

Chapter 7 - Compliance and Control Issues

Significant compliance and control issues relating to KG-DWN-98/3, RJ-ON-90/1, Panna-Mukta and Tapti PSCs have been discussed in chapters 4 to 6 of this report. This chapter deals with compliance and control issues relating to other PSCs, as well as less significant issues relating to these four PSCs.

7.1 Role of DGH

In April 1993, the GoI decided to set up the Directorate General of Hydrocarbons (DGH) under the administrative control of MoPNG with the objective of promoting the sound management of Indian petroleum and natural gas resources, having a balanced regard for the environment, safety, technological and economic aspects of the petroleum industry. **The GoI resolution of April 1993 constituting the DGH refers to the need of the MoPNG to have an appropriate agency to (a) regulate and oversee upstream activities in the petroleum and natural gas sector; and (b) also advise GoI in these areas.**

Besides the Director General, the staff of DGH is drawn on deputation/ tenure basis, mainly from upstream and other oil PSUs (ONGC, OIL, IOC and BPCL).

The functions of the DGH, as stipulated in the April 1993 resolution fall into two broad categories:

To advise the GoI on:	<ul style="list-style-type: none">• Exploration and optimal exploitation of hydrocarbons within the country, and on the strategy of exploration/ exploitation of reserves abroad by NOCs• Offering of acreage for exploration, and relinquishment of acreage by the companies;• Laying down of safety norms, framing regulations on safety in oilfield operations, prescribe pollution control measures, and assist in inspection and periodic safety audits.
To review:	<ul style="list-style-type: none">• Exploration plans and development plans for commercial discoveries of hydrocarbons of companies, and advise GoI on their adequacy;• Review and audit concurrently the management of petroleum reservoirs on operating companies, and advise on mid-course correction required to ensure sound reservoir management;• Re-assess hydrocarbon reserves discovered and

estimated by operating companies (in discussion with them).

In September 2006, MoPNG issued a fresh notification, indicating that the DGH shall exercise the following powers and functions:

- Monitoring upstream petroleum operations in India;
- Review and monitor the exploration programme and development plans for commercial discoveries of hydrocarbon reserves proposed by licensee/ lessee, with a view to optimising hydrocarbon recovery from a reservoir;
- Review management of petroleum reservoirs by licensee/ lessee and advise them;
- Ask for and maintain data, reports, information and samples (i.e. a data repository) from petroleum E&P;
- Review reserves discovered by licensee/ lessee;
- Lay down norms for declaration of discoveries; and
- Exercise powers of Gol under Rules 24, 25, 26 27 and 30⁶⁰ of PNG Rules

In our view, the roles and functions of DGH encompass two sets of functions with potential conflict of interest – an upstream regulatory function, and a function of rendering technical advice to Gol. While in 1993 (when DGH was set up), there was lack of adequate clarity on the role and position of regulators in various economic sectors, the need for clear autonomy of sectoral regulators (from the Executive) is now well recognised.

Consequently, we recommend that the functions currently discharged by the DGH be clearly demarcated. The technical advisory and related functions should be discharged by a body completely subordinate in all respects to MoPNG (either a cell/ attached office/ subordinate office within the MoPNG or a separate entity under MoPNG). Functions of a regulatory nature (review of hydrocarbon reserves and reservoir management, laying down of norms for declaration of discoveries, laying down safety and related norms and conducting safety inspections/ audits etc.) should be discharged by an autonomous body, with an arm's length relationship with Gol.

⁶⁰ These relate to preservation of cores and samples, directions to prevent waste, spacing of wells, restriction of production, and suspension of production.

7.2 Exploration/ Appraisal Issues

7.2.1 Irregular declaration of entire contract area of KG-OSN-2001/2 (Operator: RIL) as discovery area

In February 2007, the Operator exercised his option (under the PSC provisions) of not entering Exploration Phase-II at the end of Phase-I (March 2007), after availing two extensions of 6 and 5 ½ months. Instead, he irregularly declared the entire contract area of 210 sq. km. as 'discovery area' (although there were only two discoveries in the contract area) and decided to continue appraisal activities in the whole contract area. Subsequently, in September 2007, the MC approved a resolution to allow 15 months time up to 15 June 2008 for completion of the appraisal programme and to retain the whole area.

We noted that:

- The block was divided into two geographical parts (Part 'A' and Part 'B'). Out of the four wells drilled in the block, two wells (one in Part 'A' and the sole well drilled in Part 'B') were dry wells. Thus, treatment of the whole area as a 'discovery area' was irregular.
- Even though the contractor did not give a firm proposal for drilling of appraisal wells, he was still allowed to retain the whole of the contract area, purportedly for appraisal of two discoveries.
- Since the appraisal programme could not be completed by 15 June 2008, the contractor requested (July 2008) for further extension of four months up to 15 October 2008. Instead of taking action for relinquishment of area, DGH recommended (July 2008) to MoPNG for grant of further extension. MoPNG refused to grant extension and, in December 2009, asked for relinquishment with effect from 15 June 2008.
- The contractor avoided executing the MWP of drilling of four wells of depth 3500 metres/ basement each, which was a contractual obligation under Exploration Phase-II, by the simple expedient of opting out of Phase-II. Simultaneously, he managed to retain the entire contract area and avoid any relinquishment, by designating the entire block as 'discovery area'.

In reply, MoPNG stated (July 2011) that:

- The proposal for appraisal programme for the discoveries D-24 and 25 (in part "A") was submitted on 12-07-2006⁶¹, and also included declaring the whole area as discovery area.

⁶¹ Incidentally, this is just one day after the meeting of the MC of KG-DWN-98/3 on 11 July 2006, which agreed to the declaration of the entire contract area as discovery area.

- During submission of this proposal, Contractor had drilled two wells (D-24 & 25) and drilling of 3rd well was in progress in Part-A of the block. Since all the three wells were drilled in part-A, the area for retaining both part-A & B could not be decided. Accordingly, in the MC meeting held on 1 November 2006, it was decided that the contractor may drill one well in Part-B and on the basis of the results of the well in Part-B, the decision to appraise both Parts-A & B could be taken. Subsequently, the Contractor on 02-05-2007 indicated that drilling of one well (KGIII6-B1) in Part-B on 28-12-2006 indicated the presence of hydrocarbons during drilling.
- ***The validity of the geological model in conjunction with petroleum system modelling can only be proved by drilling of wells.*** Sometimes, drilling setbacks necessitate revisiting the geological model which becomes a continuous process till the production stage of a field. Even a dry well/or well with minor hydrocarbon indication does not necessarily write off an area. In the current case, the contractor had claimed that the dry well in part B of the area (where HC indication was encountered during drilling) was due to non-entrapment and non-sealing nature of the fault, which did not mean that the area was devoid of hydrocarbon; even possibility of missing the hydrocarbon zone by a whisker always existed in rollover set up.

In the case of KG-DWN-98/3, DGH was essentially of the view that drilling of wells (and successful discoveries) in all parts of the contract area was not necessary for declaration of the entire contract area as 'discovery area'. In this case, the argument for declaring the entire contract area as 'discovery area' was that while the validity of the geological model can only be proved by drilling of wells, a dry well does not necessarily mean that the area is devoid of hydrocarbons. These responses are evidently contradictory.

- The contractor had acquired 3D seismic in the whole area in excess of the committed MWP, which indicated that there was geological continuity in the two parts of the block.
- The area of Part 'B' of the block was about 78 sq. km. Relinquishment of an area of that size might not be useful for offering in bidding rounds, particularly in offshore area. On the contrary, carrying out of appraisal activities might give a chance to establish the continuation of similar hydrocarbon pool.
- MC had allowed retention of the entire/most of the contract area as discovery area (for appraising discoveries) in the case of ONGC operated block KG-DWN-98/2 and Focus Energy operated RJ-ON/6.

However, the observations made by CAG would be taken for guidance for future cases.

- As there was no provision for extension in submission of DoC, the case was recommended to MoPNG, validating the technical justifications submitted by the Contractor. Eventually, since the contractor in the block had not opted to enter the second exploration phase and DoC in respect of D-24 and 25 discoveries was not submitted within the stipulated timeline and there was no provision for extension of Appraisal Phase under the PSC, the contractor was asked on 30 December 2009 to relinquish the block with effect from 15 June 2008.

7.3 Non-compliance to PSC provisions regarding notification of discovery and submission of test reports

We found non-compliance to provisions regarding notification of discoveries in respect of KG-OSN-2001/2 block, as detailed below:

- Without first furnishing the initial particulars of the two discoveries viz. Dhirubhai-24 and Dhirubhai-25 in writing to the MC and Government, the Operator had directly given written notifications regarding potential commerciality of the discoveries.
- In the case of Dhirubhai-24 discovery, tests were completed on 4 February 2005, but the Contractor submitted the report and its opinion regarding potential commerciality to the MC on 15 December 2005 i.e. after a delay of more than eight months.

While agreeing to the audit observation regarding non-furnishing of notification of the two discoveries D-24 and D-25, MoPNG in its response (July 2011) stated that although the contractor did not provide the notification, DGH representative was present during the testing of the wells.

As regards the delay in submission of the test report, MoPNG stated that the delay occurred due to analysis of detailed testing results after observation of positive indication of hydrocarbon in well D-24, and, subsequently, results were confirmed by drilling of one more well (D-25). But the post-discovery timelines w.r.t. D-25 discovery was not compromised. MoPNG further mentioned that this practice had since been streamlined, and proper discovery notifications as per PSC provisions were being monitored.

7.4 Delay in submission/ review of appraisal programme

We noticed deficiencies relating to appraisal programme in respect of KG-OSN-2001/2 block

Block	Deficiencies
KG-OSN-2001/2 (Operator: RIL)	<ul style="list-style-type: none"> • Appraisal Programme and Work Programme and Budget (WP&B) were submitted after a delay of 3 and 16 months respectively.

Block	Deficiencies
	<ul style="list-style-type: none"> Appraisal Programme and WP&B were reviewed after delays of 13 and 8 months respectively. <p>In its reply (July 2011), MoPNG stated that there was a stipulated time period in PSC for submission of declaration of commerciality after carrying out appraisal programme. Since the time period for submission of commerciality was fixed, contractors had to carry out appraisal programme and then submit DoC as per PSC period. Hence, delayed submission of appraisal work programme and budget may not affect the timeline prescribed in PSC for submission of DoC. However, the observation made by audit in this regard was noted and would be followed for future cases.</p> <p>While we take note of MoPNG's reply that they had noted the audit observation, in fact the PSC provisions were not adhered to.</p>

7.5 Submission of Development Plan

Article 9 of Hazira PSC stipulates that within 90 days of the effective date (signing of PSC i.e. September 1994), contractor was required to submit a Comprehensive Development Plan. However, the contractor submitted the Field Development Plan after a delay of seven years.

In reply (July 2011), MoPNG stated that at the time of award, the field had GIIP of 1.9 BCF and only one gas well (Hazira – I) onland as per Information Docket. Generally, the extent of the field could not be ascertained on the basis of one well data. Field delineation was required to prepare the development plan.

The reply appears to be an afterthought, since such views were not found / recorded in the Minutes of Meeting of MC / records produced to audit at DGH.

7.6 Operating Agreement

The PSC provisions stipulate that within 15 days of the effective date (i.e. the date of signing of the PSC or the date of grant of the PEL, whichever is later)⁶², the companies constituting the contractor should execute an Operating Agreement; a copy of this agreement is to be furnished to the Government. We found that:

⁶² or such longer period as agreed to by Government.

- In the case of the MB-OSN-97/3 block (operator: RIL), we could not find documented evidence of a copy of the agreement being provided by the operator to the Government;
- Operating Agreements were executed after delays in CB-ONN-2000/1 block (4 months), KK-DWN-2000/2 (3 ½ months) and MB-OSN-2004/2 (2 months).

In reply, MoPNG stated (July 2011) that the Operating Agreements were made among the consortium partners. In our opinion, since the provision is stipulated in the PSC to which Gol is also a party, DGH is required to monitor adherence to all

7 Management Committee

The NELP PSCs provide for nomination of two Gol representatives on the MC. Till 2007, DGH was nominating two of its officers as Gol representatives on the MC. However, in March 2007, MoPNG clarified to DGH that:

- The main objective of delegation of powers was to utilise the technical expertise of DGH for better management of petroleum reservoirs and to function as a repository of relevant technical data;
- Approving payment for contractors such as unfinished committed work programme under the PSC and accepting such payments on behalf of Gol fell within the purview of Gol.

Accordingly, MoPNG appointed its officers as one of the two Gol representatives on the MC, with the other representative from DGH.

While forwarding (July 2011), the response of the operator of KG-DWN-98/3 to the draft audit findings, MoPNG has clarified the following:

- **The interpretation of the operator that decisions taken by members representing Gol on the MC is construed to be the approval of Gol is not correct. The PSC clearly identifies the difference between the approval of members representing Gol on the PSC, and the approval of Gol of the sovereign State. The PSC further clarifies that the MC shall not take any decision without prior approval of Gol, where such approval is required.**
- **The operator's statement that all procurement transactions are approved as per procedures defined by the operator and approved by the MC, is thus incorrect and should not be taken cognizance of.**
- **The approval of procurement procedure and the Development Plan, which is within the purview of MC approving functions cannot be construed to be approved by the Gol.**

uction.

We are fully in agreement with the MoPNG's stand that the approval of MC (including Gol representatives thereon) and approval by Gol are entirely different and distinct activities under the PSC provisions, and cannot be confused. This is, in a sense, similar to the participation of Gol nominee/ representatives directors on the PSU Board of Directors; approval of decisions/ actions by the PSU Board (including Gol nominees/ representatives) cannot be construed as approval by Gol.

Notwithstanding the above position, the importance of Gol representatives on the MC cannot be understated. Most actions, which would have a material impact on Gol's financial take, are taken at the level of MC (and not the Gol). Hence, the role of Gol representatives on the MC in protecting Gol's financial interests (besides ensuring sound technical management and guidance – appropriate reservoir management etc.) is critical.

However, we found numerous deficiencies in compliance with the PSC provisions relating to the Management Committee relating to frequency of meetings, circulation of notice and agenda to the members, and finalisation of minutes of meeting:

- Out of 20 PSCs scrutinised by us, we found that MC meetings were not conducted as per the prescribed frequency in respect of 7 PSCs (KK-DWN-2003/1, RJ-ONN-2002/1, RJ-ON/90/1, CB-OS/2 and CB-ONN-2000/1, Mid & South Tapti and Panna-Mukta). Further, due to incomplete records/ incorrect numbering of the MC meetings/resolutions and non-availability/ non-production of complete minutes/resolutions, frequency of the meetings could not be verified in respect of 5 PSCs (Hazira, KG-DWN-98/3, MB-OSN-97/3, NEC-DWN-2002/1 and MN-DWN-2004/3).
- Adherence to the prescribed procedure regarding issue of notices, circulation of provisional agenda and finalization of minutes of meeting in a time bound manner could not be ascertained due to incomplete records in respect of 8 PSCs (Hazira, CB-OS/2, KG-DWN-98/3, KG-OSN-2001/2, MB-OSN-97/3, NEC-DWN-2002/1, MN-DWN-2004/3 and RJ-ON-90/1).

In response to an audit enquiry as to why only 12 MC meetings were held in respect of RJ-ON-90/1 block between May 1995 and June 2009, DGH stated (February 2010) that it was handling about 250 PSCs and about 350 MLs with manpower strength. Hence, it was not always possible to strictly adhere to the time schedules of MC meetings.

Further, MoPNG, in its reply, stated (July 2011) that MC had been granted specific roles under PSC provisions and adequate meetings were held so as to ensure the role of MC. Depending on the circumstances, issues and operational requirement, MC meetings were held. Further, profit sharing mechanism was well defined in the provisions of PSC and the quantum of profit flows from the books of accounts.

Auditors were also deployed by Government to get assurance on the integrity of books of account.

A profit-sharing mechanism (as envisaged in these PSCs, as opposed to a simple royalty formula) necessitates constant oversight and monitoring, with the role of the government representatives on the Management Committee becoming critical. Once this mechanism has been accepted by MoPNG and operationalised in contractual form, it is incumbent on MoPNG and DGH to ensure that these controls work effectively and in a timely manner.

7.8 Periodical Reporting

As per the PSC, the contractors were required to submit, within the prescribed time limit, annual and quarterly reports to DGH covering various aspects such as:

- annual local procurement statements outlining their achievements in utilizing Indian resources;
- quarterly statements of costs, expenditures and receipts;
- quarterly cost recovery statement; and
- end of year statement etc.

Test check of records, however, revealed deficiencies in this regard in respect of 13 PSCs KK-DWN-2003/1, MB-OSN-97/3, KG-DWN-98/3, KG-OSN-2001/2, MN-DWN-2004/3, NEC-DWN-2002/1, CB-OS/2, Hazira field, CB-ONN-2000/1, CB-ON/1, KK-DWN-2000/2, MB-OSN-2004/2 and RJ-ONN-2002/1. Details are given in **Annexure 7.1**.

In reply, MoPNG stated (July 2011) that the operators had been submitting reports on utilization of Indian Resources, Quarterly Profit Petroleum Statement, End of Year Statement, Monthly Report etc. However, the reply is not specific to the deficiencies pointed out by audit.

7.9 Financial Issues

7.9.1 Submission of bank guarantee, financial and performance guarantee and legal opinion

As per PSC provisions, the contractors were required to submit (a) a bank guarantee (b) performance guarantee of the parent company⁶³ (c) and a legal opinion that the guarantees were legally valid, enforceable and binding. If these were not submitted in time, the PSC may be cancelled by the Government with written notice of 90 days. Further, the bank guarantees were to be renewed at least 30 days before the expiry

⁶³ or where there is no performance guarantee, from the company itself

of the guarantee period. However, we found deficiencies/ delays in the submission of these guarantees, as summarised below:

Block	Deficiencies
MB-OSN-97/3	<ul style="list-style-type: none"> • There was a delay of 5 months in submission of performance guarantee and legal opinion by RIL • Niko Resources did not furnish the performance guarantee and legal opinion. It submitted the Bank Guarantee (with 5 months' validity only upto 15 May 2002) after a delay of 18 months; also, from the available documentation, we could not verify whether the guarantee was renewed till 18 July 2003 i.e. the date of assignment of Niko Resources' participating interest to RIL.
KG-OSN-2001/2	<ul style="list-style-type: none"> • The contractors - HEPI and RIL - submitted the guarantees after a delay of 82 and 17 days respectively. Further, the bank guarantee submitted by HEPI, which had expired on 31 March 2004, was not got renewed after the expiry date. <p>In reply (December 2008), DGH stated that HEPI submitted a proposal to the Government for assignment of 10 per cent of its Participating Interest (PI) to M/s RIL on 14 June 2004. This proposal was processed at DGH and was under consideration of MoPNG; approval of assignment of PI was communicated by Government on 15 March 2005. Since the PI was proposed to be transferred to RIL, HEPI did not renew the guarantee. The reply is not acceptable, as this was not in compliance with the PSC provisions, and in any case, the renewed bank guarantee could be released after transfer of PI.</p>
NEC-2002/1	<ul style="list-style-type: none"> • The contractors - RIL and HEPI - submitted the performance guarantee after delays of 5 and 2 months respectively. Further, HEPI submitted the bank guarantee after a delay of 3 months; also, the bank guarantee was renewed, after its expiry, only up to 14 July 2006 instead of 22 July 2008.
KG-DWN-98/3	<ul style="list-style-type: none"> • From the available records, we could not verify whether the requisite guarantees were submitted by Niko Resources.

Block	Deficiencies
MN-DWN-2004/3	<ul style="list-style-type: none"> There was a delay in submission of performance guarantee and legal opinion of 2 months by RIL.
CB-ONN-2000/1	<ul style="list-style-type: none"> There were delays in submission of performance guarantee and legal opinion of 2 and 4 months by GSPC and JTI respectively.
Panna-Mukta and Mid and South Tapti	<ul style="list-style-type: none"> RIL did not submit the bank guarantee and performance guarantee.

In reply (July 2011),

- MoPNG stated (July 2011) that a strong system for monitoring the requisite guarantee was currently in place.
- Without responding to the deficiencies pointed out by audit, MoPNG mentioned that MB-OSN-97/3 and KG-OSN-2001/2 blocks had been relinquished. No justification was also given in respect of NEC-2002/1, MN-DWN-2004/3 and CB-ONN-2000/1.
- As regards KG-DWN-DWN-98/3, MoPNG sent only a copy of Financial and Performance Guarantee, copy of legal opinion and bank guarantee were not furnished.
- As regards Panna-Mukta and Mid and South Tapti, MoPNG stated that since RIL did not have a parent company, they were not required to submit the financial and performance guarantee. The reply is not tenable, as Article 29.1 of the PSC clearly stipulated that each of the companies was required to submit a financial and performance guarantee

7.9.2 Non-submission of Insurance coverage

The PSC provisions stipulated that the contractors are required to obtain and maintain insurance coverage for and in relation to petroleum operations⁶⁴ during the term of PSC and should furnish to Gol certificates evidencing that such coverage was in effect. Further, such insurance policies should include Gol as additional insured and should waive subrogation against the Gol.

⁶⁴ For such amounts and against such risks as are customarily or prudently insured in the international petroleum industry in accordance with Good International Petroleum Industry Practices

Due to non-production of records relating to insurance coverage, we could not verify whether requisite insurance coverage in respect of 7 PSCs (CB-ONN-2000/1, CB-OS/2, Hazira, KG-OSN-2001/2, KK-DWN-2003/1, MB-OSN-97/3 and MN-DWN-2004/3) was obtained and maintained by the contractors.

In reply, MoPNG stated (July 2011) that Article 24 of NELP PSC extensively deals with the insurance required to be obtained by contractors and all insurance policies include Gol as additional insured and waive subrogation against Gol. While informing that audit exceptions on insurance flagged by Gol appointed auditors were pursued and resolved, MoPNG further requested audit to advise them for any other issues to be covered in the Insurance clause. MoPNG's reply is not specific to the points raised by audit regarding non- production of records relating to insurance coverage.

Further, in the case of Panna-Mukta and Mid & South Tapti PSCs, each contractor was securing separate insurance to cover its participating interest for offshore installation with different types of risks to a different extent, resulting in non-uniformity in coverage and premium. In response (September 2010), MoPNG stated that insurance cover was essentially a business decision of the contractor, who had invested his capital upfront and aimed at protecting his investment, and was also based on the contractor's risk perception and degree of risk aversion. If the insurance policy submitted fulfilled the requirement of PSC, the policy would be acceptable to the Government. The reply is not acceptable, as MoPNG in February 2007 had instructed DGH to formulate a standardised policy for insurance coverage for consideration by Government. However, DGH had not formulated any such policy.

7.10 Royalty

- In respect of CB-OS/2 block, we found that due to delay in notification of norms for natural gas, the contractor deflated royalty payments by charging high post wellhead costs during the year 2006-07. Comparative analysis of royalty remittance statements revealed that during 2006-07, the post well head expenses ranged from 22 to 41 per cent and during 2007-08, the same ranged between just 8 and 18 per cent.
- Comparative analysis of monthly production statement and royalty remittance statement in respect of CB-OS-2 block for the month of March 2008 revealed that against the payable royalty of Rs. 7.63 crore, the licensee had paid Rs. 6.86 crore to the Government due to wrong adoption of production figure of oil for the month of March 2008. This resulted in short payment of Rs. 0.77 crore.

In response (July 2011):

- As regards the issue of deflated royalty payments, MoPNG accepted (July 2011) audit's view, indicating that DGH, through close monitoring of statutory levies, had raised these issues, which had been reported by audit.
- Regarding short payment of Rs. 0.77 crore, MoPNG intimated that ONGC, the licensee, was yet to comply with the demand for Rs.47 million and US\$ 3.8 million as short payment of royalty, and had also been advised to provide details required to calculate the short paid royalty for the years 2004-05 and 2005-06.
- MoPNG's reply does not address the specific issue of short payment of royalty due to wrong adoption of production figures of oil for the month of March 2008.

7.11 Measurement of Petroleum

PSC provisions prescribe detailed procedures to ensure accurate measurement of quantity and determination of quality of petroleum, so as to facilitate accurate Government revenue from petroleum operations, viz.

- Before commencement of production, the GoI and the contractor should mutually agree on (a) methods to be employed for measurement of volume of petroleum production, (b) point(s) at which petroleum should be measured, (c) frequency of inspections and testing of measurement appliances and relevant procedures thereto, (d) consequences of determination of error(s) in measurement.
- The contractor should give MC/ GoI timely notice of its intention to conduct measuring operations or any agreed alteration for such operations, and GoI has the right to be present and supervise, directly or through authorised operations, such operations.

However, due to non-production of complete records in this regard, we could not verify whether MoPNG/ DGH ensured strict compliance with the PSC provisions in respect of Hazira field and CB-OS-2 block.

7.12 Accounting and Auditing

7.12.1 Delayed/ non-submission of chart of accounts

As per PSC, within 90 days of the effective date, the contractor should submit and discuss proposed outline of charts of accounts and GoI should respond within 90 days. Further, Contractor and GoI should agree on chart of accounts within 180 days from the effective date. Audit, however, observed the following deficiencies in this regard:

- There was a delay in submission of Chart of Accounts in respect of CB-OS/2 (6 years), RJ-ONN-2002/1 (4 years), MB-OSN-97/3 (4½ months) and KG-DWN-98/3 (4½ months).

- Due to incomplete record provided by DGH, the fact regarding Government's response and the agreement between Contractor and Government could not be verified in respect of KG-DWN-98/3, MB-OSN-97/3 and MN-DWN-2004/3 blocks.
- Adherence of timelines in respect of any of the above three stipulations could not be verified in respect of CB-ON/1, MB-OSN-2004/2, KK-DWN-2000/2, KK-DWN-2003/1, NEC-DWN-2002/1, CB-ONN-2000/1 blocks and Hazira field, as relevant records were not made available to Audit.

In reply, MoPNG stated (July 2011) that accounts were being regularly submitted by the contractors of these initial NELP blocks in the format that is adequate to monitor the accounts. However, compliance with PSC provisions on this requirement had been streamlined in later NELP rounds.

7.12.2 Delay in submission/adoption/approval of audited accounts

As per PSC provisions, annual audited accounts were to be submitted to the MC within 60 days of the end of the year. Further, the MC was to approve the auditor's report within 30 days of submission. Audit scrutiny, however, revealed the following:

- There were delays ranging between 20 to 49 days in submission and between 1 to 9 ½ months in approval of the audited accounts in respect of 4 blocks (KG-OSN-2001/2, KK-DWN-2003/1, NEC-DWN-2002/1 and MN-DWN-2004/3). Although, no time line was provided in the PSC of KG-DWN-98/3 block regarding adoption/approval of the audited accounts by the MC after their submission, Audit noted significant delays (ranging between 8 and 20 ½ months) in approval of the accounts for the years 2000-01 to 2006-07. Details in this regard are given in **Annexure-7.2 and Annexure-7.3**.
- The process of approval and adoption of annual audited accounts had not been completed in respect of RJ-ON-90/1 (2006 and 2007) and CB-ONN-2000/1 (for 2001-02 to 2006-07). Further, the accounts of KG-OSN-2001/2 for 2007-08 were pending for adoption (November 2008) after 5 months of their submission (June 2008).
- In case of Panna-Mukta and Mid & South Tapti contract areas, the accounts had not been adopted by the MC since inception i.e. 1994-95 due to non resolution of pending Audit Exceptions.
- Timely approval and adoption of audited accounts could not be verified in respect of NEC-DWN-2002/1 (for 2005-06 and 2007-08) and KK-DWN-2000/2 (for 2002-03 and 2003-04), as supporting documents/MC Resolutions relating to adoption and approval of audited accounts for those years were not found on record.

In reply (July 2011), MoPNG stated that:

- Accounts of exploratory blocks were being adopted regularly in general. However, in some cases, due to disagreement on expenditure, work programme or related issues, the adoption got delayed. Nevertheless, the impact was immaterial, due to the fact that no cost petroleum was involved during exploration phase. We do not agree, as non-adherence to the prescribed timelines is against the spirit of PSCs.
- As regards Panna-Mukta and Tapti, there had been a wide variation in the figures indicated by the contractor and Government, and the Contractor invoked arbitration.

7.12.3 Non-compliance with GoI notified audit exceptions

As per PSCs, GoI should notify audit exceptions based on audits conducted by its representatives or CA/ consulting firms within 120 days following completion of the audit, and the contractor should answer the notice of exception within 120 days. Where the contractor failed to answer within the stipulated time, exceptions should prevail. We, however, observed that:

- In respect of CB-OS/2, DGH had not ensured compliance of audit exceptions for the years 1998-99 to 2003-04 relating to issues of policy for charging inventory to cost, parent company overheads, sale of gas etc.
- Accounts of the Panna-Mukta and Tapti JV since inception had not been approved by the Government, pending settlement of audit objections raised by the Auditors appointed by the Government.

In response, MoPNG stated (July 2011) that:

- As regards CB-OS-2, while agreeing with audit's view, the issue was being addressed in line with PSC provisions for possible reversal. CAG's advice on the issue would strengthen GoI claim.
- In respect of Panna-Mukta and Tapti, an amount of US\$ 80 million was recovered under Panna Mukta PSC in respect of short paid profit petroleum for the period 2002-06. MoPNG also proposed to recover US\$ 78 million for the year 2006-07 from Panna Mukta PSC after confirmation from CAG Audit. An amount of US\$ 0.70 million was also proposed to be recovered from Mid and South Tapti PSC, subject to arbitration.

7.13 Work Programme and Budget (WP&B)

The PSC provisions stipulate that the annual Work Programme and Budget (WP&B) for Exploration/ Development and Production Operations were to be submitted by the Contractor to the Management at least 90 days before the start of the financial

year – for review in the case of exploration operations, and for approval in the case of development and production operations. We, however, found that:

- The delays in submission of WP&B ranging from 1 to 10 months in 12 PSCs (KG-DWN-98/3, KG-OSN-2001/2, MB-OSN-97/3, NEC-DWN-2002/1, CB-ONN-2000/1, CB-ON/1, Hazira, CB-OS-2, KK-DWN-2000/2, RJ-ON-90/1, Panna-Mukta and RJ-ONN-2002/1).
- In respect of 3 blocks (KG-OSN-2001/2, KG-DWN-98/3 and CB-ONN-2000/1), Exploration & Development WP&B were reviewed/ approved after the end of the concerned financial year. In fact, in the case of CB-ONN-2000/1, the exploration budget for 2005-06 was reviewed only in March 2006 and the budget for 2006-07 was not reviewed even as of July 2008.

Block-wise and year-wise details in this regard are given in **Annexure-7.4 and Annexure 7.5** respectively.

In response to audit enquiries regarding delays in respect of the RJ-ON-90/1 block, DGH responded (October 2010) that the process of review and approval got delayed on some occasions, because of delayed submission of Operating Committee (OC)⁶⁵ approved WP&B and clarifications thereafter. Further, operations may not be stopped for want of MC's final approval; hence, in anticipation of approval, the operator continued with the work programme based on the OC recommendations.

Further, MoPNG stated (July 2011) that:

- PSC did not envisage day-to-day monitoring or oversight on the part of government representatives.
- There were instances where the operator found difficulty in placing budgets before MC as per time schedule due to factors like dispute in the operating committee stage. In RJ-ON-90/1, there had been continuous lack of agreement between ONGC, the licensee and companies, which arise out of the dispute on royalty liability. There were no quick-fix solutions for these issues.
- The operator was not permitted to drill a well before the well location was approved by DGH. The onus of obtaining MC approval lay with the operator, and work programme and associated cost not agreed were not allowed as contract cost for the purpose of profit computation. Therefore, there was adequate control over E&P operation in a license/lease area.

In our opinion, timely submission and approval of the Annual Work Programme & Budget is essential. DGH's approval for well location, before drilling, is not a substitute for regular budgetary control.

⁶⁵ Consisting of representatives of the contractors only (and not the Government)