Chapter

5

Internal Control System

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5.1 Introduction

In the international exploration and production business operations, partners safeguard their financial and non financial interests by ensuring a specific provision for partners' audit in the Joint Operating Agreement. The Company also followed this principle for its E&P assets acquired either through JVs or its subsidiary JVs.

In total, 29 E&P assets involving high risk and cost were acquired by the Company either through incorporated or unincorporated JVs or its subsidiary JVs, and 16 E&P assets were acquired with 100 per cent stake by itself or through its subsidiary. As the Company is not an operator in all these cases, it has to ensure that the decision of Operator is in line with broad parameters as fixed by the Government/other agencies and the assets acquired through JVs are secured. Hence, for such arrangements, internal control mechanism needs to be robust and should have inbuilt checks and balances on transactions/operations. Therefore, the rights, powers and periodicity of partners' audit as defined in the Joint Operating Agreements should be timely and effectively exercised by the Company either through its internal audit wing or through an external agency. As the Company was a non-operator in a majority of E&P assets and relied on the decision of the operator, there was a risk of losses arising out of unilateral imprudent decisions by the operator. Hence, in order to secure its interests, the Company should have a system of identification of key risks, mitigation plan as also monitoring of implementation and review.

The Ministry stated (October 2010) that a risk register consisting of ten risks along with the root causes and mitigation factors was compiled with the involvement of M/s KPMG and OVL team.

We do not agree with the reply of the Ministry because as per the papers furnished to Audit, while the Company had only identified the risk and mitigation factors; the action plan and implementation targets thereof were not formulated.

Inadequacies noticed in audit in the internal control system are discussed in the succeeding paragraphs. These inadequacies led to irregularities not being noticed in time and consequently corrective action got delayed.

5.2 Non formulation of risk mitigation plan

Review of records revealed that the Company despite being in the high risk and capital intensive overseas exploration and production business with a total investment of ₹ 52,491.90 crore had not formulated any risk mitigation plan (August 2010).

5.3 Non-exercising of partners' audit rights in time

Review of details of partners' audit in respect of 25 E&P assets where the Company was Non/Joint-Operator revealed that in 11 E&P assets, there was an average delay of one to three years in conducting partner's audit, though there was well defined provision and periodicity for partners' audit in JOA.

In Block 6 Egypt, we noticed that delay in conducting audit by the Company was attributable mainly to non-cooperative attitude of the operator and failure on its part to assert its contractual rights. Analysis of Draft Statement of Assets and Liabilities, as on 31 December 2008, submitted by Auditors revealed that contribution of IPR Energy (Joint Venture partner) for joint operations was not in proportion to its participation interest.

- The Company contributed US$ 40.94 million against its share of US$ 34.78 million leading to excess funding of US$ 6.16 million.
- During 2008, IPR Energy transferred US$ 1.91 million out of Joint Venture account to its own different affiliated companies without intimating the Company.
- Egyptian General Petroleum Corporation (EGPC), Egypt suspended reimbursement of the cost of US$ 9.89 million incurred by the joint venture, as it was incurred without their approval or without registration of the seismic contractor with the EGPC.

The Management stated (January, 2010) that partner's audit timings are decided based on the level of activities in the project, materiality of expenditure incurred, suitability of audit window to the other non operator parties, etc.

The Ministry added (October 2010) that the observations indicated in the above para had been taken up with the operator.

In sum, the fact is that the focus of partners' audit is not always on financial aspects and sometimes irregularities relating to non financial decisions do impact the project operations. Therefore, it is very essential to ensure regular audit to provide assurance to the stakeholders. Our technical experts also opined that for conducting partners' audit; periodicity needs to be fixed.

5.4 Financial control

- ***Inadequate budgetary control***

  An examination of the internal audit report of the Company for the year 2009-10 disclosed that the budget figures mapped in SAP was either 'NIL' or more or lesser than the budget approved by the Board, which shows wrong mapping of budget in SAP which was fraught with the risk of releasing excess payment or unnecessarily rejecting the payment.

- ***Release of payment beyond financial authority***

  Delegation of financial powers of the Company empowered the Board to sanction/ approve project wise investment upto ₹ 300 crore or US$ 75 million, whichever is less.

  - In Block-5B Sudan, the Board approved the planned expenditure of US$ 56.94 million ignoring expenditure of US$ 47.53 million already incurred till the date of approval and also released ₹ 48.71 crore over and above ₹ 300 crore without obtaining prior approval of CCEA.
  - In Block 279 Nigeria, the financial commitment to the tune of US$ 96.90 million, was approved by the Board of Directors on anticipated transfer of part stake to TOTAL (French Oil Company) and Shell.

The Management stated (January 2010) that the total investment by OVL exceeded the Board's delegated power on account of deterioration in security situation in Block 5B, Sudan. After the irregularity came to the notice the same was got ratified by the Board, ECS and CCEA by disclosing all the relevant facts.

The Ministry endorsed (October 2010) the Management's reply.

We do not agree with the Ministry's reply as the system of subsequent ratification not only deprived ECS and CCEA from deliberation on the issue but also bound them to approve the same. Moreover, above instances are indicative of a weak internal control system.

Our technical consultant while agreeing with the audit opined that there should be a strong monitoring system with multi level control at operational centre in order to avoid such recurrences.

5.5 Absence of Disaster Recovery Plan and/or Business Continuity Plan

The Company does not have a documented Disaster Recovery Plan (DRP) and/or Business Continuity Plan (BCP) to enable it to respond to a disaster situation. In the event of a natural disaster or other business interruption, a comprehensive Business Continuity Plan/Disaster Recovery Plan will help the Company to continue/resume its operations in a planned manner and ensure timely recovery of the IT systems within a reasonable period of time. Absence of a Business Continuity Plan/Disaster Recovery Plan could delay any damage control exercise and may lead to significant disruption of operations causing loss of business and revenue to client operations.

The Ministry stated (October 2010) that the Company runs its business transactions on SAP which is hosted in ONGC Data Center, Delhi with Disaster Recovery center at Baroda.

The fact remains that the Company is not having its own documented Disaster Recovery/ Business Continuity Plan.

To conclude, the Company despite being in high and capital intensive business did not formulate a risk mitigation plan and also failed to conduct partner's audit in time, which resulted in irregularities remaining unnoticed/unattended by the Management. These inadequacies could be attributed to lack of documented risk management plan and absence of robust internal control system including internal audit.

Recommendation # 3

In view of its presence in 16 countries and significant investment as non-operator, the Company should strengthen its internal audit and control system and put in place timely audit arrangements for audit of the Joint Ventures.


두성