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EFFECTIVENESS OF PRODUCTION SHARING CONTRACTS IN INDIA

This dissertation is submitted in partial fulfillment of the degree of B.A., LL.B. (Hons.)



College of Legal Studies

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CERTIFICATE

This is to certify that the research work entitled “**EFFECTIVENESS OF PRODUCTION SHARING CONTRACTS IN INDIA**” is the work done by Ms. Loveleen Singh under my guidance and supervision for the partial fulfillment of the requirement of B.A., LL.B. (Hons.) at College of Legal Studies, University of Petroleum and Energy Studies, Dehradun.

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DECLARATION

I declare that the dissertation entitled “Effectiveness of Production Sharing Contracts in India” is the outcome of my own work conducted under the supervision of Prof. Raj Kumar, at College of Legal Studies, University of Petroleum and Energy Studies, Dehradun.

I declare that the dissertation comprises only of my original work and due acknowledgement has been made in the text to all other material used.

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ABBREVIATIONS

CG Central Government

E&P Exploration and Production

EEZ Exclusive Economic Zone

EIA Environment Impact Assessment

FDI Foreign Direct Investment

GoI Government of India

IT Income Tax Act 1961

IOC International Oil Companies

JOA Joint Operating Agreement

JV Joint Venture

LNG Liquefied Natural Gas

MOPNG Ministry of Petroleum and Natural Gas

MOEF Ministry of Environment and Forest

MPSC Model Production Sharing Contract

MC Management Committee

NOC National Oil Company

OC Operating Committee

OIL Oil India Limited

ONGC Oil and Natural Gas Corporation

PSC Production Sharing Contract

PNGRB Petroleum and Natural Gas Regulatory Board

PEL Petroleum Exploration License

PML- Petroleum Mining Lease

PI Participating Interest

RSC Revenue Sharing Contract

SG State Government

VAT Value Added Tax

ACKNOWLEDGEMENT

The writing of this dissertation has been one of the most significant academic challenges I have ever had to face. Without the support, patience and guidance of the following people, this study would not have been completed. It is to them that I owe my deepest gratitude.

- Mr. Rajkumar who undertook to act as my supervisor despite his many other academic and professional commitments. His wisdom, knowledge and commitment to the highest standards inspired and motivated me.
- Dr. Tabrez Ahmed, Director CoLS, who accorded me the opportunity to undertake this study and facilitated the completion of this research work by providing the necessary guidance.
- No research is possible without the Library, University of Petroleum & Energy Studies. I take this time to express my gratitude to all the library staff for their services.
- My classmates, who have always supported, encouraged and believed in me, in all my endeavours.

CHAPTER 1

ORIGIN OF PRODUCTION SHARING CONTRACTS

1.1 Background

In the context of Economic Development of the country and Energy Security, the role of petroleum and petroleum products as a vital fuel will continue to be there though with a changing face. To address the worldwide needs and request over next 20-30 years and past, generous increment in Energy Research particularly in Hydrocarbon Sector is discriminating¹. The high capital investment is needed for profoundly indeterminate picks up and additionally a need to depend on foreign innovation for precise exploration and production activities. Oil and gas enactments shifts in every nation, they rely on upon the reason and the expectation of controlling the nation's vital assets. Notwithstanding, the primary goals of every State gathering are the same, to take control of its assets and to get income for the monetary development. To create and to make utilization of its assets, the State will collaborate with International Oil Companies (IOCs) which has the capacity, information and involvement in this industry².

The reception of a compelling administration for petroleum development is firmly affected by the geographical prospects of a nation and the innovative and budgetary assets required for exploration and production of hydrocarbons³. By requiring substantial capital investments and sophisticated technical skills, petroleum developments are often beyond the resources possessed by most governments but are likely to be provided by experienced multinational oil companies. In order to secure the objectives and priorities of host governments and, cumulatively, provide sufficient encouragement to foreign investors, a coherent regime must be selected, bearing in mind the particular circumstance of the country concerned⁴. Notwithstanding, examples can be found in appreciation of the received administrations: Western industrialized nations have

¹ Dr. Neeraj Anand, *Contemporary Issues in Energy Sector* (1st Edn.), Technology Publications, Dehradun, 2009.

² Richard D. Seba, *Economics of worldwide petroleum production* (2nd Edn.), OGCI, 2003

³ *Id*

⁴ Shilpa Kannan, *Foreign Investment in Indian Oil Exploration waning*, BBC News, 26 May 2011, at <http://www.bbc.co.uk/news/business-13559082>.

ordinarily settled an administration in view of licenses, while creating nations take after risk contracts, most solely production sharing agreements (PSAs)⁵.

There are two essential contract sorts between the State and IOCs. Firstly is by giving concession licenses to the IOCs and furthermore is by making contractual game plan between the State and the IOCs, which is generally known as Production Sharing Contract⁶.

1.2 Historical Background of PSC

The thought of the state sharing production of oil and gas with companies as a major aspect of a business endeavor was initially grown in Bolivia in the 1950s. The Production Sharing Contract (PSC) was presented in Indonesia in 1966 and PSCs are currently utilized generally to record plans for oil and gas exploration and production, especially in developing nations; today, they are utilized as a part of more than 40 nations, incorporating in Africa, Central Asia and South-East Asia⁷. The PSC is not by any means the only way by which a state may allow oil and gas exploration and production rights to business speculators. Before the development of the PSC, exploration and production of oil and gas was normally represented by method for a license or a concession, and these administrations stay in numerous jurisdictions.

Regardless, in making nations, the PSC is shortly the most generally perceived means by which state licenses business incorporation in the oil and gas industry and in various districts there are political purposes behind their appointment. Case in point, taking after Indonesian self-governance in 1945, the concessions organization went under strike by loyalist bundles. This over the long haul incited the Indonesian government declining to permit new concessions, which doubtlessly provoked a diminishing in outside enthusiasm for Indonesia's oil and gas region⁸. To stop this decrease, the government presented new enactment which accommodated production sharing game plans; such courses of action were generally thought to be less dubious

⁵ Pongsiri, Nutavoot. *Partnerships in oil and gas production-sharing contracts*. (Centre on Regulation and Competition (CRC), University of Manchester, UK, 2002), pp. 432.

⁶ Johnston, Daniel. *International petroleum fiscal systems and production sharing contracts* (Tulsa, Okla. : PennWell Books, c1994), pp. 39.

⁷ Machmud, Tengku Nathan. *The Indonesian Production Sharing Contract: An Investor's Perspective*. (Kluwer Law International (2000)), pp. 62.

⁸ Bindemann, Kirsten. *Production Sharing Agreements*. (Oxford Institute for Energy Studies WPM 25, 1999), pp. 1.

than the past concessions framework, as they empowered the government to keep up formal ownership of the assets being referred to, while licensing the private sector to adventure them .

Petroleum as an advantage of essentialness expects a crucial part in the change of economy of any country. This has incited development and development of unmistakable contracting practices on the planet as the years progressed. Production Sharing Agreements (PSAs) are amongst the most remarkable sorts of contractual arrangements for petroleum exploration and headway. Under a PSA the state as the administrator of mineral assets attracts a foreign oil companies (FOC) as a contractor to present particular and budgetary organizations for exploration and development operations. The state is expectedly identified with by the organization or one of its workplaces, for instance, the national oil companies (NOC). The FOC gets a case to a stipulated offer of the oil conveyed as a prize for the risk taken and services rendered. The state, regardless, remains the supervisor of the petroleum delivered subject just to the contractor case to its share of production. The governing body or its NOC normally has the choice to contribute in diverse parts of the exploration and headway process. Likewise, PSAs reliably show for the establishment of a joint advisory group where both sides are addressed and which screens the operations.

The important Production Sharing Contract (PSC) was stamped in 1966 in Indonesia. No not as much as 50% of host governments now use era giving contracts organization. PSCs are at usage in, Libya, Oman, Qatar, India, Bahrain, North Korea, China Indonesia, Philippines, Sudan et cetera. The area may possibly be given at unmistakable stages to the contractor⁹. It could be conceded at a stage when no exploration work has been done or coming about to some exploration work. Such grounds or squares are known as Exploration Acreage or Blocks. There could be land in which revelation of oil or gas has been made. Such grounds are perceived as Discovered Fields or fundamentally Fields¹⁰. In India PSC are in operation for Exploration Blocks, Small and Marginal Fields and Medium Size Fields. The PSC contains conditions for picking as to progression program, assessment framework and general offering of oil or gas on

⁹ Graham and Trot man, International petroleum contracts: Current trends and New directions, International Energy and resource law and policy series, London, 1994, pp257.

¹⁰ Supra.n.1.

the reason of a formula given in the PSC¹¹. In 1960, Law No. 44 was agreed in Indonesia giving that oil associations will be known as "contractors" instead of "concessionaires". The Western Oil Companies were amazingly bothered and a ton focused because of its probable impact on Middle East concessions. The associations working in Indonesia declined to recognize this law.

Transactions failed and Government of Indonesia asserted that in case agreements did not go to the associations will be nationalized. In this establishment and after the mediation of USA, a comprehension was come to by which these associations were approved to endure on the operations under an "Agreement of Work" game plan¹². The offering of production and control under a production sharing contract was not assented to by noteworthy oil associations working in Indonesia yet when some Japanese and American independents went into such contracts and others trailed in like manner. So after 1970, the things were settled and another period of Joint Ventures of oil companies with the host government began. In India, PSC joins the charging of Petroleum Exploration License expenses and royalty and additionally sharing of benefit oil left after cost recovery. Subsequently it is the mixture of both the concessionary and production sharing administration.

1.3 Historical Background of Exploration & Production in India

In the first half of 19th century, the Indian oil/gas industry traced some initial discoveries in north-eastern region of Assam. In 1830, first oil seepage in the hills near Assam-Arunachal Pradesh Border was found. In 1867, Asia's first mechanically drilled oil wells were drilled in Makum (Assam). In 1889, the first commercial discovery of crude oil was made in Digboi, Assam by "The Assam railways and trading company"¹³. ONGC explored new prospects in Assam, Cambay basin, Assam Arakan fold belt and east cost basin¹⁴. During early seventies, ONGC discovered a giant oil field named Bombay High. In 1970's Indian oil and gas industry were largely nationalized as government took over the operations of Caltex and Burma Shell and

¹¹ Chukwuma Samuel Adesina Okoli, "Production sharing agreements and licences: a distinction without a difference?", *International Energy Law Review*, 2012, Vol 8, p. no. 282-285.

¹² See Petrofed, *Review of E&P Licensing Policy*, 73-75 available at <http://petrofed.winwinhosting.net/upload/Part3.pdf>.

¹³ supra n. 1.

¹⁴ Piyush Joshi, *Law relating to infrastructure projects (2nd Edition)*, LexisNexis Butterworths Wadhwa, Nagpur 2012.

formed a national oil company named OIL. The dominant players in the Indian E&P sector have traditionally being the NOC's operating in this sector, ONGC and OIL.

Petroleum exploration and production was controlled by the Government-possessed National Oil Companies (NOCs, ONGC and OIL) in compatibility of the Industrial Policy Resolution, 1954. They discovered noteworthy amounts of oil and gas saves. In the mid 70s, they supplied almost 70% of the household necessity. However before the end of 80s, they had come to the phase of unavoidable losses. Oil generation had started to decrease though there was an enduring increment in utilization. The Government had no cash to provide for the NOCs for the improvement of a percentage of the newfound fields and the issue had components, for example, the directed oil costs, non-accessibility of suitable innovation, logistics and so on.¹⁵

1.3.1 Petroleum Sector Reforms, 1990

Given the fairly discouraging situation on the monetary and unrefined yield fronts, the government dispatched the Petroleum Sector Reforms (PSR) in 1990. Till then (1990) three rounds of exploration bidding had been experienced with no achievement in discovering new oil/gas stores by the foreign companies who just were permitted to bid¹⁶.

Under the PSR, the fourth, fifth, 6th, seventh and eighth round of exploration period were reported somewhere around 1991 and 1994. Surprisingly Indian companies with or without past involvement in E&P exercises were authorized to bid beginning with the fourth round. The NOCs had conveyed enthusiasm of upto 30% after business disclosures were made. Most companies felt this to be obstruction. The government then declared the Joint Venture Exploration Programmed in 1995. The exploration blocks were in those zones for which the petroleum exploration license was with the NOC'S and they were obliged to have a 25% to 40% partaking enthusiasm from the very first moment¹⁷. By and by this was seen as an obstacle by a few majors who felt that 25% to 40% of the normal benefits would be lost to the NOC's¹⁸. It was clear that the majors needed that blocks be cut out of ranges held by the NOC's with the

¹⁵ *Id*

¹⁶ *Supra.n.14.*

¹⁷ Analysis of the Taxation of of Petroleum crude and natural gas in India, National institute of Public Finance and policy(NIPFP), Tropical and current issues reviews and reports, Sept 2006

¹⁸ *Id*

stipulation that each of these blocks ought to have no less than one oil disclosure in it and further that the NOCs ought to have no value holding in the blocks. Regularly this was excessively for the NOCs to process they didn't consent to withdraw from the regions held by them. At last, blocks bided prior and not honored were re-bided with a couple of new blocks under NELP. An

In 1992, the government of India chose to permit private support in the upstream fragment of the oil and gas industry and chose to hand more than a few medium and little size found and created oil and gas fields to joint endeavors structured between chose private members and ONGC, the Government of India organization that attempts upstream section exercises. Then again it took the Government around 5 years to form and receive an exhaustive exploration licensing strategy the New Exploration Licensing Policy regularly called the NELP was reported in the fiscal year 1997-98.

Preceding the NELP, nine rounds of bidding methodology were attempted with the initial three being held between the time of 1980-1986 and through and through ten blocks were recompensed yet exploration did not yield any oil and gas disclosure. Since 1991, India has been welcoming bids from private companies all the time with six rounds of bidding completed before the NELP.

CHAPTER 2

EVOLUTION OF NELP

2.1 PRE- NELP

Pre independence 1866-1947

- The exploration of hydrocarbons in India started in 1866 when Mr. Goodenough of Mckillop Steward Co. bored a well close Jaipur in upper Assam and struck oil.
- First business oil revelation in 1889 at Digboi.
- In 1893 rights were allowed to the Assam oil syndicate to erect a little refinery at Margharita which prompted the development of Assam Oil Company (AOC) in 1899.

1947-1960

- After autonomy the administration of India (GOI) understood the significance of oil and gas for quick modern advancement keeping in mind encircled the mechanical policy explanation of 1948.
- Top need for advancement of petroleum organizations.
- Indo-Stanbac venture a joint wander between administration of India and Standard Vaccum Oil Company of US in 1953 gave the first oil revelation of autonomous India close Naharkotiya.
- In 1955 GOI created ONGD (oil and characteristic gas directorate) with the assistance of GSI (land overview of India).
- From 1958 ONGC began its exploration in

Himalayan foothills- Ganga fields

b. Alluvial tracks of Gujarat

c. Upper Assam and West Bengal

d. Cambay Basin

1961-1991

- In 1962 trial seismic overviews were done in the Gulf of Cambay.
- Also Western seaward Survey subtle elements brought about Bombay seaward India's greatest business disclosure.
- In 1990, business oil revelations by (Oil India constrained) in Rajasthan and in Assam in 1991.
- ONGC Videsh Ltd. (OVL) was shaped with a perspective to embrace the abroad exploration and generation exercises for the benefit of ONGC.

After 1991

The changed money related methodology balanced by the organization of India in July 1991 attempted to deregulate and de-permit the middle regions (checking petroleum division) with midway disinvestments of government esteem out in the open part tries and distinctive measures. Taking after this, ONGC was revised in February 1994 as a compelled association under the Organizations Demonstration .

Post-liberalization, a couple of barricades of trustees were arranged for investigating distinctive suggestion for remaking and imagining frameworks to meet the challenges of the new financial environment. Amongst the notable report was the Rangarajan Panel report in February 1995

which upheld deregulation of the petroleum business at one stroke. Of course, the key masterminding gathering on reconstructing of the Indian oil industry, the "R" Party, headed by the then petroleum secretary Dr. Vijay Kelkar felt the condition should be in an organized manner.

A board was launched in 1992 under the Chairmanship of P.K Kaul, past Bureau Secretary, to take a gander at the need of revamping the ONGC. This board proposed the setting up of a body with the name and style of the DGH (Directorate General of Hydrocarbons), for discharging the managerial limits of leasing and approving, wellbeing and environment moreover progression, assurance and store organization of hydrocarbon resources. In like way, DGH was arranged up by a Government determination in April 1993 through which certain announcement and regulatory parts were depended however no headway part was named.

Oil moreover traveled to another country and picked up a 20% sharing energy for the generation imparting contract for the Block IV in Oman through a farm in simultaneousness with Aggregate FINA of France. It also included in the exploration organization contract for the Farsi thwart in Iran close by OVL and Indian Oil Company Ltd.

In 1997 the GOI, remembering the deciding objective to enliven pace of private cooperation in the country, confirmed the New Exploration Licensing Policy (NELP) by giving different appealing monetary and contractual terms .

Before the NELP, the oil fields (regulation and improvement) act and Petroleum and common gas standards dealt with the issue of permit and PSU's. Under the advanced methodology winning around then, exploration pieces were awaited for exploration and creation just to national oil associations. ONGC and OIL were the primary open section associations included in exploration and creation till 1997 while IOCL was the fundamental substance concerned with refining and changing oil after extraction .

Exclusive organizations had entrance to hydrocarbon resources going before the NELP just through joint try arrangements went into with Government, as opposed to finish bolster through

an offering system. These Joint attempt arrangements considered required collaboration of the GOI through the national oil associations.

In 1986 despite offering exploration pieces (Nomination premise) to national oil associations, the Government opened up the imparting of oil and gas acreages to private speculators, including remote financial specialists .

National oil affiliations had the choice of taking 30% offering fervor for a prenelp contract at the time of a business disclosure, such that they would meet their proportionate offer of improvement and generation costs and also an extra 10% working energy for any square they picked, with 10% exploration charges being borne by them. Foremen were obliged to offer the whole give of oil social occasion to them as appraisal oil to the Government of India amidst this Pre- NELP contract stage.

- The prenelp contracts were for a period of up to 25 years, if there should be an occurrence of unrefined petroleum and related gas extendable by an additional 5 years.
- An exploration time of a most noteworthy of 7 years.
- The builders would need to surrender 25% of the agreement range to administration of India toward the end of the first time of exploration and a further a large portion of the first contract zone toward the end of the second exploration stage.
- Pre-NELP builders were not committed to pay mark or creation reward or any sovereignty on generation and were totally exempted from custom obligation commitments and distinctive charges on imports required for petroleum operations.
- Income expense occasion for a seven years time from the time of business disclosure.
- Royalty under prenelp period was settled at 10% of the wellhead regard;

- The Taxability of exploration and creation activities was determined on the reason of fragment 42 of the Income Tax Act, 1961
- Companies going into unincorporated joint endeavors were obligated to Corporate salary charge half at a large portion of the assessable wage emerging from such ventures.
- 100% use gained on exploration and creation activities was deductible;
- Any stamp obligation payable in energy about the PSC used to be borne by Government.

2.1.1 WHY NELP?

Purposes behind presentation of NELP are:-

1. Extensive sedimentary ranges stayed unexplored in the country.
2. Expanding interest supply bend.
3. Necessity of expansive capital speculation
4. Early use of sensible & suitable advancement.
5. Necessity for accelerating in existing leads & commercialization and improvement of existing disclosures.
6. Just 28 PSCs could be granted under diverse rounds to Pvt/JV organizations in 11 years under Pre-NELP rounds.
7. Level playing field between the NOCs and Pvt. /JV E&P associations.
8. NELP introduced powerful monetary and contractual terms, which are one of the best till now.

2.2 Hydrocarbon Vision 2025

The Vision clarification was point by point in the year 1999 with the objective to make clarity and specific organizing in the progression process for the hydrocarbon fragment, and moreover to make a guide that associate's Indian approach on the Hydrocarbon division up to the year 2025. The specific proposals of the vision for progressing upstream part incorporate :

- To keep pace with innovative progression and application and be at the creative bleeding edge in the overall exploration and creation industry.
- To continue with exploration underway bowls.
- Finalize a framework for assessment of the Indian sedimentary bowls to the level of 25% by 2005, half by 2010, 75% by 2015 and 100% by 2025.
- Provide globally aggressive financial terms, keeping in view the relative tentatively impression of Indian bowls, so as to draw in real oil and gas organizations and through quick assessment of offers and recompense of agreement on a period bound premise.
- Continue development obtainment and maintenance nearby advancement of indigenous Exploration & Advancement (Research and improvement).
- Ensure sufficiency of trusts for Research and advancement required for building data establishment.
- Make E&P operations perfect with nature so as to abatement discharges and releases.
- Acquire acreages abroad for exploration and creation.

2.3 New Exploration Licensing Policy

The Government of India embraced the New Exploration Licensing Policy (NELP) in the year 1997. The central objective of NELP was to give an assistance to exploration and creation practices in the upstream portion and attract private enthusiasm for the part. The plan framework gave a level playing field to the nearby open division, exclusive organizations and outside associations by imparting near regulatory, monetary and contractual terms for exploration and generation of oil and gas. This was a huge change from the prenelp organization under which ONGC and OIL were permitted with "Petroleum Exploration Lease" on a determination premise. Under NELP, the associations were rewarded licenses for exploration discourages on the reason of overall centered imparting. With a particular final objective to keep up more vital straightforwardness in the imparting process, the gift of squares is made on the reason of quantitative offer appraisal criteria, which are made open in the notice inviting offers.

2.4 Main concurrences with Government Governing Private Participation in E&P

The contractual structure between the private cooperation and the administration nearing due to NELP, for private backing in the E&P bit can be portrayed as takes after:-

- The picked individuals need to go into an assention, termed as the Joint Operating Agreement (JOA) in association with the exploration of the oil field. This assention is implied as Joint Operating Agreement.
- The picked consortium needs to go into a concurrence with the Union of India, under which the unincorporated joint try is given the benefit to grasp exploration and generation activities and a specific rate of the oil and gas made by the appropriate field is gotten by the Union of India, at a predestined expense. This assention is insinuated as Production Sharing Contract.
- A mining lease must be procured and kept up by the picked consortium to be vested with the specific right to grasp the mining activities in regards to the noteworthy oil and gas field.

2.5 FISCAL REGIME UNDER NELP

Royalty administration

Eminence, under NELP, is pegged to the business estimation of generation at wellhead as under:

- For Crude Oil it is settled at 12.5% for ashore and 10% for seaward
- For Natural Gas, it is settled at the rate of 10% for ashore and seaward
- Special impetus for deepwater pieces (i.e. past 400 misobath) - half of the above seaward sovereignty rates for the initial 7 years.

Income charge administration

The Indian Income Tax ('Act') gives extraordinary procurement to taxability of upstream organizations. Area 42 of the Act records downs the permit capacity of specific classifications of use as are determined in the PSC:

- Expenditure by method for in fructuous or failed exploration
- Expenditure caused for exploration or boring exercises or administrations or resources utilized for these exercises

It further gives that such stipends might be registered and made in the way as indicated in the PSC, and alternate procurements of the Act being considered for this reason to have been altered to the degree important to offer impact to the terms of the PSC. Likewise, for such sort of consumption, one needs to analyze the significant procurements of the PSC.

Article 17 of the Model PSC accommodates the accompanying particular remittances in registering the assessable wage of the E&P organizations:

- Exploration and boring use, both capital and income in nature, is 100% assessment deductible.
- Expenditure acquired on improvement and generation exercises (other than penetrating use) is permitted according to the procurements of the Income assessment Act ("the Act")

- All exploration and boring use is permitted to be totaled till year of initiation of business creation. Then again such consumption may be amortized just as over a 10-year period from begin of business generation. The builders might pay sovereignty at the rate of 10 percent promotion valorem deal worth at the well head.

□ Domestic assessment laws

The foreman under NELP is obliged to pay burdened under Indian Income expense Act, 1961. The expansive procurements under residential duty laws are highlighted as beneath:

a) Corporate assessment rates

The household organizations will be at risk to expense at 33.66% (counting additional charge of 10% and cess of 2%) while remote organizations will be subject to assessment at on their business pay at 41.82% (counting additional charge of 2.5% and cess of 2%).

Ensuing, profit spilling out of the Indian organization to its outside guardian is likewise subject to a Dividend Distribution Tax in India of rate of 14.025% (counting extra charge of 10% and cess of 2%).

b) Tax Holiday

The Act accommodates a 7 year salary expense occasion to an endeavor occupied with E&P exercises from the date of beginning of business generation. Despite the fact that the above seems, by all accounts, to be a sensible, for all intents and purposes, it is nonetheless, watched that the genuine benefit of assessment occasion does not stream to E&P organizations given the extensive exploration consumption which is to be situated off amid the same period. It along these lines requires a further adaptability in profiting the expense occasion period by the E&P organizations.

b) Minimum Alternate Tax

The Act accommodates installment of least substitute expense ("MAT"). MAT is payable at the rate of 7.5% of balanced book benefits, by organizations whose salary expense processed under ordinary procurements, is under 7.5% of book benefits. Endeavors occupied with the exploration and creation of mineral oils, which generally appreciate an assessment occasion, keep on being

liable to require of MAT actually amid the duty occasion period. The credit for expenses paid under MAT has been reintroduced and the same will be accessible for steal forward and set away for 5 consequent years.

2.6 Reasons behind the failure of NELP in the country

The Ministry of Petroleum and Natural Gas wanted to decrease the quantity of squares to less numbers as contrasted and before rounds. The thought is to have less pieces with a high caliber of information," an oil service official said on state of obscurity. "This will bring about higher support from the exploration and creation (E&P) firms."

1. Production Sharing Contracts

There are different sorts of squares in NELP i.e. seaward (Shallow and Deep Water) and onland (S sort squares). There is a certifiable necessity for change and changes in the creation offering contracts. There ought to appear as something else sort of creation offering contract for different sorts of square as the danger included, and the different methods are unmistakable for each piece. Each square has unmistakable essentials, issues, perils which can't be had a tendency to by one model generation offering contracts. Accordingly the Investors oftentimes surmise that it difficult to adjust under such circumstances. There are various issues relating to the comprehension of the Production Sharing Contracts .

2. Duty concerns

In barely a second there is a Seven years Tax occasion in the NELP. Yet there are number of obligation related concern in the NELP which is reliably securing financial specialists from placing assets into the NELP. The administration has additionally neglected to receive an obvious policy on broadening the expense occasion for the oil and gas division. There is authenticity in these solicitations of the oil division given that foremen need to rebate all utilization obtained in exploration if they disregard to make a disclosure. Costs are recoverable exactly when foreman make a business revelation. The oil service has perceived 34 pieces to be emptied under the ninth offering round, or Nelp-IX. Oil minister Murli Deora is passed by London to meet potential financial specialists. The move will in like manner settle the issue of

yielding cost events for making standard gas, two organization powers with direct data of the matter said however in spite of all that they have not uncovered anything regarded the time of obligation event .

Starting late there was another issue when the Finance Ministry's decided to scrap a seven year obligation event on NELP gas yield (which was realized before the last approving round) was one of the key obstructions to monetary pros. India's 2008-09 Finance Bill communicated that the importance of "mineral oil" did reject trademark gas which drove the Finance Ministry to invalidate the cost event, in spite of the way that it stayed set up for grungy petroleum. Given that a lot of India's land is more pending for gas than for oil, the scrapping of the pay obligation event had a noteworthy impact on NELP VIII, particularly on squares thought to be high in gas potential, for instance, those in the Andaman Sea. Abrogating the obligation in like manner suggested tinkering with the terms of Production Sharing Contracts (PSCs), making precariousness among speculators .

CHAPTER 3

OTHER FORMS OF MINERAL OIL CONTRACTS

The business objective of an oil company is to earn a reasonable return on its investments by entering into contractual relationships with appropriate parties which enable it to prospect for and produce oil and/or gas in areas that it determines to be prospective¹⁹. The various types of mineral oil contracts entered between the state and contracting parties are:-

3.1 Oil and Gas Leases

Under this agreement, there is little degree for an IOC to arrange customized game plans in connection to its exploration and production rights. Licensing regimes are regularly institutionalized and implanted in enactment, such that the terms of every license are indistinguishable. This administration is most basic in developed nations e.g. UK, Norway, the Netherlands, Australia. The IOC is regularly allowed complete control over the agreement range and complete responsibility for oil and gas it effectively creates. Not at all like PSCs, where responsibility for assets dependably stays with the State, in license administrations possession for the most part goes at the wellhead, with benefits subject to general assessment enactment²⁰.

In the United States and Canada where private responsibility for and gas is conceivable, the Oil, Gas and Mineral (Lease) is the essential contract under which all petroleum is produced. The lesser awards exclusive right to go into the area with the end goal of prospecting for oil and/or gas, separating and evacuating same²¹. While there are a substantial number of Lease structures being used, most have genuinely unsurprising terms.

The organization pays a money thought to the mineral manager for marking the Lease and normally is obliged to make yearly installments called postponement rentals to keep up the Lease without operations or production. Leases can be for any time span, yet the normal term is five years in many territories of the United States, ten years in remote or less dynamic zones. Amid the presence of the Lease, the organization may bore one or more wells on the property, or

¹⁹ Frank C. Alexander, "Production Sharing Contracts and Other Host Government Contract" OGEL Vol. 3 - issue 1 March 2005.

²⁰ A. Konoplyanik, "The Fight against PSAs in Russia: who is to benefit and why not the State?"(2003) I.E.L.R. p. no. 277-279.

²¹ *Id.*

consolidate the Lease into a creating unit with different Leases²². In the event that the organization is fruitful in accomplishing production, the Lease will by and large stay as a result for the term of the delivering period. The generation must be nonstop and, while it doesn't need to return a benefit to the administrator, must be a decent confidence exertion from the administrator to keep up the beneficial limit of the well or wells. The organization is in charge of making all uses regarding operations identified with the exploration and abuse of the assets from the Lease. The mineral manager is never at danger for such consumptions. Consequently the resident will pay the mineral manager a segment of the returns from offering oil and/or gas called a royalty. The resident is qualified for the rest of, a working investment, and from this sum the renter will recuperate all taxes and benefits²³.

Leases must have genuinely unsurprising terms to make them industrially significant for the renter. Regularly, there are numerous varieties of the fundamental terms of Leases, however the ideas of reward, royalty, essential term, and coherence the length of production endures are pervasive to all Leases. If a lessor is represented by counsel, or is a sophisticated lessor and thoroughly familiar with the terms of Leases, the royalty provisions and other parts of the Lease may become very complex²⁴.

3.2 International Agreements

Allowing reports utilized as a part of different nations (Contracts) are not almost as uniform. In most Western European nations, the license is utilized; in the Middle East, the concession is broadly utilized; production imparting contracts (PSC) are basic in Africa and Asia; and administration contracts are predominant in Central and South America. In spite of the fact that these Contracts may vary in approach, all give the system which gives the organization the privilege to go into the range, drill for petroleum, and if effective, to deliver and offer the production²⁵. Really, the significant qualification between the different sorts of Contracts is that concession contracts, and their descendants, consider the direct responsibility for by the organization, either set up (getting to be uncommon) or at the wellhead, while administration understandings, including PSCs, don't.

²² Barrows, 'CNOOC Offshore Fourth Round Model Contract,' *World Petroleum Arrangements* (1995).

²³ US Natural Gas Markets: Mid term prospects for natural gas supply, Energy Information Administration, Department of Energy 2001.

²⁴ *Supra.n.13*.

²⁵ Keith W. Blinn *et al.*, *International Petroleum Exploration & Exploitation Agreements* 22-23 (1986).

a) **Concession Agreements**

A concession agreement is for the most part subject to a more noteworthy level of transaction than a license. The IOC is commonly conceded exclusive rights over the agreement range and complete responsibility for oil and gas it effectively creates, subject to the installment of a sovereignty and salary assess (each of which may shift in rate relying upon the level of production) .Concession understandings have a hefty portion of the same procurements as Leases utilized as a part of the United States, which is not shocking following the concession contract was the first kind of petroleum understanding used by oil organizations in the beginning of universal exploration²⁶. Concessions come in numerous structures relying upon the specific nation, however all will contain these significant components:

- 4 The organization will have exclusive exploration and production rights.
- 5 The organization will own and dispose of the production.
- 6 The organization will pay surface rentals amid the exploration and exploitation stages.
- 7 The organization pays a royalty in kind or money to the State.
- 8 The organization pays charges on benefits got from its operations.
- 9 Equipment and installations utilized as a part of operations fit in with the organization.
- 10 There will be a mandatory work program with a definite time schedule.

Concessions are generally called 'tax and royalty' contracts since that is their most particular highlight. The concession understandings being used today are truly not quite the same as prior adaptations²⁷. Concession periods have been abbreviated extensively and the agreement regions have been definitely diminished. Organizations are presently needed to utilize huge quantities of remote nationals in their work power. Yet the greatest change has been the State's recovered control over operations²⁸. Early concessions gave the organization very nearly aggregate control over operations; however present day concessions now give the State noteworthy instruments to practice operational control, including value cooperation. Concessions are likely the most regularly utilized giving instruments as a part of the world and are utilized as a part of most OPEC nations, the United Kingdom, France, Norway, Thailand, Morocco, Australia, and more

²⁸ *Id.*

than one hundred different nations. It is an attempted and-genuine framework that has the preference that it meets expectations. To assuage the host country's discontent with the passive role it had been relegated to, most modern concessions now grant the State a participating interest in the Contract and have adjusted the taxing provisions applicable to the project so that States feel they are being adequately compensated for the exploitation of their natural resources.

b) Production Sharing Contracts

The Production Sharing Contract, or PSC, evolved as a reaction by host countries to maturation of their national goals and a willingness to regain authority of their natural resources²⁹. Pioneered by Indonesia, and now used in countries as diverse as Egypt, Libya, the Philippines, Malaysia, Peru, Trinidad, Kenya, the Ivory Coast, Equatorial Guinea, among others, most PSCs have the following basic features:

- The company is appointed as a contractor for a certain contract area.
- The company operates at its sole risk and tax under the control of the State.
- Production belongs to the State.
- The company is entitled to recover its costs out of production.
- After cost recovery, the balance of production is subject to a production split between the company and the State.
- Income tax is payable by the company.
- Equipment and installations become the property of the State.
- There is an obligatory work program with a definite time schedule.

An important feature of a PSC, as compared to a concession, is that ownership and control of production remains in the State³⁰. 'The contractor does not acquire title to its share of the petroleum until the oil reaches the export point or a mutually agreed delivery point, thus the contractor's rights are of a purely contractual nature. This fundamental change in legal positions in a PSC between the company and the State has enabled States to continue to grant valuable exploitation rights of its natural resources to foreign companies while maintaining control over the resource itself³¹.

³⁰ *Id.*

³¹ Muttitt, "Production Sharing Agreements: Oil Privatisation by Another Name?", p.5.

c) Risk Service Contracts

Under a service contract, the IOC gives its specialized services to the State to explore and produce oil and gas assets thus from numerous points of view it is like a PSC. The idea is fundamentally in light of straightforward equation: the contractor is paid a money expense for performing the service of delivering mineral assets. All production has a place with the government. The contractor is normally in charge of giving all capital related exploration and advancement of petroleum assets. Consequently, if exploration endeavors are effective, the government permits the contractor to recuperate those costs through offer of the oil or gas and pays the contractor a charge that is typically in view of the rate of the remaining incomes. This expense is regularly subject to taxes, and it is fundamentally the same to a PSC³².

Since the contractor does not get an offer of production, such terms as production sharing and benefit oil are not proper despite the fact that the number-crunching will frequently cut out an offer of incomes in the same manner that a PSC offers production³³.

Then again, remuneration to the IOC is generally by technique for an organization cost or portions considering the estimation of oil made. The term of an organizations contract is frequently short, leaving an IOC with amazing risk and no protection of a long production period (notwithstanding the way that we observe that organizations contracts may similarly be on a non-risk premise). Services contracts are basic in Iran, Iraq and Kuwait and have additionally been utilized occasionally as a part of Indonesia. Service Contracts, or Risk Service Contracts, are like PSCs as in the foreign organization is consigned to the part of contractor, yet they go much further in removing the contractor from ownership of the production. Service Contracts have numerous procurements like PSCs, yet are recognized by the way that the contractor is paid in trade instead of in for money kind. This is the main reason why Service Contracts have not been favored by international oil companies who are interested in locking in supplies to feed their

³² Taverne, "Production Sharing Agreements in Principle and Practice" in M.R. David (ed.), *Upstream Oil and Gas Agreements* (1996), pp.82-86.

³³ Risk service agreements tend to be adopted in countries with low exploration and production costs and high reserves (see Abdulaziz Alattar and Osamah Alomair, "Evaluation of Upstream Petroleum Agreements & Exploration and Production Costs" Oil, Gas & Energy Law Intelligence (June 2005).

downstream business units³⁴.

³⁴ Nakhle, *Petroleum Taxation Sharing the Oil Wealth: a Study of Petroleum Taxation Yesterday, Today and Tomorrow* (2008), p.46.

CHAPTER 4

MEANING AND RATIONALE BEHIND PSC

4.1 What is PSC?

A Production Sharing Contract (PSC) is a contractual administration entered into by the Government and the Contractor with the end goal of E&P of hydrocarbon assets, specifically, crude oil and natural gas. The Petroleum and Natural Gas Report of the Committee on the PSC Mechanism in Petroleum Industry Rules, 1959 accommodate an agreement between the Government and the licensee or tenant, to set out the terms and conditions concerning the license or lease. PSCs are currently the overwhelming mode of hydrocarbon organization in the nation.

4.2 Legal basis of PSC

The lawful premise for the Government of India to go into a PSC for the exploration and production of oil and gas from oilfields is:

- a) Article 297 of the Constitution of India (for offshore fields)
- b) Oilfields (Regulation and Development) Act 1948 (for onland and offshore fields)
- c) Authorization of Central Government under section 12, Oilfields (Regulation and Development) Act 1948 allowing for grant of mining lease on terms unique in relation to those stipulated in the Oilfields (Regulation and Development) Act 1948

4.3 The basic features of Production Sharing Contracts are:-

- The company is appointed as a contractor for a certain contract area.
- The company operates at its sole risk and tax under the control of the State.
- Production belongs to the State.
- The company is entitled to recover its costs out of production.
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1.4 Rationale behind PSC model

Petroleum advancement administrations are frequently intended to secure a complex scope of destinations and needs. While industrialized oil-creating nations' prime targets are to diminish their reliance on different states for vitality supplies and augment incomes (as an establishment for different approaches), other applicable goals may be brought up, especially with respect to developing nations. Normally portrayed by an economy subject to modest and unstable oil incomes, building up nations' needs are to expand the government control over operations, create national capacities in the oil segment and, eminently, upgrade monetary development. Regardless, remembering that they normally do not have the capital, innovation and prepared staff needed for petroleum operations, sufficient motivating forces need to be given to the business division to put resources into the nation and trust petroleum exercises³⁵. All things considered, developing countries seek to enhance two fundamental but, at certain extent, competing objectives: secure state control over production and protect foreign investment in the oil sector.

Having at the top of the priority list the aforementioned destinations, developing nations ordinarily want to enter with remote oil organizations into service contracts, by and large, and PSAs, specifically, instead of granting licenses. The contrasts between these lawful plans are of a calculated nature and lie on the level of control conceded to the outside contractor, remuneration courses of action and, fundamentally, responsibility for. In expansive terms, a license may be characterized as a managerial consent approving one or more qualified legitimate or common persons to direct a movement which would somehow be unlawful. Under a license, title to

³⁵ Hossain, *Law and Policy in Petroleum Developments, Changing Relations between Transnationals and Governments* (1979), p.111.

petroleum is transferred to the licensee if and when it is produced, the state receives compensation mainly by means of royalties and taxes and the investor has most of the control over the organizational and managerial aspects of operations³⁶.

On the other hand, a PSA can be extensively portrayed as an agreement between an oil company (contractor) and a state party (traditionally a national oil company) authorizing the former to carry out petroleum operations within a contract area. Taxes and risks of exploration and advancement are borne by the contractor who, by method for pay, gets an bid of the oil created, as per the procurements of the understanding. In spite of the fact that exercises are done by the contractor, the state party regularly regulates operations through a working board of trustees, comprising of delegates of both sides³⁷.

Ultimately, not all that ordinarily utilized, risk service agreements bid with PSAs the same contractual nature yet contractor's compensation is destined to be paid in real money³⁸. Subsequently, they have met some resistance from oil organizations, who incline toward PSAs as, at any rate, a prepared access to a block of the production methodology is given.

Generally speaking, considering the most often utilized courses of action, it is significant that the principle distinction between a PSA and a license is a greater amount of lawful nature and lies on the responsibility for regular assets. While under the recent all petroleum delivered is procured by the licensee, under the previous it is claimed by the host government, since the bid of production dispensed to the contractor at the "point of transfer" is regarded as a compensation for the risk and services taken³⁹.

Despite the eagerness and political acknowledgement indicated by developing nations for PSAs, as state's responsibility for is held and (from a certain point of view) further control over operations is given, the ampleness of a legitimate plan for petroleum development must be determined under the exact terms of the contract put forward with the host government.

³⁶ Ernest E. Smith and John S. Dzienkowski, *Materials on International Petroleum Transactions*, 2nd edn (Denver, Colorado: Rocky Mountain Mineral Law Foundation, 2000), p.55.

³⁷ *Id.*

³⁸ Nagla Nassar, *Sanctity of Contracts Revisited: A Study in Theory and Practice of Long-Term International Commercial Transactions*, (Martinus Nijhoff Publishers, 1995), p.134.

³⁹ Smith and Dzienkowski, *Materials on International Petroleum Transactions* (2000), p.55.

India embraced PSC demonstrate keeping in mind the end goal to welcome both remote and Indian organizations and to pull in speculation and most recent innovation in the upstream hydrocarbons division. The PSC model was thought to be more dynamic as Management Committee constituted under it bided a suitable discussion for consistent collaboration between the Government and contractors. Contractors were given representation on MCs, with every organization constituting the contractor being spoken to through a part on the MC. What's more, there Report of the Council on the PSC Component in Petroleum Industry are two Government chosen people on the MC⁴⁰. Accordingly, the PSC model was made operational through an arrangement of joint administration⁴¹. Government's share of profit petroleum structures some block of Government receipts and is credited under different bookkeeping head worked revenue driven petroleum. Then again, cost recuperation made by the contractor is considered to be use brought about on exploration. According to ordinances of monetary respectability, all costs from Government records ought to be made with the most extreme care keeping in mind watching money related judiciousness⁴². If there should arise an occurrence of costs under the PSC, the contractor is licensed complete recovery of tax petroleum, which diminishes the bid of Government in profit petroleum. Hence, there is a requirement for watchful checking of costs acquired. PSC is an extraordinary manifestation of subsoil utilization relations in light of common lawful contractual standards for dealings between a state and a investor regarding prospecting, exploration and extraction of mineral assets⁴³. PSC is an agreement compliant with which the state (manager of the subsoil) endows the investor to direct prospecting, exploration and extraction of mineral assets inside the cutoff points of a characterized subsoil zone on a repaid premise and for a made time period amid which the investor is certain to perform the demonstrated work at its own particular cost and own risk.

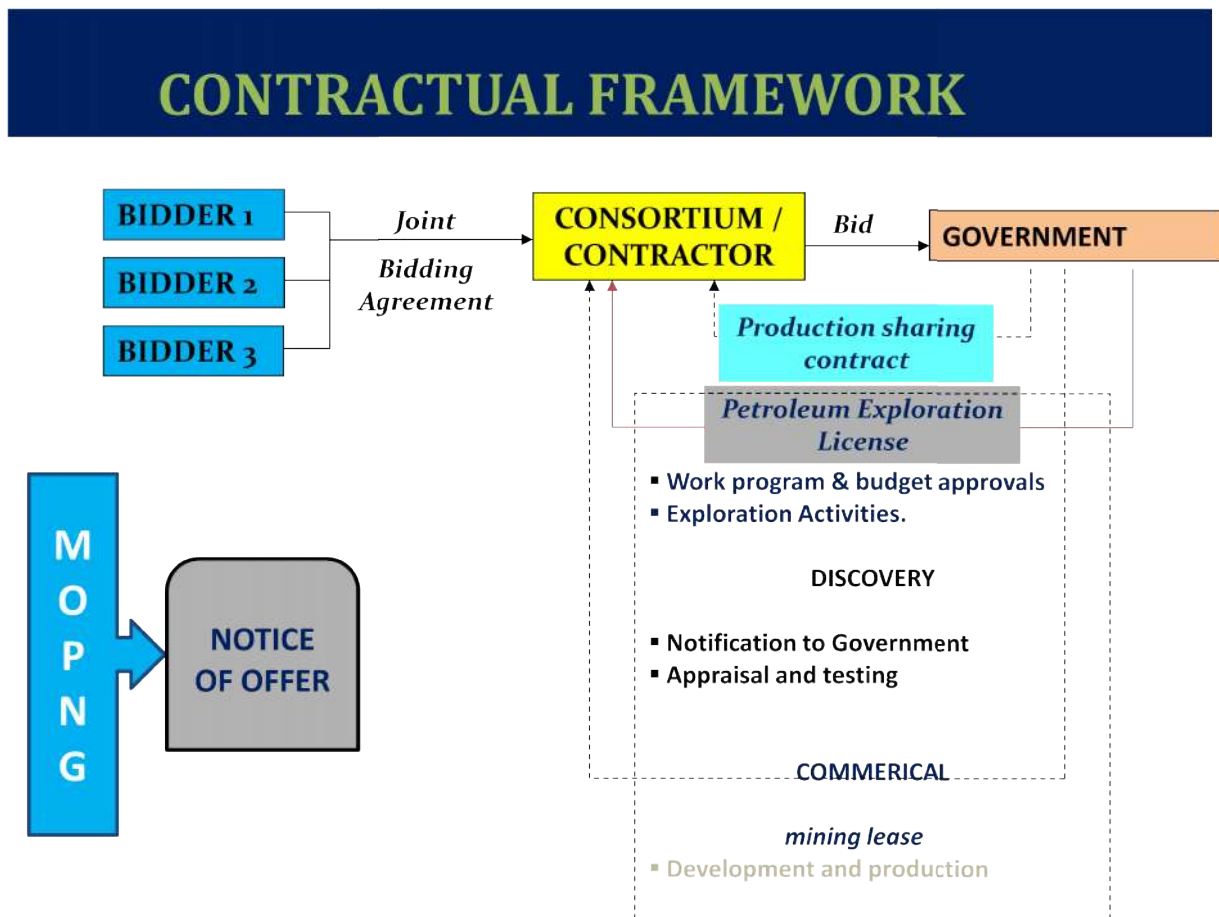
⁴⁰ Kristen Bindemann, "Production Sharing Agreements: An Economic Analysis", Oxford Institute for Energy Studies, WPN 25, October 1999, p.9.

⁴¹ Greg Gordon, "Petroleum Licensing" in Oil and Gas Law--Current Practice and Emerging Trends, 2nd edn (Dundee University Press, 2011), p.67.

⁴² *Id.*

MODEL OF PRODUCTION SHARING CONTRACTS

Figure 1. The diagrammatic representation of the production sharing contract



4

Fig 1. Model of production sharing contracts

How's production sharing contract entered into?

1. MOPNG draws out an bid called the notification of bid which has all the points of interest of the zones to be put on bided for development, exploration and production of oil.
2. Since this is an enormous venture and nobody organization has the funds to do it courageously so there will be joint sharing. That is there will be no less than 2-3 bidders in every

understanding. In this bid they will introduce their eventual fate of that specific asset range. This is known as a "consortium."

3. When this bid is submitted to the administration; it inspects the bid and acknowledges one consortium for every block put on the bid.

4. When the bid is acknowledged, they go into a Production Sharing Contract (PSC) with the Govt. Now this contract mentions the share of the bidders of the consortium and all other required details. This PSC is a Book of scriptures. On the off chance that there is any debate they allude to the PSC for determination.

5. Presently they need to seek a petroleum exploration license (PEL). The license is allowed under The Oilfields (Regulation and Development) Act, 1948 and the Petroleum and Natural Gas Governors, 1959. Without this license they can't begin any upstream exercises (exploration and production of oil) in the block apportioned to them. The MOPNG will give this license and proceeding this bidder needs to get consent from the state government additionally, i.e., from the particular state.

6. When they get the PEL they can begin the upstream exercises.

7. Once the disclosure is made then they need to educate the government of the same. The government will then send an uncommon group they could call their own to test the revelation by method for its quality and so forth and after that it should allot a specific quality confirmation to it.

8. At long last they can begin business production. For this they additionally need to get a mining lease from the government and MOPNG. This lease is usually for 20 yrs.

Basic Distinguishing Characteristics of PSCs

The essential recognizing qualities of a PSC from different sorts of a common lawful understanding are situated forward beneath.

1. The Subject of a PSC, the subject of the given contract is the concurred project of the party for the extraction of mineral assets which must be satisfied by the investor for the state. Such

program incorporates the sort, taxes and time of execution. As such, the state has contracted the investor as a contractor to perform the work imagined by the project.

Subsequently, contractual relations emerge between two legitimately rise to party, each having rights and commitments, the infringement of which should involve their legitimate obligation. The State employs the investor as a contractor for the behavior of work associated with the extraction of helpful minerals. In the meantime, it takes onto itself the commitment to exchange to the investor for utilize the subsoil range determined as a part of the agreement. In the greater part of nations on the planet, the subsoil has a place with the state. The state has an imposing business model over the utilization of the subsoil and the expulsion from it of common assets. The allowing to an investor of elite rights means that the state amid the time of PSC's legitimacy, is committed to avoid on the given subsoil region from action included in the volume of the exchange red rights and not allow such movement from third persons.

2. The State as a party to a PSC as a common law contract is finished up between lawfully measure up to parties: the state and a investor. All conditions for utilization of the subsoil and the execution of work is built by the parties by common agreement. Regardless, one needs to consider that the state taking an interest in the agreement jelly its state privileges⁴⁴. Consequently in relations for subsoil utilization emerging on the premise of a PSC, the state demonstrations in two parts: from one perspective it satisfies its commitments under the agreement, and then again it jam its state open lawful capacities. These parts may meet or clash with one another. In their outline, one ought to be guided by the accompanying rule: inside the extent of conditions gave by the agreement, the state and the investor are equivalent accomplices, outside such extension - the state settles on choices identified with subsoil use on a definitive, regulatory law premise.

3. The Movement of an Investor at its Own Cost and Risk The investor does the exercises imagined in the agreement (prospecting, inquiry, exploration, extraction and different works) at its own particular cost and risk. The state, as the other party to the agreement does not manage any costs or risks. In the event that the investor puts supports in the prospecting and exploration however did not find any minerals, or found that their extraction would be monetarily unfruitful, the exhausted stores should not be discounted to the investor. This is an essential rule of a PSC. The parties, then again, may concur something else.

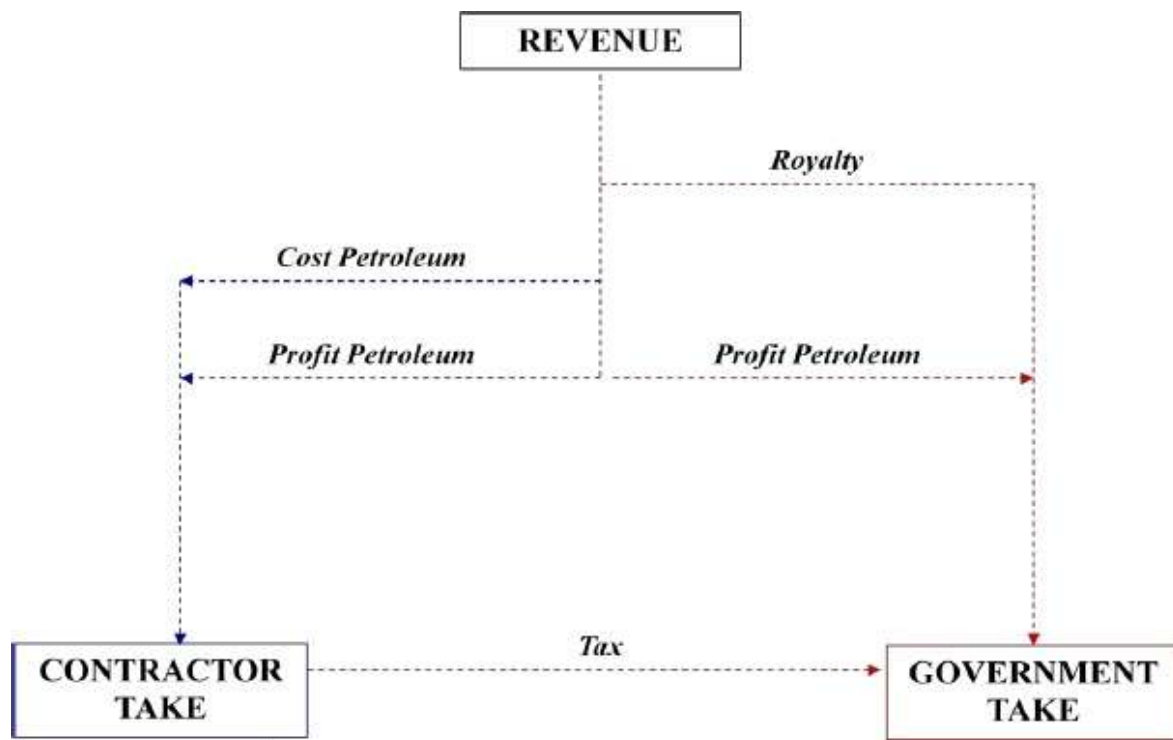
⁴⁴ *Id*

4. Ownership of Product Produced under a PSC and the Contractor Nature of an Investor under a PSC

. Under a PSC, the state exchanges to the investor just elite rights to lead movement including a subsoil zone, however does not exchange rights to such subsoil region into either possession or lease. In this manner, all extricated minerals or removed and transformed minerals (i.e., the delivered item) are the property of the state. The state contracts the investor as a contractor to perform work for it, yet to the detriment and risk of the investor. The work is done on a repaid premise, with the state paying the investor not in cash, yet with a bit of the delivered item. This is the alleged production sharing, i.e., the sharing of the consequences of the work completed by the investor.

5. The Sharing of product: Substance and Methodology Production sharing is the central part and the principle recognizing normal for a PSC. This standard really gave the agreement its name. With a specific end goal to focus the volume of the extricated crude materials and to do production sharing, the idea of the "purpose of estimation" is utilized - a self-assertive point identified with the development of removed crude materials indicated by the parties in the agreement (the mouth of the pole, the conveyance point, and so forth.). At the purpose of estimation all the crude materials being extricated is the property of the state. The production sharing is additionally completed at the same point and as a rule takes after the accompanying strategy:

- From the item delivered by the investor is divided that part that goes toward the pay of the investor's consumptions (cost –recovery item);
- That a block of the created item that remaining parts (profit item) is separated between the investor and the state in an extent gave in the PSC



6. PSC and Levy Amid exercises on the premise of a PSC, a unique tax regime is utilized for the investor. Inside the time of legitimacy of the PSC, the current state charges and other compulsory installments are supplanted by a block of the profit item. They are contemplated while drafting a consent to focus the block of the item created by the investor which stays in the responsibility for state. Evidently, no assessment profits are conceded to investors. The current duty framework is essentially supplanted by production partaking on account of the utilization of a PSC. Production sharing between the state and the investor is done on the premise of standards decided in every particular contract⁴⁵. There are two known frameworks for substitution of assessment by production sharing:-

- complete substitution of taxes by a block of profit item (for instance, in Libya, the state partitioned the delivered items in the middle of itself and the investor in the extent 81:19 without requiring any assessments or taxes);
- partial substitution, when all the while with production sharing is imagined the imposing of specific charges (for instance, in Russia profit tax and taxes for subsoil utilization are demanded, and in Indonesia - wage assessment and a profit duty are imposed).

⁴⁵ Dr. Irina Paliashvili, Production Sharing Agreements, September 14,1998, available at http://www.rulg.com/documents/The_Concept_of_Production_Sharing.htm.

Therefore, the PSC idea, from one viewpoint, ensures the premiums of the state, and on the other - makes the investor invulnerable from the changing assessment strategy of the state. Production sharing makes another technique for subsoil use, as a distinct option for the ordinary duty framework, as per which singular attributes of subsoil utilization are considered on a contractual premise in every PSC⁴⁶.

CHAPTER 5

KEY OPERATIONAL CLAUSES UNDER PSC

An abnormal state of organization across over PSCs is clear and a broad number of model structure agreements exist transversely over purviews in Africa, Central Asia and South-East Asia. Where this is the circumstance, the model structure has reliably been used as a starting stage or perspective, with conformities coming to fruition in light of plans between the IOC and state concerned noted. This part gives a strange state outline of the key terms ordinary to PSCs, and a chart of the key authentic issues rising up out of such acquisitions. Right when surveying a PSC, it is a key to consider not simply the tongue in which the terms themselves have been restricted, also to consider what material terms may have been tossed.

5.1 Parties

The parties to a PSC will constantly be a NOC, a government or a Minister representing to the State, from one viewpoint, and an IOC, on the other. It is basic for there to be a consortium of IOCs, who are by and large characterized in the agreement as "the Contractor"⁴⁷. In a few nations, the State is additionally a party to the PSC notwithstanding the NOC.

⁴⁶ *id*

⁴⁷ IOC and a consortium of IOCs collectively refered as "the Contractor", and the state entity or entities, whether the NOC, government or Minister representing the state as "the State".

5.2 Start date

The parties' commitments under a PSC starts on the "effective date"⁴⁸ which implies the later of the date on which this Contract is executed by the Parties or the date of issue of License or date from which License has been made compelling by the Central Government or State Government(s) as the case may be.

This can be an altered date, and it is characterized as the date of execution of the understanding. It can likewise be controlled by the event of a specific occasion, for example, the date on which the agreement is sanctioned by the State. The effective date means the start of the investigation stage and in this manner shows when the Contractor's exploration commitments begin.

5.4 Work Program

The contractor might begin petroleum operations not later than six months from the powerful date. Notwithstanding the bid work program responsibility in first exploration stage, the contractor should be obliged to embrace and complete the 2D seismic API, in framework size of the figures measured covering the whole contract region amid first exploration stage.

Amid the cash of second exploration stage the contractor might finish the work program which incorporates a seismic project comprising of the procurement, transforming and translation of the seismic information in connection to the exploration destinations. On the off chance that the base work program for the second exploration stage has been finished sooner than eighteen months from the end of the stage, the contractor should meet the government to talk about the likelihood of ahead of schedule surrender, unless the contractor attempt further work with the approbation of management committee .

5.5 Management Committee

Another regular highlight of a PSC is a management committee (otherwise called a operating committee or a joint operating committee), which has obligation regarding, amongst different things, facilitating and regulating the operations, checking on and supporting all work projects and plans, and investigating and endorsing proposition for surrender and relinquishment⁴⁹.

⁴⁸ Article 1.40, MPSC

⁴⁹ Article 6.2, MPSC.

Government might select two individuals representing the Government in the management committee, though every organization constituting the contractor should choose one member each to speak to organization in the Management Committee provided that in the event that the contractor constitutes one organization should have two individuals⁵⁰. The party shall designate the individuals to the management committee within thirty days of the effective date. The following matters might be put together by operator for the benefit of the contractor with the approval of operating committee⁵¹:-

- Annual work program and budget plans in respect of advancement operations and creation operations and any changes or modifications.
- Determination of development region
- Appointment of auditors alongside the extent of audits, approval and selection of audited reports.
- Collaboration with licenses or contractors of different regions.
- Claims or settlement of cases for or for the benefit of or against the contractor in abundance of points of confinement altered by the management committee now and then.
- Proposal about abandonment plan.

Unless concurred by all the individuals from the management committee, the panel should meet in any event once during the exploration period and from there on at any rate once at regular intervals or all the more as often as possible at the request of any individual⁵².

5.5 Joint Operator Agreements (JOA)

For the most part, the Contractor will be accountable for operations under the agreement; notwithstanding, where the Contractor is a consortium of IOCs, one of the IOCs is normally designated as the operator and completes this part for the benefit of itself and the other Contractor parties. The operator may be designated by the Ministry, or the Contractor may have the privilege to name the operator subject to the State's earlier endorsement. The transmit of the operator is situated out in a different agreement, known as a joint operating agreement (which will likewise administer the relationship all the more for the most part between the Contractor

⁵⁰ Article 6.4, MPSC.

⁵¹ Article 6.5, MPSC.

⁵² Article 6.7, MPSC.

and the operator), which may be attached to the contract. The operator's transmit is by and large wide, and incorporates obligation regarding the arrangement of work projects and plans, directing exploration, evaluation and development operations, and keeping up the vital protection The PSC commands that the said agreement might be steady with the procurements of the PSC and should accommodate not to mention a variety of other things⁵³:-

- The arrangement, acquiescence, evacuation and obligations of the operator
- The foundation of an operating committee embodying a concurred number of agents of the companies led by a delegate of the operator
- Functions of the said operating committee considering the procurements of the contract, strategies for choice making, recurrence and spot of gatherings
- Contribution to costs, default, sole risk, transfer of petroleum and task as between the gatherings to the operating agreement.

The operating agreement that is so entered between the individuals from the chose consortium is alluded to as "Joint Operating Agreement".

The principle issues for the most part secured by JOA are:-

- Participating interest: it will obviously stipulate the particular rate of interest that each of the individuals from the consortium has in the operations under PSC. The taking an interest demonstrates the degree of commitments and in addition the privileges of every member inside the consortium.
- Operator: it will cover the distinguishing proof of the Operator, the rights and obligations of the operator, the degree of data that the operator is obliged to give to the non operator individuals, the degree of obligation of the operator and the method for changing the operator and the arrangement of the successor operator.
- Operating Committee: Provisions of the JOA identifying with the operating committee will cover the sythesis of the operating committee, the forces and obligations of the operating committee, capacity to constitute sub committees, the way of choice making the voting technique and the system for holding gatherings of the operating committee⁵⁴.

⁵³ Article 7.2, MPSC

⁵⁴ *Id.*

- Work plans and budgets: the JOA will accommodate the strategy for forming work plans and plans in connection to the joint operations under the PSC. This will incorporate procurements in connection to exploration and evaluation of information, the development of another disclosure, technique for honor of sub-contracts and structure for control of use in connection to operations.
- Disposal of production: it will accommodate the structure as per which the gatherings can arrange their offer of the productions if any, from any new revelation made by the exploration activities embraced by the consortium.
- Transfer of participating interest: It would give a structure administering the way in which the individuals from the consortium can exchange/offer/appoint their partaking intrigue and way out the consortium⁵⁵.
- Applicable law: It will set out the law that parties have decided to oversee the JOA

5.6 Protection of Environment

The sole commitment that must be satisfied under the agreement is to bear on the investigation and generation exercises by utilizing cutting edge oilfield and petroleum industry practices and measures including propelled procedures, practices and systems for operation for the avoidance of Environmental Damage in directing its petroleum operations, which may sound like a solid procurement however extremely questionable. It accommodates the most essential statement of PSC i.e. Article 14 which is identified with the assurance of environment amid the work program for investigation and creation of hydrocarbons. It incorporates three stages which are:-

- **Site restoration:** It shall mean all exercises needed to give back a site to its state as of the Effective Date compliant with the Contractor's ecological effect concentrate on and sanction by the Government or to render a site good after-utilization (to the degree reasonable) after suspension of Petroleum Operations in connection thereto and should incorporate, where proper, legitimate surrender of Wells or other facilities, removal of equipment, structures and trash, foundation of perfect contours and seepage, substitution of top soil, re-vegetation, slant adjustment, in-filling of

⁵⁵ Article 7.2,MPSC.

excavations or some other suitable activities in the circumstances⁵⁶. The contractor shall submit proposition about site reclamation including a surrender arrangement. A yearly commitment is to be made by the gatherings in the site reclamation trust acting in consonance with the procurements of Site Restoration Fund Scheme 1999⁵⁷.

The contractor is additionally needed to cause an individual or persons with extraordinary learning in ecological matters to do natural effect studies and to submit, for thought, techniques and measures for doing site rebuilding exercises⁵⁸. The contractor is the needed to tell the legislature, in composing, the measures and routines so controlled by the contractor and such strategies are measures are liable to survey now and again in the light of winning circumstances. Once the contract is terminated or the contract area is to be relinquished, the contractor shall perform all necessary operations for site restoration in accordance with modern oilfield and petroleum industry practices and should try in a best possible manner to prevent any hazard to life, property of another as well as the surrounding environment⁵⁹.

- **Environment Impact assessment:** It is an activity to be completed before undertaking an action for guaranteeing that the movement attempted is not going to damage nature in any capacity on a short or long haul premise. An EIA focus on issues, clashes and common asset imperatives which may influence the reasonability of a task. It additionally predicts how the task could damage to individuals, their country, their livelihoods, and the other close-by formative exercises. In the wake of foreseeing potential effects, the EIA recognizes measures to minimize the effects and proposes approaches to enhance the venture practicality. "Environment" in EIA setting fundamentally concentrates, yet is not restricted to physical, compound, organic, geographical, social, temperate, and stylish measurements alongside their complex cooperation's, which influences people, groups and at last decides their structures, character, relationship, and survival. In EIA connection, "impact" and "effect" can regularly be utilized reciprocally. On the other hand, "effect" is considered as a quality judgment of the importance of an impact. Maintainable advancement is based on three essential premises i.e., monetary

⁵⁶ *Id*

⁵⁷ Article 6.6 (g), MPSC.

⁵⁸ Article 14.4, MPSC.

⁵⁹ Yousif K. Kharaka and Nancy S. Dorsey, *Environmental Issues of Petroleum Exploration and Production: Introduction*, available at <http://toxics.usgs.gov/pubs/KharakaIntro.PDF>.

development, biological equalization and social advancement. Monetary development attained to in a manner that does not consider, the ecological concerns, won't be manageable over the long haul.

*“It is necessary to understand the links between environment and development in order to make choices for development that will be economically efficient, socially equitable and responsible, as well as environmentally sound.”*⁶⁰

- **Contingency plan** The requirement of making an Oil Spill Contingency Plan (OSCP) is mandated because of the Indian Government commitments to the United Nation’s conventions on Oil Spills and its response, enforced by its marine arm, viz. International Maritime Organization (IMO)⁶¹. The OSCP gives the method, activity and the data required for an association to react to any oil slick starting because of its exercises. In the meantime, it can likewise help in offering backing to any neighboring association confronting the spill reaction issue. MPSC lawfully ties the builder to structure and present an OSCP before starting any operations on the oil or characteristic gas square. The relevant portion of the aforementioned section has been produced below⁶²:

The Contractor might, before directing any boring activities, plan and submit for audit by the Government emergency arrangements for managing Oil spills, flames, mischance and crises, intended to attain to quick and viable crisis reaction. The arrangements alluded to above should be talked about with the Government and concerns communicated might e considered. In the occasion of a crisis, mischance, Oil spill or flame emerging from Petroleum Operations influencing nature, the Contractor might forthwith inform the Government and should expeditiously actualize the significant alternate arrangement and perform such Site Restoration as may be fundamental as per current oilfield and petroleum industry hones. In the occasion of whatever other crisis or mischance emerging from the Petroleum Operations influencing nature,

⁶⁰ IL&FS Ecosmart Ltd., Hyderabad, Technical EIA Guiding manual for offshore and onshore oil and gas Exploration, Development and production; August 2010, P.No.2.v

⁶¹ Eleodoro M. Alba, *Environmental Governance in Oil Producing Developing Countries*, World Bank, Extractive Industries for Development Series (2010) available at http://siteresources.worldbank.org/EXTOGMC/Resources/3369291266963339030/eifd17_environmental_governance.pdf.

⁶² Article 14.7, MPSC.

the Contractor should make such move as may be reasonable and vital as per cutting edge oilfield and petroleum industry rehearses in such circumstances.

CHAPTER 6

KEY LEGAL AND FISCAL CLAUSES UNDER PSC

6.1 Legal clauses

The PSC gives an included framework to the control and supervision of the activities relating to the exploration, disclosure, development and production of grungy petroleum/basic gas and related hydrocarbons from the imperative field. It spreads title over the grungy petroleum/standard gas and related hydrocarbons between the government and each of the consortium people. The distinctive explanations are being depicted underneath under diverse sub heads.

6.1.1 Rights granted by PSC

The significant rights vests by the PSC with the chose consortium include:

- The exclusive right to :
 - a) Undertake, inside the predefined territory, operations led in scanning for unrefined petroleum, regular gas and related hydrocarbons, and attempt penetrating of wells and different activities connected with testing, looking over, boring and site planning identifying with exploration of raw petroleum, characteristic gas and related hydrocarbons⁶³.
 - b) Undertake the development operations in connection to oil and gas field in the significant region including however not constrained to establishment of penetrating stages, boring wells, water infusion, establishment of capacity or gas handling offices and all different

⁶³ Article 8.1, MPSC

offices needed for the development, production and conveyance of unrefined petroleum and related hydrocarbons⁶⁴.

- c) All operations directed with the end goal of creating raw petroleum/regular gas and related hydrocarbons from the significant region after the beginning of production from the applicable oil and gas fields including the operation and upkeep of vital offices⁶⁵.
- The right to utilize, for nothing out of pocket, such amounts of raw petroleum/regular gas/related hydrocarbons created from the applicable field as are sensibly needed for directing the operations of the production of oil and gas as per for the most part acknowledged practices in the worldwide petroleum industry.
 - The right to construct, as per relevant clearances, any framework and correspondence offices vital for the behavior of any exploration, development or production activities identified with the field.
 - The right to flare common gas incidentally when and as essential gave a 48-hour notification is given to the Government of India.

6.1.2 Title to petroleum, data and assets

The government is the sole holder of the petroleum hidden the contract range and might remain the sole manager of petroleum delivered compliant with the procurements of this contract. Title to the petroleum to which the contractor is entitled under this contract, and title to petroleum sold by the companies should go to the important purchaser party at the delivery point. The contractor might be in charge of all costs and risks preceding and including all the delivery point and every purchaser party should be in charge of every last one of costs and risks connected with the party's offer after the delivery point.

Assets acquired by the Contractor for utilization in Petroleum Operations should be claimed by the gatherings embodying the contractor in extent to their partaking interest gave that the government might have the right to oblige vesting of full title and ownership in it, gratis and encumbrances of any or all assets. Equipments and assets no more needed for petroleum operations amid the term of the contract might be sold, traded or overall discarded by the contractor.

⁶⁴ Article 8.2, MPSC

⁶⁵ *Id.*

6.1.3 Assignment

PSC manages assignment of partaking enthusiasm for a square if the contractor to the production sharing contract need to appoint or exchange a part or every last bit of its taking an interest enthusiasm, earlier composed assent of the government is obliged and the government should not irrationally withheld the assent if the contractor fulfills⁶⁶:-

That the planned assignee is of great standing, has the capacity and ability to meet the commitments hereunder and willing to give unequivocal undertaking to perform those commitments

Restricted trade

The planned assignee is not an organization fused in a nation with which government for approach reasons has confined exchange or business

The assignor or assignee are willing to follow sensible conditions forced by the government to guarantee the execution under the contract

The assignment or exchange won't antagonistically influence the execution or commitments under this contract or influence the enthusiasm of the nation

The planned assignor or transferor of little size ashore piece arranged as S sort square ought to have finished the base work project conferred under introductory exploration period

If the contractor dole out or exchange to an associate organization then assent ought to be gotten from the management committee.

To get the government assent the contract has additionally ought to get certain approval from management committee. To get the approval the contractor ought to fulfill the accompanying conditions

Bank guarantee

The assignee gives an unalterable unrestricted bank ensure from a rumored bank of great remaining in India⁶⁷

Exchange of shares

⁶⁶ Article 28.1, MPSC.

⁶⁷ Article 28.4, MPSC.

□ In instance of any change in the status of an organization or its shareholding bringing about change in the control of the organization or its association with the organization giving the insurances former composed assent of the Government is needed⁶⁸

Application

□ Application for agree to allot or exchange should be joined by all applicable data on the proposed assignment or exchange and its impart holding and corporate structure.

□ The candidate should likewise submit such data identifying with the imminent assignee or transferee of the assignment or exchange as the government might sensibly require to empower legitimate thought and transfer of the application.

No approval

No assignment or exchange should be viable until the approval of the government is gotten or regarded to have been gotten.

Obligations

Up on assignment or exchange of its enthusiasm for this contract, the assignor or transferor should be released or released from its commitments hereunder just to the degree that such commitments are expected by the assignee with the approval of the government.

Approval

On the off chance that the government does not issue its assent or does not react to an appeal for assignment inside 120 days of the solicitation on receipt of all data, assent might be considered to have been given by the government.

Refusal

An assignment or exchange might not be made where the partaking enthusiasm to be held by the proposed assignor or the rate enthusiasm of assignee should be under ten every penny (10%) of the aggregate taking an interest enthusiasm of every last one of constituents of the contractor,

⁶⁸ *Id.*

aside from where the government on the suggestions of the management committee might in extraordinary circumstances.

6.1.5 Termination

The Contract may be terminated by the Government upon giving ninety (90) days written notice with reasons to the other Parties of its intention to do so in the following circumstances⁶⁹:-

- (a) Has purposely presented any false proclamation to the Government in any way which was a material thought in the execution of this Contract; or
- (b) has purposefully and intentionally removed or approved the extraction of hydrocarbon not approved to be extricated by the Contract or without the power of the Government with the exception of such extractions as may be unavoidable as a consequence of operations directed hereunder as per by and large acknowledged current oilfield and petroleum industry rehearses which, when so separated, were quickly advised to the Government or
- (c) Is decreed bankrupt by an able court or goes into or plan of creation with its loan bosses or exploits any law for the benefit of borrowers; or
- (d) has passed a determination to apply to a capable court for liquidation of the Company unless the liquidation is with the end goal of amalgamation or recreation of which the Government has been pulled out and the Government is fulfilled that the Company's execution under this Contract would not be unfavorably influenced accordingly and has issued its support thereto; or
- (e) Assigned any enthusiasm for the Contract without the former composed assent of the Government as gave in Article 28; or
- (f) Failed to make any financial installment needed by law or under this Contract by the due date or inside such further period after the due date as may from that point be indicated by the Government; or
- (g) Failed to follow or has contradicted the procurements of this Contract in a material specific
- (h) Failed to follow any last determination or grant made by a sole master or authorities
- (i) Failed to complete or watch any of the terms and states of the License or Lease or the procurements of the Acts or Rules in power.

6.1.6 Force Majeure

⁶⁹ Article 30, MPSC.

Force majeure procurement is incorporated in PSC to accommodate occasions or circumstances outside the ability to control of either gathering, which cause a gathering to neglect to meet its commitments (other than an installment commitment) under the PSC . In such circumstances, the gathering concerned is soothed from risk. The gathering guaranteeing an occasion of power majeure is frequently needed to utilize sensible endeavors to uproot the reasons for non-execution and to finish execution as expeditiously as would be prudent⁷⁰.

The expression "force majeure" procurements more often than exclude normal highlights, for example,

- a point by point meaning of a force majeure occasion;
- the commitments encompassing a power majeure occasion: these more often than not oblige the gathering asserting power majeure to serve notification to the next gathering and utilize all sensible endeavors to redress the circumstance as immediately as could reasonably be expected;
- examples of occasions which constitute a power majeure occasion: this is normally a standard rundown and may be thorough or non-comprehensive; on the other hand, a few purviews have a more extensive rundown of cases than others; and
- a particular rundown of occasions which won't constitute a power majeure occasion: for instance, in most of the contracts investigated, a commitment to pay cash under the contract was rejected from the meaning of a power majeure occasion.

The term of the agreement is to be reached out by the period of time that the power majeure occasion postpones the operations. On the off chance that an occasion of Force Majeure happens and is liable to proceed for a period in overabundance of thirty (30) days, the Parties might meet to talk about the results of the Force Majeure and the game plan to be taken to alleviate the impacts thereof or to be received in the circumstances⁷¹.

6.1.7 Applicable law and language of the agreement

The Contract should be represented and translated as per the laws of India and it might qualify the Contractor for activity the rights, privileges and powers gave.

The English language should be the language of this Contract and might be utilized as a part of arbitral processes. All interchanges, listening to or visual materials or reports identifying with

⁷⁰ Article 31, MPSC.

⁷¹ *supra.n.89.*

this Contract should be composed or arranged in English. The laws will likewise incorporate corrections, modifications, adjustments, and so on⁷².

6.1.8 Change of status of companies

The party comprising the Contractor may go into exchange which may bring about change in the administration or control of a Company or the association with any underwriter of the Company with the earlier composed assent of the Government and agreeability of Article 28.2 gave that the Government is fulfilled on⁷³:

- 1 Technical and Financial quality of the new Company
- 2 Details of shareholders understanding
- 3 Composition of Board of Directors subsequent upon such exchange

6.2 Fiscal clauses

Various fiscal clauses have been described below under various sub heads.

6.2.1 Participating interests

These are the interests held by the respective participants in the venture⁷⁴. The State will generally have an option to participate as a contractor within the framework of the overall PSC; however, generally the Contractor ‘carries’ the State’s interest, which means that it bears all of the exploration costs. The rights and obligations of the Parties comprising the Contractor shall include but not be limited to⁷⁵:

- (a) The right to take Cost Petroleum in accordance with the provisions of Article 15;
- (b) The right to take its Participating Interest share of Profit Petroleum in accordance with the provisions of Article 16
- (c) The right to receive its Participating Interest share of any incidental income and receipts arising from Petroleum Operations; and
- (d) The obligation to contribute its Participating Interest share of costs and taxes including Contract Costs

⁷² Article 32, MPSC.

⁷³ Article 34, MPSC.

⁷⁴ Article 2, MPSC.

⁷⁵ *Id.*

The State can typically elect to convert its carried participation interest into a full working interest. In return, the State agrees to reimburse the Contractor for the costs it has incurred up to that point in operations, in proportion to the State's acquired percentage. Any bonuses paid up to that point may also be reimbursed in proportion to the State's acquired percentage.

6.2.2 Recovery of cost petroleum

The Contractor is qualified for recuperate its exploration and production costs from accessible oil production or gross incomes (known as cost oil). Recoverable costs are normally decided as per 'bookkeeping strategies' and are deductible taxes for the reasons of figuring the Contractor's assessable salary⁷⁶.

The contractor should be qualified for recuperate contract costs out of the rate of the aggregate estimation of petroleum created and spared from the contract region in the year as per the accompanying procurements:-⁷⁷

- a) recovery should be made first of royalty installments
- b) recovery should next be made of the production costs
- c) recovery should next be made of the exploration costs
- d) recovery than should be made of the development costs

The unrecovered part of the contract costs should be conveyed forward to the accompanying year and the contract might be qualified for recuperate such contract costs in such year or the ensuing years as though such contract costs were expected for recuperation in that year, or the succeeding years until the unrecovered.

The greatest measure of the cost petroleum to which the contractor might be entitled, as per the procurements of this article, should be X% (to be taken from the acknowledged bid) of the aggregate estimation of the petroleum delivered and spared from the contract region.

6.2.3 Production sharing of petroleum

Profit oil is the foreordained portion of oil staying after installment of eminences and cost oil, which is shared between the State and the Contractor as definite in the PSC. It is figured quarterly taking into account the production of oil in barrels every day. The parties to the

⁷⁶ Article 15.1, MPSC

⁷⁷ Article 15.8, MPSC.

contract might impart benefit petroleum in every year. A party's offer of benefit petroleum in any year, might be ascertained on the premise of the Investment Multiple actually accomplished by the contractor toward the end of the former year for the contract range⁷⁸.

Profit oil implies the aggregate estimation of Petroleum Produced and Saved from the Contract Area in a specific period, as decreased by Cost Petroleum⁷⁹.

6.2.4 Taxes, Royalties, Rentals, Duties etc

The Contractor is obliged to make a number of payments to the State during the contractual term, including those set out below. Generally, such payments are not recoverable from cost oil and are in addition to the Contractor's minimum expenditure commitments⁸⁰. The Contractor is typically required to pay various taxes in accordance with the applicable laws of the jurisdiction, including income tax, export tax and duties, import duties, and stamp duty. Royalties are payable by the Contractor to reflect its usage and exploitation of the State's property and are typically agreed upon as a percentage of the amount or value of available oil and/or gas from the contract area. The rate is dependent upon a number of factors such as the contract area, the size of the project, and the bargaining power of the Contractor. Royalties are generally allowed as a deductible tax in calculating the Contractor's income for tax purposes.

Companies shall be required to pay royalty to the government for offshore areas at the rate of 10% of the well head value of crude oil and natural gas. In case of onshore area, companies shall be required to pay to the state government at the rate of 12.5% of the well head value of crude oil and 10% of the well head value of natural gas⁸¹.

In case of an offshore area falling beyond four hundred meter isobaths, the rate of royalty payable by companies to the government shall be at the rate of 5% of the well head value of crude oil and natural gas for first seven years from the date of commencement of commercial production in the field.

6.2.5 Valuation of petroleum

⁷⁸ Article 16.1, MPSC.

⁷⁹ Article 16.3, MPSC.

⁸⁰ Article 17.1, MPSC

⁸¹ Article 17.3, MPSC

A cost for crude oil might be dead set for every month or such other period as the parties might agree (hereinafter alluded to as the delivery point) as far as United States Dollars every barrel, on import equality premise. On the off chance that some or the greater part of an organization's or contractor's aggregate offers of raw petroleum amid a delivery period are made to outsiders at a careful distance deals, all business so made should be esteemed at the weighted normal of the costs actually invoiced by an organization, figured by isolating the aggregate receipt esteem from all such deals at the delivery point by the aggregate number of barrels of the raw petroleum sold in such deals⁸².

CHAPTER 7

SURVEY OF THE CURRENT PSCs AND THE PROPOSED NEW MODEL

The exploration and production course of action for hydrocarbons is an establishment of our imperativeness security, since India has a significant and creating enthusiasm for essentialness and huge hydrocarbon holds that stay to be investigated, evaluated and created. Production Sharing Contracts (PSCs) went into between the state and oil and gas associations with the finished objective of exploration and production of hydrocarbons constitute the critical strategy for achieving our general system focus of more conspicuous autonomy in this part. The paper has gone for touching base at a component that would prompt more noteworthy collaboration between the Government and oil companies, subsequently upgrading household production, streamlining observing strategies, and incentivizing interests in the exploration and production of hydrocarbons, including from the private sector.

⁸² Article 19, MPSC.

At long last, there is the more general thought concerning complex difficulties of exploration. Impact of NELP rounds have been depicted and thought about. Figuring of Government offer of benefit petroleum has been illustrated. It additionally incorporates OALP (Open Acreage Licensing Policy) as the government wants to move from the attempted and tried NELP system of sharing exploration blocks to an "open grounds framework" sooner rather than later⁸³. The open real estate framework is gone for fundamentally expanding the pace of oil and gas exploration activity in the nation⁸⁴. The ebb and flow contractual model obliges a specific exploration period, which stipulates a period of seven or eight contracting years, dependent upon the NELP round and the territory of the piece – whether ashore, in shallow waters, or in seaward waters. When disclosures have been made amid the exploration period, evaluated as per the terms and states of the contract, and proclaimed business (i.e. presentation of commerciality has been carried out), the disclosures experience development. In any case, it may be recognized that any further hydrocarbon exploration in the midst of the development period of different revelations or business production loads exploration costs on existing divulgence. The business hobbies of GoI in existing revelations may be traded off if exploration past the exploration period is licensed, because of the way that PTIM may get discouraged in situations like the new revelation being excessively peripheral or fizzling, making it impossible to create. Subsequently, the existing cost-recovery based model is a major bottleneck in furtherance of exploration in the existing Blocks/Fields.

7.1 Issues in appreciating about existing PSCs are:-

- (a) The major issue with PSC is that the ownership and control of production stays with the state and contractor does not secure title to its share of petroleum until the oil came to the delivery point and have recently prospecting rights on an oil field for reasonably concise time i.e. 30 years.
- (b) It is also quiet on issues where amid exploration period contractor concocts the production of regular assets other than natural gas or petroleum and whether it can do the production of same or not.

⁸³ Standing Committee on Petroleum and Natural Gas (2006-07), *Report on activities of Directorate General*, available at <http://164.100.24.208/Is/CommitteeR/Petro/12rep.pdf>, once the Exploration Period is completed

⁸⁴ *Id.*

(c) Whether PSC is more compelling than Concession agreement of service contracts.

(d) Blocks are assigned just once in a year under NELP, if an organization wishes to offer for pieces after they have been allocated amid that year than it needs to sit tight for the offering to occur in the following year.

7.2 Introduction of Revenue sharing model for auctioned oil and gas blocks

The Centre is moving towards a revenue-sharing system for oil exploration contracts from the time-tested policy of production sharing. It released a draft model Revenue Sharing Contract (RSC) recently seeking public comment. The Production Sharing Contract (PSC) regime was the basis of the nine NELP (New Exploration Licensing Policy) bid rounds over the last two decades⁸⁵. These rounds resulted in over 250 PSCs, attracted investments worth over \$20 billion and led to 130 discoveries with three of them being categorized as major. Over a period, the PSC system attracted controversy becoming a challenge to both contractors and the government. Purposeless procedures took precedence and the primary purpose of finding and producing oil and gas was lost. It is unfortunate that faulty contract management has now led to changing a sound policy⁸⁶.

7.2.1 PSC vs RSC

The key difference between the PSC and RSC is that the PSC model would encourage investors to take higher exploration risks, and in the event of success, the costs could be recovered. Since only one-third of our sedimentary basins have been fully explored, a contract model that encourages intensified exploration activities should have been preferred⁸⁷. India remains one of the least explored countries and could hold large potential resources. For example, 15 basins out of a total 26 sedimentary basins in India spread over on-land, offshore and deepwater, are estimated to hold prognosticated hydrocarbon resources of over 200 billion barrels of oil equivalent. Out of these, hydrocarbon-in-place volume of 80 billion barrels has been established through exploration activities by the public sector and private oil and gas companies. There is

⁸⁵ *Supra.n.84.*

⁸⁶ ,Mayank Ashar, Putting revenue before resources is wrongThe Hindu,21st Sep 2014,available at <http://www.thehindu.com/business/Industry/putting-revenue-before-resources-is-wrong/article6430033.ece>

⁸⁷ *Id.*

still a significant 'yet to find' hydrocarbon resources of over 120 billion barrels⁸⁸. Therefore, significant increase in exploration efforts is critical and this requires the urgent attention of the new government. And Dr. Kelkar was of the view that "The Indian PSC is designed to encourage E&P [exploration and production] activity in the interest of enhancing national energy security. The committee analysis shows that under PSC, the interests of the government are aligned with the interests of the contractors. Under the PSC, as the investor returns improve, the government takes also increases as it is designed to allow the government to retain a fair share of the upside."

7.2.2 Drawbacks of RSC

Now that a final decision seems to have been taken by the government in favour of the revenue sharing model, one expected a simple, easy to manage contract structure. However, the draft model revenue sharing contract disappoints⁸⁹.

It introduces the concept of escrow account in a contract which is meant to attract risk capital to first find resources before the revenue could be shared. An escrow account, by definition, is a temporary pass-through account. Revenue in oil exploration comes post-development of a commercial discovery and these are not temporary transactions. Typical contract terms are for over 25 years. Such contracts are essentially endeavours in partnership. While the resources belong to the government, it needs oil and gas companies with technical capabilities and balance-sheet strength to make risk investments. The draft contract expects investing companies to receive all revenues only under an escrow account so that the government could protect its share of revenue, and in certain circumstances, restrict the contractors' access to the account. The spirit of partnership and trust is completely missing⁹⁰.

The other striking feature is that there is a wrong assumption of certainty about discovery-to-delivery periods and more importantly, about oil and gas production profiles. Under the draft provisions in the model contract, the contractor is expected to commit to a production profile and is liable to pay penalties if the actual production varies from the forecast by 25 per cent.

⁸⁸ *supra.n.107*.

⁸⁹ Ajoy K Das, India to proceed with revenue sharing model for auctioned oil and gas blocks, 7th July 2014, available at <http://www.miningweekly.com/article/india-to-proceed-with-revenue-sharing-model-for-auctioned-oil-and-gas-blocks-2014-07-07>.

⁹⁰ *Id.*

Nothing in oil and gas business is certain. The data from seismic surveys using the best of technology cannot tell with certainty whether the fluid seen is oil or water. One needs to drill a well to find out. And drilling a well could cost over Rs.20 crore if it's a simple, shallow, onshore well to over Rs.500 crore if it's a complex deep water well.

Finding oil and or gas is not certain to make it commercial as it has to be in right quantity and at the right price. In India, strangely very simple procedural deviations can make a discovery an illegitimate one! How much oil and gas one will end up producing is again uncertain as it is dependent upon multiple technical factors. One knows the precise answer only when the last barrel is produced from a field. To put such penal provisions is a sure way to put off serious investors who have multiple investment options across the globe.

Considering that only one-third of our sedimentary basins are fully explored, only 15 per cent of basins have been covered by 3D seismic surveys and only 15,000 wells have been drilled over 60 years (there are one million wells in production in the U.S.) what we need is a contract structure that will attract risk investment and help to step up exploration activities significantly.

The only ways to catch up on the lost decades are:-

(1) Build the National Geo Data Repository and launch Open Acreage License Policy — This allows prospective bidders to look at the data any time and offer a bid to explore in the most transparent manner;

(2) Provide market-determined oil price to ONGC and Oil India to bring marginal oil fields into production and to implement enhanced oil recovery techniques to recover more from matured oil fields;

(3) resolve the current uncertainty over gas price promptly;

(4) remove the artificial distinction between oil and gas for the purpose of tax holidays — both these are commodities of hydrocarbon molecules and can easily substitute each other and exploration risks and efforts required to find them are same, and

(5) announce the PSC extension policy to remove uncertainty over the production sharing contracts of few producing fields coming up for extension.

Launching NELP X with a revenue sharing contract model without clarity on the above five areas will be akin to putting the cart before the horse. The current draft model of revenue sharing contract needs to be revised to bring the focus back on finding resources first and the government share of the revenues needs to be collected in the same way that it collects income tax and duties.

India depends on imports to meet 75 per cent of its crude oil requirements spending close to Rs.3,000 crore everyday. If the domestic oil exploration activities are not stepped up, over the next 10 years, we would end up transferring \$1.5 trillion of our wealth (that's the current size of our economy) to oil exporting countries.

On the contrary, the countries which were able to attract investment and technology ended up finding more oil and gas resources. The most recent and fascinating examples are the discovery of super giant field in Mozambique and in Phoenix South prospect in Australia, where oil has been discovered in a place close to an initial discovery made 34 years earlier. What it tells you is that exploration is a never-ending game where perseverance and passion surely pays and the ever-advancing discovery and recovery technologies aid immensely. All that the government needs to do is to put in place enabling policies that encourage exploration endeavors for ever.

CONCLUSION

Entirely reliant on oil incomes and usually inadequate with regards to the budgetary and specialized assets needed for petroleum exercises, adding to nation's destinations are to secure government control over operations, improve economic development and give sufficient motivations to foreign investors. To achieve these targets, it has been noticed that governmental issues and imagery assume an imperative part in molding government's choices: most developing nations adopt PSAs as ownership over resources and, in principle, more control over production is given to the host government. Then again, it has been contended that possession and control over assets are not so much in close relationship. As opposed to the kind of model utilized, it is the structure of the contract and its monetary game plans that focus its viability in achieving the destinations of developing nations.

From the examination of the fiscal components of the production sharing provisos, it can be drawn that a decently adjusted expense oil roof may fulfill investor's requirement for quick cost recovery and government's desires of ahead of schedule incomes. Most notably, so as to give developing nations a compelling control over assets, the production sharing statement must be drafted effectively and shall focus on the economic rent of a project. Where organizations are permitted to hold abundance benefits, state's control over production is tested, though (typical) possession is retained.

While adjustment provisions in PSAs influence government's sovereignty and control over assets, through precisely drafted renegotiation conditions a between governments and oil organizations' contending goals can be accomplished.

Eventually, the capacity of a PSA in achieving developing nation's goals depends, on how the agreement is drafted and how the harmony between the party's requirements is accomplished. PSC framework has been successfully utilized by developing nations with potential oil reserves yet high extraction costs (particularly from offshore fields) and high exploration or specialized risks. With PSC, the issues of budgetary assets and specialized mastery can be tackled by these nations. Then again, IOCs can foresee and deal with the risks by doing geographical and seismic research and won't go before any improvement in the event that it is not gainful⁹¹.

History has proven time and again that from the financial and functional point of view, PSC and concession framework is not altogether different, however by giving a supposition that 'the administration still maintains the national responsibility for asset', PSC serves more 'political capacity' than anything else. Besides, Thomas Walde portrays that PSC as an apparatus which "provides for the government political and to the organization commercial satisfaction. The legislature can be seen to be running the show – and the organization can run it behind the disguise of lawful title symbolizing the statement of national power."⁹²

Practically speaking, the advantage of PSC for the host state is that PSC framework may be utilized as an exceptionally powerful tool for foreign investors. In the event that this framework has been managed properly by the host nation, it may bring a lot of outside capital and skill

⁹¹ D. Babusiaux et al. *Oil and Gas Exploration and Production: Reserves, Costs, Contracts. (Editions Technip (2004))*, pp. 199.

⁹² *supra.n.122*

without surrendering exorbitant control and benefits to outside diversions⁹³. By exchange of technology and good financial systems, it gives an open door for NOC to develop and build up the state's assets. From alternate point of view, the weakness of PSC is that the state will be tied by the limitations in the agreement for quite a while. Accordingly, if the legislature or political atmosphere changes, the terms of PSC can't be changed to reflect the states new needs. In any case, this negative side of PSC framework can be minimize by the state by drafting and arranging PSC framework which can maximize the state's income and restricting the IOCs' access to oil, while in the meantime making a legitimate administration that permits the state the adaptability to alter the terms of the project.

⁹³ Schiffrin, Svetlana Tsalik & Anya. *Covering Oil: A Reporter's Guide to Energy and Development*. (Open Society Institute, 2005), pp. 14.

