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IN THE UNITED STATES DISTRICT COURT

3

DISTRICT OF NEW JERSEY

4

Civ. No. 04-3749 (JAP)

5

(Consolidated Cases)

6

Hon. Joel A. Pisano

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IN RE ROYAL DUTCH/SHELL |

9

TRANSPORT SECURITIES |

10

LITIGATION |

11

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12

Videotaped Deposition of

13

JOHN MALCOLM

14

Washington, D.C.

15

Friday, October 20th, 2006

16

9:49 a.m.

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23 Job No. 22-87673

24 Pages 1 - 180

25 Reported by: Laurie Bangart-Smith

0002

1

Videotaped Deposition of

2

JOHN MALCOLM

3

4

5 Held at the offices of:

6

LEBOEUF, LAMB, GREENE & MACRAE, LLP

7

1875 Connecticut Avenue, Northwest

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Suite 1200

Washington, D.C. 20009

Taken pursuant to notice, before Laurie  
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and Notary Public in and for the District of  
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25 Alastair Hunter, KPMG representative

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0007

1 JOHN MALCOLM, October 20, 2006

2 PROCEEDINGS

3 THE VIDEOGRAPHER: Here begins Tape

4 Number 1 in the deposition of John Malcolm, in the

5 matter of Royal Dutch/Shell Transport Securities

6 Litigation, in the United States District Court,

7 District of New Jersey, Case Number 04-374.

8 Today's date is October 20th, 2006. The time is  
9 9:49 a.m. The video operator today is Cali Day of  
10 LegaLink New York. This deposition is taking  
11 place at 1875 Connecticut Avenue, Washington,  
12 D.C., 20009.

13 Would counsel please identify themselves  
14 and state whom they represent.

15 MR. MACFALL: Timothy MacFall,  
16 Bernstein, Liebhard & Lifshitz, for plaintiffs in  
17 the class.

18 MR. SILBER: Jeffrey Silber, Bernstein,  
19 Liebhard & Lifshitz, for plaintiff.

20 MR. PEITLER: Steven Peitler, Bernstein,  
21 Liebhard & Lifshitz, for plaintiff.

22 MS. AGRO: Jill Agro, General Counsel  
23 for opt-out plaintiffs.

24 MR. CRAPOL: Andrew Crapol, Debevoise &  
25 Plimpton.

0008

1 JOHN MALCOLM, October 20, 2006

2 MR. WEED: Earl Weed, in-house with  
3 Shell.

4 MR. SMITH: Colby Smith, Debevoise &  
5 Plimpton, representing the Royal Dutch Petroleum  
6 and Shell Transport and Trading and the witness.

7 MR. CORSON: Nicholas Corson, Hogan &  
8 Hartson, representing KPMG Accountants, N.V., and  
9 with me today is Alastair Hunter, a representative  
10 of KPMG Accountants, N.V.

11 MR. FOUKAS: Saavas Foukas, Hughes,  
12 Hubbard & Reed, for PricewaterhouseCoopers, LLP.

13 MS. LATIMER: Aimee Latimer, Mayer,  
14 Brown, Rowe & Maw, for defendant Sir Philip Watts.

15 MS. LIEBERMAN: Sharan Lieberman with  
16 Mayer, Brown, Rowe & Maw for defendant Sir Philip  
17 Watts.

18 MS. WICKHEM: Rebecca Wickhem of Foley &  
19 Lardner, LLP, for Judith Boynton.

20 THE VIDEOGRAPHER: The court reporter  
21 today is Laurie Bangart-Smith. Would the reporter  
22 please swear in the witness.

23

24

25 ///

0009

1 JOHN MALCOLM, October 20, 2006

2 JOHN MALCOLM,

3 having been duly sworn, testified as follows:

4 EXAMINATION BY COUNSEL FOR PLAINTIFFS

5 BY MR. MACFALL:

6 Q Good morning, Mr. Malcolm.

7 A Good morning, sir.

8 Q We met a few minutes ago. I'm Tim

9 MacFall, litigation pending against Shell. I

10 believe you've had your deposition taken before,

11 because I've seen a transcript, but just to go

12 over some of the ground rules, if you have any

13 questions, please feel free to ask. If at any

14 point you'd like to take a break or would like to

15 discuss anything with your attorney, please let me

16 know, and I'm sure we can accommodate you. While

17 the deposition is being video-recorded, it is also

18 being stenographically transcribed, so in order to

19 have a clean and accurate record, it's necessary

20 for you to speak audibly and verbally in response

21 to the questions.

22 A Thank you, sir.

23 Q As I indicated before, I believe that

24 you've had your deposition taken before. Is that

25 correct, sir?

0010

1 JOHN MALCOLM, October 20, 2006

2 A That is correct. Once.

3 Q Was that deposition conducted by the

4 Securities & Exchange Commission?

5 A That is correct.

6 Q Separate and apart from that deposition,

7 have you ever had your deposition taken?

8 A No.

9 Q Could you please briefly describe for me

10 your educational background, beginning with

11 university.

12 A Certainly. I went to University in

13 Edinburgh, Scotland. The name of the University

14 was the Heriot-Watt University. That's spelled

15 H-E-R-I-O-T, dash, W-A-T-T. My first degree was

16 in electrical and electronic engineering for four  
17 years. That was between 1968 and 1972. My second  
18 degree was a Ph.D. at the same university in  
19 process control systems; to be exact, the  
20 computer-based control of non-linear systems.

21 Q Mr. Malcolm, could you also please  
22 describe for me very briefly your educational  
23 background after you left university.

24 A Certainly. My -- I started to work for,  
25 in 1975 for ICI, who are Imperial Chemical

0011

1 JOHN MALCOLM, October 20, 2006  
2 Industries of the U.K. I worked in Heavy  
3 Chemicals in a range of engineering and operations  
4 positions. I worked for them between 1975 and  
5 1981. In 1981 I left ICI and I joined Bahrain  
6 Petroleum Company. It's a long time ago. They've  
7 got the initials BAPCO, Bahrain Petroleum Company.  
8 Bahrain is spelled B-A-H-R-A-I-N. That was a  
9 refining company. I was engaged in engineering  
10 activities, product activities, effectively  
11 regenerating one of the oldest refineries in the  
12 Gulf.

13 I stayed in BAPCO until December 1983.  
14 I then returned to Edinburgh, Scotland. I was a  
15 University Lecturer and Research Fellow at the  
16 Heriot-Watt University. I also had a small  
17 consultancy business associated with my time at  
18 Heriot-Watt.

19 In 1986, January 1986, I joined Shell.  
20 After a short orientation course in February 1986,  
21 I went to Petroleum Development Oman, which is a  
22 Government joint venture, Government private joint  
23 venture that is 60 percent Government, 34 percent  
24 Shell, four percent Total and two percent Partex  
25 from Portugal. Partex is P-A-R-T-E-X.

0012

1 JOHN MALCOLM, October 20, 2006

2 I stayed -- my first job in PDO was head  
3 of Instrumentation and Process Control. I held  
4 that job for just about over a year. I then went  
5 on and was head of Central Engineering, which was  
6 the technical support to Operations on engineering



7 projects. I left PDO around mid-1988, about  
8 July 1988. I went back to The Hague and I worked  
9 for SIPM, which is the Shell head office in The  
10 Hague. It's an old -- now it's no longer there.  
11 It's Shell International Petroleum Maatschapij,  
12 and I would find great difficulty spelling  
13 "Maatschapij" at this moment in time, but the word  
14 is Dutch for "company." I was in SIPM for about  
15 two and a half years. My first job was within  
16 Prospect Engineering, which was effectively  
17 evaluating the costing and feasibility of new  
18 prospects.

19 My second job, which was the one that  
20 took up the majority of time, was within the  
21 Standardization Spearhead, which was looking at  
22 the standards that would be applied in engineering  
23 operations throughout Shell, and it was a review  
24 of those standards to try to make them efficient  
25 and appropriate and more in line with

0013

1 JOHN MALCOLM, October 20, 2006  
2 international standards.

3 In December 1990 I went to Shell ExPro.  
4 E-X-P-R-O. That is an abbreviation for Shell,  
5 brackets, U.K. Exploration and Production,  
6 Limited, in Aberdeen. I was a Project Manager  
7 there, running a series of projects up to  
8 February 1995.

9 In 1995, February of 1995 I returned to  
10 SIPM in The Hague. My first job was as a Business  
11 Advisor for Argentina and Canada. That lasted for  
12 a short time, about three or four months. I was  
13 then involved in the Study Team which was looking  
14 at how EPT, the Technology Center, and Shell was  
15 going to be reconfigured for the future. I was in  
16 that position for something like about 18 months.  
17 I then held a position in looking after Management  
18 Systems within EPT, and I held that position for  
19 about a year.

20 The following year I was a Vice  
21 President of our Technology Center, EPT, and I did  
22 that until I think January 1998. In January 1998  
23 I took over a role again as a Business Advisor for



24 our companies in the Far East, in particular  
25 Brunei, but also some of the other companies  
0014

1 JOHN MALCOLM, October 20, 2006  
2 associated there, and I held that job until  
3 roundabout 1999, June 1999, June/July 1999.  
4 I then went from The Hague to Damascus  
5 and Syria, and I ran the -- I was General Manager  
6 for the Joint Venture Company between the  
7 Government of Syria, represented by the Syrian  
8 Petroleum Company, Shell, and at that time a  
9 company called Veba of Germany, V-E-B-A. Their  
10 shareholding was later taken over by PetroCanada.  
11 I was in -- I did that position up to 2001. In  
12 2001 I also assumed the position of General  
13 Manager for Syria Shell Petroleum Development, in  
14 addition to my job as General Manager of El Furat  
15 Petroleum Company, the joint venture, EFPC.  
16 Sorry. El Furat, F-U-R-A-T, Petroleum Company.  
17 "El Furat" is the Arabic word for the "Euphrates"  
18 as we know it in English. And I stayed in Syria  
19 until September 2002.

20 In early October, I think it was the 5th  
21 or 6th of October 2002, I went to Oman. I had a  
22 familiarization period of about three weeks, and  
23 on the 1st of November 2002 I took over my present  
24 position, which is Managing Director of Petroleum  
25 Development Oman. It is again, as I said

0015

1 JOHN MALCOLM, October 20, 2006  
2 originally, a Government private joint venture.  
3 It is predominantly an Omani company.

4 Q You described the ownership, just the  
5 various ownership interests in -- I'm going to  
6 refer to it as "PDO" for short.

7 A It would save a lot of words today.

8 Q Could you please describe for me the  
9 corporate structure organizationally of PDO.

10 A Yes. The situation in PDO is that there  
11 are two senior positions in PDO. One is the  
12 Managing Director, and the second is a Deputy  
13 Managing Director. We sometimes refer to these as  
14 "MD" and "DMD," so if you hear me slipping into

15 those acronyms, you must forgive me.

16 The management of PDO reports to a Board  
17 of Directors, and the Board of Directors of PDO  
18 comprises of four public shareholding Directors.  
19 Those public shareholders generally come from the  
20 Ministry of Finance, the Ministry of National  
21 Economy or the Ministry of Oil and Gas. There are  
22 also four private Directors; two for Shell, one  
23 for Total, and one for Partex. And there is also  
24 the Chairman of the company, and the Chairman of  
25 the company is again a Government Director, and at

0016

1 JOHN MALCOLM, October 20, 2006  
2 this moment in time the Government Director is  
3 Dr. Rumhy, His Excellency Dr. Rumhy. "Rumhy" is  
4 spelled R-U-M-H-Y. And His Excellency Dr. Rumhy  
5 is also the Minister of Oil and Gas.

6 So the management of PDO report to the  
7 Board of Directors, and any significant investment  
8 proposals and the like are, of course, discussed  
9 by the Board of Directors, but approval is then  
10 given by the shareholders, the shareholders being  
11 the Government of Oman, Shell, Total and Partex.

12 Today it is slightly different than it  
13 was when I arrived. When I arrived we had eight  
14 Directors of the company. Today we have 12, but  
15 we have myself and the Deputy Managing Director,  
16 Dr. Abdulla Lomki (phonetic), who is also the  
17 Technical Director of the company. We have  
18 another ten Directors covering the functions and  
19 the assets of the company, with individual  
20 responsibilities. Today we have -- two thirds of  
21 the Directors of the company are Omani. Eight are  
22 Omani, and four, including myself, are  
23 ex-patriots.

24 We have two aspects of the company that  
25 I think are required for clarification. One is

0017

1 JOHN MALCOLM, October 20, 2006  
2 the oil business of the company, and that oil  
3 business is shared 60/34/4/2, as I've said before.  
4 And then we also operate the gas business of the  
5 company on behalf of the Government of Oman, and

6 in that we have a separate Gas Board that we  
7 report to that today has no private shareholders  
8 on it. It is purely a Government Board of  
9 Directors. And those Directors are actually in  
10 the process of change at this moment in time, but  
11 they are all Government appointees.

12 And when I speak today, unless I speak  
13 otherwise, I will be speaking about the oil  
14 business of PDO rather than the gas and condensate  
15 business of PDO that we operate on behalf of the  
16 Government. If you require discussion of that,  
17 that is also all right, but when you hear my  
18 general responses, they are all in the mindset of  
19 the oil business in which Shell has a 34 percent  
20 interest.

21 Q I appreciate that. Thank you.

22 Mr. Malcolm, could you please describe  
23 for me generally your duties and responsibilities  
24 in your position as Managing Director of PDO.

25 A First and foremost, I report to the

0018

1 JOHN MALCOLM, October 20, 2006  
2 Board of Directors. I have a number of duties  
3 that are set out within what we call the  
4 Concession Agreement. The Concession Agreement is  
5 an agreement between the Government of Oman and  
6 the private shareholders. There are a number of  
7 associated documents with that, one of which is  
8 known as the Operating Agreement, and the  
9 Operating Agreement is a key agreement under which  
10 PDO operates.

11 We effectively present to our Board of  
12 Directors generally in the last quarter of year a  
13 Business Plan. Sometimes this is referred to as  
14 "BP" for Business Plan, and the number that  
15 follows it is generally the Business Plan for the  
16 following year. So for example, this year we are  
17 working on the Business Plan '07, which is to do  
18 with 2007 onwards, but it is a five-year plan with  
19 detail within that first year.

20 I've also got a duty to propose to the  
21 Board as well as delivering the Plan, the changes  
22 that need to be made in the organization in order

23 that we keep the organization -- when I say "the  
24 organization," I mean PDO -- alive and a healthy  
25 organization, and also the recruitment and

0019

1 JOHN MALCOLM, October 20, 2006  
2 development of staff such that we have got the  
3 appropriate organizational health within the  
4 organization to deliver our Plans.

5 The Board takes our Business Plan and,  
6 after a great deal of discussion, endorses that  
7 Business Plan, and generally gives me a capital  
8 limit, an operating limit within which to work for  
9 the following year, though the major investment  
10 decisions, of course, require to have shareholder  
11 approval, and the major contract approvals also  
12 have to have shareholder approval.

13 We have -- to put it in context -- just  
14 under 5,000 employees, about 4,900 employees. If  
15 you also include the number of contractors that we  
16 have, we have something like, employees and  
17 contractors, maybe something in the company of  
18 about 20,000 people. We have over a hundred  
19 flowing fields. We work within a concession area  
20 that is just a little bit smaller than the size of  
21 England. We have present something like about six  
22 airports in there, many thousands of kilometers of  
23 roads, and a pipeline system that runs all the way  
24 up the country, and we export all the oil for the  
25 country. We produce 90 odd percent of that oil,

0020

1 JOHN MALCOLM, October 20, 2006  
2 but we also export the oil for other parties as  
3 well, transport and export.

4 We have our own electricity generation  
5 system, 132 KV system. We have our own datacoms,  
6 IT infrastructure within the country. So it is a  
7 major undertaking between our two major production  
8 centers. Between Fahud and Marmul is  
9 approximately about 400 miles, so it gives a scale  
10 of the geographical aspect. Also, unlike many  
11 countries in the Middle East, our oil comes from a  
12 large number of smaller fields, although we have  
13 20 of what we call "large fields." These are

14 relatively small compared to the giant fields in  
15 Saudi Arabia and elsewhere in the region.

16 Q With respect to the establishments of  
17 budgets for PDO, was that set by the PDO Board as  
18 opposed to Shell?

19 A Yes. Effectively the shareholders  
20 provide the cash for PDO, both operating and  
21 capital, in proportion to their shareholding, but  
22 the budgets for PDO are set once a year. There  
23 are revisions to those budgets, of course, as with  
24 any other business, and PDO effectively makes cash  
25 calls on its shareholders as it goes through the

0021

1 JOHN MALCOLM, October 20, 2006  
2 year in order to meet the commitments that we  
3 have. We hold relatively little money in the bank  
4 compared to as a percentage of our budgets, but we  
5 have a continual cash call mechanism, so we have  
6 continual predictions of how much money is  
7 required on a weekly basis.

8 Q You described for me essentially the  
9 reporting structure in your description of PDO  
10 within PDO. Did you report to anybody within  
11 Royal Dutch/Shell?

12 MR. SMITH: In his current position?

13 MR. MACFALL: In his current position.

14 Thank you.

15 THE WITNESS: Yeah, first and foremost,  
16 my -- in the case of conflict, my loyalties first  
17 and foremost are to Petroleum Development Oman. I  
18 am a -- if I can use a very simple phrase, "I am a  
19 Shell man" trying to do my best for PDO. In case  
20 of conflict either with the Government or with  
21 Shell or with Partex or with Total with any of the  
22 shareholders, I am continually trying to do the  
23 best for PDO. I have a dotted line type reporting  
24 relationship to the Regional Business Director in  
25 Dubai, a gentleman known as Raoul Restucci, but in

0022

1 JOHN MALCOLM, October 20, 2006  
2 all cases, although we take advice from Shell on  
3 say certain technical matters and the like, where  
4 there is any conflict in any way, I then must

5 always represent PDO before any aspects of Shell.

6 And if you look at any minutes of  
7 meetings or anything from board meetings, you will  
8 see that both myself and the Deputy Managing  
9 Director, and the Deputy Managing Director is a  
10 Government appointee, whereas effectively I am one  
11 of the list of candidates that Shell proposes to  
12 be Managing Director, and the Government selects  
13 from that list, which is always a minimum of two  
14 on the list. I -- my first and foremost, my duty  
15 must always be to PDO.

16 BY MR. MACFALL:

17 Q Is your tenure as Managing Director of  
18 PDO subject to periodic approval by the Government  
19 of Oman?

20 A I, I think, I think that is a very nice  
21 way of putting it, sir. It's -- of course, I am  
22 like the Managing Director of any company; if I  
23 lose the support and trust of my Board of  
24 Directors, then it would become impossible for me  
25 to do my job. So effectively the Board of

0023

1 JOHN MALCOLM, October 20, 2006  
2 Directors approves my nomination as MD. My  
3 understanding is that I will remain in the job --  
4 the job is nominally for four years, but in the  
5 past people have stayed less than four years and  
6 people have stayed more than four years. I have  
7 been in it four years, and I haven't heard  
8 anything as yet if I'm staying or otherwise, but  
9 generally I think as long as the Government  
10 shareholder and the private shareholders both have  
11 faith in the Managing Director, then he stays  
12 there until there is a point where Shell would  
13 propose that another Managing Director would take  
14 his place. Of course, if that trust was lost,  
15 then the Managing Director, I have no doubt, would  
16 leave fairly quickly.

17 Q And I think I know the answer to this,  
18 but just so I'm perfectly clear, your salary is  
19 actually paid by Shell, correct?

20 A No.

21 Q I'm sorry. I misunderstood.



22 A What happens both for myself and for all  
23 Shell ex-patriots within PDO is that we are  
24 rewarded on a system that is known as EBAS,  
25 Ex-patriot Basic Administration System, if I've  
0024

1 JOHN MALCOLM, October 20, 2006  
2 got the four-letter acronym correct, Ex-patriot  
3 Basic Administration System, and this tries to  
4 find an equitable and efficient way in order to  
5 make sure that people of different nationalities  
6 have got the incentive to work overseas, but that  
7 they -- that that relative incentive is  
8 maintained.

9 So effectively we follow the Shell EBAS  
10 system. For those employees who we have who are  
11 direct hire to PDO, we split them on a system that  
12 looks very similar to EBAS and some who are paid  
13 in local terms, depending on what their skills are  
14 and depending on how long they're going to be  
15 there for. So effectively my salary remuneration  
16 is advised PDO, but my salary is actually paid by  
17 PDO, and -- but to be perfectly clear, there is  
18 advice given from Shell to PDO as to what my  
19 salary should be, and so there is a link. The  
20 salary is paid by PDO, but there is advice given  
21 by Shell to PDO as to what my salary should be.

22 Q Thanks very much for cleaning that up.  
23 Mr. Malcolm, are you familiar with the  
24 term "proved reserves"?

25 A I am familiar with the term "proved  
0025

1 JOHN MALCOLM, October 20, 2006  
2 reserves."

3 Q Could you explain for me your current  
4 understanding of that term.

5 A Yes, certainly. My current  
6 understanding of that term is that proved reserves  
7 are all about reasonable certainty, and there are  
8 in actual fact a number of definitions in the  
9 world. The definition that I think that we are  
10 here today and is common is the SEC definition of  
11 proved reserves, but also there are other  
12 definitions, like the SPE definition, the Society



13 of Petroleum Engineers.

14 And in different states in the world  
15 there are different definitions of what proved  
16 reserves are, but in my understanding -- and I  
17 would like to reemphasize at this point that I am  
18 a surface engineer rather than a subsurface  
19 engineer, so those who wish to go into terminology  
20 on permeability, porosity, and the like, you're  
21 dealing with the wrong man. I have an  
22 understanding of it, but I am not subsurface man,  
23 so it is about relevant certainty, and I think  
24 that what we're talking about here is the  
25 reporting against certain standards, in this case

0026

1 JOHN MALCOLM, October 20, 2006  
2 the reporting against SEC standard or SPE standard  
3 or against whatever standards would be required in  
4 a particular jurisdiction in the world.

5 Q The definition of "proved reserves" that  
6 you just provided, or your understanding as you  
7 just described it, rather, could you please tell  
8 me what the basis for that understanding is.

9 A The basis for that understanding?

10 Q Yes, sir.

11 A I think that if I would say that up to  
12 say the reserves crisis in Shell, my understanding  
13 was one of -- my general understanding was based  
14 in the concepts of P85, the probability of  
15 85 percent probability. I think that post that  
16 time -- and you quite rightly asked me for my  
17 understanding today. Apart from the experience  
18 I've gained through that, also within Shell today  
19 and for all people working in Joint Ventures who  
20 may have anything to do with reporting or helping  
21 Shell report in proved reserves, there is a need  
22 for everybody to go on some basic course as to  
23 what the understanding of SEC proved reserves are.  
24 And for those who are required to perform any  
25 reporting functions, of course, they have other

0027

1 JOHN MALCOLM, October 20, 2006  
2 training requirements.

3 I have to state that from my position

4 today as Managing Director of PDO, on the oil side  
5 of the business, we run the business then and now  
6 on the basis of expectation reserves, before 2003  
7 and post-2003, on the basis of expectation  
8 reserves.

9 Q Could you explain for me the difference  
10 between expectation reserves and proved reserves.

11 A My understanding, sir, is that  
12 expectation reserves are those which some people  
13 talk about probability of P50. They have a  
14 possibility of going up and they have a  
15 possibility of going down, and that should be  
16 fairly evenly balanced. They don't have the same  
17 certainty as P85 or proved reserves, by  
18 definition, but they are a balanced understanding  
19 of looking forward to what we believe are the  
20 expected -- the word "expectation reserves" of the  
21 company.

22 They are important for an operator in  
23 that the expectation reserves are -- there is a  
24 link, and the link is not always totally clear,  
25 but there's a link between expectation reserves

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1 JOHN MALCOLM, October 20, 2006  
2 and expected production, so there's a link between  
3 expectation reserves and the expected production.  
4 We plan our production again on a P50 basis, on a  
5 50/50 basis going forward.

6 Q When you say "we" plan, you're referring  
7 to PDO, correct?

8 A Sorry. You are perfectly correct. When  
9 I use the word "we," I am talking about PDO.

10 Q For internal purposes within PDO, am I  
11 correct that expectation reserves are normally  
12 utilized?

13 A Yes. Within PDO our expectation  
14 reserves will normally be utilized. Where we did  
15 and we have changed on our annual reports, that  
16 where we previously published reserves on our  
17 annual reports, that we used expectation reserves.  
18 We never published proved reserves.

19 THE REPORTER: I'm sorry. You need to  
20 slow down a little bit.

(Discussion off the written record.)

THE WITNESS: So although we previously used to report reserves in our Annual Report, when we did so, we reported as expectation reserves. This is on an oil basis. On -- for clarification,

JOHN MALCOLM, October 20, 2006

and I know I said I would only talk about the oil side. On the gas side of our business, we have proved reserves, but they are associated with the Government.

I also have to advise you that effective from the new Concession Agreement, which was the 1st of January 2005, inbuilt into that Concession Agreement was the need for us to produce two sets of accountancy standards. Prior to -- in our old Concession Agreement we reported on what we called Petroleum Accounting Standards, which used the depreciation that was built into the Concession Agreement. Under the new Concession Agreement effective 1/1/2005, we have to report also to IFRS, the International, International Financial Reporting Standard. I think I've got the terminology correct here.

And under IFRS we do the depreciation on a unit-of-production basis, and that unit-of-production basis is against proved reserves, but that took place effectively from the 1st of January 2005, and we effectively put in place during 2004 to ensure that our -- during 2004 we put in place a capability that we had

JOHN MALCOLM, October 20, 2006

proved reserves in place. The standard that we used, again for clarification, is the SEC standard.

BY MR. MACFALL:

Q Although PDO utilizes expectation reserves for internal purposes, did Shell report proved reserves in connection with PDO as a consequence of its holdings in PDO?

MR. SMITH: Objection to form.

THE WITNESS: I am sure -- I believe,

12 sir, and again that depending on where the shares  
13 are held, that probably all the shareholders had  
14 to report back their reserves holdings in PDO to  
15 whatever standard that they were using, but that  
16 was a reporting of the private shareholders back  
17 to their parent companies.

18 BY MR. MACFALL:

19 Q Were you involved in the reserves  
20 reporting process from PDO to Shell?

21 A I was not --

22 MR. SMITH: Objection to form and  
23 foundation.

24 THE WITNESS: Maybe I could step one  
25 back, sir, and I could just --

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1 JOHN MALCOLM, October 20, 2006

2 BY MR. MACFALL:

3 Q Absolutely.

4 A -- rephrase it if it's acceptable to  
5 you, is that PDO provides to all its shareholders  
6 information that it may require for their own  
7 internal reporting. We provide information to the  
8 Government, we provide information to the private  
9 shareholders as a body, and we provide information  
10 to any one of those individual private  
11 shareholders in a format that they may so require.  
12 In that latter category we did provide as PDO, in  
13 a format as they so required, information to Shell  
14 related to the numbers that were held in PDO, but  
15 this was a service that we were providing to Shell  
16 in line with whatever guidelines that they give  
17 us.

18 Q Specifically as part of the information  
19 provided by PDO to Shell, were proved reserves  
20 that had been booked by PDO included?

21 MR. SMITH: Objection to form and  
22 foundation.

23 THE WITNESS: I think again, sir, to go  
24 back again, PDO ran -- when you talked about  
25 booked, we booked expectation reserves. We had an

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1 JOHN MALCOLM, October 20, 2006

2 Annual Review of Petroleum Resources, an ARPR book

3 that we issued. There was a proved reserves  
4 column on that book when I arrived in PDO at the  
5 end of 2002, but it was generally acknowledged  
6 that that proved reserves number had slipped with  
7 time, and that the meaningful number in the ARPR,  
8 which we used and we needed for our company, was  
9 the expectation number.

10 BY MR. MACFALL:

11 Q With respect to that proved reserves  
12 number that was reported as part of the ARPR  
13 process, who actually calculated that number; was  
14 it PDO or Shell?

15 MR. SMITH: Objection to form and  
16 foundation.

17 THE WITNESS: I think again for  
18 clarification, we have to be careful. There's two  
19 different ARPRs. There is an ARPR that was PDO's  
20 ARPR, and I believe, although I'm not up to date  
21 with it and I can only surmise that I think Shell  
22 had a similar term as well. So the ARPR, when I'm  
23 talking about ARPR, I'm talking about PDO's ARPR,  
24 which was an expectation reserves number that did  
25 have a column for proved reserves in there on a

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1 JOHN MALCOLM, October 20, 2006  
2 kind of P85 basis, not on a rule basis as per SEC,  
3 but that number definitely during the early 2000  
4 onwards was generally accepted and was not a sound  
5 foundation. It was just an indicative number.  
6 Shell, on the other hand, may have an ARPR, and  
7 they may have proved reserves in another number.  
8 Again to go back as before, if any shareholder  
9 requests us for information or requests us to  
10 provide information in a certain format according  
11 to their guidelines, we will do so, "we" being  
12 PDO. Sorry.

13 BY MR. MACFALL:

14 Q Thank you. I realize that I am  
15 articulating this poorly, and I apologize, but  
16 what I'm trying to get at, sir, is the numbers  
17 column in the PDO ARPR which you said was reported  
18 on a P85 basis, do you know who -- and by "who" I  
19 mean PDO or -- withdrawn. With respect to the

20 proved reserves column in the PDO ARPR, do you  
21 know how that number was derived?

22 MR. SMITH: Objection to form and  
23 foundation.

24 THE WITNESS: No, I do not know how that  
25 number was derived, but I can tell you, though, if  
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1 JOHN MALCOLM, October 20, 2006  
2 I go back to our requirements under IFRS, that we  
3 have to put in place or have put in place, was  
4 effective the 1st of January 2005, that our ARPR  
5 now, today, has a proved reserves number per field  
6 that is generally in line with the SEC  
7 requirements.

8 BY MR. MACFALL:

9 Q Now, I believe you stated that at the  
10 time you arrived at PDO it was generally  
11 understood that the proved reserves number  
12 reported in PDO's ARPR was no longer accurate or  
13 not sound; is that correct?

14 MR. SMITH: Objection to form.

15 THE WITNESS: That is not quite what I  
16 said. It -- again if we go back to the fact that  
17 PDO was run on an expectation basis, the number  
18 there was concentration on within those -- and  
19 because at that point depreciation did not require  
20 proved reserves as a calculation, the column that  
21 was there for a proved reserves number was of  
22 relatively little relevance to us in running the  
23 day-to-day business of PDO. So the fact of what  
24 that number contained was, from an operator's  
25 point of view, was of relatively little  
0035

1 JOHN MALCOLM, October 20, 2006  
2 significance. Today, however, as we are now  
3 required under our new Concession Agreement which  
4 ran from the 1st of January 2005, that number does  
5 have significance for us, in order to ensure that  
6 we report accurately our financial statements, one  
7 financial statement under the IFRS and another  
8 financial statement that we do which is under  
9 Petroleum Accounts, which reflects the Concession  
10 Agreement --



11 THE REPORTER: What was the last phrase?

12 THE WITNESS: So we have two sets of

13 accounts. One is IFRS, which reflects

14 depreciation on a unit-of-production basis, and a

15 second set of accounts which we call the Petroleum

16 Accounts, which reflects the concession

17 depreciation schedule, both -- these are two

18 different schedules, but that again, sir, to

19 emphasize -- I'm sorry if I'm repetitive, but I

20 just want to try to clarify. That is effective

21 from the 1st of January 2005.

22 BY MR. MACFALL:

23 Q I appreciate that Mr. Malcolm. Thank

24 you.

25 At the time that you arrived at PDO, did

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1 JOHN MALCOLM, October 20, 2006

2 you have an understanding as to the accuracy of

3 the proved reserves number being reported in PDO's

4 ARPR?

5 MR. SMITH: Objection to form and

6 foundation.

7 THE WITNESS: I did not have -- I came

8 into PDO in November 2002. We had -- as you will

9 have read all the reports, we had a number of

10 different problems at that time. I cannot say

11 that proved reserves was a concern for me at that

12 moment in time.

13 What was a significant concern for me

14 and for all the shareholders was the production

15 fall-off that was occurring, and the reason for

16 that production fall-off and understanding those

17 reasons in order that we mitigate that fall-off,

18 and I think that from -- and I can only surmise

19 here, and I do that very carefully. I think there

20 was concern from the Shell shareholder about the

21 reputation of, impact of this fall-off in

22 production reserves or fall-off in production

23 within PDO.

24 So we had, you know, concerns within PDO

25 as to our reputation in the outside world, and

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1 JOHN MALCOLM, October 20, 2006



2 there was deep concerns within the Government and  
3 under private shareholders and the significant  
4 fall-off in production that was occurring in 2002  
5 and was predicted to occur in 2003.

6 BY MR. MACFALL:

7 Q With regard to your understanding that  
8 there was concern by the Shell shareholder with  
9 regard to the reputational impact of the  
10 production fall-off, what is the basis of your  
11 understanding of that?

12 A I think the basis of my understanding on  
13 that is that when I went to PDO, the tremendous  
14 support that I received from Senior Management in  
15 Shell in terms of, for example, the availability  
16 of new Senior Directors of the company, the need  
17 to bring in specific expertise, I -- you know, it  
18 was a difficult job at the time, but it was very  
19 clear that this long relationship between  
20 predominantly Shell and the Government, but the  
21 private shareholders and the Government in  
22 particular, Shell being the 85 percent private  
23 shareholder, there was concern that -- I think a  
24 feeling that, not just about reputation, but, as  
25 in all relationships, long-standing

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1 JOHN MALCOLM, October 20, 2006  
2 relationships -- I think it's fair to bear in mind  
3 that this is a relationship that goes back over 40  
4 years -- that there was a need to do something to  
5 get the situation regulated, to get the production  
6 back according to plan again, and the support both  
7 from the Government side and from the Shell side  
8 that I received was outstanding.

9 Q With regard to the Shell shareholder  
10 concern regarding the representational impact of  
11 the production fall-off, was that concern about  
12 its reputation with the Omani Government?

13 MR. SMITH: Objection to form.

14 THE WITNESS: I cannot speak for Shell.  
15 If you wish me to speak as the Managing Director  
16 of PDO, I think that they had concern, of course,  
17 with their reputation not just within Oman, but  
18 the globalized effect that it can have, but

19 especially within the region where PDO, over a  
20 period of say 20 years, from 1980 onwards, had  
21 been the most outstanding company, one of the most  
22 outstanding companies in the Middle East, with a  
23 relatively difficult resource base, hydrocarbon  
24 resource base, and an ability to build a  
25 production to over 800,000 barrels a day over  
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1 JOHN MALCOLM, October 20, 2006  
2 those 20 years, that had been a truly outstanding  
3 feat. And I think -- from my point of view, I  
4 think everybody within PDO was concerned about  
5 their reputation. I know that all the PDO staff  
6 were concerned about not just whether or not they  
7 were letting down the shareholders, but whether  
8 they were letting down the country, because, of  
9 course, a significant percentage of the income of  
10 Oman comes from PDO.

11 BY MR. MACFALL:

12 Q Could you generally describe for me the  
13 nature of the production fall-off which you've  
14 just referenced.

15 MR. SMITH: Objection to form and  
16 foundation.

17 THE WITNESS: I could describe for you  
18 roughly how the numbers were within 2002 and 2003.

19 BY MR. MACFALL:

20 Q Why don't we break it down this way. It  
21 may be a little bit easier. Are you familiar with  
22 the production rates at PDO from the seventies  
23 through the time that you were actually positioned  
24 there as Managing Director?

25 A I have a detailed understanding of the  
0040

1 JOHN MALCOLM, October 20, 2006  
2 production numbers from 2002 onwards. I have  
3 general understanding of the production numbers  
4 prior to that, and I have still memories after 20  
5 odd years of what the production numbers were in  
6 1986.

7 Q Based on that understanding, did there  
8 come a time that you can recall when the  
9 production rate at PDO declined?

10 A I think the --

11 MR. SMITH: Objection to form.

12 THE WITNESS: I think that if you go  
13 back over the history of PDO from its first  
14 shipment in 1967, it had -- actually, I can think  
15 of at least two notable points where it declined,  
16 one of those being in 1972, so it has gone through  
17 a number of waves of development. Whether or not  
18 you get a decline generally means whether or not  
19 the new wave of development started before the  
20 last wave rolled out.

21 BY MR. MACFALL:

22 Q Following the decline, the initial  
23 decline in '72 that you are aware of, did the  
24 production rates then increase?

25 A If you take say the history between say  
0041

1 JOHN MALCOLM, October 20, 2006  
2 the late seventies, especially from about 1980  
3 onwards, around about 1980 -- and I need to check  
4 for you the exact dates, but roundabout 1980 there  
5 was a major infrastructure development put in in  
6 Oman that effectively -- prior to that time most  
7 of the development was in North Oman, and they  
8 built a pipeline system that ran from the coast  
9 near Muscat. Our point, our offices on the coast  
10 are known as Mina Al Fahal, M-I-N-A, A-L,  
11 F-A-H-A-L, were sometimes referred to as "MAF."  
12 And MAF is near Muscat, and that is the point at  
13 which we'd load the tankers, and there was a new  
14 pipeline system that was run all the way down to  
15 the south of Oman to Marmul, and this allowed the  
16 development of a large number of small fields  
17 right down this pipeline system.

18 And the business model that PDO had at  
19 that time, which was an extremely successful  
20 business model, was one of finding, by  
21 exploration, small fields, and then very quickly  
22 developing those fields and hooking them up to  
23 this pipeline. And so you see that from right  
24 about 1980 onwards, that "find it, develop it,  
25 hook it up" mentality was an extremely successful

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1 JOHN MALCOLM, October 20, 2006  
2 business model for PDO, and which they did in a  
3 very cost-effective manner. And I remember some  
4 of that from my time in '86 to '88. The other  
5 parts, of course, I have to take from what I've  
6 read.

7 Q Did there come a time subsequent to the  
8 period that you just described when Oman  
9 experienced -- again experienced decline in  
10 production rates?

11 A My understanding from reading the  
12 figures is that around about '99/2000 we saw --  
13 although there was some relatively minor, in  
14 percentage terms, missing of production targets,  
15 the production tended to plateau right about '99,  
16 2000, 2001, around about 800,000 plus barrels per  
17 day. I use that as a generality, around about  
18 830,000, but of that type.

19 Q Are you familiar with the Business Plans  
20 that are generated at PDO?

21 MR. SMITH: Objection to form. While  
22 he's been there or a different time frame?

23 BY MR. MACFALL:

24 Q While you've been there. Thank you.

25 A I am familiar, of course, with the  
0043

1 JOHN MALCOLM, October 20, 2006  
2 Business Plans that were issued certainly at the  
3 end of 2003, 2004, into 2005, and the one that  
4 we're writing just now at the end of 2006, the  
5 Business Plan that was in place in November 2002  
6 was in place when I came to the company, and so  
7 my -- although I am familiar with that Plan, I am  
8 familiar with that Plan from reading the Plan and  
9 executing the Plan rather than building and  
10 developing the Plan.

11 Q Do you recall if the Business Plan that  
12 was in place when you arrived at PDO in November  
13 of 2002 contained production targets with regard  
14 to oil in Oman?

15 A Yes, I do.

16 Q Do you recall approximately what that  
17 target was in the Business Plan that was effective

18 upon your arrival at PDO?

19 A Again, sir, for clarification so I can  
20 answer fully your question, there were effectively  
21 two Business Plans in place. One was a Business  
22 Plan that was going to the Board in October 2002  
23 to be approved for 2003 onwards, so that is what  
24 we call the BP 2003. There was also the end of  
25 the Business Plan for BP 2002, which I don't know  
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1 JOHN MALCOLM, October 20, 2006  
2 but would have been issued around about  
3 November 2001. So the production in 2002 was  
4 relative to the plan that had been put in place at  
5 the end of 2001, whereas the production for 2003  
6 was relative to the Plan that was in place when I  
7 walked into PDO in October 2002.

8 Q Thank you. Were you familiar with the  
9 Plan that was in place for 2002 which had been  
10 formulated in November of 2001?

11 A I was -- I was aware of it, but I was  
12 aware obviously in more detail with the 2003 plan  
13 than I was with the 2002 plan, because I was  
14 coming in looking forward for the following year.  
15 You come and take over a company in November,  
16 there is a limit to your flexibility in what you  
17 can do in the last two months of the year, so my  
18 key focus was on 2003 rather than 2002, but I can  
19 still remember the numbers roughly that were in  
20 place in 2002, and if I remember correctly, I  
21 think that the average production in 2002 for the  
22 year was something like 773,000 barrels a day. It  
23 was 770,000 barrels a day, and that I have to do  
24 from memory, sir. That is not an exact figure.

25 Q I do appreciate that. Do you recall if  
0045

1 JOHN MALCOLM, October 20, 2006  
2 the 2002 -- if the Business Plan in place with  
3 respect to 2002 contained production targets for  
4 2002?

5 A My memory serves me to remember that  
6 there were really two targets for 2002. There was  
7 an original target, if I remember correctly, of  
8 about 830,000 barrels a day, and this had been

9 revised downwards, I'm not sure what point,  
10 probably near the end of 2001 -- on that you need  
11 to check the facts -- down to 815,000 barrels a  
12 day. So I think that if you took formally to the  
13 Plan that was 815, I think there had been an  
14 aspiration of 830 originally.

15 Q Do you recall upon your arrival at PDO  
16 in November of 2002 if anyone within PDO discussed  
17 with you the failure to meet the 2002 production  
18 target as set forth in PDO's Business Plan?

19 A I think that all the shareholders were  
20 concerned. I had discussions with all of them,  
21 the Government in particular, and at that moment  
22 in time the Chairman of the Board was the  
23 Undersecretary at the Ministry of Oil and Gas,  
24 effectively one level down from the Minister, and  
25 there was obviously deep concern not just about

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1 JOHN MALCOLM, October 20, 2006  
2 the production in 2002, but the predictions for  
3 2003.

4 Q Do you recall what those predictions --  
5 withdrawn. Were you familiar with the predictions  
6 that were being made for 2003?

7 A The 2003 production target was in BP  
8 2003, which was approved at the time I arrived,  
9 and it was a target, 703,000 barrels a day.

10 Q Do you know how that target was  
11 established?

12 A I was not there when the work was done,  
13 sir. To put it into context, around about the  
14 second quarter of the year we made a first pass of  
15 the Business Plan for the following year around  
16 about April, May, so that was done in 2002 when I  
17 was not there, and then there's more detail added  
18 through the summer, and around about September,  
19 generally October, once we get into the fourth  
20 quarter of 2003, that Business Plan is firmed up.  
21 And then from that point there it goes to the  
22 Board for approval, and my understanding is that  
23 the number that was approved was 703, and I have  
24 no -- I was not there, so I have no detailed  
25 knowledge of how it was put together, just an



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1 JOHN MALCOLM, October 20, 2006

2 understanding.

3 Q Do you recall if there was concern  
4 amongst the PDO shareholders that the target for  
5 oil production decreased from approximately 830 or  
6 815 barrels per day to approximately 703 barrels  
7 per day from 2002 to 2003?

8 A Just for clarification, sir, in 2002 my  
9 understanding is that the average production was  
10 around about 770,000, and in 2003 the target was  
11 703,000, so effectively you see that in, from the  
12 aspirations -- and these I only can take from what  
13 I read -- at the end of 2001 of 830 reduced to  
14 815, the production had fallen to 770,000, which  
15 is a significant fall-off, percentage-wise and  
16 absolute-wise, and then the fall-off predicted for  
17 2002, of course, is something like eight, nine  
18 percent. It's 70,000 -- 770 odd thousand. It  
19 was -- that was a significant number, both -- and  
20 I'd like to stress, the numbers I'm quoting you  
21 are average numbers, so you have between the start  
22 of the year and the end of the year, it is the  
23 average number in between, so in actual fact the  
24 deltas are actually bigger than that, so it was  
25 quite a difficult time.

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1 JOHN MALCOLM, October 20, 2006

2 Q Do you remember if you had any  
3 discussions with management at Shell as opposed to  
4 PDO concerning the production decline at PDO in or  
5 about 2002?

6 A Yes. I had discussions. My Key Point  
7 was the Regional Business Director at the time, a  
8 Mr. Din Megat, D-I-N, Megat, M-E-G-A-T. "Din" is  
9 actually short for Zahrudin, Z-A-H-R-U-D-I-N. And  
10 he was the Regional Business Director. He had a  
11 Business Advisor for Oman, a chap called Paul  
12 Mann. And Mr. Megat reported to Mr. Walter van  
13 der Vijver, and Mr. van der Vijver, of course,  
14 reported -- was a member of the CMD, reported to  
15 Mr. Watts, but they -- the Regional Business  
16 Director was kind of the pivotal point.



17 Q Do you recall if you had discussions  
18 with Mr. Megat in or about 2002 about ways to  
19 improve oil production at PDO?

20 A I think that when I came into PDO,  
21 sir -- if I can just rephrase your question and  
22 I'll come back and answer the question if I miss  
23 it.

24 Q That's fine.

25 A When I came into PDO, I was very much  
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1 JOHN MALCOLM, October 20, 2006  
2 into listening mode rather than advocacy mode,  
3 because there was, there was obviously a number of  
4 things happening at once, and so I was trying to  
5 understand, trying to read as many documents as I  
6 could, to listen to our shareholders to try to  
7 look at where the trends were, because there was,  
8 there was very, very significant concern. There  
9 were already plans built into BP 2003 of what we  
10 would need to do in 2003 to try to build a better  
11 future in 2004 plus. So my focus was partly about  
12 2003 but also those things that we were going to  
13 have to try to do in 2003 to ensure that the  
14 future was better for PDO than the short-term  
15 outlook.

16 So I was trying to balance at all times,  
17 and in my discussions with all parts of the  
18 company, both Government and Shell, were the  
19 short-term needs, the medium-term needs and the  
20 longer term needs, and in those first two to three  
21 months it was really trying to understand, trying  
22 to listen to people, trying to listen to my  
23 Management Team, trying to listen to the  
24 Shareholder Advisors, trying to listen to the  
25 Government, but mainly to try to get an

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1 JOHN MALCOLM, October 20, 2006  
2 understanding of what was actually happening in  
3 the company.

4 Q Thank you. Do you recall if --  
5 withdrawn. Do you recall having discussions with  
6 anyone at PDO concerning the reasons for the  
7 decline in production between 2001 and 2002?

8 A Yes. I had discussions, in particular  
9 with our Deputy Managing Director, Dr. Abdulla  
10 Lomki. He is a man of tremendous experience and  
11 who I respect greatly. He is also -- unlike me,  
12 he is a petroleum engineer by background, so we  
13 have -- I hope to think we have complementary  
14 skills, but he has insights and skills that I  
15 value, and today, even today on a, I think almost  
16 on a daily or every two days we sit and talk to  
17 understand, so I had a lot of insights from  
18 Dr. Lomki.

19 I also sat to look with our Corporate  
20 Planners as to how this Plan had been put  
21 together, just again to try to get an  
22 understanding of where we were going. I had  
23 discussions with our Directors in North Oman, I  
24 had discussions with our Directors in South Oman,  
25 and a lot of it was to listen, because the company

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1 JOHN MALCOLM, October 20, 2006  
2 was, was in a very fragile position at that moment  
3 in time. It was a very proud company. I know  
4 "pride" is maybe the wrong word to say, but when  
5 you've had 20 years of going upwards and then to  
6 be faced with such significant shortfalls from  
7 your targets, of course, it hits the morale of the  
8 company.

9 MR. SMITH: Whenever you wrap up at a  
10 convenient line of questioning, we've been going a  
11 little over an hour, time for a break.

12 MR. MACFALL: You can go off the record.

13 THE VIDEOGRAPHER: We are going off the  
14 record. The time is 10:52 a.m.

15 (Whereupon, a short recess was taken.)

16 THE VIDEOGRAPHER: We are back on the  
17 record. The time is 11:11 a.m.

18 BY MR. MACFALL:

19 Q Mr. Malcolm, did there come a time in  
20 2002 when you gained an understanding of the  
21 reasons for the production shortfall or the  
22 production fall-off at PDO?

23 A That is a good question. I think  
24 that -- I think my understanding was really better

25 by say about the end of First Quarter 2003 and  
0052

1 JOHN MALCOLM, October 20, 2006  
2 then significantly better by the end of Second  
3 Quarter 2003, so I think that I took over, for the  
4 last two months of 2002, a very, very hectic time.  
5 I understood a number of things. By the end of  
6 the First Quarter 2003 I had an understanding of  
7 some of our short-term issues. By the end of  
8 Second Quarter 2003, I had a feeling for some of  
9 our longer term issues.

10 Q Could you describe for me your  
11 understanding of the reasons for the shortfall as  
12 of the end of the Second Quarter of 2003.

13 A I can give you the long answer, I can  
14 give you the short answer. Maybe, sir, I could  
15 give you the outline, and then if you want more  
16 depth, we could do that.

17 Q That would be fine.

18 A I think fundamentally, in my opinion --  
19 it is my opinion. I think fundamentally around  
20 about the mid-nineties, PDO's business model  
21 changed and changed from this very successful  
22 company of "find a field, develop the field, hook  
23 it up," to a stage where, although we continued to  
24 find fields with our exploration ventures, the  
25 fields were generally not easy to hook up.

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1 JOHN MALCOLM, October 20, 2006

2 So if you look at the total number of  
3 flowing fields in PDO, it tended to plateau around  
4 about 1988, because there is always a two- to  
5 three-year project time between finding something  
6 and developing it and for it to flow, so the  
7 numbers, if you look at the total numbers, you see  
8 that they're there. We found some very  
9 interesting fields, and we're developing one of  
10 those today, but the time scale just took longer  
11 to develop.

12 I think also that '98, with a  
13 \$10-a-barrel oil price, affected not just PDO but  
14 all the companies within the E&P business. Major  
15 long-term investments at \$10 a barrel were not

16 feasible, so it is -- I think that is also a  
17 distortion, but effectively the, in my opinion,  
18 the business model in PDO had changed, and there  
19 was a need for us to do a number of things.

20 One was to manage our existing  
21 infrastructure better. The second one was for us  
22 to have even more secondary recovery. When I use  
23 that term, I generally mean water injection, but I  
24 also mean gas injection. Some people would refer  
25 to it as "pressure maintenance." And then lastly,  
0054

1 JOHN MALCOLM, October 20, 2006  
2 the need for us to look to the longer term and to  
3 tackle some of the difficult fields that needed  
4 tertiary recovery, sometimes known as Enhanced Oil  
5 Recovery, EOR.

6 So I think that it became fairly clear  
7 that there was a need for us to look at short-term  
8 issues, the medium-term issues mainly with  
9 secondary recovery, and then the longer term  
10 issues, which was to get Enhanced Oil Recovery,  
11 especially for three major fields that we had at  
12 that time to flow and to move onwards. And I  
13 think that underlying all of that was a need to  
14 have a sound understanding of our fields, the need  
15 to dedicate more resource to field development  
16 planning, petroleum engineering studies, and we,  
17 we made a decision around about the end of the  
18 first quarter to actually set up an in-country  
19 study center to that end.

20 So we -- I think that we had a fairly --  
21 and that is in the most broad sense -- we had a  
22 fairly clear sense of direction where we were  
23 going, a need to try to get the efficiencies up in  
24 our existing operation, to try to get these  
25 secondary recovery projects in as quickly as  
0055

1 JOHN MALCOLM, October 20, 2006  
2 possible, and to really start to get the longer  
3 term Enhanced Oil Recovery products in place.  
4 These things, rather than being done sequentially,  
5 really had to be done in parallel, which had  
6 significant resource.

7 Q Subsequent to the end of the Second  
8 Quarter 2003, did PDO endeavor to undertake  
9 activities with regard to the various items you  
10 discussed in order to improve production rates?

11 A I think that the other key aspect  
12 happened at the end of -- we actually, say, for  
13 example, at the end of the First Quarter to  
14 beginning of the Second Quarter 2002, we went back  
15 to the shareholders and requested significant  
16 additional operating funds to be used on -- to  
17 make the existing fields more efficient and  
18 effective. We set up the Study Center. We  
19 started to put in place plans for an EOR  
20 directorate. And the other aspect that gave us  
21 tremendous insight was the first stage of our  
22 business planning process, which was carried out  
23 around about April/May 2003, which again, sir, I  
24 know I keep talking about different Business  
25 Plans, was effectively the Business Plan which we  
0056

1 JOHN MALCOLM, October 20, 2006  
2 refer to as BP04 which was endorsed in something  
3 like November of that year.

4 Q Do you recall if Shell, as opposed to  
5 PDO, dedicated additional assets in an effort to  
6 improve production rates at PDO in or around 2002,  
7 2003?

8 MR. SMITH: Objection to form.

9 THE WITNESS: I think first of all, the,  
10 the program as we have it or had it at that point  
11 in time was a Business Plan that had been approved  
12 by the Board of Directors and was being resourced  
13 by a number of different means. Where we  
14 requested support from our private shareholder or  
15 a public shareholder at that time, we got it. For  
16 example, my request for funds around about  
17 April 2003, which was a significant request, we --  
18 substantially that request was met by a public  
19 shareholder. And likewise with a private  
20 shareholder, where we needed support on, say,  
21 doing studies or the like, that support was  
22 forthcoming, but I have to stress for you that  
23 these were studies done on behalf of PDO and were

24 paid for in most part by PDO.

25

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1 JOHN MALCOLM, October 20, 2006

2 BY MR. MACFALL:

3 Q Specifically with regard to the studies,  
4 do you recall any of the studies that were  
5 conducted for PDO during that time period?

6 A Yes.

7 MR. SMITH: I just want to make sure  
8 we're clear about what "that time period" means.

9 BY MR. MACFALL:

10 Q Sure. That's 2002 -- well, let's make  
11 it 2002 to 2004.

12 A That's a long period. I think that  
13 studies can have a wide variety of definitions.  
14 You can have relatively short, very front-end  
15 studies to see if a project is viable, or you can  
16 actually have longer studies leading to a Field  
17 Development Plan, which can either be on an  
18 existing field that has been running say for  
19 decades, but you want to update the Field  
20 Development Plan, or it can be on say a new field  
21 for which a Field Development Plan is required so  
22 that you can base your predicted production and  
23 your predicted economics and the like.

24 So we had a range of studies that were  
25 being done, some of them, for example, on the

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1 JOHN MALCOLM, October 20, 2006

2 secondary recovery on the waterfloods, these were  
3 mainly screening studies, front-end type studies,  
4 and we were running nine or ten of those studies  
5 in parallel, and I think we reported out in April  
6 of 2003, and from that then we prioritized which  
7 ones we were going to take forward. And we had a  
8 number of other Field Development Plans that were  
9 ongoing at that time, because many of our Field  
10 Development Plans really were in need of renewal.

11 Q Do you recall if during that period  
12 technical resources from outside of Oman were  
13 provided by Shell in an effort to increase  
14 production?



15 A I would not use those words, sir, but  
16 maybe if I could rephrase your words to answer  
17 your question.

18 Q Sure.

19 A It is that again the plan was one of  
20 PDO's so we would have a plan that was supported  
21 by our Directors. We would go to many sources.  
22 For example, for Field Development Plans, Shell,  
23 of course, had -- were, of course, our technical  
24 advisor and we have great respect for their  
25 capability, but we went to other people in 2003

0059

1 JOHN MALCOLM, October 20, 2006  
2 and 2004. PGS -- I don't know what "PGS" stands  
3 for; I only know them as PGS. There's another  
4 company called TRCS that we used, but -- so when  
5 we did these things, it was very much a  
6 relationship between ourselves and Shell, where  
7 they -- we would define "this is what we would  
8 like." They would either -- if it was done  
9 outside the PDO, then they would do it almost like  
10 a contractual relationship, because they were  
11 getting paid for this in the vast majority of the  
12 cases, so that yes, if we had a study to be done  
13 that we couldn't do in-country and needed to be  
14 done, we would go to some external party, and that  
15 external party was often Shell.

16 Q Do you recall if during the period of  
17 2002 until or through -- withdrawn. Do you recall  
18 during the period of 2002 until 2004 SEPTAR, if  
19 you're familiar with that acronym, performed any  
20 work at PDO?

21 A The names of what I would refer to as  
22 EPT, the EP Technology Center, have many names.  
23 SEPTAR is one of the names I recognize, but some  
24 of those names change so fast for me that I'm not  
25 always -- but I think SEPTAR stood for Shell EP

0060

1 JOHN MALCOLM, October 20, 2006  
2 Technology and Research, but I cannot even  
3 remember what it stood for, but it's something of  
4 that nature. But EPT is an organization  
5 effectively centered in Rijswijk, but it has



6 offices also in Houston as well, but our dealings  
7 were going back through Shell, through our  
8 Business Advisor in particular, and saying we  
9 would like this study done, and that study then to  
10 be organized by EPT first then to sit down and go  
11 through all the milestones of that study in a  
12 normal -- maybe not a strictly contractual  
13 relationship, but is a, you know, this is what we  
14 need done, will you do it and check the  
15 deliverables were in line with what we had  
16 requested. The major difference with Shell versus  
17 our other suppliers is, under our terms of our  
18 agreement with Shell, these studies were done at  
19 cost rather than on a profit basis.

20 Q With regard to the technical work that  
21 was performed by EPT, are you aware if any of that  
22 work was done in Houston?

23 A I, I would not be surprised that some of  
24 that work would be done in Houston. I can think  
25 of one study, but I can't remember what date it  
0061

1 JOHN MALCOLM, October 20, 2006  
2 was, whether it was 2004 or whatever, but I can  
3 think of one study that was done at Houston.

4 Q Do you recall the nature of the study?

5 A It was just a Field Development Plan.

6 Q Do you recall if there were any EPT  
7 personnel out of Houston who were in Oman in  
8 connection with PDO's efforts to increase  
9 productivity?

10 MR. SMITH: Objection to form.

11 THE WITNESS: I cannot answer that  
12 question in the form that you put it, sir.

13 BY MR. MACFALL:

14 Q I'll see if I can rephrase if for you,  
15 sir, unless -- do you recall any Shell personnel  
16 based out of Houston doing technical work on  
17 behalf of PDO during the time period 2002 until  
18 2004?

19 A I think that they -- for clarification,  
20 sir, there are two broad categories of personnel.  
21 One personnel is those who are seconded to PDO, a  
22 bit like myself. They join PDO, they work for

23 PDO, they are paid for by PDO, their salary is  
24 paid by the Finance Department of PDO. And so we  
25 have secondees from all over the world, uh, from  
0062

1 JOHN MALCOLM, October 20, 2006  
2 the Far East, from Malaysia, Brunei, Australia, to  
3 the Americas, Venezuela, the U.S., everywhere. I  
4 think we have today well over 50 different  
5 nationalities in PDO.

6 So the possibility that one of them was  
7 U.S., definitely we have some very good U.S.  
8 engineers, and whether they were in Houston before  
9 that or not is another issue, or whether they were  
10 in New Orleans, I wouldn't know, but this is our  
11 secondment of staff into PDO, and they come to PDO  
12 nominally for something like four years, and then  
13 they will return, but when they are in PDO, they  
14 are PDO staff.

15 Q Excluding the individuals who are  
16 seconded to PDO, do you recall anybody from Shell  
17 who was based in Houston who did work on behalf of  
18 PDO during that period?

19 A I, I am sure that there were one or two,  
20 but again most of that coordination was at a level  
21 below me, and for me to try to hesitate to answer  
22 on this, I would mislead you, but I'm sure that,  
23 given the global nature of the business, that  
24 there were people coming from the Far East, there  
25 were people maybe coming from Nigeria, there were  
0063

1 JOHN MALCOLM, October 20, 2006  
2 people coming from Houston. I have no, I have no  
3 doubt that there were, there were some people, but  
4 that is just the globalized nature of the  
5 business.

6 Q Can you identify any individuals who  
7 might be familiar with the personnel performing  
8 the actual technical work of PDO during the time  
9 period 2002/2004?

10 A I suspect that most of that you could  
11 find back near EPT. John Darley, who was the head  
12 of EPT during that time. We probably have got a  
13 few names here and there, but if you want

14 something that is very concrete, then I would  
15 suggest that probably EPT would be your best port  
16 of call, because they would actually know what was  
17 done at one place and what was done somewhere  
18 else, rather than us doing we think he came from  
19 here and we think he came from there, but I would  
20 have thought the control mechanism would be from  
21 EPT, but that is my understanding, and I may be  
22 wrong.

23 Q Okay, thank you.

24 Do you recall if during your tenure at  
25 PDO, particularly in 2002, you were aware of any  
0064

1 JOHN MALCOLM, October 20, 2006  
2 tension between the Omani Government and Shell as  
3 a consequence of the fall-off in production?

4 MR. SMITH: Objection to form.

5 THE WITNESS: Maybe I could answer or  
6 rephrase your question.

7 BY MR. MACFALL:

8 Q Let me try and do it for you.

9 A Yeah, it's better if you do it.

10 Q Did you have an understanding of the  
11 relationship between the Government of Oman and  
12 Shell prior to and then subsequent to the decline  
13 in production which PDO experienced in the late  
14 nineties and early 2000s?

15 MR. SMITH: Objection to form.

16 THE WITNESS: I can only talk about my  
17 understanding when I was there.

18 BY MR. MACFALL:

19 Q That's fair.

20 A You know, so when you talk about '99 and  
21 2000, then it would just be conjecture on my part,  
22 but if you are asking me how did I find  
23 relationships when I went into Oman and took over  
24 the job on the 1st of November 2002, those  
25 relationships were extremely tense. They were  
0065

1 JOHN MALCOLM, October 20, 2006  
2 extremely tense, and understandably so. All sides  
3 were concerned, both the Government and the  
4 private shareholders.

5 Q Do you recall, when you arrived at PDO,  
6 if anyone from the Oman Government expressed to  
7 you that they believed Shell was responsible for  
8 the decline in production at PDO?

9 MR. SMITH: Objection to form.

10 THE WITNESS: I think the -- I'm trying  
11 to get the essence behind your question, sir. I  
12 think that, of course, in any close relationship  
13 which has endured for decades, when things start  
14 to unravel, even in the closest of relationships,  
15 one side can blame the other. This is the nature  
16 of human relationships under stress. I think  
17 that -- so that underlying tension was there,  
18 there is no doubt, and it's easy to move into a  
19 blame culture in that situation.

20 I think that it has to be said that  
21 Shell's response in that situation -- and I will  
22 also say the Government's response in that  
23 situation -- was really one of trying to  
24 understand the underlying problems, and with very  
25 visible commitment on both sides to fixing them.

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1 JOHN MALCOLM, October 20, 2006

2 As I've said, in early 2003 the Government  
3 significantly increased the amount of operating  
4 expenditure.

5 Shell redirected people to be seconded  
6 into PDO to build up our Study Center so that we  
7 could do Field Development Plans, so the tensions,  
8 of course, were there, as there would be in any  
9 good relationship that is under real, real  
10 pressure. The individuals, of course, one in any  
11 organization, individuals will blame the other  
12 side, but -- and yes, there was tension, but there  
13 was also, I think, more importantly, especially  
14 from the top of Shell downwards, of what is it we  
15 can do to fix the situation.

16 I use the word "fix." That is, rectify  
17 the situation. What can we do to get this  
18 production understood, this fall-off; what is it  
19 we can do to rebuild our reputation. But this is  
20 all about -- this is all about production. This  
21 is very, very much attributable to production,

22 some cost issues as well, but this is, as you  
23 stated earlier, sir, the fall-off in production in  
24 2002 from Plan numbers to actual and the fall-off  
25 in production to be anticipated in 2003, so -- but  
0067

1 JOHN MALCOLM, October 20, 2006  
2 it was one of what can we do to support PDO to  
3 bring us back to where we were again, on both  
4 sides.

5 (Exhibit No. 1 was marked for  
6 identification and attached to the deposition  
7 transcript.)

8 BY MR. MACFALL:

9 Q You've just been handed a document  
10 marked for identification as Malcolm Exhibit 1. I  
11 would note for the record that it is  
12 correspondence that is not addressed to you, and  
13 it precedes your tenure at PDO. However, I'd like  
14 you to look at the document, sir, and once you've  
15 had an opportunity to review it, just let me know.

16 A I won't mark it, but if you'd mind just  
17 a moment.

18 Q Sure.

19 Have you had an opportunity to  
20 adequately review that, sir?

21 A If I need to go back again to get some  
22 more of the details, I trust you will forgive me,  
23 but I hope to answer some of your questions on my  
24 initial review.

25 Q Do you recall first if you've ever seen  
0068

1 JOHN MALCOLM, October 20, 2006  
2 this document before?

3 A I do not recall seeing it.

4 Q It is a letter from Dr. Mohammed bin  
5 Hamad Al Rumhy to Walter van der Vijver, who's  
6 listed as the Group Managing Director, CEO,  
7 Exploration and Production for Shell.

8 A Yes.

9 Q The signature or the signatory to the  
10 letter; is that the same individual that you've  
11 identified as the Deputy Managing Director of PDO  
12 currently?

13 A No. He is the Chairman of PDO at this  
14 moment in time, so Dr. Rumhy is the Minister of  
15 Oil and Gas today, as he was at this time, and he  
16 is also Chairman of our Board of Directors, and he  
17 has been Chairman from, if I remember correctly,  
18 from around about mid-2003. So he's Chairman of  
19 PDO.

20 MR. SMITH: So when you said "at this  
21 time" earlier, you meant today, not the date of  
22 the exhibit you're looking at?

23 THE WITNESS: Yes.

24 MR. SMITH: I just wanted the record to  
25 be clear on that.

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1 JOHN MALCOLM, October 20, 2006

2 THE WITNESS: So he was the Minister of  
3 Oil and Gas in 2001, and I think he was many years  
4 before that as well, and he is the Minister of Oil  
5 and Gas today. The difference between today and  
6 then is that today he is also the Chairman of PDO,  
7 PDO's Board of Directors.

8 BY MR. MACFALL:

9 Q Directing your attention specifically to  
10 the second paragraph of the letter, Dr. Rumhy  
11 discusses the decline in production at PDO of  
12 black oil. He then goes on to indicate the  
13 Ministry or the Government of Oman's belief that  
14 there were several factors that were either  
15 responsible or contributing to the production  
16 issue, and then they are listed by point beneath  
17 that paragraph.

18 Specifically directing your attention to  
19 the second of those, "Reserve Booking  
20 Methodology," at the time that you arrived at PDO  
21 in 2002, were you aware of the concern previously  
22 expressed by the Government of Oman that the  
23 booking reserve methodology was a contributing  
24 factor in connection with the decline in  
25 production?

0070

1 JOHN MALCOLM, October 20, 2006

2 MR. SMITH: Objection to form.

3 BY MR. MACFALL:



4 Q Can you answer the question, or would  
5 you like me to rephrase, sir?

6 A I, I understand the meaning. I think I  
7 understand the meaning of this letter. If that is  
8 what you wish me to comment on?

9 Q Well, why don't we do it this way. Why  
10 don't you first describe for me what you believe  
11 is meant here.

12 MS. LATIMER: Objection to form.

13 BY MR. MACFALL:

14 Q Why don't you describe to me, sir, your  
15 understanding of what's discussed here.

16 A My understanding of what this is about  
17 is, first of all, one has to understand the  
18 Concession Agreement between PDO -- between the  
19 private shareholders and the Government of Oman  
20 that was in place prior to the new Concession  
21 Agreement that was signed, was effective the 1st  
22 of January 2005, and as part of the reward  
23 mechanism, there was a reward mechanism in terms  
24 of production-related or in actual fact well  
25 generation. There was a percentage that was  
0071

1 JOHN MALCOLM, October 20, 2006  
2 there.

3 And there was also a reward mechanism  
4 for additional expectation reserves, which were  
5 sometimes referred to as "old oil." An  
6 additional -- although people used the word  
7 "reserves," it was effectively "Discovered Scope  
8 For Discovery," generally understood in the  
9 industry as DSFR, Discovered Scope For Recovery,  
10 which really related more to exploration. So it  
11 was something that made a focus on exploration,  
12 and there was a reward tied to successful  
13 exploration and there was a reward tied to  
14 successful development of fields. The development  
15 one was the old oil; the first one was the new  
16 oil.

17 And if we take your point here, the  
18 Reserves Booking Methodology, I think -- and I  
19 cannot comment at this point. I can, though,  
20 comment from when I was in the company, that His

21 Excellency Dr. Rumhy had a viewpoint for which I  
22 have a tremendous amount of sympathy, that Field  
23 Development Plans, total Field Development Plans  
24 are the basis, ultimately the basis for booking  
25 reserves. They are expectation reserves. They  
0072

1 JOHN MALCOLM, October 20, 2006  
2 are not the only basis. You can have sector plans  
3 as well, but he was, he was concerned about a lack  
4 of Field Development Plans. In 2002, I don't know  
5 if that was his concern at that point.

6 Q Leaving aside the letter for a moment,  
7 did Dr. Rumhy ever express to you a concern that  
8 expectation reserves were booked by Shell in order  
9 to receive incentive payments from the Omani  
10 Government?

11 A I think in my conversations, that was  
12 always an underlying concern, and it's an  
13 understandable underlying concern. And I note  
14 that within this letter here, the mention of a  
15 prepayment of \$30 million, I knew about this  
16 prepayment, I hadn't seen all the details here,  
17 and which was effectively equivalent to stating  
18 that there was concern over something like  
19 200 million barrels of expectation reserves.

20 Q Just with regard to the second page,  
21 with regard to the prepayment of \$30 million, the  
22 letter references or specifically states that that  
23 was "against future de-booking of reserve." Do  
24 you have knowledge of that de-booking, sir?

25 A That again, I had knowledge of it or  
0073

1 JOHN MALCOLM, October 20, 2006  
2 started to get an understanding of it when I came  
3 in, and there was concern that -- I think -- and  
4 you have to bear with me. I think it was  
5 associated with the Yibal Field. There was  
6 concern that -- and whether it was just that field  
7 or a number of other fields, there was concern  
8 that maybe the \$30 million here would have been  
9 because the old oil -- if we say it's old oil --  
10 was credited at 15 cents per barrel, so that's  
11 why, sir, it's equivalent to something like

12 200 million barrels -- again I have to stress --  
13 of expectation reserves.

14 Q Do you have knowledge of the actual  
15 de-booking of those reserves, as referenced in the  
16 letter?

17 MR. SMITH: Objection; form and  
18 foundation.

19 BY MR. MACFALL:

20 Q Let me withdraw it. Do you know if  
21 reserves at the Yibal Field were actually  
22 de-booked, separate and apart from anything to do  
23 with Project Rockford?

24 MR. SMITH: After this letter?

25  
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1 JOHN MALCOLM, October 20, 2006

2 BY MR. MACFALL:

3 Q During it, yes.

4 A It's -- I, I want to try to answer your  
5 question, but your question is actually an  
6 all-encompassing question. It is, it is -- and I  
7 want to try to answer without talking for too  
8 long, but effectively in May, around about  
9 May 2003, so this was all in going -- I wasn't  
10 totally sure of all the details on it. In  
11 May 2003 we put together a program for BP04, which  
12 was going to be endorsed in November, and we did  
13 it in a very bottoms-up style.

14 When we did that in that bottom-up style  
15 where we tried to say we have so many reserves,  
16 where is a project that is matched to these  
17 reserves, finally, and then you keep doing this,  
18 and then you're left or we were left with a number  
19 of reserves on our books that we could not match  
20 to projects within a 30-year window. And again  
21 I'd like to stress that we in PDO run not on the  
22 basis of license expiration or anything; we run in  
23 terms of one year, five years, 30 years.

24 And when we did that bottom-up plan, we  
25 realized or we believed that we were several

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1 JOHN MALCOLM, October 20, 2006

2 hundred million barrels of reserves that we could

3 not match to projects, and we called these our  
4 "Matched Reserves." I think in hindsight the  
5 terminology would have been better as the  
6 "Unmatched Reserves," but you don't change the  
7 terminology halfway through. And those reserves  
8 were then reviewed by a Shell -- our work was then  
9 reviewed by Shell STOIP and Reserves Team, which  
10 then reported -- Stock Tank Oil Initially In  
11 Place, so it's S-T-O-I-I-P. The STOIP and  
12 Reserves -- and when I say "reserves" again, I'm  
13 talking about expectation reserves.

14 They were reviewed, and there was a  
15 report, an initial report-out made out in  
16 September 2003, and a final report-out in I think  
17 it was December 2003, and these -- this kind of  
18 prepayment was effectively resolved within that  
19 total issue, so this prepayment, in my  
20 understanding, was not resolved as a kind of in it  
21 alone; it was part of a bigger issue that resulted  
22 in eventually us removing something like -- I  
23 can't remember the exact number, sir, but  
24 something like about 900 million barrels of  
25 expectation reserves from our -- or putting a  
0076

1 JOHN MALCOLM, October 20, 2006  
2 qualification -- let me be correct -- a  
3 qualification of 900 million barrels of  
4 expectation reserves in our books.

5 Q You've gone to great lengths to  
6 distinguish between "expectation" and "proved  
7 reserves" because of the operating structure of  
8 PDO. Do you have an understanding as to whether  
9 there is a relationship between expectation  
10 reserves as reported within PDO and proved  
11 reserves reported by Shell?

12 MR. SMITH: Objection to form and  
13 foundation.

14 THE WITNESS: First of all, I am not  
15 responsible for reporting proved reserves for  
16 Shell. Maybe I can answer your question in a more  
17 general manner.

18 Firstly, from where I come from -- and  
19 again I am a surface engineer, not a subsurface

20 engineer -- expectation reserves are a 50/50  
21 probability. They are based middle course on  
22 which we therefore base our future production  
23 forecast. Proved reserves outside a rule-based  
24 deterministic system are generally seen as P85,  
25 reasonable certainty, and all the different  
0077

1 JOHN MALCOLM, October 20, 2006  
2 meanings that those two words bring with it, but  
3 they are reasonable certainty.

4 For PDO, even our P85 type reserves,  
5 which were not that good quality at the time, were  
6 not actually to be comparable with what Shell  
7 would have reported, because as I said before, we  
8 go over a 30-year period, whereas at that moment  
9 in time Shell would have had to report, I  
10 believe -- and it's only my understanding --  
11 within the 2012 license expiring.

12 So the correlation between these  
13 expectation reserves that go on for 30 years and  
14 reported reserves on a proved basis that go on  
15 until 2012, it all becomes a bit flimsy. There is  
16 a correlation, but it is something that you cannot  
17 say this number is ten, this number is one. You  
18 would need to work your way through it, and again  
19 I -- you know, I am trying to be as helpful as  
20 possible, sir, but I don't think that there is a  
21 direct correlation between those two numbers, in  
22 my understanding, for the reasons I've given.

23 BY MR. MACFALL:

24 Q The volume of expectation reserves  
25 reported by PDO; do you have any understanding of  
0078

1 JOHN MALCOLM, October 20, 2006  
2 whether that included the proved reserves reported  
3 by Shell?

4 MR. SMITH: Objection to form.

5 THE WITNESS: Again I, I was not  
6 involved in Shell's reporting mechanism. We, as  
7 PDO, provided a service of calculation based on  
8 guidelines to Shell. If you ask me, though, the  
9 question the other way around, about do we believe  
10 our proved reserves of P85 within PDO are

11 encompassed within our P50 in PDO, yes, the answer  
12 is yes, because the P85 is reasonable certainty,  
13 the P50 is expectation, so one is a subset of the  
14 other, but I cannot answer your first question,  
15 sir. I'm sorry to have deviated to answer it from  
16 a PDO context.

17 BY MR. MACFALL:

18 Q Never mind. Appreciate it.

19 Mr. Malcolm, are you aware if Shell as opposed to  
20 PDO reported proved reserves in connection with  
21 PDO during the period of 1999 until 2004?

22 MR. SMITH: Objection to form.

23 THE WITNESS: Again I, I was not there  
24 in 1999, and I can only speak for PDO in those  
25 years. And I do know both from in hindsight that  
0079

1 JOHN MALCOLM, October 20, 2006  
2 we did provide a service to Shell, and with PDO  
3 being such a significant producer from a  
4 production point of view, I would have been sure  
5 that Shell would have needed to report proved  
6 reserves. It's not a -- it's not a small part.  
7 It is, you know, 200,000 plus production Shell  
8 share.

9 BY MR. MACFALL:

10 Q And just so I'm clear, you may have told  
11 me this before, but I just want to make sure my  
12 understanding is correct. PDO did not calculate  
13 proved reserves for Shell during that period of  
14 time; am I correct?

15 MR. SMITH: Objection to form.

16 THE WITNESS: Sir, I don't think that's  
17 what I said. Maybe I can restate what I said.  
18 Was that PDO provided a service to Shell and any  
19 other shareholder who required it, for us to aid  
20 them in their reporting by taking our data and  
21 giving it back in the guidelines that they  
22 submitted to us. So if Shell or Total or anyone  
23 else had said to us, "Here is a guideline, can you  
24 please apply this guideline and give us a number  
25 out," we would have done so and showed them the  
0080

1 JOHN MALCOLM, October 20, 2006



2 basis of that, but we would have tried to  
3 reasonably stay within that guideline.

4 BY MR. MACFALL:

5 Q Thank you. Then I clearly  
6 misunderstood.

7 Do you recall as part of the services  
8 that PDO provided to Shell, it, in fact, provided  
9 Shell with proved reserves numbers in accordance  
10 with Shell's guidelines?

11 A I remember that. I have to say I do not  
12 remember it for the end of 2002, but I do remember  
13 it for the end of 2003.

14 Q Are you familiar with the process by  
15 which PDO calculated proved reserves numbers for  
16 Shell?

17 A I am, I am now, and I had an  
18 understanding of it around about the Third Quarter  
19 of 2003.

20 Q Could you explain for me, please, your  
21 understanding of that process.

22 A And again I am not, not an expert on it,  
23 but it effectively was based on production  
24 forecasts going forward to license extension with  
25 some form of overlay on, as the years got closer  
0081

1 JOHN MALCOLM, October 20, 2006  
2 to license extension, of reducing the numbers, but  
3 it was effectively based on a forward-looking  
4 production.

5 Q Do you know who was -- withdrawn. Was  
6 there an individual or individuals at PDO who were  
7 responsible for actually conducting the  
8 calculations to derive the proved reserves  
9 reported to Shell?

10 MR. SMITH: Objection; lack of  
11 foundation.

12 THE WITNESS: Again I think there were,  
13 was a department involved in providing this  
14 service to Shell, according to their guidelines.  
15 That department was their Corporate Planning  
16 Department.

17 BY MR. MACFALL:

18 Q Do you recall the name of any of the --

19 withdrawn. Who was the head of Corporate Planning  
20 at PDO at the time? And "at the time" I mean  
21 between 2002 and 2004.

22 A Between 2002 and -- for 2002 and 2003,  
23 there was a change made in 2004, and I need to go  
24 back to check the records, but from when I came in  
25 in 2002 throughout the whole of 2003, Stuart  
0082

1 JOHN MALCOLM, October 20, 2006  
2 Clayton, sometimes known as John Stuart Clayton,  
3 because his first name is John, but no one uses  
4 that name, was the head of Corporate Planning, and  
5 he reported to our Technical Director and our  
6 Deputy Managing Director.

7 Q Are you aware if Mr. Clayton was  
8 involved in the submission of information to Shell  
9 with regard to the proved reserves at PDO?

10 MR. SMITH: Same time frame; '02 to '04?

11 MR. MACFALL: Yes. Thank you.

12 THE WITNESS: I was aware in 2003. As  
13 I've said before, in end of 2002 when I just  
14 walked into the company, there were so many other  
15 issues going around about my head at that time  
16 that I do not recollect that, but in 2003, yes.

17 BY MR. MACFALL:

18 Q Thank you. If you could direct your  
19 attention back to Exhibit 1 for a moment,  
20 specifically on Page 1, the reference to  
21 methodology, in Number 3 it says "Scorecard." Do  
22 you recall, not during this time frame, but during  
23 your tenure at PDO, if Shell's scorecards were  
24 ever asserted as an issue in connection with oil  
25 production by the Omani Government?

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1 JOHN MALCOLM, October 20, 2006

2 MR. SMITH: Objection to form and  
3 foundation.

4 THE WITNESS: I, I think, sir, I have to  
5 correct your question if you wouldn't mind.

6 BY MR. MACFALL:

7 Q Sure.

8 A Is that we didn't have a Shell  
9 scorecard; we had a PDO scorecard.

10 Q Thank you.

11 A And our PDO scorecard, definitely around  
12 about the time that I came in, had expectation and  
13 even looser Discovered Scope For Recovery targets  
14 on that scorecard.

15 Q Did anyone from the Oman Government ever  
16 express to you during your tenure at PDO that the  
17 reserves component of the PDO scorecard was  
18 somehow related to the decline in production?

19 A I think that -- I find that a difficult  
20 question to answer, sir, in that the scorecard is  
21 there to -- relates to the Business Plan and  
22 therefore relates to the targets within the  
23 Business Plan. It's a focusing tool for the staff  
24 at PDO. So in itself it relates to the Business  
25 Plan, but I think your question was not actually

0084

1 JOHN MALCOLM, October 20, 2006  
2 related to the scorecard. You were asking me  
3 whether --

4 Q Whether you had ever received complaints  
5 from anyone within the Omani Government or  
6 expressions of concern -- let me withdraw the  
7 question or rephrase it. Did you ever receive any  
8 expressions of concern by members of the Omani  
9 Government that the reserves metric on PDO's  
10 scorecard was somehow related to the decline in  
11 oil production at PDO?

12 MR. SMITH: Objection to form.

13 THE WITNESS: I can state that when I  
14 came into PDO at the end of 2002, there was  
15 concern about the expectation reserves that were  
16 held on the books, and that was expressed to me by  
17 the then Chairman of the Board, which is different  
18 from the scorecard. They have concerns about the  
19 scorecard as to whether or not it produces the  
20 right behaviors, but I think your question was  
21 more about the, about the expectation reserves.  
22 Did they have concerns about the expectation  
23 reserves? Yes. Did they have concerns about the  
24 behaviors that scorecards can produce? Yes.  
25 Sorry to have to restate at least --

0085

1 JOHN MALCOLM, October 20, 2006

2 MR. MACFALL: No, I appreciate the  
3 clarification. Why don't we go off the record for  
4 a second.

5 THE VIDEOGRAPHER: This marks the end of  
6 Tape 1 in the deposition of Mr. Malcolm. We are  
7 going off the record. The time is 12:00 p.m.

8 (Whereupon, a short recess was taken.)

9 THE VIDEOGRAPHER: This marks the  
10 beginning of Tape 2 in the deposition. We are  
11 back on the record. The time is 12:06 p.m.

12 BY MR. MACFALL:

13 Q Mr. Malcolm, with regard to the PDO  
14 scorecard, could you describe for me what, if any,  
15 issues were discussed with you by members of the  
16 Omani Government concerning the PDO scorecard.

17 MR. SMITH: Objection to form and  
18 foundation.

19 BY MR. MACFALL:

20 Q You can answer, sir, if you can.

21 A I think the, um, there were -- with  
22 scorecards there are a number of generic concerns  
23 that you will get with any Government. One of  
24 them is whether or not the scorecard is too easy,  
25 because those scorecards are related to the

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1 JOHN MALCOLM, October 20, 2006

2 payment of staff. It's a relatively small  
3 percentage, but it's still significant, whether  
4 the scorecards are too easy. Whether the  
5 scorecard reflects the Business Plan, because it  
6 should reflect the Business Plan.

7 And so the concept of scorecards does  
8 not lie easily with a Civil Service-based  
9 organization, but I think they understood the need  
10 for focus, and so many of the discussions were  
11 around what, I think what the major of the  
12 Government shareholder saw as important versus  
13 what we at PDO would see as important versus what  
14 the private shareholder would see as important.  
15 So say, for example, the weighting on production  
16 or the weighting on safety and the like, so it is  
17 more about not that anybody -- there was, of

18 course, unanimity about the Business Plan and the  
19 scorecard reflects that Business Plan, but really  
20 the weightings on the various aspects of the  
21 scorecard and whether or not the scorecard would  
22 produce the right behaviors, because, as you know,  
23 sir, it's easy to chase short-term targets. You  
24 had to have this balance in the scorecard.

25 Q Thank you.

0087

1 JOHN MALCOLM, October 20, 2006

2 Did there come a time during your tenure  
3 at PDO when there was concern with regard to the  
4 accuracy of PDO's reported expectation reserves?

5 A That concern, sir, as I said before, was  
6 around about May 2003 when we did the Business  
7 Plan exercise, the start of the Business Plan  
8 exercise for BP03. BP04. I apologize. And when  
9 we built the Business Plan that year, we built it  
10 bottom-up and tried to match reserves to projects  
11 and discovered that we had this matched reserves  
12 issue. At the time, I think in May 2003, we  
13 thought the number was about 700 million plus. It  
14 later transpired to be 900 million plus, but that  
15 was later in the year. Again, the numbers that I  
16 mentioned, as you quite readily said, sir, are  
17 expectation reserves numbers.

18 Q The bottom-up exercise that you  
19 reference; is that something different than the  
20 STOIIP and Reserve Review?

21 A Yes, sir. The situation is that we were  
22 putting together the Business Plan, and we were  
23 taking the individual projects in the Business  
24 Plan and associating them with reserves that would  
25 be developed over say a 30-year time scale. When

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1 JOHN MALCOLM, October 20, 2006

2 we presented our first pass to our shareholders on  
3 both sides, there was concern, because we, as the  
4 operator, were saying we believed that there were  
5 700 million barrels of expectation reserves that  
6 we could not match to projects in the Business  
7 Plan. It was a significant step.

8 There was concern in both sides, in the

9 private shareholders and the Government  
10 shareholders. There was challenge, and our  
11 response to that challenge was one of we do not  
12 think our work is perfect, because it had been  
13 done in a relatively short period of time and  
14 quite quickly, but the right way to resolve this  
15 was to have a review of the STOIIP, Stock Tank Oil  
16 Initially In Place, and the expectation reserves,  
17 and there was such a review.

18 I think the review was effectively  
19 initiated in around about June 2003, and it was a  
20 review that was actually a Shell review and was  
21 paid for by Shell, but, as was shown subsequently  
22 and was the intention at the time, to be openly  
23 shared with the other partners, in particular the  
24 Government.

25 Q Going back to the bottoms-up exercise  
0089

1 JOHN MALCOLM, October 20, 2006  
2 that was undertaken in connection with the  
3 Business Plan, do you recall who it was that  
4 actually performed the technical work of matching  
5 the reserves with the individual fields?

6 MR. SMITH: Objection to form.

7 THE WITNESS: It is difficult to say one  
8 person. Maybe if I can rephrase your question if  
9 it's acceptable to you, sir, is that the  
10 coordination of the activity was done by Corporate  
11 Planning Department. The actual detailed  
12 activities were done by many other people in the  
13 organization who were responsible for particular  
14 fields and the projects associated with those  
15 fields. So the coordination element was  
16 coordinated by the Corporate Planning Department,  
17 which reports to our Deputy Managing Director and  
18 Technical Director.

19 BY MR. MACFALL:

20 Q Do you recall if Mr. Clayton was  
21 involved in that process?

22 A Yes, he was.

23 Q Do you recall why a bottoms-up review  
24 was conducted in connection with the Business Plan  
25 in or about May of 2003?



0090

1 JOHN MALCOLM, October 20, 2006

2 A It's -- of course, one's memory, after  
3 three and a bit years, is a bit hazy, but I think  
4 that the underlying thing was that we wanted to  
5 get a far better grip on the details of our  
6 business and particularly our projects going  
7 forward, and it was -- we sought in that high  
8 level detail -- we were actually using a new tool  
9 that was available at the time for building our  
10 Business Plan, which was very, very helpful to us.  
11 It actually allowed us to do something that would  
12 stretch it, be a little bit difficult, but it was  
13 a good tool, and it was to try to give us that  
14 clear insight into not just that we've got five  
15 billion or whatever the number was of expectation  
16 reserves, but how, how are we going to develop  
17 those into production over the foreseeable future.  
18 And it was to get that very much tighter grasp on  
19 the production versus expectation reserves and our  
20 plans and our projects and everything that goes  
21 with them, and our facilities, and so it was just  
22 a significantly more detailed exercise, and in my  
23 opinion it was a good piece of work.

24 Q Were the findings with regard to the  
25 mismatched or matched reserves discovered as a

0091

1 JOHN MALCOLM, October 20, 2006

2 result of the bottoms-up exercise memorialized in  
3 a written report?

4 A I cannot remember that, sir, but the  
5 number was well-known and was discussed with the  
6 shareholders or the Directors.

7 Q With regard to Shell as one of the  
8 shareholders of PDO, was the -- were the results  
9 of the bottoms-up exercise communicated to it --  
10 let me rephrase the question. I'm sorry. Do you  
11 recall if the conclusions reached regarding  
12 reserves in the bottoms-up exercise were  
13 communicated to Shell?

14 A They were communicated to all our  
15 shareholders, including Shell.

16 Q Do you recall how it was communicated to

17 Shell?

18 A I think first -- again my memory is hazy  
19 after this time, but, of course, the first kind of  
20 frequent contact was with the Business Advisor,  
21 Paul Mann, and therefore Paul up through the rest  
22 of the Shell organization. And we communicated it  
23 to both the Government and Shell, and I think, of  
24 course, it was such a large number, there was  
25 shock on all sides. And there was also concern of  
0092

1 JOHN MALCOLM, October 20, 2006  
2 "are you sure you've got this right," you know, on  
3 all shareholders. It was a very big number. It  
4 was 700 million out of five billion. It was a  
5 significant percentage.

6 And I think that to go back to your  
7 specific point about Shell, I think that the great  
8 thing that we got from Shell was, of course,  
9 challenge of do you think you have this right, and  
10 we said, yeah, we believe as a first pass, it's a  
11 good first pass number, but we strongly recommend  
12 there is a review done such that all shareholders  
13 can get assurance that the operator's figures are  
14 sound.

15 And, you know, from the time I had come  
16 in up until about that point, people were always  
17 saying, well, should we have a reserves review,  
18 who is going to pay for it. All of these things  
19 went back and forward that you always get from  
20 shareholders on issues of cost, but Shell was  
21 extremely good at this point. They said this is a  
22 cause for concern. We must put this concern to  
23 rest one way or another. And they, at their own  
24 cost, instigated staff around the STOIIP and  
25 Reserves Review, and Corporate and PDO, we were  
0093

1 JOHN MALCOLM, October 20, 2006  
2 providing all our numbers and all our data.

3 Q Now, you referenced communication with  
4 Paul Mann. Do you recall if you communicated  
5 personally with Paul Mann concerning the findings  
6 reached in the bottoms-up exercise?

7 A I may well have done, but -- I don't

8 remember it, but I certainly communicated with Din

9 Megat, the Regional Business Director.

10 Q Do you recall how it was that you  
11 communicated with Mr. Megat? Was it by telephone,  
12 for example, or e-mail?

13 A I can't remember, sir. I can remember,  
14 however, that they came in for a technical meeting  
15 sometime in June, and I can remember we discussed  
16 it, and it was -- I cannot remember the exact  
17 date, but sometime in June there was total  
18 agreement that we should have a review done of  
19 these numbers.

20 Q Was the technical meeting conducted with  
21 regard to the findings in the bottoms-up exercise?

22 A Again I need to go back to my diary to  
23 check all the dates, but the general format was  
24 that we would have regular Technical Shareholders  
25 Meetings. I cannot remember the exact date that

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1 JOHN MALCOLM, October 20, 2006  
2 that Technical Shareholders Meeting took place,  
3 but I believe it was around about early June 2003,  
4 which was at the point that we were saying to our  
5 shareholders, because we, we have a Technical  
6 Shareholders Meeting before kind of every board,  
7 we have three or four board meetings a year, so it  
8 was around about that time we gave them the first  
9 pass of the plan, and you're saying the plan, we  
10 think we're 700 million barrels of expectation  
11 reserves short that we can't match to projects.

12 Q Did anyone from Shell request an  
13 opportunity to review the data that had been  
14 utilized to reach that conclusion in the  
15 bottoms-up exercise?

16 A That, sir, was subsequent to when we did  
17 the STOIP and Reserves Review and Expectation  
18 Review, and that we provided all our data that we  
19 had utilized and the rationale and everything like  
20 that, so, of course, we provide that data to both  
21 sets of shareholders as requested, but in this  
22 particular case as it was a Shell STOIP and  
23 Reserves Review, they specifically, of course,  
24 wanted to know how we got to our figures, they

25 wanted to check our figures, the methodology, et

0095

1 JOHN MALCOLM, October 20, 2006

2 cetera, of the figures.

3 Q For my own edification, we've used the  
4 term several times, and I just want to make sure  
5 that I have an accurate understanding; the term  
6 "STOIP," which I believe you said is Stock Tank  
7 Oil Initially In Place --

8 A Yes, sir.

9 Q -- could you please explain for me what  
10 that is, sir.

11 A Well, sir, you've got a simple surface  
12 engineer who is going to have to explain it to  
13 you, but maybe I can give you my understanding --

14 Q Thank you.

15 A -- my explanation, is that if you take a  
16 reservoir of oil -- and some people mistakenly  
17 think of it like a tank, but it is not a tank. It  
18 is small particles of oil encased in grains of  
19 sand or in grains of carbonate, depending on the  
20 source of that reservoir, whether that reservoir  
21 of rock is a sandstone or whether it's a  
22 carbonate, but you have got -- within the pores of  
23 that reservoir you have got oil and in some cases  
24 you've got water as well, and it is under  
25 tremendous pressures. Oil and gas is under

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1 JOHN MALCOLM, October 20, 2006

2 tremendous pressure, depending on how deep it is.  
3 The deeper it is, generally the deeper the  
4 pressure, but if you conceptually lifted all of  
5 that oil out of the ground, conceptually, and you  
6 placed it into a tank on the surface, that would  
7 be, in my understanding, the Stock Tank Oil  
8 Initially In Place. Now, I think that the  
9 terminology is an old one. And again I'm not a  
10 reservoir engineer, so I couldn't tell you where  
11 it comes from, but that is my understanding, and  
12 it is the -- it is truly the maximum amount of oil  
13 that you could ever recover from a reservoir. And  
14 as such, that is -- it is an important number in  
15 that you could never theoretically -- not even

16 theoretically -- you could never physically exceed  
17 that number, because you have taken every single  
18 molecule and said if I put it on the surface, what  
19 would I get.

20 Q Thank you very much. I appreciate that,  
21 Mr. Malcolm.

22 Prior to the initiation of the STOIIP  
23 and Reserve Review, do you recall if anyone from  
24 the Government of Oman expressed the belief that  
25 Shell should not conduct the review?

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1 JOHN MALCOLM, October 20, 2006

2 A That is a good question, sir. I can  
3 only answer it within the time frame that I was in  
4 Oman, so I cannot answer it prior to that for you,  
5 but I can answer it within the time frame that I  
6 was in Oman, which is effectively on seat from the  
7 1st of November.

8 There was concern about expectation  
9 reserves bookings, and this exhibit you put in  
10 front of me is that type of concern. And as the  
11 Managing Director of the Operator -- so you sit  
12 between all the shareholders -- my viewpoint when  
13 I came into the company was: If you have this  
14 concern, let us do a review of the reserves. If  
15 you are concerned about the numbers, let's do a  
16 review.

17 I had a lot of discussions with the  
18 Government, I had discussions with Shell, and the  
19 arguments were always about who was going to pay  
20 for the review and who was going to do the review.  
21 I pursued this for several months, but eventually  
22 I put my time and effort onto something else, but  
23 effectively, after doing the bottoms-up build,  
24 first pass of the program built, at that point the  
25 number was significant, we thought greater than

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1 JOHN MALCOLM, October 20, 2006

2 700 million.

3 And when I raised this with Shell, there  
4 was no doubt. They said, oh, this is cause for  
5 concern we have to address, and they said that  
6 they would do this at their own costs. They would

7 share the results with the Government, and the  
8 Government had an alternative, that they had the  
9 right to do their own review if they were not  
10 happy with whatever the results of the Shell  
11 review were, which I thought was very good,  
12 because it moved the whole business forward.  
13 Again this was an expectation reserves review.

14 Q Was there a STOIP and Reserves Review  
15 Team that worked on the review for Shell?

16 A My understanding, there was. I cannot  
17 give you all the names in that team, but it was  
18 led by a gentleman called Stan Christianson.  
19 There were several members of that team. It went  
20 from maybe three to eight. There were a number of  
21 members, because it went over a significant period  
22 of time. It went from effectively -- I think it  
23 was initiated, as I said, sometime in June, and I  
24 think it closed out sometime in December.

25 Q Generally do you recall if any members  
0099

1 JOHN MALCOLM, October 20, 2006  
2 of SEPTAR participated in the STOIP and Reserves  
3 Review?

4 MR. SMITH: Objection to form.

5 THE WITNESS: I -- again the word  
6 "SEPTAR," I am unsure about. We saw this as staff  
7 from EPT manning the study. The staff that were  
8 actually involved, I know there was some review  
9 drafts that went up with names then again, but  
10 again you would really need to ask those the head  
11 of EPT as to who they were and where they came  
12 from, et cetera.

13 BY MR. MACFALL:

14 Q Just one more question along those lines  
15 with regard to this review: Are you familiar with  
16 an organization or entity known as the Bellaire  
17 Technology Center?

18 A Yes, I know of the Bellaire Technology  
19 Center.

20 Q Could you describe for me -- well, do  
21 you have an understanding of what it is?

22 A I think that today, organizationally, I  
23 am a little bit out of date with what is happening



24 in Shell in the Center. You have to realize I've  
25 been running Joint Ventures now since 1999, and  
0100

1 JOHN MALCOLM, October 20, 2006  
2 when you're running a joint venture, your focus is  
3 on the joint venture, and sometimes how things are  
4 organized in our Corporate Center of Shell, I  
5 don't always pick them all up, but there was a  
6 point where the Bellaire Technical Center  
7 essentially used to be -- my understanding was the  
8 Research and Development Support Center based in  
9 Houston, and they have -- and again this all  
10 happened after I left EPT in 1997, but there is  
11 this kind of relationship between themselves and  
12 Rijswijk on where work is done, et cetera.

13 Q Do you recall if Bellaire Technology  
14 Center did any work in connection with the STOIIP  
15 and Reserves Review conducted in 2003 in PDO?

16 A From my side I simply saw it as a  
17 Shell-led study from people in Rijswijk, supported  
18 by the original Business Director and the EP CEO,  
19 because they were effectively footing the bill at  
20 the end of the day, how they resourced that study  
21 was really -- I really had no concerns apart from  
22 to make sure that they resourced it with very,  
23 very good people such that the outcome of the  
24 study would be credible.

25 Q I believe you indicated that that study,  
0101

1 JOHN MALCOLM, October 20, 2006  
2 the STOIIP and Reserves Review, ran from  
3 approximately June of 2003 until December of 2003,  
4 correct?

5 A It did. It was different peaks in  
6 activity. The key reporting, the first -- there  
7 was a number of report-outs, but the significant  
8 one was in September 2003, which was a kind of  
9 peak report-out, but my understanding is I think  
10 the -- and I need to go check my facts again, but  
11 I think the study was closed off near the end of  
12 December, near the end of 2003.

13 Q Did there come a time during that  
14 period, June of 2003 to December of 2003, when the

15 STOIP and Reserves Review Team initially  
16 confirmed that there were -- withdrawn. I believe  
17 you indicated that the STOIP and Reserves Review  
18 Team concluded that the mismatch in reserves and  
19 fields was even greater than that found as a  
20 result of the bottoms-up review; is that correct?

21 MR. SMITH: Objection to form.

22 THE WITNESS: I, I think, sir, that  
23 maybe I could restate what I understand, is that  
24 in May 2003 we did a bottoms-up exercise, and we  
25 were sure or we felt that we had 700 million plus

0102

1 JOHN MALCOLM, October 20, 2006  
2 matched expectation reserves at risk. We did not  
3 see that as an absolute number. This was our  
4 first-pass, bottoms-up exercise. We did further  
5 work during that period, and in parallel with the  
6 STOIP and Reserves Review, they were also doing  
7 their work.

8 My understanding is that there was a  
9 Technical Shareholders Meeting around about  
10 September 2003, mid-September, I can't remember  
11 the date, and there was a presentation made at  
12 that Technical Shareholders Meeting behind the  
13 STOIP and Reserves Team Leader, Stan  
14 Christianson, on the, their findings on, or their  
15 interim findings, because they had not formally  
16 concluded.

17 They also had a prior presentation I  
18 think in maybe six weeks earlier than that to the  
19 Government, but the key one, as I remember well,  
20 was that September TSM, Technical Shareholders  
21 Meeting in The Hague, and they came out and said,  
22 no, we think PDO are conservative. We think the  
23 number is 934, 930 something, maybe it was six.  
24 In actual fact, these numbers don't matter,  
25 because the uncertainty in these numbers are so

0103

1 JOHN MALCOLM, October 20, 2006  
2 large, but they felt from their viewpoint the  
3 number was 930. I think that number then changed  
4 up to 960 or something. By the end of the year  
5 there was a whole pile of -- we had, uh, as PDO,

6 "we," PDO, had in principle, from our maturing  
7 understanding of the problems, no push-back on the  
8 930 number that they presented in September, and  
9 we were just pleased that we had got support from  
10 an independent body to support our concerns.

11 BY MR. MACFALL:

12 Q I believe you stated that that was, that  
13 number you believe was delivered at a presentation  
14 at a Technical Shareholders Meeting in September  
15 of 2003, correct?

16 A Around about then, yes.

17 Q Okay. Did you also indicate that that  
18 Technical Shareholders Meeting occurred at the  
19 Hague?

20 A I believe it was in The Hague. Again I  
21 need to check, I need to check my facts, but I  
22 think that one was held in The Hague.

23 Q Do you recall if all the shareholders of  
24 PDO attended that meeting?

25 A All shareholders attended the meeting,  
0104

1 JOHN MALCOLM, October 20, 2006  
2 including the other two private shareholders.

3 Q Did there come a time when Senior  
4 Management at Shell was apprised of the issue  
5 concerning the expectation reserves at PDO?

6 MR. SMITH: Objection to form and  
7 foundation.

8 THE WITNESS: When you say the word  
9 "Senior Management," sir, who are you referring  
10 to?

11 BY MR. MACFALL:

12 Q I'll identify specific individuals. Are  
13 you aware if Walter van der Vijver ultimately  
14 became aware of the mismatch between fields and  
15 expectation reserves at PDO?

16 A From my recollection, I believe that  
17 Walter van der Vijver, in June 2003, was advised  
18 of our belief and the mismatched volumes, and he  
19 authorized the Reserves Review, the payment of the  
20 Reserves Review. He took away all of this  
21 dillydallying on it in terms of who was paying  
22 what, but my understanding is he was working on

23 the recommendation of Din Megat as well as myself.

24 Q What's the basis of your understanding  
25 regarding when it was that Mr. van der Vijver was  
0105

1 JOHN MALCOLM, October 20, 2006  
2 advised of the findings made during the bottoms-up  
3 exercise?

4 MR. SMITH: Objection to form.

5 THE WITNESS: Again, sir, maybe I can  
6 reiterate my last answer, is that I believe in  
7 June 2006 (sic), when he came out to see how  
8 things were going in Oman, he was appraised around  
9 about that time. I cannot remember the exact  
10 date, but the beginning of 2006. And he was, I  
11 think like all parties, concerned that we should  
12 have this finding but supported PDO's request that  
13 we should have a review. No doubt this was, this  
14 was a significant thing. I think there was a few  
15 quick checks done by Din Megat and his people to  
16 say have these guys done something really stupid  
17 here, but I think once those quick checks were  
18 done -- which I think it was, given the time it  
19 was done, it was a reasonable piece of work,  
20 because it was done very, very fast, a bottoms-up  
21 review.

22 MR. SMITH: In your response to this  
23 question, you referred to "June 2006." Is that  
24 what you meant?

25 THE WITNESS: No. I'm sorry. I think  
0106

1 JOHN MALCOLM, October 20, 2006  
2 I'm getting a little bit tired here. June 2003.  
3 Thank you. I think six months, but June 2003. My  
4 apologies. Thank you for correcting me.

5 MR. MACFALL: In view of that, would  
6 this be a convenient time to take a break for  
7 lunch?

8 MR. SMITH: Sure.

9 THE VIDEOGRAPHER: We are going off the  
10 record. The time is 12:36 p.m.

11 (Whereupon, the lunch recess was taken.)

12 (Exhibit No. 2 was marked for  
13 identification and attached to the deposition

14 transcript.)

15 THE VIDEOGRAPHER: We are back on the  
16 record. The time is 1:21 p.m.

17 BY MR. MACFALL:

18 Q Good afternoon, Mr. Malcolm.

19 A Good afternoon.

20 Q Sir, you've just been handed a document  
21 that's been marked as Malcolm Exhibit 2 for  
22 identification. I'd ask you to take a look at  
23 that, sir. I would note for the record that you  
24 are shown as neither the author nor a recipient of  
25 the document, but if you could take an opportunity

0107

1 JOHN MALCOLM, October 20, 2006  
2 to look at it, and we'll discuss it when you're  
3 done.

4 Are you ready, Mr. Malcolm?

5 A Yes. I may have to go back to look at  
6 some details if your questions are detailed.

7 Q Absolutely. I would note for the  
8 record, before we begin, that the first page of  
9 the document is an e-mail from Philip Watts to  
10 various individuals, Mr. Van der Veer,  
11 Mr. Brinded, Mr. Skinner, Mr. van der Vijver. It  
12 references three attachments. The document that  
13 I've put in front of you contains what I believe  
14 is the first of those attachments, and I would  
15 just note that based on our search with regard to  
16 consecutive Bates numbers, that the other two  
17 attachments did not follow, but in any event, my  
18 questions are limited and really relate to the  
19 first attachment.

20 The subject, as indicated on the first  
21 page, is "Oman Visit," January 9th through 12th,  
22 2003. Mr. Malcolm, do you recall Mr. Watts coming  
23 to visit Oman in January of 2003?

24 A I do.

25 Q Were you aware of the purpose of

0108

1 JOHN MALCOLM, October 20, 2006  
2 Mr. Watts' visit at that time?

3 A My understanding of his visit and  
4 that -- and subsequent visits was that Mr. Watts

5 was trying to rebuild again the relationship  
6 between Shell and the Government of Oman and did  
7 it in a very tangible way in terms of showing the  
8 support and personally trying to resolve the  
9 problems that occurred in PDO and elsewhere, but I  
10 think it was to try to get again this alignment  
11 back in with the shareholders.

12 Q With respect to the document in front of  
13 you, do you recall if you've ever seen this  
14 before, sir?

15 A I don't, I don't recall having seen this  
16 before.

17 Q Directing your attention specifically to  
18 the second page of the document, there appears a  
19 Preamble at top, what is labeled "Preamble," with  
20 a series of bullet points that follows. And I  
21 realize that --

22 A This, sir, is under the second page of  
23 the document?

24 Q Second page of the document, first page  
25 of, I believe --

0109

1 JOHN MALCOLM, October 20, 2006

2 A Oh, sorry.

3 Q Okay. I believe this may have occurred  
4 prior to your tenure at PDO, but let me ask you.  
5 The second bullet point under the Preamble  
6 references negotiations with something called the  
7 "GISCO deal." Do you have an understanding of  
8 what that refers to, sir?

9 A I have a, I do not have a complete  
10 understanding of GISCO. My understanding is that  
11 GISCO, I think it stands for Gas Infrastructure  
12 Services Company, but it may -- but I'm not  
13 totally involved with it. It was a vehicle to  
14 help finance the upstream investment of the Oman  
15 LNG plant, OLNG, and so although the Government  
16 has a hundred percent ownership of the, of the  
17 upstream gas asset, that this was a vehicle that  
18 allowed the private shareholder to invest in the  
19 infrastructure required to get that gas to the  
20 downstream plant, which is referred to in here as  
21 "OLNG."



22 Q Thank you, sir.

23 Beneath that section is a section

24 captioned "The Key Meetings." Do you see that,

25 sir?

0110

1 JOHN MALCOLM, October 20, 2006

2 A Yes.

3 Q The first sentence, the first paragraph

4 beneath that caption references a briefing

5 document that had been provided to Mr. Watts. Do

6 you have any familiarity with a briefing document

7 provided to Mr. Watts in or about this time

8 regarding PDO?

9 A There would have been several briefing

10 documents for Mr. Watts. Generally the

11 coordinator of these would have been John Crocker,

12 and he would have taken information in from other

13 parties. With most of these briefing documents,

14 those that were outside my business remit, I had

15 no concern. That was for someone else, but my

16 only concern in all such briefing documents is

17 that they were accurate and reflected the facts.

18 So I am sure at that time myself, and John Crocker

19 would have come to me with some form of briefing

20 document and said, John, I'm going to show this,

21 and I would have said I don't think that's right

22 or whatever, but the responsibility generally for

23 providing the briefing document would have been

24 John Crocker, and it would have been his decision

25 as to what went.

0111

1 JOHN MALCOLM, October 20, 2006

2 Q What position did he hold, sir?

3 A He held at that time the position of

4 Shell Representative Office Oman. You may see in

5 his e-mails and some other correspondence his

6 reference indicator is SROO-GM, the General

7 Manager of the Shell Representative Office Oman,

8 and his function was very much as the title says;

9 it was a representational type function. He has

10 also another title, which is that of Shell Country

11 Chairman, which is again the kind of coordination

12 aspect of the various joint ventures that Shell

13 may have in Oman, and it has one in PDO, of  
14 course, one in the gas business, OLNG as it's  
15 mentioned here, and the other one, of course, is  
16 Shell Oman Markets, which is a 49 percent Shell  
17 Company and a 51 percent totally public offering  
18 company.

19 Q Thank you.

20 That sentence continues, indicating that  
21 Mr. Watts had an extensive session with John  
22 Crocker, yourself, Agnus Cassens and Peter Cryer.  
23 Could you identify Mr. Crocker for me, please.

24 A Mr. Crocker was --

25 Q Oh, I'm sorry. I apologize. Would you

0112

1 JOHN MALCOLM, October 20, 2006  
2 identify Ms. Cassens for me, please.

3 A Yes, certainly. Agnus Cassens is the --  
4 was and still is the General Manager of Oman LNG,  
5 Oman Liquid Natural Gas, which we all refer to as  
6 "OLNG," which is again a joint venture company  
7 between private shareholders and the Government.

8 Q Is it Agnus or Angus?

9 A He is German, and so it is -- although  
10 it's spelled -- I think you've got the correct  
11 spelling, but it's Agnus.

12 Q Thank you.

13 And Mr. Cryer?

14 A I'm not actually too sure of what his  
15 job description was, but he was effectively with  
16 Shell International Gas, SIG, and so he was, uh,  
17 had some responsibility for the, the third "train"  
18 in negotiations that's talked about here in this  
19 document, but I'm sorry, I don't know exactly what  
20 his job title is.

21 Q That's fine, sir.

22 Do you recall attending the meeting with  
23 Mr. Watts and the individuals shown here in this  
24 document?

25 A It was a long time ago, but I, I recall

0113

1 JOHN MALCOLM, October 20, 2006  
2 the meeting.

3 Q Do you recall if the issue of the

4 production shortfall at PDO was discussed during  
5 that meeting?

6 A The -- more than the shortfall, the  
7 discussion was about the Business Plan, which, as  
8 we've said before, at that time was BP03. What we  
9 intended to do is to tackle the short, medium and  
10 long-term issues, and I think that this talks  
11 about those in some ways, about the waterflood  
12 projects and the UR projects.

13 Q Do you recall if expectation reserves  
14 were discussed specifically during this meeting?  
15 And I do realize this was prior to the bottoms-up  
16 exercise.

17 A I do not. I do not recall expectation  
18 reserves being discussed at this meeting.

19 Q The sentence continues with a reference  
20 to "HM." Could you please identify that  
21 individual for me, sir.

22 A Yeah. "HM" here stands for His Majesty,  
23 Sultan Kaboos, who is the Sultan of Oman.

24 Q Do you recall attending any meetings  
25 between Mr. Watts and His Majesty, the Sultan of  
0114

1 JOHN MALCOLM, October 20, 2006  
2 Oman?

3 A Yes, I do.

4 Q Do you recall approximately how long  
5 that meeting lasted?

6 A From my memory -- and there were several  
7 meetings, but if you're talking about this  
8 particular one --

9 Q I am.

10 A -- the meeting was effectively split  
11 into three parts. The first part where was His  
12 Majesty and Sir Philip Watts had a meeting in  
13 private. There was then a meeting at which  
14 myself, John Crocker and another Government  
15 Minister -- I don't remember what Government  
16 Ministers were there, but it was only about five,  
17 five or six people in the room, where there was a  
18 general discussion where I took His Majesty  
19 through the plan for 2003, and then that was  
20 followed then by dinner.

21 Q Do you recall if His Majesty commented  
22 upon the Business Plan?

23 A His Majesty commented upon the Business  
24 Plan, and as I read this, a point came back about,  
25 uh, that we discussed actually earlier in the  
0115

1 JOHN MALCOLM, October 20, 2006  
2 morning, but the dip in production in PDO in the  
3 early seventies, and His Majesty was understanding  
4 of PDO's problems and I think appreciated this --  
5 I hate to use the word "total," but almost total  
6 commitment from Shell, from top down, that they  
7 were going to do whatever was required to get this  
8 production issue sorted out and get PDO back to  
9 being a successful company again, what resources  
10 that took or whatever.

11 So you see this, and I think this text  
12 actually explains it better than any words of mine  
13 could have done, is that this commitment to  
14 understanding the problems, trying to get the  
15 alignment back again, you know, that at the end of  
16 the day we have a long, long association with  
17 Oman, and we or Shell at that point wanted to do  
18 the right thing. They wanted to get things back  
19 on track.

20 Q Was there any discussion of the specific  
21 efforts that Shell would undertake in order to  
22 increase production at Oman?

23 MR. SMITH: This was during the meeting  
24 with His Majesty?

25 MR. MACFALL: Yes.

0116

1 JOHN MALCOLM, October 20, 2006

2 THE WITNESS: Most -- there was the side  
3 meeting, the first meeting that I was not part of,  
4 so I cannot remember, but the -- in this meeting  
5 I -- if I remember the meeting correctly, and  
6 again you must excuse me; it is such a long time  
7 ago. We had a number of place cards of kind of  
8 view drafts that I would through, take His Majesty  
9 through to say this is what we're trying to do  
10 specifically in 2003 and going forward in terms of  
11 the waterfloods and the O.R. projects.

12 BY MR. MACFALL:

13 Q Directing your attention now  
14 specifically to Number 3 which appears beneath  
15 that first full paragraph it states or it  
16 discusses a "declaration that the Concession  
17 negotiation should start in March" of 2003, and it  
18 continues. The "Concession" that's referenced  
19 here; is that the Concession that includes the  
20 Operating Agreement or Concession between Shell  
21 and Oman?

22 MR. SMITH: Objection to form.

23 THE WITNESS: My understanding of what  
24 is referred to here is the Concession Agreement  
25 that was originally signed in 1937 between IPC,  
0117

1 JOHN MALCOLM, October 20, 2006  
2 which was then the Iraq Petroleum Company, which  
3 consisted of a large number of partners, was for  
4 75 years, and ran from 1937 to 2012. The first  
5 major activity of IPC was in 1955, approximately,  
6 maybe it was '56, you must excuse me, and that was  
7 a drilling of the Fahud 1 well, which was a dry  
8 well, and there was another two subsequent wells  
9 drilled, but effectively my understanding again  
10 from my reading of the subject is that IPC,  
11 various members of IPC split off at that point,  
12 and you were left with effectively Shell with  
13 85 percent and Partex was 15 percent.

14 They did some rudimentary seismic in the  
15 early 1960s, and in 1962 they went back and  
16 drilled in Yibal, they hit oil. They drilled in  
17 Natih, N-A-T-I-H, they hit oil. They went back to  
18 Fahud on the other side of the Yibal and they hit  
19 oil, and effectively from 1967 onwards you had  
20 this -- or from 1960 onwards you had this very,  
21 very close relationship between Shell and the  
22 country. In 1967 was the first export of oil from  
23 the country, and that relationship, that had been  
24 in place ever since.

25 To put it in context, sir, is that the  
0118

1 JOHN MALCOLM, October 20, 2006  
2 85 percent -- the company was reconstituted at

3 some point, I think it was in 1960 -- 1980 I think  
4 it was, and the Government is today 60 percent  
5 public, 40 percent private. If you take  
6 85 percent of 40 percent, you come out with 34, so  
7 that's -- Total bought back in again, ten percent  
8 of the 15 percent of Partex later. So this refers  
9 to the Concession Agreement that was signed in  
10 1937 that ran until 2012 that had gone through a  
11 number of changes but was a Concession Agreement  
12 under which we were operating at that time.

13 And without prompting, I think the words  
14 here, which I have not read before, "His Majesty  
15 made a resounding declaration." I think that most  
16 people who were associated with Shell, although we  
17 knew we had -- at PDO we had a massive change  
18 program to go through. This was in beginning  
19 2003. The Concession Agreement was running out in  
20 2012. I don't think anybody would have raised the  
21 issue of the Concession extension, because -- I  
22 hate to use the word -- many of us were ashamed of  
23 the state that PDO was in, but His Majesty  
24 actually made the declaration in the meeting, and  
25 I was sitting, I was sitting there when he said

0119

1 JOHN MALCOLM, October 20, 2006  
2 the words, and, you know, it was an incredible  
3 vote of confidence in Phil Watts and in Shell. He  
4 actually made that declaration at that meeting.

5 BY MR. MACFALL:

6 Q The following paragraph references a  
7 meeting with -- between Mr. Watts and Ministers  
8 Macki and Rumhy, together with Mr. Crocker and  
9 yourself. Do you recall that meeting, sir?

10 A I remember this meeting, but not as  
11 clearly as I remember the previous meeting. And  
12 sir, maybe I could just say for the record, I know  
13 that all of this is taken in confidence, this  
14 testimony, but the previous meeting with His  
15 Majesty is very, very strictly confidential.

16 Q I do appreciate that.

17 A And I'm trying to be as open as possible  
18 within that belief and that confidence.

19 MR. SMITH: Just so the record reflects



20 this fact, I think we will certainly designate  
21 those portions of the transcript as highly  
22 confidential under the Confidentiality Agreement  
23 in the case.

24 MR. MACFALL: Understood.

25 MR. SMITH: Okay.

0120

1 JOHN MALCOLM, October 20, 2006

2 THE WITNESS: So to go back and answer  
3 your question, sir, I remember this meeting, but  
4 not as clearly as I remember the other meeting.  
5 The other aspect, of course, on this meeting is  
6 that it is mainly about the Downstream Gas  
7 Business.

8 BY MR. MACFALL:

9 Q The third sentence of that paragraph  
10 characterizes the meeting as "rather frank" and  
11 "at times difficult" and then continues. To the  
12 best of your recollection, did any part of the  
13 discussion that was difficult concern the oil  
14 portion of Shell's concerns in Oman versus the  
15 gas?

16 A I, I think that as far -- my  
17 understanding, sir, I have to see it from my  
18 viewpoint, is that when you have problems on one  
19 side of your business, of course, that affects  
20 your shareholders or the Government's judgment on  
21 another side of the business. So you effectively  
22 had one Operator, PDO, which was operating on both  
23 sides of the business, so if you got problems on  
24 one side of your business, it is natural that your  
25 majority shareholders should be upset about the

0121

1 JOHN MALCOLM, October 20, 2006

2 whole business.

3 Q I believe you had stated that Mr. Watts  
4 made several visits to Oman during that period,  
5 and that's 2002 until 2004; is that correct?

6 A Yes. I think the -- his last visit was  
7 right about New Year 2003.

8 Q Do you recall approximately how many  
9 times --

10 A When I say "New Year 2003," I mean New

11 Year 2004, the 31st of December, 2003.

12 Q Thank you for that clarification, sir.

13 Do you recall approximately how many  
14 times Mr. Watts visited Oman during that period?

15 A I, I would need to go and check my, my  
16 diary, but I would have said it was once every  
17 three or four months. I know that he was there at  
18 this time. I know that he was there at year-end.  
19 I cannot remember if there was one or two visits  
20 in between, but again my memory fails me in that,  
21 but he was there rebuilding the relationship.

22 Q Did you meet with Mr. Watts during each  
23 of his visits during 2002 and 2004?

24 MR. SMITH: Objection to form.

25 THE WITNESS: When Sir Philip Watts came

0122

1 JOHN MALCOLM, October 20, 2006  
2 to Oman, I think -- I believe that I met him on  
3 each one of those occasions.

4 BY MR. MACFALL:

5 Q Do you recall if you had occasion to  
6 discuss with Mr. Watts, during any of his visits  
7 to Oman, the issue of the mismatch between the  
8 expectation reserves and specific fields at PDO?

9 MS. LATIMER: Object to the form.

10 BY MR. MACFALL:

11 Q You can answer if you can.

12 A First of all, I think my understanding  
13 is -- and I have no documentary proof of this. My  
14 understanding is that when we briefed Din Megat  
15 and Walter van der Vijver in June 2003, that that  
16 briefing would have naturally gone to Sir Philip  
17 Watts. I have no doubts that he would understand  
18 that. And I know from a meeting that was held, I  
19 think it was in October or so, he was up to speed  
20 with the expectation reserves interim outcome that  
21 came from the STOIIP and Reserves Review, and he  
22 and I -- I was briefing him before we met with His  
23 Majesty on I think it was the 31st of December,  
24 2003, as to progress on -- as to what progress  
25 there had been on our business during the year.

0123

1 JOHN MALCOLM, October 20, 2006

2 Q Separate and apart from any briefing  
3 that Mr. Watts would have or may have received  
4 from Mr. Megat and others at Shell, do you recall  
5 specifically discussing the expectation reserves  
6 issue with him during that period?

7 A Yes. I remember making -- I think it  
8 was a presentation to, a very short presentation  
9 to the CMD, must have been October-ish 2003, and I  
10 remember going through the view drafts that we  
11 were going to use, because when we went to see His  
12 Majesty, I would actually take His Majesty through  
13 the work that PDO was doing at that time, because  
14 it was very much PDO's plan of where we were going  
15 with Shell providing support, so that that  
16 distinction was always made. And so I can  
17 remember in the end of December 2003 going through  
18 the view drafts that I was going to utilize on our  
19 briefing for His Majesty that evening on the  
20 31st of December.

21 Q Excluding the CMD presentation about  
22 which you just testified, do you recall speaking  
23 with Mr. Watts during any of Mr. Watts' visits to  
24 Oman in connection -- withdrawn. At any point  
25 when Mr. Watts came to Oman during the period of  
0124

1 JOHN MALCOLM, October 20, 2006  
2 2002 to 2004, do you recall speaking with him, in  
3 Oman, concerning the PDO reserves issue?

4 A I remember very clearly briefing him  
5 before we went to see His Majesty in 1st December  
6 of 2003. That is very, very clear in my mind, and  
7 it was -- because at that point, if my memory  
8 serves me well, I think the Shell Reserves and  
9 STOIP Review had been close -- had been  
10 substantially closed out. I think it had been  
11 closed out in December of 2003, but that is the  
12 one I remember. I don't remember in between. My  
13 problem is I can't remember the visits in between.  
14 I remember the visit very clearly in January, I  
15 remember the visit very clearly in December, and I  
16 think there was another one in between there, but  
17 again -- and I remember the CMD presentation that  
18 was around about October.

19 Q With regard to the CMD presentation, I  
20 take it that that took place at The Hague; is that  
21 correct?

22 A I cannot remember if it took place in  
23 The Hague or London. At that time Shell had two  
24 head offices.

25 Q Do you recall approximately how long  
0125

1 JOHN MALCOLM, October 20, 2006  
2 your presentation lasted?

3 MR. SMITH: To the CMD?

4 BY MR. MACFALL:

5 Q To the CMD. Thank you.

6 A It wasn't very long. Again it was over  
7 three years ago, but it's off the order of not  
8 more than -- I would have been surprised if it was  
9 more than 30 minutes, but it's -- most of these  
10 things have some form of pre-reading beforehand  
11 and very, very few drafts and clarifications.

12 Q Do you recall if there was reading  
13 material provided to the CMD prior to your  
14 presentation concerning the subject matter of your  
15 presentation?

16 A I have no doubt that there would have  
17 been reading matters supplied. That would  
18 generally have been, uh, come up through the  
19 General Manager or one of the advisors to CMD.  
20 They would have channelled all that through. I'm  
21 sure that we vastly would have contributed to  
22 whatever information was required.

23 Q What was the subject of your  
24 presentation to the CMD at that time?

25 A That was a long time ago. My  
0126

1 JOHN MALCOLM, October 20, 2006  
2 understanding, sir, is that this was sometime in  
3 October 2003. You may well have the exact date  
4 there to remind me. It really had kind of two --  
5 two major milestones had come in place. One had  
6 been the presentation on the Reserves and STOIP  
7 Review, and then the other one had been  
8 effectively -- and up to that point had been all  
9 about expectation issues, and then the other one

10 had been after the Reserves Auditor, Shell's  
11 Reserves Auditor had come in, which I think was  
12 just before that date. It was end of September,  
13 beginning of October, where the whole issue of the  
14 proved reserves issue had come in, which was -- up  
15 to that point everybody was focused on  
16 expectation.

17 Q Do you recall if any part of your  
18 presentation contained proved reserves as opposed  
19 to expectation reserves?

20 A I believe that there was one view draft  
21 in there that had proved, but that was after the  
22 external or the Shell Reserves Auditor.

23 Q Was there any discussion amongst or  
24 between yourself and members of the CMD in  
25 connection with that presentation during your  
0127

1 JOHN MALCOLM, October 20, 2006  
2 meeting with them?

3 A Again, sir, it's a long time ago. I'm  
4 sure there was clarifications raised, but the  
5 details I cannot remember, to be honest, after  
6 three and a quarter years, but I'm sure the  
7 minutes of meeting -- there must be minutes of  
8 meeting which show any such discussions.

9 Q Did there come a time during 2003 when  
10 you became aware of an issue arising in connection  
11 with proved reserves versus expectation reserves?

12 A Yeah. I think that up to about  
13 September 2003 we had so many problems on the  
14 expectation reserves -- to put this in context,  
15 something like 20 percent of our expectation  
16 reserves were placed in, at best, a category of  
17 doubt whether or not they were moved into scope or  
18 whether they were moved further out, but they were  
19 in a significant category of doubt. And again I  
20 don't remember the exact date, but around about  
21 the end of September, maybe it was beginning of  
22 October, the Reserves Auditor came in for Shell to  
23 check and prove reserves, and there was a  
24 presentation made, and it's at that point I  
25 realized that from Shell's viewpoint that they --

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1 JOHN MALCOLM, October 20, 2006

2 just as we had a problem on expectation reserves,  
3 there was also a problem on proved reserves that  
4 was proportionately bigger than one would have  
5 expected.

6 (Exhibit No. 3 was marked for  
7 identification and attached to the deposition  
8 transcript.)

9 BY MR. MACFALL:

10 Q Mr. Malcolm, I've just handed you a  
11 document that has been marked as Malcolm Exhibit 3  
12 for identification. There is no indication on the  
13 document that you are either an author, a  
14 recipient or were copied, but I would ask you to  
15 look at it, sir, and let me know when you're done.

16 A It's a complicated attachment.

17 Q It is, sir. Do you recall if you've  
18 ever seen this document before, Mr. Malcolm?

19 A I cannot recall having seen this  
20 document before.

21 Q For the record, the document is an  
22 e-mail and attachment. The e-mail is from John  
23 Pay, dated September 8, 2003, to Paul Mann, John  
24 Blascos, and a cc to various individuals. The  
25 subject line on the e-mail reads "PDO Reserves

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1 JOHN MALCOLM, October 20, 2006

2 Meetings: Notes."

3 The attachment is captioned "Notes on  
4 SIEP/PDO Reserves Meeting, 26-27 August 2003." On  
5 the first page of the notes themselves, second  
6 page of the document, sir, the first sentence in  
7 the first full paragraph references a meeting  
8 between the SIEP Hydrocarbon Resource Coordinator  
9 and PDO staff. Do you recall if such a meeting  
10 occurred, sir?

11 A I do not recall such a meeting  
12 occurring, but John Pay must have visited PDO to  
13 have the meeting, so I have no doubt that such  
14 meeting did occur.

15 Q Do you recall meeting with Mr. Pay at  
16 any point in or around August of 2003?

17 A No, I don't. And again that may be my



18 memory, but I do not remember meeting with him.

19 Q Beneath the first full paragraph there  
20 is two sections with numbers appearing next to  
21 them, the first of which is captioned "ARPR Match  
22 With Project Data." The paragraph beneath that  
23 references some 715 million barrels, a hundred  
24 percent PDO share, of expectation reserves. That  
25 first sentence states that it "may need to be  
0130

1 JOHN MALCOLM, October 20, 2006  
2 de-booked."

3 My question is: Do you recall if there  
4 was discussion in PDO about the possibility of  
5 de-booking approximately 715 million barrels of  
6 expectation reserves in or about August of 2003?

7 MR. SMITH: Objection to form.

8 THE WITNESS: I think, sir, that this  
9 number, as I understand it -- again I was not at  
10 the meeting, but this number I think reflects that  
11 the number that came out of our bottoms-up  
12 exercise. At this moment in time, if you  
13 remember, I think the reserves, the STOIIP and  
14 Reserves Review reported out substantially around  
15 about the middle of September, so this number I  
16 believe is the number that we in PDO believed were  
17 the volumes at risk at that time, and whether or  
18 not we -- what means that we would identify these  
19 at-risk reserves, they would certainly not be part  
20 of any foundation for a future production program.

21 So the, the match reserves issue, one is  
22 you're saying when we match reserves at projects,  
23 this is how we see our production levels going  
24 forward. You're left with this other bundle, and  
25 then you're left with a question of what do you  
0131

1 JOHN MALCOLM, October 20, 2006  
2 actually do with it in terms of your ARPR, but  
3 what is clear in your ARPR is that you actually  
4 have to identify it and you have to flag it some  
5 way, or it's suspect. You can take them all off  
6 or you can flag them, and then, as you do Field  
7 Development Plans, you can confirm or otherwise  
8 that you're going to remove them.

9 BY MR. MACFALL:

10 Q Do you recall if there were discussions  
11 within PDO in or about August of 2003 that those  
12 expectation reserves be de-booked? And by "those"  
13 I mean the expectation reserves which were  
14 identified as -- in connection with the bottoms-up  
15 exercise.

16 MR. SMITH: Objection to the form.

17 THE WITNESS: I do not -- first of all,  
18 in terms of timing, sir, I don't recall such  
19 discussions, but in terms of timing, in May we had  
20 flagged the problem as we understood it. There  
21 was an ongoing STOIP and Reserves Review being  
22 carried out. We actually didn't need to make a  
23 decision until we issued our ARPR effective 1st of  
24 January 2003. So I don't totally buy into whether  
25 or not we needed to book or de-book at this moment

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1 JOHN MALCOLM, October 20, 2006  
2 in time, and as hindsight shows, the number was  
3 actually far bigger than 715. It was 900 and  
4 something.

5 So there was really a concern of how do  
6 we handle this in our ARPR. Do you just take it  
7 off the bottom line? Do you make a provision?  
8 How do you actually handle it? But at that moment  
9 in time, 715 was still our first pass number for  
10 me. I think it was 715. If you'd ask me what  
11 number it was, I would say it was greater than  
12 700, but that was more or less the number in May.

13 BY MR. MACFALL:

14 Q Did Mr. Pay hold the position of SIEP  
15 Hydrocarbon Resource Coordinator at Shell in or  
16 about August of 2003?

17 MR. SMITH: Objection to form and  
18 foundation.

19 THE WITNESS: I, I could not -- I have  
20 no knowledge. I can only take the exhibit that  
21 you have put in front of me which says that he  
22 held such a position.

23 BY MR. MACFALL:

24 Q Did you have any interaction with  
25 Mr. Pay during 2003 to 2004?

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1 JOHN MALCOLM, October 20, 2006

2 A Not that I can remember.

3 Q If you look at Number 2 beneath the  
4 first paragraph, it's captioned "Proposed Approach  
5 to Reserves Categorization," and material follows  
6 after regarding expectation developed reserves,  
7 proved developed reserves, expectation undeveloped  
8 reserves and proved undeveloped reserves.

9 The first sentence with regard to that  
10 says, "Of the remaining Shell Reserves within  
11 license, a revised subclassification is proposed  
12 by PDO as follows," and that material follows.

13 A Sorry, sir. So we're in Section 2?

14 Q Section 2. I'm sorry.

15 A And then we've got "Expectation  
16 Developed Reserves, all projects in the Operating  
17 phase"?

18 Q Right, that section there, the sentence  
19 that precedes it.

20 A Oh, yes.

21 Q Okay, "a revised subclassification," the  
22 sentence reads, "is proposed by PDO." Do you  
23 recall PDO proposing a revised subclassification  
24 with respect to reserves in or about August of  
25 2003?

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1 JOHN MALCOLM, October 20, 2006

2 MR. SMITH: Objection to form and  
3 foundation.

4 THE WITNESS: Again I don't believe I  
5 was at this meeting, sir, and at that point in  
6 time, up to that point my understanding was that  
7 we had on our books expectation reserves and we  
8 had on our books proved reserves, and as I advised  
9 you earlier, those proved reserves numbers were of  
10 dubious value, and I see here that some of them  
11 were even negative numbers, which backs up my  
12 statement. That someone would want to split the  
13 division down between developed and undeveloped  
14 does not sound to me to be unreasonable. It gives  
15 a greater feeling of -- a handle on what parts are  
16 dependent on future projects and what parts are

17 dependent on installed capacity. So I was not  
18 involved in this, but it is not an unreasonable  
19 further classification, half into developed and  
20 undeveloped.

21 BY MR. MACFALL:

22 Q Were you aware of anyone within PDO  
23 proposing a subclassification revision or scheme  
24 to --

25 MR. SMITH: Objection to form.

0135

1 JOHN MALCOLM, October 20, 2006

2 MR. MACFALL: I wasn't even done. I'll  
3 rephrase it.

4 BY MR. MACFALL:

5 Q Do you know what Mr. Pay is talking  
6 about or the author of this note is talking about  
7 when they reference the proposal by PDO of the  
8 classification set forth here or the  
9 subclassification set forth here?

10 MR. SMITH: Objection to form and  
11 foundation.

12 THE WITNESS: Sir, I don't really  
13 understand the question, but -- I want to try to  
14 answer it, but I don't understand it.

15 BY MR. MACFALL:

16 Q Sure. The note indicates that the  
17 subclassification that we've been discussing with  
18 respect to reserves was proposed by PDO. Do you  
19 know who at PDO, if anyone, proposed that  
20 subclassification scheme?

21 MR. SMITH: Objection to form and  
22 foundation.

23 THE WITNESS: This, this was a  
24 significant amount of time ago, and so I find it  
25 extremely difficult to answer that question, but

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1 JOHN MALCOLM, October 20, 2006

2 obviously between our head of Reservoir  
3 Engineering and our head of Planning, Corporate  
4 Planning, one could have, uh, one could have seen  
5 that they would have proposed such a split,  
6 because to go back again, sir, as I said rather at  
7 the beginning, one of the problems that we had in

8 PDO when I came in was a lack of up-to-date Field  
9 Development Plans. In those Field Development  
10 Plans we had put in place an in-country Study  
11 Center to actually build those plans, and what  
12 those plans tried to do for you is to actually  
13 give you some greater focus for going forward on  
14 the development of the field, especially in those  
15 aspects that are to date undeveloped reserves,  
16 that have no wells drilled for them at that moment  
17 in time.

18 So the split between developed and  
19 undeveloped is, is -- you know, that someone  
20 should propose such a split is not, you know,  
21 unusual in any way. I think that the real issue,  
22 of course, is how do you define -- how do you  
23 define your undeveloped reserves in a mature field  
24 if you actually have a drilling program going  
25 forward and not an FDP. So again, sir, I'm

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1 JOHN MALCOLM, October 20, 2006  
2 reading something, you know, and trying to  
3 interpret it, but it is not unreasonable that you  
4 split between what is already an installed  
5 capacity and what is going to be the future  
6 installed capacity.

7 BY MR. MACFALL:

8 Q I believe you indicated two individuals.  
9 I'm sorry. It was the Senior Petroleum Engineer I  
10 believe is one position. Withdrawn. Let me try  
11 that again. Were there individuals within PDO  
12 whose scope of responsibility would have included  
13 the classification of various reserves at PDO?

14 A Yes.

15 Q And could you just identify by title  
16 once again for me those positions, sir.

17 A The, the -- this was in 2003. If you  
18 just let me look at the reference indicators,  
19 organizations change so quickly.

20 Q Sure.

21 A Effectively in terms of our most senior  
22 reservoir engineer or most senior petroleum  
23 engineer at that time would have been Stuart  
24 Evans, who is today -- I cannot remember his title

25 at that time, but today is our Petroleum

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1 JOHN MALCOLM, October 20, 2006  
2 Engineering Director. And one of the people  
3 mentioned here, Dave Kemshell, works for him. So  
4 in terms of a guidance, in terms of how we handle  
5 petroleum engineering issues internally within PDO  
6 effectively comes under the agreement of the  
7 Petroleum Engineering Director, and the consistent  
8 reporting and pooling together of those issues  
9 comes under the remit of the head of Corporate  
10 Planning.

11 Q Mr. Malcolm, I'd now like to direct your  
12 attention to the following page in the document,  
13 sir. If you could turn to that page, please,  
14 you'll see about a third of the way down the page  
15 there is an item numbered 3, "Potentially Exposed  
16 Proved Reserves." Do you see that, sir?

17 A Yes.

18 Q Beneath that the paragraph discusses  
19 reserves that are potentially exposed, according  
20 to this -- there is a reference in the first  
21 sentence to potential of exposure "due to a lack  
22 of technical maturity." Do you see that, sir?  
23 It's in the second line.

24 A Yes.

25 Q Do you recall any reserves at PDO being

0139

1 JOHN MALCOLM, October 20, 2006  
2 exposed in or about August of 2003 due to a lack  
3 of technical maturity?

4 MR. SMITH: Objection to form and to  
5 foundation.

6 THE WITNESS: As I have explained  
7 previously, in PDO it is a company that's run on  
8 an expectation basis. We realized that we did not  
9 have -- we had a matched reserves problem of,  
10 something like what we thought was 715 million.  
11 It was actually higher than that. And by the  
12 definition, effectively those reserves could not  
13 be matched with the project, so the Field  
14 Development Plans also that we knew and we were  
15 working very hard on was to try to prove up our



16 percentage of STOIP that was covered. I cannot  
17 remember the exact numbers, but when I went into  
18 PDO it was something like ten or 15 percent, and  
19 we have been dramatically building up again the  
20 coverage of our fields with up-to-date Field  
21 Development Plans since, since I moved in, and  
22 today I think we're at over 60 percent in terms of  
23 STOIP, and increasing.

24 So to answer your question, sir, I  
25 cannot answer your question under the proved side.  
0140

1 JOHN MALCOLM, October 20, 2006  
2 I can definitely answer it under the expectation  
3 side, is that we needed greater maturity of those  
4 Field Development Plans, not just to confirm the  
5 de-bookings, but to actually show the upside on  
6 developments.

7 BY MR. MACFALL:

8 Q Mr. Malcolm, I'd like now to direct your  
9 attention about halfway through that paragraph,  
10 middle line -- I'll give you the lines. Six lines  
11 from the bottom of the paragraph there is a  
12 sentence that begins, "PDO proposes to retain."  
13 Do you see that, sir?

14 A Yes.

15 Q Okay. And the sentence reads, "PDO  
16 proposes to retain these reserves on the books  
17 pending completion of technical project definition  
18 work." Is the reference there, if you know, to  
19 technical project definition work a reference to  
20 the STOIP Reserves Review that was ongoing at  
21 that time?

22 MR. SMITH: Objection to form. That's a  
23 compound question.

24 THE WITNESS: I'm not quite sure what a  
25 compound question is, sir.

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1 JOHN MALCOLM, October 20, 2006

2 MR. SMITH: It's more than one question.

3 THE WITNESS: More than one question.

4 BY MR. MACFALL:

5 Q I'll rephrase the question. Is the  
6 reference to "technical project definition work"

7 in that sentence a reference to the STOIP and

8 Reserves Review?

9 MR. SMITH: Objection to form and lack  
10 of foundation.

11 THE WITNESS: Sir, again, if you ask me  
12 what do I assume by that question, I think that  
13 the stance in PDO on expectation volumes, let us  
14 talk first and foremost, was that once we  
15 finished -- once the STOIP and Reserves Review  
16 had been finished, we should be very careful at  
17 how we booked and de-booked reserves.

18 So if you take, for example, the  
19 expectation volumes that were at risk, internally  
20 within PDO, although we were -- we saw the need to  
21 qualify those reserves in some manner or other, we  
22 saw just writing off reserves on the basis of a  
23 very quick review was not the right way to do it,  
24 and the right way to do things was to ensure that  
25 our reserves were tied up with up-to-date Field  
0142

1 JOHN MALCOLM, October 20, 2006  
2 Development Plans for which we had a plan in  
3 place.

4 So we saw that to book and de-book  
5 definitive reserves within PDO's expectation  
6 volumes, we should try to do so wherever possible  
7 with a Field Development Plan, and we had a number  
8 of plans going forward for our fields. That  
9 doesn't mean to say that we shouldn't be prudent  
10 in qualifying numbers, but we shouldn't just say  
11 we'll take 200 million of that field. We saw that  
12 we had to get some rigor back into the system, and  
13 we have Field Development Plans that said this is  
14 where we start today, this is the development  
15 production we have, these are the projects we have  
16 in the pipeline, this is how we see the  
17 undeveloped and future undeveloped coming from.

18 So that was, that was the mindset within  
19 PDO was one of let us do this in a very rigorous  
20 and professional manner. Let's not just, because  
21 we think the number is 715, go ahead and whack 715  
22 off. As we found out later on, the number we  
23 thought came out to be 900 and something. So it

24 was yes, we have a problem of reserves at risk. I  
25 think it says further down here that in terms of  
0143

1 JOHN MALCOLM, October 20, 2006  
2 proved reserves as far as PDO was concerned, our  
3 numbers were actually, on the books were seen as  
4 conservative, so I think there's a -- when this is  
5 being written, there is a complication here  
6 between what Shell has and what PDO has, but if  
7 you read the Paragraph Number 4, it says, "As  
8 such, PDO may be able to revise upwards its  
9 overall estimate of Proved Reserves, even after  
10 taking into account the potential de-bookings,"  
11 because our proved reserves numbers were so low  
12 anyhow, because they had not been updated for such  
13 a long time. So I think that the way this is  
14 written was a little bit confusing.

15 PDO's viewpoint on booking reserves was  
16 that we should book and de-book wherever possible  
17 the way that PDO -- we felt the way that PDO  
18 should book and de-book reserves should be tied up  
19 with Field Development Plans. When I say  
20 "reserves" in that case, I'm substantially at that  
21 point talking about expectation reserves, and  
22 today, given the new Concession Agreement and our  
23 IFRS requirements, it would also apply to the  
24 proved reserves as well.

25  
0144

1 JOHN MALCOLM, October 20, 2006

2 BY MR. MACFALL:

3 Q You had stated that the STOIP and  
4 Reserves Review issued interim findings in or  
5 about September of 2003; is that correct?

6 A About the middle of September, sir. I  
7 think it was maybe the 18th or sometime in the  
8 middle of September.

9 Q Did those interim findings include a  
10 quantification of exposed expectation reserves at  
11 PDO?

12 MR. SMITH: Objection to form and  
13 foundation.

14 BY MR. MACFALL:

15 Q You can answer.

16 A I -- from what I remember, sir, the  
17 number that was presented as matched reserves at  
18 that presentation by Stan Christianson was a  
19 number like 930 something million. I think it was  
20 934 or 936, but again my memory is -- but it was  
21 of that order, and it was understood that there  
22 was further work to be done to increase the  
23 percentage of STOIIP coverage by that review, and  
24 that continued up to December. And again I cannot  
25 remember the number in December, but I think it

0145

1 JOHN MALCOLM, October 20, 2006  
2 was a number like 960 something.

3 Q Do you recall if the STOIIP and Reserves  
4 Review interim findings indicated that there were  
5 any proved reserves that were exposed in or about  
6 September of 2003?

7 MR. SMITH: Objection to form.

8 THE WITNESS: My understanding is that  
9 by, almost by definition, that review was on  
10 STOIIP and expectation reserves.

11 BY MR. MACFALL:

12 Q Do you recall when at first --  
13 withdrawn. Did there come a time when you learned  
14 that there were issues with proved reserves that  
15 were related to the expectation reserves issues at  
16 PDO?

17 MR. SMITH: Objection to form.

18 THE WITNESS: I cannot answer that  
19 question in the form that you put it. I can,  
20 sir -- and I want to help and be helpful. I can  
21 say that my understanding for the proved reserves  
22 issue was around the time that the Reserves,  
23 Shell's Reserves Auditor came in, which was around  
24 about October, and -- but that was, that was, in  
25 my opinion, it's connected but separate. I don't

0146

1 JOHN MALCOLM, October 20, 2006  
2 think that you can combine the two issues  
3 together.

4 BY MR. MACFALL:

5 Q By -- the auditor you're referring to;

6 is that Anton Barendregt?

7 A Yes.

8 Q Did he conduct an audit of PDO on behalf  
9 of Shell in 2003?

10 A Yes.

11 Q Did you meet with Mr. Barendregt during  
12 the course of that audit?

13 A Yes.

14 MR. SMITH: If you're going to change to  
15 that subject, could we take a quick break  
16 beforehand.

17 THE VIDEOGRAPHER: This marks the end of  
18 Tape 2 in the deposition of Mr. Malcolm. We are  
19 going off the record. The time is 2:25 p.m.

20 (Whereupon, a short recess was taken.)

21 THE VIDEOGRAPHER: This marks the  
22 beginning of Tape 3 in the deposition of  
23 Mr. Malcolm. We are back on the record. The time  
24 is 2:42 p.m.

25

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1 JOHN MALCOLM, October 20, 2006

2 (Exhibit No. 4 was marked for  
3 identification and attached to the deposition  
4 transcript.)

5 BY MR. MACFALL:

6 Q You've just been handed a document that  
7 was marked for identification as Malcolm Exhibit  
8 4. I'd ask you to take a look at the document and  
9 peruse it briefly and tell me if you recognize it.

10 A Yes, sir.

11 Q Do you recognize the document, sir?

12 A I recognize the document. I recognize  
13 the first page rather than all the detailed  
14 attachments, but I recognize it.

15 Q What is it that you recognize it to be,  
16 sir?

17 A My understanding is that this is the  
18 report from Anton Barendregt, who is the Group  
19 Reserves Auditor for Shell, and it refers to the  
20 "SEC Proved Reserves Audit, PDO (Oman) 25-28  
21 October 2003."

22 Q The dates that are shown on the document

23 itself, October 25th through 28th of 2003; do you  
24 recall if that was when Mr. Barendregt was present  
25 at PDO in Oman?

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1 JOHN MALCOLM, October 20, 2006

2 A I remember Mr. Barendregt being present  
3 in Oman. Whether or not it was between those  
4 dates, I cannot remember, but I remember him being  
5 present in Oman in October of 2003.

6 Q I believe you indicated previously that  
7 you met with Mr. Barendregt at some point during  
8 his audit of PDO; is that correct?

9 A Yes.

10 Q Okay. Do you recall approximately how  
11 many times you met with Mr. Barendregt during the  
12 course of that audit?

13 A I think that I listened to the close-out  
14 presentation, and I think I met with him once.

15 Q Could you describe for me, please, what  
16 you mean by "close-out presentation."

17 A The -- effectively when an audit is  
18 given or a review is given, it is normally what we  
19 call a close-out presentation, which is  
20 effectively a summary of findings.

21 Q Was that presentation given by  
22 Mr. Barendregt?

23 A I assume it was, but again it is vague  
24 in my mind.

25 Q Do you recall if Mr. Barendregt was

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1 JOHN MALCOLM, October 20, 2006

2 accompanied by anybody during the course of the  
3 audit?

4 MR. SMITH: Objection to form.

5 BY MR. MACFALL:

6 Q I'll rephrase the question. Did anyone  
7 accompany Mr. Barendregt -- withdrawn. Excluding  
8 PDO personnel, are you aware of anyone who  
9 assisted Mr. Barendregt in the conduct of the  
10 audit?

11 A I cannot remember anyone excluding PDO  
12 personnel. I may be wrong, sir, but I cannot  
13 remember.



14 Q Excluding the close-out presentation --

15 A And that, even that is vague in my mind  
16 as to whether or not I attended, because I  
17 remember, when I flipped through this, seeing some  
18 drafts and the like, but I think I was at the  
19 close-out presentation, but I remember one other  
20 meeting with him.

21 Q With regard to the other meeting with  
22 Mr. Barendregt, do you recall approximately how  
23 long that meeting lasted, sir?

24 A It was a, it was a -- again after three  
25 plus years, it was a, it was a, it was a

0150

1 JOHN MALCOLM, October 20, 2006  
2 relatively short meeting. It was 30 minutes type  
3 meeting, of that order.

4 Q Do you recall if anyone else was present  
5 during that time?

6 A I think Stuart Clayton was present  
7 during that time. Again I -- that is just  
8 recollection. I need to go and check notes or my  
9 diary or whatever to check that again, but that's  
10 my recollection.

11 Q Just going off topic for a second, sir,  
12 did you typically keep notes of your various  
13 meetings at PDO?

14 A Not, not as rigorously as I should keep  
15 such notes, no.

16 Q Did you keep some notes in connection  
17 with meetings that you conducted at PDO?

18 A Yes, of course.

19 Q Were those notes made part of any PDO or  
20 Shell files, to the best of your knowledge?

21 A Not to the best of my knowledge.

22 Q With regard to -- withdrawn. Did you  
23 keep a diary in connection with the various  
24 meetings that you had at PDO during 2002, 2004?

25 A I basically run an electronic diary

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1 JOHN MALCOLM, October 20, 2006  
2 using Microsoft Outlook, so I don't have a diary  
3 as you would traditionally understand it, sir, but  
4 if you looked at my agenda during the day, you

5 would see a very large number of meetings in it.

6 Q Did you print out paper copies of the  
7 Outlook diary that you kept?

8 A The only ones we normally -- my  
9 secretary prints out at the beginning of the week  
10 the Outlook diary for that week and then has to  
11 change it frequently during the week as I --

12 Q With regard to the paper print-out that  
13 your secretary does at the beginning of the week,  
14 do you know if that print-out is made part of any  
15 Shell or PDO files?

16 A No.

17 Q No, you don't know, or no, it's not?

18 A No, I know it's not, because we, we  
19 maintain the diary.

20 Q I'm sorry. I'm not sure I understood.  
21 You said you know that it's not because you do or  
22 don't maintain a diary?

23 A We maintain an electronic diary.

24 Q I see. Thank you.

25 A So we have no need to maintain paper

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1 JOHN MALCOLM, October 20, 2006  
2 copies, many of which would not reflect the actual  
3 diary.

4 Q Do you recall if you produced copies of  
5 the notes which you took of various meetings at  
6 PDO during 2002/2004 to Shell in connection with  
7 this litigation?

8 A No.

9 Q No, you don't recall or no, you did not  
10 produce it?

11 A No, I know that I gave permission to  
12 Shell to take everything that I had electronically  
13 on my system, on my e-mail system, and that is  
14 the -- although I take other notes, they are  
15 generally not as structured as the notes of  
16 meeting that end up electronically, either minutes  
17 of meeting or whatever.

18 Q Do you retain copies of the notes of the  
19 meetings that you take by hand?

20 A Not consistently.

21 Q Do you have any copies of notes that you

22 took by hand at any of the various meetings you  
23 attended at PDO?

24 A Yes, I'm sure I have some.

25 MR. MACFALL: Plaintiffs respectfully  
0153

1 JOHN MALCOLM, October 20, 2006  
2 request, to the extent that they have not been  
3 produced, that copies of such notes for the  
4 relevant time period be produced.

5 MR. SMITH: I will take your request  
6 under advisement, but I will note for the record  
7 that PDO is a separate entity, is not under  
8 Shell's control, and it is not a party to this  
9 action, nor is Mr. Malcolm a party to this action,  
10 but as I say, we will take your request under  
11 advisement.

12 MR. MACFALL: I appreciate that. And if  
13 necessary, that material can be subpoenaed. Well,  
14 maybe not.

15 MR. SMITH: Good luck.

16 THE WITNESS: I have to advise you, sir,  
17 that on all of my written notes I have, I have  
18 written "Confidential To Counsel" on all of them.

19 MR. SMITH: He's not asking you about  
20 notes connected with your meetings with us in  
21 connection with your representation here.

22 MR. MACFALL: No, not at all.

23 THE WITNESS: Okay.

24 BY MR. MACFALL:

25 Q We wandered somewhat far afield, and I  
0154

1 JOHN MALCOLM, October 20, 2006  
2 apologize for that. Getting back to the meeting  
3 you had with Mr. Barendregt, do you recall if the  
4 topic of proved reserves was discussed during that  
5 meeting?

6 A The topic of -- the topic of the audit  
7 was proved reserves.

8 Q I take it then that your answer is yes,  
9 it was discussed?

10 A Yes.

11 MR. SMITH: Objection to form.

12 BY MR. MACFALL:

13 Q Could you please describe for me  
14 generally what was discussed with regard to proved  
15 reserves during that meeting between yourself and  
16 Mr. Barendregt.

17 MR. SMITH: Objection to form and  
18 foundation.

19 THE WITNESS: The -- as I remember, and  
20 again it's a significant time ago, the key issue  
21 that was raised was my understanding of the  
22 likelihood of the Concession extension. That was  
23 fundamentally what he wanted to know, and I  
24 advised him where we stood as I understood it.  
25 And from my recollection, I also advised my  
0155

1 JOHN MALCOLM, October 20, 2006  
2 concern that we should not assume, make  
3 assumptions of Concession extension that would  
4 show that we took for granted what was actually in  
5 the right of the Oman Government, not within  
6 Shell's right.

7 BY MR. MACFALL:

8 Q Do you recall if you and Mr. Barendregt  
9 discussed what significance, if any, the  
10 Concession extension had in connection with proved  
11 reserves?

12 A Apart from the obvious, that PDO's  
13 proved reserves beyond 2012 would or would not be  
14 included, so . . .

15 Q Do you recall if you indicated to  
16 Mr. Barendregt whether or not it was likely that  
17 the Concession extension would be granted?

18 MR. SMITH: Objection to form.

19 THE WITNESS: I was advised -- I was  
20 asked what my opinion was, and my opinion was that  
21 I believe that the Concession extension  
22 discussions were continuing as they were at that  
23 moment in time, which you have seen from Sir  
24 Philip Watts' memo that you put before me earlier  
25 on, and in hindsight we can see that roundabout  
0156

1 JOHN MALCOLM, October 20, 2006  
2 February 2004 there was a Memorandum of  
3 Understanding signed.

4 BY MR. MACFALL:

5 Q Did you indicate to Mr. Barendregt,  
6 however, that it was likely that a Concession  
7 extension would be granted?

8 MR. SMITH: Objection to form.

9 THE WITNESS: I, I, I don't recognize  
10 your question in that form. I -- my understanding  
11 and my memory of that meeting was one more of the,  
12 you know, how were these -- were discussions  
13 ongoing in principle, was there likely to be a  
14 Concession extension, I said yes, but my major  
15 concern was that it should not be seen as being  
16 taken for granted, because that was not -- that  
17 would not be good for relationships with the  
18 Government.

19 BY MR. MACFALL:

20 Q Okay. With the caveat that you had  
21 informed Mr. Barendregt that it should not be  
22 taken for granted, am I correct that you did  
23 inform him, with that caveat, that it was likely  
24 that the Concession extension would be granted?

25 A He asked for my opinion, and I gave him  
0157

1 JOHN MALCOLM, October 20, 2006  
2 my opinion about what was happening on the  
3 likelihood, from the meetings I had been at, and  
4 when you read his report afterwards, you know, he,  
5 as I understood it, took a very balanced  
6 viewpoint, was this really has to happen in a very  
7 short period of time, in like two months, or it's  
8 not relevant. And it didn't happen within that  
9 short period of time and therefore it was not  
10 relevant. I think that's really what he wanted to  
11 try and to find out, was it was going to happen  
12 tomorrow or the next day or whatever before the  
13 U.N., but it didn't happen --

14 THE REPORTER: You need to slow down.  
15 Trying to find out whether it was going to  
16 happen --

17 THE WITNESS: Tomorrow or the next day.  
18 Again, sir, you know, this is three and a bit  
19 years ago. I have many, many meetings.

20 BY MR. MACFALL:

21 Q I do appreciate that, Mr. Malcolm, and I  
22 also appreciate your patience, sir.

23 In addition -- excuse me. Withdrawn.

24 Excluding the topic of the Concession extension,  
25 do you recall any other topics being discussed  
0158

1 JOHN MALCOLM, October 20, 2006  
2 with regard to proved reserves during that meeting  
3 with Mr. Barendregt?

4 MR. SMITH: Objection to form.

5 THE WITNESS: I don't fully recall all  
6 the items. I recall the concern about the, the  
7 likelihood that the Shell methodology that had  
8 been used up to that point was likely to restate,  
9 as is stated here. I think this is very clear.

10 BY MR. MACFALL:

11 Q Do you recall if you discussed with  
12 Mr. Barendregt the interim findings of the STOIIP  
13 and Reserves Review with regard specifically to  
14 the match-up between reserves and particular  
15 projects?

16 A I do not remember, but I'm sure he was  
17 advised of it by our staff, because that interim  
18 had been about a month earlier, and I think he  
19 refers to it in his report here.

20 Q Do you recall if you discussed with  
21 Mr. Barendregt the quantity of proved reserves as  
22 PDO that were exposed?

23 MR. SMITH: Objection to form.

24 THE WITNESS: I, I don't remember the,  
25 the discussion, plus the fact again, sir, this  
0159

1 JOHN MALCOLM, October 20, 2006  
2 was a, this was a Shell issue rather than a PDO  
3 issue, and again, you know, from your previous  
4 document, as far as PDO's proved reserves, which  
5 were also inaccurate, but it would appear they  
6 were inaccurate very conservatively.

7 BY MR. MACFALL:

8 Q Subsequent to Mr. Barendregt's audit,  
9 did you have any discussions with Mr. van der  
10 Vijver concerning PDO's proved reserves?

11 MR. SMITH: When you say "subsequent" to



12 his audit, do you mean the time he visited Oman or  
13 the date of Exhibit 4?

14 BY MR. MACFALL:

15 Q Subsequent to the time he visited Oman.

16 A Subsequent to Anton Barendregt's visit?

17 Q Yes. I'm sorry. To Mr. Barendregt's  
18 visit.

19 A Again, the dates are confusing, but I do  
20 not believe on proved reserves -- again I, I need  
21 to look back, but I, I don't know at this moment  
22 in time, but if he came in in that last quarter,  
23 we would definitely have put out the status on all  
24 reserves, on proved and expectation, because the  
25 reserves, the STOIP and Reserves Review which had  
0160

1 JOHN MALCOLM, October 20, 2006  
2 been primarily expectation, we had kind of closed  
3 out in September substantially, and then this  
4 thing came along in October or around about just  
5 shortly thereafter.

6 Q Without limiting it to the time period  
7 after Mr. Barendregt's visit --

8 A I cannot remember, sir.

9 Q Thank you.

10 Do you recall if the issue of -- or any  
11 issue concerning PDO's proved reserves was raised  
12 with you by any individual at Shell prior to  
13 Mr. Barendregt's visit?

14 MR. SMITH: Objection to form. He  
15 already said PDO doesn't have proved reserves.

16 MR. MACFALL: I'll rephrase the  
17 question.

18 BY MR. MACFALL:

19 Q Do you recall if, prior to  
20 Mr. Barendregt's audit, Shell's reporting of  
21 proved reserves at PDO was discussed with you by  
22 anyone from Shell?

23 A By anybody from Shell? No.

24 Q No, you don't recall or no, there were  
25 no such conversations?

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1 JOHN MALCOLM, October 20, 2006

2 A No, I don't recall. No, I don't recall.

3 I am -- and for clarification, in case -- I  
4 probably was briefed by our head of Corporate  
5 Planning before this came in, before the audit  
6 came in, but that is not from Shell. That would  
7 be simply the normal management. Either myself or  
8 the DMD would have been briefed.

9 Q Mr. Malcolm, I'd like to direct your  
10 attention to the bottom of the first page of the  
11 document, referring to Mr. Barendregt's Audit  
12 Report. The third line from the bottom, you see  
13 the word "unsatisfactory"? Do you see that, sir?

14 A Yes, I see it.

15 Q Okay. The sentence reads, "The overall  
16 opinion on the state of PDO's 1/1/2003 Proved  
17 Reserves submission, taking account of the audit's  
18 findings (see Attachment 3) is unsatisfactory."  
19 Do you recall if Mr. Barendregt indicated to you,  
20 prior to the issuance of this report, that PDO  
21 would be receiving an unsatisfactory rating with  
22 regard to its proved reserves submission?

23 MR. SMITH: Objection to form.

24 THE WITNESS: If there was, as I think  
25 there was, a close-out presentation, then we would

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1 JOHN MALCOLM, October 20, 2006  
2 have had that it was going to be unsatisfactory,  
3 and we would not have been surprised by waiting  
4 for the report. There would have been an  
5 indication. Whether it was Mr. Barendregt told me  
6 or whether it was one of my staff told me, I can't  
7 remember, but it was not a surprise.

8 BY MR. MACFALL:

9 Q Were you personally concerned by the  
10 unsatisfactory rating given by Mr. Barendregt in  
11 connection with PDO reserves submission?

12 A I am concerned, of course, with all  
13 unsatisfactory audits within PDO, but in this  
14 particular case this was about a service we were  
15 doing for others, according to their guidelines.  
16 At the time I was very, very much more concerned  
17 about the thought that 20 percent of my  
18 expectation reserves had been agreed by an  
19 external review to have been lacking substance and

20 backing, and that -- and the implications for my  
21 company on that were very, very, very clear going  
22 forward. The proved reserves number is not a  
23 number that we run the company on.

24 Q Could you describe for me what the  
25 implications of a possible de-booking concerning

0163

1 JOHN MALCOLM, October 20, 2006  
2 the expectation reserves at PDO was or were.

3 MR. SMITH: Objection to form.

4 MR. MACFALL: Let me rephrase the  
5 question.

6 BY MR. MACFALL:

7 Q I believe you indicated that there were  
8 certain implications as a result of the STOIP and  
9 Reserves Review finding. What were those  
10 implications?

11 A I think the -- there was even greater  
12 support and substance for a drive to put in place  
13 up-to-date Field Development Plans in order that  
14 we could clearly make sound bookings, whether up  
15 or down, in our ARPR, and that was an ongoing  
16 process and had been from the early part of 2003,  
17 was the drive to get these new Field Development  
18 Plans in place. And where you have this -- your  
19 expectation reserves are under threat by  
20 20 percent, of course, gave even greater impetus  
21 to really understanding the development of these  
22 fields, because expectation reserves and  
23 expectation production over a longer period of  
24 time are tied closely together.

25

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1 JOHN MALCOLM, October 20, 2006

2 (Exhibit No. 5 was marked for  
3 identification and attached to the deposition  
4 transcript.)

5 BY MR. MACFALL:

6 Q Mr. Malcolm, you've just been handed a  
7 document marked for identification as Malcolm  
8 Exhibit 5 for identification. I'd like for you to  
9 take a look at that, sir, and ask you if you  
10 recognize it.

11 Do you recall if you've ever seen this

12 document before, sir?

13 A No, I do not recall seeing this document  
14 before.

15 Q For the record, the document is an  
16 e-mail string, the most recent e-mail of which is  
17 from Frank Coopman, dated November 6, 2003,  
18 addressed to Anton Barendregt, re "Draft Reserves  
19 Audit Report (PDO)." Within that e-mail there is  
20 attached -- or at least part of that e-mail  
21 string -- I'm sorry -- is an e-mail from  
22 Mr. Barendregt to Mr. Coopman dated November 6,  
23 2003. It also appears on the first page.

24 Mr. Malcolm, it's to that e-mail I'd  
25 like to direct your attention, specifically after

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1 JOHN MALCOLM, October 20, 2006  
2 the "Frank," and then there is one sentence there,  
3 a more fulsome paragraph, the first sentence of  
4 which reads, "The reason why I'm lenient in this  
5 case is because I have had the personal assurance  
6 from many people in PDO, including the MD, that a  
7 deal about the license extension is around the  
8 corner and that a HOA is likely to be signed  
9 before the end of 2003."

10 My question, sir: The reference to  
11 "MD"; is that a reference to you as the Managing  
12 Director of PDO?

13 MR. SMITH: Objection to form and  
14 foundation.

15 THE WITNESS: I can only assume that it  
16 refers to me, but it could refer to others, but if  
17 we read this sentence carefully and if the  
18 sentence as written is correct, "from many people  
19 in PDO, including MD," then it is me.

20 BY MR. MACFALL:

21 Q Based on your earlier testimony, am I  
22 correct that you did not indicate to  
23 Mr. Barendregt that a license extension is "around  
24 the corner"?

25 MR. SMITH: Objection to form and

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1 JOHN MALCOLM, October 20, 2006

2 foundation.

3 MR. MACFALL: I'll withdraw that and  
4 rephrase it.

5 BY MR. MACFALL:

6 Q You testified a few minutes ago --

7 A Yes.

8 Q -- about a conversation that you had  
9 with Mr. Barendregt concerning the likelihood of a  
10 Concession extension.

11 A (Nods.)

12 Q My recollection -- and we can go back  
13 and check -- is that you did not indicate to  
14 Mr. Barendregt that a Concession extension was --  
15 withdrawn. Let me ask you: Did you indicate to  
16 Mr. Barendregt at any point that the Concession  
17 extension was imminent as opposed to likely?

18 MR. SMITH: Objection to form.

19 THE WITNESS: My recollection is that I  
20 was asked about this, you know, and my opinion was  
21 that, you know, it was ongoing and an MOU would be  
22 signed at some point. I cannot remember saying it  
23 would be signed before the end of 2003. And my  
24 major concern at the time was that people should  
25 not write anything in external reports that would

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1 JOHN MALCOLM, October 20, 2006  
2 be taken for granted that we would get such an  
3 extension, and so it is a very -- I was asked for  
4 my opinion, did I believe an MOU was going to be  
5 signed. I gave my opinion based on the meetings.  
6 You have seen several of Watts' minutes and  
7 everything else, but I cannot remember implying,  
8 and I don't think this sentence actually says it,  
9 that John Malcolm said it was going to be before  
10 the end of 2003. It's written in a very nebulous  
11 manner here. I think that what was discussed was  
12 did I believe we were going to get one signed.  
13 Yes. When it was going to be? It was sometime  
14 soon. In actual fact, in hindsight it came out in  
15 February 2004.

16 BY MR. MACFALL:

17 Q Thank you, Mr. Malcolm. I think we're  
18 trying to get to the same place on that

19 ultimately. Thank you.

20 Directing your attention to the third --

21 I guess it's actually the fourth full paragraph if  
22 you'll include the one-sentence paragraph at the  
23 top, that begins with the sentence, "I could  
24 insist on de-booking." Do you see that, sir?

25 A Yes.

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1 JOHN MALCOLM, October 20, 2006

2 Q And it continues, "400 million barrels  
3 now," and goes on. The 400 million barrels  
4 reference, do you recall -- withdrawn. That  
5 reference is not to expectation reserves to the  
6 best of your knowledge, is it?

7 MR. SMITH: Objection to form and  
8 foundation.

9 BY MR. MACFALL:

10 Q Withdrawn. Do you have an understanding  
11 as to what Mr. Barendregt is referring to there?

12 MR. SMITH: Objection to form and  
13 foundation.

14 BY MR. MACFALL:

15 Q You can answer.

16 A The only assumption I can make of the  
17 Reserves Auditor who does the audit -- as we saw  
18 from your earlier minutes of the audit, this was  
19 the SEC Proved Reserves Audit, so one has to  
20 believe that this number refers to proved  
21 reserves, and the number, as all the other numbers  
22 I've given you in expectation reserves, this  
23 number does not tie in, so we have to believe that  
24 this is the reserves number that he believed was  
25 at risk as a reserves auditor.

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1 JOHN MALCOLM, October 20, 2006

2 Q Was Mr. Barendregt at that time in a  
3 position to insist that PDO de-book any reserves?

4 MR. SMITH: Objection to form and  
5 foundation. These are not PDO's reserves.

6 MR. MACFALL: I never said they were.

7 BY MR. MACFALL:

8 Q My question was: Was Mr. Barendregt, in  
9 his position as auditor at Shell, in a position to



10 insist or positioned to cause de-booking of any of

11 PDO's reserves, at PDO?

12 A To restate, this was a Proved Reserves  
13 Audit. PDO ran its business on the basis of  
14 expectation reserves. We, PDO's management, had  
15 seen at risk 700 plus million barrels of reserves  
16 in May 2003. This has subsequently been reviewed  
17 and also matured over that period of time, that by  
18 September 2003 we believed that we had some  
19 936 million at risk. There were discussions going  
20 on with the PDO management and PDO shareholders  
21 how to best handle this expectation de-booking.  
22 That is an issue for PDO and its shareholders.  
23 This, sir, is not an issue for me. This is an  
24 issue for Shell, this auditor and its  
25 shareholders.

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1 JOHN MALCOLM, October 20, 2006

2 Q That's fine. Thank you, Mr. Malcolm.

3 Mr. Malcolm, did PDO ultimately --  
4 withdrawn. Did there come a time when PDO  
5 de-booked expectation reserves?

6 A Yes, sir. I, I would need to check the  
7 actual data. Again these things happened several  
8 layers below me, but our policy is to book and  
9 de-book reserves on the basis of FDPs, and as we  
10 bring the FDPs in one after another, we take the  
11 matched reserves on or off the books, depending on  
12 how they come in. My understanding is that in our  
13 ARPR -- but that needs to be checked -- we have  
14 clearly that we have this vulnerability to these  
15 matched reserves, but our policy is to take them  
16 off the books as we get the FDPs or, in some  
17 cases, actually to add reserves. And today we  
18 have, we have a pretty structured process that has  
19 the support of all the shareholders.

20 Q Are you aware if Shell ultimately  
21 de-booked or recategorized -- withdrawn. Let me  
22 try again. Are you aware if Shell recategorized  
23 any volume of proved reserves reported to it by  
24 PDO?

25 MR. SMITH: Objection to form.

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1 JOHN MALCOLM, October 20, 2006

2 THE WITNESS: Sir, I am aware of the  
3 presentations that were made by Shell in 2004, and  
4 in one of those presentations, sir, there was a  
5 reference made to PDO. And again, sir, again I  
6 can only surmise that when you have over  
7 200,000 barrels a day of equity production, I  
8 would suspect that this would be the case, based  
9 on the documents you put in front of me.

10 BY MR. MACFALL:

11 Q Did you have any meetings with  
12 representatives of the Omani Government subsequent  
13 to February 2004?

14 A I did, sir.

15 Q Do you recall if during the course of  
16 any of those meetings the recategorization of  
17 Shell's proved reserves was discussed?

18 A I did, sir.

19 Q Who were those meetings with, sir?

20 A Again I'd like for the record to say  
21 that the meeting I'm going to describe is a highly  
22 confidential meeting and should not be reported  
23 outside, as possible.

24 MR. SMITH: Again we would invoke the  
25 highly confidential provisions of the Protective

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1 JOHN MALCOLM, October 20, 2006

2 Order in this case --

3 MR. MACFALL: We would abide with --

4 MR. SMITH: -- in connection with his  
5 response.

6 MR. MACFALL: Obviously we would abide  
7 by the terms and will abide by the terms.

8 MR. SMITH: Thank you.

9 THE WITNESS: I cannot remember the  
10 exact date, but sometime in the Second Quarter of  
11 2004, the Finance and Energy Council requested  
12 that I come and give them a presentation on  
13 reserves in PDO. The Finance and Energy Council  
14 is probably the most powerful council in Oman. It  
15 is headed up -- it has at least the Minister of  
16 National Economy, the Minister of Commerce and  
17 Industry, the Minister of Oil and Gas. It has

18 basically something like about six people of that  
19 type of rank. Very, very powerful committee.

20 When they asked if I would come and give  
21 them a presentation on expectation reserves and  
22 proved reserves, I suggested to them that they  
23 would be better to ask the Shell representative  
24 office to present Shell's proved reserves numbers  
25 to them, and they declined my suggestion and said  
0173

1 JOHN MALCOLM, October 20, 2006  
2 that they would far rather that I presented my  
3 understanding of both sets of numbers to them.

4 BY MR. MACFALL:

5 Q Did you consult with anyone at Shell in  
6 preparation for that presentation?

7 A Yes. I cannot remember all the people,  
8 but I definitely discussed with Andy Wood, who is  
9 now the Shell Representative Office Oman Country  
10 Chairman of Shell, to explain to him that a lot of  
11 this was outside my agreement. This is what the  
12 Government had requested, so I did so. And from  
13 Shell's side, you know, whoever the Government  
14 wanted to make this presentation to them, that was  
15 fine.

16 Q Did the presentation include information  
17 concerning the recategorization of only proved  
18 reserves at PDO or within all of Shell?

19 A It was only concerned with PDO.

20 Q Do you recall as part of that  
21 presentation you indicated to the representatives  
22 from the Omani Government the quantity of proved  
23 reserves recategorized by Shell in connection with  
24 PDO?

25 A Yes, I did, and I don't actually  
0174

1 JOHN MALCOLM, October 20, 2006  
2 remember the number, but I remember the percentage  
3 well. It was 40 percent, because it was a real  
4 concern for the Government.

5 Q How is it that the Government expressed  
6 that concern to you if you recall?

7 A His Majesty's Ministers are very capable  
8 and smart men. If we go back to where we came in

9 when you were asking me about P50, P85, et cetera,  
10 in hindsight I realize what concerned them greatly  
11 was that they understood that expectation reserves  
12 could go up and down and that proved reserves  
13 could go up but generally not too often down.  
14 They were more solid.

15 And I think there was a tremendous  
16 concern in Oman that their Managing Director --  
17 and I am their Managing Director. I know you see  
18 me today as otherwise, but I am also their  
19 Managing Director. That their Managing Director  
20 was saying that the expectation reserves of PDO  
21 were likely to be down by 20 percent, and external  
22 sources were saying that the proved reserves of  
23 PDO, as reported by Shell, were down by  
24 40 percent, and they were naturally extremely  
25 concerned by this, because one would expect that

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1 JOHN MALCOLM, October 20, 2006  
2 the proved reserves percentage would be lower than  
3 the expectation reserves percentage. So the  
4 numbers did not match up.

5 This, by the way, I surmise, a very long  
6 meeting. I explained to them how the license  
7 cutoff worked, how the previous calculation of  
8 Shell had worked versus the SEC calculation, et  
9 cetera, and I believe at the end of that meeting  
10 they understood why 20 percent and 40 percent  
11 added up. And there was I believe concerns and  
12 there are still concerns about reserve, but I  
13 believe the incongruous nature of those two  
14 numbers was put to rest, and I then understood why  
15 they wanted me to present numbers to them.

16 Q Do you recall approximately how long  
17 that presentation lasted?

18 A It would have lasted at least an hour,  
19 maybe an hour and a half. In some cases, of  
20 course, you're dealing with very capable people,  
21 and you are putting in some very technical terms,  
22 so there was a number of clarifications on what  
23 these technical terms meant and a number of other  
24 things, but they had -- in my opinion, they had  
25 the right to call in their Managing Director to

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1 JOHN MALCOLM, October 20, 2006  
2 explain two numbers that they could not balance in  
3 their mind, that these two numbers held together,  
4 one that was reported in press and one that was --  
5 they had reported by PDO's in expectation.

6 Q Do you recall approximately when that  
7 meeting occurred?

8 A I can only guess it was around about the  
9 Second Quarter sometime. It was after all the  
10 announcements, after all the fall-out.

11 Q After Second Quarter '02?

12 A Yes.

13 MR. MACFALL: Can we take a short break.

14 MR. SMITH: Sure.

15 THE VIDEOGRAPHER: We are going off the  
16 record. The time is 3:22 p.m.

17 (Whereupon, a short recess was taken.)

18 THE VIDEOGRAPHER: We are back on the  
19 record. The time is 3:32 p.m.

20 MR. MACFALL: Mr. Malcolm, I'd like to  
21 thank you very much for your time and candor, sir.  
22 At this point I have no further questions.

23 MR. SMITH: Thank you. We have nothing.

24 THE VIDEOGRAPHER: This marks the end of  
25 the deposition of Mr. Malcolm. The total number

0177

1 JOHN MALCOLM, October 20, 2006  
2 of tapes used today was three. We are going off  
3 the record. The time is 3:32 p.m.

4 (Signature having not been waived, the  
5 videotaped deposition of JOHN MALCOLM was  
6 concluded at 3:32 p.m.)

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0178

1 JOHN MALCOLM, October 20, 2006

2  
3 ACKNOWLEDGEMENT OF WITNESS

4  
5 I, JOHN MALCOLM, do hereby acknowledge  
6 that I have read and examined the foregoing  
7 testimony, and the same is a true, correct and  
8 complete transcription of the testimony given by  
9 me, and any corrections appear on the attached  
10 Errata sheet signed by me.

11  
12  
13

14 (DATE) (SIGNATURE)

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0179

1 JOHN MALCOLM, October 20, 2006

2 E R R A T A S H E E T

3 IN RE: ROYAL DUTCH/SHELL SECURITIES LITIGATION

4 RETURN BY:

5 PAGE LINE CORRECTION AND REASON

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25 (DATE) (SIGNATURE)

0180  
1 JOHN MALCOLM, October 20, 2006  
2 E R R A T A S H E E T  
3 IN RE: ROYAL DUTCH/SHELL SECURITIES LITIGATION  
4 RETURN BY:

5 PAGE LINE CORRECTION AND REASON

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25 (DATE) (SIGNATURE)

0181

1 JOHN MALCOLM, October 20, 2006

2

3 CERTIFICATE OF SHORTHAND REPORTER -- NOTARY PUBLIC

4 I, Laurie Bangart-Smith, Registered

Professional Reporter, the officer before whom the

5 foregoing deposition was taken, do hereby certify

that the foregoing transcript is a true and

6 correct record of the testimony given; that said

testimony was taken by me stenographically and

7 thereafter reduced to typewriting under my

supervision; and that I am neither counsel for,

8 related to, nor employed by any of the parties to

this case and have no interest, financial or

9 otherwise, in its outcome.

10 IN WITNESS WHEREOF, I have hereunto set

my hand and affixed my notarial seal this 23rd

11 day of October, 2006.

12

13

14 My commission expires: March 14th, 2011

15

16

17 \_\_\_\_\_

18 LAURIE BANGART-SMITH

NOTARY PUBLIC IN AND FOR

19 THE DISTRICT OF COLUMBIA

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copy megal, man?

**Sultanate of Oman**  
**Ministry of Oil & Gas**  
**Muscat**



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 وَزَارَةُ النِّفْطِ وَالْخِزَانَةِ  
 مسقط

Copy Croiber/Megal/Man

URGENT

It is a pity that he wrote this letter.

Please recommend the appropriate response (written/oral).

Thanking, Walter

No : 4/14/2397/2001  
 Date : 09-10-2001

Mr. Walter van de Vijver  
 Group Managing Director  
 Royal Dutch / Shell Group of Companies  
 CEO Exploration & Production.

After Compliments,

Thank you very much for your letter of 1<sup>st</sup> October 2001. On behalf of the government I thank you for the attention given to our problem of production as was discussed during our meetings.

There were a number of issues that were mentioned that many of us believe are responsible to the sudden and unexpected decline in PDO black oil production. I think it is appropriate to record some of our concern while allowing PDO management to come up with a comprehensive "recovery plan". Many of us strongly believe that the following factors are either responsible or contributed to the production "crisis". These include, but not limited, to the following factors: -

- 1) The Asset management Style.
- 2) Reserve booking methodology
- 3) Score Card
- 4) Contracts and Contracting Management.
- 5) Human Resource Management.

Some of the above factors are some-what inter-connected, for example reserve booking vs. scorecard.

Reference to your letter, therefore, I am concerned that you are still putting a lot of emphasis on reserve booking and score card; the very factors that many of us blame for the current crisis.

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**EXHIBIT**

tabbies

Malcolm I

*Sultanate of Oman*  
*Ministry of Oil & Gas*  
*Muscat*



سُلْطَانَةُ عُومَانِ  
 وَزَارَةُ النِّفْطِ وَالْجَوَارِ  
 مَسْقُوط

If the emphasis of 815 kbpd is a realistic production (in PDO's view) then the government agree. However if the focus is on the score card; then we would like to revisit the whole issue of scorecard. Similarly on reserve booking. While we appreciate and thank you for making a pre-payment of 30 M\$ against future de-booking of reserve, MOG will scrutinize strictly the 2001 reserve bookings (old oil) that do not contain a comprehensive development and exploitation programs.

I will therefore like to discuss further these two issues in order to avoid any negative impact/influence they may have towards our goal for recovery. I will further discuss our thoughts with Steve and John Crocker.

Once again we thank you for visiting us in Oman and hope to see you here soon.

Best regards,

*M. Rumhy*



Dr. Mohammed bin Hamad Al Rumhy  
 Minister of Oil and Gas.

CC: H.E. Ahmed A. Macki  
 Minister of National Economy & Deputy Chairman  
 Of Financial Affairs & Energy Resources Council.

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**Unknown**

**From:** Watts, Philip B SI-MGDPW  
**Sent:** 13 January 2003 16:54  
**To:** Van der Veer, Jeroen J SI-MGDJV; Brinded, Malcolm A SI-MGDMB; Skinner, Paul PD SI-MGDPS; Van De Vijver, Walter SI-MGDWV  
**Subject:** Oman visit - 9-12 January 2003

I have just returned from Oman and send this visit report with a number of attachments (one of which should not have wide circulation). The matters arising need urgent action, as suggested in this note.

I look forward to discussing it at CMD tomorrow.



Oman visit 9-12  
January 2003.d...



Oman visit -  
attachment 2.doc



Attachment 3 - Gas  
Draft Guide...

password for attachment 2+3: leicesterPW

Phil

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Incoming mail is certified Virus Free.  
Checked by AVG anti-virus system (<http://www.grisoft.com>).  
Version: 6.0.567 / Virus Database: 358 - Release Date: 24/01/2004

**EXHIBIT**

tabbles

*Malcolm 2*

VIJVER 1450

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## Oman visit – 10-12 January 2003

### Preamble

- I went to Salalah last September when it became clear that a very concerning situation had arisen in Government relations regarding PDO oil production.
- This came in the wake of the fractious time of the renegotiations of the GISCO deal.
- My apology to HM was received graciously and I undertook to go back to see him to discuss PDO.
- At that time HM adjudicated on the "Government Train" and declared that Shell would have "12%".
- He also encouraged the Minister to get on with the Concession negotiations in a positive manner.

### The key meetings

After reading a comprehensive briefing document I had an extensive session with John Crocker, John Malcolm, Agnus Cassens and Peter Cryer before going to see HM. My (restricted) account of the one-to-one meeting is attached. This was followed by the full session with HM, described by John Crocker in the next attachment.

In short,

1. PDO gets the breathing space to demonstrate delivery which will take 18-24 months before the turnaround can be measured in barrels (as opposed to words today).
2. I gave the Shell commitment to help the third/Government train be successful ... but giving proper advice, initially with Ministers Macki & Rumhy the following day.
3. HM made a resounding declaration that the Concession negotiations should start in March this year and end at the latest by March 2004.

The following morning I went to see Ministers Macki and Rumhy together with John Crocker and John Malcolm. The 2 hour meeting is described in the attachment. It was rather frank, at times difficult but, if all parties do as agreed, could be highly productive. The bottom line was that we would draft and send to them for comment the ground rules for finalization of the arrangements for the Government Train. A draft of these is attached. The key points agreed in the meeting and now recorded are:

1. Shell's commitment to help GT to happen quickly.
2. The Minister's commitment to share all data
3. My "four points"
  - (i) A bankable SPA
  - (ii) A good EPC
  - (iii) Comfort (and ultimately approval) from the existing leaders/buyers of Trains 1 and 2.
  - (iv) The pivotal, primary role of OLNG

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4. Resolution of other outstanding issue
  - (i) the IPP
  - (ii) the LNG shipping

#### The Outlook

- So we face the final negotiations for Train 3 over the next weeks and the renegotiation of the Concession agreement (and reserves booking fee) against the backdrop of a long hard road to turn round PDO oil production.

#### Suggested Actions

##### (i) The Oil

- PDO is getting tremendous support and this will be further personified by the visits of Messrs. Megat/Darley at end January and the visit by MGDWV in March.
- March is a critical watershed for progress of the key waterflood and EOR projects.
- Perish the thought that PDO doesn't deliver (but, of course, this needs the co-operation and timely support of numerous Ministries ... a point I made and will reinforce in my subsequent visits.

##### (ii) The "Government Train"

- This now needs the most urgent Shell action which in terms of the necessary formal Shell approvals for a "success case" will need
  - (i) authority for OLNG to take their share of the project at the mid-February board meeting of OLNG
  - (ii) consideration of authority for FID by CMD in February and Conference on 5 March.
- This will require dedicated effort by all concerned in order to gain some initiative rather than just fight a rearguard action before being "dragged kicking and screaming to the party".

##### (iii) The Concession

- We need to have an overview/initial mandate to negotiate paper to CMD in February
- Again, this will require dedicated resources which wisely uses John Crocker as the leading "general" rather than him spending too much time in the trenches.

In conclusion, all these matters are interconnected and we need to maintain a holistic Shell overview.

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I would like to pay tribute to the dedicated efforts of a lot of people who work in a difficult atmosphere, notably

- John Malcolm, who has made a very good first impression both internally and externally.
- Charles Watson and his people who have been pushed from pillar to post and lacked information on which to make decisions.
- Agnus Cassens who is in an unenviable position serving a board that is at cross purposes.
- Not least, John Crocker who as the Shell Representative is the lightning rod for all the tensions of the last year and can expect a lot more of the same to come.

I look forward to discussing this all at CMD tomorrow.

Phil Watts  
13 January 2003

Attachments 1,2,3

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Attachment 1

Meeting with HM

We had a pleasant one-to-one discussion for about 20 minutes at his request, covering the following areas:

Recollection of last meeting

- I reflected on our first meeting in Salalah last September, reminding him of my regret for the difficulties with the oil production.
- He graciously brushed this aside and wanted to hear of the progress.

The Oil

- I talked of the PDO plan agreed with the Ministry, my personal commitment to giving the necessary Shell support and the need to get on with its implementation, making it very clear that we were in for a tough 18-24 months before the turnaround could be expected. I stressed that it needed the cooperation of all concerned – PDO, Shell and all the Ministries, especially MOG.
- I mentioned that this was not an exercise in “more of the same” but a fundamental shift to water flood and EOR projects, supported by the ongoing oil and gas exploration programmes. I noted that the next few years was not only about oil production turnaround but also about implementing the new technologies necessary to assure the future of PDO for the next generation.
- He reminisced about the difficulties experienced by PDO in the mid-70's and was sure that the current difficulties would be overcome.

Concession

- I intentionally did not mention this matter but HM had an oblique reference to it when he recounted how a third party (the sons of Sheik Zaid) has put forward the idea that Occidental had some proposals. He had asked for them to be written down and sent to the Ministry so that they could be passed on to Shell.
- He said a few times that he was not pressing for their acceptance, just our consideration as to whether their ideas might be useful. (He noted that he had asked the third party how they would feel if they were the owners of the concession and were approached in this way!).

The Third Train

- By way of introduction of this item I asked for permission to mention a matter of serious concern. He had already in the previous item talked about a spirit of frankness and asked me to continue.
- I worried about the lack of alignment and trust in relation to the “Government Train Project”. Completely in sorrow rather than anger I wished that the third

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train would have been a simple expansion of OLNG but acknowledged that this was a matter of "sovereign right" and now that the decision had been taken – and that HM had adjudicated in the 12% interest for Shell – we would do all in our power to make the GTP a success.

- In the spirit of true partnership I said that we would honestly express our concerns at the meeting with Ministers Macki and Rumhy in the morning.
- I hoped that matters could be sorted out in weeks rather than months lest this issue undermine the necessary good co-operation to make progress in all our activities.
- HM responded very favourably to this.

#### Conclusion

- HM made some very pleasant concluding remarks and presented me with a historical memento – a pen with an oryx head on the cap, produced in the very early days of PDO.
- On the way out, I expressed admiration for the model of the recently completed Grand Mosque in Muscat and mentioned that I would be visiting it on the following day. He was delighted and proceeded to give me an extra 10 minute discourse on its design (in which he was intimately involved).

MGDPW  
13 January 2003

VIJVER 1455

**Khila, Hedaya ONPS**

---

**From:** Pay, John JR SIEP-EPS-P  
**Sent:** Monday, September 08, 2003 14:16  
**To:** Mann, Paul SEPI-EPM; Blascos, John SIEP-EPB-C  
**Cc:** Clayton, Stuart ONP; Kemshell, David UPR; Harthy, Said DTEM7  
**Subject:** PDO Reserves Meeting: Notes

Paul, John

Please find attached notes on my visit to PDO of 26 - 27 August 2003. They have been seen by those copied.



Notes of PDO  
Meeting Final.ZIP...

John Pay  
Group Hydrocarbon Resource Coordinator  
Shell International Exploration and Production B.V.  
Tarel van Bylandtlaan 30, Postbus 683, 2501 CR The Hague, The Netherlands

Tel: +31 (70) 377 7405 Other Tel: +31 (0)6 5252 1964  
Email: john.pay@shell.com  
Internet: <http://www.shell.com/eandp-en>

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### Notes on SIEP / PDO RESERVES MEETING, 26-27 August 2003

The SIEP Hydrocarbon Resource Co-ordinator (HRC) met with PDO staff to review the current status of PDO resource volumes in preparation for the forthcoming annual resource volume reporting exercise. This note summarizes the outcome of this meeting. The ongoing STOIP and Reserves Review, together with the SEC Reserves Audit scheduled for October 2003, will provide considerable further clarity on the distribution of hydrocarbon resources in the PDO portfolio and may result in the following being fine-tuned. In addition it should be noted that whilst the HRC in general supports the approach suggested by PDO (although please refer to comments below), this does not necessarily imply that the Shell Group Reserves Auditor will also concur.

#### 1. ARPR match with project data

Work to date indicates that some 715 million bbl (100% PDO share) of Expectation reserves may need to be debooked. This relates to reserves in the PDO / MOG (Ministry of Oil and Gas) ARPR for which no development project is currently identified. Also referred to as "match volumes", the reserves concerned are primarily associated with the Yibal, Marmul, Qarn Alam, Al Hurwaisal, Lekhwair, Saih Rawl and Saih Nihayda fields.

#### 2. Proposed approach to reserves categorization

Of the remaining Shell Reserves within licence, a revised sub-classification is proposed by PDO as follows:

Expectation Developed Reserves:	all projects in the "Operating" phase
Proved Developed Reserves:	set equal to Expectation Developed Reserves (see Note (i) below)
Expectation Undeveloped Reserves:	all existing Expectation Undeveloped Reserves, excluding "match volumes" (see (1) above).
Proved Undeveloped Reserves:	all projects with existing Expectation Undeveloped Reserves that are in the "Execution" or "Design" phases or which are planned to reach these phases by the end of 2008 (see Note (ii) and item (3) below)
	and which are targetted at the proved area of an existing producing field
	and which employ proved (in PDO operations) technology and recovery processes (see Note (iii) below).

#### Notes:

- i HRC comment: Setting Proved Developed Reserves equal to Expectation Developed Reserves is likely to be justified for mature producing assets. However, in newly developed (and hence immature) fields, consideration might be given to using a more conservative estimate pending confirmation of reservoir performance.
- ii HRC comment: The preferred approach of PDO is to work exclusively with the Expectation estimate of reserves for each project, assigning these reserves to either the Proved or "Probable" category based on the criteria listed above (Expectation Reserves for the Company being the sum of Proved and Probable). Again, this approach is likely to be justified for some projects, but certainly not for all and PDO is advised to take this into account when defining

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Undeveloped Proved Reserves, particularly for projects in new and immature fields. The SEC requires Proved Reserves to be estimated such that upward revisions are much more likely to occur in future than downward revisions. Whilst not specifically stated, other guidance published by the SEC and recent correspondence with Shell clearly indicates that they view this criterion as being applicable at least at the field level, and not at the overall portfolio level.

- iii SEC rules prohibit the disclosure of Proved Reserves in relation to improved recovery processes that have not yet been proved effective through observation of actual reservoir performance (pilot test or installed project). In Shell's current interpretation of the rules, reserves may be booked for processes that have been proved effective in local analogous situations. PDO's approach is consistent with this.

### 3. Potentially exposed Proved Reserves

The approach quoted above for Proved Undeveloped Reserves implies that Proved Reserves that have been booked for some projects are potentially exposed due to a lack of technical maturity – the maturation of a project to the "Design" phase is broadly comparable with the Shell Group's VAR-3 hurdle, and several projects for which Proved Reserves have been disclosed have yet to reach this level of maturity. The total volume of Proved Reserves that is potentially exposed in this way is 612 mln bbl (100% PDO basis). PDO proposes to retain these reserves on the books pending completion of technical project definition work. Reserves for projects that will be underpinned in this manner by the end of 2008 are proposed not to be debooked from the Proved Reserves category. The majority of the reserves in question will actually be underpinned much sooner than 2008 (approximately 75% covered by the end of 2005). The HRC concurs with PDO's suggested approach as being pragmatic.

### 4. ARPR data consistency

A brief review of the data in the PDO 2002 ARPR identified some areas of concern: several fields carry negative proved reserves with most, if not all, other fields having proved reserves that appear to be low by comparison with the expectation figure. As such, PDO may be able to revise upwards its overall estimate of Proved Reserves, even after taking into account the potential debookings referred to in (1) above. This may be of interest to the MOG, particularly if, in its dealings with third parties, greater emphasis might be placed on Proved Reserves than has been usual to date (there was some discussion of this point between the HRC, the STOIP and Reserves Review Team and PDO staff).

### 5. Shell shareholder considerations

From the Shell shareholder perspective, there is a mis-match between the Proved reserves disclosed by Shell via the SEC and those disclosed by PDO to the MOG. The former should be constrained by licence expiry in 2012 and yet the volume is higher (on a WI-equivalent basis) than the latter, which in principle reflects a 30-year production window. Noting item (4) above, it is likely that the PDO/MOG figures can be revised significantly upwards, but nevertheless it appears to be inevitable that the Shell / SEC figures must be revised downward to reflect a more balanced view of production that is reasonably certain to be achieved before licence expiry, consistent with the categorization summarized in (2) above.

From the Shell point of view, the licence expiry date is itself subject to revision: the advice of the Shell shareholder representative and the HRC on which date to use should be sought in good time for compiling the annual reserves report to Shell.

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NOTE - 29 Nov 2003

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From:	Anton A. Barendregt	Group Reserves Auditor, SIEP - EPF - GRA
To:	Frank Coopman	Chief Financial Officer, SIEP - EPF
	John Bell	Corporate Support Director, SIEP - EPS
	John Malcolm	Managing Director, PDO
Copy:	Abdulla Lamki	Deputy Managing Director, PDO
	Stuart Clayton	Head, Economics, Technology & Planning, PDO
	Stuart Evans	Petroleum Engineering Value Assurance Manager, PDO
	Fatma Kharusi	Finance Director, PDO
	Guy Janssens	Controller, PDO
	Lynda Armstrong	Exploration Director, PDO
	Dave Kemshell	Corporate Function Discipline Head Reservoir Engineering, PDO
	Said Al Harty	Reserves Coordinator, PDO
	(circulation)	SIEP - EPS-P: Hans Bakker, John Pay
	Andrew Vaughan	Technical Director, SEPI - EPM
	Maarten Wetselaar	Finance Director, SEPI - EPM
	Ken Marnoch	Internal Auditor EP, SI-FSAR, The Hague
	Han van Delden	Partner, KPMG Accountants NV
	Brian Puffer	PriceWaterhouseCoopers

## SEC PROVED RESERVES AUDIT - PDO (OMAN), 25-28 Oct 2003

I have audited the Proved Reserves submissions of Petroleum Development Oman (PDO) for the year 2002 and the processes that were followed in their preparation. These submissions present the PDO contribution to the Group's externally reported Proved and Proved Developed Reserves and their associated changes as at 31 December 2002.

Total Group share Proved Reserves booked by PDO at the end of 2002 were 144 mln m3 of oil. This represents some 5% of total Group share Proved Reserves on an oil-equivalent basis. Proved reserves replacement ratio for PDO over 2002 was -19%.

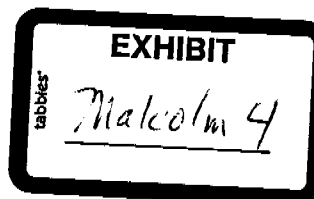
The last previous SEC proved reserves audit for PDO was carried out in 1999. This current audit verified the PDO procedures against those laid down in the "Petroleum Resource Volume Guidelines, SIEP 2002-1100/1101" (based, inter alia, on FASB Statement 69). It included a verification of the technical and commercial maturity of the reported reserves, a verification that margins of uncertainty were appropriate, that Group share and net sales volumes had been calculated correctly and that reported reserves changes were classified correctly. It also included a verification that the annual production (sales) submission through the Finance system was consistent with the reserves submission. The audit took the form of detailed discussions about the reserves reporting process with PDO staff. Emphasis was placed on the procedures and methods followed and less on detailed individual field estimates.

The audit found that PDO's Group share proved developed reserves are largely reasonable, but that some 40% of the submitted proved total reserves at 1.1.2003 do not fulfil present reserves guidelines. The reason for this is partly the progressive tightening of Group reserves guidelines (following SEC guidance), but more fundamentally that submitted proved reserves have not been reviewed and reduced in the light of recent downturns in oil production rates. The technical maturity of the projects associated with proved undeveloped reserves had also been eroded due to lack of medium- and long-term field development planning work. PDO have recognised this and have embarked on an aggressive study programme to address the maturation of the associated projects. An imminent agreement with the Government regarding an extension to the current production licence may provide further (partial) relief from the necessity to de-book the overstated volumes.

In view of the many positive changes foreseen during 2004, the audit suggestion is that the present volumes be continued unchanged per 1.1.2004 (reduced by 2003 production), but that a properly based portfolio of proved reserves should be submitted by 1.1.2005. The overall opinion on the state of PDO's 1.1.2003 Proved Reserves submission, taking account of the audit's findings (see Attachment 3), is unsatisfactory. However, improvements have been set in motion.

A summary of the findings and observations is included in the Attachments.

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A.A. Barendregt

Attachments 1, 2, 3

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## SEC PROVED RESERVES AUDIT - PDO and GISCO 25-28 Oct 2003

## MAIN OBSERVATIONS

1. PDO are the operator in a land-based concession in the Oman interior. Shareholders in PDO are the Oman Government (60%) and the 'private shareholders' (Shell, TFE and Partex). Shell holds 85% of the private shareholders' share of 40% and has thus title to 34% of the PDO produced crude. PDO are free to use produced gas for own use and for re-injection where needed, but the Oman Government has exclusive title to the exported gas. Hence, no gas reserves are carried by PDO. The current production licence started in 1967 and ends on 24th June 2012.

A separate agreement has been concluded between Shell, Total and Partex with the Oman Government regarding processing and further export of the associated and non-associated gas produced from PDO fields. This gas plant has been funded jointly between the co-venturers and the Oman Government and in recognition of this funding each of the co-venturers receives an annual fee, which is translated back into entitlement volumes for gas and NGL. This operation, administered by GISCO, is not addressed in this audit report.

PDO projects are in principle approved by the PDO board. The Group Capital Allocation system has little influence on these decisions. The verbal statement was made that many of the latest projects might not have passed the stringent Group criteria. UTC levels (an important screening tool for the PDO board) have risen above \$4/bl in recent years and the current outlook is that these may rise further, up to \$10/bl for some projects.

2. PDO production levels had climbed gradually from 200 Mb/d in the early 1970's to a plateau of 850 Mb/d in the late 1990's. A relatively steep decline has set in since 2001 and current production is at some 700 Mb/d. The fundamental reason for the decline is the progressing maturity of the many producing fields, as evidenced by increasing water cuts and, to a lesser extent, increasing GORs. The first signs of field decline had been countered by an aggressive drilling campaign, including many horizontal wells, which has helped to maintain the earlier plateau production level. Decline, or at least production at lower levels, has now been accepted as inevitable by PDO (and the shareholders), although further development options are still pursued vigorously.

Prior to and during Programme Build preparation in 2003, PDO staff recognised that some 900 MMstb (100% volumes) of expectation undeveloped reserves could not be supported by identifiable projects. These volumes were still based on assumed recovery factors, which should be seen as an outdated practice. After initial shareholder resistance, these 'unmatched' volumes have now been moved out of the 30-year Programme Build window. To address the resulting shortfall, Shell committed a team from SIEP-EPT and other sources to carry out a comprehensive review of the STOIPs and reserves of the PDO operated fields (the STOIP and Reserves Review Team, or SRRT). This review was in the final stages of completion during the audit. Preliminary conclusions by the SRRT were that PDO's STOIP estimates could largely be confirmed and that the expectation project reserves estimates in the 2003 Programme Build could generally be supported. Some exceptions were still found in Marmul and Yibal, where expectation reserves in these fields were considered to be some 20 mln m3 too high. The SRRT also noted that the great majority of the projects associated with the undeveloped reserves were not properly defined (i.e. passed VAR3) and that some were notional to very notional.

The auditor is indebted to the SRRT for sharing their preliminary conclusions with him. The review was found to be highly opportune and it provided a firm basis for the audit's findings.

3. The characteristics of the PDO fields tend to be complex in nature. The predominant reservoirs in the northern part of the concession are the Natih and Shuaiba carbonates, which are generally tight and which show varying degrees of fracturing. The predominant reservoirs in the South are the Haima and Al Khilata sandstones. The latter is of glacial origin and has been deposited onto the heavily scoured and eroded Haima sands. It tends to be highly heterogeneous, showing poor to excellent permeabilities.

The oil in these reservoirs varies from medium-light to heavy quality, with generally low GORs. Coupled with generally poor aquifer activity, this means that reservoir energy tends to be low and that pressure maintenance methods of recovery have to be applied. Water injection is used most widely, but gas injection under gas-oil gravity drainage has been implemented successfully in the steeply dipping Fahud field. Steam and polymer injection have been tried with varying success in the Marmul field in the South. A steam injection pilot has been in progress for several years in the heavily fractured Qam Alam field and a field wide application is now planned. Injection of gas alternated by water (WAG) is seen as a possible further recovery mechanism. Horizontal wells have been used quite successfully and these have led to significantly improved field rates and, in many cases, improved recoveries.

The heterogeneous nature of both the carbonates and the sandstones make good sweep efficiencies a

challenging target. The current average recovery factor is some 23% and major fields like Fahud and Natih have recovery factors in this range. The best recoveries are in the 40-50% range (Yibal, Rima, Saih Nihaida). The aspiration by the Oman Government and by PDO is to raise the target recoveries to the latter level for all fields. This will require extraction of the oil from the less permeable portions of the reservoirs, which is counteracted by the many bypass routes (higher permeable 'thief zones' or fractures) that surround these lighter portions.

Many of the PDO fields started production before or during the 1970's and production declines are apparent in a number of them. As mentioned, these declines have been countered by an aggressive drilling campaign, and this has helped maintain the PDO plateau production through the 1990's. The many infill wells did not always yield the additional reserves that were aspired. A striking example is seen in the Yibal field, where a massive horizontal infill well campaign did raise production, but where the subsequent much steeper decline seems to point towards an ultimate recovery that is not much different from that seen before, see Fig.1. A possible mild arrest of the decline may be evident from recent measurements. The lesson seems to be that many fields will yield additional recoverable volumes, but that they need sufficient time. The prevailing reservoir heterogeneities make gas-oil gravity drainage or induced/spontaneous water imbibition the only realistic option for further recovery. The associated time frames can hardly be accelerated.

4. The SRRT have identified that lack of reservoir understanding is the single most important bottleneck to production increases and further oil development maturation. Good reservoir understanding requires a reliable and representative 3D reservoir model (first static, then dynamic) and the experience in many other operations in the Group is that the availability of good 3D seismic is key to such modelling. Spectacular results have been seen in a number of other Group operated areas making e.g. reservoir character or oil fill clearly visible. Many teams in the South Oman area to claim that, due to the complex overburden (a number of strong reflective events) and due to the poor acoustic contrast at reservoir level, little use can be made of existing seismic in reservoir characterisation and 3D mapping. This opinion seems to be contradicted by experience in the Rima field, where it has been shown that dedicated re-processing (Cheats and van Gogh filtering) and close cooperation with Exploration Processing can yield much improved results. Further pursuit of this, to see whether similar results can be obtained in other fields, is strongly encouraged and supported.
5. There is mis-alignment between individual field proved reserves and the corporate PDO submission. The root cause for this has been that PDO have historically focused mainly on expectation reserves because these are the basis for business planning. Expectation reserves are also the subject of intensive discussions with the Oman Government (and also the basis for reserves addition bonuses!). Proved reserves estimates for individual fields were prepared but these have hardly been updated and they have now shrunk to unrealistic levels (see 6 below). Because of this, PDO have maintained corporate Group share proved total reserves as an independent entity, not linked to individual field volumes. This approach has not only caused problems with the audit trail but, more seriously, it allowed the Group proved reserves estimate to drift away from realistic levels, see 8 below.
6. Probabilistic estimates of STOIP and ultimate recoveries have been prepared by PDO prior to and in early stages of field development. Recovery factor ranges were obtained from preliminary reservoir modelling. Although new well results are incorporated, the probabilistic parameter ranges still seem to reflect early well data only, i.e. little adjustment seems to be made for subsequent dynamic STOIP and recovery determination from production performance. Hence, the current proved vs. expectation recovery ranges in individual fields are too wide for the current stage of field development. The 1999 reserves audit made the same observation. It is therefore disappointing to see that no progress has been made in this respect.

The conservative nature of the current field proved (P85) recoveries has been further exposed by progressing cumulative production from the fields. With proved and expectation ultimate recoveries fixed, the range between proved and expectation remaining reserves will widen with progressing production. This is clearly visible in Figure 2. Cumulative production has already overtaken proved ultimate recovery in some fields, with the result that these fields now carry negative proved remaining reserves, which is of course impossible. Examples are Rima, Sayyala, Wafra and Runib.

Group reserves guidelines state clearly that field / reservoir reserves estimates should be made separately for developed (no further activity, or NFA) and undeveloped reserves. The latter must be project based, i.e. they must be associated with clearly identified future development activities (wells, facilities). Estimation of total recoveries based on (largely assumed) recovery factors is archaic and is considered indefensible with the current state of petroleum engineering technology.

Proved developed reserves should be derived in a deterministic manner, using reservoir model simulations and production trend extrapolations. Proved undeveloped reserves should be evaluated through simulation, using either a low case model realisation or e.g. a specific assessment for infill wells whether they address 'proved areas'. This practice should result in proved undeveloped reserves growing towards expectation levels with progressing field maturity, see Fig. 2.

7. Expectation developed reserves are generally, and correctly, derived from well and cluster decline analysis (through Oil Field Manager software) or from reservoir simulation models. The Group share proved



developed estimate was derived from the expectation NFA forecast, cut off at the end-of-licence in June 2012. This is in accordance with Group guidelines. However, the link between Group share / corporate proved reserves and individual field estimates should be re-established.

8. There is a serious flaw in the corporate total proved reserves estimate (and, by implication, in the undeveloped reserves estimate) in that this estimate was not reviewed when the PDO oil production started to decline rapidly from 2000 onwards. Group share reserves should be producible within the current licence period (ending in 2012) and the achievement of production of the stated volumes in that time period has rapidly become unlikely.

The majority of the declared corporate undeveloped field reserves are associated with identified projects. However, many of these are notional or highly notional. There are of course more mature projects, but many of these are recognised as needing further work or re-work in order to become matured towards the required VAR3 (or FID) level. Even some projects/volumes based on FDPs from the late 1990's, which did pass VAR3 earlier, are now seen as out of date because of subsequent well and field performance. The estimate made by PDO and the SRRT is that 80-90% of the presently identified undeveloped reserves are yet to pass through the VAR3 stage. This means that these volumes do not fulfil present Group and SEC guidelines. It is accepted that the latter have tightened over the last three years (from 'defined' projects to VAR3) and thus further increased the exposure.

The main reason for this regrettable situation is that proper modern static and dynamic modelling has received insufficient attention in PDO in recent years. Much attention was diverted towards short-term activities to provide new well proposals. The situation is now being addressed through an urgent and aggressive study programme.

The Group share undeveloped reserves at 1.1.2003 (and hence the total proved reserves) contain therefore a large portion that does not fulfil current Group reserves guidelines. A preliminary estimate made by PDO during 2003 is that of the 907 MMstb (Group share) booked at 1.1.2003, some 400 MMstb are exposed in this manner.

It is noted that the 907 MMstb submission at 1.1.2003 had been based on SIEP advice, reducing it from a higher value proposed by PDO. This advice was seen as a preliminary correction, pending results of further PDO investigations and the planned 2003 reserves audit. The approach was supported by the Group reserves auditor, but he did express concern in his end-2002 report that PDO's proved reserves were overstated.

The impact of this effective overstatement of reserves is somewhat reduced by the fact that discussions between PDO and the Oman Government towards an extension of the current production licence are currently in progress and that a Heads of Agreement is expected before the end of 2003. A formal extension agreement could then be signed during the first half of 2004. This should bring some 300 MMstb of mature project reserves (230 MMstb developed, 70 MMstb undeveloped) into the Group reserves portfolio.

9. It was noted during the audit that PDO are proposing to carry a number of projects with positive expectation reserves but zero proved reserves. These volumes relate to projects and exploration discoveries, whose development plan is not yet sufficiently mature to merit the booking of proved reserves. The expectation volumes have been agreed with the Oman Government and reserves addition- and exploration bonuses will be received for them. The Group guidelines state clearly that expectation reserves can only be booked if the associated projects fulfil the conditions for proved reserves. If the latter is not the case, the expectation volumes should be booked as SFR.
10. The consistency between reserves and Finance was good. There was full agreement between the 1.1.2003 submissions for reserves and for annual production through Ceres/FIRST, without any corrections being required.

The verification of the correctness of proved developed and proved total reserves used for UOP asset depletion calculations was not relevant in the case of PDO, because UOP asset depletion was not applied in the past. The operating agreement stipulates a 40-30-10-10-10% depreciation profile for all capex and this is applied for calculation of the PDO profit margin and for PDO tax returns. Shell Group accounts returns are prepared by Shell Oman Trading (SOMANT) and they do not declare any share in the PDO assets.

PDO accounts are declared with asset depreciation through the abovementioned 5-year profile. This is not in accordance with international accounting practices, which require UOP depletion, based on proved total and proved developed reserves. This has led to continuing qualifications in external auditor reports (since 1967), which the Oman Government now want to see removed. Hence, PDO will need to start maintaining proper estimates of individual field proved developed and proved total (i.e. undeveloped) reserves. In view of the current state of PDO's proved reserves estimates (both corporate and by field), PDO have considered it not realistic to start with the new method of UOP accounting per 1.1.2004. A start per 1.1.2005 was seen to be the earliest possible as it would be desirable to avoid major swings in individual field reserves and asset values due to the necessary corrections to be applied during 2004. This view is fully supported.

Following the implementation of the new method of asset accounting, PDO will be required to re-state their accounts back to 2000. The intention was to do this on the basis of the 1.1.2005 volumes, correcting back

only for annual production. The auditor recommendation is to include annual transfers from undeveloped to developed volumes (i.e. development activity) as well, since without this correction the earlier proved developed reserves would become too large.

11. By way of audit trail, PDO issue an annual ARPR report, which lists full life cycle (i.e. 30-years) recoverable volumes of oil+condensate (from PDO facilities) and associated gas. The format of the report seems somewhat cumbersome (duplicated data and unnecessary data, e.g. depletion rates, high estimates) and it could benefit from a simplification.

There is no note or report describing the basis or background for the Group share reserves submission. There is a spreadsheet, but this is not very accessible. Individual field proved reserves in the 1.1.2003 submission are clearly wrong (e.g. larger than expectation volumes and also larger than full-field-life proved reserves). The submission listed changes in the 'Improved Recovery', 'Extensions and Discoveries', and 'Transfers from Undeveloped to Developed' categories, but there was no audit trail to link this back in a quantitative manner to individual fields. The audit trail for PDO's Group share proved reserves is thus extremely poor. Guidelines for a proper audit trail are published on the EPB-P website ('Planning'/Reserves', to be moved to a new EPS website in due course) and these should be followed. What is needed is a set of tables, at field level, with a format as presented in Att.2 and with a brief note describing the source of the constituent data.

It was noted that, whilst there is a central PDO library, field teams tend to keep project reports in personal filing cabinets. The SRRT reported instances where documents had to be obtained from the Ministry because no copies could be found within PDO, following the temporary abandonment and re-assignment of the Fahud field team. This is clearly an undesirable situation and corrective measures should be undertaken.

12. The auditor's suggestion for the way forward is as follows:

- In view of the short period left to end-2003, it will not be possible to arrive at a properly defined set of individual field proved reserves that could form a sound basis for the PDO corporate Group share proved reserves booking.
- Assuming that a Heads of Agreement can be obtained with the Oman Government before end 2003 regarding an extension of the PDO production licence, it is argued that the impact of the present reserves overstatement is reduced.
- Hence, it is suggested that the present proved developed and proved total Group share reserves volumes be continued in the 1.1.2004 submission, correcting only for 2003 production and for transfers from developed to undeveloped. Total proved reserves replacement ratio should thus be 0%.
- The proper sum of full life cycle proved developed reserves for all fields and proved undeveloped reserves for all projects fulfilling Group reserves criteria should then be booked per 1.1.2005. This would require the maturation of at least some 200 MMstb of proved project volumes, to obtain a 100% proved reserves replacement ratio over 2004, see Table 1 below. Group share reserves should be a straight 34% of PDO oil reserves.
- It is suggested to invite the Group Reserves Auditor for a consultation visit towards the end of 2004 to verify with him the status of the proved developed and proved undeveloped reserves portfolio.

Group share total proved reserves 1.1.2003 (MMstb)	907
2003 Production	-87
Group share total proved reserves 1.1.2004 (MMstb)	820
Group share total proved reserves 1.1.2004 (MMstb)	820
Overstatement 400 MMstb	-400
Transfer from beyond-licence	+287
New matured proved reserves	+200
2004 Production	-87
Group share total proved reserves 1.1.2005 (MMstb)	820

Table 1 – Possible progression of PDO proved reserves during 2003 / 2004

#### Recommendations

1. Continue pursuing the possible improvements in reservoir characterization and modelling that may be obtained from dedicated seismic re-processing (cf Rima).
2. Declare proved developed as equal to expectation developed reserves in fields where there is either a good simulation history match or where there is a well-defined decline rate extrapolation. New fields and



reservoirs with neither of these should be assigned a conservative (low case) value for proved developed reserves.

3. Prepare proved and expectation estimates of undeveloped reserves by individual project and by field. Proved estimates should preferably be based on low case simulation model realisations and should be seen to be growing towards expectation levels with progressing field cumulative production. Projects should be ranked according to their maturity, e.g. 'firm' (VAR3/FID), 'mature' (documented FDP), 'possible' (VAR2) etc.
4. Invite the Group Reserves Auditor for a consultation visit towards the end of 2004 to verify the status of Group share proved developed and proved undeveloped reserves.
5. In the re-statement of PDO accounts for years back to 2000, correct the 1.1.2005 volumes back to earlier years by adding annual production and by subtracting annual transfers from undeveloped to developed reserves.
6. Classify projects with expectation reserves but zero proved reserves as SFR in the next appropriate submission.
7. Improve the audit trail for the Group reserves submission by following the guidelines for reserves audit trails on the EPB/Planning/Reserves website.
8. Ensure that the central library facilities are fully utilised by all teams, particularly where it relates to proper storing and indexing of copies of all reports and meeting notes (e.g. with the Ministry).

GRA 000319

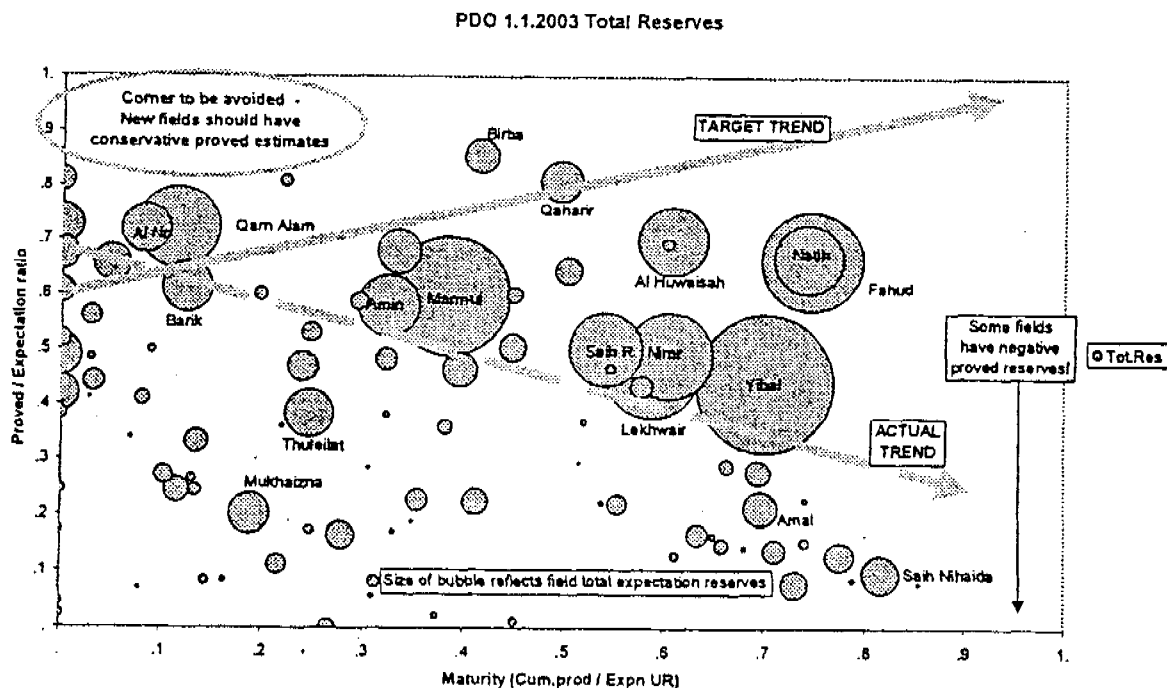
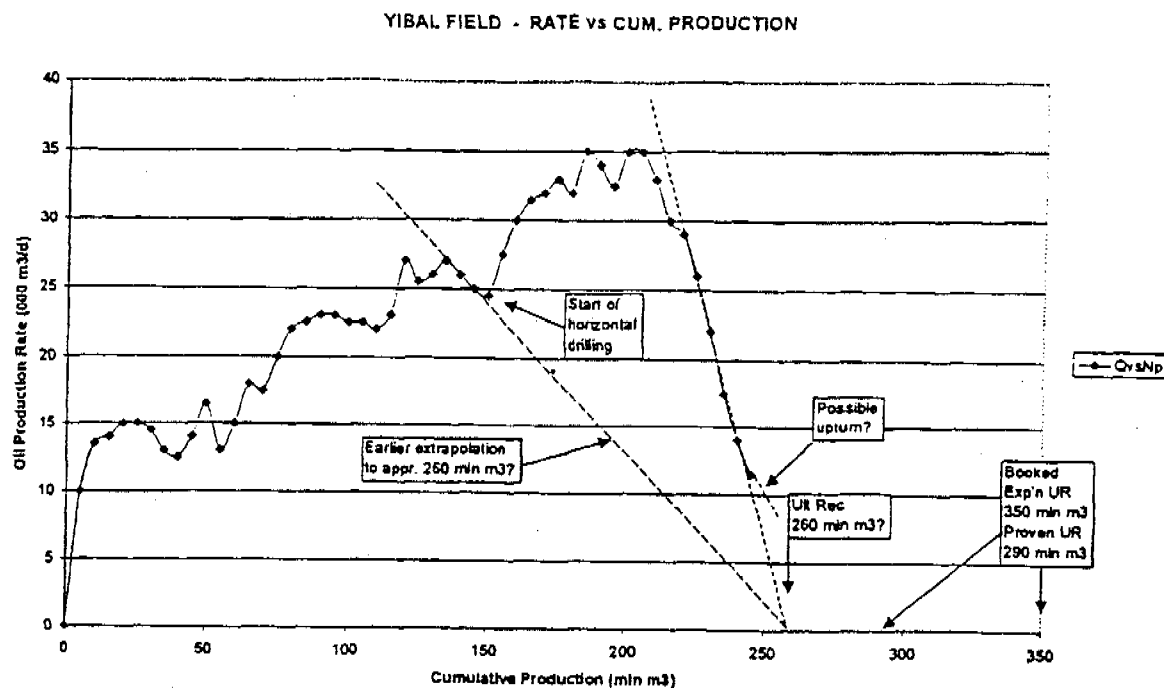


Figure 1 - Yibal field oil rate decline versus cumulative production

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7

implies expectation too high or proved too low?  
Which? 500?

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**Figure 2 - Ratio of Proved / Expectation Reserves versus progressing field maturity**

**GRA 000321**

PDO		Proved Oil Reserves Changes 2002 (100%, min m3)															
Field	Proved Res. 1.1.2002	Revisions/ Reopening	Impaired Recovery	Estimate/ Decrease	Purchased in place	Sales in place	New Develop- ment Reserves (Transit Unit is	Proved Res. 2002	Proved Res. 1.1.2003	Shed Equity Share % 1.1.2002	Shed Equity Share % 2002 Prod	Shed Equity Share % 1.1.2003	Net Shed Equity 1.1.2002 (10% m3)	Net Shed Equity 1.1.2003 (10% m3)	Comments		
Proved Developed Reserves																	
YBAL	15.76	0.00						5.00	10.76	136.22%	34 %	136.22%	21.47	14.86			
FAMUD	40.15	0.00						3.58	36.56	16.89%	34 %	16.89%	8.78	6.19			
WARMUL	12.08	0.00						2.18	10.91	64.97%	34 %	64.97%	8.30	7.00			
LEONHAR	21.17	0.00						4.91	16.26	45.28%	34 %	45.28%	9.58	7.30			
NATHI	17.50	0.00						1.74	16.11	28.5%	34 %	28.5%	5.10	4.69			
SHMA	0.21	0.00						4.60	7.88	81.33%	34 %	81.33%	7.38	4.83			
AL HAKUSAN	12.56	0.00						1.37	87.19%	34 %	34 %	37.19%	2.38	1.77			
SAN RAH	9.03	0.00						1.79	4.55	27.15%	34 %	27.15%	4.42	3.26			
DARH ALAM	0.84	0.00						2.37	6.71	48.87%	34 %	48.87%	0.77	0.74			
Other Fields	55.04	0.00						0.09	0.75	32.01%	34 %	32.01%	15.84	11.83			
Proved Under Res. (min m3)	193.58	0.00	0.00	0.00	0.00	0.00	0.00	44.76	148.80	43.57%	34 %	47.19%	82.41	62.77			
Proved Undeveloped Reserves																	
YBAL	35.39	0.00						25.39	15.7%			15.7%	1.39	1.39			
FAMUD	0.79	0.00						0.79	291.9%			291.9%	2.32	2.32			
WARMUL	36.97	0.00						36.97	26.91%			26.91%	8.68	8.68			
LEONHAR	5.84	0.00						5.84	59.34%			59.34%	3.34	3.34			
NATHI	1.76	0.00						1.76	11.56%			11.56%	0.78	0.78			
SHMA	0.00	0.00						0.00	37.18%			37.18%	4.67	4.67			
AL HAKUSAN	12.51	0.00						12.51	163.17%			163.17%	0.76	0.58			
SAN RAH	8.15	0.00						8.15	36.78%			36.78%	4.80	4.80			
DARH ALAM	27.32	0.00						27.32	43.56%			43.56%	1.55	3.55			
Other Fields	55.87	0.00						55.87	22.18%			22.18%	6.78	6.78			
Proved Under Res. (min m3)	225.80	0.00	0.00	0.00	0.00	0.00	0.00	225.80	36.05%			36.05%	81.40	81.40			
Net Gross Equity																	
Proved Developed Reserves	82.41	-4.42					0.00	15.22	62.77	62.77							
Proved Total Reserves	163.81	-4.42	0.00	0.00	0.00	0.00	0.00	15.22	144.17	144.17							
1.1.2003 Subbalance																	
Proved Dev Res	63.89	-4.92					7.37	15.22	62.77	62.77							
Proved Tot Res	162.28	-4.74	0.34	1.49				15.22	144.17	144.17							
Comments before used by SGP																	
No L1.2002 said data provided																	
No book said for Transfers under/over & Extensions/Discoveries and Impaired Recovery																	
Contributor factors used by PDO																	
1 m3 = 1 m3																	
1 bbl = 0.0293 m3																	
1 bbl = 0.0293 m3																	

PDO/Gisco, Oct 2003

## CHECKLIST SEC RESERVES AUDITS

Attachment 3

COMPANY: PDO		AREA / FIELD: ALL FIELDS	
Audit criteria		Result	Comments
<b>1 TECHNICAL MATURITY</b>			
1.01	Is 3D seismic available and used for the field(s) in question?	+	3D Seismic coverage is universal over all discovered fields.
1.02	Are seismic processing and interpretation state-of-the-art?	O	Seismic tends to be of poor quality due to strong shallow multiples, surface rugosity and other irregularities, e.g. local sinkholes. Filtering (Cheats, van Gogh) has been applied with mixed success. Results are more promising in one area (Rima cluster) where it is anticipated that good information can be obtained on structure and small scale faulting, but, more importantly on reservoir stratification and perhaps characterisation.
1.03	Is seismic quality used / adequate for proving hydrocarbon bearing areas?	N.A.	Oils tend to be generally heavy and of low GOR. Acoustic contrast with water is small and oil bearing areas cannot be distinguished from seismic.
1.04	Is well data coverage adequate?	+	The majority of fields have been developed by numerous wells, both vertical and horizontal.
1.05	Are fluid levels known?	+	Since seismic and regional aquifer pressures are not reliable for predicting OWCs these tend to be specifically targeted by appraisal wells.
1.06	Are petrophysical well data quality and quantity adequate?	O	Not all wells had full suites of logs during major development drilling phases (GR and resistivity only, no porosity tools). This is a slight hindrance in reservoir characterisation.
1.07	Is reservoir producibility for undeveloped reserves supported by production tests or other evidence?	+	Most fields are now in production. Production tests are carried out in exploration / appraisal wells.
1.08	Are there proper volumetric estimates?	+	Volumetric estimates have been made for all fields. Most date back from the older generation of mapping packages (Zycor, CPS, Supervol). Most of these were coarse layered or coarse gridded. However, the recent (STEP staffed) STOIP and Reserves Review Team has largely confirmed the validity of these estimates.
1.09	Are representative PVT data available and have they been properly accounted for in the volumetric estimate?	+	Proper sampling and analysis is done for new fields.
1.10	Are gas GHVs measured properly for sales gas conditions and accounted for in reserves submissions?	+	No gas reserves are carried
1.11	Are static models available / adequate?	X	Proper modern static and dynamic modelling has received insufficient attention in recent years. A large volume of booked reserves is based on older and outdated FDPs or on earlier volumetric estimates. This is now being addressed through an urgent study programme. Petrel models are the present standard.
1.12	Are dynamic models available / adequate?	X	See above. MoReS models are now downloaded from Petrel.
1.13	Are history matches available / adequate?	X	History matches are gradually becoming available as models are matured.
1.14	Are the recovery factors for proved reserves realistic?	X	PDO and the STOIP and Reserves Review Team have concluded that a number of the older (FDP) expectation reserves estimates have been overstated (Yibal, Marmul, Qarn Alam). Individual field proved reserves are still based on old probabilistic volumetrics, in which the margins are much too wide in relation to the field's maturity. As for the booked proved corporate Shell share reserves, these cannot be tied back to realistic proved individual field estimates.
1.15	Are developed reserves based on proper NFA (No Further Activity) forecasts?	+	Expectation developed reserves are based on NFA forecasts - derived from well and cluster decline analysis (through Oil Field Manager software). The origin of the corporate proved developed estimate was not clear, but its volume seems broadly in line with the expectation NFA forecast, cut off at the end-of-licence in 2014.
1.16	Are developed reserves based on existing wells, completions and facilities, or do they require only minor costs (<10% project cost) to be hooked up?	+	Yes; No behind-pipe reserves are carried.

+ = Good O = Satisfactory X = Unsatisfactory N.A. = Not Applicable

PDO/Gisco, Oct 2003

## CHECKLIST SEC RESERVES AUDITS

Attachment 3

1.17	Have development projects been defined for undeveloped reserves or can they be defined?	X	The majority of undeveloped field reserves are associated with identified projects. However, many of these are notional or highly notional, while others have no forecast associated with them in the Business Plan.
1.18	Are there auditable development project plans with costs, benefits and economics?	X	A large majority of the undeveloped reserves projects are notional, with at best only approximate forecasts and cost estimates.
1.19	Are the projects technically mature or is further data gathering necessary?	X	The majority of projects are recognised as needing further work or re-work in order to become matured. Even many projects/volumes based on FDPs from the late 1990's are now seen as out of date because of subsequent well and field performance.
1.20	Are improved recovery estimates based on a successful pilot or analogue or are they otherwise supportable?	O	There are ample water injection projects in the PDO operated area. This could normally count as a sufficient analogue base for proving further new water injection projects. However, the reservoirs concerned (notably the Al Khilata sandstone and some shallower fractured carbonates) present a high degree of variability and such analogues may not always be representative.
1.21	Have the projects successfully passed a VAR3/VAR4 review or are they otherwise ready for application for funding?	X	PDO and the STOIP / Reserves Review Team have recognised that 80-90% of the undeveloped reserves are yet to pass through the VAR3 stage. This includes a number of projects that have gone through such a stage in the past but which are now seen to need updating.
1.22	Are the projects firmly planned to go ahead - are there any potential show stoppers?	O	The Oman Government, as the major shareholder, is firmly committed to maximise oil recovery in a manner that is beneficial to them. Only projects with very poor economics would be at risk of not being executed.
<b>2 COMMERCIAL MATURITY</b>			
2.01	Are the projects economically viable (meeting Group Scr. Crit. over range of possible future scenarios / low case reserves)?	O	PDO projects are in principle approved by the PDO board. The Group Capital Allocation system has little influence on these decisions. The verbal statement was made that many projects would not have passed the stringent Group criteria. Previous UTC levels were at some \$4/bl, but these have risen in recent years and the current outlook is that these may rise to levels up to \$10/bl.
2.02	Have forecasts been cut off when rates become uneconomic?	N.A.	Forecasts are cut off at the end of the current production licence (24th June 2012). This long before production levels have declined below economic production levels.
2.03	Have the latest Group Screening / Reference Criteria been used?	O	See 2.01 above
2.04	Are assumed prices and costs RT (or justified if not)?	O	See 2.01 above
2.05	Is export infrastructure (pipelines, terminals etc) available or, if not, is it firmly planned and fully included in the economics?	+	Most of the export infrastructure is already in place. Any extensions would be included in the relevant economics.
2.06	Is project financing available or can it reasonably be expected to be available?	+	Yes
2.07	Are developed reserves actually in production?	+	Yes, see 1.15.
2.08	Have all major gas project reserves been committed or contracted to sales, e.g. through a HOA, GSA?	N.A.	PDO is free to use produced gas for own use and for re-injection where needed, but they have no title to exported gas. Hence, no gas reserves are carried.
2.09	Can smaller gas project reserves reasonably be expected to be sold in existing markets and through existing / firmly planned facilities?	N.A.	
2.10	If neither, is there a firm commitment (eg FID) that supports the assumption and maturing of a future market?	N.A.	
<b>3 REASONABLE CERTAINTY</b>			
3.01	Is the uncertainty range of volumetric parameters and STOIP estimates adequate?	X	STOIP ranges were evaluated probabilistically after the early static (deterministic) modelling. Parameter ranges tended to take into account well log data only, but no adjustment was made for dynamic STOIP determination from production performance. Hence these ranges were perhaps defensible at the time of their preparation but they are too wide for the current stage of field development.
3.02	Have 'proved areas' been defined (lowest known fluid contact, 'continuity of production', no major/sealing faults) and are they realistic?	+	Water contact levels are well known and well control tends to be more than adequate.
3.03	Are proved (developed and total) reserves consistent with these 'proved areas'?	+	Yes

+ = Good O = Satisfactory X = Unsatisfactory N.A. = Not Applicable

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## CHECKLIST SEC RESERVES AUDITS

Attachment 3

3.04	Is the uncertainty range of developed recovery adequate?	○	Although there is no clear audit trail for the composite proved developed recovery estimate, it appears to align with the expectation NFA forecast within the licence period. This is largely reasonable for a portfolio with the size and maturity of PDO's. Some downward corrections should be made for new developed fields. The composite proved forecast is not linked back to proved estimates for individual fields. The reason is that no such individual field estimates are made.
3.05	Is the uncertainty range of undeveloped recovery adequate?	X	The undeveloped forecast within licence contains a large number of projects that are far from mature and which can therefore not be regarded as proved (or, for that matter as true expectation). The composite proved undeveloped estimate includes a significant number of these immature projects. This is not in accordance with SEC and Group guidelines. As for the developed reserves, the composite proved undeveloped forecast is not linked back to proved estimates for individual fields because no such proved estimates are made.
3.06	Have market / production constraint uncertainties been taken into account?	N.A.	Offtake is at maximum field capacity.
3.07	Is the Group / Region / Asset Holder committed to proceed with development?	+	Yes, see also 1.22.
3.08	What is ratio of field(s) cum.prod. / expectation total recovery?		0.59
3.09	Can the field(s) be considered mature?		On average, yes, although there are numerous small new fields.
3.10	Are proved reserves for fields (or other entities used for asset depreciation) added together arithmetically?	+	Yes
3.11	Are proved reserves within fields (or within entities used for asset depreciation) added together probabilistically?	○	Field recovery estimates are now generally made in a deterministic manner. Probabilistic addition is no longer appropriate.
3.12	Is any assumed dependency in probabilistic addition appropriate?	N.A.	
4	GROUP SHARE CALCULATION		
4.01	Are proved and proved developed reserves fully producible within the licence period (or its extension if there is a legal right) and within production ceilings/constraints?	X	The proved developed reserves align with the expectation NFA forecast, which is appropriate for mature fields. The proved undeveloped reserves are likely to be overstated because they are not fully supported by proved projects.
4.02	Are the forecasts required to demonstrate the above condition consistent with the firm Base Case presented in the latest Business Plan?	X	The proved total estimate is well in excess of the 'Tranche 1' projects forecast from the 2002 Business Plan and similar forecasts from the 2003 Business Plan.
4.03	Is the hydrocarbon Equity share calculated properly (regular production contracts)?	+	The Group share is 34%, which is 85% of the 'private shareholders' share of 40% in the PDO operated fields.
4.04	Is the hydrocarbon PSC entitlement share (net cost oil + profit oil only) calculated properly?	N.A.	
4.05	Is the hydrocarbon Purchase Right share (to the extent that economic benefit is derived from production while still bearing share of risks and rewards) calculated properly?	N.A.	
4.06	Are royalties that are (formally or customarily) paid in cash included in reserves?	+	Royalties are paid in cash and are not deducted from liftings nor reserves bookings.
4.07	Are royalties paid in kind excluded from reserves?	N.A.	
4.08	Are volumes delivered free of charge as fees in kind (e.g. for infrastructure used by third parties) included in reserves? Similarly, are volumes received as fees in kind excluded from reserves?	N.A.	Minor streams of third party crude are exported through PDO pipelines. Fees are paid in cash.
4.09	Has historic Group under- or overlift (e.g. compared with other co-venturers) been accounted for?	N.A.	
4.10	Have gas volumes produced from the reservoir but not yet sold (e.g. through UGS, gas re-injection into another reservoir or a swap deal with another field) been properly maintained in reserves?	N.A.	No gas reserves are carried
4.11	Have gas volumes paid for by the buyer but not yet produced and sold ('take-or-pay' gas) been properly maintained in reserves?	N.A.	
4.12	Have separate submissions been made for Equity, Entitlement and Purchase Right volumes?	N.A.	
5	AUDIT TRAILS		
5.01	Are proved and proved developed reserves estimates up-to date?	X	The composite total proved reserves within-l licence estimate has largely been maintained from previous years, in spite of the growing immaturity of the constituent projects.

+ = Good - ○ = Satisfactory X = Unsatisfactory N.A. = Not Applicable

PDO/Gisco, Oct 2003

## CHECKLIST SEC RESERVES AUDITS

Attachment 3

5.02	Can reported net Group equity reserves be reconciled with individual field reserves estimates?	X	No; The individual proved / expectation reserves ratios for individual fields are too low, particularly for the more mature fields (see Att 4).
5.03	Can reserves changes be reconciled with individual field changes?	X	Changes have been reported in the 'Improved Recovery', 'Extensions and Discoveries', 'Transfers from Undeveloped to Developed' categories and of course in 'Revisions'. There was no audit trail note to link this back in a quantifiable manner to individual fields. The ARPR is in full 30-year life cycle volumes only.
5.04	Are reserves changes reported in the appropriate categories?	X	Since the source of the changes was not clear, it could not be established whether the categorisation of the changes was appropriate.
5.05	Is there a document in place describing the OU's reserves reporting procedures?	O	A document has been in circulation in draft form for some time. A final version is anticipated in November this year.
5.06	Are technical reports available describing reasons and justifications for new reserves estimates in sufficient detail?	O	FDP documents were prepared upon the conclusion of studies. Very few of these have been issued in recent years because of time pressure.
5.07	Are reports numbered / indexed properly and is there a central library where copies are kept?	X	Whilst there is a central library with search facilities, field teams tend to keep project reports in personal filing cabinets.
5.08	Is the annual reserves submission supported by a sufficiently detailed summary note explaining the reserves changes (classified in revisions, extensions, sales-in-place etc) per field, with references to detailed reports as appropriate?	X	An ARPR report is issued annually, which lists full life cycle (i.e. 30-years) recoverable volumes of oil+condensate (from PDO facilities) and associated gas. The format seems somewhat cumbersome (duplicated data and unnecessary data e.g. depletion rates, high estimates). It could benefit from a simplification. A note describing the basis for the Group estimates was not present, only a complex spreadsheet.
5.09	Are electronic data bases containing both historic submissions data and current reserves data in place and accessible?	+	Yes, largely in the form of spreadsheets.
5.10	Do these data bases also contain references to detailed reports?	O	No
6	CONSISTENCY WITH FINANCIAL REPORTING		
6.01	Are proved and proved developed reserves based on fiscalised volumes under sales conditions?	+	Yes
6.02	Are oil, NGLs and sales gas reported in their appropriate categories?	+	Yes; Oil (and any co-produced oil gas condensate) is reported by PDO, gas and ex-gas plant liquids entitlements are reported by Gisco.
6.03	Are own use, fuel, losses etc excluded?	+	Gas own fuel and losses are not relevant to the calculation of Group share oil entitlements.
6.04	Are annual Oil+NGL production volumes in reserves submissions consistent with Upstream sales volumes reported into the Finance (Ceres) system? (Ceres line 0933, which is the sum of line 7385 (Reward Oil/NGL) and line 0871 (= 8462-Oil + 8464-NGL for Consolidated Companies + line 3596 (= 0931-Oil + 0932-NGL) for Assoc. Companies).	+	Yes
6.05	Are annual gas production volumes in reserves submissions consistent with Upstream Gas production available for Sales (GpafS) volumes reported into the Finance (Ceres) system? (Ceres line 9130).	N.A.	No gas reserves carried by PDO
6.06	Are the Financial and Reserves accounting of production / sales fully consistent with each other also in cases like royalties, fees-in-kind, underlift/overlift, gas re-injection/UGS, take-or-pay gas?	+	Yes (only royalties are applicable here)
6.07	Are the net Shell share reserves reported properly and consistently with Finance reporting (100% for consolidated Shell companies, with minority reserves reported separately, or actual percentage if less than 50%)?	+	PDO prepares the submissions as an associated company with 34% Group share.

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+ = Good O = Satisfactory X = Unsatisfactory N.A. = Not Applicable

PDO/Gisco, Oct 2003

## CHECKLIST SEC RESERVES AUDITS

Attachment 3

6.08	Are reported proved total and proved developed reserves consistent with those used for asset depreciation in Group Accounts?	N.A.	PDO has not applied UOP asset depletion in the past. The operating agreement stipulates a 40-30-10-10-10% depreciation profile for all capex and this is applied for calculation of the Shell margin and for tax submissions. Shell Group returns are made by Sonant who do not hold any share in the PDO assets, hence no asset depreciation is applicable for Group accounts. PDO accounts are managed with depreciation through the abovementioned 5-year profile. This is not in accordance with international accounting practices, which require UOP depletion, based on proved total and proved developed reserves. This has led to qualifications in external auditor reports, which the Oman Government now want to see removed. Hence, PDO will need to maintain proper estimates of individual field proved developed and proved total (i.e. undeveloped) reserves, probably starting at 1.1.2005.
7	OVERALL		
7.01	If Group guidelines should not or not completely have been followed, are results still reasonable / overstated / understated?	X	Group share proved developed reserves at 1.1.2003 are largely acceptable. However, Group share total (i.e. undeveloped) reserves are not in accordance with SEC and Group guidelines and have thus been overstated significantly.
7.02	Do the reported proved and proved developed reserves estimates give a reasonably accurate reflection of shareholder value?	+	In spite of the above comment, the currently reported volumes give a reasonable reflection of shareholder value if account is taken of the probable extension of the current production licence agreement beyond 2012.

Weight Score (0-100%)

1	TECHNICAL MATURITY	30% 47%
2	COMMERCIAL MATURITY	9% 72%
3	REASONABLE CERTAINTY	21% 67%
4	GROUP SHARE CALCULATION	8% 50%
5	AUDIT TRAILS	16% 23%
6	CONSISTENCY WITH FINANCIAL REPORTING	7% 100%
7	OVERALL OPINION	8% 50%
TOTAL SCORE		100% 54%

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PDO03-Att3.xls, CheckList

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02/12/2003, 13:30

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Treatment Requested

V00100702

**Unknown**

**From:** Coopman, Frank F SIEP-EPF  
**Sent:** 06 November 2003 16:44  
**To:** Barendregt, Anton AA SIEP-EPF-DIR; Pay, John JR SIEP-EPS-P  
**Subject:** RE: Draft Reserves audit report (PDO)

Anton,  
 I understand and respect your rationale.

## -----Original Message-----

**From:** Barendregt, Anton AA SIEP-EPF-DIR  
**Sent:** 06 November 2003 01:17  
**To:** Coopman, Frank F SIEP-EPF; Pay, John JR SIEP-EPS-P  
**Subject:** RE: Draft Reserves audit report (PDO)

Frank,

Trust you're aware that the report is still in draft form.

The reason why I am 'lenient' in this case is because I have had the personal assurance from many people in PDO, including the MD, that a deal about the licence extension is around the corner and that aHOA is likely to be signed before end-2003. If this was Russia, I'd still be cautious, but in Oman I feel one can safely assume that the deal is indeed much more than 'reasonably certain'.

The way I see it, is that we therefore have some 300 out of the overstated 400 MMbbls as more than 'reasonably certain'. Much more certain, in my opinion, than the volumes for projects that we still need to get VAR3 on, particularly if the latter is still some years away - I'm not only thinking of PDO here, but more particularly of SPDC, and quite possibly others.

I could insist on debooking the 400 MMbbls now, only to see most of it re-instated again a year later. But then I should also, and even more so, insist on debooking all projects for which we have no VAR3/FID at 1.1.2004. Our guidelines say we shouldn't do that, with some justification, I believe. Personally I'd rather defend the Oman case to the SEC than the SPDC case, because in Oman we're looking at bridging a one-year gap, in SPDC it's bound to be (much?) longer.

If you want me to explain this to the external auditors, I'd be more than happy to.

Regards,

Anton

## -----Original Message-----

**From:** Coopman, Frank F SIEP-EPF  
**Sent:** woensdag 5 november 2003 9:10  
**To:** Pay, John JR SIEP-EPS-P  
**Cc:** Barendregt, Anton AA SIEP-EPF-DIR  
**Subject:** FW: Draft Reserves audit report

John,

Assume you have read the attached audit report. I did.  
 It is a very balanced report, although I am not so sure that our external auditors are as lenient as Anton.  
 It will be a tough one to explain to the SEC!

## -----Original Message-----

**From:** Barendregt, Anton AA SIEP-EPF-DIR  
**Sent:** 04 November 2003 02:18  
**To:** Clayton, Stuart PDO-DTEM; Harthy, Said SAA PDO-DTEM7  
**Cc:** Evans, Stuart ES PDO-DPVM  
**Subject:** Draft Reserves audit report

Stuart, Said,

GRA 000311



V00100686

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 Treatment Requested

Herewith my draft report, with apologies for the slight delay (I'm travelling and I couldn't get E-mail access until now).

I'd be grateful for your comments by mid this month, if possible.

Many thanks once again for your cooperation.

PS What is Stuart E's job title?

Regards,

Anton

<< File: PDO03-Covnt.doc (Compressed) >> << File: PDO03-Att3.xls (Compressed) >>

—  
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**GRA 000312**