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File No. O-22015/55/2014-ONG-IV/EO
Government of India
Ministry of Petroleum & Natural Gas

New Delhi, August 30, 2016

To,

The Chairman & Managing Director,
CAIRN India Ltd.,
DLF Atria, Phase-2, Jacaranda Marg
DLF City, Gurgaon – 122002.
Haryana, India

Subject: Draft Audit exceptions in respect of KG-ONN-2003/1 for the Year 2013-14

Sir,

I am directed to refer to Auditor's Reports on the subject cited above and to forward the following exception for taking necessary action:

Exception No. 1: Functioning of MC Meetings

a. Number of meetings held:

As per Article 5.2 of JOA, The Operating Committee shall meet at least once every six (6) months during the exploration period.

As against the above requirements, only one OC meeting was held in the year 2013-14 on 31.10.2013.

As per Article 6.7 of PSC, The management Committee shall meet at least once every six (6) months during the exploration period.

As against the above requirements, only one MC meeting was held in the year 2013-14 on 06.08.2013.

b. MC members:

As per Article 6.2 of PSC, Govt. shall nominate two (2) members representing Govt. in the Management Committee, whereas each company constituting the contractor shall nominate one (1) member each to represent company in the MC.

According to the information provided to us, only one member representing Govt. has been appointed but the minutes of MC meeting were signed by two members of Govt.

Recommendation: Under the PSC & JOA, the Management Committee and Operating Committee is constituted for the purpose of proper performance of Petroleum Operations and conduct of less MC/OC meetings than required under PSC/JOA would adversely affect the Governance mechanism and monitoring of PSC/JOA. Minimum meetings as per PSC & JOA must be conducted. The nomination and appointment of MC/OC members should be strictly as per PSC/JOA.

Shri A. Kumar H
San K. C. [Signature]
02/07
31/8

15215/2016/PS-Cell-Dr
31/8/2016
[Stamp: DIRECTOR, PETROLEUM & NATURAL GAS, GOVERNMENT OF INDIA]

DGH Comments: Operator needs to explain the exception raised by the Auditor.

Exception No. 2: Actual Vs. Budget

Original Budget, Revised Budget and actual expenditure for FY 2013-14 is furnished below:

(US\$)				
Fin. Year	Expenditure Description	Original Budget	Revised Budget	Actual expenditure
2013-14	Geological & Geophysical Support	3,243,441	3,243,441	3,579,222
	Analysis, Studies & Investigation	1,500,000	1,500,000	207,344
	Rig Mobilisation / Demobilisation	4,256,000	4,295,707	4,089,844
	Drilling preparation / Close Out	484,128	484,129	228,579
	Drilling-Tangible and Intangible	51,649,463	65,416,813	61,837,138
	General & Administrative Costs	1,185,999	1,186,000	967,599
	FDP Preparation		800,000	
	PEL / License Fees	24,231	24,231	20,089
	Overheads	693,433	774,753	914,253
	Total Expenditure	63,036,696	77,725,074	71,844,070

It can be inferred from above analysis that the actual expenditure is far below the revised budgeted expenditure for 2013-14 and above the original budget estimate for 2013-14, indicating that the activities were not in commensuration with the financial budget prepared.

Recommendation: The operator should prepare budget as per proper planning.

DGH Comments: All actuals more than budget need to be approved by MC.

Exception No. 3: Delay in Submission of Local Procurement Statement

As per clause 10.2 of Appendix C of PSC, "The Local Procurement Statement shall be submitted to the Government within sixty (60) days after the end of each year."

During the course of audit, it was observed that the Local procurement Statement for the year 2013-14 was submitted to the Government on 13.06.2014, whereas the due date for the same was 30.05.2014.

Recommendation: It is recommended to timely submit the documents so required to the Govt.

DGH Comments: Operator needs to ensure submission of all documents in time.

Exception No. 4: Delay in Recovery of Cash Calls

As per Article I of EXHIBIT "A" accounting procedure of JOA, Operator shall issue when it deems appropriate, but in any case no more than once per calendar month, cash call (cash calls) notices to the parties at least (30) days prior to the date on which the parties have to make available to operator the required funds (due date).

During the course of review of the cash calls raised for the financial year 2013-14, it is observed that there were delays in receiving the cash call amounts from the consortium partner.

The detail of the cash call raised and cash call paid by the parties and the delay on Cash Calls of the 3 defaulting Parties is as follows:

A) For Cairn India Ltd.

Cash Call raised (Rs.)	Date of Cash Call raised	Due date	Cash Call received (Rs.)	Date of payment	Delay (days)
93,007,313	26-Mar-13	20-Apr-13	93,007,313	22-Apr-13	2
144,099,970	10-Jun-13	10-Jul-13	144,099,970	16-Aug-13	37
574,048,066	13-Jul-13	12-Aug-13	574,048,066	13-Nov-13	93
253,532,486	05-Oct-13	04-Nov-13	253,532,486	29-Nov-13	25
246,057,824	10-Nov-13	09-Dec-13	246,057,824	13-Jan-14	35
231,430,905	09-Dec-13	11-Jan-14	231,430,905	07-Feb-14	27
244,955,205	06-Jan-14	05-Feb-14	244,955,205	21-Feb-14	16

B) For ONGC

Cash Call raised (Rs.)	Date of Cash Call raised	Due date	Cash Call received (Rs.)	Date of payment	Delay (days)
96,803,530	26-Mar-13	20-Apr-13	96,803,530	26-Jun-13	67
149,981,587	10-Jun-13	10-Jul-13	149,981,587	27-Sep-13	79
597,478,600	13-Jul-13	12-Aug-13	597,478,600	27-Sep-13	46
263,880,750	05-Oct-13	04-Nov-13	263,880,750	29-Nov-13	25
256,101,001	10-Nov-13	09-Dec-13	-	-	Above 112
240,877,064	09-Dec-13	11-Jan-14	-	-	Above 79
254,953,377	06-Jan-14	05-Feb-14	-	-	Above 54

Recommendation: Cash Calls must be raised and received as per PSC/JOA provisions.

DGH Comments: Operator needs to settle the issues between the contractors.

Exception No. 5: Delay in Adoption of Annual Accounts

In terms of Article 25.4.3 of PSC, the Contractor shall submit the audited accounts to the Management Committee for approval within sixty (60) days from the end of the year. The Management Committee shall consider and approve the auditor's report within thirty (30) days after the submission of such report.

The actual date of submission / approval by MC for FY 2013-14 is as given below:

Fin. Year	Due Date	Date of approval by MC of the Audited Accounts	Delay (days)
2013-14	30.06.2014	02.02.2015	217

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Recommendation: It is recommended to adopt the annual accounts in accordance with the time limits prescribed in PSC.

DGH Comments: Annual Accounts are required to be adopted as per PSC provisions.

Exception No. 6: Submission of Audited Accounts to Govt. without MC approval

In terms of Article 25.4.4 of PSC, copy of the Auditor's report shall be submitted to the Govt. within thirty (30) days after the approval of the Management Committee.

It was observed that the contractor have submitted Auditors Report to Govt. without approving the same from the Management Committee.

The actual date of approval by MC and submission to Govt. for FY 2013-14 is as given below:

Fin. Year	Date of Submission to Govt.	Date of approval by MC
2013-14	30.06.2014	02.02.2015

Recommendation: It is recommended to submit the annual audited accounts to Govt. only after the approval of the same in Management Committee.

DGH Comments: Reasons for non compliance need to be reported.

Exception No. 7: Statements

The operator prepares a Statement of Sources and Application of Funds as at 31st march every year. The operator also prepares certain Statements (Format 1, 2, 2A, 3, 4, 5 and 5A) under the requirements of Director General of Hydrocarbons of India (DGH) and the production Sharing Contract (PSC).

Our perusal of the Report for the above year revealed that the Auditors had not given the Statements (Format 1, 2, 2A, 3, 4, 5 and 5A) strictly as per format prescribed by DGH for such statements is different from what the operator has submitted. Several heads which are present in format prescribed by DGH are not mentioned in statements prepared by auditor due to the Nil amount. The details are given in Annexure-1.

Recommendation: It is recommended to strictly follow the formats prescribed by DGH.

DGH Comments: Reasons for non compliance need to be reported. Corrective action required.

Exception No. 8: Disclosure of Significant Accounting Policy in financial Statement

The financial statements of the operator have, in significant accounting policy, disclosed that the expenditure is accounted in Joint Venture books on accrual basis.

However, the License fee is accounted in Joint Venture books on paid basis. But, there is no disclosure given regarding this license fee in the financial statements.

Recommendation: It is recommended to give disclosure that the License fee is accounted on paid basis in significant accounting policy.

DGH Comments: Disclosure needs to be made as suggested.

Exception No. 9: Internal Audit

The operator has a policy of conducting the Internal Audit of the company, as a whole (Cairn India Ltd.) which has multiple Blocks where they are the operators / partners. The Internal Audit is planned function-wise as per the policy of the company as per a schedule approved by the company's Board. As a result of such a policy, there are financial years when certain Blocks in the company may not get subjected to internal audit at all and at times only a particular function in the block is subjected to audit. Although, for the company as a whole such a policy to get a function-wise audit may be meeting the intent and requirement of law, however considering that the company is in Oil business and the business model is such that all exploration business is carried out as per Blocks awarded and PSC executed for individual Blocks, the company's policy relating to internal audit program may have to be amended so as to ensure that Block-wise internal audit is conducted as per a periodic schedule.

The argument to conduct Block-wise Internal Audit gets further supplemented by the fact that the entire accounting and audit system under the PSC is Block-wise and not function-wise.

Recommendation: The company needs to supplement / amend its Internal Audit Program to ensure that all the Blocks get covered under Internal Audit by probably planning the audit Block-wise as well as function-wise.

DGH Comments: Operator needs to explain the exception raised by the auditor.

Exception No. 10: Time and Cost Allocation

Based on the information and explanation given by the management and as stated by the Statutory Auditors of the Block, the allocation of personnel, common and other general administrative costs is based on procedures set out by the Operator and the basis of allocation is certified by the auditors of the operator.

It was observed that the formal report of the auditors was addressed to the company as a letter and is not a certificate.

Further, the letter does not in any way certify or assure that the procedure set out by the operator for such allocation is correct and as per industry practice. As per the letter the auditors have restricted their 'comments' and scope, to carry out procedures as given in the Annexure of the report, only and that they have found that allocation is based on costs incurred and recorded by the company and is 'in all material respects' in accordance with the procedures given and payroll costs are as per Operators Personnel Policies. Hence, clearly they have not examined or tested the applicability or correctness of the procedures themselves.

Still further, the letter carries various disclaimers in Para 5, 6 & 8 that dilute the very purpose of the engagement / assignment.

Recommendation: The Operator needs to ensure that they obtain a formal certificate for the assignment and other similar assignments in the future. It may be pointed out that the operator is specifically giving that a certificate is obtained in Note 5 of Schedule 5. Further, the certificate should clearly state that the basis of allocation of costs is correct and as per prevalent industry practice and that ALL costs have been allocated as per that practice. In our opinion in case such an exercise / certificate is diluted then the very purpose of the

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exercise is defeated and it may not be able to provide the relevant comfort to the Management Committee or Auditors.

DGH Comments: Proper certificate need to be obtained giving proper reasoning for correctness of the procedure adopted for allocation of time & cost.

Exception No. 11: Reconciliation between the Contractors

During the course of audit, it was observed that no reconciliation is done between the contractors to the PSC.

Recommendation: It is recommended to have reconciliation done between the contractors to the PSC and the same must be signed by all the contractors.

DGH Comments: Reconciliation needs to be prepared.

Exception No. 12: Minimum Work Program (MWP)

The operator gives a brief background of the block in its Notes to Statement of Sources and Application of Funds, however it was observed that it is not showing the position of the Minimum Work program (MWP) for its Blocks in the notes or anywhere else in the accounts.

Recommendation: The Company should incorporate a note on the MWP in its accounts as it is a very important commitment and the basis of operation till the block goes into development stage.

DGH Comments: Note as suggested need to be prepared.

2. The contractor is required to forward their compliance reports/further comments directly to DGH within 15 days from receipt of the letter.

Yours faithfully,



(Rakesh Mishra)

Under Secretary to the Govt. of India

Copy to:-

1. DG, Directorate General of Hydrocarbons, Noida with the request to monitor the progress and to ensure compliance of the audit exception.