

**Deepwater Development Project of KG-DWN-98/3 (D6 block) in
Krishna Godavari Basin**

This refers to the various reports, comments and statements that have appeared in the newspapers on issues related to D6 gas field in Krishna-Godavari basin of India. These have emanated from political parties, bureaucrats, corporate entities, including of course the stakeholders. There has been criticism from various quarters on the so-called *Gold Plating* of the development cost of the D6 field. There have also been impassioned pleas for treating the gas as “sovereign national asset”. This has become the subject matter of endless debate.

For the ready reference of the reader, a brief account of the history of the D6 block is presented.

Based on the results of the global competitive bidding, the Government of India awarded the exploration block KG-DWN-98/3 to the consortium of Reliance Industries Limited and a Canadian company, Niko Resources Limited in April 2000 under New Exploration Licensing Policy (NELP) – I. On 12th April 2000 the Government of India signed a production sharing contract (PSC) with the consortium of Reliance Industries Limited (Participating interest - 90%) and Niko Resources Limited (Participating interest – 10 %).

The contractor for the block, based on exploration activities, has made 19 hydrocarbon discoveries. One such discovery MA – Oil has been producing oil @ 10,000 bopd since mid September 2008. Two major gas discoveries, D1 & D3, are on production since April, 2009. It is envisaged that at peak production the two gas fields would together contribute 80 MMSCMD (about twice the current national gas production). This project happens to be the first deepwater development project in India. It is pertinent to mention here that the Dhirubhai gas discovery is the largest gas discovery in the world for the year 2002. In any other country, it would have been hailed and cherished. However, we are content with squabbling over this outstanding success.

A capital investment of US \$ 8.836 billion was envisaged for development of D1 and D3 gas fields. Another investment of US \$ 2.234 billion was required for another development project, MA Oil in the same block. The main issue that has come to the fore is the capital expenditure for the development of the gas field.

In order to comprehend the issue, it is important to understand the Production Sharing Contract and certain fundamental aspects of the Field Development Plan (FDP) and the role of the Management Committee in the decision making process with reference to the Field Development Plan.

The Production Sharing Contract (PSC) is considered sacrosanct. All the E & P operations come under the ambit of the PSC. It is a document signed between the contractor and government of India and is valid during the tenure of the contract.

Under the provisions of the PSC, a Management Committee comprising representatives of the contractor and the government of India is constituted. The Management Committee has wide ranging functions and responsibilities with respect to the PSC and the decisions are taken through majority opinion.

While approving the Field Development Plans (FDPs) the Management Committee approves only the related development activities and not the cost involved as the approval of the costs are taken separately through annual work program and budgets which may span 5 to 7 years. In addition, the procurement of the items is carried out as per set Purchase and Procurement procedure as defined in the PSC. Notwithstanding the above, the PSC also requires auditing of the exploration and development expenditure by internal as well as Government appointed auditors. Even the whole process of expenditure starting from Management Committee review/ approval of work program and budget to purchase and procurement of materials & equipments are amenable to CAG audit. The CAG team is carrying out the audit work, since their request to access the Operator's records have been agreed.

The issue of high Capex was raised on the floor of Parliament in 2007 to which the Hon'ble Minister of Petroleum and Natural Gas Shri. Murli Deora submitted detailed clarifications.

A PIL related to *approval of Capital Expenditure for D1 & D3 gas field project* was also filed in the Delhi High Court with request for investigations against Government officials. The PIL, however, was rejected by the Hon'ble High Court.

Upon further complaints, the D1 & D3 project was reviewed by various agencies, such as Expenditure Division and Revenue Division of Finance Ministry. Government also appointed independent and reputed technical experts and evaluated the development plan.

In the opinion of the experts, the development plan is highly cost effective and fast track. A CAG audit is being carried out. However, they have scrutinized all the records at DGH for last one year.

The Goldman Sachs Report on Global Finding & Development Costs 2008 clearly states that the out of 32 deep water projects developed in the world, D6 ranks amongst the lowest in terms of costs and amongst the fastest in terms of time from discovery to production.

DGH also took measures to get the cost validated by Indian expert, Dr. P. Gopalakrishnan as well as by International Engineering Consultant M/s Mustang International.

It needs to be appreciated that the principles and documents used for profit sharing under PSC is similar to that based on which the corporate tax system functions. PSC requires that the contractors maintain details of expenditure incurred by them following accounting standards, duly supported by documents. The expenditure allowed for cost recovery is limited to the amount verified by two

levels of audit done by independent firms of chartered accountants. The PSC also regulates the procurement process of the contractor to ensure that expenditure is incurred at arms length. Expenditure not in line with the PSC is not cost recoverable.

The idea of gold plating betrays a lack of knowledge of business economics. Inflating the expenditure does not benefit any stakeholder- neither the contractor nor the government. No company would like to increase its investment unproductively. Every addition dollar of wasteful investment dents the profit of the contractor. For a business enterprise, there is no motivation to gold plate its investment. Due to the higher share of profit generally earned by the contractors, the loss to the contractors due to inefficiency or gold plating is higher than to the government.

It is important for all the stakeholders in the E & P sector in India to realize that the global perception of India's hydrocarbon endowment is rapidly changing with more investments and modern technology pouring into India. The discoveries of oil and gas in various basins has resulted in a paradigm shift in the way E & P companies across the globe view the hydrocarbon prospectivity of India. Today, India is a favored destination for companies to invest in E & P business. The fair and transparent procedures and practices adopted by the DGH, under the Ministry of Petroleum & Natural Gas have resulted in creating an E & P brand image that has become the hallmark of our efforts. It is a matter of pride for us that our PSC finds mention in the curriculum of the University of Aberdeen and Harvard University.

Energy remains the primary driver of our economy. Oil and gas are critical components of our energy basket and will continue to play a crucial role in meeting the energy requirements of our country in the foreseeable future until some renewable form of energy becomes viable. It is, therefore, very important that we stand united in our efforts towards energy security and in meeting the objectives of India Hydrocarbon Vision 2025. E & P companies in India are doing well and it is our responsibility to nurture and encourage them. A substantial amount of investment of about 17 billion USD is committed in the PSC regime of which about 9 billion USD is under the NELP regime.

The Govt. of India and DGH have together created a brand image for the E & P sector in India. It is important that the same is nurtured and strengthened. In order to achieve this, it is imperative that the government, DGH, media and industry complement each other's strengths. While criticism and dissent is an intrinsic characteristic of a democracy, it should not become the obsessive subject of endless public debate. Irresponsible and biased views and opinions are bound to send negative signals to the E & P companies across the world and cause irreparable damage to the growth and development of the oil and gas industry in India.

Therefore, my appeal to all concerned is that before criticizing the actions of the DGH and the Govt. of India, it is important and essential to understand the issues in their entirety and in an unbiased manner.