

---

## **Chapter-5**

### **Conclusion and Gist of Recommendations**

---

## Chapter 5 - Conclusion and Gist of Recommendations

### 5.1 Conclusion

The hydrocarbon demand in the country exceeds the domestic crude oil and natural gas production. Keeping in view this demand, the Government of India opened up the Exploration and Production sector with the implementation of New Exploration Licensing Policy (NELP) in 1997. This policy provides a level playing field to the private sector by giving the same fiscal and contract terms as applicable to National Oil Companies for exploration acreage.

Under NELP, the Government and a private or public company, whether foreign or domestic, enter into a Production Sharing Contract (PSC). The PSC for specific fields / blocks is the basis for petroleum operations, cost recovery, profit sharing and other aspects. In addition, the DGH has been entrusted with regulatory responsibilities concerning the PSCs for discovered fields/exploration blocks, promotion of investment and monitoring of E&P activities etc.

The current audit of PSCs conducted, to get an assurance that the revenue interests of the GoI were properly protected and that the monitoring and control systems established were effective in ensuring compliance to the PSC provisions, has disclosed weaknesses in the areas of management and fulfilment of contractual obligations.

With regard to transparency and accountability in the manner in which regulatory responsibilities were discharged, audit examination revealed that there was scope for strengthening the PSC regime and implementation thereof so as to ensure that the best interests of GoI as owner of the natural resources were adequately protected. Timely approvals for budgets and development plans, efficient decision-making on the part of GoI in respect of valuation of hydrocarbons, signing commercial agreements, etc are areas where delays are a matter of concern.

Provisions relating to relinquishment of contract area, declaration and assessment of the viability of discoveries and their commerciality, sharing of risk, approval of development plans are some of the areas in the existing PSC model, which may require critical review and rationalisation so that there are no loose ends or vagueness. There were deficiencies in implementation of procurement and service contracts which have led to our recommendations for disallowance of cost recovery and/or recognition of additional revenue. **(KG-DWN-98/3 Block)**

In the PMT JV, Audit noticed instances of deficiencies in award and implementation of procurement and service contracts, deficiencies in the practice of charging production

inventory to accounts and allocation of common expenditure between Panna-Mukta and Tapti contract areas. COSA has also not been formalized with IOCL since 1994. PMT JV is yet to determine transportation losses of condensate as agreed with ONGC in the settlement agreement in December 2005. **(PMT Blocks)**

The PSC of RJ-ON-90/1 block provided that GoI or its nominee was under obligation to purchase the entire crude oil from the Contract Area. The GoI nominated refineries, however, could not uplift the RJ crude. Further, PSC provided that a price for the crude oil would be agreed between the Parties and would be subject to agreement by GoI. However, the price of the RJ crude was yet to be finalized by GoI in the absence of which sale of RJ crude was taking place at a provisional price agreed between the Operator and the buyers. Also, GoI, on the request of the Operator, agreed to shift the delivery point from Barmer to Salaya with a condition that the GoI may designate multiple PSU refineries and laying of a pipeline from Barmer to Salaya and Salaya to Bhogat in Gujarat. The pipeline was delayed leading to increase in pipeline cost to US\$ 1108 million (March 2013) against the approved cost of US\$ 941 million. **(RJ-ON-90/1 block)**

## **5.2 Gist of Recommendations**

- MoPNG / DGH may take action for timely approval of WP&B and annual audited accounts in future and expedite the pending approvals.
- MoPNG may ensure that the disallowed cost of three wells amounting to US\$ 160.81 million is recovered.
- In view of the PSC provisions, MC's acceptance of discovery area in July 2006 and MoPNG's decision of July 2008 (conveyed in February 2009), further exploration activities in the 'discovery area' from July 2006 onwards (which included drilling of eight exploration wells and six appraisal wells of discoveries resulting from these exploration wells at an expenditure of US\$ 427.03 million) was improperly carried out at the risk of revenue of the commercial discoveries made in the Block.
  - Normally the entire amount of US\$ 427.03 million would require to be disallowed for cost recovery since these activities were not in line with PSC provisions. However, from a pragmatic point of view, it had to be kept in mind that the exploration had resulted in a commercial discovery viz. D34 for which a development plan had already been approved. In three other cases viz. D29, D30 and D31 discoveries, review of commerciality was under finalisation.
  - At this stage, keeping in mind the national interest and energy security, Audit recommends that MoPNG should accept sharing of exploration cost of only those of the abovementioned wells which resulted in a commercial discovery

and disallow the cost recovery of US \$118.99 million already effected by the Operator on the remaining wells. As regards the well cost in respect of D29, D30 and D31 discoveries, since the matter regarding the DoC was under consideration in MoPNG, the same may also be considered for disallowance in case they are not found to be commercially viable subsequently.

- MoPNG may develop consistent and uniform parameters for evaluating commerciality of discoveries and fix norms / criteria for working out techno-economic analysis of a FDP.
- MoPNG may take urgent steps to resolve the differing views of the Contractor and DGH on the reserves estimates and take appropriate action to increase production.
- The PSC provisions relating to pricing and sale of Crude Oil and Condensate may be followed and decision on pricing and sale of Crude Oil and Condensate may be taken at the earliest.
- MoPNG may consider issuing audit exceptions under Sections 1.9 of the Accounting Procedure to the PSC amounting to US\$ 690.70 million (approximately) - in respect of expenditure related issues (US\$ 386.83 million), revenue issues (US\$ 250.93 million) and accounting issues (US\$ 52.94 million) as per the specific audit opinion expressed relating to KG-DWN-98/3 block.
- The common expenditure should be appropriately allocated to Panna-Mukta and Tapti fields on a reasonable basis *viz.* actual expenditure identifiable to a particular contract area or in the ratio of expenditure on the primary activity.
- PMT JV may ensure that production inventory is charged to accounts only when such material is removed from inventory and used in petroleum operations as provided in the PSC
- GoI may ensure expeditious conclusion of COSA between IOCL and PMT JV by resolving the contentious issues.
- PMT JV may ensure that all facilities used for petroleum operations (pre-wellhead and post-wellhead activities) are considered for computing the wellhead value while arriving at royalty payable to GoI and also work out and remit the additional royalty to GoI by considering the upgraded reserves for amortization of capex.

- The Operator of RJ Block should carry out cost recovery in accordance with PSC provisions, as any deviation in this regard would impact payment of PP to the GoI.
- GoI should promptly finalize the price for the RJ crude so that the calculation of the PP, Royalty etc. could be made on firm basis.

**Dated: 12 August 2014**

**Place : New Delhi**



**(ANAND MOHAN BAJAJ)  
Principal Director of Audit  
(Economic and Service Ministries)**

**Countersigned**



**Dated: 13 August 2014**

**Place : New Delhi**

**(SHASHI KANT SHARMA)  
Comptroller and Auditor General of India**