OVERVIEW

Oil and natural gas are the largest conventional source of primary energy in the world and constitute a critical input for economic growth together with other forms of primary energy viz. hydro electricity, nuclear power and coal. In the year 2002 the worldwide consumption of primary energy was 9,405 million metric tonne of oil equivalent, of which the share of hydrocarbons was 62 per cent. Thus, it is clear that the business of exploration, production, refining and marketing of hydrocarbons, generically known as 'petroleum sector' constitutes a very vital sector in the national economy. Considering the growing importance of oil and natural gas in our economy an attempt has been made to review the performance of the Public Sector Undertakings in this sector and present a separate Report.

The Report consists of following six chapters: -

Chapter-1	Petroleum Sector Profile
Chapter-2	Follow up action on audit reviews in the last five years' Audit Reports
Chapter-3	Three reviews on some of the activities of PSUs in Petroleum Sector
Chapter-4	Paragraphs on individual transactions of PSUs in Petroleum Sector
Chapter-5	Two Reviews on IT Audit
Chapter-6	Corporate Governance in Oil PSUs

This Audit Report includes reviews on Branching and capacity augmentation of northern region pipelines of Indian Oil Corporation Limited, Arbitration cases, Production sharing contracts and IT audit in respect of re-engineering project (Manthan) of Indian Oil Corporation Limited and pay roll application in Oil and Natural Gas Corporation Limited. These themes were selected in audit for review on the basis of their relative importance in the functioning of concerned organisation. It also includes 31 paragraphs in respect of eight PSUs. The draft paragraphs were finalised after taking into consideration the replies of the Management of PSUs. The draft paragraphs were also forwarded to the Ministry of Petroleum and Natural Gas under whose administrative control the PSUs are working for its replies/comments within a period of six weeks. Replies to 20 paragraphs from the Ministry were awaited.

The audit observations included in this report highlight deficiencies in the Management of PSUs having serious financial implications. Some of these are:

Review on Branching and Capacity augmentation of Pipelines in Northern Region-IOCL

Increase in the pipe size of Mathura-Tundla Pipeline without approved proposals for extension of the pipeline to Kanpur and Gwalior and for expansion of Mathura refinery rendered the expenditure of Rs.6.20 crore on increased pipe size infructuous.

(Para 3.1.5)

Due to delayed review of the demand-supply position, the Company incurred an infructuous expenditure of Rs.2.24 crore on the capacity augmentation of the Panipat-Ambala-Jalandhar sections of the Mathura-Jalandhar Pipeline.

(Para 3.1.6)

An expenditure of Rs.66.68 crore incurred on Phase–II augmentation of Kandla-Bhatinda Pipeline was avoidable as the throughput did not at any time justify this augmentation.

(Para 3.1.9)

Encashment of the bank guarantees of the contractor in excess of requirements resulted in payment of interest of Rs.70.29 crore.

(Para 3.1.10)

Review on Performance of Production Sharing Contracts with private exploration and production companies -ONGC

Since 1991, the Government invited foreign and domestic private sector companies to participate in the development of oil and gas fields, fully/partly discovered, and the exploratory blocks. The audit results of the production sharing contracts (PSC) between the Government, ONGC and the foreign and domestic private sector companies, in respect of medium-sized fields, were examined and incorporated in the CAG's Audit Report of 1996. This report contains a follow-up of the Audit review of the issues raised in the previous Audit Report and the performance of the production sharing contracts.

(Paras 3.3.1 and 3.3.3)

The major issues of 'non-reimbursement of past costs to ONGC', 'import parity price not made applicable for gas produced by national oil companies (ONGC and OIL)' and 'non-finalisation of agreement for sale of crude oil and gas with the Government's nominees (IOCL and GAIL)' raised in the CAG's Audit Report of 1996 remained unaddressed in spite of the assurances given to Audit by the Government.

(Para 3.3.4)

Gas price allowed to different JVs was higher than the price it was sold by GAIL to consumers. ONGC was asked by the Government to meet the loss suffered by GAIL on this account and consequently it absorbed an adverse impact of Rs.4265 crore upto March 2004 in respect of five medium-sized fields.

(Para 3.3.4 ii)

The non-finalisation of the Agreements for sale of crude oil and gas led to non-recovery of Rs.277.15 crore for transportation of gas by ONGC and short payment of Rs.300.59 crore to ONGC towards processing charges in respect of Panna/Mukta gas.

(Para 3.3.5 i)

Transportation charges and processing charges in respect of Tapti field had not been finalised and the provisional tariff affected the Government/ONGC take.

(Para 3.3.5 ii)

Deficiencies in PSC of Ravva JV led to the disputes over calculation of profit petroleum, such as computation of pre-tax rate of return (PTRR) and payment of production bonus (Rs.47.56 crore) to ONGC.

(Para 3.3.5 iii)

The recovery of levies by the Government was adversely affected due to absence of defination of 'wellhead value' of gas on which the royalty was to be calculated and a provision in PSCs in deviation with draft PSCs approved by ONGC Board on payment of royalty/cess on the Government's share of profit petroleum.

(Para 3.3.6 i and ii)

ONGC was obliged to bear 100 per cent royalty in respect of pre-NELP exploratory blocks (Rs.228.78 crore upto March 2004 in respect of two blocks) irrespective of its participating interest in JVs.

(Para 3.3.6 iii)

Irregularities on individual transactions

The irregularities pointed out are broadly of the following nature:

- Undue favours to contractors/violation of contractual obligations of Rs.288.10 crore in two cases.
- Loss of revenue of Rs.82.37 crore in five cases due to weaknesses in the control systems.
- Wasteful/infructuous expenditure of Rs.65.56 crore in seven cases.
- Avoidable excess expenditure of Rs.45.69 crore in nine cases.
- Idle investment and blocking of funds of Rs.28.22 crore in five cases.

Gist of some of the important paragraphs included in the Report is as follows:

Engineers India Limited suffered a loss of Rs.2.60 crore in recommending incorrect specifications in October 1999 in the consultancy work relating to transfer pipelines.

(Para 4.1.1)

Defective planning and lack of foresight of Indian Oil Corporation Limited (IOCL) resulted in infructuous expenditure of Rs.8.95 crore in 1999-00 on replacement of pipeline with higher diameter at Kandla Port.

(Para 4.1.2)

IOCL purchased land for an amount of Rs.2.78 crore in July 1998 to set up an LPG Bottling Plant at Bhilwara (Rajasthan) without carrying out detailed feasibility study. The project was subsequently abandoned thereby resulting in blockage of Rs.2.78 crore besides infructuous expenditure of Rs.37.90 lakh.

(Para 4.1.3)

IOCL incurred an infructuous expenditure of Rs.2.17 crore during 2000-01 on an abandoned project as it decided to shift its depot from Satna to Bagha without considering liability of providing employment to local people and without entering into contract with Hindustan Petroleum Corporation Limited for sharing cost of railway siding, which were necessary for economic viability of the depot.

(Para 4.1.4)

Creation of computerised loading facilities by IOCL at Karnal bottling plant in July 1998 and September 2000 without proper planning resulted in an infructuous expenditure of Rs.2.01 crore out of which only facilities costing Rs.79 lakh only could be purposefully used.

(Para 4.1.5)

Failure to consider financial position of vendors before award of contracts and consequent delay in supply/installation of gas compressors led to flaring of low-pressure gas and consequent loss of revenue of Rs.71.02 crore during the period between August 2001 and December 2003 to Oil and Natural Gas Corporation Limited (ONGC).

(Para 4.1.6)

Imprudent decision of Bharat Petroleum Corporation Limited (BPCL) to augment the tankage capacity at Haldia refinery led to an idle investment of Rs.11.35 crore made in April 2000/March 2003.

(Para 4.2.1)

BPCL decided (February 2002) to surrender 56,779 square metres of land procured at Navalur to re-site the existing Depot at Hubli. This resulted in an infructuous expenditure of Rs.1.88 crore.

(Para 4.2.2)

Hindustan Petroleum Corporation Limited (HPCL) incurred additional expenditure of Rs.1.39 crore on outsourcing the bitumen filling work keeping its own plant idle during October 2000 to April 2004.

(Para 4.2.3)

Delay in surrender of land by IBP Company Limited (IBP) to Railways resulted in an avoidable payment of rent and other expenses amounting to Rs.3.66 crore during the period April 2000 to November 2002.

(Para 4.2.4)

The decision of IBP to take possession of an unsuitable piece of land and delay in deciding to dispose it of in July 1994 and October 1994 resulted in blockage of Rs.1.08 crore.

(Para 4.2.5)

IOCL failed to comprehensively assess the demand for low sulphur heavy stock which led to under utilisation of Storage tanks and railway siding constructed at a cost of Rs.8.40 crore and commissioned during December 1999 to March 2001.

(Para 4.2.7)

The IOCL made an idle investment of Rs.4.03 crore in the bitumen emulsion plant made in April 1999 due to improper assessment of future demand of bitumen emulsion.

(Para 4.2.8)

ONGC incurred an infructuous expenditure of Rs.38.86 crore during 1999-00 to 2001-02 in setting up offshore facilities and re-entry in a well without assessing fully the hydrocarbon potential of the gas field.

(Para 4.3.1)

ONGC incurred an infructuous expenditure of Rs.9.32 crore during 1999 on re-entry of an already drilled exploratory well due to negligence in measuring length of casing pipes and consequential short-landing of the casing in the well.

(Para 4.3.2)

Failure of HPCL to supply necessary inputs timely to the contractor resulted in Visakh Refinery loosing the benefit of Rs.14.95 crore, during 1997-98 to June 2000-01, towards price reduction for the delay in completion of the contract.

(Para 4.5.2)

Due to delay in surrendering the tank the IBP suffered a loss of Rs.1.28 crore towards its rental charges for the period from April 2001 to December 2002.

(Para 4.5.3)

ONGC awarded work for operation and maintenance of three multi support vessels to an incompetent party and suffered a loss of Rs.205.05 crore during 2001-02 and 2002-03 as poor performance of the contractor led to non-availability of own vessels.

(Para 4.5.4)

Due to delay in requesting IOCL for marketing its products within the country instead of exporting to avail benefits of excise duty exemption for north eastern refineries, the Bongaigaon Refinery and Petrochemicals Limited (BRPL) had to suffer a loss of Rs.4.09 crore for the exports made during the period March-August 2002.

(Para 4.6.1)

The BRPL failed to avail exemption of sales tax benefits on export sales and thereby incurred avoidable expenditure of Rs.1.21 crore during the period from July 2000 to August 2001.

(Para 4.6.2)

HPCL failed to avail of timely customs duty exemption, which resulted in an additional interest cost of Rs.3.36 crore during November 2001 to April 2003.

(Para 4.6.3)

IOCL transferred petroleum products to its locations outside Andhra Pradesh during April 2002 to June 2003 as stock transfer instead of requesting HPCL to execute the supplies and attracted avoidable purchase tax amounting to Rs.10.39 crore.

(Para 4.6.4)

ONGC incurred an avoidable expenditure of Rs.22.19 crore due to its failure to avail exemption of customs duty on goods imported for use in non-designated areas during the period from June 1999 to July 2001.

(Para 4.6.5)

Due to lack of proper follow up ONGC could not obtain essentiality certificate from the Directorate General of Hydrocarbons for availing the benefit of 'Nil' customs duty, which resulted in avoidable expenditure of Rs.3.82 crore in May-July 2000.

(Para 4.6.6)

Injudicious concessions extended by BRPL to a private sector company in supply of Naphtha from July 2000 to April 2002 resulted in undue favour of Rs.28.81 crore to a customer and loss of Rs.54.22 crore on account of bad debts written off in the accounts.

(Para 4.7.1)

HPCL failed to review its credit policy to Ferro Alloys Corporation Limited, which resulted in loss of Rs.3.69 crore plus interest during December 1998 to March 1999.

(Para 4.7.2)

ONGC could not realise sales dues of Rs.509.07 crore towards supply of natural gas to 33 consumers between April 1979 to May 1992 as well as interest thereon amounting to Rs.1,875.07 crore due to disputes raised by these customers in regard to the revised price of gas remaining unresolved.

(Para 4.7.3)

Some of the highlights in respect of Reviews on IT Audit

Review on Re-engineering Project (Manthan) of Indian Oil Corporation Limited

Instead of doing the rollout of the project beyond the first 99 sites by in-house expertise as per plan, the work was assigned to five outside consultants entailing an additional and avoidable expenditure of Rs.9.56 crore.

(Para 5.1.4)

Due to delay of over two years from September 2002 to November 2004 in completion of the IT re-engineering project (Manthan) the Company could not derive the projected benefits of Rs.358 crore per annum from on-line integrated business processes and optimisation in Supply Chain Management.

(Para 5.1.6)

Appointment of vendor for delivery of 'add-ons' software packages was done without inviting global tender. The bid was finalised after a delay of 25 months in evaluation of techno-commercial bid, waiving important tender conditions.

(Para 5.1.8)

The Company failed to identify and allocate Rs.20.32 crore as the cost of manpower deployed from various divisions towards implementation of the project.

(Para 5.1.9)

The Company had not been able to provide adequate training to all users for operating in the new technological environment.

(Para 5.1.13)

The Company had failed to appreciate the possible risks of not keeping the off-site data back up at site(s) other than their Primary Data Centre before 'go-live' of sites. Instances of breakdown of leased links interrupting the business transactions occurred at sites, which were not put on the three tiers Communication Network.

(Paras 5.1.14 and 5.1.31)

Although 'As Is' business processes continued to be in operation, their non-incorporation as 'To Be' business processes in the ERP Software resulted in gaps in the functionalities provided by SAP.

(Para 5.1.17)

Adequate sign-off procedures were not followed by the Company at the time of 'go-live' of SAP which resulted in uploading the data without purification. This was confirmed when Audit noticed that data in respect of lube inventory was not correctly uploaded at depot at Ajmer in December 2003 which resulted in difference of Rs.2.63 crore (May 2004) in the physical inventory and stock as per SAP.

(Paras 5.1.23 and 5.1.36)

The Management had not carried out any independent certifications. No post implementation review of the system was conducted by outside agencies

(Para 5.1.45)

The Company had not been able to identify any tangible benefits of the project so far. None of the Critical Success Factors had been achieved despite implementation of SAP at 292 sites (March 2004).

(Paras 5.1.9 and 5.1.45)

Review on pay roll application in Mumbai Region of Oil and Natural Gas Corporation Limited

There was a provision in the payroll application to store and process data relating to advances to employees and monitor its recovery with interest but due to incomplete data entry such opportunity was not used which led to creation of incomplete and unreliable database.

(Para 5.2.9)

Over payments and short recoveries of various allowances and advances to the staff illustrated weakness in payroll system being operated by Mumbai Region. This resulted in an excess and irregular payment/short recovery totaling Rs.4 crore during 2001-02 out of which an amount of Rs.12.18 lakh has been recovered subsequently by the Management after having pointed out by Audit.

(Para 5.2.11)