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POLICY FRAMEWORK FOR STREAMLINING OPERATIONS OF PRODUCTION SHARING CONTRACTS

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Introduction

On 18 July 2018, the Cabinet Committee on Economic Affairs approved policy framework for streamlining operations of production sharing contracts (PSCs) for increased domestic production of hydrocarbon resources (Policy).

By way of background, the Government of India had awarded 28 exploration blocks (13 offshore and 15 onshore) to private companies between 1980. This was prior to the implementation of New Exploration Licensing Policy (NELP) where Oil and Natural Gas Corporation Limited and Oil India Limited have the right of participation in the blocks after hydrocarbon discoveries. In 2017, the Government of India had approved policy to grant extension of 10 years to PSCs awarded under the pre-NELP blocks. Now, for pre-NELP blocks, the Policy provides for: (i) sharing and cost recovery of levies; and (ii) tax benefits.

Sharing and cost recoverability of levies in pre-NELP blocks

The Policy provides an enabling framework for sharing royalty, cess and other statutory levies in proportion to the participating interest of the contractor in pre-NELP blocks. Further, the levies have been made cost recoverable with prospective effect and can thus be recovered from the sale of hydrocarbons before sharing of the profits with the Government of India.

Tax Benefit

Section 42 of Income Tax Act, 1961 (IT Act) allows companies to claim 100% of expenditure incurred under a PSC as a deduction for computing taxable income in the same year. 13 out of 28 PSCs for pre-NELP discovered fields did not have provisions for tax benefit under Section 42 of IT Act. The Policy now prospectively extends tax benefits under Section 42 of IT Act to operational blocks under pre-NELP discovered fields. This is expected to provide uniformity in PSCs and provide incentive to contractors to make additional investment during the extended period of PSCs.

Other key policy initiatives

Apart from the specific benefits for the pre-NELP blocks, the Policy provides for extension of time period for exploration and appraisal of operational blocks in the north

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eastern region by 2 years and 1 year, respectively. This is bearing in mind the logistical difficulties of north eastern region and in line with the Hydrocarbon Vision 2030 for North East, 2016. Further, to boost natural gas production in the region, the Policy provides marketing and pricing freedom for natural gas to be produced from discoveries which have not commenced production as of 1 July 2018. The Policy also relaxes the timeline for giving written notice to notify the occurrence of a force majeure event in the PSCs from 7 days to 15 days.

Comment

The Policy is expected to provide clarity on certain outstanding issues in relation to pre-NELP blocks. The PSCs in north eastern region and pre-NELP blocks in which investment for additional development and production activities is envisaged will specifically benefit from the Policy. This Policy along with other policies like Open Acreage Licensing Policy and Discovered Small Field Policy are steps to incentivise domestic production of natural gas and to allow the Government of India to achieve its target of expanding the share of natural gas in the energy mix to around 25% by 2025.

- Dibyanshu (Partner) and Prateek Bhandari (Senior Associate)

For any queries please contact: editors@khaitanco.com

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Mumbai

One Indiabulls Centre, 13th Floor
Tower 1 841, Senapati Bapat Marg
Mumbai 400 013, India

T: +91 22 6636 5000
E: mumbai@khaitanco.com

New Delhi

Ashoka Estate, 12th Floor
24 Barakhamba Road
New Delhi 110 001, India

T: +91 11 4151 5454
E: delhi@khaitanco.com

Bengaluru

Simal, 2nd Floor
7/1, Ulsoor Road
Bengaluru 560 042, India

T: +91 80 4339 7000
E: bengaluru@khaitanco.com

Kolkata

Emerald House
1 B Old Post Office Street
Kolkata 700 001, India

T: +91 33 2248 7000
E: kolkata@khaitanco.com