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Date: September 10, 2014

To:

Shri Rakesh Mishra,
Under Secretary (Exploration), Ministry of Petroleum and Natural Gas,
Government of India

Feedback regarding Draft Model Revenue Sharing Contract

Dear Shri Mishra,

We are happy to provide our feedback and comments on the Draft Model Revenue Sharing Contract (MRSC), as per letter no. O-32011/63/2013-ONG-I (FTS-29027) dated August 20, 2014 published on the MoPNG website. We request you to consider our comments while finalizing the model revenue sharing contract, and publish the finalized model contract on the MoPNG website. We are also sending you a hard copy of our comments by post, and it may reach you in a few days. Our comments and feedback are as follows:

1. The letter purports to seek feedback about the draft MRSC only from private/JV companies. However, as it is now well established that petroleum and natural gas, along with other natural resources, are national properties, it would be appropriate to actively seek comments from all citizens in the country and not only oil or gas producers. It is in this spirit that we are providing our comments on the draft MRSC.
2. MoPNG had published a draft uniform policy for awarding hydrocarbon acreages in September 2013, and we had provided our feedback on it through letter no. PEG/2013/122 dated October 14, 2013. To the best of our knowledge, no final policy for awarding acreages has been published after this draft. It is very difficult to comment upon a draft MRSC in the absence of a policy that will govern awarding of acreages. For example, it is unclear how the winner of a bidding process would be chosen to whom this contract would be applicable. Without a clear policy, it is also unclear how the revenue sharing percentages would be determined for other hydrocarbons that may be extracted than the one for which the block is designated as permitted under Article 5.7 of the draft MRSC. Therefore, we strongly urge you to finalize the acreage awarding policy and MRSC only after publishing revised drafts of both the policy and MRSC, and seeking feedback on both. Notwithstanding this, we are providing our views on the current draft MRSC.
3. Article 14 of the draft MRSC broadly talks about the contractor's responsibility to protect the environment under prevailing laws. However, given past concerns about land subsidence due to oil and gas extraction activities and the well-known concerns regarding water pollution and usage associated with hydrocarbon extraction from shale rocks, it would be prudent to have specific and well-defined clauses to address these concerns, and ensure that contractors' operations do not compromise on these important aspects.

4. Appendix D provides details on calculation of Government's revenue share based on production from a block. We propose that the Government share of production for the month should be calculated by simply multiplying the Government share of daily average production volume (calculated in para 8.1.4 of Appendix D) with the number of days in the given month. The currently proposed method, of first determining the Government share of production in percentage terms (para 8.1.5) and then using that to determine Government share (para 8.1.6) is both unnecessarily complex and could lead to rounding off errors as with the given example. Using the method proposed by us, Government revenue would correctly amount to 360,000 Bbl rather than 359,775 Bbl shown in the sample calculation – the difference being due to rounding off errors arising because of using 53.3% rather than 53-and-one-third of a percent. The cumulative effect of such rounding off errors across blocks and over the months and years could add up to be significant, and hence we suggest adopting the simpler approach suggested.
5. Article 15.5 states that the Government revenue share should be transferred from the Escrow account if it has sufficient funds available within 15 days of the end of the month. However, no such condition or timeline is imposed on payments to be made by the contractor by Demand Draft in case the Escrow account does not have sufficient funds. A similar timeline should be imposed for such payments also. Given that Article 16.3 of the draft MRSC and clause 3.1 of the proposed Escrow agreement permit the contractor to withdraw funds from the Escrow account on a daily basis (unless in the case of default), it is important to do so as it is not clear how the Escrow account would have sufficient funds to be used to pay the Government share.
6. Article 20.1 gives the contractor the right to use natural gas from the field to be used for reinjection, captive power generation etc. However, there is no clarity on the monitoring and verification mechanisms in place to ensure that the quantities of gas claimed to be used by the contractor under Article 20.1 are indeed used for permitted purposes. It would be desirable that the MRSC (or the policy governing it) is more explicit about such monitoring mechanisms.
7. The contract does not make it clear how the quantities of production and sales reported by the contractor would be verified. It is possible that such details would be present in the policy governing the contract. However, since the policy is not publicly available, we would like to point this out as an important aspect requiring greater clarity, and with sufficient checks and balances, as it is an important determinant of Government revenue.
8. Article 20.4 in its current form first states (Article 20.4.1) that the value of petroleum shall be determined based on import parity price when the Government determines that the sale price realized is not consistent with arms-length sales. It then states (Article 20.4.2) that the total sales to third parties shall be valued at the weighted average price of the sales. We propose that the wording of Article 20.4 (and its sub-articles) be simplified to clearly state that firstly, all sales of petroleum by the contractor shall be based on arms-length transactions and secondly, that when the Government determines that the sale price realized is not consistent with arms-length sales, it shall use import parity price. The current phrasing of the Article does not mandate sales to be based on arms-length transactions.
9. Article 20.4.4 states that an 'arithmetic average' price per barrel would be considered for determining Government share. We suggest that weighted average price per barrel should instead be used. This would also make it consistent with Article 20.4.2.
10. It is not clear from the contract document whether the Government has an option to take its share of the revenue in kind, if it so chooses and the modalities for the same. It may be desirable to retain such an option for reasons of flexibility.

We hope you will consider our suggestions positively. Thanking you,

With best regards

A handwritten signature in black ink, appearing to read 'Ashok Sreenivas', with a long horizontal flourish extending to the right.

Ashok Sreenivas

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