

BRAZILIAN PETROLEUM CORP  
Form 6-K  
April 10, 2007

---

**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

---

**FORM 6-K**

Report of Foreign Private Issuer  
Pursuant to Rule 13a-16 or 15d-16 of the  
Securities Exchange Act of 1934

**For the month of April, 2007**

**Commission File Number 1-15106**

---

**PETRÓLEO BRASILEIRO S.A. - PETROBRAS**  
(Exact name of registrant as specified in its charter)

**Brazilian Petroleum Corporation - PETROBRAS**  
(Translation of Registrant's name into English)

**Avenida República do Chile, 65**  
**20031-912 - Rio de Janeiro, RJ**  
**Federative Republic of Brazil**  
(Address of principal executive office)

Indicate by check mark whether the registrant files or will file annual reports under cover Form 20-F or Form 40-F.

Form 20-F  Form 40-F

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes  No

---

## MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of PETRÓLEO BRASILEIRO S.A. - **PETROBRAS** and subsidiaries ( the Company ) is responsible for establishing and maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting.

The Company's internal control over financial reporting is a process designed by, or under the supervision of, the Company's Audit Committee, Chief Executive Officer, Chief Financial Officer and effected by the Company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with accounting principles generally accepted in the United States. The Company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis. Therefore even those systems determined to be effective can provide only reasonable assurance with respect to consolidated financial statements preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2006, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations - COSO - of the Treadway Commission. Based on that assessment, management has concluded that as of December 31, 2006 the Company's internal control over financial reporting is effective.

Management's assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2006 has been audited by KPMG Auditores Independentes, the Company's independent registered public accounting firm, which opinion is stated in their report, dated April 5, 2007, included herein.

By: /s/ JOSÉ SERGIO GABRIELLE DE AZEVEDO

José Sérgio Gabrielli de Azevedo

*Title: Chief Executive Officer*

*April 5, 2007*

By: /s/ ALMIR GUILHERME BARBASSA

Almir Guilherme Barbassa

*Title: Chief Financial Officer*

*April 5, 2007*

**Petróleo Brasileiro S.A. - Petrobras and subsidiaries**

**Consolidated Financial Statements  
December 31, 2006, 2005 and 2004  
with Report of Independent  
Registered Public Accounting Firm**

---

**PETRÓLEO BRASILEIRO S.A. PETROBRAS  
AND SUBSIDIARIES**

CONSOLIDATED FINANCIAL STATEMENTS

Contents

<u>Report of Independent Registered Public Accounting Firm</u>	<u>1</u>
<u>Consolidated Balance Sheets</u>	<u>3</u>
<u>Consolidated Statements of Income</u>	<u>5</u>
<u>Consolidated Statements of Cash Flows</u>	<u>7</u>
<u>Consolidated Statements of Changes in Shareholders' Equity</u>	<u>9</u>
Notes to the Consolidated Financial Statements	
1. <u>The Company and its Operations</u>	<u>11</u>
2. <u>Summary of Significant Accounting Policies</u>	<u>12</u>
3. <u>Income Taxes</u>	<u>25</u>
4. <u>Cash and Cash Equivalents</u>	<u>29</u>
5. <u>Marketable Securities</u>	<u>30</u>
6. <u>Accounts Receivable, Net</u>	<u>31</u>
7. <u>Inventories</u>	<u>32</u>
8. <u>Recoverable Taxes</u>	<u>33</u>
9. <u>Property, Plant and Equipment, Net</u>	<u>34</u>
10. <u>Investments in Non-Consolidated Companies and Other Investments</u>	<u>41</u>
11. <u>Petroleum and Alcohol Account - Receivable from Federal Government</u>	<u>43</u>
12. <u>Financings</u>	<u>44</u>
13. <u>Financial Income (Expenses), Net</u>	<u>53</u>
14. <u>Project Financings</u>	<u>54</u>
15. <u>Capital Lease Obligations</u>	<u>60</u>
16. <u>Employees Post-Retirement Benefits and Other Benefits</u>	<u>61</u>
17. <u>Shareholders' Equity</u>	<u>76</u>
18. <u>Domestic and International Acquisitions</u>	<u>84</u>
19. <u>Commitments and Contingencies</u>	<u>92</u>
20. <u>Derivative Instruments, Hedging and Risk Management Activities</u>	<u>108</u>
21. <u>Natural Gas Derivative Contract</u>	<u>113</u>
22. <u>Financial Instruments</u>	<u>114</u>
23. <u>Segment Information</u>	<u>115</u>
24. <u>Related Party Transactions</u>	<u>128</u>
25. <u>Accounting for Suspended Exploratory Wells</u>	<u>130</u>
26. <u>Subsequent Events</u>	<u>134</u>
<u>Supplementary Information on Oil and Gas Exploration and Production</u>	<u>138</u>

**Report of Independent Registered Public Accounting Firm**

The Executive Board and Shareholder of  
Petróleo Brasileiro S.A. - Petrobras

We have audited the accompanying consolidated balance sheet of Petróleo Brasileiro S.A. - Petrobras (and subsidiaries) as of December 31, 2006, and the related consolidated statements of income, shareholders' equity and comprehensive income, and cash flows for the year then ended. We also have audited management's assessment, included in the accompanying Management's Report on the Internal Control over Financial Reporting, that Petróleo Brasileiro S.A. - Petrobras (and subsidiaries) maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Petróleo Brasileiro S.A. - Petrobras' management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on these consolidated financial statements, an opinion on management's assessment, and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audits. The accompanying consolidated balance sheet of Petróleo Brasileiro S.A. - Petrobras as of December 31, 2005 and the related consolidated statements of income, shareholders' equity and cash flows for each of the years ended December 31, 2005 and 2004, were audited by other auditors whose report thereon dated February 17, 2006, expressed a unqualified opinion on those statements.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Petróleo Brasileiro S.A. - Petrobras as of December 31, 2006, and the results of its operations and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, management's assessment that Petróleo Brasileiro S.A. - Petrobras maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Furthermore, in our opinion, Petróleo Brasileiro S.A. - Petrobras maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

As discussed in the Note 2(k) to the consolidated financial statements, the Company adopted the recognition and disclosure provisions of Statement of Financial Accounting Standards No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans*, as of December 31, 2006.

KPMG Auditores Independentes

Rio de Janeiro, Brazil  
April 5, 2007

**PETRÓLEO BRASILEIRO S.A. - PETROBRAS  
AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

December 31, 2006 and 2005

Expressed in Millions of United States Dollars

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents (Note 4)	12,688	9,871
Marketable securities (Note 5)	346	456
Accounts receivable, net (Note 6)	6,311	6,184
Inventories (Note 7)	6,573	5,305
Deferred income taxes (Note 3)	653	479
Recoverable taxes (Note 8)	2,593	2,087
Advances to suppliers	948	652
Other current assets	843	750
	<b>30,955</b>	<b>25,784</b>
<b>Property, plant and equipment, net (Note 9)</b>	<b>58,897</b>	<b>45,920</b>
<b>Investments in non-consolidated companies and other investments (Note 10)</b>	<b>3,262</b>	<b>1,810</b>
<b>Other assets</b>		
Accounts receivable, net (Note 6)	513	642
Advances to suppliers	852	462
Petroleum and alcohol account receivable from Federal Government (Note 11)	368	329
Government securities	479	364
Marketable securities (Note 5)	94	129
Restricted deposits for legal proceedings and guarantees (Note 19 (a))	816	775
Recoverable taxes (Note 8)	1,292	639
Deferred income taxes (Note 3)	61	7
Goodwill (Note 18)	243	237
Prepaid expenses	244	246
Inventories (Note 7)	210	236
Fair value asset of gas hedge (Note 20)	-	547
Other assets	394	511

		5,566	5,124
<b>Total assets</b>		<b>98,680</b>	78,638

See the accompanying notes to the consolidated financial statements.



	As of December 31,	
	2006	2005
<b>Liabilities and shareholders equity</b>		
<b>Current liabilities</b>		
Trade accounts payable	5,418	3,838
Short-term debt (Note 12)	1,293	950
Current portion of long-term debt (Note 12)	2,106	1,428
Current portion of project financings (Note 14)	2,182	2,413
Current portion of capital lease obligations (Note 15)	231	239
Accrued interest	247	221
Income taxes payable	235	409
Taxes payable, other than income taxes	3,122	3,014
Deferred income taxes (Note 3)	8	6
Payroll and related charges	1,192	918
Dividends and interest on capital payable (Note 17)	3,693	3,068
Contingencies (Note 19)	25	72
Advances from customers	880	609
Employees post-retirement benefits obligation Pension (Note 16)	198	206
Other payables and accruals	956	770
	<b>21,786</b>	<b>18,161</b>
<b>Long-term liabilities</b>		
Long-term debt (Note 12)	10,510	11,503
Project financings (Note 14)	4,192	3,629
Capital lease obligations (Note 15)	824	1,015
Employees post-retirement benefits obligation Pension (Note 16)	4,645	3,627
Employees post-retirement benefits obligation Health care (Note 16)	5,433	3,004
Deferred income taxes (Note 3)	2,916	2,166
Provision for abandonment (Note 9 (d))	1,473	842
Contingencies (Note 19)	208	238
Deferred purchase incentive (Note 21)	-	144
Other liabilities	428	318
	<b>30,629</b>	<b>26,486</b>
<b>Minority interest</b>	<b>1,966</b>	<b>1,074</b>
<b>Shareholders equity</b>		
Shares authorized and issued (Note 17)		
Preferred share 2006 1,850,394,698 shares and 2005 1,849,478,028 shares	7,718	4,772
Common share 2006 and 2005 2,536,673,672 shares	10,959	6,929
Capital reserve - fiscal incentive (Note 17)	174	159
Retained earnings		

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

Appropriated (Note 17)	<b>23,704</b>	20,095
Unappropriated	<b>10,541</b>	11,968
Accumulated other comprehensive income		
Cumulative translation adjustments	<b>(6,202)</b>	(9,432)
Postretirement benefit reserves adjustments net of tax - pension cost	<b>(2,052)</b>	(1,930)
Postretirement benefit reserves adjustments net of tax- health care cost	<b>(987)</b>	-
Unrealized gains on available-for-sale securities, net of tax	<b>446</b>	356
Unrecognized loss on cash flow hedge, net of tax	<b>(2)</b>	-
	<b>44,299</b>	32,917
<b>Total liabilities and shareholders equity</b>	<b>98,680</b>	78,638

See the accompanying notes to the consolidated financial statements.

**PETRÓLEO BRASILEIRO S.A. - PETROBRAS  
AND SUBSIDIARIES**

CONSOLIDATED STATEMENTS OF INCOME

December 31, 2006, 2005 and 2004

Expressed in Millions of United States Dollars

(except number of shares and earnings per share)

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Sales of products and services</b>	<b>93,893</b>	74,065	51,954
Less:			
Value-added and other taxes on sales and services	<b>(17,906)</b>	(14,694)	(10,906)
Contribution of intervention in the economic domain charge CIDE	<b>(3,640)</b>	(3,047)	(2,620)
<b>Net operating revenues</b>	<b>72,347</b>	56,324	38,428
Cost of sales	<b>40,061</b>	29,828	21,279
Depreciation, depletion and amortization	<b>3,673</b>	2,926	2,481
Exploration, including exploratory dry holes	<b>934</b>	1,009	613
Selling, general and administrative expenses	<b>4,989</b>	4,474	2,901
Impairment (Note 9 (e))	<b>21</b>	156	65
Research and development expenses	<b>727</b>	399	248
Other operating expenses	<b>1,081</b>	1,453	480
<b>Total costs and expenses</b>	<b>51,486</b>	40,245	28,067
Equity in results of non-consolidated companies (Note 10)	<b>28</b>	139	172
Financial income (Note 13)	<b>1,165</b>	710	956
Financial expenses (Note 13)	<b>(1,340)</b>	(1,189)	(1,733)
Monetary and exchange variation on monetary assets and liabilities, net (Note 13)	<b>75</b>	248	450
Employee benefit expense for non-active participants (Note 16)	<b>(1,017)</b>	(994)	(650)
Other taxes	<b>(594)</b>	(373)	(440)
Other expenses, net	<b>(17)</b>	(28)	(181)
	<b>(1,700)</b>	(1,487)	(1,426)

<b>Income before income taxes, minority interest and extraordinary item</b>	<b>19,161</b>	14,592	8,935
---	---------------	--------	-------

See the accompanying notes to the consolidated financial statements.

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Income tax expense (Note 3)</b>			
Current	(5,011)	(4,223)	(2,114)
Deferred	(680)	(218)	(117)
	<b>(5,691)</b>	(4,441)	(2,231)
Minority interest in results of consolidated subsidiaries	(644)	35	(514)
Income before extraordinary item	<b>12,826</b>	10,186	6,190
Extraordinary gain net of tax (Note 10 (b))	-	158	-
<b>Net income for the year</b>	<b>12,826</b>	10,344	6,190
<b>Net income applicable to each class of shares</b>			
Common	<b>7,417</b>	5,982	3,580
Preferred	<b>5,409</b>	4,362	2,610
<b>Net income for the year</b>	<b>12,826</b>	10,344	6,190
<b>Basic and diluted earnings per share (Note 17 (c))</b>			
<b>Common and preferred</b>			
Before effect of extraordinary item	<b>2.92</b>	2.32	1.41*
After effect of extraordinary item	<b>2.92</b>	2.36	1.41*
<b>Basic and diluted earnings per ADS</b>			
Before effect of extraordinary item	<b>11.68</b>	9.28	5.64*
After effect of extraordinary item	<b>11.68</b>	9.44	5.64*
<b>Weighted average number of shares outstanding</b>			
Common	<b>2,536,673,672</b>	2,536,673,672	2,536,673,672*
Preferred	<b>1,849,903,144</b>	1,849,478,028	<u>1,849,478,028*</u>

\* Restated for the effect of the 4-1 stock split on September 1, 2005 (see Note 17).

See the accompanying notes to the consolidated financial statements.

**PETRÓLEO BRASILEIRO S.A. - PETROBRAS  
AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

December 31, 2006, 2005 and 2004

Expressed in Millions of United States Dollars

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Cash flows from operating activities</b>			
Net income for the year	<b>12,826</b>	10,344	6,190
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation, depletion and amortization	<b>3,673</b>	2,926	2,481
Dry hole costs	<b>493</b>	597	520
Loss on property, plant and equipment	<b>225</b>	292	231
Minority interest in results of consolidated subsidiaries	<b>644</b>	(35)	514
Deferred income taxes	<b>680</b>	218	117
Foreign exchange and monetary loss (gain)	<b>465</b>	140	23
Accretion expense asset retirement obligation	<b>32</b>	51	33
Impairment of oil and gas properties	<b>21</b>	156	65
Provision for uncollectible accounts	<b>78</b>	118	164
Equity in the results of non-consolidated companies	<b>(28)</b>	(139)	(172)
Financial income (loss) on hedge operations	<b>434</b>	170	(466)
Others	<b>-</b>	(8)	23
<b>Decrease (increase) in operating assets</b>			
Accounts receivable	<b>308</b>	(1,510)	(1,027)
Petroleum and alcohol account	<b>(7)</b>	(9)	(20)
Interest receivable on government securities	<b>4</b>	3	(38)
Inventories	<b>(533)</b>	38	(1,527)
Advances to suppliers	<b>(552)</b>	(167)	3
Prepaid expenses	<b>32</b>	38	(70)
Recoverable taxes	<b>(552)</b>	(540)	(578)
Others	<b>261</b>	82	173
<b>Increase (decrease) in operating liabilities</b>			
Trade accounts payable	<b>1,385</b>	275	838
Payroll and related charges	<b>200</b>	215	(20)
Taxes payable, other than income taxes	<b>(133)</b>	566	(65)
Income taxes payable	<b>(190)</b>	(56)	120
Employees post-retirement benefits obligation Pension	<b>489</b>	647	353
Employees post-retirement benefits obligation Health care	<b>656</b>	557	380
Accrued interest	<b>21</b>	8	18

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

Contingencies	(79)	(65)	81
Provision for abandonment	(57)	325	(171)
Other liabilities	281	(122)	(18)
<b>Net cash provided by operating activities</b>	<b>21,077</b>	15,115	8,155

See the accompanying notes to the consolidated financial statements.



	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Cash flows from investing activities</b>			
Additions to property, plant and equipment	<b>(14,643)</b>	(10,365)	(7,718)
Investment in non-consolidated companies	<b>(187)</b>	(71)	(142)
Investment in marketable securities	<b>205</b>	169	678
Acquisition of Liquigás Distribuidora S.A.	<b>-</b>	-	(511)
Acquisition of USA trading and refining companies	<b>(416)</b>	-	-
Received cash related to investment in Nigeria	<b>199</b>	-	-
Dividends received from non-consolidated companies	<b>130</b>	60	53
Restricted deposits for legal proceedings	<b>31</b>	-	(103)
<b>Net cash used in investing activities</b>	<b>(14,681)</b>	(10,207)	(7,743)
<b>Cash flows from financing activities</b>			
Short-term debt, net issuances and repayments	<b>228</b>	(1,058)	(680)
Proceeds from issuance and draw-down of long-term debt	<b>2,251</b>	1,697	1,457
Principal payments of long-term debt	<b>(2,555)</b>	(1,120)	(1,160)
Repurchase of securities Notes (see Note 12(c))	<b>(1,046)</b>	-	-
Proceeds from project financings	<b>1,524</b>	1,492	971
Payments of project financings	<b>(1,209)</b>	(1,392)	(652)
Payment of capital lease obligations	<b>(334)</b>	(134)	(331)
Dividends paid to shareholders	<b>(3,144)</b>	(2,104)	(1,785)
Dividends paid to minority interests	<b>(69)</b>	(6)	(24)
<b>Net cash provided by (used) in financing activities</b>	<b>(4,354)</b>	(2,625)	(2,204)
Increase (decrease) in cash and cash equivalents	<b>2,042</b>	2,283	(1,792)
Effect of exchange rate changes on cash and cash equivalents	<b>775</b>	732	304
Cash and cash equivalents at beginning of year	<b>9,871</b>	6,856	8,344
<b>Cash and cash equivalents at end of year</b>	<b>12,688</b>	9,871	6,856

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Supplemental cash flow information:</b>			
<b>Cash paid during the year for</b>			
Interest, net of amount capitalized	<b>877</b>	1,083	995

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

Income taxes	<b>4,686</b>	3,843	2,054
Withholding income tax on financial investments	<b>26</b>	29	69

**Non-cash investing and financing transactions during the year**

Recognition of asset retirement obligation SFAS 143	<b>632</b>	356	158
Consummation of gas hedge asset with deferred purchase incentive liability	-	-	169

See the accompanying notes to the consolidated financial statements.

**PETRÓLEO BRASILEIRO S.A. - PETROBRAS  
AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**

December 31, 2006, 2005 and 2004

Expressed in Millions of United States Dollars (except per-share amounts)

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Preferred shares</b>			
Balance at January 1,	4,772	4,772	2,973
Capital increase from undistributed earnings reserve (Note 17(a))	2,939	-	1,799
Capital increase from issue of preferred shares (Note 17(b))	7	-	-
<b>Balance at December 31,</b>	<b>7,718</b>	4,772	4,772
<b>Common shares</b>			
Balance at January 1,	6,929	6,929	4,289
Capital increase from undistributed earnings reserve (Note 17(c))	4,030	-	2,640
<b>Balance at December 31,</b>	<b>10,959</b>	6,929	6,929
<b>Capital reserve - fiscal incentive</b>			
Balance at January 1,	159	134	118
Transfer from unappropriated retained earnings	15	25	16
<b>Balance at December 31,</b>	<b>174</b>	159	134
<b>Accumulated other comprehensive loss</b>			
<b>Cumulative translation adjustments</b>			
Balance at January 1,	(9,432)	(12,539)	(14,450)
Change in the year	3,230	3,107	1,911
<b>Balance at December 31,</b>	<b>(6,202)</b>	(9,432)	(12,539)

**Postretirements benefit reserves adjustments net of taxes -  
pension cost**

Balance at January 1,	<b>(1,930)</b>	(1,975)	(1,588)
Accounting change SFAS 158	<b>(131)</b>	-	-
Other decreases (increases)	<b>(38)</b>	68	(586)
Tax effect on above	<b>47</b>	(23)	199
<b>Balance at December 31,</b>	<b>(2,052)</b>	(1,930)	(1,975)

**Postretirements benefit reserves adjustments net of tax -  
health care cost**

Balance at January 1,	-	-	-
Accounting change SFAS 158	<b>(987)</b>	-	-
<b>Balance at December 31,</b>	<b>(987)</b>	-	-

**Unrecognized gains (losses) on available-for-sale securities,  
net of tax**

Balance at January 1,	<b>356</b>	460	157
Unrealized gains (losses)	<b>137</b>	(158)	459
Tax effect on above	<b>(47)</b>	54	(156)
<b>Balance at December 31,</b>	<b>446</b>	356	460

See the accompanying notes to the consolidated financial statements.

Unrecognized loss on cash flow hedge, net of tax (Note 20 (e))	Year ended December 31,		
	2006	2005	2004
Balance at January 1	-		
Unrealized losses	(3)	-	-
Tax effect on above	1	-	-
	(2)	-	-
<b>Appropriated retained earnings</b>			
Legal reserve			
Balance at January 1,	2,225	1,520	1,089
Transfer from unappropriated retained earnings, net of gain or loss			
on translation	820	705	431
<b>Balance at December 31,</b>	<b>3,045</b>	<b>2,225</b>	<b>1,520</b>
<b>Undistributed earnings reserve</b>			
Balance at January 1,	17,439	9,688	9,372
Capital increase	(6,969)	-	(4,439)
Transfer from unappropriated retained earnings, net of gain or loss			
on translation	9,604	7,751	4,755
<b>Balance at December 31,</b>	<b>20,074</b>	<b>17,439</b>	<b>9,688</b>
<b>Statutory reserve</b>			
Balance at January 1,	431	318	235
Transfer from unappropriated retained earnings, net of gain or loss			
on translation	154	113	83
<b>Balance at December 31,</b>	<b>585</b>	<b>431</b>	<b>318</b>
<b>Total appropriated retained earnings</b>	<b>23,704</b>	<b>20,095</b>	<b>11,526</b>
<b>Unappropriated retained earnings</b>			
Balance at January 1,	11,968	13,199	14,141

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

Net income for the year	<b>12,826</b>	10,344	6,190
Dividends (per share: 2006 US\$0.83 to common and preferred share; 2005 US\$0.68 to common and preferred shares; 2004 - US\$0.42 to common and preferred shares)	<b>(3,660)</b>	(2,982)	(1,847)
Appropriation to fiscal incentive reserve	<b>(15)</b>	(24)	(16)
Appropriation to reserves	<b>(10,578)</b>	(8,569)	(5,269)
<b>Balance at December 31,</b>	<b>10,541</b>	11,968	13,199
<b>Total shareholders' equity</b>	<b>44,299</b>	32,917	22,506
<b>Comprehensive income (loss) is comprised as follows:</b>			
Net income for the year	<b>12,826</b>	10,344	6,190
Cumulative translation adjustments	<b>3,230</b>	3,107	1,911
Postretirements benefit reserves adjustments net of tax - pension cost	<b>(25)</b>	45	(387)
Unrealized gains (losses) on available-for-sale securities	<b>90</b>	(104)	303
Unrecognized loss on cash flow hedge	<b>(2)</b>	-	-
<b>Total comprehensive income</b>	<b>16,119</b>	13,392	8,017

See the accompanying notes to the consolidated financial statements.

**PETRÓLEO BRASILEIRO S.A. - PETROBRAS  
AND SUBSIDIARIES****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

Expressed in Millions of United States Dollars

(except when specifically indicated)

**1. The Company and its Operations**

PETRÓLEO BRASILEIRO S.A. - PETROBRAS is Brazil's national oil company and, directly or through its subsidiaries (collectively, "Petrobras" or the "Company"), is engaged in the exploration, exploitation and production of oil from reservoir wells, shale and other rocks, and in the refining, processing, trade and transport of oil and oil products, natural gas and other fluid hydrocarbons, in addition to other energy related activities. Additionally, Petrobras may promote the research, development, production, transport, distribution and marketing of all sectors of energy, as well as other related or similar activities.

Petrobras was incorporated under Law No. 2,004 on October 3, 1953. Until November of 1995, Petrobras was the exclusive agent of the Brazilian Federal Government (the "Federal Government") for purposes of exploiting the Federal Government's constitutional and statutory control over activities involving exploration, production, refining, distribution, import, export, marketing and transportation of hydrocarbons and oil products in Brazil and its continental waters. When adopted in 1953, the relevant provisions of the Brazilian constitution and statutory law gave the Federal Government a monopoly in these areas subject only to the right of companies then engaged in oil refining and the distribution of oil and oil products to continue those activities in Brazil. Therefore, except for limited competition from those companies in their grandfathered activities, Petrobras had a monopoly over its businesses for approximately 42 years. As a result of a change in the Brazilian constitution in November of 1995, and the subsequent and ongoing implementation of that change, Petrobras has ceased to be the Federal Government's exclusive agent in Brazil's hydrocarbons sector and up to 2001 had been operating in an environment of gradual deregulation and increasing competition.

In accordance with Law No. 9,478 ("Petroleum Law") and Law No. 9,990, dated August 6, 1997 and July 21, 2000, respectively, the fuel market in Brazil was totally liberalized beginning January 1, 2002 permitting other companies to produce and sell on the domestic market, and also to import and export oil products.

The Company also has oil and gas operations in international locations, with the most significant international operations being in other Latin American countries.

## **2. Summary of Significant Accounting Policies**

In preparing these consolidated financial statements, the Company has followed accounting policies that are in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The preparation of these financial statements requires the use of estimates and assumptions that affect the assets, liabilities, revenues and expenses reported in the financial statements, as well as amounts included in the notes thereto.

Estimates adopted by management include: oil and gas reserves, pension and health care liabilities, environmental obligations, depreciation, depletion and amortization, abandonment costs, contingencies and income taxes. While the Company uses its best estimates and judgments, actual results could differ from those estimates as future confirming events occur.

Certain prior years amounts have been reclassified to conform to current year presentation standards. These reclassifications had no impact on the Company's net income

### **(a) Basis of financial statements preparation**

The accompanying consolidated financial statements of PETRÓLEO BRASILEIRO S.A. - PETROBRAS (the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and the rules and regulations of the Securities and Exchange Commission (SEC). U.S. GAAP differs in certain respects from Brazilian accounting practice as applied by Petrobras in its statutory financial statements prepared in accordance with Brazilian Corporate Law and regulations promulgated by the Brazilian Securities and Exchange Commission (CVM).



**2. Summary of Significant Accounting Policies** (Continued)**(a) Basis of financial statements preparation** (Continued)

The U.S. dollar amounts for the years presented have been translated from the Brazilian Real amounts in accordance with Statement of Financial Accounting Standards SFAS No. 52 - Foreign Currency Translation ("SFAS 52") as applicable to entities operating in non-hyperinflationary economies. Transactions occurring in foreign currencies are first remeasured to the Brazilian Real and then translated to the U.S. dollar, with remeasurement gains and losses being recognized in the statements of income. While Petrobras has selected the U.S. Dollar as its reporting currency, the functional currency of Petrobras and all Brazilian subsidiaries is the Brazilian Real. The functional currency of PIFCo and certain of the special purpose companies is the U.S. dollar, and the functional currency of Petrobras Energia Participaciones S.A. - PEPSA is the Argentine Peso.

The Company has translated all assets and liabilities into U.S. dollars at the current exchange rate (R\$2.138 and R\$2.3407 to US\$1.00 at December 31, 2006 and 2005, respectively), and all accounts in the statements of income and cash flows (including amounts relative to local currency indexation and exchange variances on assets and liabilities denominated in foreign currency) at the average rates prevailing during the year. The net translation gain in the amount of US\$3,230 in 2006 (2005 - US\$3,107 and 2004 - US\$1,911) resulting from this remeasurement process was excluded from income and presented as a cumulative translation adjustment ("CTA") within Accumulated Other Comprehensive Income in the consolidated statements of changes in shareholders' equity.

**(b) Basis of consolidation**

The consolidated financial statements include the accounts of the Company and all majority-owned subsidiaries in which (a) the Company directly or indirectly has either a majority of the equity of the subsidiary or otherwise has management control, or (b) the Company has determined itself to be the primary beneficiary of a variable interest entity in accordance with FIN 46(R).

**2. Summary of Significant Accounting Policies (Continued)****(b) Basis of consolidation (Continued)**

The following majority-owned subsidiaries and variable interest entities are consolidated:

<b>Subsidiary companies</b>	<b>Activity</b>
Petrobras Química S.A. PETROQUISA and subsidiaries	Petrochemical
Petrobras Distribuidora S.A. BR and subsidiaries	Distribution
BRASPETRO Oil Services Company BRASOIL and subsidiaries	International operations
BRASPETRO Oil Company BOC and subsidiaries	International operations
Petrobras International BRASPETRO B.V. PIB and subsidiaries (1)	International operations
Petrobras Gás S.A. GASPETRO and subsidiaries	Gas transportation
Petrobras International Finance Company PIFCo and subsidiaries	Financing
Petrobras Transporte S.A. TRANSPETRO and subsidiaries	Transportation
Downstream Participações Ltda. and subsidiaries	Refining and distribution
Petrobras Netherlands BV PNBV and subsidiaries	Exploration and Production
Petrobras Comercializadora de Energia Ltda. PCEL	Energy
Petrobras Negócios Eletrônicos S.A. E-PETRO and subsidiaries	Corporate
5283 Participações Ltda.	Corporate
Fundo de Investimento Imobiliário RB Logística FII	Corporate
UTE Nova Piratininga Ltda.	Energy
FAFEN Energia S.A.	Energy
Baixada Santista Energia Ltda.	Energy
Sociedade Fluminense de Energia Ltda. SFE (2)	Energy
TERMOAÇU S.A.	Energy
TERMOBAHIA Ltda. (3)	Energy
TERMOCEARÁ Ltda.	Energy
TERMORIO S.A. (3)	Energy
TERMOMACAÉ Ltda. (4)	Energy
TERMOMACAÉ Comerc. de Energia Ltda. (4)	Energy
Ibiritermo S.A.	Energy
 <b>Special purpose entities consolidated according to FIN 46(R)</b>	 <b>Activity</b>
Albacora Japão Petróleo Ltda.	Exploration and Production
Barracuda & Caratinga Holding Company B.V.	Exploration and Production
Companhia Petrolífera Marlim	Exploration and Production
NovaMarlim Petróleo S.A.	Exploration and Production
Cayman Cabiunas Investments Co.	Exploration and Production
Cia. de Desenv. e Modernização de Plantas Industriais - CDMPI	Exploration and Production
Companhia Locadora de Equipamentos Petrolíferos S.A. CLEP	Exploration and Production
PDET Off-shore S.A.	Exploration and Production
Companhia de Recuperação Secundária S.A.	Exploration and Production
EVM Leasing Corporation	Exploration and Production
Nova Transportadora do Nordeste S.A.	Transportation

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

Nova Transportadora do Sudeste S.A.	Transportation
Gasene Participações Ltda.	Transportation
Manaus Geração Termelétrica Participações Ltda.	Energy
Blade Securities Limited.	Corporate
Codajás Coari Participações Ltda.	Transportation
Charter Development CDC (5)	Exploration and Production
Companhia Mexilhão do Brasil (6)	Exploration and Production

**2. Summary of Significant Accounting Policies (Continued)****(b) Basis of consolidation (Continued)**

- (1) Parent Company of Petrobras Energia S.A. - PEPSA others international companies.
- (2) Consolidated according to ARB 51, commencing December 31, 2005. Consolidated according to FIN 46(R), commencing December 31, 2003 until September 30, 2005. Formerly were not consolidated in Petrobras financial statements.
- (3) Consolidated according to ARB 51, commencing December 31, 2005. Consolidated according to FIN 46(R), commencing December 31, 2003 until September 30, 2005. Formerly were accounted for as capital leases pursuant to SFAS 13.
- (4) Former Macaé Merchant. Consolidated according to ARB 51, commencing December 31, 2005. Macaé Merchant formerly was consolidated according to FIN 46(R). (see Note 18(1)).
- (5) Consolidated according to FIN 46(R). Company is a new SPE formed in 2005 to support project finance.
- (6) Consolidated according to FIN 46(R). Company is a new SPE formed in 2006 to support project finance.

**(c) Cash and cash equivalents**

Cash and cash equivalents consist of highly liquid investments that are readily convertible into cash and have an original maturity of three months or less at date of acquisition.

**(d) Marketable securities**

Marketable securities are accounted for under SFAS No. 115 - Accounting for Certain Investments in Debt and Equity Securities ("SFAS 115") and have been classified by the Company as available-for-sale, held-to-maturity or trading based upon intended strategies with respect to such securities. The marketable securities classified as trading are short term in nature as the investments are expected to be liquidated, sold, or used for current cash requirements. The marketable securities classified as available-for-sale are long term in nature as the investments are not expected to be sold or otherwise liquidated in the next twelve months. Debt securities that management has the intent and the ability to hold to maturity are classified as held-to-maturity.

Trading securities are marked-to-market through current period earnings, available-for-sale securities are marked-to-market through other comprehensive income, and held-to-maturity securities are recorded at amortized cost.

**2. Summary of Significant Accounting Policies (Continued)****(d) Marketable securities (Continued)**

The Company has certain available-for-sale investments in companies with publicly traded shares. The Company also has available-for-sale and trading securities arising from its consolidation of investments in an exclusive fund. There were no transfers between categories of investments.

**(e) Accounts receivable**

Accounts receivable is stated at estimated realizable values. An allowance for doubtful accounts is provided in an amount considered by management to be sufficient to meet probable future losses related to uncollectible accounts.

**(f) Inventories**

Inventories are stated as follows:

- Raw materials are comprised principally of crude oil inventories, which are stated at the lower of average cost or market value.
- Oil products and fuel alcohol are stated, respectively, at average refining and purchase cost, adjusted when applicable to their realizable value.
- Materials and supplies are stated at average purchase cost, not exceeding replacement value and imports in transit are stated at identified cost.

**(g) Investments in non-consolidated companies**

The Company uses the equity method of accounting for all long-term investments for which it owns between 20% and 50% of the investee's outstanding voting stock or has the ability to exercise significant influence over operating and financial policies of the investee. The equity method requires periodic adjustments to the investment account to recognize the Company's proportionate share in the investee's results, reduced by receipt of investee's dividends.

## 2. Summary of Significant Accounting Policies (Continued)

### (h) Property, plant and equipment

- Costs incurred in oil and gas producing activities

The costs incurred in connection with the exploration, development and production of oil and gas are recorded in accordance with the successful efforts method. This method requires that costs the Company incurs in connection with the drilling of developmental wells and facilities in proved reserve production areas and successful exploratory wells be capitalized. In addition, costs the Company incurs in connection with geological and geophysical activities are charged to the statements of income in the year incurred, and the costs relating to exploratory dry wells on unproven reserve properties are charged to the statements of income when determined as dry or uneconomical.

- Capitalized costs

The capitalized costs are depreciated based on the unit-of-production method using proved developed reserves. These reserves are estimated by the Company's geologists and petroleum engineers in accordance with SEC standards and are reviewed annually, or more frequently when there are indications of significant changes in the Company's reserves.

- Property acquisition costs

Costs of acquiring developed or undeveloped leaseholds including lease bonus, brokerage, and other fees are capitalized. The costs of undeveloped properties that become productive are transferred to a producing property account.

- Exploratory costs

Exploratory wells that find oil and gas in an area requiring a major capital expenditure before production begins are evaluated annually to assure that commercial quantities of reserves have been found or that additional exploration work is underway or planned. Exploratory costs related to areas where commercial quantities have been found are capitalized, and exploratory costs where additional work is underway or planned continue to be capitalized pending final evaluation. Exploratory well costs not meeting either of these tests are charged to expense. All other exploratory costs (including geological and geophysical costs) are expensed as incurred. Exploratory dry holes are expensed.

## 2. Summary of Significant Accounting Policies (Continued)

### (h) Property, plant and equipment (Continued)

- Development costs

Costs of development wells including dry holes, platforms, well equipment and attendant production facilities are capitalized.

- Production costs

Costs incurred with producing wells are recorded as inventories and are expensed when the products are sold.

- Abandonment costs

The Company makes its annual reviews and revision of its estimated costs associated with well abandonment and the demobilization of oil and gas production areas, considering new information about date of expected abandonment and revised cost estimates to abandon. The changes in estimated asset retirement obligation are principally related to the commercial declaration of new fields, certain changes in cost estimates, and revisions to abandonment information provided for non-operated joint ventures.

- Depreciation, depletion and amortization

Depreciation, depletion and amortization of leasehold costs of producing properties are recorded using the unit-of-production method applied on a field by field basis as a ratio of proved developed reserves. Production platform under capital lease are depreciated on a straight-line basis over the estimated useful lives of the platforms. Depreciation, depletion and amortization of all other capitalized costs (both tangible and intangible) of proved oil and gas producing properties is recorded using the unit-of-production method applied on a field by field basis as a ratio of proved developed reserves produced. The straight-line method is used for assets with a useful life shorted than the life of the field.

**2. Summary of Significant Accounting Policies** (Continued)**(h) Property, plant and equipment** (Continued)

- Depreciation, depletion and amortization (Continued)

Other plant and equipment are depreciated on a straight-line basis over the following estimated useful lives:

Building and improvements	25-40 years
Equipment and other assets	3-30 years
Platforms (1)	15-25 years
Pipelines	30 years

(1) In 2006 the Company reviewed prospectively the estimation of depreciation and changed the rate from 10-25 to years to 15-25 years and the effect in the result was US\$67.

- Impairment

In accordance with SFAS No. 144 - Impairment of Long-Lived Assets ( SFAS 144 ), management reviews long-lived assets, primarily property, plant and equipment to be used in the business and capitalized costs relating to oil and gas producing activities, whenever events or changes in circumstances indicate that the carrying value of an asset or group of assets may not be recoverable on the bases of undiscounted future cash flows. The reviews are carried out at the lowest level of assets to which the Company is able to attribute identifiable future cash flows. The net book value of the underlying assets is adjusted to their fair value using a discounted future cash flows model, if the sum of the expected undiscounted future cash flows is less than the book value.

- Maintenance and repairs

The actual costs of major maintenance, including turnarounds at refineries and vessels, as well as other expenditures for maintenance and repairs, are expensed as incurred.



**2. Summary of Significant Accounting Policies** (Continued)**(h) Property, plant and equipment** (Continued)

- Capitalized interest

Interest is capitalized in accordance with SFAS No. 34 - Capitalization of Interest Cost ( SFAS 34 ). Interest is capitalized on specific projects when a construction process involves considerable time and involves major capital expenditures. Capitalized interest is allocated to property, plant and equipment and amortized over the estimated useful lives or unit-of-production method of the related assets. Interest is capitalized at the Company's weighted average cost of borrowings.

**(i) Revenues, costs and expenses**

Revenues from sales of crude oil and oil products, petrochemical products and others are recognized on an accrual basis when the title is transferred to the customer. Revenues from sales of natural gas are accounted for when the natural gas is transferred to the customer. Subsequent adjustments to revenues based on production sharing agreements or volumetric delivery differences are not significant. Costs and expenses are accounted for on an accrual basis.

**(j) Income taxes**

The Company accounts for income taxes in accordance with SFAS No. 109 - Accounting for Income Taxes ("SFAS 109"), which requires an asset and liability approach to recording current and deferred taxes. The effects of differences between the tax bases of assets and liabilities and the amounts recognized in the financial statements have been treated as temporary differences for the purpose of recording deferred income taxes.

The Company records the tax benefit of all net operating losses as a deferred tax asset and recognizes a valuation allowance for any part of this benefit which management believes will not be recovered against future taxable income using a "more likely than not" criterion.

**2. Summary of Significant Accounting Policies (Continued)****(k) Employees post-retirement benefits**

The Company sponsors a contributory defined-benefit pension plan covering substantially all of its employees, which is accounted for by the Company in accordance with SFAS No. 87 - Employers Accounting for Pensions ("SFAS 87") and SFAS 158 - Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an Amendment of FASB Statements No. 87, 88, 106 and 132(R) ( SFAS 158 ). Disclosures related to the plan are according to FASB Statement No. 132-R, Employers Disclosures about Pensions and Other Post-retirement Benefits ( SFAS No. 132-R ) (see Note 2 (r)).

In addition, the Company provides certain health care benefits for retired employees and their dependents. The cost of such benefits is recognized in accordance with SFAS No. 106 - Post-retirement Benefits Other Than Pensions ("SFAS 106") and SFAS 158 .

The Company also contributes to the Brazilian pension and government sponsored pensions of international subsidiaries, social security and redundancy plans at rates based on payroll, and such contributions are expensed as incurred. Further indemnities may be payable upon involuntary severance of employees but, based on current operating plans, management does not believe that any amounts payable under this plan will be significant.

**(l) Environmental and remediation costs**

Environmental and remediation costs relating to current operations are expensed or capitalized, as appropriate, depending on whether such costs are expected to provide future economic benefits. Liabilities are recognized when the costs are considered probable and can be reasonably estimated.

**(m) Compensated absences**

The liability for future compensation of employees for vacations is accrued as earned.

**2. Summary of Significant Accounting Policies (Continued)****(n) Earnings per share**

Earnings per share are computed using the two-class method, which is an earnings allocation formula that determines earnings per share for both preferred shares, which are participating securities and common shares. The preferred shares participate in dividends and undistributed earnings with the common shares at a predetermined formula. Such formula allocates the net income, as if all of the net income for each year had been distributed, first to the preferred shares in an amount equal to the preferred shares' priority minimum annual dividend of the higher of 3% of their shareholders equity or 5% of their paid-in capital as stated in the statutory accounting records, then to common shares in an amount equal to the preferred shares' priority dividend on a per share basis and any remaining net income is allocated equally to the common and preferred shares. As a result of a 2005 stock split, each American Depositary Share (ADS) for common shares represents four shares of the Company's common shares or four shares of the Company's preferred shares.

**(o) Research and development costs**

Research and development costs are charged to expense when incurred.

**(p) Accounting for derivatives and hedging activities**

The Company applies SFAS No. 133 Accounting for Derivative Instruments and Hedging Activities, together with its amendments and interpretations, referred to collectively herein as SFAS 133. SFAS 133 requires that all derivative instruments be recorded in the balance sheet of the Company as either an asset or a liability and measured at fair value. SFAS 133 requires that changes in the derivative's fair value be recognized in the income statement unless specific hedge accounting criteria are met; and the Company designates. For derivatives designated as accounting hedges, fair value adjustments are recorded either in the income statements or Accumulated Other Comprehensive Income, a component of shareholders' equity, depending upon the type of accounting hedge and the degree of hedge effectiveness.

## 2. Summary of Significant Accounting Policies (Continued)

### (p) Accounting for derivatives and hedging activities (Continued)

The Company uses derivative financial instruments for economic hedging purposes to mitigate the risk of unfavorable price movements for crude oil purchases. These instruments are marked-to-market with the associated gains or losses recognized as Financial Income or Financial Expense.

The Company may also use derivative financial instruments for economic hedging purposes to mitigate the risk of unfavorable exchange-rate movements on its foreign currency-denominated funding. Gains and losses from changes in the fair value of these contracts are recognized as Financial Income or Financial Expense.

For cash flow hedges, the gains and losses associated with the derivative instruments are deferred and recorded in Accumulated Other Comprehensive Income until such time as the hedged transaction impacts earnings, with the exception of any hedge ineffectiveness; which is recorded directly in earnings.

### (q) Recently issued accounting pronouncements

- **FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, An Interpretation of FASB Statement 109 (FIN 48)**

In July 2006, the FASB issued FIN 48, that clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements and prescribes a threshold of more-likely-than-not for recognition of tax benefits of uncertain tax positions taken or expected to be taken in a tax return. FIN 48 also provides related guidance on measurement, derecognition, classification, interest and penalties, and disclosure. The provisions of FIN 48 will be effective for the Company on January 1, 2007, with any cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. The Company is in the process of assessing the impact of adopting FIN 48 on its results of operations and financial position. The Company does not expect that the adoption of FIN 48 will have a material effect on the Company's financial position or results from operations.

**2. Summary of Significant Accounting Policies (Continued)****(q) Recently issued accounting pronouncements (Continued)****• FASB Statement No. 157, Fair Value Measurements ( SFAS 157 )**

In September 2006, the FASB issued SFAS 157, which will become effective for the Company on January 1, 2008. This standard defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements but would apply to assets and liabilities that are required to be recorded at fair value under other accounting standards. The impact, if any, to the Company from the adoption of SFAS 157 in 2008 will depend on the Company's assets and liabilities at that time that are required to be measured at fair value.

**• FASB Statement 159 The Fair Value Option for Financial Assets and Financial Liabilities. SFAS 159**

In February 2007, the FASB issued SFAS 159 The Fair Value Option for Financial Assets and Financial Liabilities. SFAS 159, that permits the measurement of certain financial instruments at fair value. Entities may choose to measure eligible items at fair value at specified election dates, reporting unrealized gains and losses on such items at each subsequent reporting period. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the potential impact of the fair value option but it is not expected to have a significant effect on reported financial position or statements of income.

**(r) Recently adopted accounting pronouncements****• FASB Statement 158 - Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an Amendment of FASB Statements No. 87, 88, 106 and 132(R) ( SFAS 158 )**

In September 2006, the FASB issued SFAS 158, which became effective for the Company on December 31, 2006. See Note 16(d).

**3. Income Taxes**

Income taxes in Brazil comprise federal income tax and social contribution, which is an additional federal income tax. The statutory enacted tax rates for income tax and social contribution have been 25% and 9%, respectively for the years ended December 31, 2006, 2005 and 2004.

The Company's taxable income is substantially generated in Brazil and is therefore subject to the Brazilian statutory tax rate. The following table reconciles the tax calculated based upon statutory tax rates to the income tax expense recorded in these consolidated financial statements.

	<b>Year ended December 31,</b>		
	<b>2006</b>	2005	2004
Income before income taxes, minority interest and extraordinary item:			
Brazil	<b>18,589</b>	13,739	8,168
International	<b>572</b>	853	767
	<b>19,161</b>	14,592	8,935
Tax expense at statutory rates	<b>(6,515)</b>	(4,961)	(3,038)
Adjustments to derive effective tax rate:			
Non-deductible post-retirement health-benefits	<b>(277)</b>	(244)	(157)
Change in valuation allowance	<b>101</b>	76	159
Tax benefit on interest on shareholders' equity	<b>994</b>	791	650
Others	<b>6</b>	(103)	155
Income tax expense per consolidated statement of income	<b>(5,691)</b>	(4,441)	(2,231)

**3. Income Taxes (Continued)**

The following table shows a breakdown between domestic and international income tax and social contribution expense (benefit) recorded in these consolidated financial statements:

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Income tax			
expense per consolidated statement of income:			
Brazil			
Current	<b>(4,750)</b>	(3,973)	(1,922)
Deferred	<b>(686)</b>	(179)	(258)
	<b>(5,436)</b>	(4,152)	(2,180)
International			
Current	<b>(261)</b>	(250)	(192)
Deferred	<b>6</b>	(39)	141
	<b>(255)</b>	(289)	(51)
	<b>(5,691)</b>	(4,441)	(2,231)

TRANSPORTADORA BRASILEIRA GASODUTO BOLÍVIA-BRASIL S.A. TBG, a subsidiary of GASPETRO, has accumulated tax losses which have resulted in income tax and social contribution carryforwards amounting to US\$345 as of December 31, 2006 (US\$377 in 2005). These credits are being carried forward on a monthly basis against the taxes payable, in accordance with the existing legislation. These credits were accumulated between 1999 and 2002, based on a technical study approved by the Board of Directors on the expected generation of future taxable income and profitability in the past three years which allows realization thereof in ten years at the maximum.

PEPSA also has tax credits amounting to US\$366 as of December 31, 2006 (US\$443 in 2005), which could be offset against future taxable income and, for which a valuation allowance is recognized in the consolidated financial statements for December 31, 2006 and 2005. As of December 31, 2006, PEPSA has booked a US\$335 allowance for tax loss carryforwards (US\$352 in 2005) because, as of such dates, management believes that it is more likely than not that future taxable income will not be sufficient to absorb the net deductible temporary differences and accumulated tax loss carryforwards. These tax loss carryforwards have been generated mainly due to operating losses occurred during the Argentinean crisis in 2001 and 2002.

**3. Income Taxes (Continued)**

Annually PEPSA's management evaluates the recovery of tax loss carryforwards taking into consideration, among other elements, the projected business profits, tax planning strategies, temporariness of future taxable income, considering the term of expiration of the loss carryforwards, the future reversions of the existing temporary differences and the recent-year tax history. All the evidence available both positive and negative is duly weighted and considered in the analysis.

At December 31, 2006 and 2005, the PEPSA's management partially reversed the tax loss carryforward allowance booked in prior years recognizing a tax benefit of US\$17 and US\$63, respectively. PEPSA's management will continue analyzing the feasibility of recovering the tax loss carryforwards for which the allowance was recognized.

The deferred tax amounts recorded are principally generated through transactions occurring in Brazil and there are no significant deferred tax amounts from international locations. There is no netting of taxes between international jurisdictions.

The major components of the deferred income tax accounts in the consolidated balance sheet are as follows:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Current assets</b>		
Inventories	<b>101</b>	(12)
Lease obligations	<b>53</b>	58
Provision for profit sharing	<b>159</b>	131
Employees' post-retirement benefits	<b>65</b>	86
Other temporary differences	<b>295</b>	219
	<b>673</b>	482
<b>Current liabilities</b>		
Other temporary differences	<b>(28)</b>	(9)
	<b>(28)</b>	(9)
<b>Net current deferred tax assets</b>	<b>645</b>	473
<b>Current deferred tax liabilities</b>	<b>(8)</b>	(6)
<b>Current deferred tax assets</b>	<b>653</b>	479





**3. Income Taxes (Continued)**

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Non-current assets</b>		
Employees' post-retirement benefits, net of Accumulated postretirement benefit reserves adjustments	<b>2,101</b>	1,291
Interest on shareholder's equity	-	159
Deferred charges	<b>159</b>	124
Tax loss carryforwards	<b>514</b>	592
Investments	<b>53</b>	102
Lease obligations	<b>51</b>	61
Inventories revaluation	<b>37</b>	37
Derivatives	<b>11</b>	60
Allowance for doubtful accounts	<b>47</b>	47
Provision for contingencies	<b>67</b>	28
Project financings	<b>95</b>	64
Other temporary differences, not significant individually	<b>328</b>	110
Valuation allowance	<b>(426)</b>	(524)
	<b>3,037</b>	2,151
<b>Non-current liabilities</b>		
Capitalized exploration and development costs	<b>(4,041)</b>	(2,995)
Property, plant and equipment	<b>(1,140)</b>	(584)
Hedge	<b>(21)</b>	(199)
Investments	<b>(88)</b>	(81)
Tax effect on unrealized loss on investments available-for-sale	<b>(186)</b>	(168)
Other temporary differences, not significant individually	<b>(416)</b>	(283)
	<b>(5,892)</b>	(4,310)
Net non-current deferred tax liabilities	<b>(2,855)</b>	(2,159)
Non-current deferred tax assets	<b>61</b>	7
Non-current deferred tax liabilities	<b>(2,916)</b>	(2,166)
Net deferred tax liabilities	<b>(2,210)</b>	(1,686)



**3. Income Taxes (Continued)**

Although realization of net deferred tax assets is not assured, management believes that, except where a valuation allowance has been provided, such realization is more likely than not to occur. The amount of the deferred tax asset considered realizable could, however, be reduced if estimates of future taxable income are reduced. Tax loss carryforwards generated in Brazil do not expire and are available for offset against future taxable income, limited to 30% of taxable income in any individual year. PEPSA tax loss carryforward principally expire in years beyond 2007, and may be offset against future taxable income without limitation. The following presents the changes in the valuation allowance for the years ended December 31, 2006, 2005 and 2004:

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Balance at January 1,	<b>(524)</b>	(596)	(749)
Reductions	<b>101</b>	76	159
Cumulative translation adjustments	<b>(3)</b>	(4)	(6)
Balance at December 31,	<b>(426)</b>	(524)	(596)

The Company has not recognized a deferred tax liability of approximately US\$190 for the undistributed earnings of its foreign operations that arose in 2006 and prior years as the Company considers these earnings to be indefinitely reinvested. A deferred tax liability will be recognized when the Company no longer demonstrates that it plans to permanently reinvest the undistributed earnings. As of December 31, 2006 the undistributed earnings of these subsidiaries were approximately US\$560.

**4. Cash and Cash Equivalents**

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Cash	<b>1,692</b>	1,539
Investments - Brazilian reais(1)	<b>4,072</b>	6,280
Investments - U.S. dollars (2)	<b>6,924</b>	2,052
	<b>12,688</b>	9,871

(1) Comprised primarily federal public bonds with immediate liquidity and the securities are tied to the American dollar quotation or to the remuneration of the Interbank Deposits DI.

(2) Comprised primarily by Time Deposit and securities with fixed income.

**5. Marketable Securities**

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Marketable securities classification:		
Available-for-sale	<b>185</b>	163
Trading	<b>112</b>	361
Held-to-maturity	<b>143</b>	61
	<b>440</b>	585
Less: Current portion of marketable securities	<b>(346)</b>	(456)
Long-term portion of marketable securities	<b>94</b>	129

Marketable securities are comprised primarily of amounts the Company has invested in an exclusive fund, excluding the Company's own securities, which are considered repurchased. The exclusive fund is consolidated, and the equity and debt securities within the portfolio are classified as trading or available-for-sale under SFAS 115 based on management's intent. Trading securities are principally Brazilian bonds, which are bought and sold frequently with the objective of making short-term-profits on market price changes. Available-for-sale securities are principally, LCN (Credit Liquid Note) agreements and certain other bonds for which the Company does not have current expectations to trade actively. Trading securities are presented as current assets, as they are expected to be used in the near term for cash funding requirements. Available-for-sale securities are presented as other assets, as they are not expected to be sold or liquidated within the next twelve months.

The Company holds National Treasury Bonds "Series P" (NTN-P) issued by the Federal Government which are accounted for as available-for-sale securities in accordance with SFAS 115.

**6. Accounts Receivable, Net**

Accounts receivable, net consisted of the following:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Trade	<b>7,944</b>	7,889
Less: Allowance for uncollectible accounts	<b>(1,120)</b>	(1,063)
	<b>6,824</b>	6,826
Less: Long-term accounts receivable, net	<b>(513)</b>	(642)
Current accounts receivable, net	<b>6,311</b>	6,184

	<b>As of December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Allowance for uncollectible accounts			
Balance at January 1,	<b>(1,063)</b>	(904)	(780)
Additions	<b>(78)</b>	(118)	(164)
Write-offs	<b>60</b>	10	66
Cumulative translation adjustments	<b>(39)</b>	(51)	(26)
Balance at December 31,	<b>(1,120)</b>	(1,063)	(904)
Allowance on short-term receivables	<b>(584)</b>	(196)	(150)
Allowance on long-term receivables	<b>(536)</b>	(867)	(754)

**6. Accounts Receivable, Net (Continued)**

At December 31, 2006 and 2005, long-term receivables include US\$608 and US\$599 respectively relating to payments made by the Company to suppliers and subcontractors on behalf of certain contractors. These contractors had been hired by the subsidiary BRASOIL for the construction/conversion of vessels into FPSO ( Floating Production, Storage and Offloading ) and FSO ( Floating, Storage and Offloading ) and failed to make the payments to their suppliers and subcontractors. The Company made the payments to avoid further delays in the construction/conversion of the vessels and consequent losses to BRASOIL.

Based on consultations with legal advisers, the Company's management has determined that these payments can be reimbursed, since they represent BRASOIL's rights with respect to the contractors, for which reason judicial action was filed with international courts to seek reimbursement. However, as a result of the uncertainties related to the realization of such receivables, the Company recorded an allowance for all credits not backed by collateral. Such allowance amounted to US\$536 and US\$527 as of December 31, 2006 and 2005, respectively.

**7. Inventories**

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Products		
Oil products	<b>2,220</b>	2,020
Fuel alcohol	<b>160</b>	66
	<b>2,380</b>	2,086
Raw materials, mainly crude oil	<b>2,989</b>	2,266
Materials and supplies	<b>1,274</b>	1,047
Others	<b>140</b>	142
	<b>6,783</b>	5,541
Current inventories	<b>6,573</b>	5,305
Long-term inventories	<b>210</b>	236



**8. Recoverable Taxes**

Recoverable taxes consisted of the following:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Local:		
Domestic value-added tax (ICMS) (1)	<b>2,829</b>	1,830
Income tax and social contribution	<b>357</b>	275
PASEP/COFINS (2)	<b>291</b>	157
Foreign value-added tax (IVA)	<b>104</b>	123
Other recoverable taxes	<b>304</b>	341
	<b>3,885</b>	2,726
Less: Long-term recoverable taxes	<b>(1,292)</b>	(639)
Current recoverable taxes	<b>2,593</b>	2,087

(1) Domestic value-added sales tax are composed of credits generated by commercial operations and by the acquisition of property, plant and equipment and can be offset with taxes of the same nature.

(2) PASEP and COFINS are social security contributions payable in respect of sales of products and services and financial revenues.

These contributions and the domestic value-added tax (ICMS) are not cumulative and amounts paid related to these taxes in the acquisition of products and/or services can be offset when these products and services are sold, which means a tax credit is generated when the purchase is made and such credit is then offset upon sale to final customer.

The income tax and social contribution recoverable will be offset against future taxable income.

Petrobras plans to fully recover these taxes, and as such, no allowance has been provided.

**9. Property, Plant and Equipment, Net****(a) Composition of balance**

Property, plant and equipment, at cost, are summarized as follows:

	As of December 31,					
	2006			2005		
	Cost	Accumulated depreciation	Net	Cost	Accumulated depreciation	Net
Buildings and improvements	2,422	(935)	1,487	1,696	(755)	941
Oil and gas assets	26,274	(10,605)	15,669	21,500	(9,589)	11,911
Equipment and other assets	34,654	(16,996)	17,658	28,359	(14,902)	13,457
Capital lease platforms and vessels	2,660	(1,322)	1,338	2,651	(1,233)	1,418
Rights and concessions	1,828	(336)	1,492	1,492	(210)	1,282
Land	262	-	262	226	-	226
Materials	1,253	-	1,253	820	-	820
Expansion projects - Construction and installations in progress:						
Exploration and production	10,731	-	10,731	9,553	-	9,553
Supply	5,152	-	5,152	4,546	-	4,546
Gas and energy	3,231	-	3,231	1,356	-	1,356
Distribution	195	-	195	185	-	185
International	5	-	5	-	-	-
Corporate	424	-	424	225	-	225
	<b>89,091</b>	<b>(30,194)</b>	<b>58,897</b>	72,609	(26,689)	45,920

**9. Property, Plant and Equipment, Net (Continued)****(b) New Hydrocarbons Law of Bolivia**

The new Bolivian Hydrocarbons Law 3,058 has been in force since May 19, 2005. This law revokes the former Hydrocarbons Law 1,689 dated April 30, 1996.

The new law establishes, among other matters, a higher tax burden for companies of the sector, through royalties of 18% and a direct tax on hydrocarbons (IDH) of 32%, to be applied directly on 100% of the production, on top of taxes in force by operation of Law No. 843. In addition, the new legislation determines substitution of shared risk contracts for new contracts observing the models established in the Law, and introduces changes in the oil products distribution activity.

On May 20, 2005, contracts were entered into for association among Yacimientos Petrolíferos Fiscales Bolivianos - YPF (Bolivian state-owned company) and fuel distribution companies to extend the term of Distributors' operations up until YPF accumulates sufficient funds to develop this segment all over the Bolivian territory. On June 30, 2006 the contracts term expired through which the major distribution companies distributed hydrocarbons in Bolivia. YPF took over national distribution as from that date. The company Petrobras Bolivia Distribución, which allowed the ownership of a major part of this business, is still operating in the sector through the service stations it owns.

As of May 1, 2006, Supreme Decree 28,701 was enacted in Bolivia, through which, the natural hydrocarbon resources were nationalized. As a consequence, the companies that are currently engaged in gas and petroleum production activities, will have to transfer the ownership of all hydrocarbon production to Yacimientos Petrolíferos Fiscales Bolivianos (YPF). A transition period has also been established of 180 days as from the date the aforementioned decree is enacted, in which companies that are currently operating should execute the new contracts established by YPF. Companies which have not executed these contracts by the end of this term may be unable to continue operating in the country.

**9. Property, Plant and Equipment, Net** (Continued)**(b) New Hydrocarbons Law of Bolivia** (Continued)

The aforementioned Decree establishes that fields with a certified average natural gas production of over 100 million cubic feet per day in 2005, as is the case with the San Alberto and San Antonio fields where the Company operates, an additional amount will be paid to YPFB of 32% over of the production value, rising to a total of 82% of the Bolivian government's interest. The Bolivian Ministry of Hydrocarbons and Energy shall determine on a case-by-case basis via auditing the final share to be paid to the Companies in the contract to be executed. Up to December 31, 2006 the Company had recorded a provision to pay the additional share to YPFB of 32% on the hydrocarbon production, to an amount equal to US\$99. The regulatory decrees which among other matters shall establish the means for paying this share have not yet been issued.

Furthermore, according to this decree the State is nationalizing the shares required for YPFB to control, with a minimum of 50% plus one share, Petrobras Bolivia Refinación S.A. - PBR, in which Petrobras has an indirect interest of 100% (Petrobras International Braspetro B.V. - 51% and Petrobras Energia S.A. - 49%). The equity interest will be transferred to YPFB when the parties reach an agreement about the amount of economic compensation to be paid by YPFB to Petrobras, besides the former compliance of some legal and statutory assumptions. The parties have not yet commenced the assessment process.

On October 28, 2006 Petrobras Bolivia and its partners executed operating contracts with YPFB for San Alberto and San Antonio fields. These contracts establish that the revenues, royalties, profit shares, IDH, shipment and compression will be absorbed by YPFB, and the cost of production and investments made by the companies should be reimbursed as remuneration to the owner. Any difference which may exist will be distributed between the Bolivian state company and the companies, at percentages varying according to production and the investment recovery factor. These contracts will come into force as from approval by the Bolivian National Congress and their official registration.

In a document attached to contracts entitled "Investments made", Petrobras and its partners state the investment amounts net of amortization, which will be reviewed taking into account the results of the audits contracted by the Hydrocarbons Ministry, that are currently in progress. To date, the Company is not aware of the result of these audits and the possible effects on its investments.

**9. Property, Plant and Equipment, Net** (Continued)**(b) New Hydrocarbons Law of Bolivia** (Continued)

Supreme Decree 28,900-A issued October 28, 2006 established that the companies will continue operating in Bolivia in accordance with Supreme Decree 28,701, including article 3, paragraph 1 which establishes the additional payment of 32% for the San Alberto and San Antonio fields until the aforementioned contracts have been registered.

On November 28, 2006 the National Congress approved the 44 oil contracts (exploration and production), which include the contracts that Petrobras participates in/or operates, which mainly include the San Alberto and San Antonio fields. On January 11, 2007 Laws were published by which the Bolivian Legislative Branch approved these contracts, including those referring to the San Alberto and San Antonio fields. To date the contracts have not been registered at a registry office, despite the fact there is no justifiable reason for the delay. The contracts will come into force after they have been effectively registered.

PBR and PEBIS continue their normal operations under the control and management of the Company, and hence their consolidated financial statements are still being included in the Company's consolidated financial statements. The consolidated total assets balance of PEBIS as of December 31, 2006 amounted to US\$1,173.

**(c) Review of operating agreements in Venezuela**

In March of 2006, PESA, through its controlled and associated companies in Venezuela, entered into Memoranda of Understanding (MOU) with PDVSA and Corporación Venezolana del Petróleo S.A. (CVP) in order to finalize the migration of operational agreements to mixed-capital companies. The MOUs establish that the interest of private partners in mixed-capital corporate companies should be limited to 40%, while the Venezuelan government participates with the remaining 60%. Thus, PESA's indirect interest in the fields of Oritupano Leona, La Concepción, Acema and Mata Areas was defined as being of 22%, 36%, 34.5% and 34.5%, respectively.

Pursuant to the terms of the MOU, CVP shall acknowledge dividable and transferable credits in favor of the private companies with interest in the mixed-capital companies, which shall not be subject to interest and may be used in payment of the acquisition bonus of new areas for petroleum exploration and production activities or for a license to engage in gas exploration and production.

**9. Property, Plant and Equipment, Net** (Continued)**(c) Review of operating agreements in Venezuela** (Continued)

During the transition period and until the mixed capital companies are in operation, the consortia's operations have been conducted and supported by Petrobras Energia Venezuela under the supervision of an integrated operating committee, on which PDVSA representatives shall form the majority.

Due to the change in structure of shareholding interest in the mixed capital companies, from April 1, 2006 the Company no longer consolidates the assets, liabilities and results of the aforesaid operations in its consolidated statements, but presents them as equity investments in non-consolidated companies and other investments, which increased the balance of such account by US\$878.

**(d) New Hydrocarbons Law in Ecuador**

In April 2006, the Law which amended the Hydrocarbons Law (Ley de Hidrocarburos) was enacted in Ecuador, which establishes the Government shall hold a minimum share of 50% in the extraordinary revenues, generated by increases to the sale price of Ecuadorian oil (average monthly effective FOB sale price) as compared to the monthly average oil sale price established in the contract, stated in the currency of the month of settlement. In July, 2006 the regulations of said Law were published which Ecuadortlc S.A., a subsidiary of PESA, and Petroecuador interpreted differently. The application of this law is being disputed by Ecuadortlc and Petroecuador.

**(e) SFAS No. 143 - Accounting for asset retirement obligations**

Since January 1, 2003, Petrobras adopted SFAS No. 143 - Accounting for Asset Retirement Obligations ("SFAS 143"). Under SFAS 143, the fair value of asset retirement obligations are recorded as liabilities on a discounted basis when they are incurred, which is typically at the time the related assets are installed. Amounts recorded for the related assets will be increased by the amount of these obligations and depreciated over the related useful lives of such assets. Over time, the amounts recognized as liabilities will be accreted for the change in their present value until the related assets are retired or sold.

Measurement of asset retirement obligations is based on currently enacted laws and regulations, existing technology and site-specific costs. There are no assets legally restricted to be used in the settlement of asset retirement obligations.

**9. Property, Plant and Equipment, Net** (Continued)**(e) SFAS No. 143 - Accounting for asset retirement obligations** (Continued)

A summary of the annual changes in the abandonment provision is presented as follows:

	<b>Liabilities</b>
Balance as of December 31, 2004	403
Depreciation and impairment	-
Accretion expenses	51
Liabilities incurred	356
Liabilities settled	(4)
Revision of provision	(21)
Cumulative translation adjustment	57
Balance as of December 31, 2005	842
Depreciation and impairment	-
Accretion expenses	32
Liabilities incurred	632
Liabilities settled	(4)
Revision of provision	(112)
Cumulative translation adjustment	83
Balance as of December 31, 2006	1,473

**(f) Impairment**

For the years ended December 31, 2006, 2005 and 2004, the Company recorded impairment charges of US\$21, US\$156 and US\$65, respectively. During 2006, the impairment charge was primarily related to producing properties in Brazil and principle amounts were related to Petrobras Córrego de Pedras on-shore field. During 2005, the impairment charge was primarily related to investments in Venezuela (US\$134), due to the tax and legal changes implemented by the Ministry of Energy and Petroleum of Venezuela (MEP), previously mentioned. During 2004, the impairment charge was related to producing properties in Brazil, principle amounts were related to the Company's Cioba's off-shore field (US\$30). The impairment expenses recorded in 2004 were primarily due to capital expenditures made in 2004 to producing fields with only marginal reserves.

**9. Property, Plant and Equipment, Net (Continued)**

**(g) Return of exploration areas to the ANP**

In the 2006 financial year, Petrobras returned to the National Petroleum Agency - ANP the rights over:

- The BCE-5 exploratory concession - total return of the retained area for assessment;
- The BT-POT- 26 exploratory concession, blocks POT-T-210, POT-T-211 and POT-T-257 total early return of the three blocks;
- The BT-POT-35 exploratory concession, block POT-T-563 - total early return of the block;
- The REC-T-41 exploratory concession, block BT-REC-11 - total return of the retained area for assessment; and
- The exploratory concessions BC-60, BES-100, BC-20, BC-30, BS-400, BS-500 and BC-50 - total returns of the blocks, not including the areas retained by Commercial Declaration or annexing.

**(h) Return to ANP of fields at the Production Stage operated by Petrobras**

In the 2006 financial year, Petrobras returned to the National Petroleum Agency - ANP the rights over the fields Beija-Flor, Dias D'Ávila, Fazenda Gameleira, Miranga Leste and Vale do Quiricó, all located in the state of Bahia.

**(i) 8th bidding for exploratory blocks of ANP**

In November of 2006, Petrobras acquired twenty-one new exploratory blocks of the twenty-two areas it competed for in the 8th Round of Bidding conducted by the National Petroleum Agency - ANP.

Petrobras acquired exclusive rights for seven blocks and a further fourteen blocks in consortium with other companies, two of which the Company will operate.

The bonuses offered by Petrobras and its partners amounted to US\$130, with the Company accounting for US\$116. This Bid has been suspended in full, because of the injunction awarded by the Federal Courts of the Federal District. The bonuses will be paid when this issue is resolved.



**10. Investments in Non-Consolidated Companies and Other Investments**

Petrobras conducts portions of its business through investments in companies accounted for using the equity and cost methods. These non-consolidated companies are primarily engaged in the petrochemicals and product transportation businesses.

	<b>Total ownership</b>	<b>Investments</b>	
		<b>2006</b>	<b>2005</b>
Equity method	20 % - 50% <sup>(1)</sup>	<b>1,883</b> <sup>(2)</sup>	974
Investments available-for-sale	8% - 17%	<b>715</b>	647
Investments at cost		<b>664</b>	189
<b>Total</b>		<b>3,262</b>	1,810

(1) As described further in this Note, certain thermoelectrics with ownership of 10% to 50% are also accounted as equity investments due to particularities of significant influence.

(2) Includes US\$878 related to investments in Venezuela, excluded from consolidation in 2006. (See Note 9 (c)).

At December 31, 2006 and 2005, the Company had investments in companies with publicly traded shares: BRASKEM S.A., Petroquímica União S.A. - PQU and Companhia Petroquímica do Sul S.A. - COPESUL. The Company's investments in these companies with publicly traded shares amounts to less than 20% of the investee's total voting shares, are classified as available-for-sale and have been recorded at market value. The Company has recorded unrealized gains (losses) for the difference between the fair value and the cost of the investment on these investments of US\$548 and US\$494 as of December 31, 2006 and 2005, respectively. These holding gains are reflected as a component of shareholder's equity, net of tax, with changes in the unrealized balance recorded as a component of comprehensive income.

The Company also has investments in companies for the purpose of developing, constructing, operating, maintaining and exploring thermoelectric plants included in the federal government's Priority Thermoelectric Energy Program, with equity interests of between 10% and 50%. The balance of these investments as of December 31, 2006 and 2005 includes US\$20 and US\$179 respectively, and are included as equity method investments due to the Company's ability to exercise significant influence over such operations.

The Company's investments in equity of non-consolidated companies generated equity earnings (losses) in results of non-consolidated companies of US\$28 for the year ended December 31, 2006 (2005 - US\$139; 2004 - US\$172).

**10. Investments in Non-Consolidated Companies and Other Investments (Continued)****(a) Acquisition of interest of CEG RIO**

Petrobras, through its subsidiary Petrobras Gás S.A. - GASPETRO, concluded on July 11, 2005 the acquisition of 12.41% of the shares (common and preferred) of Distribuidora de Gás Natural Canalizado CEG-RIO, for US\$17. With this acquisition, the shareholdings of GASPETRO in said company were increased to 37.41% . The Company has accounted for its investment using the equity method, retrospectively from the date of the initial investment. Due to the immateriality of the involved amounts the Company has not retrospectively applied the equity method to the 2004 Financial Statements. The acquisition of the additional interest in CEG RIO was recorded using the purchase method of accounting.

**(b) Exchange of assets - Petrobras and REPSOL - YPF**

On December 28, 2000, Petrobras and Repsol YPF entered into a Contract for the Exchange of Assets, under which Petrobras, in exchange of shares of EG3 in Argentina, assigned to Repsol YPF a 30% shareholding in Refinaria Alberto Pasqualini REFAP, the right to sell fuels in approximately 230 gas stations of BR Distribuidora and a 10% interest in the Albacora Leste field.

The contract established in its 4th clause that the parties receiving the shares of EG3 and REFAP should, in the course of eight years after January 1, 2001, review every year the reference values of EG3 Group and REFAP S.A. (denominated escalators ) to adjust them observing the conditions of said clause and to allow determining at the end of the period the definitive value of the shares of EG3 and REFAP, as well as definitive assets position and payment thereof to the creditor, under common agreement between the parties. Under the Escalators Liquidation Agreement entered into on December 29, 2005, and effective as from January 1, 2006, the companies performed early and definitive liquidation of the escalators.

The final value, including monetary restatement, due by Repsol YPF to Petrobras, related to EG3 share, for the full period of 8 (eight) years, including the projections for 2006, 2007 and 2008 amounted to US\$335. Of this amount US\$95 was applied to reduce property, plant and equipment and US\$158 was recorded as extraordinary gain, net of US\$82 of income tax on December 31, 2005.

**10. Investments in Non-Consolidated Companies and Other Investments (Continued)****(b) Exchange of assets Petrobras and REPSOL YPF (Continued)**

The final value, including monetary restatement, due by Petrobras to Repsol YPF, related to the 30% shareholding in REFAP, for the full period of 8 (eight) years, including the projections for 2006, 2007 and 2008 amounted to US\$255. This amount was recorded as component of other expenses, net.

Those amounts are definitive, and not subject to review or verification by any of the parties, thus liquidating application and quantification of escalators, as provided for in the Escalators Liquidation Agreement.

**11. Petroleum and Alcohol Account - Receivable from Federal Government****(a) Changes in the Petroleum and Alcohol account**

The following summarizes the changes in the Petroleum and Alcohol account for the years ended December 31, 2006 and 2005:

	<b>Year ended December 31,</b>	
	<b>2006</b>	<b>2005</b>
Opening balance	<b>329</b>	282
Financial income (Note 24)	<b>7</b>	9
Translation gain	<b>32</b>	38
Ending balance	<b>368</b>	329

The Petroleum and Alcohol account arose in periods previous to December 31, 2002 as a result of regulation in the fuels market. The Federal Government has certified the balance and placed a portion of the amount (US\$53) in a restricted use account.

**(b) Settlement of the Petroleum and Alcohol Accounts with the Federal Government**

As defined in Law No. 10,742 dated October 06, 2003, the settlement of the Petroleum and Alcohol account with the Federal Government should have been completed by June 30, 2004. Petrobras has been working with the Ministry of Mines and Energy - MME and Secretary of the National Treasury - STN in order to resolve remaining issues necessary to conclude the settlement process.

**11. Petroleum and Alcohol Account - Receivable from Federal Government (Continued)****(b) Settlement of the Petroleum and Alcohol Accounts with the Federal Government (Continued)**

The remaining balance of the Petroleum and Alcohol account may be paid as follows: (1) National Treasury Bonds issued at the same amount as the final balance of the Petroleum and Alcohol account; (2) offset of the balance of the Petroleum and Alcohol account, with any other amount owed by Petrobras to the Federal Government, including taxes; or (3) by a combination of the above options.

**12. Financings****(a) Short-term debt**

The Company's short-term borrowings are principally sourced from commercial banks and include import and export financing denominated in United States dollars, as follows:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Import - oil and equipment	<b>148</b>	340
Working capital	<b>1,145</b>	610
	<b>1,293</b>	950

The weighted average annual interest rates on outstanding short-term borrowings were 4.68% and 4.09% at December 31, 2006 and 2005, respectively.

**12. Financings (Continued)****(b) Long-term debt**

## • Composition

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Foreign currency		
Notes	<b>4,217</b>	5,871
Financial institutions	<b>3,550</b>	3,215
Sale of future receivables	<b>680</b>	1,241
Suppliers credits	<b>1,215</b>	1,349
Senior exchangeable notes	<b>330</b>	330
Assets related to export program to be offset against sales of future receivables	<b>(150)</b>	(300)
Repurchased securities (1)	<b>(19)</b>	(356)
	<b>9,823</b>	11,350
Local currency		
National Economic and Social Development		
Bank - BNDES (state-owned company, see Note 24)	<b>825</b>	298
Debentures:		
BNDES (state-owned company, see Note 24)	<b>656</b>	291
Other banks	<b>1,093</b>	935
Others	<b>209</b>	57
	<b>2,793</b>	1,581
Total	<b>12,616</b>	12,931
Current portion of long-term debt	<b>(2,106)</b>	(1,428)
	<b>10,510</b>	11,503

(1) At December 31, 2006 and 2005, the Company had amounts invested abroad in an exclusive investment fund that held debt securities of some of the Petrobras group companies and some of the SPEs that the Company consolidates according to FIN 46(R), in the total amount of US\$245 (US\$2,078 in 2005). These securities are considered to be extinguished, and thus the related amounts, together with applicable interest have been removed from the presentation of marketable securities and long-term debt, of US\$28 (US\$356 in 2005), and project financings, of US\$226 (US\$1,722 in 2005), respectively. (see also Note 14). Gains and losses on the extinguishment are recognized as incurred. Subsequent reissuances of notes at amounts greater or lower than are recorded as premium or discounts and are amortized over the life of the notes. Petrobras incurred in expenses in the total amount of US\$160 on the extinguishment of debt during 2006 and US\$17 during 2005. As of December 31, 2006 and 2005, the Company had

an outstanding balance of net premiums on reissuance that amounted to US\$45 and US\$56, respectively.

**12. Financings** (Continued)**(b) Long-term debt** (Continued)

- Composition of foreign currency denominated debt by currency

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Currencies		
United States dollars	<b>8,928</b>	10,679
Japanese Yen	<b>626</b>	409
Euro	<b>269</b>	262
Others	-	-
	<b>9,823</b>	11,350

- Maturities of the principal of long-term debt

The long-term portion at December 31, 2006 becomes due in the following years:

2008	<b>1,466</b>
2009	<b>799</b>
2010	<b>1,543</b>
2011	<b>810</b>
2012	<b>1,788</b>
2013 and thereafter	<b>4,104</b>
	<b>10,510</b>

- Composition of long-term debt by annual interest rate

Interest rates on long-term debt were as follows:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Foreign currency		
6% or less	<b>2,373</b>	3,686
Over 6% to 8%	<b>3,805</b>	2,603
Over 8% to 10%	<b>3,321</b>	4,491
Over 10% to 15%	<b>324</b>	570

	<b>9,823</b>	11,350
Local currency		
6% or less	<b>470</b>	85
Over 6% to 8%	<b>167</b>	266
Over 8% to 10%	<b>858</b>	264
Over 10% to 15%	<b>1,298</b>	966
	<b>2,793</b>	1,581
	<b>12,616</b>	12,931



**12. Financings (Continued)****(b) Long-term debt (Continued)**

- Structured finance of exports

Petrobras and Petrobras Finance Ltd. - PFL have certain contracts (Master Export Contract and Prepayment Agreement) between themselves and a special purpose entity not related to Petrobras, PF Export Receivables Master Trust ( PF Export ), relating to the prepayment of export receivables to be generated by PFL by means of sales on the international market of fuel oil and other products acquired from Petrobras.

As stipulated in the contracts, PFL assigned the rights to future receivables in the amount of US\$1,800 (1<sup>st</sup> and 2<sup>nd</sup> tranches) to PF Export, which, in turn, issued and delivered to PFL the following securities, also in the amount of US\$1,800:

- US\$1,500 in Senior Trust Certificates, which were negotiated by PFL on the international market at face value. The amount was transferred to Petrobras as prepayment for exports to be made to PFL, according to the prepayment agreement.
- US\$300 in Junior Trust Certificates, which are held in the portfolio of PFL. If PF Export incurs any losses on the receipt of the value of the exports transferred by PFL, these losses will be compensated by the Junior Trust Certificates.

The assignment of rights to future export receivables represents a liability of PFL, which will be settled by the transfer of the receivables to PF Export as and when they are generated. This liability will bear interest on the same basis as the Senior and Junior Trust Certificates, as described above. The Junior Trust Certificates form a 20% guarantee to the Senior Trust Certificates.

On September, 2005 Petrobras prepaid an amount of US\$330 to PETROBRAS FINANCE LTD. PFL respective to the export prepayments. Subsequent, PETROBRAS FINANCE LTD. PFL paid on September 1, 2005 an equal amount related to the Senior Trust Certificates series A2 and C with floating rates, issued by PF Export, maturing on 2010 and 2013, respectively.

**12. Financings (Continued)****(b) Long-term debt (Continued)**

- Structured finance of exports (Continued)

On March 1, 2006 Petrobras prepaid US\$334 to PETROBRAS FINANCE LTD. PFL respective to the export prepayments. Subsequent, PETROBRAS FINANCE LTD. PFL paid on March 1, 2006 an equal amount related to the Senior Trust Certificates series A1 and B with fixed rates, issued by PF Export, maturing in 2010 and 2011, respectively.

On May 26, 2006, PFL has successfully completed a solicitation of consents from holders of the Series 2003-A 6.4% Senior Trust Certificates due 2015 issued by PF Export Receivables Master Trust. The amendments sought to eliminate exports of bunker fuel from the transaction so that the securities have been collateralized only by receivables from sales of fuel oil exported by Petrobras and to reduce the minimum average daily gross exports of fuel oil for any rolling twelve-month period. PFL also obtained the consent from the holders of Series 2003-B 3.75% due 2013. The amendments became effective on June 1, 2006.

As a result of these amendments, the premium rate of the guarantee of the Series 2003-B was reduced from 1.8% to 1.1% .

- GASENE Project, Urucu-Coari-Manaus gas pipeline project and Urucu-Coari liquefied petroleum gas line project

On December 5, 2005, Petrobras obtained a bridge loan from the National Bank for Economic and Social Development (BNDES), in the amount of US\$342, for the special purpose company Transportadora GASENE S.A., responsible for the project aimed at interconnecting the Southeastern and Northeastern gas pipeline networks GASENE, and US\$342 for the special purpose company Transportadora Urucu Manaus S.A. proceeding with the financial structuring of the projects Urucu-Coari-Manaus gas pipeline and the Urucu-Coari liquefied petroleum gas (LPG) line.

**12. Financings** (Continued)**(b) Long-term debt** (Continued)

- Financing for P-51 and P-52 platforms

On November 25, 2004, the Board of Directors of Petrobras approved the execution of a contract in the amount of up to US\$379 between the National Bank for Economic and Social Development (BNDES) and the wholly-owned subsidiary PETROBRAS NETHERLANDS B.V. - PNBV for the financing of Brazilian assets and services to be used in the construction of the P-52 production platform.

The amount is provided by BNDES within the BNDES-Exim post-shipment program, under the buyer credit standards, which includes financing no other than Brazilian national goods and services within the investment. The financing will be amortized over a 10-year period after conclusion of the platform construction work, expected for May 2007. The interest rate is 36-month LIBOR plus 2% during the grace period and the 60-month LIBOR plus 2% thereafter.

On December 17, 2004, PETROBRAS NETHERLANDS B.V. - PNBV, a wholly-owned subsidiary of Petrobras, entered into a credit facility of US\$280 for financing of the construction of platforms P-51 and P-52. This loan is guaranteed by export credit agencies of Norway, United Kingdom and Italy. The Agreement states either a floating rate (Libor plus 0.6%) or a fixed interest rate (4.86%) .

On November 17, 2004, PETROBRAS NETHERLANDS B.V. - PNBV, a wholly-owned subsidiary of Petrobras, entered into a additional Commercial Loan Facility Agreement with BNP Paribas to grant to PETROBRAS NETHERLANDS B.V. - PNBV a credit facility of US\$100 for financing of the construction of platforms P-51 and P-52. The agreement states a floating interest rate of Libor plus 1.4% .

**12. Financings (Continued)****(b) Long-term debt (Continued)**

- Global Notes

On October 06, 2006, PIFCo issued Global Notes to the amount of US\$500. The notes have an effective rate of 6.185% per annum and a ten-year term. This is the lowest borrowing cost for PIFCo over this term and represented a rate of 1.55% over and above the US T-bond for a similar term. The Global Notes were offered at 99.557% of the face value with a stated of 6.125% per annum. PIFCo used the proceeds from this issuance principally to repay trade-related debt.

**(c) Debt repurchase offer (Tender) of notes**

On July 24, 2006, (PIFCo), a wholly owned subsidiary of the Company, concluded its debt repurchase offer (Tender) announced on July 18, 2006. The amount of notes tendered for five series of notes was US\$888. The repurchased securities related to 2006 amount to US\$1,046. Including the notes previously repurchased by the Company and its affiliates, also included in the tender, the total value reached US\$1,215. The purpose of this initiative was to reduce total debt outstanding and simplify the debt profile, thus benefiting from the Company's current strong cash generation. The transaction was settled on July 27, 2006 and all the notes tendered were canceled from this date. Upon conclusion of the Tender PIFCo incurred expenses in the total amount of US\$160.

**(d) Debentures issue**

On August 02, 2006 the Extraordinary General Meeting held by ALBERTO PASQUALINI - REFAP S.A., a subsidiary of the Company, approved the value of the private issue of simple, nominative and book-entered debentures in the amount of US\$391. The debentures are being issued in order to expand and modernize REFAP's industrial facilities and to raise its oil processing capacity from 20,000 m<sup>3</sup>/day to 30,000 m<sup>3</sup>/day, in addition to increasing the portion of national oils being processed.

**12. Financings (Continued)****(d) Debentures issue (Continued)**

The issue was made under the following terms up to December 30, 2006 and amortization over 96 months plus a 6-month grace period; 90% of the debentures shall be subscribed by the BNDES yielding interest at the Long-term Interest Rate +3.8% p.a.; 10% of the debentures shall be subscribed by BNDES Participações S.A. (BNDESPAR) at the interest rate of the BNDES basket of currencies + 2.3% p.a..

On September 08, 2006, the Financing Contract was executed and the first installment was made available in the amount of US\$278. On December 19, 2006 was made available the remaining amount of US\$113.

**(e) Japanese Yen Bonds**

On September 27, 2006, PIFCo concluded a private placement of securities in the Japanese capital market ( Shibosai ) for a total of ¥ 35 billion (US\$298) due September 2016. The issue was a private placement in Japanese market with a partial guarantee of Japan Bank for International Cooperation (JBIC) and bears interest at the rate of 2.15% per annum, payable semiannually. In the same date, PIFCo entered into a swap agreement with Citibank, swapping the total amount of this debt to a U.S. dollar denominated debt. PIFCo used the proceeds principally to finance PNBV, an affiliate, for construction of lines interconnecting the P-51, P-52 and P-53 production platforms to the PRA-1 autonomous repumping unit. See note 20(e).

**(f) Guarantees and covenants**

Financial institutions abroad do not require guarantees from the Company. The financing granted by BNDES - National Bank for Social and Economic Development is guaranteed by a lien on the assets being financed.

**12. Financings** (Continued)**(f) Guarantees and covenants** (Continued)

The Company's debt agreements contain affirmative covenants regarding, among other things, provision of information; financial reporting; conduct of business; maintenance of corporate existence; maintenance of government approvals; compliance with applicable laws; maintenance of books and records; maintenance of insurance; payment of taxes and claims; and notice of certain events. The Company's debt agreements also contain negative covenants, including, without limitation, limitations on the incurrence of indebtedness; limitations on the incurrence of liens; limitations on transactions with affiliates; limitations on the disposition of assets; limitation on consolidations, mergers, sales and/or conveyances; negative pledge restrictions; change in ownership limitations; ranking; use of proceeds limitations; and required receivables coverages. Petrobras' management affirms that the Company is in compliance with the covenants within debt agreements.

At December 31, 2006 and 2005, GASPETRO had secured certain debentures issued to finance the purchase of the transportation rights in the Bolivia/Brazil pipeline with 3,000 shares of its interest in TBG, a subsidiary of GASPETRO responsible for the operation of the pipeline.

The Federal Government guarantees TBG's Multilateral Credit Agency debt, which had an outstanding balance of US\$367 and US\$402 at December 31, 2006 and 2005, respectively. During 2000, the Federal Government, the Company, TBG, PETROQUISA and Banco do Brasil S.A. entered into an agreement whereby the revenues of TBG will serve as a counter-guarantee to this debt until the debt has been extinguished.

Petrobras entered into standby purchase agreements in support of the obligations of its wholly-owned subsidiary, PIFCo, under the note issuances in 2001, 2002 and 2003 and their respective indentures. Petrobras has the obligation to purchase from the noteholders any unpaid amounts of principal, interest or other amounts due under the notes and the indenture applies, subject to certain limitations, irrespective of whether any such amounts are due at maturity of the notes or otherwise.

**12. Financings (Continued)****(g) Lines of credit**

At December 31, 2006 and 2005, the Company had fully utilized all available lines of credit for the purchase of imports. Outstanding lines of credit at December 31, 2006 and 2005 were US\$1,370 and US\$1,688, respectively. Lines of credit are included in short-term debt and long-term debt.

**13. Financial Income (Expenses), Net**

Financial expenses, financial income and monetary and exchange variation on monetary assets and liabilities, net, allocated to income for the years ended at December 31, 2006, 2005 and 2004 are shown as follows:

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Financial expenses			
Loans and financings	<b>(1,076)</b>	(1,135)	(1,055)
Capitalized interest	<b>1,001</b>	612	267
Leasing	<b>(105)</b>	(98)	(94)
Project financings	<b>(370)</b>	(334)	(316)
Losses on derivative instruments	<b>(481)</b>	(103)	(233)
Repurchased securities losses	<b>(160)</b>	(17)	(137)
Other	<b>(149)</b>	(114)	(165)
	<b>(1,340)</b>	(1,189)	(1,733)
Financial income			
Investments	<b>566</b>	337	199
Customers	<b>231</b>	84	24
Government securities	<b>79</b>	90	42
Advances to suppliers	<b>27</b>	33	32
Gain on fair value hedge	<b>-</b>	93	553
Other	<b>262</b>	73	106
	<b>1,165</b>	710	956
Monetary and exchange variation on monetary assets and liabilities, net	<b>75</b>	248	450
	<b>(100)</b>	(231)	(327)

**14. Project Financings**

Since 1997, the Company has utilized project financings to provide capital for the continued development of the Company's exploration and production and related projects.

The special purpose entities associated with the project finance projects are consolidated based on FIN 46(R) and the project financing obligation represents the debt of the consolidated SPEs with the third-party lender.

The Company's responsibility under these contracts is to complete the development of the oil and gas fields, operate the fields, pay for all operating expenses related to the projects and remit a portion of the net proceeds generated from the fields to fund the special purpose companies' debt and return on equity payments. At the conclusion of the term of each financing project, the Company will have the option to purchase the leased or transferred assets from the consolidated special purpose company.

The following summarizes the liabilities related to the projects that were in progress at December 31, 2006 and 2005:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Barracuda/Caratinga	<b>1,405</b>	2,435
Charter Development - CDC (1)	<b>876</b>	346
Cabiúnas	<b>683</b>	799
PDET Offshore S.A.	<b>662</b>	188
Transportadora Gasene	<b>617</b>	236
Nova Transportadora do Sudeste - NTS (2)	<b>543</b>	461
Nova Transportadora do Nordeste - NTN (2)	<b>449</b>	385
Codajás (3)	<b>411</b>	215
Espadarte/Voador/Marimbá (EVM)	<b>282</b>	399
Companhia Locadora de Equipamentos Petrolíferos - CLEP	<b>226</b>	1,700
Cia. de Desenvolvimento e Modernização de Plantas Industriais - CDMPI	<b>175</b>	-
Nova Marlim	<b>142</b>	286
Cia Petrolífera Marlim	<b>57</b>	139
Albacora	<b>46</b>	55
Pargo, Carapeba, Garoupa and Cherne (PCGC)	<b>26</b>	35
Fundo de Investimento Imobiliário - FII (4)	<b>-</b>	85
Repurchased securities (5)	<b>(226)</b>	(1,722)
	<b>6,374</b>	6,042
Current portion of project financings	<b>(2,182)</b>	(2,413)
	<b>4,192</b>	3,629



**14. Project Financings (Continued)**

- (1) Charter Development CDC is responsible for Marlim Leste (P-53 project).
- (2) Nova Transportadora do Sudeste NTS and Nova Transportadora do Nordeste NTN take part in the consortium responsible for Malhas Project.
- (3) Codajás consolidates Transportadora Urucu - Manaus S.A. which is responsible for the Amazonia Project.
- (4) Investment Fund for Fixed Assets FII is responsible for Certified Receipts of Acceptance of Fixed Assets CRI Macaé Project.
- (5) At December 31, 2006 and 2005, the Company had amounts invested abroad in an exclusive investment fund. These securities are considered to be extinguished, and thus the related amounts, together with applicable interest have been removed from the presentation of marketable securities and project financings (see also Note 5).

The Company has received certain advances amounting to US\$376 which are recorded as project financings obligations and are related to assets under agreements with investors, which are included to the property, plant and equipment balance. Such asset and obligation amounts are presented gross as the obligation can only be settled through delivery of the fully constructed asset.

At December 31, 2006, the long-term portion of project financings becomes due in the following years:

2008	1,252
2009	993
2010	666
2011	401
2012	158
2013 and thereafter	722
	4,192

As of December 31, 2006, the amounts of cash outlay commitments assumed related to consolidated structured project financings are presented as follows:

Cia. de Desenvolvimento e Modernização de Plantas Industriais CDMPI	733
Transportadora Gasene	601
PDET Offshore S.A.	378
Charter Development - CDC	224
	1,936



**14. Project Financings (Continued)**

The following summarizes the projects, their purposes, the guarantees and estimated investments of each project:

<b>Project</b>	<b>Purpose</b>	<b>Main guarantees</b>	<b>Total estimated investments</b>
<b>Barracuda/ Caratinga</b>	To allow development of production in the fields of Barracuda and Caratinga in the Campos Basin the SPC Barracuda and Caratinga Leasing Company B.V. (BCLC), is in charge of building all of the assets (wells, submarine equipment and production units) required by the project and is also the owner of them.	Guarantee provided by Brasoil to cover BCLC's financial requirements.	US\$3,100
<b>CLEP</b>	Companhia Locadora de Equipamentos Petrolíferos - CLEP furnishes assets related to oil production located in the Campos Basin through a lease agreement for the period of 10 years, and at the end of which period Petrobras will have the right to buy shares of the SPC or project assets.	Lease prepayments in case revenue is not sufficient to cover payables to the lenders.	US\$1,250
<b>Cabiúnas</b>	Project with the objective of increasing gas production transportation from the Campos Basin. Cayman Cabiunas Investment Co. Ltd. (CCIC), supplies assets to Petrobras under an international lease agreement.	Pledge of 10.4 billion m <sup>3</sup> of gas.	US\$850

**14. Project Financings (Continued)**

<b>Project</b>	<b>Purpose</b>	<b>Main guarantees</b>	<b>Total estimated investments</b>
<b>Malhas Project - (NTN / NTS)</b>	Consortium between TRANSPETRO, Transportadora Nordeste Sudeste (TNS), Nova Transportadora do Sudeste (NTS) and Nova Transportadora do Nordeste (NTN). NTS and NTN supply assets related to natural gas transportation. TNS (a 100% GASPETRO company) supplies assets that have already been previously set up. TRANSPETRO is the gas pipes operator.	P r e p a y m e n t s based on transportation capacity to cover any consortium cash insufficiencies	US\$1,000
<b>EVM</b>	Project with the objective of allowing set up of submarine oil production equipment in the fields Espadarte, Voador, Marimbá and other seven smaller fields in the Campos Basin. EVM Leasing Co. (EVMLC), supplies assets to Petrobras under an international lease agreement.	Pledge of certain oil volumes.	US\$1,070
<b>NovaMarlim</b>	Consortium with NovaMarlim Petróleo S.A. (NovaMarlim) which supplies submarine oil production equipment and refunds Petrobras for operating costs resulting from the operation and maintenance of field assets.	30% of the field production limited to 720 days.	US\$933
<b>PDET</b>	PDET Offshore S.A. is the future owner of the Project assets whose objective is that of improving the infrastructure to transfer oil produced in the Campos Basin to the oil refineries in the Southeast Region and export. The assets will be later leased to Petrobras for 12 years.	All of the project s assets will be pledged as collateral.	US\$1,270
<b>Marlim</b>	Consortium between Companhia Petrolífera Marlim (CPM), which furnishes to Petrobras submarine equipment for oil production of the	70% of the field production limited to 720 days	US\$1,500

Marlim field.

<b>Albacora</b>	Consortium between Petrobras and Albacora Japão Petróleo Ltda. (AJPL), which furnishes to Petrobras oil production assets of the Albacora field in the Campos Basin.	Pledge of assets	US\$170
<b>Albacora/ PETROS</b>	Consortium between Petrobras and Fundação PETROS de Seguridade Social, which furnishes to Petrobras oil production assets of the Albacora field in the Campos Basin.	Pledge of assets	US\$240
<b>PCGC</b>	Companhia de Recuperação Secundária (CRSec) supplies assets to be used by Petrobras in the fields Pargo, Carapeba, Garoupa, Cherne and others through a lease agreement with monthly payments.	Additional lease payment if revenue is not sufficient to cover payables to lenders.	US\$134

**14. Project Financings (Continued)**

<b>Project</b>	<b>Purpose</b>	<b>Main guarantees</b>	<b>Total estimated investments</b>
<b>Marlim Leste (P-53) Project (CDC)</b>	To develop production in the Marlim Leste field, Petrobras will use Floating Production Unit P-53, to be chartered from Charter Development LLC, a company incorporated in the state of Delaware, U.S.A. The Bare Boat Charter agreement will be effective for a 15-year period counted from the date of signature.	<u>Completion</u> : the flow of charter payments to be made by Petrobras will begin at a certain date.  <u>Cost Overrun</u> : Any increase in P-53 construction costs will represent an increase in charter amounts payable by Petrobras.	US\$1,180
<b>Amazônia (Codajás)</b>	Construction of a gas pipeline with length of 385 km, between Coari and Manaus, and a GLP pipeline with length of 285 Km between Urucu and Coari, both under the responsibility of Transportadora Urucu - Manaus S.A. and the construction of a thermoelectric plant, in Manaus, with capacity of 488 MW through Companhia de Geração Termelétrica Manauara S.A.	Being negotiated	US\$1,300
<b>GASENE</b>	Transportadora Gasene S.A. is responsible for the construction and future ownership of pipelines to transport natural gas with a total length of 1.4 thousand km and transportation capacity of 20 million cubic meters per day, connecting the Cabiúnas Terminal in Rio de Janeiro to the city of Catu, in Bahia state.	To be defined.	US\$2,000
<b>CDMPI (modernization of REVAP)</b>	This project has the objective of raising the Henrique Lage (REVAP) refinery's national heavy oil processing capacity, bringing the diesel it produces into line with the new national specifications and reducing pollution levels. To achieve this, the SPE Cia. de Desenvolvimento e Modernização de Plantas Industriais - CDMPI was founded, which shall construct and lease to Petrobras	Prepaid rental to cover any cash deficiencies of CDMPI.	US\$900

a Retarded Coking plant, a Coke Naphtha Hydrotreatment plant and related plants to be installed at this refinery.

<b>Mexilhão</b>	Construction of a platform (PMXL-1) to produce natural gas at Campos de Mexilhão and Cedro, located in the Bacia de Santos, State of São Paulo, which shall be held by Companhia Mexilhão do Brasil (CMB), responsible for obtaining the funds necessary to build such platform. After building the PMXL-1 shall be leased to Petrobras, holder of the exploration and production concession in the aforementioned fields	To be defined	US\$595
-----------------	---	---------------	---------

**14. Project Financings (Continued)**

Project	Purpose	Main guarantees	Total estimated investments
<b>P-55 and P-57</b>	<p>To develop production at Module 3 in the Roncador field (P-55) and Phase 2 of Jubarte field (P-57). A Deepwater charter LLC and a Deepblue Charter LLC are responsible for jointly contracting four SPCs to build the UEP: one for the P-55 hull, another for the P-57 hull, as well as two other for Generation and Compression Modules for both UEPs. At the end, PNBV shall charter the P-55 from Deepwater and the P-57 from Deepblue and will sub-charter them to Petrobras.</p> <p>Undergoing selection process for the SPCs (IDB with interaction).</p>	<p>Future chartering commitment of Petrobras with PNBV and PNBV with the owner of UEP (Deepwater and Deepblue).</p>	US\$1,960
<b>Termobahia</b>	<p>Acquisition of 49% of the interest held by ABB-EV- Equity Venture (ABB-EV) in TERMOBAHIA, comprised of shares and credits via the financial structuring agreed with the Interamerican Development Bank. An SPE was structured called BLADE Securities Ltd ( BLADE ), headquartered in Ireland, which shall be the successor of the rights held by ABB-EV until Petrobras presents a strategic partner.</p>	None given.	US\$39.6

**Blade Securities Limited**

The Special Purpose Company (SPC) BLADE Securities Ltd ( BLADE ), was created by the Deutsche Bank (DB), in order to support Petrobras in its transactions related to the acquisition of a 49% interest held by ABB-EV in TERMOBAHIA power plant. (See Note 18 (h)). The financial structuring involves two simultaneous operations: the acquisition of ABB-EV's rights and the sale of such rights to a private institution, DB, until a strategic partner is



introduced by Petrobras within a maximum period of one year.

Under the agreements, PIFCo paid to Blade US\$1, and in return, Blade transferred to PIFCo the right to any dividends to be received from TERMOBAHIA and the rights to the shares of TERMOBAHIA either for PIFCo or a Petrobras subsidiary. Additionally, PIFCo paid to Blade US\$38, and in return, Blade transferred to PIFCo any amounts received from TERMOBAHIA related to the subordinated loan recorded as notes receivable, which has an interest rate of 8% p.a. and an expiry date of 2023, and the right to the loans receivable for PIFCo or a Petrobras subsidiary. (See Note 18(h)).

**14. Project Financings (Continued)**

As a result of the transaction series, Petrobras recognized a US\$4 gain on debt extinguishment on December 31, 2005, related to the fact it will no longer be paying 18.79% interest to a third party lender. Due to immateriality, the Company has not applied step acquisition accounting to the purchase of the interest in TERMOBAHIA.

**15. Capital Lease Obligations**

The Company leases certain offshore platforms and vessels, which are accounted for as capital leases. At December 31, 2006, assets under capital leases had a net book value of US\$1,338 (US\$1,419 at December 31, 2005).

The following is a schedule by year of the future minimum lease payments at December 31, 2006:

2007	300
2008	313
2009	284
2010	230
2011	112
2012	62
2013 and thereafter	36
Estimated future lease payments	1,337
Less amount representing interest at 6.2% to 12.0% annual	(282)
Present value of minimum lease payments	1,055
Less current portion of capital lease obligations	(231)
Long-term portion of capital lease obligations	824

**16. Employees Post-retirement Benefits and Other Benefits****(a) Employees post-retirement benefits balances**

The balances related to Employees Post-retirement Benefits are represented as follows:

	As of December 31,			
	2006		2005	
	Pension benefits	Health care benefits	Pension benefits	Health care benefits
Current liabilities	198	-	206	-
Long-term liabilities	4,645	5,433	3,627	3,004
Employees post-retirement projected benefit obligation	4,843	5,433	3,833	3,004
Accumulated other comprehensive income	3,110	1,495	2,941	-
Tax effect	(1,058)	(508)	(1,011)	-
Net balance recorded in shareholders equity	2,052	987	1,930	-

**(b) Pension plan - Fundação Petrobras de Seguridade Social - PETROS**

The Fundação Petrobras de Seguridade Social (PETROS) was established by Petrobras as a private, legally separate nonprofit pension entity with administrative and financial autonomy. As such, PETROS has the following principle objectives:

- (i) institute, manage and execute benefit plans for the companies or entities with which it has signed agreements;
- (ii) provide administration and execution services for benefit plans focused on post-retirement payments; and
- (iii) promote the well-being of its members, especially with respect to post-retirement payments.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(b) Pension plan - Fundação Petrobras de Seguridade Social PETROS (Continued)**

The PETROS plan is a contributory defined-benefit pension plan introduced by Petrobras in July of 1970, to supplement the social security pension benefits of employees of Petrobras and its Brazilian subsidiaries and affiliated companies. In order to fund its objectives, PETROS receives monthly contributions from the sponsoring companies of the PETROS Plan amounting to 12.93% of the salaries of participants in the plan. Additionally PETROS is funded by income resulting from the investment of these contributions. The Company's funding policy is to contribute to the plan annually the amount determined by actuarial calculations. In the calendar 2006 year, benefits paid totaled US\$713 (US\$570 in 2005).

The Company's liability related to future benefits to plan participants is calculated on an annual basis by an independent actuary, based on the Projected Unit Credit method. The assets that guarantee the pension plan are presented as a reduction to the net actuarial liabilities.

The actuarial gains and losses generated by the differences between the values of the obligation and assets determined based on projections and the actual figures, are respectively included or excluded from the calculation of the net actuarial liability and recorded as Postretirements benefit reserves adjustments net of tax - pension cost, in shareholders' equity. Actuarial gains and losses are amortized during the average remaining service period of the active employees of approximately 10 years at December 31, 2006, in accordance with the procedure established by SFAS 87.

The relation between contributions by the sponsors and participants of the PETROS Plan, considering only those attributable to the Company and subsidiaries in the 2006 and 2005 financial years, was 1.00 to 1.00. The Company's best estimate of contributions expected to be paid in 2007 relative to the pension plan approximates US\$194, with total pension benefit payments in 2007 expected to be US\$830.

According to Constitutional Amendment No. 20, the computation of any deficit in the defined-benefit plan in accordance with the actuarial method of the current plan (which differs from the method defined in SFAS 87), must be equally shared between the sponsor and the participants, by an adjustment to the normal contributions.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(b) Pension plan - Fundação Petrobras de Seguridade Social PETROS (Continued)**

The PETROS Plan is closed to new employees of the Petrobras system joining from September 2002 and the Company contracted a group life insurance policy to cover employees commencing employment with the Company subsequent to closure of the of the PETROS plan; this policy will remain in effect until a new private pension plan is implemented.

**Plan assets**

Plan assets are invested primarily in government securities, investment funds, equity instruments and properties.

The table below describes the types of plan assets:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Government securities	<b>44%</b>	45%
Investments funds	<b>27%</b>	26%
Equity instruments	<b>20%</b>	18%
Other	<b>9%</b>	11%
	<b>100%</b>	100%

Plan assets include the following securities of related parties:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Petrobras common shares	<b>304</b>	178
Petrobras preferred shares	<b>429</b>	343
Government controlled companies	<b>54</b>	14
Government securities	<b>4,952</b>	3,899
Securities of other related parties	<b>171</b>	183
	<b>5,910</b>	4,617

PETROS provided certain financing for the continued development of the Albacora oil and gas field located in the Campos basin, that is classified as securities of other related parties (see Note 14).



**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(b) Pension plan - Fundação Petrobras de Seguridade Social PETROS (Continued)****Plan assets (Continued)**

The Company uses 6.19% as the expected long-term rate of return over inflation on PETROS assets. The PETROS portfolio of investments as of December 31, 2006 was comprised of 71% securities, 44% of which were held-to-maturity government securities that earn interest at 6% annually plus the IPCA (Consumer Price Index) variation and 27% of which were Investments Funds that earn interest approximate to the CDI (Certificado de Depósito Interbancário, or Interbank Deposit Certificate), which has been yielding more than 6% annually. Thus, the Company considers a 6.19% long term interest rate appropriate to calculate the expected return on assets, as such aligns with the composition of the PETROS asset portfolio.

PETROS has a significant volume of investments in government securities, mainly NTN-B bonds, which by an agreement with the Supplementary Social Security Department will be held-to-maturity being recorded at fair value, for which a net present adjustment was required. Thus, the percentage of assets allocated in this investment will remain the same over the short term.

**New benefits plan**

In May of 2001, the Board of Directors of Petrobras approved the creation of a mixed social security plan, for current and new employees, based on defined contribution formula for programmable benefits and a defined benefit formula for risk benefits. However, the migration of participants and beneficiaries of the previous plan (PETROS) to the new plan was suspended, pursuant to a Federal Judicial ruling arising from an injunction filed by the employee union. A court order in 2004 granted the injunction ruling against the new plan and invalidating any changes to the PETROS plan premised upon intended migration to a new plan. This court decision is under appeal.

In 2003, the Company formed a task force with representatives of the National Union of Oil Workers (FUP), unions and PETROS, among others, in order to evaluate alternatives to a new model for the Company's supplementary pension plan, including analyses of negotiated arrangements for the settlement of actuarial deficits.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(b) Pension plan - Fundação Petrobras de Seguridade Social PETROS (Continued)****New benefits plan (Continued)**

On April 19, 2006, the Company, aiming to achieve an agreement regarding its Supplementary Pension Plan, presented to employee participants and retirees a proposal to bring equilibrium to the actual PETROS Plan and the implementation of a new plan, denominated PETROS Plan 2.

Execution of the proposal presented by the Company's Executive Board was subject to a number of conditions, including the renegotiation of the PETROS Plan Regulations, in relation to the means of readjusting the benefits and pensions, considering a significant rate of individual accession of employees and dependants.

The overall renegotiation target previously set by the Company had not been achieved. As a result the proposal presented by Petrobras became null and void.

On January 08, 2007, the Petrobras Board of Directors approved the reopening of the PETROS Plan renegotiation process, in order to meet the claims of the trade unions, as most participants were in favor of the renegotiation.

The new target for the minimum accession number to the renegotiation was set at 2/3 (two-thirds) of the members and the final deadline for them to make their choice was February 28, 2007. The renegotiation target was met and the proposal submitted by the Company became effective, and PETROS is calculating the amounts to be funded by the sponsors, that will reduce the deficit of the PETROS Plan, as established by Brazilian pension law.

On October 20, 2006, the Board of Directors of Petrobras approved the introduction of PETROS Plan 2 for employees currently with no pension plan.

The New Supplementary pension plan was formulated according to the Variable Contribution model. In this model, the contributions are capitalized in individuals accounts, and the pension benefits are established according to the account balances. This plan also includes risk benefits with coverage for illness, incapacity and death, and a lifetime income.



**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(b) Pension plan - Fundação Petrobras de Seguridade Social PETROS (Continued)****New benefits plan (Continued)**

The PETROS Plan 2 also includes a minimum benefit for payment of annuities which guarantees coverage of the benefit to ensure it does not have a monetary value of under 30% of the average contribution salary.

On December 20, 2006 the Department for Coordinating and Controlling State Companies (DEST) decided to approve the proposed PETROS Plan 2, which was also approved on January 05, 2007 by the Ministry of Mines and Energy.

On January 19, 2007, the PETROS Decision-making Board approved the PETROS Plan 2, which will be referred for assessment and statement by the Supplementary Pensions Office - SPC, for the proper final approval, whereupon it may be offered to the employees who are not presently covered by a supplementary pension plan sponsored by the Company.

Petrobras and the other sponsors will fully assume the contributions corresponding to the period in which the new participants had no plan. This past service shall consider the period from the date of admission to the date enrolment commenced in the PETROS Plan 2. The disbursements will be conducted over the first months for contributions up to the total months the participant had no plan, and shall cover the portion relating to the participants and sponsor. The maximum estimated value of this actuarial commitment as of December 31, 2006 if the plan is approved by SPC and accepted by all new employees was US\$109.

This New Plan also allows the Company to maintain the pension coverage it offers, mitigates the risks presented by the defined benefit model adopted and considerably reduces the possibility of future deficits. The impact of joining the new plan and its related benefit costs will be valued according to the standards established in SFAS 87, 132 and 158 and will only be computed and recognized in the accounts when the plan is implemented.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(b) Pension plan - Fundação Petrobras de Seguridade Social PETROS (Continued)****TRANSPETRO**

TRANSPETRO maintains a defined-contribution private pension scheme with PETROS called Plano TRANSPETRO, which receives monthly contributions equivalent to 5.32% of the payroll of the members and is equal to the contributions made by the participants.

**(c) PETROBRAS ENERGIA PEPSA (including PESA)****Defined contribution plan****Supplementary Pension Plan for Personnel**

In November 2005, the Board of Directors of Petrobras Energia approved the implementation of a defined voluntary contributions plan which all of the Company's employees may elect to join Petrobras Energia. Through this plan, Petrobras Energia will make contributions to a trust equivalent to the contributions made by the employees that will subscribe to the plan to a mutual fund or AFJP, at their choice, in conformity with a scheme defined for each salary level. The participating employees may make voluntary contributions exceeding those established in the mentioned scheme, which will not be considered for purposes of the contributions to be made by Petrobras Energia.

In the fiscal years ended December 31, 2006 and 2005, Petrobras Energia recorded an expense of US\$3 and US\$7, respectively, attributable to such benefits.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)**

**(c) PETROBRAS ENERGIA PEPSA (including PESA) (Continued)**

**Defined benefit plan**

**Indemnity Plan**

This is a defined benefit plan for all the employees who fulfill certain conditions, and consists of granting, upon retirement, a one-month salary per years of service at the Company, in conformity with a decreasing scale considering the years of effectiveness of the plan.

**Compensating Fund**

This is a defined benefit plan for all employees of Petrobras Energia who have joined the Company prior to May 31, 1995, and have reached a certain number of years of service. The employee benefit is based on the last computable salary and years of service of each employee included in the fund.

The plan is of a supplemental nature, that is to say the benefit to the employee is represented by the amount determined under the provisions of this plan, after deducting benefits payable to the employee under the contribution plan and the public retirement system, in order that the aggregate benefit to each employee equals the one stipulated in this plan.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(c) PETROBRAS ENERGIA PEPSA (including PESA) (Continued)****Defined benefit plan (Continued)**

The plan calls for a contribution to a fund exclusively by Petrobras Energía and without any contribution by the employees, provided that they should make contributions to the retirement system for their whole salary. As provided in Petrobras Energía's By-laws, the Company makes contributions to the fund on the basis of a Board of Directors proposal to the Shareholders Meeting up to 1.5% of net income for each year. The assets of the fund were contributed to a trust. The goals with respect to asset investment are: (i) the preservation of capital in US dollars, (ii) the maintenance of high levels of liquidity, and (iii) the attainment of the highest yields possible on a 30-days basis. For this reason, the assets are invested mainly in bonds, corporate bonds, mutual funds, and certificates of deposits. The Bank of New York is the trustee and Watson Wyatt is the managing agent. Should there be an excess (duly certified by an independent actuary) of the funds under the trust agreement to be used to settle the benefits granted by the plan, Petrobras Energía will be entitled to make a choice and use it, in which case it would have to notify the trustee thereof.

**(d) SFAS 158 - Employers Accounting for Defined Benefit Pension and Other Postretirement Plans**

In September 2006, the FASB issued SFAS 158 - Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an Amendment of FASB Statements No. 87, 88, 106 and 132(R) ( SFAS 158 ), which became effective for the Company on December 31, 2006. This standard requires the Company to recognize the overfunded or underfunded status of each of its defined benefit pension and other postretirement benefit plans as an asset or liability and to reflect changes in the funded status through Accumulated other comprehensive income, as a separate component of shareholders' equity.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(d) SFAS 158 - Employers Accounting for Defined Benefit Pension and Other Postretirement Plans (Continued)**

The incremental effect of applying SFAS 158 on individual line items of the balance sheet as of December 31, 2006 were as follows:

	<b>Pre-FAS 158 with Minimum Liabilities Adjustments</b>	<b>FAS 158 Adoption Adjustments</b>	<b>Post FAS 158</b>
Deferred taxes	3,459	(543)	2,916
Employees post-retirement projected benefits obligation Pension	4,712	131	4,843
Employees post-retirement projected benefits obligation Health care	3,938	1,495	5,433
Accumulated other comprehensive income - pension adjustments	(1,956)	(96)	(2,052)
Accumulated other comprehensive income - health care adjustments	-	(987)	(987)
Total Liabilities and shareholders equity	98,680	-	98,680
Total shareholders equity	45,382	(1,083)	44,299

**(e) Health care benefits - Assistência Multidisciplinar de Saúde (AMS)**

Petrobras and its Brazilian subsidiaries maintain a health care benefit plan (AMS), which offers defined benefits and covers all employees (active and inactive) together with their dependents. The plan is managed by the Company, with the employees contributing fixed amounts to cover principal risks and a portion of the costs relating to other types of coverage in accordance with participation tables defined by certain parameters including salary levels.

The Company's commitment related to future benefits to plan participants is calculated on an annual basis by an independent actuary, based on the Projected Unit Credit method. The health care plan is not funded or otherwise collateralized by assets. Instead, the Company makes benefit payments based on annual costs incurred by plan participants.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(e) Health care benefits - Assistência Multidisciplinar de Saúde (AMS) (Continued)**

Until 2006, the actuarial gains and losses generated by the differences between the values of the obligation determined based on projections and the actual figures, were respectively included or excluded when defining the net actuarial obligation.

As of December 31, 2006, according to SFAS 158 (See Note 16(d)), the actuarial gains and losses generated by the differences between the values of the obligation determined based on projections and the actual figures, are respectively included or excluded from the calculation of the actuarial obligation and recorded as Postretirements benefit reserves adjustments net of tax- health care cost , as Accumulated Other Comprehensive Income, in shareholders equity.

The gains and losses recorded as Accumulated Other Comprehensive Income are amortized over the average remaining service period of the active employees.

Upon adoption of SFAS 158, as of December 31, 2006 the liabilities related to health care increased by US\$1,495 and shareholders equity reduced by US\$987, net of income taxes.

On December 15, 2006, Petrobras implemented the Medicine Benefit, which provides special terms on the acquisition of certain medicines by members of the AMS from participating drugstores, located throughout Brazil.

Following the introduction of this benefit, the unrecognized prior service cost estimated by independent actuary, as of December 31, 2006 was US\$86, and will be amortized over the average remaining service period of the active employees. The unrecognized prior service cost was included in Accumulated Other Comprehensive Income and presented in Change in Benefit Obligations, as Plan Amendments .

For measurement purposes, a 10% annual rate of increase in the per capita cost of covered health care benefits was assumed upon adoption of SFAS 106. The annual rate was assumed to decrease to 4.5% from 2007 to 2036.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(e) Health care benefits - Assistência Multidisciplinar de Saúde (AMS) (Continued)**

Assumed health care cost trend rates have a significant effect on the amounts reported for the post-retirement health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	<b>One percentage point-increase</b>	<b>One percentage point-decrease</b>
Effect on total of services and interest cost component	113	(91)
Effect on post-retirement benefit obligation	832	(679)

**LIQUIGÁS DISTRIBUIDORA S.A.**

Liquigás maintains a health care benefit plan, which offers defined benefits and covers LPG employees. At December 31, 2006, Liquigás recorded liabilities in connection with future post-retirement health care benefit costs, in the amount of US\$18 (US\$16 in 2005). The plan is managed by Liquigás and the liability related to future benefits to plan participants is calculated on an annual basis by an independent actuary, based on the Projected Unit Credit method, according to SFAS 106, SFAS 132 Employers' Disclosures about Pensions and Other Post-retirement Benefits and an amendment of FASB Statements No. 87, 88, and 106 ( SFAS 132 ) and SFAS 158.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(f) Funded status of the plans**

The funded status of the plans at December 31, 2006 and 2005, based on the report of the independent actuary, and amounts recognized in the Company's balance sheets at those dates, are as follows:

	<b>As of December 31,</b>			
	<b>2006</b>		<b>2005</b>	
	<b>Pension Benefits (2)</b>	<b>Health Care Benefits (3)</b>	<b>Pension Benefits (2)</b>	<b>Health care Benefits (3)</b>
Change in benefit obligation:				
Benefit obligation at beginning of year	14,422	4,974	11,509	4,025
Service cost	174	81	146	74
Interest cost	1,712	595	1,381	489
Actuarial loss (gain)	244	(599)	363	(28)
Benefits paid	(713)	(175)	(570)	(141)
Plan amendments - Medicine benefit	-	86		
Others	7	-	(2)	-
Gain on translation	1,392	471	1,595	555
Benefit obligation at end of year (1)	17,238	5,433	14,422	4,974
Change in plan assets:				
Fair value of plan assets at beginning of year	9,413	-	7,104	-
Actual return on plan assets	2,447	-	1,609	-
Company's contributions	187	175	155	141
Employees' contributions	135	-	112	-
Benefits paid	(713)	(175)	(570)	(141)
Others	(1)	-	(2)	-
Gain on translation	927	-	1,005	-
Fair value of plan assets at end of year	12,395	-	9,413	-
Reconciliation:				
Funded status	(4,843)	(5,433)	(5,009)	(4,974)
Unrecognized actuarial loss			4,117	1,970
Net amount recognized			(892)	(3,004)



Amounts recognized in the balance sheet consist of:

Employees post-retirement benefits obligation	<b>(4,843)</b>	<b>(5,433)</b>	(3,833)	(3,004)
Accumulated other comprehensive income	<b>3,110</b>	<b>1,495</b>	2,941	-
Net amount recognized	<b>(1,733)</b>	<b>(3,938)</b>	(892)	(3,004)

(1) Projected benefit obligation, measured at December 31, 2006 and 2005. The TRANSPETRO plan has no participants to date and the PEPSA plan is defined contribution for employees above a specified salary level, and thus such plans have no effect on projected benefit obligation. Thus, the projected benefit obligation disclosed above is aggregated to all Petrobras group companies.

(2) Includes PETROS (Petrobras group companies), PEPSA and PELSA pension benefits obligations.

(3) Includes AMS (Petrobras group companies) and Liquigás health care benefits obligations.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(f) Funded status of the plans (Continued)**

Net periodic benefit cost includes the following components:

	As of December 31,			
	2006		2005	
	Pension Benefits	Health Care Benefits	Pension Benefits	Health care Benefits
Service cost-benefits earned during the year	174	81	146	74
Interest cost on projected benefit obligation	1,712	595	1,381	489
Expected return on plan assets	(1,157)	-	(887)	-
Gain on translation	30	11	56	22
Recognized actuarial loss	322	140	376	141
	<b>1,081</b>	<b>827</b>	1,072	726
Employees contributions	(133)	-	(112)	-
Net periodic benefit cost	<b>948</b>	<b>827</b>	960	726

The main assumptions adopted in 2006 and 2005 for the actuarial calculation are summarized as follows:

	2006		2005	
	Pension benefits	Health care benefits	Pension benefits	Health care benefits
Discount rates	Inflation: 4.5% + 6%	Inflation: 4.5% + 6%	Inflation: 5% + 6%	Inflation: 5% + 6%
Rates of increase in compensation levels	Inflation: 4.5% + 2.02%	Inflation: 4.5% + 2.02%	Inflation: 5% + 2.08%	Inflation: 5% + 2.08%
Expected long-term rate of return on assets	Inflation: 4.5% + 6.19%	Not applicable	Inflation: 5% + 6.19%	Not applicable
Mortality table	AT 2000*	AT 2000*	AT 2000	AT 2000

(\* Segregated by sex (male and female)).

Petrobras has aggregated information for all defined benefit pension plans. The domestic benefit plans of Petrobras, BR Distribuidora, PETROQUISA, and REFAP contain similar assumptions and the benefit obligation related to PEPSA, the international plan, is not significant to the total obligation and thus has also been aggregated. All Petrobras group pension plans have accumulated benefit obligation in excess of plan assets.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(f) Funded status of the plans (Continued)**

The determination of the expense and liability relating to the Company's pension plan involves the use of judgment in the determination of actuarial assumptions. These include estimates of future mortality, withdrawal, changes in compensation and discount rate to reflect the time value of money as well as the rate of return on plan assets. These assumptions are reviewed at least annually and may differ materially from actual results due to changing market and economic conditions, regulatory events, judicial rulings, higher or lower withdrawal rates or longer or shorter life spans of participants.

According to the requirements of SFAS 87, and subsequent interpretations, the discount rate should be based on current prices for settling the pension obligation. Applying the precepts of SFAS 87 in historically inflationary environments such as Brazil creates certain issues as the ability for a company to settle a pension obligation at a future point in time may not exist as long-term financial instruments of suitable grade may not exist locally as they do in the United States.

Although the Brazilian market has been demonstrating signs of stabilization under the present economic model, as reflected in market interest rates, it is not yet prudent to conclude that market interest rates will be stable.

In 2004, Petrobras approved a change to a new mortality table of the actuarial assumptions of the pension and healthcare plans in Brazil; this new mortality table reflects updated assumptions and changes relative to the profile of employees, retirees and pensioners, based on longevity, age of invalidity and invalid mortality tables.

**(g) Cash contributions and benefit payments**

In 2006, the Company contributed US\$187 to its pension plans. In 2007, the Company expects contributions to be approximately US\$194. Actual contribution amounts are dependent upon investment returns, changes in pension obligations and other economic factors. Additional funding may ultimately be required if investment returns are insufficient to offset increases in plan obligations.

**16. Employees Post-retirement Benefits and Other Benefits (Continued)****(g) Cash contributions and benefit payments (Continued)**

The following benefit payments, which include estimated future service, are expected to be paid by the pension fund in the next 10 years:

	<b>Pension benefits</b>	<b>Health care benefits</b>
2007	830	196
2008	902	224
2009	985	256
2010	1,082	292
2011	1,192	332
Subsequent five years	7,949	2,371

**17. Shareholders Equity****(a) Capital**

The Company's subscribed and fully paid-in capital at December 31, 2006 consisted of 2,536,673,672 common shares and 1,850,364,698 preferred shares, and at December 31, 2005 consisted of 2,536,673,672 common shares and 1,849,478,028 preferred shares, as retroactively restated for stock split, mentioned below. The preferred shares do not have any voting rights and are not convertible into common shares and vice-versa. Preferred shares have priority in the receipt of dividends and return of capital.

On May 13, 2005, Petrobras management approved the proposed share split and the related amendment to article 4 of the Company's by-laws. These issues were discussed by the shareholders at the Extraordinary General Meeting (EGM) held on June 15, 2005.

The Extraordinary General Meeting held on July 22, 2005 decided to effect a split of each Company's share into four, resulting in a free distribution of 3 (three) new shares of the same type for each original share, based on the shareholding structure at August 31, 2005. At the same date, an amendment to article 4 of the Company's by-laws to cause capital be divided into 4,386,151,700 shares, of which 2,536,673,672 are common shares and 1,849,478,028 are preferred shares, with no nominal value, was approved. This amendment to the Company's bylaws is effective from September 1, 2005.

**17. Shareholders Equity** (Continued)**(a) Capital** (Continued)

The relation between the American Depositary Receipt (ADS) and shares of each class was changed from one to four shares for one ADS. All share and per share information in the accompanying financial statements and notes has been adjusted to reflect the result of the share split.

Current Brazilian law requires that the Federal Government retain ownership of 50% plus one share of the Company's voting shares.

Shareholders at the Extraordinary General Meeting held June 01, 2006 approved the incorporation of shares in PETROQUISA by Petrobras, pursuant to the re-ratification of the Protocol of Merger and Incorporation on the share incorporation transaction executed by the two companies. The Board of Directors of the Company approved the issue of 886,670 preferred shares of the Company in connection with the incorporation of shares in PETROQUISA by Petrobras.

To implement the transaction, the exchange ratio for the shares to be used was based on the net equity value of both companies at the base date of December 31, 2005, when 4,496 preferred shares issued by Petrobras were attributed to each batch of 1,000 common or preferred shares issued by PETROQUISA.

No Petrobras shareholders had stated their intention to exercise the right to withdraw by the legal deadline of July 07, 2006. Five PETROQUISA shareholders with a total interest of 1,015,910 shares exercised the right to withdraw by the established deadline (by July 05, 2006) and were reimbursed at the rate of R\$153.47 (US\$71) per batch of 1,000 shares, using funds provided by PETROQUISA, on July 10, 2006. Petrobras then acquired the shares for the same price, thereby transferring ownership.

**17. Shareholders Equity** (Continued)**(a) Capital** (Continued)

On December 15, 2006, pursuant to article 29, section II of the Company By-laws, the Board of Directors authorized the buyback of part of the preferred shares in circulation for future cancellation, using funds from the profit reserves subject to the following terms:

- Objective: reduce the excess of cash and enhance the capital structure, helping to reduce the cost of Petrobras capital.
- Amount: up to 91,500,000 preferred shares, corresponding to 4.9% of the total of this class of share in circulation, which is 1,850,364,700 shares.
- Price: the acquisition will occur on the Stock Exchange, at market values on the acquisition dates throughout the buyback term.
- Term: up to 365 (three hundred and sixty-five) days as from December 15, 2006.

In line with its share buyback policy, the Board of Directors concluded the current cash situation enables this project to be implemented without compromising the dividend payment and the investment program, while maintaining the operating and financial targets established in the Strategic Plan.

At an Extraordinary General Meeting held together with the General Ordinary Meeting, on April 2, 2007, the shareholders of Petrobras approved an increase in the Company's capital to US\$24,623 (R\$52,644) through the capitalization of revenue reserves accrued during previous financial years, in the amount of US\$1,577 (R\$3,372), and of statutory reserve, in the amount of US\$471 (R\$1,008), and without the issuance of new shares, in accordance with article 169, paragraph 1, Law No. 6.404/76. This capitalization aimed to bring the Company's capital in line with the investments of an oil company given intensive use of capital and extended operating cycles.

**17. Shareholders Equity** (Continued)**(a) Capital** (Continued)

At an Extraordinary General Meeting held together with the General Ordinary Meeting, on April 3, 2006, the shareholders of the Company approved an increase in the Company's capital to US\$22,397 (R\$48,248) through the capitalization of retained earnings accrued during previous financial years, in the amount of US\$6,969 (R\$15,012), and without the issuance of new shares, in accordance with article 169, paragraph 1, Law no. 6,404/76. This capitalization aimed to bring the Company's capital in line with the investments of an oil company given intensive use of capital and extended operating cycles.

The General Extraordinary Meeting, held together with the General Ordinary meeting on March 29, 2004, increased the Company's capital to US\$11,701, through the capitalization of revenue reserves accrued during previous financial years, in the amount of US\$4,439, and without the issuance of new shares, in accordance with article 169, paragraph 1, Law No. 6,404/76. This capitalization was made in order to bring the Company's capital in line with the investment requirements of an oil company given intensive use of capital and extended operating cycles.

The Extraordinary General Meeting held on March 29, 2004 also approved an increase in the Company's authorized capital (paragraph 1, article 4, of the Company's by-laws) from R\$30.000 million to R\$60.000 million, through the issuance of up to 200,000,000 (two hundred million) preferred shares for payment in cash, assets and credit capitalization.

**(b) Dividends and interest on shareholders equity**

In accordance with the Company's by-laws, holders of preferred and common shares are entitled to a minimum dividend of 25% of annual net income as adjusted under Brazilian Corporate Law. In addition, the preferred shareholders have priority in the receipt of an annual dividend of at least 3% of the book value of the shares or 5% of the paid-in capital in respect of the preferred shares as stated in the statutory accounting records. As of January 1, 1996 amounts attributed to shareholders as interest (see below) can be deducted from the minimum dividend computation. Dividends are paid in Brazilian reais. The Company paid US\$760 in dividends during the year ended December 31, 2006 (2005 - US\$275 - 2004 - US\$366). No withholding tax is payable on distributions of dividends made since January 1, 1996.



**17. Shareholders Equity** (Continued)**(b) Dividends and interest on shareholders equity** (Continued)

Brazilian corporations are permitted to attribute interest on shareholders equity, which may either be paid in cash or be used to increase capital stock. The calculation is based on shareholders equity amounts as stated in the statutory accounting records and the interest rate applied may not exceed the Taxa de Juros de Longo Prazo (long-term interest rate or the "TJLP") as determined by the Brazilian Central Bank. Such interest may not exceed the greatest of 50% of net income or 50% of retained earnings plus revenue reserves. Interest on shareholders equity, is subject to withholding tax at the rate of 15%, except for untaxed or exempt shareholders, as established by Law No. 9,249/95. The Company paid US\$2,453 in interest on shareholders equity during the year ended December 31, 2006 (2005 - US\$1,835 - 2004 - US\$1,443).

The dividends related to the fiscal year ended December 31, 2006 approved at the Ordinary General Meeting held on April 2, 2007, in the amount of US\$3,693, corresponding to US\$0.84 per common and preferred share and US\$3.36 per ADS conforms to the by-laws in regard to guaranteed rights of preferred shares (article 5), and distributes dividends calculated on the adjusted net income to common and preferred shareholders. This dividend includes interest on capital approved by the Board of Directors on October 20, 2006, in the amount of US\$2,052, which was made available to shareholders on January 4, 2007, based on the shareholding position of October 31, 2006.

The second portion of interest on capital, approved by the Board of Directors on December 15, 2006, was made available to shareholders on March 30, 2007, based on the shareholding position of December 28, 2006, amounting to US\$923. The final portion of dividends in the amount of US\$718, approved by the Board of Directors on February 12, 2007, which will be made available based on the shareholding position of April 2, 2007, when occurred the Ordinary General Meeting which resolved the matter.

Interest on capital amounts are subject to withholding tax at the rate of 15%, except for untaxed or exempt shareholders, as established by Law No. 9,249/95. The dividends and the final portion of the interest on shareholders equity will be paid until June 1, 2007 as established by the General Shareholders Meeting. These amounts will be monetarily restated from December 31, 2006 to the initial date of payment, according to the variation in the SELIC rate.

**17. Shareholders' Equity** (Continued)

**(b) Dividends and interest on shareholders' equity** (Continued)

Interest on shareholders' equity was included with the proposed dividend for the year, as established in the Company's by-laws, generated an income tax and social contribution credits of US\$1,012 (US\$791 in 2005, and US\$650 in 2004).

The dividends related to the fiscal year ended December 31, 2005, approved at the General Shareholders' Meeting held April 3, 2006, in the amount of US\$2,998, (including the portions of interest on shareholders' equity, in the amount of US\$933, paid to the shareholders on January 5, 2006, and in the amount of US\$939, paid to the shareholders on March 22, 2006) were made available to shareholders on May 23, 2006.

The dividends related to the fiscal year ended December 31, 2004, approved at the General Shareholders' Meeting held March 31, 2005, in the amount of US\$1,900, (including the portion of interest on shareholders' equity, in the amount of US\$1,239, paid to the shareholders on February 15, 2005) were made available to shareholders on May 17, 2005.

Brazilian law permits the payment of dividends only from retained earnings as stated in the statutory accounting records. At December 31, 2006, the Company had appropriated all such retained earnings.

In addition, at December 31, 2006, the undistributed reserve in appropriated retained earnings, amounting to US\$20,074, may be used for dividend distribution purposes, if so approved by the shareholders, however, the Company's stated intent is to use such reserve to fund working capital and capital expenditures.

**17. Shareholders Equity** (Continued)**(c) Basic and diluted earnings per share**

Basic and diluted earnings per share amounts have been calculated as follows:

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Income before extraordinary item	<b>12,826</b>	10,186	6,190
Extraordinary gain, net of taxes	-	158	-
Net income for the period	<b>12,826</b>	10,344	6,190
Less priority preferred share dividends	<b>(577)</b>	(426)	(297)
Less common shares dividends, up to the priority preferred			
Shares dividends on a per-share basis	<b>(791)</b>	(584)	(407)
Remaining net income to be equally allocated to common and preferred shares	<b>11,458</b>	9,334	5,486
Weighted average number of shares outstanding			
Common/ADS	<b>2,536,673,672</b>	2,536,673,672	2,536,673,672
Preferred/ADS	<b>1,849,903,144</b>	1,849,478,028	1,849,478,028
Basic and diluted earnings per share			
Common and preferred (*) (**)	<b>2.92</b>	2.32	1.41
Basic and diluted earnings per ADS (*) (**)	<b>11.68</b>	9.28	5.64

(\*) Per share data is presented after extraordinary item .

(\*\*) Considers effect of 4 for 1 stock split that occurred on September 1, 2005.

**(d) Capital reserves**

- AFRMM

Relates to the Merchant Marine (AFRMM) freight surcharges levied in accordance with relevant legislation. These funds are used to purchase, enlarge or repair vessels of the Company s transport fleet.

- Fiscal incentive reserve

This reserve consists of investments in tax incentives in the Northeast Investment Fund (FINOR), arising from allocations of part of the Company's income tax.

**17. Shareholders Equity (Continued)****(e) Appropriated retained earnings**

Brazilian Law and the Company's by-laws require that certain appropriations be made from retained earnings to reserve accounts annually. The purpose and basis of appropriation to such reserves are as follows:

- Legal reserve

This reserve is a requirement for all Brazilian corporations and represents the annual appropriation of 5% of net income as stated in the statutory accounting records up to a limit of 20% of capital stock. The reserve may be used to increase capital or to compensate for losses, but may not be distributed as cash dividends.

- Undistributed earnings reserve

This reserve is established in accordance with Article 196 of Law No. 6,404/76 to fund the Company's annual investment program. The appropriation of income for the year ended December 31, 2004 included a retention of earnings in the amount of US\$4,396, of which US\$4,392 related to net income for the year and US\$4 to the remaining balance of retained earnings, approved by the General Shareholders' Meeting held on March 31, 2005. This proposal was intended to cover partially the annual investment program established in the capital budget for 2005.

The destination of net income for the year ended December 31, 2005 included retention of profits of US\$6,453, with a US\$6,449 amount, arising from net income for the year, and the US\$4 retaining earnings remaining balance. This retention was intended to cover partially the annual investment program established in the 2006 capital budget, ad referendum of the General Shareholders' Meeting of April 3, 2006.

The destination of net income for the year ended December 31, 2006 includes retention of profits of US\$8,004 with a US\$7,775 amount, arising from net income for the year, and the US\$229 retaining earnings remaining balance. This proposal is intended cover to partially meet the annual investment program established in the 2007 capital budget, ad referendum of the General Shareholders' Meeting of April 2, 2007.

**17. Shareholders Equity** (Continued)**(e) Appropriated retained earnings** (Continued)

- Statutory reserve

This reserve is provided through an amount equivalent to a minimum of 0.5% of subscribed and fully paid in capital at year-end. The reserve is used to fund the costs incurred with research and technological development programs. The accumulated balance of this reserve cannot exceed 5% of the capital stock, according to Article 55 of the Company's by-laws.

**18. Domestic and International Acquisitions****(a) Acquisition of Pasadena Refinery**

On September 1, 2006, the Company, through its wholly owned subsidiary Petrobras America Inc., concluded the acquisition of 50% of the shares of Pasadena Refinery System, Inc., a US based refining and trading company owned by the Belgian group Compagnie Nationale a Portefeuille SA - CNP. The purchase price was of approximately US\$416 and was based on economic valuation model of expected future earnings of the refinery. Due to immateriality, proforma information has not been presented.

The acquisition was consumated principally to expand Petrobras' international activities according to the Strategic Plan.

The current capacity of the Pasadena Refinery is of about 100,000 bpd. The Company and the other partner are already conducting studies to expand its capacity and install units that will enable it to process heavy oils, including Petrobras' Marlim production, and deliver high quality products.

With Petrobras entering as a partner in the enterprise, the refinery will be modified in order to process approximately additional 70,000 bbl/day of heavy oil and other batches, including production in the Marlim field. The refinery's operational modernization process should be completed in four years and all of the byproducts to be produced will comply with the highest standards of quality adopted in the United States.

**18. Domestic and International Acquisitions (Continued)****(b) Acquisition of Liquigás Distribuidora S.A.**

On August 9, 2004, the Company's subsidiary, Petrobras Distribuidora S.A. - BR, acquired from ENI B.V. 100% of the capital of its Brazilian subsidiary Liquigás Distribuidora S.A. (former Sophia do Brasil S.A. and Agip do Brasil S.A.), assuming its control from that date.

The purchase price paid for Liquigás Distribuidora S.A. was based on an economic valuation model of expected future earnings of Liquigás Distribuidora S.A., which considered relevant factors, including the potential effects of the economic situation of Brazil. The acquisition of Liquigás Distribuidora S.A. totaled US\$511. The Company paid US\$225 in cash, and settled a debt of US\$225 that the former Agip do Brasil had with ENI BV. An additional amount of US\$61 related to subsequent purchase price adjustments was paid on December 10, 2004.

The acquisition of Liquigás Distribuidora S.A. was recorded using the purchase method of accounting and the financial statements of Liquigás Distribuidora S.A. were included in the consolidated Petrobras financial statements, beginning in August of 2004. The purchase price allocation was based on the fair market value.

Liquigás Distribuidora S.A. is a liquefied petroleum gas (LPG), fuel and lubricant distributor, and has 21.5% share in the LPG market in Brazil, 3.8% of total fuel distribution domestic market with a network of more than 1,500 service stations and 3% share in the Brazilian lubricant distribution market.

The acquisition of Liquigás Distribuidora S.A. contributes toward achieving the objectives established in Petrobras' Strategic Planning for its subsidiary BR of expanding its share in the LPG distribution segment, and also of consolidating its penetration in the automotive fuel distribution market in certain regions of the country.

**18. Domestic and International Acquisitions** (Continued)**(b) Acquisition of Liquigás Distribuidora S.A.** (Continued)

The following unaudited pro forma summary financial information presents the consolidated results of operations as if the acquisition of Liquigás Distribuidora S.A. had occurred at the beginning of the years presented.

	<b>2004</b>	
	<b>As reported</b>	<b>Pro-forma (unaudited)</b>
Net operating revenues	38,428	39,529
Cost of Sales	(21,279)	(22,222)
Net income for the period	6,190	6,182
Basic and diluted earnings per common and preferred share (*)	1.41	1.41
Basic and diluted earnings per ADS (*)	5.64	5.64

(\*) Considers effect of 4 for 1 stock split that occurred on September 1, 2005.

**(c) Acquisition of Triunfo's shares by PETROQUISA**

The Company's subsidiary, Petrobras Química S.A. PETROQUISA decided to exercise its preemptive right in the acquisition of shares held by PRIMERA Indústria e Comércio Ltda. in the capital of Petroquímica Triunfo S.A. (Triunfo) in response to the put option.

After exercise of its preemptive right on May 14, 2004, PETROQUISA, which had previously held 45.22% of voting capital and 59.92% of capital stock of Petroquímica Triunfo increased its interest to 70.45% of voting capital and 85.04% of its capital stock. The results of Triunfo have been included to the Petrobras Consolidated Financial Statements since May of 2004. Due to immateriality, the Company has not prepared pro forma information respective to this business combination.

The acquisition was consummated principally to expand Petrobras' petrochemical activities according to the Strategic Plan approved in May 14, 2004.

The Company paid US\$32 (R\$101 million) in cash and this purchase price was based on an economic valuation model of expected future earnings of Petroquímica Triunfo S.A.

Petroquímica Triunfo S.A. produces low-density polyethylene and has an installed capacity of 160,000 tons per year. Triunfo's activities are exclusively in Brazil.



**18. Domestic and International Acquisitions (Continued)****(d) Acquisition of FAFEN Energia S.A.**

On December 27, 2004, Petrobras approved the acquisition of the remaining 80% interest in the FAFEN Energia S.A. thermoelectric power plant, thus bringing its ownership interest to 100%. Petrobras will pay EDP Brasil S.A. US\$36 for the acquisition, payable as follows: 50% - 30 days after the closing of the operation, 25% one year thereafter and the remaining 25% - two years thereafter. This thermoelectric power plant has an installed capacity of 133 MW for electricity generation and 42 ton/hour for steam generation and is located in the State of Bahia.

The acquisition of FAFEN was recorded using the purchase method of accounting and the assets and liabilities were included in the consolidated Petrobras financial statements as of December 31, 2004. Results of operations were included in the consolidated Petrobras financial statements beginning on January 2005.

The purchase price for FAFEN was allocated based on the fair market value of the assets acquired and the liabilities assumed as of the acquisition date as determined by independent appraisers. Due to immateriality, the Company has not prepared pro-forma information respective to this business combination.

**(e) Acquisition of Baixada Santista Energia Ltda. - BSE**

On March 9, 2005, Petrobras approved the conditions agreed with Marubeni Corporation, for the purchase of quotas held by Marubeni Corporation in Baixada Santista Energia Ltda. BSE, a special purpose company incorporated within the UTE Cubatão Project. This operation involves approximately US\$90, and project resumption will meet the present requirements for the energy and steam power generation system renewal for the Cubatão Refinery (RPBC). Upon conclusion, this plant will have an installed capacity of 200 MW for electricity generation and 400 ton/hours for steam generation.

The Thermoelectric Plant of Cubatão is expected to start operating in October 2007 and will supply 47 MW and 415 t/h of steam to Refinaria Presidente Bernardes in Cubatão (RPBC), belonging to Petrobras. Electricity surplus will be made available to the market. Due to immateriality, the Company has not prepared pro forma information respective to this business combination.

**18. Domestic and International Acquisitions** (Continued)**(f) Acquisition of new businesses in Colombia, Paraguay and Uruguay**

In December 2005, Petrobras signed three Share Purchase Agreements for the acquisition of fuel businesses (retail and trade markets) in Colombia and of total operations conducted by Shell in Paraguay and Uruguay.

In March 2006, Petrobras, through its controlled company Petrobras International Braspetro B.V., acquired the business of commercialization and distribution of Shell in Paraguay, related to fuel operations (retail and commercial market), including gas stations with convenience stores in all Paraguayan territory; LPG commercialization assets; installations for commercialization of aviation products for the airports in Asunción and Cidade Del Este.

On April 28, 2006 Petrobras concluded the purchase of the assets of Shell in Colombia, relating to the fuel distribution and commercialization. The acquisition comprises 39 service stations and convenience shops in Bogotá and surrounding areas, storage base and lubricant mixing plant in Puente Aranda, and one terminal in Santa Marta.

In June 2006, Petrobras acquired, via its subsidiary Petrobras International Braspetro B.V. - PIB BV, Shell's assets in Uruguay relating to the distribution and sale of fuel throughout Uruguay.

The Company paid US\$116 for these acquisitions that are part of a package involving the assets of Shell in Colombia, in Paraguay and in Uruguay.

Due to immateriality, the Company has not prepared pro-forma information respective to this business combination.

**(g) Acquisition of a 49% interest in TERMOBAHIA**

The Special Purpose Company (SPC) BLADE Securities Ltd ( BLADE ), was created by the Deutsche Bank (DB), in order to support Petrobras in its transactions related to the acquisition of a 49% interest held by ABB-EV in TERMOBAHIA power plant. (See note 14).

**18. Domestic and International Acquisitions (Continued)**

**(g) Acquisition of a 49% interest in TERMOBAHIA (Continued)**

On December 28, 2005, Petrobras exercised its preemptive right and concluded the acquisition of a 49% interest held by ABB-EV in TERMOBAHIA, comprising shares and amounts receivable in the total amount of US\$45, under a financial structuring agreed upon with the IDB.

This financial structuring involves two simultaneous operations: the acquisition of ABB-EV's rights and the sale of such rights to a private institution until a strategic partner is introduced by Petrobras within a maximum period of one year. The Company's previous investment on TERMOBAHIA was being accounted for in accordance to FIN 46 ( R ).

On August 10, 2006, Petrobras concluded the acquisition of the equity interest and the credits relating to the Subordinated Loan of EIC Electricity S.A. in TERMOBAHIA for the amount of US\$2, raising its interest to 31%.

At the conclusion of this operation, the equity interests in TERMOBAHIA's were held as follows: Petrobras 31%, PETROS 20% and BLADE 49%.

Due to the immateriality, proforma information has not been presented (see Note 14 discussion regarding Blade).

**(h) Agreement for sale and association with Teikoku Oil Co. Ltd. in operations in Ecuador**

On January 11, 2007 the Ministry of Energy and Mines of Ecuador approved the agreement between Petrobras Energia S.A., PESA and Teikoku for sale of 40% of the rights and obligations in the participation contracts in Blocks 18 and 31 in Ecuador. The Company does not expect to have a material impact on its Financial Statements as a result of this agreement.

**18. Domestic and International Acquisitions (Continued)****(i) Eletrobolt**

On August 13, 2004, the Board of Directors of Petrobras approved the financial conditions for the acquisition of 100% interest of Eletrobolt Thermoelectric plant from Sociedade Fluminense de Energia, with a share purchase price of US\$65. The Company's previous variable interest in Eletrobolt was being accounted for in accordance with FIN 46(R) and the 2004 share acquisition was accounted for as a business combination but had no material impact on Petrobras consolidated accounting records. Due to immateriality, proforma information has not been presented.

**(j) Termorio**

In February, 2005, in order to facilitate the financial restructuring process of Termorio, Petrobras acquired the remaining 50% interest of Termorio's voting capital from NRG for US\$83 bringing its ownership to 100% of total and voting capital. The Company's previous variable interest in Termorio was being accounted for in accordance with FIN 46(R) and the 2005 share acquisition was accounted for as a business combination but had no material impact on Petrobras consolidated accounting records. Due to immateriality, proforma information has not been presented.

**(k) Termoceará**

On June 24, 2005, Petrobras acquired Termoceará Ltda., a plant with net generation capacity of 220 MW/h. The acquisition price was equal to US\$137, of which US\$81 related to the purchase of tangible assets of the thermoelectric plant and US\$56 was designated to settle payables to the lenders of the project (BNDES and Eximbank). The excess of amounts paid over fair value of assets acquired is attributable to intangible assets and goodwill.

The Company's previous variable interest in Termoceará was being accounted for in accordance with FIN 46(R) and the 2005 share acquisition was accounted for as a business combination but had no material impact on Petrobras consolidated accounting records. Due to immateriality, proforma information has not been presented.

**18. Domestic and International Acquisitions (Continued)****(I) TermoMacaé Ltda. and TermoMacaé Comercializadora de Energia Ltda. (former Macaé Merchant)**

In February 2005, the arbitration proceedings began related to the dispute between Petrobras and El Paso arising from the economic and financial imbalance deemed to exist relative to the construction and operation of the Macaé Merchant Thermoelectric Plant. Petrobras claims such contract to be invalid and require renegotiation as a result of changed economics. Related to the disputes, Petrobras made a court ordered bank deposit related to unpaid contingency the amounts, while awaiting final decision of the Arbitration proceedings.

In March 2006 Petrobras and El Paso agreed to settle certain disputes involving the Macaé Merchant Consortium. Under this settlement, the capital participation contract was terminated and El Paso finalized the sale of the plant to Petrobras, which in April 2006 paid US\$357 to acquire the companies TermoMacaé Ltda (f.k.a. El Paso Rio Claro Ltda.) and TermoMacaé Comercializadora de Energia Ltda. (f.k.a. El Paso Rio Grande Ltda.), terminating the Macaé Merchant Consortium Contract and thereby settling the controversies.

Under the acquisition process, El Paso gave guarantees to Petrobras relating to certain liabilities, limited to US\$120, including approximately US\$78, referring to a federal tax assessment, which El Paso believes it has excellent chances of successfully contesting, and for which it has presented its defense to the Brazilian tax authorities. In respect of the acquisition of the assets, any successes involving given tax benefits, tax receivables and potential recoveries on financial revenues shall be prorated between Petrobras and El Paso as mutually agreed.

On July 05, 2006 Petrobras was reimbursed for the amounts deposited by virtue of the preliminary decision pronounced by the Arbitral Tribunal, to the amount of US\$259, including financial yields, given the dismissal of the Arbitration Proceeding.

The Company's previous variable interest in TermoMacaé was being accounted for in accordance with FIN 46(R) and the 2006 share acquisition was accounted for as a business combination but had no material impact on Petrobras consolidated accounting records. Due to immateriality, proforma information has not been presented.

**18. Domestic and International Acquisitions (Continued)****(m) Acquisition of shares in Gaseba Uruguai S.A.**

In November 2005, the Board of Directors of Petrobras approved the acquisition of 51% of the capital of Gaseba Uruguay - Grupo Gaz de France S.A. (Gaseba), a natural gas distribution concession company in Montevideo, Uruguay from GDF International.

In June 2006, Petrobras acquired 66% of the shares in Gaseba. The share acquisition took place over two stages: 51% of the shares held by Grupo Gaz de France were acquired on June 2, 2006 and 15% of the shares held by Acodike Supergas S.A. were acquired on June 29, 2006. The acquisition price was equal to US\$14 and due to immateriality, proforma information has not been presented.

**19. Commitments and Contingencies**

Petrobras is subject to a number of commitments and contingencies arising in the normal course of its business. Additionally, the operations and earnings of the Company have been, and may be in the future, affected from time to time in varying degrees by political developments and laws and regulations, such as the Federal Government's continuing role as the controlling shareholder of the Company, the status of the Brazilian economy, forced divestiture of assets, tax increases and retroactive tax claims, and environmental regulations. The likelihood of such occurrences and their overall effect upon the Company are not predictable.

The Company currently has several contracts to purchase crude oil, diesel fuel and other oil products, which require the Company to purchase a minimum of approximately 129,925 barrels per day at respective current market prices.

Petrobras provided guarantees to the ANP for the minimum exploration program defined in the concession contracts for exploration areas, totaling US\$2,425 (US\$2,244 in 2005). Out of this total, US\$1,137 (US\$1,875 in 2005) represents a pledge on the oil to be extracted from previously identified fields already in production, for areas in which the Company had already made commercial discoveries or investments. For areas whose concessions were obtained by bidding from the ANP, Petrobras has given bank guarantees totaling US\$372 through December 31, 2006 (US\$369 in 2005).

**19. Commitments and Contingencies (Continued)**

In 1993, the Company signed a long-term contract to buy gas ( The Gas Supply Agreement or "GSA") with Yacimientos Petrolíferos Fiscales Bolivianos, the Bolivian state oil company for the purchase of natural gas. Under this contract, with maturity in 2019, the Company is required to purchase 80% of the natural gas transported through the Bolivia/Brazil natural gas pipeline over a 20 year term at contract prices ranging from US\$1.07 per MMBTU to US\$1.17 MMBTU, based upon throughput. The pipeline achieved an average throughput of 24.4 million cubic meters per day during 2006.

The Company has exclusive supply contracts with certain service stations. These contracts are typically for seven years and require the Company to sell product at market prices.

**(a) Litigation**

The Company is a defendant in numerous legal actions involving civil, tax, labor, corporate and environment issues arising in the normal course of its business. Based on the advice of its internal legal counsel and management's best judgment, the Company has recorded accruals in amounts sufficient to provide for losses that are considered probable and reasonably estimable. At December 31, 2006 and 2005, the respective amounts accrued by type of claims are as follows:

	<b>As of December 31,</b>	
	<b>2006</b>	<b>2005</b>
Labor claims	<b>38</b>	7
Tax claims	<b>47</b>	87
Civil claims	<b>97</b>	79
Commercials claims and other contingencies	<b>51</b>	62
	<b>233</b>	235
Contingencies for joint liability	-	75
Total	<b>233</b>	310
Current contingencies	<b>(25)</b>	(72)
Long-term contingencies	<b>208</b>	238

**19. Commitments and Contingencies (Continued)****(a) Litigation (Continued)**

As of December 31, 2006 and 2005, in accordance with Brazilian law, the Company had paid US\$816 and US\$775, respectively, into federal depositories to provide collateral for these and other claims until they are settled. These amounts are reflected in the balance sheet as restricted deposits for legal proceedings and guarantees.

The Company is a party to several contracts related to the acquisition and upgrade of production Platform P-36, which was lost in its entirety in 2001. Pursuant to those contracts, the Company had an obligation to pay the insurance proceeds to a Security Agent for distribution according to specified clauses established in the contracts. The Company contends that it is entitled to the insurance proceeds under the contractual arrangements, and other parties contend that they are also entitled to such proceeds. The issue is subject to international proceedings in a British court. Pending determination of the issue by the international court, the Company committed to deposit cash collateral in the amount of US\$175, in order to facilitate the issuance of a guarantee by a Security Agent, for the payment of creditors. At December 31, 2006, this amount was included in the balance sheet as restricted deposits for legal proceedings and guarantees.

**Plaintiff: Kallium Mineração S.A.**

On May 28, 1981, Kallium Mineração S.A. brought an action against Petromisa, a former subsidiary of Petrobras, in the Federal Court of the State of Rio de Janeiro alleging damages of approximately US\$450 relating to the rescission of a contract to develop a potassium salt mine. On August 10, 1999, a decision was handed down that considered most of the plaintiff's petitions to be without grounds (losses, damages and loss of profit), requiring only the Company to reimburse all expenses incurred as a result of the prospecting research carried out, in accordance with amounts to be calculated in the final award. No award for loss of profit was established in the decision. In September of 1999 both parties filed appeals with the appeals court in the state of Rio de Janeiro. Granted by the lower court, both parties filed appeals, which were rejected. Petrobras is awaiting judgment of the Extraordinary Appeal filed before the STF and the special appeal on December 18, 2003. A special appeal brought by Kallium is also pending judgment. Based on the opinion of its legal advisers, management does not expect an unfavorable outcome in this case and considers the risk of loss with respect to this lawsuit to be possible.



**19. Commitments and Contingencies (Continued)****(a) Litigation (Continued)****Plaintiff: PORTO SEGURO IMÓVEIS LTDA.**

On November 23, 1992, PORTO SEGURO IMÓVEIS LTDA., a minority shareholder of PETROQUISA, filed a suit against Petrobras in the State Court of Rio de Janeiro related to alleged losses resulting from the sale of a minority holding by PETROQUISA in various petrochemical companies included in the National Privatization Program introduced by Law No. 8,031/90.

In this suit, the plaintiff claims that Petrobras, as the majority shareholder in PETROQUISA, should be obliged to reinstate the loss caused to the net worth of PETROQUISA, as a result of the acts that approved the minimum sale price of its holding in the capital of privatized companies. A decision was handed down on January 14, 1997 that considered Petrobras liable with respect to PETROQUISA for losses and damages in an amount equivalent to US\$3,406.

In addition to this amount, Petrobras was required to pay the plaintiff 5% of the value of the compensation as a premium (see art. 246, paragraph 2 of Law No. 6,404/76), in addition to attorneys' fees of approximately 20% of the same amount. However, since the award would be payable to PETROQUISA and Petrobras holds 99.0% of its capital, the effective disbursement if the ruling is not reversed will be restricted to 25% of the total award. Petrobras filed an appeal with the State Court of Rio de Janeiro, and received a favorable decision from the Third Civil Court on February 11, 2003, which, by a majority vote, accepted Petrobras' appeal to reverse the judgment and ruled the plaintiff's case to be without grounds, the revising judge's decision that held the case to be partially with grounds to reduce the amount of compensation to US\$1,538 being overruled. Against this decision, Porto Seguro filed another appeal (motion to reverse or annul) with the State Court of Rio de Janeiro, and the Fourth Civil Court handed down a unanimous decision on March 30, 2004 requiring Petrobras to indemnify PETROQUISA and Porto Seguro the amounts of US\$2,359 and US\$590 respectively (the latter representing 5% in premium and 20% in attorney's fees). Due to this result, Petrobras lodged appeal with high and supreme courts, which was dismissed. In view of this decision, interlocutory appeal was filed with High Court - STJ and Supreme Court - STF, which was converted into Special Appeal by STJ.

**19. Commitments and Contingencies** (Continued)**(a) Litigation** (Continued)**Plaintiff: PORTO SEGURO IMÓVEIS LTDA.** (Continued)

On May 6, 2005, the Superior Court of Justice (STJ) accepted the interlocutory appeal and determined that the special appeal was to be proceeded with. Porto Seguro lodged an appeal against the interlocutory decision, which was accepted by a majority vote on December 15, 2005, and suspension of the special appeal filed by Petrobras was reinstated. The Company filed an Interlocutory appeal against this latest decision, which was ruled on April 4, 2006 and which unanimously overturned a decision which restored the impediment on the Special Appeal brought by Petrobras, due to an impediment on one of the justices, determining another decision be pronounced. Special Appeal by PORTO SEGURO rejected under a judgment delivered on September 05, 2006. In performance of the decision published on June 05, 2006, we are now awaiting assignment of the agenda to reexamine the matter relating to the blocking of Petrobras' Special Appeal. If the award is not reversed, the indemnity estimated to PETROQUISA, including monetary correction and interest, would be US\$4,612. As Petrobras owns 100% of PETROQUISA's share capital, a portion of the indemnity estimated at US\$3,044, will not represent a disbursement from Petrobras' Group. In case of loss, Petrobras would have to pay US\$201 to Porto Seguro and US\$922 to Lobo & Ideas by means of attorney's fees, however based on the opinion of its legal advisers, the Company does not expect to obtain an unfavorable ruling in this case and considers the risk of loss with respect to this lawsuit to be possible.

**19. Commitments and Contingencies (Continued)****(a) Litigation (Continued)****Plaintiff: The Fisherman s Federation of the State of Rio de Janeiro (FEPERJ)**

The Fisherman s Federation of the State of Rio de Janeiro (FEPERJ) filed a civil suit against the Company with the Rio de Janeiro State Court for compensation of miscellaneous damages amounting to US\$224, which it is claiming in the name of its members, as a result of the oil spill in Guanabara Bay on January 18, 2000. At that time, Petrobras paid out extrajudicial indemnification to everyone who proved to be fishermen when the accident occurred. According to the records of the national fishermen s register, only 3.339 could claim indemnification. A decision was handed down on February 7, 2002 which ruled the claim partially without grounds, rejecting pain and suffering, and requiring the Company to pay compensation for material damages and loss of profit to be calculated at the award phase. The ruling expressly declares that it is not reasonable to consider an award based on the amount claimed, since it was without economic base. On February 02, 2007 a decision, partly accepting the expert report, was published. That expert report was prepared to establish the parameters for calculating the award, which amounts to US\$516 at that date. Petrobras will appeal before Rio de Janeiro s Supreme Court, because the parameters set in the decision differs from those already defined by that same court. In accordance with the Company s expert assistant calculation, the recorded amount of US\$12 represents the award that will be set by the court at the end of the process. Based on its legal counsels opinion, the Company s Administration believes it is possible that the Company will not prevail in this case.

**Plaintiff: São Paulo State tax authorities**

The São Paulo tax authorities filed a tax suit against the Company, to demand payment of ICMS on naphta-petrochemical operations carried out in the state for the period from September 1984 to February 1989. The suit was tried at all levels and the legal system eventually opposed the argument defended by the Company, having understood that, in the specific case of these operations, ICMS would apply.

The case was settled and the Company entered into an agreement to pay US\$122 plus interest, totaling US\$151, in 60 equal successive installments beginning April 2005.

**19. Commitments and Contingencies** (Continued)**(a) Litigation** (Continued)**Plaintiff: São Paulo State tax authorities** (Continued)

Taking advantage of the tax benefits awarded by Law 12.399/06, in November 2006 the Company settled the debt in advance by paying the amount of US\$53, reducing the fine amount by 80% and the interest amount by 50%, generating a real saving of US\$101.

**Plaintiff: Unions of Petroleum Workers**

Petrobras is a defendant in three labor claims filed by the UNIONS OF PETROLEUM WORKERS of three federal states (Rio de Janeiro, São Paulo and Sergipe), alleging that official inflation rates for 1987, 1989 and 1990 (understatement of the official inflation rate - Bresser, Summer and Collor Plans) were not fully included in the workers' salaries.

The suits are in different procedural phases, as described below:

UNIONS OF PETROLEUM WORKERS of federal state of Sergipe (SINDIPETRO/SE): Case ruled to have grounds. Process on enforcement phase. The judge granted decision determining SINDIPETRO/SE to present new calculations, which is pending. This is awaited. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$47 calculations, which is pending. Based on the opinion of its legal advisers, the Company considers the risk of loss with respect to this lawsuit to be possible.

UNIONS OF PETROLEUM WORKERS of federal state of Rio de Janeiro (SINDIPETRO/RJ): Petrobras understands there is no debt, since corresponding amounts were paid by the clause of the collective bargain in 1993. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$86. Based on the opinion of its legal advisers, the Company considers the risk of loss with respect to this lawsuit to be remote.

**19. Commitments and Contingencies (Continued)****(a) Litigation (Continued)****Plaintiff: Unions of Petroleum Workers (Continued)**

UNIONS OF PETROLEUM WORKERS of federal state of São Paulo (SINDIPETRO/SP): Case ruled to have grounds, with final and unappealable decision delivered. Petrobras filed Termination Action - denied. Appeal by Petrobras was accepted and decision granted suspending agreement and issuing new decision to deny plaintiff's request on Labor Claim. Extraordinary Appeal filed by SINDIPETRO, which was denied entertainment, and is now pending judgment on the Interlocutory Appeal subsequently filed.

The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$45. Based on the opinion of its legal advisers, the Company considers the risk of loss with respect to this lawsuit to be remote.

Based on previous favorable ruling on similar cases and TST abridgment of law, Company management does not expect an unfavorable outcome on the cases. Petrobras contested the expert report determining the amount of indemnification, which is pending judgment. Management assesses risk of loss to be possible.

**Plaintiff: Adailton de Oliveira Bittencourt and Others**

Adailton de Oliveira Bittencourt and Others, filed Labor claims for payment of break and lunch hour, after introduction of 6 working hours per day by 1988 Brazilian Constitution. Period claimed: September 28, 1989 to November 30, 1992 due to the introduction of a six-hour working day by the 1988 Federal Constitution. Denied in first instance. Appeal granted by the Regional Labor Tribunal (TRT). Petrobras filed appeal for clarification of decision, denied on September 25, 2002 and October 24, 2002 respectively. A Motion for Clarification was lastly filed on October 15, 2004 to obtain further clarification without changing the ruling. Final and unappealable decision pronounced. The case is currently at the award calculation stage, at which the amounts due to the plaintiffs are determined. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$3. Based on the opinion of its legal advisers, the Company considers the risk of loss with respect to this lawsuit to be possible.

**19. Commitments and Contingencies (Continued)****(a) Litigation (Continued)****Plaintiff: Distribution Companies**

The Company was sued in court by certain small oil distribution companies under the allegation that it does not pass on to state governments the State Value-Added Tax (ICMS) collected according to the legislation upon fuel sales. These suits were filed in the states of Goiás, Tocantins, Bahia, Pará, Maranhão and in the Federal District.

Of the total amount related to legal actions of approximately US\$419, up to December 31, 2006 some US\$38 (US\$34 in 2005) had been withdrawn from the Company's accounts as a result of judicial rulings of advance relief, which were annulled as a result of an appeal filed by the Company.

The Company, with the support of the state and federal authorities, has succeeded in stopping the execution of other withdrawals, and is making all possible efforts to obtain reimbursement of the amounts that were previously withdrawn from its accounts.

**(b) Notification from the INSS - joint liability**

The Company received various tax assessments related to social security amounts payable as a result of irregularities in presentation of documentation required by the INSS, to eliminate its joint liability in contracting civil construction and other services, stipulated in paragraphs 5 and 6 of article 219 and paragraphs 2 and 3 of article 220 of Decree No. 3,048/99.

In order to guarantee the appeals' filing and/or the obtainment from INSS of Debt Clearance Certificate, US\$55 from the amounts disbursed by the Company is recorded as sheet as restricted deposits for legal proceedings and guarantees and may be recovered under the respective proceedings in progress, which are related to 343 assessments amounting to US\$178. Petrobras' legal department expects a possible defeat regarding these assessments, as it considers the risk of future disbursement to be possible.

Petrobras had disbursed during 2006 US\$35 (US\$85 in 2005), referring to administrative suits filed by the INSS claiming the Company's joint liability.

**19. Commitments and Contingencies (Continued)****(b) Notification from the INSS - joint liability (Continued)**

Internally, procedures were revised to improve the inspection of contracts and require the presentation of documents, as stipulated in the legislation, to substantiate the payment of INSS amounts due by contractors. Petrobras continues to analyze each tax assessment received in order to recover amounts, as permitted through administrative processes of the INSS.

**(c) Tax assessments****Plaintiff: Internal Revenue Service of Rio de Janeiro Withholding Tax related to charter of vessels**

The Internal Revenue Service of Rio de Janeiro filed two Tax Assessments against the Company in connection with Withholding Tax (IRRF) on foreign remittances of payments related to charter of vessels of movable platform types for the years 1998 through 2002.

The Internal Revenue Service, based on Law No. 9,537/97, Article 2, considers that drilling and production platforms cannot be classified as sea-going vessels and therefore should not be chartered but leased. Based on this interpretation, overseas remittances for servicing chartering agreements would be subject to withholding tax at the rate of 15% or 25%.

The Company disagrees with the Internal Revenue Service's interpretation as to charter contracts, given that the Federal Supreme Court has already ruled that, in the context of its judgment with respect to the IPI (Federal VAT) tax, offshore platforms are to be classified as sea-going vessels. Additionally, the 1994 and 1999 Income Tax Regulations support the non-taxation (RIR/1994) and the zero tax rate (RIR/1999) for the remittances in question.

On June 27, 2003, the Internal Revenue Service served a tax assessment notice on the Company amounting to R\$3,064 million (US\$1,066) covering the period from 1999 to 2002. Using the same arguments, on February 17, 2003, another tax assessment notice had already been issued for R\$93 million (US\$32) with respect to 1998, against which, on March 20, 2003, the Company filed an appeal. According to the fiscal authorities, the Company should have withheld that tax, incident on remittances made to abroad for payment of the hiring of vessels of the mobile platform type, used in oil exploration and production.

**19. Commitments and Contingencies (Continued)****(c) Tax assessments (Continued)****Plaintiff: Internal Revenue Service of Rio de Janeiro Withholding Tax related to charter of vessels (Continued)**

Petrobras has defended itself against these tax assessments. Administrative appeals were lodged with High Court of Appeals for Fiscal Matters, last administrative level, which still await trial. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 for the period 1998 is US\$55 and for the period 1999 to 2002 is US\$1,831. Based on its legal counsels advice, the Company has assessed risk of loss to be possible.

**Plaintiff: Federal finance authorities State Value-Added Tax related to the Sinking of P-36 Platform**

Rio de Janeiro state finance authorities filed a Tax Assessment against the Company in connection with State Value-Added Tax (ICMS) related to the Sinking of P-36 Platform. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$253 Petrobras filed a Voluntary Appeal, pending examination. To allow the appeal to proceed an amount of US\$20 was deposited and a bank guarantee to the amount of US\$31 taken out, which corresponds to 30% of the total amount. The voluntary appeal was accepted. However, the assessment was upheld under the Special Appeal brought by the State Treasury. On October 02, 2006, the appeal deposit and bank guarantee were converted into income for the state. The matter was then referred to the courts. The remaining amount deriving from the tax credit, duly restated, relating to the final quarter of 2006 is around US\$149, which corresponds to 70% of the total claim. As the administrative proceedings have reached a conclusion and the amount will be recorded as an overdue federal liability, 20% will be added as attorneys fees. Based on its legal counsels advice, the Company has assessed risk of loss to be possible.



**19. Commitments and Contingencies** (Continued)**(c) Tax assessments** (Continued)**Plaintiff: Rio de Janeiro state finance authorities II and IPI Tax related to the Sinking of P-36 Platform**  
(Continued)

Rio de Janeiro state finance authorities filed a Tax Assessment against the Company in connection with II (Import Tax) and IPI (Federal VAT) related to the Sinking of P-36 Platform. Trial court ruling against Petrobras. An appeal was lodged, which is pending judgment. Petrobras filed for a writ of mandamus and obtained an injunction that barred tax collection. Pending special appeal filed by the Federal Reserve/National Finance Secretary. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$203. Due to the favorable decision the Company obtained under the Writ of Mandamus, the administrative proceeding has been stayed, meaning the parties have not had the chance to submit the Voluntary Appeal. Based on its legal counsels advice, the Company has assessed risk of loss to be possible.

**Plaintiff: Rio de Janeiro state finance authorities II and IPI Tax related to TERMORIO equipments**

Rio de Janeiro state finance authorities filed a Tax Assessment against the Company in connection with II (Import Tax) and IPI (Federal VAT) contesting the tax classification as Other Electricity Generation Groups for the import of the equipment belonging to the thermoelectric power station TERMORIO S.A. On August 15, 2006, TERMORIO submitted a contestation of the tax assessment to the Federal Revenue Department.

On September 15, 2006, the case was referred to the Federal Revenue Service in Florianópolis, where it is still being examined under administrative proceedings. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$227. Based on its legal counsels advice, the Company has assessed risk of loss to be possible.

**19. Commitments and Contingencies (Continued)****(c) Tax assessments (Continued)****Plaintiff: Internal Revenue Services**

Internal Revenue Services denied PASEP base reduction. Internal Revenue Services Appeal denied in 2nd instance and voluntary appeal of Petrobras accepted. Pending special appeal filed by the Internal Revenue Services. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$13. Based on its legal counsels advice, the Company has assessed risk of loss to be possible.

**Plaintiff Alagoas state finance authorities**

Alagoas state finance authorities filed a Tax Assessment against the Company in connection with reversal of ICMS Credit. Petrobras is awaiting judgment of the appeal by the second administrative level. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$32. Based on its legal counsels advice, the Company has assessed risk of loss to be possible.

**(d) Environmental matters**

The Company is subject to various environmental laws and regulations. These laws regulate the discharge of oil, gas or other materials into the environment and may require the Company to remove or mitigate the environmental effects of the disposal or release of such materials at various sites.

The Company's management considers that any expenses incurred to correct or mitigate possible environmental impacts should not have a significant effect on operations or cash flows.

**PEGASO - (Programa de Excelência em Gestão Ambiental e Segurança Operacional).**

During 2000 the Company implemented an environmental excellence and operational safety program - PEGASO - (Programa de Excelência em Gestão Ambiental e Segurança Operacional). The Company made expenditures of approximately US\$4,081 from 2000 to December 31, 2006 under this program. During the years ended December 31, 2006 and 2005 the Company made expenditures of approximately US\$562 and US\$545 respectively. The Company believes that future payments related to environmental clean-up activities resulting from these incidents, if any, will not be material.

**19. Commitments and Contingencies** (Continued)**(d) Environmental matters** (Continued)**Guanabara Bay pipeline rupture**

On January 18, 2000, a pipeline from one of the Company's terminals to a refinery in the Guanabara Bay ruptured, causing a release of crude oil into the bay. On January 19, 2001, the Rio de Janeiro State Prosecutor filed a criminal lawsuit against the Company. The Company is contesting the legal basis for the criminal lawsuit. Additionally, the Federal Prosecutor has filed criminal lawsuits against the former president of the Company (that finished) and 9 other employees. The Company cannot predict if the outcome of these proceedings will have a material adverse effect on the financial condition, results of operations or cash flows of the Company.

The local federal tribunal dismissed the complaint against the Company's former president, and this dismissal is not subject to appeal.

On April 30, 2002, the judge determined that the Company could not appear as a defendant in this criminal proceeding as a result of an injunction the Company obtained from the court, although the decision is still subject to appeal.

On October of 2003 the judge determined that in regard to one of the employees the suit will be suspended for the period of 2 years, under certain conditions that defendant will have to observe.

In addition, as a result of the spill, on January 27, 2000, the National Council for the Environment enacted a resolution that obligated the IBAMA (Brazilian Institute for the Environment and Renewable Resources), state environmental agencies and local environmental agencies and non-governmental agencies to evaluate the control and prevention measures and environmental licensing status of all industrial facilities for the production of oil and oil products in Brazil. This resolution also mandated that the Company perform an independent environmental audit of all of its industrial installations located in the State of Rio de Janeiro.

Since 2000, the Company implemented independent environmental audits in all of the Company's plants located in Brazil that was concluded during December of 2003. The Company implemented almost all of the auditors recommendations.

**19. Commitments and Contingencies (Continued)****(d) Environmental matters (Continued)****Presidente Getúlio Vargas refinery oil spill**

On July 16, 2000, an oil spill occurred at the Presidente Getúlio Vargas refinery releasing crude oil in the surrounding area. The Federal and State of Paraná Prosecutors have filed a civil lawsuit against the Company seeking US\$1,176 in damages, which have already been contested by the Company. Additionally, there are two other actions pending, one by the Instituto Ambiental do Paraná (Paraná Environmental Institute) and by another civil association called AMAR that have already been contested by the Company. Awaiting initiation of the expert investigation to quantify the amount. The maximum exposure including monetary restatement for Petrobras as of December 31, 2006 is US\$39. The court determined that the suits brought by AMAR and the Federal and State Prosecutors be tried as one. Based on its legal counsels advice, the Company's Administration has assessed risk of loss to be possible.

**Cypriot flag vessel Vergina II collision**

On November 4, 2000, the Cypriot flag vessel Vergina II chartered by Petrobras collided with the south pier at the Company's Almirante Barroso terminal in São Sebastião and spilled oil in the São Sebastião canal. As a result of the accident, the Company was fined approximately US\$30 by various local environmental agencies. The Company is currently contesting these fines.

**Araucária-Paranaguá pipeline rupture**

On February 16, 2001, the Company's Araucária-Paranaguá pipeline ruptured and as a result fuel oil was spilled into the Sagrado, Meio, Neves and Nhundiaquara Rivers located in the state of Paraná. As a result of the accident, the Company was fined approximately US\$80 by the Instituto Ambiental do Paraná (Paraná Environmental Institute), which was contested by the Company through administrative proceeding but the appeal was rejected. The court determined that the suits brought by AMAR and the Federal and State Prosecutors be tried as one. Based on its legal counsels advice, the Company's Administration has assessed risk of loss to be possible.

**19. Commitments and Contingencies (Continued)****(d) Environmental matters (Continued)****Oil spill related to the sinking of P-36 Platform**

On March 15, 2001, a spill resulting from the accident involving the P-36 platform occurred, causing a release of diesel fuel and crude oil. The Company was fined by the IBAMA US\$3 in April of 2001 for the spill and improper use of chemicals to disperse the oil. The Company is currently contesting these fines.

**Rupture of production line at well on the Belém Farm field**

On May 12, 2003, the rupture of a connection socket on a production line at well FZB-71, on the Belém Farm field, in the city of Aracati-CE, resulted in the spill of approximately 7 (seven) thousand liters of oil at an area located far from any communities or water sources. The Company's Contingency Plan was immediately activated and cleaning work for the area was carried out. Petrobras was charged with a penalty of US\$0.04 by the Environment Superintendence of the State of Ceará (Semace) and up to 90% of this amount can be reduced by compliance with a Commitment Term entered into with the referred environmental entity.

**Fault in the connection of arms of vessel Nordic Marita, anchored at the Maritime Terminal Almirante Barroso (Tebar), in São Sebastião, on the North coast of São Paulo**

On June 3, 2003, a fault in the connection of one of the unloading arms of vessel Nordic Marita, anchored at the Maritime Terminal Almirante Barroso (Tebar), in São Sebastião, on the North coast of São Paulo, caused a spill of approximately 27 thousand liters of oil from Campos basin. As a result of this accident, Petrobras was charged with a penalty of US\$0.17 by the IBAMA and of US\$0.12 by Basic Sanitation, Technology and Environment Protection Agency of the State of São Paulo (CETESB). An appeal was filed against both charges based on the understanding that the Company acted in the most efficient possible manner in order to minimize possible impacts on the environment.

**19. Commitments and Contingencies (Continued)****(d) Environmental matters (Continued)****Rupture of a pipeline between Cabiúnas and Duque de Caxias Refinery**

On August 26, 2003, the rupture of a pipeline between TRANSPETRO's terminal in Cabiúnas (Macaé) and Duque de Caxias Refinery caused the spill of 20 (twenty) liters of oil in an area of the city of Cachoeiras de Macacu. The Company immediately determined that the oil located in the service area of the pipeline should be removed, and took preventive measures to protect a creek, near to the Soarinhos River, with checks and oil-absorbing materials. In spite of the effective procedures adopted by Petrobras and the non-existence of environmental damages, the Company received a fine from IBAMA in the amount of US\$0.69, but filed an administrative proceeding with this entity.

**(e) Minimum operating lease payments**

The Company is committed to make the following minimum payments related to operating leases as of December 31, 2006:

2008	2,273
2009	1,527
2010	762
2011	402
2012	317
2013 and thereafter	390
Minimum operating lease payment commitments	5,671

The Company incurred US\$2,016, US\$1,417 and US\$1,247, in rental expense on operating leases at December 31, 2006, 2005 and 2004, respectively.

**20. Derivative Instruments, Hedging and Risk Management Activities**

The Company is exposed to a number of market risks arising from its normal course of business. Such market risks principally involve the possibility that changes in interest rates, foreign currency exchange rates or commodity prices will adversely affect the value of the Company's financial assets and liabilities or future cash flows and earnings. The Company maintains a corporate risk management policy that is executed under the direction of the Company's executive officers.

**20. Derivative Instruments, Hedging and Risk Management Activities (Continued)**

The Company may use derivative and non-derivative instruments to implement its corporate risk management strategy. However, by using derivative instruments, the Company exposes itself to credit and market risk. Credit risk is the failure of a counterparty to perform under the terms of the derivative contract. Market risk is the possible adverse effect on the value of an assets or liability, including financial instruments that results from changes in interest rates, currency exchange rates, or commodity prices. The Company addresses credit risk by restricting the counterparties to such derivative financial instruments to major financial institutions. Market risk is managed by the Company's executive officers. The Company does not hold or issue financial instruments for trading purposes.

In 2004, the Petrobras Executive Board organized a Risk Management Committee comprising executive managers of all business areas and of several corporate areas for the purpose of ensuring integrated management of risk exposures and formalization of the main guidelines adopted by the Company to manage significant risks and uncertainties associated with its activities. The Risk Management Committee was created with a view towards concentrating risk management information and discussions and facilitating communications with the Board of Directors and the Executive Board.

**(a) Foreign currency risk management**

The Company's foreign currency risk management strategy may involve the use of derivative instruments to protect against foreign exchange rate volatility which may impact the value of certain of the Company's obligations.

During 2000, the Company entered into three zero cost foreign exchange rate collars to reduce its exposure to variations between the U.S. Dollar and the Japanese Yen, and between the U.S. Dollar and the EURO, relative to long-term debt denominated in foreign currencies with a face value of approximately US\$470. The Company did not apply hedge accounting for these relationships. The collars were constructed by the simultaneous purchase of a call option and sale of a put option with the same counterparty and with equal premiums.

**20. Derivative Instruments, Hedging and Risk Management Activities (Continued)****(a) Foreign currency risk management (Continued)**

These collars establish a price ceiling and a price floor for the associated exchange rates. If the exchange rate falls below the floor, the counterparties will pay the Company the difference between the spot rate at the maturity date and the floor, calculated based on the notional amount of the contracts. Conversely, if the exchange rate increases above the ceiling, the Company will pay the counterparties the difference between the spot rate at the maturity date and the ceiling, calculated based on the notional amount of the contracts on the notional amount. The maturity dates of the derivatives contracts coincide with the maturity dates of each of the notes.

The Yen zero cost collar contracts were settled on September 8, 2003, with a cash payment of US\$68. One of the Euro zero cost collars was settled on December 31, 2004, with a cash receipt of US\$18.

The call option component of the Company's zero cost foreign exchange collars at December 31, 2006 had a fair value of US\$21 (US\$12 at December 31, 2005) and the put option components a fair value of zero at December 31, 2006 (US\$(1) at December 31, 2005).

**(b) Commodity price risk management**

## Petroleum and oil products

The Company is exposed to commodity price risks as a result of the fluctuation of crude oil and oil product prices. The Company's commodity risk management activities are primarily undertaken through the uses of future contracts traded on stock exchanges; and options and swaps entered into with major financial institutions. The futures contracts provide economic hedges for anticipated crude oil purchases and sales, generally forecasted to occur within a 30 to 360 day period, and reduce the Company's exposure to volatility of such prices.

The Company's exposure from these contracts is limited to the difference between the contract value and market value on the volumes contracted. Crude oil future contracts are marked-to-market and related gains and losses are recognized in currently period earnings, irrespective of when the physical crude sales occur. For the years ended December 31, 2006, 2005 and 2004, the Company entered into commodity derivative transactions for 26.42%, 26.79% and 33.06%, respectively, of its total import and export trade volumes.



**20. Derivative Instruments, Hedging and Risk Management Activities** (Continued)**(b) Commodity price risk management** (Continued)

The open positions in the futures market, compared to spot market values, resulted in recognized losses of US\$2, US\$1 and US\$2 for the years ended December 31, 2006, 2005 and 2004, respectively.

A long-term position was opened in January 2001 via the sale of put options for 52 million barrels of West Texas Intermediate (WTI) oil, over a period extending from 2004 to 2007, with the objective of obtaining price protection for this quantity of oil and to provide the funding institutions of the Barracuda/Caratinga project with a minimum guaranteed margin to cover the debt servicing. The put options were structured to ensure that the financial institutions participating in the financing of the development of the fields receive the price required to generate the minimum required return on investment. The Company accounts for the put options on a mark to market basis. During 2006, 2005 and 2004 the Company realized no gain or loss.

**(c) Interest rate risk management**

The Company's interest rate risk is a function of the Company's long-term debt and to a lesser extent, its short-term debt. The Company's foreign currency floating rate debt is principally subject to fluctuations in LIBOR and the Company's floating rate debt denominated in Reais is principally subject to fluctuations in the Brazilian long-term interest rate (TJLP) as fixed by the National Monetary Counsel. The Company currently does not utilize derivative financial instruments to manage its exposure to fluctuations in interest rates. However, the Company will consider assessing the use of various types of derivatives to reduce its exposure to interest rate fluctuations and may use such financial instruments in the future.

**20. Derivative Instruments, Hedging and Risk Management Activities (Continued)****(d) Risk Management activity at PEPSA**

PEPSA uses derivative instruments such as options, swaps and others, mainly to mitigate the risk of changes in crude oil prices, interest rates and foreign exchange rates. Such derivative instruments are designed to mitigate specific exposures, and when designated as accounting hedges are assessed periodically to assure high correlation of the derivative instrument to the hedged risk exposure identified and to ensure that the derivative is highly effective in achieving offsetting changes in the cash flows of the hedged risk. PEPSA in the past designated certain relationships as accounting hedges for its crude oil derivative instruments and its interest rate swaps derivative instruments, but holds no such instruments at December 31, 2006; nor are any implemented accounting hedges outstanding.

As of December 31, 2006, PEPSA did not have commodity derivative transactions that qualify for hedge accounting purposes in accordance with SFAS No. 133 Accounting for Derivative Instruments and Hedging Activities ("SFAS 133"). PEPSA accounted for a loss of US\$103 for the year ended December 31, 2005 due to derivative financial instruments that did not qualify for hedge accounting.

At December 31, 2006, PEPSA had forward sales of US dollars in exchange for Argentine pesos. During the current fiscal year, the Company recognized a US\$2 gain. As of December 31, 2006 and 2005 the face value of effective contracts amounts to US\$18 and US\$52, respectively, at the average exchange rate of 3.26 and 3 Argentine pesos per US dollar, respectively. Without considering the above-mentioned operations, as of December 31, 2006, the Company did not have any other positions in derivatives instruments.

**(e) Cash flow hedge**

In September, 2006 PIFCo entered into cross currency swap under which it swaps principal and interest payments on Yen denominated bonds for U.S. dollar amounts. Under U.S. GAAP, foreign currency cash flow hedges can only be designated as such when hedging the risk to the entity's functional currency, and therefore, this cross currency swaps is qualified for hedge accounting designation take into account that PIFCo's functional currency is the US dollar, and the assessment of hedge effectiveness indicates that the change in fair value of the designated hedging instrument is highly effective.

**20. Derivative Instruments, Hedging and Risk Management Activities (Continued)****(e) Cash flow hedge (Continued)**

The hedged item is ¥ 35 billion bond, ten-year maturity, carrying a semi-annual coupon of 2.15% p.a. The hedge instrument is a cross currency swap, ten year maturity, under which US dollars is paid and Japanese Yen is received mirroring the Yen bond conditions. The effectiveness test was made at the inception at the hedge based on the hypothetical derivative method. The effectiveness test will be made on an ongoing basis on a quarterly basis.

The transaction gain or loss arising from the remeasurement of Yen denominated bonds is offset by the reclassification relating to the remeasurement of the hedged item at spot rates from other comprehensive income to earnings. The cross currency swap at December 31, 2006 had a fair value of (US\$9) due to the devaluation of the Japanese Yen when compared to US dollar since the inception of the instrument.

**21. Natural Gas Derivative Contract**

In connection with the long-term contract to buy gas ( The Gas Supply Agreement or "GSA") to supply thermoelectric plants and for other uses in Brazil, the Company entered into a contract, with the company Empresa Petrolera ANDINA, a gas producer in Bolivia, that constituted a derivative financial instrument under SFAS 133. This contract, the Natural Gas Price Volatility Reduction Contract (the "PVRC"), was executed with the purpose of reducing the effects of price volatility under the GSA.

The terms of the PVRC provided for a price collar for the period from 2005 to 2019, with the Company receiving cash payments when the calculated price is above the established ceiling, and the Company making cash payments when the price is below the established floor, with no cash payments being made when the price is between the ceiling and the floor.

As of December 31, 2005, the Company recorded an asset based on the fair value of the derivative in the amount of US\$547 and a liability of US\$144, which was deemed a deferred purchase incentive.

Due to the new Hydrocarbons Law of Bolivia (see Note 9(b)), the other party to the PVRC contested the contract, alleging among others, force majeure and excessive onus. On August 12, 2006, the parties agreed to cancel the PVRC. As a result, on August 14, 2006 the Company received US\$41 and wrote-off accounts receivable related to the PVRC amounting to US\$77.

**21. Natural Gas Derivative Contract (Continued)**

The Company adjusted the fair value asset and liabilities related to the PVRC by recording a financial expense of US\$328 during the first quarter of 2006 as a result of the tax increases in Bolivia. In the second quarter of 2006, the Company wrote-off the remaining fair value asset of US\$94 as a consequence of the cancellation of contract.

**22. Financial Instruments**

In the normal course of its business activities, the Company acquires various types of financial instruments.

**(a) Concentrations of credit risk**

Substantial portions of the Company's assets including financial instruments are located in Brazil while substantially all of the Company's revenues and net income are generated in Brazil. The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of its cash and cash equivalents, government securities, the Petroleum and Alcohol account, trade receivables and futures contracts.

The Company takes several measures to reduce its credit risk to acceptable levels. All cash and cash equivalents in Brazil are maintained with major banks. Time deposits in U.S. dollars are placed with creditworthy institutions in the United States. Additionally, all of the Company's available-for-sale securities and derivative contracts are either exchange traded or maintained with creditworthy financial institutions. The Company monitors its credit risk associated with trade receivables by routinely assessing the creditworthiness of its customers. At December 31, 2006 and December 31, 2005, the Company's trade receivables were primarily maintained with large distributors.

**(b) Fair value**

Fair values are derived either from quoted market prices where available, or, in their absence, the present value of expected cash flows. Fair values reflect the cash that would have been either received or paid if the instruments were settled at year end in an arms length transaction between willing parties. Fair values of cash and cash equivalents, trade receivables, the Petroleum and Alcohol account, short-term debt and trade payables approximate their carrying values. The fair value for the Company's available-for-sale government securities equals their carrying value.

**22. Financial Instruments** (Continued)**(b) Fair value** (Continued)

The fair values of other long-term receivables and payables do not differ materially from their carrying values.

The Company's debt including project financing obligations, resulting from FIN 46(R) consolidation amounted to US\$14,702 at December 31, 2006 and US\$15,132 at December 31, 2005 and had estimated fair values of US\$13,984 and US\$15,239, respectively.

**23. Segment Information**

The following segment information has been prepared in accordance with SFAS No. 131 - Disclosure about Segments of an Enterprise and Related information ("SFAS 131"). The Company operates under the following segments, which are described as follows:

- **Exploration and Production** - This segment includes the Company's exploration, production development and production activities of oil, liquefied natural gas and natural gas in Brazil, for the purpose of supplying refineries in Brazil as well as selling surplus Brazilian production in domestic and foreign markets and limited oil trading activities and transfers of natural gas to the Company's Gas and Energy segment.
- **Supply** - This segment includes the Company's refining, logistic, transportation, exportation and the purchase of crude oil, as well as the purchase and commercialization activities for oil, oil products and fuel alcohol. Additionally, this segment includes petrochemical and fertilizers division, which includes investments in domestic petrochemical companies and the Company's two domestic fertilizer plants.
- **Distribution** - This segment represents the oil product and fuel alcohol distribution activities conducted by the Company's majority owned subsidiary, Petrobras Distribuidora S.A. - BR in Brazil. In accordance with the Company's strategic objectives to increase market share in the LPG distribution segment and consolidate the automotive fuels distribution market in certain regions of Brazil, its distribution business includes the operations of Liquigás Distribuidora S.A (formerly known as Sophia do Brasil S.A. and Agip do Brasil S.A.), which was acquired on August 9, 2004.

**23. Segment Information** (Continued)

- Gas and Energy - This segment currently encompasses the purchase, sale, transportation and distribution of natural gas produced in or imported into Brazil. Additionally, this segment includes the Company's participation in domestic electricity production, including investments in domestic natural gas transportation companies, state owned natural gas distributors and thermoelectric companies.
- International - This segment represents the Company's international Exploration and Production, Supply, Distribution and Gas and Energy activities conducted in 15 countries outside Brazil .

The items that cannot be attributed to the other areas are allocated to the group of corporate entities, especially those linked with corporate financial management, overhead related with central administration and other expenses, including actuarial expenses related with the pension and health-care plans for non-active participants.

The accounting information by business area was prepared based on the assumption of controllability, for the purpose of attribution to the business areas only items over which these areas have effective control.

The main criteria used to record the results and assets by business segments are summarized as follows:

- Net operating revenues: these were considered to be the revenues from sales to third parties, plus revenues between the business segments, based on the internal transfer prices established by the areas;
- Costs and expenses includes the costs of products and services sold, calculated per business segment, based on the internal transfer price and the other operating costs of each segment, as well as operating expenses, based on the expenses actually incurred in each segment;
- Assets: covers the assets relating to each segment.

**23. Segment Information** (Continued)

The following presents the Company's assets by segment:

**As of December 31, 2006**

	<b>Exploration and Production</b>	<b>Supply</b>	<b>Gas and Energy</b>	<b>International (see separate disclosure)</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Current assets (1)	2,966	9,668	1,256	2,371	1,978	15,413	(2,697)	30,955
Cash and cash equivalents	-	-	-	-	-	12,688	-	12,688
Other current assets	2,966	9,668	1,256	2,371	1,978	2,725	(2,697)	18,267
Investments in non-consolidated companies and other investments	33	970	394	1,721	20	124	-	3,262
Property, plant and equipment, net	33,979	9,828	6,828	5,722	1,468	1,072	-	58,897
Non current assets	1,388	354	1,119	460	209	2,523	(487)	5,566
Petroleum and Alcohol account	-	-	-	-	-	368	-	368
Government securities	-	-	-	-	-	479	-	479
Other assets (1)	1,388	354	1,119	460	209	1,676	(487)	4,719
Total assets	38,366	20,820	9,597	10,274	3,675	19,132	(3,184)	98,680

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of

2006, switched to allocating all financial results and items of financial nature to the corporate level.



**23. Segment Information** (Continued)

As of December 31, 2006

**International**

	<b>Exploration and Production</b>	<b>Supply</b>	<b>Gas and Energy</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Current assets (1)	1,486	1,019	954	134	219	(1,441)	2,371
Cash and cash equivalents	-	-	-	-	-	-	-
Other current assets	1,486	1,019	954	134	219	(1,441)	2,371
Investments in non-consolidated companies and other investments	990	360	280	66	25	-	1,721
Property, plant and equipment, net	4,436	834	216	162	94	(20)	5,722
Non current assets	546	36	49	13	669	(853)	460
Other assets (1)	546	36	49	13	669	(853)	460
Total assets	7,458	2,249	1,499	375	1,007	(2,314)	10,274

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.

**23. Segment Information** (Continued)

As of December 31, 2005

	<b>Exploration and Production</b>	<b>Supply</b>	<b>Gas and Energy</b>	<b>International (see separate disclosure)</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Current assets (1)	2,770	8,116	1,052	1,815	1,918	12,644	(2,531)	25,784
Cash and cash equivalents	-	-	-	-	-	9,871	-	9,871
Other current assets	2,770	8,116	1,052	1,815	1,918	2,773	(2,531)	15,913
Investments in non-consolidated companies and other investments	9	822	438	418	20	103	-	1,810
Property, plant and equipment, net	25,876	8,098	5,328	4,655	1,238	768	(43)	45,920
Non current assets	971	396	1,349	459	392	1,780	(223)	5,124
Petroleum and Alcohol account	-	-	-	-	-	329	-	329
Government securities	-	-	-	-	-	364	-	364
Other assets (1)	971	396	1,349	459	392	1,087	(223)	4,431
Total assets	29,626	17,432	8,167	7,347	3,568	15,295	(2,797)	78,638

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.



**23. Segment Information** (Continued)

As of December 31, 2005

**International**

	<b>Exploration and Production</b>	<b>Supply</b>	<b>Gas and Energy</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Current assets (1)	1,486	660	552	72	227	(1,182)	1,815
Cash and cash equivalents	-	-	-	-	-	-	-
Other current assets	1,486	660	552	72	227	(1,182)	1,815
Investments in non-consolidated companies and other investments	141	51	204	-	22	-	418
Property, plant and equipment, net	3,801	530	192	78	59	(5)	4,655
Non current assets	483	34	57	22	2,173	(2,310)	459
Other assets (1)	483	34	57	22	2,173	(2,310)	459
Total assets	5,911	1,275	1,005	172	2,481	(3,497)	7,347

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.

**23. Segment Information** (Continued)

Revenues and net income by segment are as follows:

	Year ended December 31, 2006							Total
	Exploration and Production	Supply	Gas and Energy	International (see separate disclosure)	Distribution	Corporate	Eliminations	
Net operating revenues to third parties	3,351	42,831	2,833	4,938	18,394	-	-	72,347
Inter-segment net operating revenues	32,387	15,128	1,257	1,133	287	-	(50,192)	-
Net operating revenues	35,738	57,959	4,090	6,071	18,681	-	(50,192)	72,347
Cost of sales	(13,635)	(51,802)	(3,531)	(4,088)	(16,967)	-	49,962	(40,061)
Depreciation, depletion and amortization	(2,166)	(669)	(197)	(417)	(143)	(81)	-	(3,673)
Exploration, including exploratory dry holes	(501)	-	-	(433)	-	-	-	(934)
Impairment	(20)	-	-	(1)	-	-	-	(21)
Selling, general and administrative expenses	(465)	(1,357)	(360)	(540)	(982)	(1,306)	21	(4,989)
Research and development expenses	(346)	(141)	(78)	(2)	(5)	(155)	-	(727)
Other operating expenses	(22)	(40)	(270)	(22)	(77)	(662)	12	(1,081)
Costs and expenses	(17,155)	(54,009)	(4,436)	(5,503)	(18,174)	(2,204)	49,995	(51,486)
Equity in results of non-consolidated companies	-	5	(1)	37	-	(13)	-	28
Financial income (expenses), net (1)	-	-	-	-	-	(100)	-	(100)

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

Employee benefit expense	-	-	-	-	-	(1,017)	-	(1,017)
Other taxes	(45)	(73)	(49)	(63)	(79)	(285)	-	(594)
Other expenses, net	(73)	(20)	(15)	30	23	38	-	(17)
Income before income taxes, minority interest, extraordinary item and accounting change	18,465	3,862	(411)	572	451	(3,581)	(197)	19,161
Income tax benefits (expense)	(6,278)	(1,312)	140	(255)	(153)	2,100	67	(5,691)
Minority interest in results of consolidated subsidiaries	(229)	(10)	(231)	(194)	-	20	-	(644)
Net income for the year	11,958	2,540	(502)	123	298	(1,461)	(130)	12,826

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.

**23. Segment Information** (Continued)

Year ended December 31, 2006

**International**

	<b>Exploration and Production</b>	<b>Supply</b>	<b>Gas and Energy</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Net operating revenues to third parties	685	2,068	719	1,440	26	-	4,938
Inter-segment net operating revenues	1,831	1,450	41	6	-	(2,195)	1,133
Net operating revenues	2,516	3,518	760	1,446	26	(2,195)	6,071
Cost of sales	(948)	(3,307)	(577)	(1,433)	(26)	2,203	(4,088)
Depreciation, depletion and amortization	(309)	(65)	(14)	(16)	(13)	-	(417)
Exploration, including exploratory dry holes	(433)	-	-	-	-	-	(433)
Impairment	(1)	-	-	-	-	-	(1)
Selling, general and administrative expenses	(154)	(85)	(17)	(99)	(185)	-	(540)
Research and development expenses	-	-	-	-	(2)	-	(2)
Other operating expenses	(4)	4	13	9	(44)	-	(22)
Costs and expenses	(1,849)	(3,453)	(595)	(1,539)	(270)	2,203	(5,503)
Equity in results of non-consolidated companies	20	12	2	-	3	-	37
Other taxes	(13)	(8)	-	(2)	(40)	-	(63)
Other expenses, net	29	-	11	33	(43)	-	30
Income before income taxes, minority interest, and accounting change	703	69	178	(62)	(324)	8	572
Income tax benefits (expense)	(305)	(25)	(79)	28	130	(4)	(255)
	(172)	(14)	(22)	25	(11)	-	(194)

Minority interest in results  
of consolidated  
subsidiaries

Net income (loss) for the  
year

226	30	77	(9)	(205)	4	123
-----	----	----	-----	-------	---	-----



**23. Segment Information** (Continued)

Revenues and net income by segment are as follows:

	<b>Year ended December 31, 2005</b>							
	<b>Exploration and Production (1)</b>	<b>Supply (1)</b>	<b>Gas and Energy</b>	<b>International (see separate disclosure)</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Net operating revenues to third parties	1,874	33,229	1,932	3,647	15,642	-	-	56,324
Inter-segment net operating revenues	26,950	12,286	1,232	880	225	-	(41,573)	-
Net operating revenues	28,824	45,515	3,164	4,527	15,867	-	(41,573)	56,324
Cost of sales	(11,327)	(40,033)	(2,484)	(2,425)	(14,357)	-	40,798	(29,828)
Depreciation, depletion and amortization	(1,571)	(644)	(105)	(461)	(100)	(45)	-	(2,926)
Exploration, including exploratory dry holes	(860)	-	-	(149)	-	-	-	(1,009)
Impairment	(22)	-	-	(134)	-	-	-	(156)
Selling, general and administrative expenses	(358)	(1,195)	(612)	(424)	(914)	(1,026)	55	(4,474)
Research and development expenses	(153)	(55)	(22)	(2)	(1)	(166)	-	(399)
Other operating expenses	(45)	(130)	(475)	(123)	59	(739)	-	(1,453)
Costs and expenses	(14,336)	(42,057)	(3,698)	(3,718)	(15,313)	(1,976)	40,853	(40,245)
Equity in results of non-consolidated companies	-	10	56	68	-	5	-	139
Financial income (expenses), net	-	-	-	-	-	(231)	-	(231)

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

(2)									
Employee benefit expense	-	-	-	-	-	(994)	-	(994)	
Other taxes	(20)	(32)	(23)	(51)	(68)	(179)	-	(373)	
Other expenses, net	(15)	(7)	(11)	27	(15)	(7)	-	(28)	
Income before income taxes, minority interest extraordinary item and accounting change	14,453	3,429	(512)	853	471	(3,382)	(720)	14,592	
Income tax benefits (expense)	(4,914)	(1,163)	193	(289)	(160)	1,647	245	(4,441)	
Minority interest in results of consolidated subsidiaries	(70)	(21)	(23)	(38)	-	187	-	35	
Income before effect of change in accounting principle	9,469	2,245	(342)	526	311	(1,548)	(475)	10,186	
Extraordinary gain net of tax	-	-	-	-	-	158	-	158	
Net income for the year	9,469	2,245	(342)	526	311	(1,390)	(475)	10,344	

(1) In 2005 revenues from commercialization of oil to third parties are being classified in accordance with the points of sale, which could be Exploration & Production or Supply segments. Until 2004, revenues from commercialization of oil were completely allocated to Exploration & Production. This classification generated no significant impact on the results reported for these segments and segments information has not been restated as it is impractical to gather and collect data for prior periods as to point of sale.

(2) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.

**23. Segment Information** (Continued)

Year ended December 31, 2005

**International**

	<b>Exploration and Production</b>	<b>Supply</b>	<b>Gas and Energy</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Net operating revenues to third parties	920	1,079	536	1,090	22	-	3,647
Inter-segment net operating revenues	1,476	1,279	31	4	-	(1,910)	880
Net operating revenues	2,396	2,358	567	1,094	22	(1,910)	4,527
Cost of sales	(665)	(2,151)	(452)	(1,020)	(22)	1,885	(2,425)
Depreciation, depletion and amortization	(360)	(65)	(13)	(11)	(12)	-	(461)
Exploration, including exploratory dry holes	(142)	-	-	(7)	-	-	(149)
Impairment	(134)	-	-	-	-	-	(134)
Selling, general and administrative expenses	(123)	(60)	(7)	(68)	(166)	-	(424)
Research and development expenses	-	-	-	-	(2)	-	(2)
Other operating expenses	(144)	11	8	1	(47)	48	(123)
Costs and expenses	(1,568)	(2,265)	(464)	(1,105)	(249)	1,933	(3,718)
Equity in results of non-consolidated companies	4	18	2	-	40	4	68
Other taxes	(14)	(5)	(1)	(1)	(30)	-	(51)
Other expenses, net	(5)	(1)	-	-	33	-	27
Income before income taxes, minority interest, extraordinary item and accounting change	813	105	104	(12)	(184)	27	853
Income tax benefits (expense)	(275)	(36)	(35)	4	62	(9)	(289)

Minority interest in results of consolidated subsidiaries	15	(20)	(10)	3	(26)	-	(38)
Net income (loss) for the year	553	49	59	(5)	(148)	18	526

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.

**23. Segment Information** (Continued)

Year ended December 31, 2004

	<b>Exploration</b>		<b>Gas</b>	<b>International</b>				
	<b>And</b>	<b>Supply</b>	<b>and</b>	<b>(see separate</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
	<b>Production</b>		<b>Energy</b>	<b>Disclosure)</b>				
Net operating revenues to third parties	2,487	20,981	1,547	3,085	10,328	-	-	38,428
Inter-segment net operating revenues	16,384	7,786	474	519	158	-	(25,321)	-
Net operating revenues	18,871	28,767	2,021	3,604	10,486	-	(25,321)	38,428
Cost of sales	(7,093)	(25,915)	(1,995)	(1,871)	(9,470)	-	25,065	(21,279)
Depreciation, depletion and amortization	(1,322)	(548)	(100)	(423)	(59)	(29)	-	(2,481)
Exploration, including exploratory dry holes	(419)	-	-	(194)	-	-	-	(613)
Impairment	(51)	-	(14)	-	-	-	-	(65)
Selling, general and administrative expenses	(235)	(960)	(178)	(334)	(567)	(627)	-	(2,901)
Research and development expenses	(109)	(53)	(9)	(2)	(2)	(73)	-	(248)
Other operating expenses	29	(57)	(188)	(48)	(78)	(138)	-	(480)
Costs and expenses	(9,200)	(27,533)	(2,484)	(2,872)	(10,176)	(867)	25,065	(28,067)
Equity in results of non-consolidated companies	-	12	68	92	-	-	-	172
Financial income (expenses), net (1)	-	-	-	-	-	(327)	-	(327)
Employee benefit expense	-	-	-	-	-	(650)	-	(650)

Edgar Filing: BRAZILIAN PETROLEUM CORP - Form 6-K

Other taxes	(12)	(25)	(30)	(47)	(54)	(272)	-	(440)
Other expenses, net	(117)	24	(8)	(10)	(2)	(68)	-	(181)
Income before income taxes, minority interest, extraordinary item and accounting change	9,542	1,245	(433)	767	254	(2,184)	(256)	8,935
Income tax benefits (expense)	(3,244)	(419)	170	(51)	(86)	1,312	87	(2,231)
Minority interest in results of consolidated subsidiaries	(349)	(1)	(84)	(148)	-	68	-	(514)
Net income (loss) for the year	5,949	825	(347)	568	168	(804)	(169)	6,190

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.

**23. Segment Information** (Continued)

Year ended December 31, 2004

**International**

	<b>Exploration and Production</b>	<b>Supply</b>	<b>Gas and Energy</b>	<b>Distribution</b>	<b>Corporate</b>	<b>Eliminations</b>	<b>Total</b>
Net operating revenues to third parties	713	1,084	405	865	18	-	3,085
Inter-segment net operating revenues	1,087	1,076	26	15	-	(1,685)	519
Net operating revenues	1,800	2,160	431	880	18	(1,685)	3,604
Cost of sales	(461)	(1,797)	(337)	(940)	(17)	1,681	(1,871)
Depreciation, depletion and amortization	(326)	(63)	(13)	(10)	(11)		(423)
Exploration, including exploratory dry holes and impairment	(194)	-	-	-	-	-	(194)
Selling, general and administrative expenses	(111)	(53)	(11)	(60)	(99)	-	(334)
Research and development expenses	-	-	-	-	(2)	-	(2)
Other operating expenses	(75)	9	12	(2)	8	-	(48)
Costs and expenses	(1,167)	(1,904)	(349)	(1,012)	(121)	1,681	(2,872)
Equity in results of non-consolidated companies	8	21	7	-	56	-	92
Other taxes	(16)	(7)	-	(7)	(17)	-	(47)
Other expenses, net	14	-	-	-	(24)	-	(10)
Income before income taxes, minority interest, extraordinary item and accounting change	639	270	89	(139)	(88)	(4)	767
Income tax benefits (expense)	(140)	(60)	(20)	31	137	1	(51)

Minority interest in results of consolidated subsidiaries	5	(4)	(2)	(4)	(143)	-	(148)
Net income (loss) for the year	504	206	67	(112)	(94)	(3)	568

(1) In order to align the financial statements of each business segment with the best practices of companies in the Oil & Gas sector and to improve the understanding of Petrobras management, the Company, since the first quarter of 2006, switched to allocating all financial results and items of financial nature to the corporate level.



**23. Segment Information** (Continued)

Capital expenditures incurred by segment for the years ended December 31, 2006, 2005 and 2004 are as follows:

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Exploration and Production	<b>7,329</b>	6,127	4,574
Supply	<b>1,936</b>	1,749	1,367
Gas and Energy	<b>1,664</b>	694	782
International			
Exploration and Production	<b>2,304</b>	1,067	666
Supply	<b>202</b>	79	43
Distribution	<b>77</b>	16	12
Gas and Energy	<b>54</b>	13	6
Distribution	<b>351</b>	207	47
Corporate	<b>726</b>	413	221
	<b>14,643</b>	10,365	7,718

The Company's gross sales, classified by geographic destination, are as follows:

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Brazil	<b>70,733</b>	57,669	40,905
International	<b>23,160</b>	16,396	11,049
	<b>93,893</b>	74,065	51,954

The total amounts sold of products and services to the two major customers in 2006 were US\$7,978 and US\$5,689 (US\$6,258 and US\$4,594 in 2005; and US\$4,269 and US\$3,108 in 2004).

**24. Related Party Transactions**

The Company is controlled by the Federal Government and has numerous transactions with other state-owned companies in the ordinary course of its business.

Transactions with major related parties resulted in the following balances:

	<b>As of December 31,</b>			
	<b>2006</b>		<b>2005</b>	
	<b>Assets</b>	<b>Liabilities</b>	<b>Assets</b>	<b>Liabilities</b>
PETROS (pension fund)	<b>479</b>	<b>71</b>	362	15
Banco do Brasil S.A.	<b>5,014</b>	<b>517</b>	5,944	56
BNDES (Note 12 (b))	-	<b>1,491</b>	-	589
BNDES (Project financing)	-	<b>1,823</b>	-	1,336
Federal Government	-	<b>1,190</b>	-	966
Restricted deposits for legal Proceedings	<b>676</b>	-	637	-
Government securities	<b>67</b>	-	269	-
Petroleum and Alcohol account - receivable from Federal Government (Note 11)	<b>368</b>	-	329	-
Others	<b>786</b>	<b>149</b>	1,926	776
	<b>7,390</b>	<b>5,241</b>	9,467	3,738
Current	<b>5,382</b>	<b>2,957</b>	7,458	2,400
Long-term	<b>2,008</b>	<b>2,284</b>	2,009	1,338

**24. Related Party Transactions (Continued)**

These balances are included in the following balance sheet classifications:

	<b>As of December 31,</b>			
	<b>2006</b>		<b>2005</b>	
	<b>Assets</b>	<b>Liabilities</b>	<b>Assets</b>	<b>Liabilities</b>
<b>Assets</b>				
<b>Current</b>				
Cash and cash equivalents	<b>4,497</b>	-	5,908	-
Accounts receivable (Note 6)	<b>653</b>	-	308	-
Other current assets	<b>232</b>	-	1,242	-
<b>Other</b>				
Accounts receivable (Note 6)	-	-	32	-
Government securities	<b>67</b>	-	269	-
Petroleum and Alcohol account - receivable				
from Federal Government (Note 11)	<b>368</b>	-	329	-
Restricted deposits for legal proceedings	<b>676</b>	-	637	-
Pension fund	<b>479</b>	-	362	-
Other assets	<b>418</b>	-	380	-
<b>Liabilities</b>				
<b>Current</b>				
Current portion of long-term debt	-	<b>148</b>	-	70
Current liabilities	-	<b>68</b>	-	723
Dividends and interest on capital payable to Federal Government	-	<b>1,743</b>	-	966
Current portion of project financings	-	<b>998</b>	-	640
<b>Long-term</b>				
Long-term debt	-	<b>1,342</b>	-	545
Project financings	-	<b>825</b>	-	696
Other liabilities	-	<b>117</b>	-	98
	<b>7,390</b>	<b>5,241</b>	9,467	3,738

**24. Related Party Transactions (Continued)**

The principal amounts of business and financial operations carried out with related parties are as follows:

	<b>Year ended December 31,</b>					
	<b>2006</b>		<b>2005</b>		<b>2004</b>	
	<b>Income</b>	<b>Expense</b>	<b>Income</b>	<b>Expense</b>	<b>Income</b>	<b>Expense</b>
Sales of products and services						
BRASKEM S.A.	<b>1,788</b>	-	1,488	-	1,049	-
COPEL S.A.	<b>1,132</b>	-	373	-	501	-
Manaus Energia S.A.	-	-	-	-	-	-
Petroquímica União S.A.	<b>588</b>	-	885	-	828	(15)
Others	<b>315</b>	-	954	-	582	-
Financial income	-	-	-	-	-	-
Petroleum and Alcohol account receivable from Federal Government (Note 11)	<b>7</b>	-	9	-	4	-
Government securities	-	-	-	-	3	-
Others	<b>71</b>	-	47	-	(113)	-
Financial expenses	-	<b>8</b>	-	11	-	13
Other expenses, net	-	<b>(2)</b>	-	(262)	2	-
	<b>3,905</b>	<b>6</b>	3,756	(251)	2,856	(2)

**25. Accounting for Suspended Exploratory Wells**

The Company's accounting for exploratory drilling costs is governed by Statement of Financial Accounting Standards No. 19, Financial Accounting and Reporting by Oil and Gas Producing Companies (SFAS No. 19). On April 4, 2005, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP FAS 19-1) that amended SFAS No. 19 with respect to the deferral of exploratory drilling costs. The Company adopted FASB Staff Position FAS 19-1) Accounting for Suspended Wells Costs effective from January 1, 2005. There was no material impact at adoption.

**25. Accounting for Suspended Exploratory Wells (Continued)**

Costs the Company has incurred to drill exploratory wells that find commercial quantities of oil and gas are carried as assets on its balance sheet under the classification Property, plant and equipment as unproved oil and gas properties. Each year, the Company writes off the costs of these wells that have not found sufficient proved reserves to justify completion as a producing well, unless (1) the well is in an area requiring major capital expenditure before production can begin and (2) additional exploratory drilling is under way or firmly planned to determine whether the capital expenditure is justified.

As of December 31, 2006, the total amount of unproved oil and gas properties was US\$2,054, and of that amount US\$321 (US\$195 of which related to projects in Brazil) represented costs that had been capitalized for more than one year, which generally are a result of (1) extended exploratory activities associated with offshore production and (2) the transitory effects of deregulation in the Brazilian oil and gas industry, as described below.

In 1998, the Company's government-granted monopoly ended and the Company signed concession contracts with the Agência Nacional de Petróleo (National Petroleum Agency, or ANP) for all of the areas the Company had been exploring and developing prior to 1998, which consisted of 397 concession blocks. Since 1998, the ANP has conducted competitive bidding rounds for exploration rights, which has allowed the Company to acquire additional concession blocks. After a concession block is found to contain a successful exploratory well, we must submit an Evaluation Plan to the ANP for approval. This Evaluation Plan details the drilling plans for additional exploratory wells. An Evaluation Plan is only submitted for those concession areas where technical and economic feasibility analyses on existing exploration wells evidence justification for completion of such wells. Until the ANP approves the Evaluation Plan, the drilling of additional exploratory wells cannot commence. If companies do not find commercial quantities of oil and gas within a specific time period, generally 4-6 years depending on the characteristics of the exploration area, then the concession block must be relinquished and returned to the ANP. Because the Company was required to assess a large volume of concession blocks in a limited time frame even when an exploratory well has found sufficient reserves to justify completion and additional wells are firmly planned, finite resources and expiring time frames in other concession blocks have dictated the timing of the planned additional drilling.

**25. Accounting for Suspended Exploratory Wells (Continued)**

The following table shows the net changes in capitalized exploratory drilling costs during the years ended December 31, 2006 and 2005:

	<b>Unproved oil and gas properties (*)</b>	
	<b>Year ended December,31</b>	
	<b>2006</b>	<b>2005</b>
Beginning balance at January 1	<b>2,061</b>	1,684
Additions to capitalized costs pending determination of proved reserves	<b>2,186</b>	1,247
Capitalized exploratory costs charged to expense	<b>(493)</b>	(597)
Sales of reserves	<b>(199)</b>	-
Transfers to property, plant and equipment based on the determination of the proved reserves	<b>(1,614)</b>	(423)
Cumulative translation adjustment	<b>113</b>	150
Ending balance at December 31,	<b>2,054</b>	2,061

(\*) Amounts capitalized and subsequently expensed in the same period have been excluded from the above table.

The following table provides an aging of capitalized exploratory well costs based on the date the drilling was completed and the number of projects for which exploratory well costs have been capitalized for a period greater than one year since the completion of the drilling:

	<b>Aging of capitalized exploratory well costs</b>	
	<b>Year ended December 31,</b>	
	<b>2006</b>	<b>2005</b>
Capitalized exploratory well costs that have been capitalized for a period of one year or less	<b>1,733</b>	1,155
Capitalized exploratory well costs that have been capitalized for a period greater than one year	<b>321</b>	906
Ending balance	<b>2,054</b>	2,061
Number of projects that have exploratory well costs that have been capitalized for a period greater than one year	<b>50</b>	42



**25. Accounting for Suspended Exploratory Wells (Continued)**

Of the US\$321 for 50 projects that include wells suspended for more than one year since the completion of drilling, approximately US\$103 are related to wells in areas for which drilling was under way or firmly planned for the near future and that we have submitted an Evaluation Plan to the ANP for approval and approximately US\$54 incurred in costs for activities necessary to assess the reserves and their potential development.

The US\$321 of suspended well cost capitalized for a period greater than one year as of December 31, 2006 represents 66 exploratory wells and the table below contains the aging of these costs on a well basis:

Aging based on drilling completion date of individual wells:

	<b>Million of dollars</b>	<b>Number of wells</b>
2005	160	43
2004	120	11
2003	31	3
2002	-	-
2001	10	9
	321	66



**26. Subsequent Events****(a) Global Notes**

On January 4, 2007, PIFCo, a wholly owned subsidiary of Petrobras, announced an offer for the exchange of securities (Exchange Offering) totaling up US\$500 (face value) for the five series of notes.

The objective of the Exchange was offer to the investors the opportunity to substitute the five old notes listed below, with PIFCo's new benchmark issued on October 06, 2006, with a coupon of 6.125% per annum and maturity in 2016.

The settlement of the Exchange Offering occurred on February 7, 2007 and as a result, PIFCo received and accepted a tender amount of US\$399 (face value of the Notes). All the notes received were cancelled in the same day and as a consequence, PIFCo issued US\$399 of Global Notes due 2016 that bear interest at the rate of 6.125% per annum, payable semi-annually. The new Notes constitute a single, fungible series with the US\$500 Global Notes due 2016 and issued on October 06, 2006, amounting to US\$899 in securities issued with maturity in 2016. PIFCo also paid to the investors a cash amount equivalent to US\$56 as a result of the Exchange. The table below presents the result of the Exchange.

<b>US\$ Million</b>				
<b>Old notes</b>	<b>Interest rate</b>	<b>Maturity</b>	<b>Principal after Settlement</b>	<b>Accepted for Exchange</b>
Global Step-Up Notes	12.375%	2008	127	8
Senior Notes	9.875%	2008	224	14
Senior Notes	9.750%	2011	236	51
Global Notes	9.125%	2013	374	124
Global Notes	7.750%	2014	398	202
			<b>1,359</b>	<b>399</b>

<b>US\$ Million</b>				
<b>New notes</b>	<b>Interest rate</b>	<b>Maturity</b>	<b>Principal after Exchange</b>	<b>Total Reopened</b>
Global Notes	6.125%	2016	899	399
			<b>899</b>	<b>399</b>

**26. Subsequent Events (Continued)****(b) Leasing of the Araucária Gas Thermoelectric Power Station**

Petrobras announced on January 3, 2007 that it had executed two service provision and leasing contracts with UEG Araucária and COPEL. The first contract refers to the leasing of the Araucária Gas Thermoelectric Power Station executed by Petrobras and UEG, in force until December 31, 2007 which may be extended for a period of up to 12 months. The second contract involves the provision of maintenance and operating services regarding the UEG Araucária, executed by Petrobras and COPEL Geração, in force until December 31, 2008 or the end of the leasing agreement, whichever occurs first.

Under the two contracts, a fixed monthly payment will be due of US\$8.89 per MWh multiplied by the reference voltage (428,35 MW) plus a variable monthly payment of US\$15.54 per MWh, on the effective energy generated. These proceeds are used to cover all costs and taxes incurred by UEG.

Executing these contracts will enable better allocation of the gas produced to meet the fundamental commitments referring to the energy sold by the Company.

**(c) Repactuation of PETROS Plan**

During 2006 Petrobras presented to employee participants and retirees a proposal to bring equilibrium to the actual PETROS Plan. On February 28, 2007 the target for the minimum accession number to the renegotiation set at 2/3 (two-thirds) of the members and was met (see Note 16 (b)).

The renegotiation process consists of changing the plan's regulation, particularly the articles related to how the benefits are readjusted, disentailing the readjustment of the benefits paid to retirees and pensioners from wage increases granted to active employees and INSS retirees. Petros Plan benefits, disentailed from the active employees wage and INSS retirement and pension plan readjustments, will be adjusted based on the IPCA (cost of living index).

**26. Subsequent Events** (Continued)

**(c) Repactuation of PETROS Plan** (Continued)

The financial incentive to be granted to the participants, whether employees or retirees, as negotiated by the labor union representatives as a counterpart for the Plan's repactuation, amounted to US\$425 and was paid on March 2007.

The proposal's approval also opens the way to reach agreements with Labor Union Representations in order to liquidate and extinguish legal suits, particularly the Public Civil Suit regarding Petrobras System's complementary retirement issues. The demands that refer to the items to be removed from the lawsuits will be attended to through the calculation of their actuarial value and paid for by Petrobras, in 20 years, respecting the Plan's liquidity conditions.

**26. Subsequent Events (Continued)****(d) Ipiranga Group Acquisition**

On March 19, 2007, Ultrapar Participações S.A. ("Ultrapar") has celebrated, with the acknowledgement of Petróleo Brasileiro S.A. ("Petrobras") and Braskem S.A. ("Braskem") a contract with the controlling shareholders of Refinaria de Petróleo Ipiranga S.A, Distribuidora de Produtos de Petróleo Ipiranga S.A. and Companhia Brasileira de Petróleo Ipiranga for the acquisition of their total interest in those companies, including petrochemical and distribution assets.

After the completion of the acquisition, the businesses of the Ipiranga Group will be managed by Ultrapar, Petrobras and Braskem. Ultrapar will hold 100% interest of the oil products and lubricant distribution businesses located in the South and Southeast regions of Brazil, Petrobras will hold 100% interest of the oil products and lubricant distribution businesses located in the North, Northeast and Central West regions of Brazil. Petrobras and Braskem will hold the petrochemical assets in the proportion of 60% and 40% respectively. The assets related to refining operations will be equally shared between Petrobras, Ultrapar and Braskem.

The conclusion of operation is estimated to occur during the fourth quarter of 2007. The transaction will occur in some fases including acquisitions and incorporation of shares, delisting of public companies in Brazilian Stock Exchange and segregation of the distribution and petrochemical assets.

The total value estimated for the operation is US\$4.0 billion and Petrobras will pay approximately US\$1.3 billion for its interest. The transaction will be presented for appreciation of the Brazilian Anti-trust Authorities (CADE Administrative Board for Economic Defense), the Secretary for Economic Rights and the Secretary for Economic Monitoring.

**PETRÓLEO BRASILEIRO S.A. - PETROBRAS  
AND SUBSIDIARIES****SUPPLEMENTARY INFORMATION ON OIL AND GAS EXPLORATION AND  
PRODUCTION ACTIVITIES (UNAUDITED)**

Expressed in Millions of United States Dollars  
(except when specifically indicated)

In accordance with SFAS 69 - Disclosures About Oil and Gas Producing Activities ("SFAS 69"), this section provides supplemental information on oil and gas exploration and producing activities of the Company. The information included in items (i) through (iii) provides historical cost information pertaining to costs incurred in exploration, property acquisitions and development, capitalized costs and results of operations. The information included in items (iv) and (v) present information on Petrobras' estimated net proved reserve quantities, standardized measure of estimated discounted future net cash flows related to proved reserves, and changes in estimated discounted future net cash flows.

Beginning in 1995, the Federal Government of Brazil undertook a comprehensive reform of the country's oil and gas regulatory system. On November 9, 1995, the Brazilian Constitution was amended to authorize the Federal Government to contract with any state or privately-owned company to carry out the activities related to the upstream and downstream segments of the Brazilian oil and gas sector. This amendment eliminated Petrobras' effective monopoly. The amendment was implemented by the Petroleum Law, which liberated the fuel market in Brazil beginning January 1, 2002.

The Petroleum Law established a new regulatory framework ending Petrobras' exclusive agency and enabling competition in all aspects of the oil and gas industry in Brazil. As provided in the Petroleum Law, Petrobras was granted the exclusive right for a period of 27 years to exploit the petroleum reserves in all fields where the Company had previously commenced production. However, the Petroleum Law established a procedural framework for Petrobras to claim exclusive exploratory (and, in case of success, development) rights for a period of up to three years with respect to areas where the Company could demonstrate that it had "established prospects". To perfect its claim to explore and develop these areas, the Company had to demonstrate that it had the requisite financial capacity to carry out these activities, alone or through financing or partnering arrangements.

The "International" geographic includes activities in Angola, Argentina, Bolivia, Colombia, Ecuador, Mexico, Nigeria, Peru, the United States of America, Venezuela, Iran, Lybia and Tanzania. The Company has immaterial non-consolidated companies involved in exploration and production activities; the amounts related to such are in the line item titled "Company's share of unconsolidated affiliates".

**(i) Capitalized costs relating to oil and gas producing activities**

The following table summarizes capitalized costs for oil and gas exploration and production activities with the related accumulated depreciation, depletion and amortization, and asset retirement obligation assets:

	<b>As of December 31, 2006</b>		
	<b>Brazil</b>	<b>International</b>	<b>Worldwide</b>
Unproved oil and gas properties	683	1,371	2,054
Proved oil and gas properties	23,967	4,240	28,207
Support equipment	13,851	454	14,305
Gross capitalized costs	<b>38,501</b>	<b>6,065</b>	<b>44,566</b>
Depreciation and depletion	<b>(14,979)</b>	<b>(1,902)</b>	<b>(16,881)</b>
Construction and installations in progress	<b>23,522</b>	<b>4,163</b>	<b>27,685</b>
	<b>10,457</b>	<b>273</b>	<b>10,730</b>
Proportional interest of net capitalized costs of equity companies	<b>33,979</b>	<b>4,436</b>	<b>38,415</b>
		<b>224</b>	<b>224</b>
Net capitalized costs	<b>33,979</b>	<b>4,660</b>	<b>38,639</b>

	<b>As of December 31, 2005</b>		
	<b>Brazil</b>	<b>International</b>	<b>Worldwide</b>
Unproved oil and gas properties	1,340	721	2,061
Proved oil and gas properties	18,734	4,374	23,108
Support equipment	10,755	1,034	11,789
Gross capitalized costs	30,829	6,129	36,958
Depreciation and depletion	<b>(14,378)</b>	<b>(2,463)</b>	<b>(16,841)</b>
Construction and installations in progress	16,451	3,666	20,117
	9,418	135	9,553
Net capitalized costs	25,869	3,801	29,670



**(ii) Costs incurred in oil and gas property acquisition, exploration and development activities**

Costs incurred are summarized below and include both amounts expensed and capitalized:

	<b>Year ended December 31, 2006</b>		
	<b>Brazil</b>	<b>International</b>	<b>Worldwide</b>
Property acquisitions			
Proved	-	86	86
Unproved	38	630	668
Exploration costs	1,752	430	2,182
Development costs	6,022	817	6,839
	<b>7,812</b>	<b>1,963</b>	<b>9,775</b>
Proportional interest of costs incurred of equity companies		24	24
	<b>7,812</b>	<b>1,987</b>	<b>9,799</b>

	<b>Year ended December 31, 2005</b>		
	<b>Brazil</b>	<b>International</b>	<b>Worldwide</b>
Property acquisitions			
Unproved	220	126	346
Exploration costs	1,741	420	2,161
Development costs	4,687	647	5,334
	6,648	1,193	7,841

	<b>Year ended December 31, 2004</b>		
	<b>Brazil</b>	<b>International</b>	<b>Worldwide</b>
Property acquisitions			
Unproved	156	17	173
Exploration costs	1,003	250	1,253
Development costs	3,591	404	3,995
	4,750	671	5,421





**(iii) Results of operations for oil and gas producing activities**

The Company's results of operations from oil and gas producing activities for the years ending December 31, 2006, 2005 and 2004 are shown in the following table. The Company transfers substantially all of its Brazilian crude oil and gas production to the supply segment in Brazil. The prices calculated by the Company's model may not be indicative of the price the Company would have realized had this production been sold in an unregulated spot market.

Additionally, the prices calculated by the Company's model may not be indicative of the future prices to be realized by the Company after January 1, 2002, when full price deregulation began. Gas prices used are contracted prices to third parties.

Production costs are lifting costs incurred to operate and maintain productive wells and related equipment and facilities, including such costs as operating labor, materials, supplies, fuel consumed in operations and the costs of operating natural liquid gas plants. Production costs also include administrative expenses and depreciation and amortization of equipment associated with production activities.

Exploration expenses include the costs of geological and geophysical activities and non-productive exploratory wells. Depreciation and amortization expenses relate to assets employed in exploration and development activities. In accordance with SFAS 69, income taxes are based on statutory tax rates, reflecting allowable deductions. Interest income and expense are excluded from the results reported in this table.

	<b>Year ended December 31, 2006</b>		
	<b>Brazil</b>	<b>International</b>	<b>Worldwide</b>
Net operating revenues:			
Sales to third parties	<b>3,351</b>	<b>684</b>	<b>4,035</b>
Intersegment (1)	<b>31,171</b>	<b>1,830</b>	<b>33,001</b>
	<b>34,522</b>	<b>2,514</b>	<b>37,036</b>
Production costs (2)	<b>(11,761)</b>	<b>(949)</b>	<b>(12,710)</b>
Exploration expenses	<b>(501)</b>	<b>(434)</b>	<b>(935)</b>
Depreciation, depletion, amortization	<b>(2,166)</b>	<b>(309)</b>	<b>(2,475)</b>
Impairment of oil and gas properties	<b>(20)</b>	<b>(1)</b>	<b>(21)</b>
Other operating expenses	<b>(22)</b>	<b>(3)</b>	<b>(25)</b>
Results before income taxes	<b>20,052</b>	<b>818</b>	<b>20,870</b>
Income tax expense	<b>(6,818)</b>	<b>(279)</b>	<b>(7,097)</b>
	<b>13,234</b>	<b>539</b>	<b>13,773</b>
Proportional interest in results of producing activities of equity companies	<b>-</b>	<b>20</b>	<b>20</b>
Results of operations (excluding corporate overhead and interest cost)	<b>13,234</b>	<b>559</b>	<b>13,793</b>



**(iii) Results of operations for oil and gas producing activities (Continued)**

	Year ended December 31, 2005		
	Brazil	International	Worldwide
Net operating revenues:			
Sales to third parties	1,874	920	2,794
Intersegment (1)	25,997	1,476	27,473
	27,871	2,396	30,267
Production costs (2)	(10,342)	(665)	(11,007)
Exploration expenses	(871)	(142)	(1,013)
Depreciation, depletion, amortization	(1,571)	(360)	(1,931)
Impairment of oil and gas properties	(11)	(134)	(145)
Other operating expenses	(29)	-	(29)
Results before income taxes	15,047	1,095	16,142
Income tax expense	(5,116)	(372)	(5,488)
Results of operations (excluding corporate overhead and interest cost)	9,931	723	10,654

	Year ended December 31, 2004		
	Brazil	International	Worldwide
Net operating revenues:			
Sales to third parties	2,308	713	3,021
Intersegment (1)	16,001	1,087	17,088
	18,309	1,800	20,109
Production costs (2)	(6,771)	(461)	(7,232)
Exploration expenses	(418)	(195)	(613)
Depreciation, depletion, amortization	(1,322)	(327)	(1,649)
Impairment of oil and gas properties	(51)	-	(51)
Other operating expenses	(41)	(64)	(105)
Results before income taxes	9,706	753	10,459
Income tax expense	(3,396)	(278)	(3,674)
Results of operations (excluding corporate overhead and			

interest cost)	6,310	475	6,785
----------------	-------	-----	-------

(1) Does not consider US\$1,216 (US\$953 for 2005) related to field processing activities, for which Petrobras has no attributable quantity of reserve. The amount, which relates principally to dry gas volumes, is considered in Petrobras' net operating revenues of US\$35,738 (US\$28,824 for 2005) for the segment of E&P Brazil (Note 23).

(2) Does not consider US\$1,873 (US\$985 for 2005) related to field processing activities, for which Petrobras has no attributable quantity of reserve. The amount, which relates principally to dry gas volumes, is considered in Petrobras' cost of sales of US\$13,634 (US\$11,327 for 2005) for the segment of E&P Brazil (Note 23).

**(iv) Reserve quantities information**

The Company's estimated net proved oil and gas reserves and changes thereto for the years 2006, 2005 and 2004 are shown in the following table. Proved reserves are estimated by the Company's reservoir engineers in accordance with the reserve definitions prescribed by the Securities and Exchange Commission.

Proved oil and gas reserves are the estimated quantities of crude oil, natural gas and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions. Proved reserves do not include additional quantities recoverable beyond the term of the concession or contract, or that may result from extensions of currently proved areas, or from application of secondary or tertiary recovery processes not yet tested and determined to be economic.

Proved developed reserves are the quantities expected to be recovered from existing wells with existing equipment and operating methods. Proved undeveloped reserves are those volumes which are expected to be recovered as a result of future investments in drilling, re-equipping existing wells and installing facilities necessary to deliver the production from these reserves.

In some cases, substantial new investments in additional wells and related facilities will be required to recover these proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of reserves are subject to change as additional information becomes available.

**(iv) Reserve quantities information** (Continued)

A summary of the annual changes in the proved reserves of crude oil and natural gas follows:

	Oil (millions of barrels)			Gas (billions of cubic feet)		
	Brazil	International	Worldwide	Brazil	International	Worldwide
<b>Worldwide net proved developed and undeveloped reserves</b>						
<b>Reserves at December 31, 2003</b>	<b>9,051.4</b>	<b>720.7</b>	<b>9,772.1</b>	<b>8,111.4</b>	<b>3,090.9</b>	<b>11,202.3</b>
Revisions of previous estimates	(414.9)	(18.8)	(433.7)	(262.1)	276.4	14.3
Improved recovery	50.2	13.2	63.4	13.2	26.8	40.0
Extensions and discoveries	1,079.1	47.4	1,126.5	569.4	89.7	659.1
Purchase of reserves in place - PEPSA	-	0.6	0.6	-	18.5	18.5
Production for the year	(522.4)	(61.1)	(583.5)	(477.6)	(209.5)	(687.1)
<b>Reserves at December 31, 2004</b>	<b>9,243.4</b>	<b>702.0</b>	<b>9,945.4</b>	<b>7,954.3</b>	<b>3,292.8</b>	<b>11,247.1</b>
Revisions of previous estimates	123.0	0.5	123.5	842.4	(32.6)	809.8
Improved recovery	1.1	(9.4)	(8.3)	6.9	0.2	7.1
Extensions and discoveries	250.9	47.8	298.7	990.0	38.6	1,028.6
Production for the year	(584.5)	(58.8)	(643.3)	(529.8)	(210.9)	(740.7)
<b>Reserves at December 31, 2005</b>	<b>9,033.9</b>	<b>682.1</b>	<b>9,716.0</b>	<b>9,263.8</b>	<b>3,088.1</b>	<b>12,351.9</b>
Interest loss in Venezuela	-	(240.5)	(240.5)	-	(171.2)	(171.2)
Revisions of previous estimates	463.4	(15.3)	448.1	322.1	(459.2)	(137.1)
Improved recovery	6.9	6.7	13.6	7.6	9.9	17.5
Acquisition of reserves	0.9	8.9	9.8	45.7	16.0	61.7
Sale of reserves	-	(4.5)	(4.5)	-	-	-
Extensions and discoveries	112.8	21.4	134.2	320.6	65.2	385.8
	(616.0)	(42.6)	(658.6)	(532.9)	(209.8)	(742.7)

Production for the  
year

<b>Reserves at December 31, 2006</b>	<b>9,001.9</b>	<b>416.2</b>	<b>(1)</b>	<b>9,418.1</b>	<b>9,426.9</b>	<b>2,339.0</b>	<b>11,765.9</b>	<b>(1)</b>
Proportional interest in net proved developed and undeveloped reserves of equity companies		65.7		65.7		77.3		77.3
<b>Net proved Developed Reserves</b>								
At January 1, 2003	3,912.9	94.7		4,007.6	3,892.5	2,043.9		5,936.4
At December 31, 2003	3,629.5	404.1		4,033.6	4,398.1	2,548.4		6,946.5
At December 31, 2004	4,129.8	383.1		4,512.9	4,427.6	2,495.2		6,922.8
At December 31, 2005	4,071.7	365.9		4,437.6	4,088.8	2,333.7		6,422.5
At December 31, 2006	3,987.7	232.9		4,220.6	4,115.4	1,758.0		5,873.4
Proportional interest in proved reserves of equity companies		36.7		36.7		43.1		43.1

(1) Includes reserves of 134.0 million barrels of oil and 504.8 billions of cubic feet of gas in 2006 (222.8 million barrels of oil and 550.6 billions of cubic feet of gas in 2005; and 228.6 million barrels of oil and 445.6 billions of cubic feet of gas in 2004) attributable to 41.38% minority interest in PEPSA, which is consolidated by Petrobras.



**(iv) Reserve quantities information** (Continued)

The decrease in reserves is related to revisions of previous estimates due to Bolivia and Venezuela new nationalization measures during 2006. The new regulation in Venezuela reduced our reserves as PDVSA became the main controller of the companies created to operate the fields with private companies. In Bolivia, due to new government regulations, occurred a decrease in the reserves. In Nigeria, the consortium in charge of Akpo field was constituted by Total, Petrobras and a Nigerian private company called SAPETRO. The agreement underwritten by these companies established that TOTAL and Petrobras carried the investment cost of the third part and it would be compensated in the future with SAPETRO's production/reserves.

Along 2006, SAPETRO sold its participation to a Chinese oil company and, as part of this agreement, Petrobras and TOTAL were reimbursed for their past carrying investments

**(v) Standardized measure of discounted future net cash flows relating to proved oil and gas quantities and changes therein**

The standardized measure of discounted future net cash flows, related to the above proved oil and gas reserves, is calculated in accordance with the requirements of SFAS 69. Estimated future cash inflows from production in Brazil are computed by applying year-end prices based upon the Company's internal pricing methodology for oil and gas to year-end quantities of estimated net proved reserves. Estimated future cash inflows from production related to the Company's International segment are computed by applying year-end prices for oil and gas to year-end quantities of estimated net proved reserves. Future price changes are limited to those provided by contractual arrangements in existence at the end of each reporting year. Future development and production costs are those estimated future expenditures necessary to develop and produce year-end estimated proved reserves based on year-end cost indicators, assuming continuation of year-end economic conditions. Estimated future income taxes are calculated by applying appropriate year-end statutory tax rates. These rates reflect allowable deductions and are applied to estimated future pre-tax net cash flows, less the tax basis of related assets. Discounted future net cash flows are calculated using 10% midperiod discount factors. This discounting requires a year-by-year estimate of when the future expenditures will be incurred and when the reserves will be produced.

The information provided does not represent management's estimate of Petrobras' expected future cash flows or value of proved oil and gas reserves. Estimates of proved reserve quantities involves uncertainty and change over time as new information becomes available. Moreover, probable and possible reserves, which may become proved in the future, are excluded from the calculations.

**(v) Standardized measure of discounted future net cash flows relating to proved oil and gas quantities and changes therein (Continued)**

The arbitrary valuation prescribed under SFAS 69 requires assumptions as to the timing and amount of future development and production costs. The calculations are made as of December 31 each year and should not be relied upon as an indication of Petrobras' future cash flows or the value of its oil and gas reserves.

	<b>Brazil</b>	<b>International</b>	<b>Worldwide</b>
<b>At December 31, 2006</b>			
Future cash inflows	477,051	24,691	501,742
Future production costs	(175,483)	(5,726)	(181,209)
Future development costs	(30,185)	(2,679)	(32,864)
Future income tax expenses	(93,914)	(7,051)	(100,965)
Undiscounted future net cash flows	177,469	9,235	186,704
10 percent midyear annual discount for timing of estimated cash flows	(83,582)	(3,566)	(87,148)
Standardized measure of discounted future net cash flows	93,887	5,669	99,556
Proportional interest in standardized measure of discounted future net cash flows related to proved reserves of equity companies	-	472	472
<b>At December 31, 2005</b>			
Future cash inflows	496,355	36,014	532,369
Future production costs	(170,638)	(7,339)	(177,977)
Future development costs	(25,934)	(2,946)	(28,880)
Future income tax expenses	(103,726)	(10,929)	(114,655)
Undiscounted future net cash flows	196,057	14,800	210,857
10 percent midyear annual discount for timing of estimated cash flows	(95,580)	(5,962)	(101,542)
Company's share by unconsolidated affiliates	-	61	61
Standardized measure of discounted future net cash flows	100,477	8,899 *	109,376
<b>At December 31, 2004</b>			
Future cash inflows	366,045	24,222	390,267
Future production costs	(131,090)	(4,003)	(135,093)
Future development costs	(19,315)	(2,224)	(21,539)
Future income tax expenses	(74,758)	(5,889)	(80,647)
Undiscounted future net cash flows	140,882	12,106	152,988
10 percent midyear annual discount for timing of estimated cash flows	(69,397)	(5,423)	(74,820)
Company's share by unconsolidated affiliates	-	121	121

Standardized measure of discounted future net cash flows	71,485	6,804 *	78,289
--	--------	---------	--------

(\* Includes US\$1,338 in 2006 (US\$2,379 in 2005 and U.S.\$1,774 in 2004) attributable to 41.38% minority interest in PEPSA, which is consolidated by Petrobras.

**(v) Standardized measure of discounted future net cash flows relating to proved oil and gas quantities and changes therein (Continued)**

The following are the principal sources of change in the standardized measure of discounted net cash flows:

	<b>Brazil</b>			<b>International</b>			<b>Worldwide</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
Balance at January 1	100,477	71,485	35,522	8,899	6,804	5,297	109,376	78,289	40,819
Sales and transfers of oil and gas, net of									
production costs	(22,761)	(17,529)	(11,538)	(1,505)	(1,731)	(1,339)	(24,266)	(19,260)	(12,877)
Development costs incurred	6,022	4,686	3,591	817	647	404	6,839	5,333	3,995
Purchases of reserves	-	-	-	101	-	73	101	-	73
Sales of reserves	-	-	-	(105)	-	-	(105)	-	-
Extensions, discoveries and improved less									
related costs	2,509	6,599	12,881	494	554	1,015	3,003	7,153	13,896
Interest loss in Venezuela	-	-	-	(1,305)	-	-	(1,305)	-	-
Revisions of previous quantity estimates	10,373	4,156	(4,892)	(1,825)	92	(58)	8,548	4,248	(4,950)
Net changes in prices and production costs	(12,698)	48,525	51,115	(976)	4,981	2,042	(13,674)	53,506	53,157
Changes in future development costs	(5,274)	(9,405)	(292)	(749)	(658)	(504)	(6,023)	(10,063)	(796)
Accretion of discount	10,048	7,148	3,552	1,006	994	739	11,054	8,142	4,291
Net change in income taxes	5,191	(15,188)	(18,454)	817	(2,784)	(865)	6,008	(17,972)	(19,319)
Balance at December 31	93,887	100,477	71,485	5,669	8,899	6,804	99,556	109,376	78,289
Proportional interest in standardized measure of discounted future net cash flows related to proved reserves of equity companies				472			472		

## SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: April 09, 2007

PETRÓLEO BRASILEIRO S.A--PETROBRAS

By:           /s/ Almir Guilherme Barbassa          

**Almir Guilherme Barbassa**  
**Chief Financial Officer and**  
**Investor Relations Officer**

## FORWARD-LOOKING STATEMENTS

This press release may contain forward-looking statements. These statements are statements that are not historical facts, and are based on management's current view and estimates of future economic circumstances, industry conditions, company performance and financial results. The words "anticipates", "believes", "estimates", "expects", "plans" and similar expressions, as they relate to the company, are intended to identify forward-looking statements. Statements regarding the declaration or payment of dividends, the implementation of principal operating and financing strategies and capital expenditure plans, the direction of future operations and the factors or trends affecting financial condition, liquidity or results of operations are examples of forward-looking statements. Such statements reflect the current views of management and are subject to a number of risks and uncertainties. There is no guarantee that the expected events, trends or results will actually occur. The statements are based on many assumptions and factors, including general economic and market conditions, industry conditions, and operating factors. Any changes in such assumptions or factors could cause actual results to differ materially from current expectations.

---