Production Sharing Contract

February 10, 2021

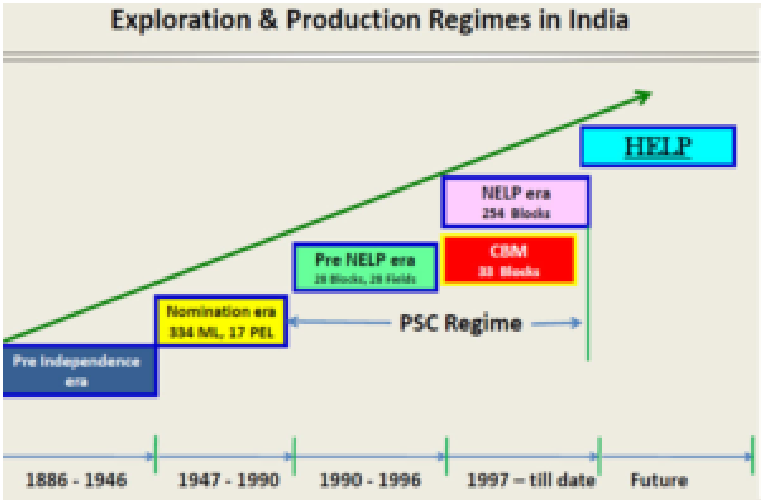
In News: Government has taken multiple steps to enhance exploration & production of oil and gas to reduce imports and make the country AtmaNirbhar through various policies under Production Sharing Contract (PSC) regime.

About Production Sharing Contract (PSC)

- Production Sharing Contract (PSC) is a term used in the Hydrocarbon industry and refers to an agreement between Contractor and Government whereby Contractor bears all exploration risks, production and development costs in return for its stipulated share of (profit from) production resulting from this effort.
- The costs incurred by the contractor are recoverable in case of commercial discovery. Thus, PSC is a fiscal regime existing in the exploration and production of hydrocarbons.
- Production Sharing Contracts became widely adopted as part of the New Exploration and Licensing Policy (NELP) launched by the Government in 1997 for enhanced exploration of oil and gas resources in the country.
- The Production Sharing Contracts (PSCs) under NELP are based on the principle of "profit sharing".
- When a contractor discovers oil or gas, he is expected to share with the Government the profit from his venture, as per the percentage given in his bid. Until a profit is made, no share is given to the Government, other than royalties and cesses. Thus, in production sharing contracts (PSC), Government's take depends on biddable share of profit petroleum/ gas after allowing for cost recovery.
- In other words, PSC allows the contractor to recover his cost, before giving the Government its share in the contractor's revenues, in case there is commercial

discovery leading to production (Not all drilling leads to discovery of oil/gas). Thus, a certain proportion of the balance revenues of the contractor are shared with the Government.

- The PSC regime has been changed with a revenue sharing contract model in 2016.
- However, the new regime is applicable only for future contracts that would be awarded by the Government.



Production Sharing Contract (PSC) regime for early monetization of hydrocarbon discoveries, Discovered Small Field Policy, Hydrocarbon Exploration and Licensing Policy, Policy for Extension of Production Sharing Contracts, Policy for early monetization of Coal Bed Methane, Setting up of National Data Repository, Appraisal of Unappraised areas in Sedimentary Basins, Re-assessment of Hydrocarbon Resources, Policy framework to streamline the working of Production Sharing Contracts in Pre-NELP and NELP Blocks, Policy to Promote and Incentivize Enhanced Recovery Methods for Oil and Gas, Policy framework for exploration and exploitation of Unconventional Hydrocarbons under existing Production Sharing Contracts, Coal Bed Methane contracts and Nomination fields.

The New Exploration Licensing Policy (NELP)

- The Government of India formulated a policy called New Exploration Licensing Policy in 1997.

- The main objective was to attract significant risk capital from Indian and Foreign companies, state of part technologies, new geological concepts and best management practices to explore oil and gas resources in the country to meet rising demands of oil and gas.
- This policy, NELP was approved in 1997 and it became effective in February, 1999 Since then licenses for exploration are being awarded only through a competitive bidding system and National Oil Companies (NOCs) are required to compete on an equal footing with Indian and foreign companies to secure Petroleum Exploration Licences (PELs).
- Nine rounds of bids have so far been concluded under NELP, in which production sharing contracts for 254 exploration blocks have been signed.

The salient features of NELP are as under:

- 100% FDI is allowed under NELP
- No mandatory state participation through ONGC/OIL or any carried interest of the Government.
- Blocks to be awarded through open international competitive bidding.
- ONGC and OIL to compete for obtaining the petroleum exploration licenses on a competitive basis instead of the existing system of granting them PELs on nomination basis.
- ONGC and OIL to get the same fiscal and contract terms as private companies.
- Freedom to the contractors for marketing of crude oil and gas in the domestic market.
- Royalty at the rate of 12.5% for the onland areas and 10% for offshore areas.
- Royalty to be charged at half the prevailing rate for deep water areas beyond 400 m bathymetry for the first 7 years after commencement of commercial production.
- Cess to be exempted for production from blocks offered

under NELP.

- Companies to be exempted from payments of import duty on goods imported for petroleum operations.
- No signature, discovery or production bonuses.
- A Model Production Sharing Contract (MPSC) which is reviewed for every NELP round.
- Contracts to be governed in accordance with applicable Indian Laws.