreed upon in the petroleum contracts or approved by the competent State Management Bodies;
2. Assorted petroleum bonuses and other non-recoverable undertakings as agreed upon in the petroleum contracts;
3. The interests on loans for investment in exploration, field development and oil and gas production;
4. Fines and compensation for damages and losses incurred due to the faults of such organizations or individuals;
5. The payment of royalty, export tax, value added tax, enterprise income tax in Vietnam and overseas, and tax on profit transfer abroad;
6. Losses indemnified by insurance;
7. Financial support for social and charity purposes;

8. Unreasonable or unjustifiable expenses which cannot be evidenced in the auditing, tax settlement and inspection.

Article 52. Enterprise income tax exemption and reduction

Organizations and individuals conducting oil and gas exploration and production under the investment encouragement projects shall be entitled to enterprise income tax exemption for the first year since the taxable income is generated, and fifty-percent (50%) reduction of their taxable enterprise income tax amount for one following year. The Prime Minister shall decide the specific cases entitled to enterprise income tax exemption for the first two years since the taxable income is generated and fifty-percent (50%) reduction of the taxable enterprise income tax amount for two subsequent years.

Article 53. Mode of enterprise income tax payment

The enterprise income tax shall be collected in cash and temporarily paid every quarter and settled every year.

Article 54. Import tax exemption

1. The following goods items which are imported directly by organizations and/or individuals conducting oil and gas prospecting exploration and production activities or by entrusted agents shall be exempt from import tax:
 - Equipment, machinery, special-use transport means necessary for petroleum activities, special-use transport means for conveyance of workers (cars of 24 or more seats, water transport means) including components, details, spare parts: support auxiliaries, moulds, accessories accompanying the machinery, special-use transport means, the above-said transport means;
 - Supplies necessary for petroleum activities, which cannot be produced at home yet;
 - Medical equipment and emergency medicines for use on drilling platforms and floating works when they are approved by the Ministry of Health;
 - Goods temporarily imported for re-export in service of petroleum activities;
 - Office furniture and equipment in service of petroleum activities;
2. Goods prescribed in Clause 1 of this Article which are imported by subcontractors and/or other organizations and/or individuals for supply to organizations and individuals conducting oil and gas prospecting exploration and production activities through petroleum services contracts or goods supply contracts shall be exempt from import tax.

Article 55. Value added tax

1. The following goods and items imported directly by organizations and/or individuals conducting oil and gas prospecting, exploration and production activities or by entrusted agents shall not be liable to value added tax:
 - Equipment, machinery and their spare parts, special-use transport means, which cannot be produced at home yet but are necessary for oil and gas prospecting exploration and production activities.

- In case of importing a complete synchronous equipment and machinery line which is imported and not liable to value added tax, but includes equipment and/or machinery which can be domestically manufactured, the value added tax shall not be imposed;
 - Imported supplies which can not be produced in the country but are necessary for exploration and, production activities as well as field development;
 - Goods temporarily imported for re-export in service of oil and gas prospection, exploration and production activities.
2. Goods prescribed in Clause 1 of this Article, which are imported by subcontractors as well as other organizations and/or individuals for supply to organizations and/or individuals conducting oil and gas prospection exploration and production activities through oil and gas services contracts or goods supply contracts, shall not be liable to value added tax.

Article 56. Retrospective collection of tax arrears

Goods exempted from import tax under the provisions of Article 54, or not liable to value added tax under the provisions of Article 55 of this Decree, if being:

1. Assigned in Vietnam not for the purpose of servicing the petroleum activities, then must be permitted by the Trade Ministry and subject to retrospective payment of import tax as well as other kinds of tax according to the provisions of Vietnamese law;
2. Assigned in Vietnam for the purpose of servicing the petroleum activities, then must be permitted by the Trade Ministry, and exempted from retrospective payment of import tax but subject to the payment of other kinds of tax according to the provisions of Vietnamese law;
3. Transferring the ownership over supplies and equipment to the Vietnam Oil and Gas Corporation as agreed upon in the petroleum contracts, the contractors shall be exempt from retrospective payment of import tax and other taxes, but the Vietnam Oil and Gas Corporation shall have to pay taxes and charges related to the property ownership transfer and pay the levies for the use of capital with regard to the amount of capital being the value of assets received from the contractors.

Article 57. Determination of lists of equipment, machinery and supplies, which can be produced in the country

The Ministry of Planning and Investment shall issue the lists of equipment, machinery, special-use transport means and supplies, which can be produced in the country for use as basis for import tax exemption under the provisions in Article 54 and the determination of goods not liable to value added tax under the provisions in Article 55 of this Decree.

Article 58. Export tax exemption

1. Goods temporarily imported or goods imported but not used up shall be exempted from export tax when they are re-exported.

2. The oil and gas volume belonging to the royalty of the State, when being exported shall not be liable to export tax.

Article 59. Enterprise income tax paid due to transfer of petroleum contract-participating capital

1. Contractors that are foreign organizations or individuals conducting oil and gas prospection, exploration and production activities shall have to pay enterprise income tax on income generated from the transfer of capital participating in the petroleum contracts according to the provisions of the Law on Foreign Investment in Vietnam.
2. Vietnamese organizations and individuals conducting oil and gas prospection, exploration and production activities shall have to pay enterprise income tax on the income generated from the transfer of the capital participating in the petroleum contracts according to the Enterprise Income Tax Law.

Article 60. Taxes to be paid by subcontractors

Subcontractors and other organizations or individuals who sign contracts for supplying of goods and services to organizations and/or individuals conducting oil and gas prospection, exploration and production activities shall have to pay assorted taxes according to the current law provisions, except in the case of import of goods prescribed in Article 54 and Article 55 of this Decree.

Article 61. Tax calculation year

The tax calculation year for organizations and individuals conducting oil and gas prospection, exploration and production activities shall commence on January 1st and end on December 31st of the calendar year. Organizations and individuals conducting oil and gas prospection, exploration and production activities may request the Ministry of Finance to permit the application of their own 12-month fiscal years for the enterprise income tax calculation and payment.

Article 62. Accounting regime registration

Organizations and individuals conducting oil and gas prospection, exploration and production activities shall have to register their applicable accounting regimes with the Ministry of Finance and bear examinations and inspections of the financial authorities.

Article 63. Financial reports

Organizations and individuals conducting oil and gas prospection, exploration and production activities shall have to send their annual financial reports to the investment license-granting bodies, the oil and gas State Management Body, the Ministry of Finance and the General Department of Statistics within 3 months from the end of the fiscal year. Before being sent to the above-said bodies, the financial reports must be audited by a Vietnamese independent auditing company or other independent auditing companies licensed to operate in Vietnam according to the provisions of Vietnamese legislation on audit.

Chapter VI

THE STATE MANAGEMENT OVER PETROLEUM ACTIVITIES

Article 64. The Government's and the Prime Minister's competence for State management over petroleum activities

1. The Government shall exercise the unified State management over petroleum activities. The Government shall perform the following tasks and exercise the following powers:
 - Issuing legal documents on management of petroleum activities;
 - Deciding on strategies, policies and planning for development of petroleum industry;
 - Deciding on cooperation in petroleum activities in the areas overlapping with foreign countries;
 - Deciding plans for international cooperation on oil and gas prospecting; exploration and production;
 - Considering and deciding other matters according to its competence.
2. The Prime Minister shall perform the following tasks and exercise the following powers:
 - Issuing lists of blocks, determining and adjusting boundaries of blocks;
 - Representing the Government in approving petroleum contracts;
 - Representing the Government in considering and deciding on the transfer of rights and obligations of petroleum contracts;
 - Considering and deciding on appointment of bidders in order to select partners for signing petroleum contracts;
 - Considering and deciding on other matters according to his/her competence.

Article 65. Competence of the oil and gas State Management Body

The oil and gas State Management Body in charge of petroleum shall perform the function of State management over petroleum activities according to the Government's regulations; have the following tasks and powers:

1. Drafting and submitting to the competent State bodies for promulgation or promulgating in accordance to its jurisdiction the legal documents on petroleum;
2. Drafting and submitting to the Government for approval the strategies and plans for development of petroleum industry;

3. Drafting and submitting to the Government for approval the development plans and important petroleum investment projects;
4. Submitting to the Government the policies of encouraging oil and gas exploration and production;
5. Submitting to the Prime Minister for decision on appointment of bidders to select partners for signing petroleum contracts;
6. Examining, inspecting and supervising petroleum activities;
7. Deciding on other matters under its competence of State management over petroleum activities.

Article 66. Competence of the ministries, the ministerial level agencies, the agencies attached to the Government and the provincial-level People's Committees for State management over petroleum

1. The Ministry of Planning and Investment shall appraise and submit to the Prime Minister for approval the bidding results for oil and gas exploration and production blocks; assume the prime responsibility for the appraisal, granting investment licenses and adjusting investment licenses for petroleum investment projects according to the provisions of legislation on foreign investment in Vietnam; submit to the Prime Minister for permission of transferring the rights and obligations of petroleum contracts; report to the Prime Minister on the situation of investment license granting in respect of petroleum in Vietnam; perform other tasks authorized by the Prime Minister.
2. The ministries the ministerial-level agencies the agencies attached to the Government and the provincial-level People's Committees shall, within the ambit of their respective jurisdiction have to settle or coordinate with the oil and gas State Management Body the Ministry of Planning and Investment and concerned bodies in settling matters regarding to land, rational use of water sources, particularly aquaculture areas, marine creature preservation areas, health resort and tourist areas and other matters related to the carrying out of petroleum activities.

Chapter VII

INSPECTION OF PETROLEUM ACTIVITIES

Article 67. Specialized inspection

Petroleum activity inspection is the specialized inspection which aims to ensure the observance of the Petroleum Law and legal documents related to petroleum activities. The oil and gas State Management Body shall perform the function of petroleum specialized inspection and issue decisions oil petroleum activity inspection. An inspection decision shall include the following principal contents:

- The composition of the inspection team;
- The inspected subjects;

- The inspection contents;
- The inspection place;
- The inspection duration;
- The requirements on inspected subjects.

Article 68. Rights and responsibilities of inspection teams

1. The-inspection teams shall have the following rights:

- To bring along necessary technical means in service of inspection activities.
- To request the inspected subjects to supply necessary documents within a given time limit. If passing such time limit the inspections' requests are not met, the inspection teams shall issue decisions on application of other necessary measures to gather materials according to the provisions of Vietnamese law.
- To issue decisions on temporary suspension of petroleum activities when there appear to be danger of accidents, serious losses and damages to people, property and environment.
- The temporary suspension duration must not exceed 15 days. Within 24 hours from the time when the decision is issued, the inspection team shall have to notify its decision to the competent State Management Bodies and propose handling measures. Within 15 days from the date when the inspection team issues the suspension decision, the competent State Management Bodies shall have to issue the handling decision.
- To propose the competent State Management Bodies to handle the acts breaching the legislation on petroleum.

2. When conducting the inspection, the inspection teams shall have to abide by the law provisions and take responsibility before law for their decisions.

Article 69. Decisions of inspection teams

Upon the conclusion of the inspection, the decisions of the inspection teams shall be notified to the inspected subjects and sent to the competent State Management Bodies. Where the inspected subjects disagree with the decisions of the inspection teams, the inspected subjects shall, within 30 days after the receipt of such decisions, be entitled to lodge their complaints to the competent State Management Bodies. Within 30 days after the receipt of the written complaints, the competent State Management Bodies shall have to reply about the settlement of such complaints.

Article 70. Executing decisions of the inspection teams

The inspected subjects must abide by the decisions of the inspection teams. In case of complaint, the inspected subjects still have to abide by the decisions of the inspection teams while awaiting the results of complaint settlement. Where the inspection teams' decisions are not executed by the inspected subjects, the settlement shall be handled according to the provisions of legislation on handling of administrative violations.

Chapter VIII

HANDLING OF VIOLATIONS

Article 71. Levels of sanction against acts of violation

1. The levels of pecuniary penalty against acts of violation prescribed in Article 43 of the Petroleum Law are detailed as follows:
 - a. Conducting illegal petroleum activities shall be subject to a fine of up to USD 100,000 (one hundred thousand);
 - b. Failing to abide by the technical process, criteria and regulations on oil and gas exploration and production causing damage to petroleum natural resources or environment, or damage to the property of the State and/or individuals shall, apart from the compensation to the damage be subject to a fine of up to USD 100,000 (one hundred thousand).
 - c. Conducting oil and gas prospection, exploration and production activities beyond the contractual areas without permission of the oil and gas State Management Body shall be subject to a fine of up to USD 50,000 (fifty thousand).
 - d. Falsely declaring and/or evading royalty, enterprise income tax and other kinds of tax shall, apart from the full payment of outstanding tax amounts, be subject to the payment of fines for false declaration and/or evasion of tax under the provisions of Vietnamese law.
 - e. Failing to notify the oil and gas State Management Body and the Vietnam Oil and Gas Corporation of natural resources other than petroleum, antiques, or valuable property discovered in the contractual areas shall be subject to a fine of up to USD 10,000 (ten thousand) and such specimen antiques and/or property are confiscated;
 - f. Obstructing, inspection activities shall be subject to a fine of up to USD 10,000 (ten thousand).
2. In addition to the above-prescribed pecuniary penalty levels, organizations and individuals committing acts of administrative violation shall also be subject to other forms and measures of administrative sanction under the provisions of the legislation on handling of administrative violations.

Article 72. Competence to handle violations

The competence to handle the above violations is stipulated as follows:

1. The Head of the oil and gas State Management Body shall handle the violations and decide the pecuniary penalty levels prescribed at Points a, b: c, d and a of Clause 1, Article 71 of this Decree.
2. Heads of the inspection teams shall handle the violations and decide the pecuniary penalty levels prescribed at Point f Clause 1, Article 71 of this Decree.

Chapter IX

IMPLEMENTATION PROVISIONS

Article 73. Law application

The parties of the contracts signed before the effective date of the 9th June, 2000 Law Amending and Supplementing a Number of Articles of the Petroleum Law shall continue to exercise the rights and perform the obligations as agreed in the petroleum contracts. The provisions of the 9th June, 2000 Law Amending and Supplementing a Number of Articles of the Petroleum Law shall also apply to petroleum contracts already signed; such application shall be effected only after this Law takes effect.

Article 74. Effect of the Decree

This Decree take effect in 15 days after its signing and replaces Decree No. 84/CP dated 17th December 1996. The previous regulation on petroleum activities, which are contrary to this Decree, shall all be annulled. The State Management Bodies shall, within the scope of their respective functions and powers, have to guide the implementation of this Decree.

Article 75. Responsibility for implementation

The ministers, the head of ministerial - level agencies, the heads of the agencies attached to the Government, the presidents of the People's Committees of the provinces and centrally-run cities and Vietnam Oil and Gas Corporation are held responsible for implementing this Decree.

FOR THE GOVERNMENT

PRIME MINISTER

PHAN VAN KHAI

Annex 3

Prime Minister's Decision No. 216 of 7 November 1998¹²

Government

No. 216/1998/QD-TTg

Hanoi, November 7, 1998

PRIME MINISTER'S DECISION ON INVESTMENT INCENTIVES FOR
PETROLEUM ACTIVITIES IN DEEP WATER, FAR-OFFSHORE AREAS AND
AREAS OF SPECIALLY DIFFICULT GEOGRAPHY, ECONOMY AND
TECHNOLOGY

PRIME MINISTER

Based on the Law on Government Organization dated September 30, 1992;

Based on the Petroleum Law dated July 6, 1993;

Based on the Law on Foreign Investment in Vietnam dated November 12, 1996;

In order to encourage investment in petroleum activities in deep water, far-offshore areas
and areas of specially difficult geography, economy and technology;

Upon the request of Minister of Finance (Official Letter No. 3398 TC/TCDN dated
September 5, 1998);

DECIDES:

Article 1 Organizations, individuals conducting petroleum activities enjoy favorable
incentive policies if having one of the following three conditions:

1. Petroleum activity in a area of water depth of over 200 meters.
2. Petroleum activity in a far-offshore area.

¹² This English translation is an unofficial translation provided for informational purposes only. All questions of interpretation must be resolved by reference to the official Vietnamese text.

3. Petroleum activity in an area of especially difficult geography, economy and technology.

Based on the decision of the authorized state management agency, PetroVietnam will announce the deep water, far-offshore areas and areas of especially difficult geography, economy and technology when issuing bidding documents of petroleum fields for exploration.

Article 2 Organizations and individuals conducting petroleum activities in Article 1–specified areas of this decision will enjoy the favorable taxes as follows:

1. Reduction of the corporate income tax rate from 50% down to 32%.
2. Favorable tax rate of 5% for overseas profit transmittal as stipulated in the Law on Foreign Investment in Vietnam.
3. Exemption of export tax for the portion of petroleum under State natural resource tax.

Article 3 Depending on each specific project, contract parties can come to arrangement in the petroleum contract on fee exemption of commission for signatures and reference document.

Article 4 Contract parties can come to an agreement in the petroleum contract on the terms and mode of interruption of the implementation of their contract rights, and obligations in case of arisen problems that cannot be foreseen and overcome. The duration of interruption will not be included in the duration of the contract.

In case of the discovery of a gas field of commercial value with unavailability of gas consumers, Contractor is allowed to get hold of the field area for the period approved by the Government.

Contract parties can come to an agreement in the contract on the conditions relating to the above interruption and hold of contract field area.

Article 5 Upon the request of PetroVietnam, the authorized state management agency can adjust the area for exploration as stipulated in item 4, Article 38 of the Petroleum Law, to be large enough, meeting the requirement for an area of a petroleum contract.

Article 6 Level of cost recovery for petroleum activities in the areas specified in Article 1 of this decision is 70% of the total actual exploitation output from the contract field.

Article 7 After meeting the full domestic gas requirement, or upon the consideration that the domestic market is not well conditioned for gas consumption, the Government will permit gas exploitation organizations and individuals to export gas.

Article 8 The State Bank of Vietnam ensures the gas exploitation organizations and individuals to exchange Vietnamese currency collected from their sale of gas in domestic market into foreign currencies.

Article 9 In case of serious breakdowns, organizations and individuals conducting petroleum activities enjoy exemption from normal customs clearances for personnel and equipment and materials for the purpose of emergency assistance.

Article 10 This decision comes into effect 15 days from the date of signing.

Ministers, Heads of Ministerial agencies, Heads of Government bodies, Chairmen of Provincial and City People's Committees under the Central Government, Chairman of Management Board and General Directors of PetroVietnam are responsible for the implementation of this decision.

Prime Minister

Phan Van Khai

(Signed and Stamped)