

SEVENTH REPORT

COMMITTEE ON PUBLIC UNDERTAKINGS

(2015-2016)

SIXTEENTH LOK SABHA

JOINT VENTURE OPERATIONS OF ONGC VIDESH LIMITED

MINISTRY OF PETROLEUM AND NATURAL GAS

[Action taken by the Government on the Observations / Recommendations contained in the Twenty-seventh Report of Committee on Public Undertakings on Joint Venture Operations of ONGC Videsh Limited based on Audit Report No. 28 of 2010-11 (Performance Audit)].



Presented to Lok Sabha on

Laid on the table of Rajya Sabha on

LOK SABHA SECRETARIAT

NEW DELHI

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based on Audit Report No. 28 of 2010-11
(Performance Audit).

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(2015 – 2016)

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19. Shri Muthukaruppan
20. Shri Rangasayee Ramakrishna
21. Shri C. M. Ramesh
22. Shri Tapan Kumar Sen

INTRODUCTION

I, the Chairperson, Committee on Public Undertakings having been authorized by the Committee to submit the Report on their behalf, present this Seventh Report on action taken by the Government on the Observations / Recommendations contained in the Twenty-seventh Report of Committee on Public Undertakings on Joint Venture Operations of ONGC Videsh Limited based on Audit Report No. 28 of 2010-11 (Performance Audit).

2. The Twenty-seventh Report was presented to Lok Sabha / laid on the Table of Rajya Sabha on 5 February, 2014. Replies of the Government to the Observations / Recommendations contained in the Report were received on 19 December 2014. The draft Report was considered and adopted by the Committee at their Sitting held on 9 June 2015. The Minutes of the Sitting are given in Appendix-I.

3. An analysis of the action taken by Government on the Observations / Recommendations contained in the Twenty-seventh Report is given in Appendix-II.

New Delhi
6 August 2015
15 Shravana, 1937(S)

SHANTA KUMAR
Chairperson,
Committee on Public Undertakings.

CHAPTER I

REPORT

This Report of the Committee deals with the action taken by the Government on the Observations/Recommendations contained in the Twenty-seventh Report of the Committee on Public Undertakings (Fifteenth Lok Sabha) on “Joint Venture Operations of ONGC Videsh Limited based on Audit Report No. 28 of 2010-11 (Performance Audit)” which was presented to Lok Sabha on the 5th February, 2014.

2. Action Taken notes have been received from the Government in respect of all the twenty-one Observations / Recommendations contained in the Report. These have been categorized as follows:

- (i) Observations / Recommendations which have been accepted by the Government (Chapter II)
Sl. Nos. 1,5,6,7, 8, 9, 10,11,13,14,19,20 and 21 (Total 13)
- (ii) Observations / Recommendations which the Committee do not desire to pursue in view of the Government’s replies (Chapter III)
Sl. Nos. 2,3,4, and 12 (Total 04)
- (iii) Observations / Recommendations in respect of which replies of the Government have not been accepted by the Committee (Chapter IV)
Sl. Nos. 15,16, 17 and 18 (Total 04)
- (iv) Observations / Recommendations to which the Government have furnished interim replies. (Chapter V)
(NIL)

3. The Committee desire that response to their comments in Chapter - I of the Report should be furnished to them expeditiously.

4. The Committee will now deal with the Action Taken by the Government on some of the Observations/Recommendations in succeeding paragraphs.

Recommendations Serial No. 5 and 6

Loss in acquisition of MTPN Block, Congo

5. In their 27th Report (Fifteenth Lok Sabha), the Committee observed that OVL acquired (Feb 2007) 20 per cent Participating Interest in the MTPN Block, Congo, from ENI (Operator) by swapping with ONGC’s 34 per cent PI in Block MN-DWN in India. According to the Audit, the reservations of the in house team of OVL about the operator providing 2D and 3D seismic data only for viewing purpose and the parameters considered by them for volumetrics and estimated volumes calculated being based on a 2002 interpretation were overlooked by the Company and it went ahead with the acquisition. Moreover, the decision to acquire the Block with total reserves of 634.75 MMB estimated by the operator in respect of five prioritized prospects viz. Hiti East, Hiti Central, Nkasu, Ntangu and Tehitebi was taken ignoring the disappointing results of

earlier drilled two wells viz. HTNM-1 and ZULU Marine-1 which had to be abandoned due to non-discovery of hydrocarbons. Further, the Committee noted that after revalidation of 3D data, the operator had replaced the earlier prioritized five prospects with another prospect i.e. HVAM-1 and estimated total reserve of 322.8 MBOE in 5 layers in view of the discouraging results of already prioritized prospects. However, on drilling of HVAM-1, OVL discovered only a reserve of 20.22 MBOE in one layer. The operator also could not achieve the targeted depth of 5024 meters due to operational problem as drilling was stopped at a target depth of 4,516 meters.

6. The Ministry in its action taken reply have stated that while replying to the observations of audit on this issue, the Company had submitted statement of facts in order to enable audit to have proper comprehension on the issue for arriving at informed conclusion. It may be appropriate to reiterated the said facts as given below:

- The participation of OVL in MTPN Block in Congo was under a swap deal between ONGC / OVL and ENI. The swap deal was a strategic alliance where in ONGC wanted international firms with deepwater expertise to come in as partners in India and OVL was looking for a foothold in the oil rich West African Country. OVL was in an advantageous position in terms of cost connotation to each party on the basis of past cost & carry agreed in the deal.
- After OVL's entry into the MTPN block, the 3D seismic data was reprocessed and re-interpreted which validated the earlier findings leading to prioritization of prospects for drilling by the consortium (ENI, Exxon and OVL).
- Despite two wells being dry, the well drilled in the block after OVL's entry was successful with oil find, though sub-commercial because of being located in ultra-deep water. Deviation between end result and pre-drill prediction is part & parcel of every risky exploration venture.

On the basis of the above, OVL considered the deal as a sound business decision.

7. The office of the C&AG in their vetted remarks on the aforesaid reply of the Government has stated that the Government has reiterated its reply which has already been considered by them.

8. Further, in their 27th Report (Fifteenth Lok Sabha), the Committee were not convinced by the logic extended by OVL that being a swap deal, the Company decided to carry out internal technical evaluations without appointing a third party consultant and the Company engages technical, financial and legal consultants for due diligence of only producing/discovered assets of significant value. The Committee also found untenable the other contention that as the investment in this exploration acreage was comparatively lower in comparison to discovered or producing assets, it was considered adequate to rely on in-house assessment and that the outcome of drilling a well on such prospect could result in a discovery or it may turn out to be dry (unsuccessful). The explanation of OVL that the data sources for evaluation of a block either for OVL team or third party consultant would be the same as provided by the operator is also unsound. By this strange logic of the Company, there is no need for having third party consultant in any of such projects. It is common knowledge that same set of data is open to different interpretations by different experts. The Company's alibis for selective reliance on in-house teams and third party consultant in these projects are not

convincing and raise doubts about the Company's approach. The Committee had recommended that henceforth the Company should invariably follow due diligence in all projects before acquisition. Furthermore, the mechanism of in-house evaluation and circumstances where evaluation by independent consultant would be necessary should be codified in the documented policy brought out by the Company so that in future no scope is left for subjective decisions.

9. The Ministry of Petroleum & Natural Gas in their action taken reply have stated that the human resource engaged by the Company for internal due diligence are adequately experienced with requisite skill to carry out the job. The decision to engage consultant for obtaining second opinion on exploration opportunities is taken by the company on a case to case basis depending on geological complexities (possibility of value addition), cost intensiveness and available timeframe within which decisions are to be taken. Nevertheless, to strengthen the capability of in-house technical team, OVL has resorted to four pronged action plan viz., induction of state-of-the-art software/hardware, skill enhancement of technical team through training and work association, subscribing to the professional global database for techno-commercial insight and improving knowledge management specially the intrinsic knowledge.

10. Additionally, while acknowledging the recommendation of the Committee on the issue, it is submitted that, the Company has introduced many new measures to further strengthen the acquisitions process of high risk overseas E&P assets. The policy on engagement of independent consultant and introduction of zero based risk review matrix are few of the risk-reduction measures codified in the Business Development Policy of the Company. As recommended by the Committee, due diligence is being carried out usually for all the projects.

11. The office of the C&AG in their vetted remarks on the reply of the Government has stated that the Company, in its approved BD Policy, has codified the mechanism of in-house evaluation and circumstances necessitating evaluation by independent consultant. In the codified mechanism for appointment of consultants for 'Exploratory Assets' as given under para 6.2.1 of 'Business Development policies for acquisition of oil and gas assets' of the Company, technical consultants would be appointed whenever necessary considering value, complexity or requirement of the opportunity. However, Company has not decided a maximum threshold value of investment beyond which appointment of technical consultant would be necessary for exploratory assets. Having threshold value would effectively strengthen the mechanism.

12. The Committee take note of the various measures introduced by the OVL for strengthening capability of its in house technology team and also codification of the mechanism for appointment / engagement of independent consultants for evaluation of exploratory assets, wherever necessary, in its Business Development Plan. However, the Committee found that BD Policy of the Company does not indicate the maximum threshold value of investment beyond which appointment of technical consultant would be necessary for exploration assets. The Committee, therefore, desire that OVL should suitably amend its BD Policy for fixing a maximum threshold value of investment beyond which appointment of technical consultant would be necessary so that it would effectively strengthen the mechanism. The Committee would like to be apprised

of the action taken in this regard within three months of presentation of this Report to Parliament.

Recommendations Serial No. 15 and 16

Acquisition Of Imperial Energy Corporation

13. In their original Report, the Committee had noted that Imperial Energy Corporation Plc (IEC), an E&P Company was acquired by OVL in January, 2009 for Rs. 10,320 crore. Cabinet Committee on Economic Affairs (CCEA) had approved the acquisition with the stipulation that the Internal Rate of Return (IRR) would be in the excess of 10% and an option to farm-out part of its stake to a Russian firm. As per OVL's assessment, the project was viable with average daily rate of production of 35,000 barrels for 2009 and up to 80,000 barrels per day by 2011. Due to unrealistic estimation of reserves/production, OVL has suffered a huge loss of Rs. 1182.14 crore during the period 2008-09 to 2009-10. Since OVL did not chose to farm-out part of its stake to a local partner, the entire loss has to borne out by it. Moreover, the Company has also suffered a production loss of 10.8 million barrels and has not been able to achieve the stipulated IRR of 10%.

14. The Ministry of Petroleum & Natural Gas in their action taken reply have stated that the Company has reiterated the fact that like any other new business opportunity of OVL, the acquisition of Imperial Energy was preceded by technical due diligence by the in house team of ONGC/OVL and Pangea (technical consultant engaged by OVL for technical due diligence). Also, prior to the acquisition, the reserves of the Imperial Energy were certified by DeGolyer & MacNaughton (D&M), an internationally reputed independent US based reserves audit firm. The acquisition was made considering all the above three independent reserve estimations. The projected production from the asset was based on the data from certain drilled key wells in the oilfields of Imperial Energy prior to its acquisition by OVL following standard industry procedure. It is only unfortunate that after acquisition, production from some of the fields were not as expected due to heterogeneity of the reservoirs arising out of geological complexities. The success in one of the fields i.e. Maiskoye, which has achieved higher production than pre-acquisition estimates, corroborates this fact.

15. As regards, OVL not choosing to farm-out part of its stake to a local partner, the entire loss has to borne out by it, the Ministry has stated that farm out option depends, amongst other thing; on risk reward perception & prevailing market condition. In the acquisition strategy formulated as per the conditions prevalent at the time of making the offer for acquisition of the asset in August 2008, OVL had no plan to farm out any stake of the target asset and hence no participating interest (PI) was farmed-out. However, approval of Government of India was sought for possible farming out suitable Participating Interest (PI) to Russian entity(ies) on mutually agreed terms at an appropriate time as there was an apprehension that while according approval for the acquisition, the Russian Government may put a condition of giving certain PI to a Russian entity as was done in an early case involving SINOPEC (China) in case of Udmurtneft. With regard to the possibility of achieving IRR of 10%, it may be noted that the estimated IRR at the time of asset acquisition was on cash flow basis achieved on full project life which extends over more than 20 years under licenses granted to it valid till 2028-32 (and further extendable). The achieved IRR at the end of project life would

vary based on the results of the ongoing efforts of Imperial to commercially exploit the tight oil reserves of the asset.

16. The office of the C&AG in their vetted remarks on the aforesaid reply of the Government has stated that the Company has reiterated its earlier reply which has already been considered by them earlier.

17. Observing that OVL's contention that though M/s Rosneft (a local company) initially expressed its willingness to partner in the project but withdrew from the same in October, 2008 due to various compulsions is devoid of merit as the acquisition was done only in January, 2009 i.e. three months after the withdrawal of Rosneft. The Committee in their 27th Report opined that the Ministry's admission that production levels of IEC have not been commensurate with the levels envisaged at the time of acquisition primarily due to unforeseen geological complexities from the tight reservoirs of the asset is a tacit admission of the shortcomings pointed out by the Audit in this acquisition. The Company's assertion that such reservoirs elsewhere in the world have been successfully exploited with appropriate technology and favourable fiscal (tax) regime also confirms the Committee's growing apprehensions that things are not well with this acquisition of the Company and there would be further financial implications before there is any possibility of IEC's balance sheet coming out of red. While expressing their disapproval of the Company's error of judgement in the instant case, the Committee also felt that the Ministry has also not acquitted itself well as this acquisition was beyond the powers of the Company and had been done with the approval of CCEA. The Committee, therefore desired that a comprehensive review of this acquisition and its performance alongwith its future prospects so as to arrive at a well considered decision about its future be taken. The Committee had further desired to be apprised the outcome of such a review at the earliest.

18. The Ministry of Petroleum & Natural Gas in their action taken reply have stated that it is a fact that the acquisition process for Imperial Energy was concluded in January 2009. But it may be noted that subsequent to receipt of approval of the Government on 22.08.2008 authorizing OVL to make binding offer, OVL had made a binding offer to the shareholders of Imperial Energy on 26 August 2008, subject to receipt of approval of regulatory authorities of the Russian Federation to the acquisition. Further, as mentioned in the earlier para, OVL had no plan to farm out any stake of the target asset and hence on refusal of Rosneft, there was no further effort by OVL to divest any participating interest(PI) in the venture. Post-acquisition, through focused efforts Imperial Energy was successful in ramping up the production from approximately 6000 bopd at the time of acquisition to 19200 bopd in mid-2011. However, unlocking the oil in place from the tight reservoirs with infusion of the right exploitation technology in a cost efficient manner has been the major technical challenges to the company. The company is currently engaged in pilot scale application of horizontal drilling and fracking with partnership of a US based independent E&P company having expertise in this area to exploit these reservoirs. The full-fledged application of the new technology to enhance production from the asset shall follow the ongoing pilot program based on its results. It may be noted that the earlier submission of OVL that such reservoirs elsewhere in the world have been successfully exploited with appropriate technology, had reference to the very recent technological breakthroughs made in the area of exploitation of tight oil / gas reservoirs especially the shale oil / gas reservoirs of North America. The Company believes that application of similar technology, supported by

the tax breaks offered by the host government, will help in turning around the performance of the Imperial Energy asset. The company is closely monitoring the current technology application endeavor, the results of which will decide the future action plan for the asset and the Committee will be apprised of the developments on the issue. Lessons learned would be used in future acquisition.

19. The office of the C&AG in their vetted remarks on the aforesaid reply of the Government have stated that the assurance given by the Government regarding review of the acquisition and performance of IEC asset will be watched in future.

20. The Committee are irked at the intransigent stand taken by the OVL justifying acquisition of Imperial Energy Corporation (IEC) asset. Except reiterating its earlier reply OVL has not offered any justification for its ill conceived decision not to farm-out part of its stake in IEC to local Russian firms / entities and its unrealistic estimation of oil reserves and production targets. The Ministry's claim that post-acquisition IEC was successful in ramping up production from 6000 barrels of oil per day (bopd) to 19200 bopd is woefully short of the estimated production target ranging from 35000 to 80000 bopd. The Committee have now been informed that OVL is currently engaged in Pilot scale application of a new technology in partnership with a US based independent Exploration and Production company and its full fledged application will be based on results of Pilot Programme. It has also been stated that OVL is closely monitoring the current technology endeavour brought about by technology breakthrough made in this regard in North America, the results of which will decide the future action plan for the IEC asset. The Committee express the hope that the use of new technologies in the field of exploitation of tight oil / gas reservoirs that are currently underway would help OVL to achieve turnaround in the performance of its asset. The Committee desire that they may be apprised of the progress made in this regard.

Recommendations Serial No. 17 and 18

NN Block, Qatar

21. The Committee in their 27th Report (Fifteenth Lok Sabha) had noted that OVL acquired 100% participation interest in Najwat Najem Block, (NN) Qatar and estimated the volume of Original Oil in Place (OOIP) at 187.72 million metric barrel of oil equivalent (MMBO) in spite of risk of pre-existing poor event continuity attached with its reserves estimations. Further, OVL decided to appraise the Block by itself despite knowing that about 12-16 leading E&P international oil companies were interested in the Block. This go alone decision not only deprived the Company of mitigating the impact of risk known to it, by leveraging the combined financial strength and sharing experience of the JV partners but also resulted in financial loss.

22. The Ministry of Petroleum and Natural Gas in their Action Taken Reply has stated that Company had reiterated its stand that in view of NN Block being a discovered asset, sharing of risk with Partner(s) was not in the strategic consideration of the Company. Though, many companies had shown interest for the same block, no company had approached OVL for partnership.

23. In their Original Report, the Committee had noted that being a discovered field, OVL had decided to do the field appraisal on its own. It has also submitted that it did not receive any expression of interest to farm-in in the Block from the 12 to 16 leading E&P companies which were interested in the project and decided to appraise the discovery by itself in expectation of associated reward which did not materialise. OVL has also contended that even if it had decided to take partners there could have been criticism if the project would have been successful. The Committee take exception to this convoluted set of logics extended by the Company to cover up the errors in its commercial judgement. Had the Company made any serious efforts to rope in partners, the risk factor involved in the project would have been mitigated to a considerable extent. The Committee recommend that given the high risk nature of exploration and production industry, the Company should exercise more prudence when faced with similar situations in future.

24. The Ministry of Petroleum and Natural Gas in their Action Taken Reply has stated that while agreeing with Committee's recommendation, the Company has introduced many new measures to further strengthen the acquisitions process of high risk overseas E&P assets.

25. The office of the C&AG in their vetted remarks on the aforesaid reply of the Government have stated that the measures adopted by the Company for strengthening its in-house capabilities for evaluation of investment opportunities would be watched during future audits.

26. From the Action Taken Reply furnished by the Ministry of Petroleum & Natural Gas, the Committee regret to note that OVL has not furnished any plausible explanation for neither carrying out due diligence before acquiring 100% participatory interest nor farming out its stake in NN Block, Qatar to other interested parties, so as to reduce the risk. While reiterating its earlier recommendation, the Committee desire that in respect of future projects relating to discovered fields OVL should tread with caution and exercise prudence before appraising the discovered asset entirely by itself. The Committee would also like to be apprised of the results of the measures adopted by the Company, for strengthening its in-house capabilities for evaluation of various investment opportunities.

CHAPTER II

RECOMMENDATIONS / OBSERVATIONS WHICH HAVE BEEN ACCEPTED BY THE GOVERNMENT

Recommendation Serial No. 1

Absence of an E&P Policy

The Committee are surprised to note that ONGC Videsh Ltd. (OVL), which started focusing on acquiring oil and gas assets from the year 2000, did not have a well defined policy for acquisition of Exploration and Production (E&P) assets all these years. The Ministry of Petroleum and Natural Gas also seems to have been oblivious to this serious lacuna in the policy framework of OVL throughout this period. When this shortcoming was brought to their notice, the MoP&NG initially took the stand that there was no need for such a policy. Subsequently, it was conveyed that such a policy if put in black and white would be detrimental to the functioning of the Company as its competitors would be able to predict its acquisition strategies easily. Later on, both the Ministry and the Company veered to another argument that a policy, though not documented, was always in vogue. However, surprisingly, on 17 August, 2012 i.e. just five days before the representatives of the Ministry and OVL had to testify in the matter before the Committee on 22 August, 2012, the Board of OVL met and the 'existing policy' in practice was reviewed, updated and documented as 'Business Development Policies for Acquisition of Oil and Gas Assets' and approved. The Committee while strongly deprecating the vacillation of the OVL and the Ministry in the matter, take satisfaction in the fact that a much needed corrective has been put in the System, albeit, very belatedly. Now that a documented Policy for acquisition of E&P Assets has been put in place by OVL, the Committee hope that due diligence process could be carried out to mitigate risks involved in the high risk and capital intensive Exploration and Production business

Reply of the Government

The best in class practices being employed at OVL have now been documented as guidelines in the Business Development policy to carry out due diligence and risk evaluation of investment opportunities. These practices will continue to be followed to mitigate risk involved in the high risk and capital intensive Exploration and Production business.

Remarks of office of C&AG on the reply of the Government

The Company has documented its BD policy for acquisition of oil & gas assets which was duly approved by the Board. Hence, no further comments.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 5

MTPN Block, Congo

OVL acquired (Feb 2007) 20 per cent Participating Interest in the MTPN Block, Congo, from ENI (Operator) by swapping with ONGC's 34 per cent PI in Block MN-DWN in India. According to the Audit, the reservations of the in house team of OVL about the operator providing 2D and 3D seismic data only for viewing purpose and the parameters considered by them for volumetrics and estimated volumes calculated being based on a 2002 interpretation were overlooked by the Company and it went ahead with the acquisition. Moreover, the decision to acquire the Block with total reserves of 634.75 MMB estimated by the operator in respect of five prioritized prospects viz. Hiti East, Hiti Central, Nkasu, Ntangu and Tehitebi was taken ignoring the disappointing results of earlier drilled two wells viz. HTNM-1 and ZULU Marine-1 which had to be abandoned due to non-discovery of hydrocarbons. Further, the Committee note that after revalidation of 3D data, the operator had replaced the earlier prioritized five prospects with another prospect i.e. HVAM-1 and estimated total reserve of 322.8 MBOE in 5 layers in view of the discouraging results of already prioritized prospects. However, on drilling of HVAM-I, OVL discovered only a reserve of 20.22 MBOE in one layer. The operator also could not achieve the targeted depth of 5024 meters due to operational problem as drilling was stopped at a target depth of 4,516 meters.

Reply of the Government

While replying to the observations of audit on this issue, the Company had submitted statement of facts in order to enable audit to have proper comprehension on the issue for arriving at informed conclusion. It may be appropriate to reiterated the said facts as given below:

- The participation of OVL in MTPN Block in Congo was under a swap deal between ONGC / OVL and ENI. The swap deal was a strategic alliance where in ONGC wanted international firms with deepwater expertise to come in as partners in India and OVL was looking for a foothold in the oil rich West African Country. OVL was in an advantageous position in terms of cost connotation to each party on the basis of past cost & carry agreed in the deal.
- After OVL's entry into the MTPN block, the 3D seismic data was reprocessed and re-interpreted which validated the earlier findings leading to prioritization of prospects for drilling by the consortium (ENI, Exxon and OVL).
- Despite two wells being dry, the well drilled in the block after OVL's entry was successful with oil find, though sub-commercial because of being located in ultra-deep water. Deviation between end result and pre-drill prediction is part & parcel of every risky exploration venture.

On the basis of the above, OVL considered the deal as a sound business decision.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its earlier reply which has already been considered in audit.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 6

The Committee are not at all convinced by the logic extended by OVL that being a swap deal, the Company decided to carry out internal technical evaluations without appointing a third party consultant and the Company engages technical, financial and legal consultants for due diligence of only producing/discovered assets of significant value. The other contention that as the investment in this exploration acreage was comparatively lower in comparison to discovered or producing assets, it was considered adequate to rely on in-house assessment and that the outcome of drilling a well on such prospect could result in a discovery or it may turn out to be dry (unsuccessful) are also untenable. The explanation of OVL that the data sources for evaluation of a block either for OVL team or third party consultant would be the same as provided by the operator is also unsound. By this strange logic of the Company, there is no need for having third party consultant in any of such projects. It is common knowledge that same set of data is open to different interpretations by different experts. The Company's alibis for selective reliance on in-house teams and third party consultant in these projects are not convincing and raise doubts about the Company's approach. The Committee recommend that henceforth the Company should invariably follow due diligence in all projects before acquisition. Furthermore, the mechanism of in-house evaluation and circumstances where evaluation by independent consultant would be necessary should be codified in the documented policy brought out by the Company so that in future no scope is left for subjective decisions.

Reply of the Government

The human resource engaged by the Company for internal due diligence are adequately experienced with requisite skill to carry out the job. The decision to engage consultant for obtaining second opinion on exploration opportunities is taken by the company on a case to case basis depending on geological complexities (possibility of value addition), cost intensiveness and available timeframe within which decisions are to be taken.

Nevertheless, to strengthen the capability of in-house technical team, OVL has resorted to four pronged action plan viz., induction of state-of-the-art software/hardware, skill enhancement of technical team through training and work association, subscribing to the professional global database for techno-commercial insight and improving knowledge management specially the intrinsic knowledge.

Additionally, while acknowledging the recommendation of the Committee on the issue, it is submitted that, the Company has introduced many new measures to further strengthen the acquisitions process of high risk overseas E&P assets. The policy on engagement of independent consultant and introduction of zero based risk review matrix are few of the risk-reduction measures codified in the Business Development

Policy of the Company. As recommended by the Committee, due diligence is being carried out usually for all the projects.

Remarks of office of C&AG on the reply of the Government

The Company, in its approved BD policy, has codified the mechanism of in-house evaluation and circumstances necessitating evaluation by independent consultant. In the codified mechanism for appointment of consultant for 'Exploratory Assets' as given under para 6.2.1 of 'Business Development policies for acquisition of oil and gas assets' of the Company, technical consultants would be appointed whenever necessary considering value, complexity or requirement of the opportunity. However, Company has not decided a maximum threshold value of investment beyond which appointment of technical consultant would be necessary for exploratory assets. Having threshold value would effectively strengthen the mechanism.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Comments of the Committee

Please see para 12 of Chapter I.

Recommendation Serial No. 7

AD7 Block, Myanmar

The Committee note from the findings of the Audit that the Company approved acquisition of 20% participation interest in AD7 Block, Myanmar based on the assessment of its technical team of geoscientists on 11 August, 2008. While doing so, it conveniently ignored the assessment of its Geologist and Geophysicists (G&G) Group on 18 August, 2008 which had warned that the assessment of the technical team was based on untested and un-established sand and on thin study. The G&G Group reconfirmed its earlier recommendation when it was later on asked to re-examine seismic data and drilling results of two of the wells drilled in the Block. The Company relinquished the Block in January, 2009 after incurring an expenditure of Rs. 74.99 crores.

Reply of the Government

It is submitted that, new sands were targeted for exploratory probing in Block AD-7 and these sands were not tested / established in the adjoining block A1-A3. The comments of G&G team pointed out by Audit refer to the same as 'untested' & 'unestablished', implying new sands which are the primary motivation of exploratory drilling. Hence, it is factually not correct to state that the Block was acquired against the recommendations of G&G group. There was no disagreement between the technical team and the G&G Group on either the presence or the prospectivity of G-7 sand in the Block AD-7. The G&G group is part of the overall technical team framework which carried out the due diligence. The G&G Group only expressed the limitations in estimating the resource potential and risk of G-7 sand in the Block AD-7 because of being an untested objective in the area. In exploratory areas, in general, target sands / reservoirs are not established at the time of Farm-in decisions and these only provide

the value multipliers in case proven on drilling. In the instant case, additional sands were expected besides G-7 and therefore, it would not have been appropriate to downgrade the prospectivity of the Block as a whole. Moreover, the seismic expression as observed by the G&G team depends on the thickness and the continuity of the sand over a reasonable area and is always not diagnostic.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its earlier reply which has already been considered in audit.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 8

OVL's plea that both the groups had same opinion and the G&G Group had merely expressed limitations in estimating the resource potential does not carry convictions with the Committee. Furthermore, the Committee are also not convinced by the reasoning of OVL that the decision to farm-in in the Block AD-7 was based on sound understanding of the risk-reward perception followed in the industry. The Committee feel that when there was a difference of opinion between two of its own in-house entities, OVL was bound to adopt further due diligence and extreme caution in the matter. Instead, OVL threw caution to winds and went for the acquisition in a cavalier manner. The result was obvious, as it had to relinquish the acquisition within a few months after losing substantial public funds. The Committee while deprecating the action of the Company in the instant case desire that a well laid out procedure should be evolved and put in place to decide on such difference of opinion amongst the in-house evaluations and/or between in-house and independent evaluation so as to ensure that the decisions are invariably taken in the interest of public exchequer and OVL.

Reply of the Government

The decision to participate in AD-7 block was based on interpreted exploration potential in the block by the technical evaluation team, consisting of few nominated geoscientists from the pool of geoscientists in the company. While recommending for participation in the block, the technical evaluation team was aware of the fact that the target horizon is an untested sand, as there was no well drilled in the block. As sands in similar geological set up in adjacent area were proved to be gas bearing, such risk in exploration was worth taking. It may kindly be noted that while commenting on the evaluation by the technical team, the G&G group only brought out the facts that the target reservoir is untested in the block and the assessed reserves may represent the high-case. While acknowledging Committee's concern on the issue, it is submitted that, the Company has introduced many new measures like engagement of independent consultant and introduction of zero based risk review matrix etc. to further strengthen the acquisitions process of high risk overseas E&P assets. Wherever the difference of opinion in the evaluation has emerged, management has ensured that the decisions taken are in the interest of the organization.

Remarks of office of C&AG on the reply of the Government

The Government has not accepted the recommendations of COPU as neither the BD policy of the Company has specified nor the Company has intimated about the procedure laid down, if any, in case of difference in opinions on evaluation of investment opportunity.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 9

NC-188 and NC-189, Libya

The Committee note that OVL acquired 49% participation interest in NC-188 and NC-189 Blocks in Libya and entered into farm-in agreement with Turkish Petroleum Overseas Company without further detailing or revalidation of its technical team's report from an independent consultant. It is only after drilling two wells in NC-188 Block, the Company realised that there were high exploration risks with only small limited reserve structures in the blocks. The in-house technical team in its re-evaluation of data also opined that the Block did not have any significant left over potential. The project was accordingly relinquished after incurring an expenditure of Rs. 68.51 crore.

Reply of the Government

The exploration risk is inherent in all exploratory drilling operations and it is not correct to infer that only after drilling two wells, high risk was perceived.

Remarks of office of C&AG on the reply of the Government

No further comments please.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 10

OVL's argument that the decision to acquire the two blocks was taken based on the positive feedback from two rounds of studies - two visits to Ankara of its team led by GM (Exploration) and study by expert from KDMIPE, the premier institute of ONGC – reflects inadequacies in the in-house evaluation. OVL has informed that the capability of in-house technical team has been strengthened by induction of state-of-the-art software / hardware, skill development of technical team, subscription to professional global database and knowledge management. The Committee desire that OVL should take such further steps as may be necessary to ensure that in-house capability is not found wanting in any respect.

Reply of the Government

There is no denying the fact that in exploration ventures, due to inherent risks involved, multiple opinions are obtained to improve confidence in taking investment decisions. OVL has experience of failing in projects despite positive recommendations from third party consultant and also has experience of success in venture

recommended through in-house due diligence. It is acknowledged that there is always scope to further strengthen the internal processes & in-house capabilities for which OVL has taken numerous steps in the past 2-3 years like induction of state-of-the-art software/hardware, skill enhancement through training and work association, subscribing to the professional global database for techno-commercial insight and improving intrinsic knowledge management.

Remarks of office of C&AG on the reply of the Government

The compliance to the measures adopted by the Company for strengthening its in-house capabilities for evaluation of investment opportunities will be watched during future audits.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 11

11 and 12 Blocks, Turkmenistan

The Committee note that OVL acquired 30% participatory interest in 11 and 12 Blocks, Turkmenistan on the recommendation of its in-house team. According to audit, the acquisition was based on seller's estimates of recoverable reserves and also based **on old seismic data of 2003**. OVL has contended that seismic data is not perishable and its utility is enhanced by re-processing and integration of new drilling information and that E&P evaluation at any point of time can be done with the available data and dry / abandoned wells, even if untested, offer valuable information. The Committee feel that the question is not whether such information is valuable or not, but whether such information is sufficient to make a commercial decision involving huge funds. The Committee, therefore, as desired in a preceding para, recommend strengthening of in-house capability and processes.

Reply of the Government

It is submitted that for an opportunity on offer, the available data is shared with prospective interested companies on a level playing field. There may be limitations on the volume and quality of data available but the limitations are same for every competing party. However, the investment decision may vary depending on the outcome of due diligence by each party. OVL has taken numerous steps in the part 2-3 years in order to strengthen its internal processes and in-house capabilities viz. induction of state-of-the-art software/hardware, skill enhancement through training and work association, subscribing to the professional global database for techno-commercial insight and improving intrinsic knowledge management.

Remarks of office of C&AG on the reply of the Government

The compliance to the measures adopted by the Company for strengthening its in-house capabilities for evaluation of investment opportunities will be watched during future audits.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 13

Acquisition Of E&P Assets Of Omimex De Columbia By MECL

The Committee find from the Audit Report that at the time of acquisition of E&P assets of Omimex de Columbia in Columbia by Mansarovar Energy Columbia Limited (MECL) - a 50:50 JVC of OVL and Sinopec (National Oil Company of China), the consultant appointed by the Company had cautioned that Ecopetrol (National Oil Company of Columbia) being the sole buyer of the produce of Omimex field, their loss might be detrimental to field production. The Company, however, went ahead with the acquisition without even inserting an appropriate clause in agreement for safeguarding its interest in the event of non-lifting of crude oil by Ecopetrol. As a result, MECL had to defer production of 2,10,000 barrels of crude oil (Company's share was 1,05,000 barrels being 50 per cent) during 2009 due to non-lifting of crude oil by Ecopetrol on account of non-functioning of its refinery. Further, the Company also incurred loss on account of non/delayed realisation of revenue due to non lifting of crude production by Ecopetrol.

Reply of the Government

At the time of acquisition, Contract between Ecopetrol and Omimex de Colombia Limited was already in place and, hence, inclusion of clause for safe guarding the company was not feasible. During takeover from OMIMEX, the field produced oil @ 17000 bopd. The production since then has increased to 39000 bopd presently. Even with increase in production, MECL has not faced any major evacuation problem except in 2009 when a production deferment was observed due to operational constraints in the field and maintenance & accident in the refinery. Now with improved infrastructure, MECL has many alternatives like local sales, dispatch through port to evacuate any further increase in production.

Remarks of office of C&AG on the reply of the Government

No further comments please.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 14

Justifying its decision OVL has stated that Ecopetrol being the major national oil company of Columbia is having all pipeline infrastructure which is used to evacuate the crude oil otherwise it would not have been possible to evacuate heavy oil. Furthermore, Ecopetrol is a major stakeholder of the Nare association contract in which MECL holds 50% interest. About non-inclusion of an appropriate clause about lifting of crude in the agreement OVL has informed the Committee that whenever a National Oil Company refinery enters into an agreement to lift crude from producers, the contract provision of "Take or Pay" is not included generally. The Committee while agreeing with the concerns of the Audit about the risks involved in the project due to only a single buyer being there to lift the crude produced also appreciate the factual position explained by

OVL. The Committee understand that since OVL did not have much leverage in changing the contract and it had to either acquire or leave the asset it has taken a calculated risk to bid for the asset. Nevertheless, the Committee desire that OVL should endeavour to ensure that Ecopetrol continues to cooperate with MECL in all manner and lift the entire production regularly so as to avoid a repeat of 2009. Since, a Company of the Government is involved in the tie-up from the other side the Ministry of Petroleum and Natural Gas should also fully support the endeavours of the Company through the channels of Ministry of External Affairs.

Reply of the Government

Considering the future production forecast, evacuation alternatives have been explored as a continual improvement process.

- New delivery points like Barranquilla Exports (ECP and MECL started the evacuation alternative called Barranquilla exports by trucks in August 2010 to mitigate the deferred production by evacuation constrains) and Local sales have been added as evacuation alternatives to avoid production loss in the event of non-lifting of crude by Ecopetrol. Further, spare capacity of 13500 BOPD was bought in GAC (Galan Ayacucho Covenas) pipeline with the cooperation of Ecopetrol.
- MECL is confident that entire quantity of produced crude can be evacuated.

It is also to submit that OVL has been approaching MEA/Embassies to coordinate the acquisitions and has been leveraging the strength of our mission to facilitate Business Development / Operations.

Nevertheless, suggestion of the Committee regarding seeking support of Ministry of External Affairs through Ministry of Petroleum & Natural Gas would be followed in right earnest in future as well.

Remarks of office of C&AG on the reply of the Government

The compliance to the measures adopted by the Company to safeguard its interest in the event of non-lifting of crude by Ecopetrol would be watched during future audits.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 19

Success Rate in exploration

According to Petroleum Secretary, the global success rate in exploration and production assets hovers somewhere around 30% while in the case of OVL, it has been around 42%. It is observed from the information furnished by the Ministry of P&NG that the international companies' average success rate during 2010 ranged between 24% and 60%. In so far as the exploration success rate of OVL is concerned, varying figures have been furnished by the Government and the Audit. The Government has indicated it to be 42% on a holistic basis and 40.19% if the oil and gas wells of the blocks

relinquished due to sub-commercial discoveries are not considered. However, according to Audit the success of exploratory efforts of OVL on the basis of only exploration blocks instead of drilled wells, works out to a mere 19.35% (6/31x100) as against 40.19% indicated by the Government. Notwithstanding the claims and counter claims of the Government and the Audit in the matter, the Committee strongly feel that even the highest success rate of 42% indicated by the Government is nowhere near the global best of 60%. Apparently, the Company has a long way to go before it can even think of being amongst the global leaders in this business. In the opinion of the Committee, if OVL is to carve out a niche for itself in the intensely competitive business of oil exploration, it has to be fully geared up in its operations, evaluation, delivery and production. The Committee, therefore, desire Government and OVL to suitably re-orient the functioning of the Company with a view to enable it to be a global leader without any further loss of time.

Reply of the Government

As per international practice, the exploration success ratio is calculated by dividing the number of oil & gas wells drilled during a particular period by the total number of exploration wells drilled during the same period and the ratio is usually expressed in percentage. The success rate of 42% and 40.19% reported by OVL to C&AG is based on the above principle. But the success rate of 19.35% calculated by Audit is by dividing the number of successful exploration ventures by the total number of exploration ventures OVL was associated with during the period for which performance audit was carried out.

At the same time, the Company has desired to assure the Committee that with improved due diligence supported by second opinion, the Company will strive to achieve higher exploration success.

Remarks of office of C&AG on the reply of the Government

The measures adopted by the Company for strengthening its in-house capabilities for evaluation of investment opportunities will be watched during future audits.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 20

Finding Cost

On the parameter of finding cost, the Committee have been informed that based on 1P reserves (proved reserves), the finding cost of international companies varies between USD 1.60/boe and USD 15.80/boe (11 year moving average upto 2011) with median at USD 5.24/boe. The finding cost (11 year average) of ONGC, the parent Company of OVL is stated to be USD 4.31/boe. OVL's finding cost according to the Company is USD 1.65/boe based on IP reserves. The Audit has, however, worked out the finding cost of OVL at USD 5.14/boe for 1P reserves as it had excluded the Farsi Block reserves in Iran because OVL only had a service contract for the project and no ownership on hydrocarbon reserve. The Committee tend to go by the justifications

given by the Audit while assessing the finding cost of OVL at USD 5.14/boe. They, however, feel that even this figure compares well with the global average of USD 5.24/boe. The Company should, however, not rest on its laurels as there is still a lot of scope for improvement given the fact that there are companies with as low a finding cost as USD 1.60/boe. The Committee, therefore, desire OVL to strive to bring down its finding cost so that it is comparable with the best in the field with prompt induction of appropriate technologies and business practices.

Reply of the Government

The availability of overseas exploration acreages are in more complex areas than the traditional petroleum regions with its associated operational, environmental and geopolitical challenges. This affects both the denominator of reserve accretion with high risk and the numerator of higher cost. In spite of the challenges the company is able to maintain its finding cost comparable with peers as noted by honorable committee. Notwithstanding the above, the company would continue to work towards bringing down its finding cost.

As regards consideration of reserves of Farsi exploration efforts for working out finding cost, though it is correct that the company does not have ownership of the hydrocarbon reserve under service contract but these reserves have been established due to exploratory efforts of the company. It would be appropriate to consider exploration cost and reserves established in Farsi block for working out the finding cost. It is also submitted that the Iran project is also a commercial operation and the got contribution of discovered reserves should be factored into to the economics of operations.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its earlier reply. The efforts of the Company to bring down finding cost would be watched during future audits.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 21

Internal Rate of Return

Comparison of anticipated and actual Internal Rate of Return (IRR) of a project indicates the success or otherwise of a venture. The Committee have, however, not been provided with this information in respect of OVL's projects abroad, citing reasons such as IRR varying from project to project; IRR being known only after the completion of project life cycle, IRR calculation not being possible for projects which are yet to achieve cash break even; IRR being a business secret which companies keep confidential by all means to maintain their competitive position . The Committee are not convinced of these reasons and would like the Ministry of P&NG to ascertain from the Ministry of Finance and the Department of Public Enterprises whether the information regarding IRR of a project is treated as commercial secret and whether there are any guidelines regarding IRR concerning public undertakings and the Committee be

apprised of the position. Incidentally, the Committee find at least one instance of IRR of OVL being in public domain on the internet.

This was, however, termed as an unauthorised disclosure by OVL when a clarification was sought from it. The Committee desire that the case of unauthorized disclosure of IRR on internet be inquired into and a report, fixing the responsibility and action taken be furnished to the Committee immediately.

Reply of the Government

As advised by the Committee, MoP&NG has consulted the Department of Public Enterprises (DPE) and Department of Expenditure (DoE), Ministry of Finance. DPE has informed that it has not laid down any guidelines/or instructions on IRR. Department of Expenditure has forwarded the Guidelines for Formulation, Appraisal and Approval of Government Plan Funded Projects / Schemes (dated 15.11.2007). The Guidelines do not comment on whether the IRR can be put in the public domain or not.

As submitted earlier, the information on IRR is a business secret and the companies keep this information confidential and do not share in public domain. Such information is hardly ever available in public domain. Disclosure of any confidential/business sensitive information like IRR harms the business interests of the company by diluting competitive position. As stated earlier, the IRR varies from project to project and it can be worked out only after achievement of cash breakeven.

OVL has also informed that the IRR disclosed in public domain was about ONGC-Cairn deal in 2003 and was not related to OVL. The matter has been further enquired into by ONGC and their findings are as under:

- i. The document downloaded from the website appears to be a report which does not carry any credentials / references / source.
- ii. The relevant Board agenda along with its annexures were reviewed and it was found that the document downloaded from the internet relating to IRR, was not part of the agenda and also there is no reference of the document in the minutes of the Board.
- iii. The source through which the document became available in the public domain could not be established.
- iv. Unauthorized disclosure from ONGC's office is unlikely, as Confidential documents are closely guarded and supervised by the company's secretariat.

Therefore, it is submitted that there appears to be no unauthorized disclosure by ONGC / OVL in the case under reference.

Unfortunate / unauthorized disclosure of information in one case should not become a basis for disclosing the business sensitive information in another case, as it would increase the vulnerability of the entity which has been the victim of the unauthorized disclosure in the first place.

Remarks of office of C&AG on the reply of the Government

No further comments please.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

CHAPTER III

RECOMMENDATIONS /OBSERVATIONS WHICH THE COMMITTEE DO NOT DESIRE TO PURSUE IN VIEW OF THE GOVERNMENT'S REPLIES

Recommendation Serial No. 2

Block 5B, Sudan

OVL acquired Block-5B, Sudan (May, 2004) with 23.5 percent participation interest at USD 24.06 million with "carry over finance" of 3.72 per cent participation interest of Sudapet (National Oil Company of Sudan). The Committee note from the Audit Report that the consultants in their pre-acquisition technical study of the Block 5B, Sudan had expressed several reservations. These included the assessed reserve in the Block being based on limited data made available by the Seller; denial of permission to copy data from the data room; only two days being given for review of data; and the security problems in the Block area. The OVL, however, overlooked the reservations of the consultants. The Consortium could not implement the scheduled seismic and drilling plan till 2006 for want of accessibility to the area and restrictions by the local authorities. Coupled with this, the non-implementation of Minimum Work Commitment (MWC) led to OVL incurring additional security charges, idle hiring charges for drilling rig and other incidental and operational charges after acquisition of the Block. To further compound the problems out of the three prospects prioritized by the consultant for drilling, the Operator drilled only one prioritized well in addition to two wells in the non-prioritized swamp during 2008. The drilling of the remaining prioritized swamp wells was dropped due to the less prospectivity of reserves in one of them and allotment of the other to a third party by the local authorities in complete violation of the agreement. The three wells drilled brought no hydrocarbon discovery, and thus forced the Company to relinquish the Block on 19 February, 2009 after incurring an expenditure of USD 89.5 million equivalent to Rs. 423.84 crore. The Audit pointed out that while going for this acquisition, OVL took cognizance of the adjoining Block 5A which it was also prospecting and completely ignored the security scenario in Sudan.

Reply of the Government

It is a standard practice followed by the sellers of E&P assets that they give access to their data room to the prospective buyers for a limited period, say for 2 to 3 days. This is in view of time constraints with the seller and there being multiple prospective buyers to view the data. Also, the sellers do not allow copying of the data in view of their concern for confidentiality.

As regards the reservations of the consultants like assessed reserve in the Block being based on limited data made available by the seller, denial of permission to copy data from the data room, only two days being given for review of data, and the security problems in the Block area, they include such statements invariably as a disclaimer in their reports to restrict their legal liabilities, which, therefore, need not be overemphasized.

It may be mentioned that security is important but not the sole consideration in arriving at the oil and gas investment decisions. It is known that at the time of

acquisition of Block 5A and 5B the Company was already operating in its GNOP, Sudan asset successfully.

The decision to acquire the Block 5B was taken not only on the basis of the report of consultant but also considering the overall regional oil prospectivity trend, knowing the fact that adjoining blocks such as Blocks 6,1, 2, 4 and 5A were having oil discoveries in similar geological set up.

To summarise, a holistic approach, even considering the risks/concerns expressed by the consultants, was taken while taking an investment decision for Block 5B and there was no overlooking of consultant's reservations.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its earlier reply which has already been considered in audit.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 3

OVL in its defence has submitted before the Committee that the advice of the consultants regarding Block 5B, Sudan was not overlooked and that such reservations are invariably included by consultants in their reports as a disclaimer to restrict their legal liabilities. As regards only two days being given for review of data, OVL contended that it is a standard practice followed by the Sellers of E&P assets in view of time constraints and also the Sellers do not allow copying of data in view of their concern for confidentiality. About the security concerns raised by the consultants, OVL informed that security situation in Sudan was and remains a challenge but the Company was already prospecting in Block 5A which is adjacent to Block 5B, hence, there was no reason for any undue alarm. OVL has also submitted that none of these factors are strong enough reasons for OVL or for that any other oil company to discontinue its operations in Sudan. The decision to acquire Block 5B was taken not only on the basis of the report of consultants but also considering the overall regional oil prospectivity trend, knowing the fact that adjoining blocks were having oil discoveries in similar geological set up. A holistic approach, even considering the risks/concerns expressed by the consultant was taken while making an investment decision for Block.

Reply of the Government

A holistic approach was taken in the matter considering the risks / concerns expressed by the consultants, while taking an investment decision for Block 5B and there was no overlooking of consultant's reservation.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its reply its earlier reply which has already been considered in audit.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 4

The Committee are of the considered view that since the operator was not able to enter the contract area even after a lapse of considerable period and further E&P business being highly risky and capital intensive, OVL should have given due consideration to the limitations expressed by the consultants instead of brushing aside the reservations expressed by them as a mere disclaimer. Going by this strange logic and if the consultant's genuine concerns were to be so non-chalantly ignored, there was then no need for even hiring a consultant. The Company would have better safeguarded its financial interests, had it gone for revalidation of the data before proceeding further in the matter. The Committee feel that the decision of OVL not to contest Minimum Work Contract (MWC) with the authority based on the prospectivity perception of block 5B is totally imprudent as operating a producing property in a country does not provide guarantee to the success in another E&P opportunity. Moreso, when the Seller had already violated the production sharing contract by allotting part of the area to a third party.

Reply of the Government

When two opportunities in Sudan, i.e. blocks 5A and 5B were offered to OVL in 2004-05, the Company was already holding stake in a producing property in the country. It was an opportunity to create a critical business mass for the company in the country as the offered blocks were located in similar geological set up and contiguous to the already discovered prospective oil & gas trend. One of the two blocks i.e. 5A could be converted into a commercial producer but there was no exploration success in block 5B, which was subsequently relinquished. As a matter of practice, the Company does not reject arbitrarily the recommendations of the Consultants, even though certain observation from the Consultant at times are downplayed keeping the overall techno-strategic consideration. Nevertheless, in the instant case, the limitations reflected by the Consultant in the report were a normal caveat to restrict its legal obligations, which is a usual industry practice for consultants. Being an operator in the producing property acquired in 2003, OVL was already aware of the security situation in Sudan. The decision to acquire the blocks was by balancing the consideration on security situation and the perceived prospectivity for hydrocarbons.

Remarks of Office of C&AG on the Reply of the Government

The Government has reiterated its earlier reply which has already been considered in audit.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 12

NN Block, Qatar

The Committee note that OVL signed an agreement with Qatar Petroleum for acquisition of 100 per cent participation interest in NN Block in Qatar with the express stipulation that it could only extract crude oil from the designated Block and had no right

over gas or any other minerals discovered from the Block. In spite of this stipulation, the Company without following any due diligence relied solely on the maps and data provided by Qatar Petroleum for estimation of oil reserves without getting it revalidated from an independent technical consultant. Consequently, against the estimated OOIP of 187.72 MMB, the Company on drilling discovered that the actual recoverable was a meagre 2.24 MMB. With such low reserves and no contractual right on the gas, the Company had to relinquish the Block in May, 2008, thereby, rendering the entire expenditure of Rs. 369.45 crore infructuous. The Company's argument that the 3D seismic data was reprocessed and re-interpreted by Geo-Data Processing and Interpretation Centre (GEOPIC), ONGC which is renowned for its professional standards and a Multi-disciplinary Team of experts from ONGC and OVL checked and revalidated the interpretation based on the reprocessing (by GEOPIC) does not justify the exclusion of independent consultant's advice while going for such an important strategic investment decision involving 100 per cent participation. The Company's second argument that since the data made available by Qatar Petroleum was the only source of information and to estimate the reserves and evaluate the block even the independent consultant would have to use the same data also appears tenuous as in the given circumstances when the Company's rights in the acquisition were restricted to crude oil only, it was all the more essential to be doubly sure about the estimation of reserves through an independent consultant.

Reply of the Government

The Company has reiterated its stand that in view of NN Block being a discovered asset, sharing of risk with Partner (s) was not in the strategic consideration of the Company. On the internal due diligence, the Company used the available data with further value addition by reprocessing and also by engaging the domain expertise from premier institute of the Parent Company. The setback in the project was due to deviation in fluid type and volume with reference to the pre-appraisal predictions, which is usual in global E&P business, for which the E&P business is construed as high risk. At the same time, the Company has introduced many new measures like engagement of independent consultant and introduction of zero based risk review matrix etc. to further strengthen the acquisitions process of high risk overseas E&P assets. Wherever the difference of opinion in the evaluation has emerged management has ensured that the decisions taken are in the interest of the organization.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its earlier reply. However, the compliance to the measures adopted by the Company to strengthen the acquisition process would be watched during future audits.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

CHAPTER IV

RECOMMENDATIONS / OBSERVATIONS IN RESPECT OF WHICH REPLIES OF THE GOVERNMENT HAVE NOT BEEN ACCEPTED BY THE COMMITTEE

Recommendation Serial No. 15

Acquisition Of Imperial Energy Corporation

The Committee note that Imperial Energy Corporation Plc (IEC) an E&P Company was acquired by OVL in January, 2009 for Rs. 10,320 crore. Cabinet Committee on Economic Affairs (CCEA) had approved the acquisition with the stipulation that the Internal Rate of Return (IRR) would be in the excess of 10% and an option to farm-out part of its stake to a Russian firm. As OVL's assessment, the project was viable with average daily rate of production of 35,000 barrels for 2009 and up to 80,000 barrels per day by 2011. Due to unrealistic estimation of reserves/production, OVL has suffered a huge loss of Rs. 1182.14 crore during the period 2008-09 to 2009-10. Since OVL did not chose to farm-out part of its stake to a local partner, the entire loss has to borne out by it. Moreover, the Company has also suffered a production loss of 10.8 million barrels and has not been able to achieve the stipulated IRR of 10%.

Reply of the Government

Unrealistic estimation of reserves/production: As submitted earlier, the Company has reiterated the fact that like any other new business opportunity of OVL, the acquisition of Imperial Energy was preceded by technical due diligence by the in house team of ONGC/OVL and Pangea (technical consultant engaged by OVL for technical due diligence). Also, prior to the acquisition, the reserves of the Imperial Energy were certified by DeGolyer & MacNaughton (D&M), an internationally reputed independent US based reserves audit firm. The acquisition was made considering all the above three independent reserve estimations.

The projected production from the asset was based on the data from certain drilled key wells in the oilfields of Imperial Energy prior to its acquisition by OVL following standard industry procedure. It is only unfortunate that after acquisition, production from some of the fields were not as expected due to heterogeneity of the reservoirs arising out of geological complexities. The success in one of the fields i.e. Maiskoye, which has achieved higher production than pre-acquisition estimates, corroborates this fact.

Since OVL did not chose to farm-out part of its stake to a local partner, the entire loss has to borne out by it: It may be noted that farm out option depends, amongst other thing; on risk reward perception & prevailing market condition. In the acquisition strategy formulated as per the conditions prevalent at the time of making the offer for acquisition of the asset in August 2008, OVL had no plan to farm out any stake of the target asset and hence no participating interest (PI) was farmed-out.

However, approval of Government of India was sought for possible farming out suitable Participating Interest (PI) to Russian entity(ies) on mutually agreed terms at an

appropriate time as there was an apprehension that while according approval for the acquisition, the Russian Government may put a condition of giving certain PI to a Russian entity as was done in an early case involving SINOPEC (China) in case of Udmurtneft.

Imperial Energy has not been able to achieve the stipulated IRR of 10%: With regard to the possibility of achieving IRR of 10%, it may be noted that the estimated IRR at the time of asset acquisition was on cash flow basis achieved on full project life which extends over more than 20 years under licenses granted to it valid till 2028-32 (and further extendable). The achieved IRR at the end of project life would vary based on the results of the ongoing efforts of Imperial to commercially exploit the tight oil reserves of the asset.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its earlier reply which has already been considered in audit.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Comments of the Committee

Please see para 20 of Chapter I.

Recommendation Serial No. 16

OVL's contention that though M/s Rosneft (a local company) initially expressed its willingness to partner in the project but withdrew from the same in October, 2008 due to various compulsions is devoid of merit as the acquisition was done only in January, 2009 i.e. three months after the withdrawal of Rosneft. The Ministry's admission that the production levels of IEC have not been commensurate with the levels envisaged at the time of acquisition primarily due to unforeseen geological complexities from the tight reservoirs of the asset, in the opinion of the Committee, is a tacit admission of the shortcomings pointed out by the Audit in this acquisition. The Company's assertion that such reservoirs elsewhere in the world have been successfully exploited with appropriate technology and favourable fiscal (tax) regime also confirms the Committee's growing apprehensions that things are not well with this acquisition of the Company and there would be further financial implications before there is any possibility of IEC's balance sheet coming out of red. While expressing their disapproval of the Company's error of judgement in the instant case, the Committee also feel that the Ministry has also not acquitted itself well as this acquisition was beyond the powers of the Company and had been done with the approval of CCEA. The Committee, therefore desire a comprehensive review of this acquisition and its performance alongwith its future prospects so as to arrive at a well considered decision about its future. The Committee would like to be apprised the outcome of such a review at the earliest.

Reply of the Government

It is a fact that the acquisition process for Imperial Energy was concluded in January 2009. But it may be noted that subsequent to receipt of approval of the

Government on 22.08.2008 authorizing OVL to make binding offer, OVL had made a binding offer to the shareholders of Imperial Energy on 26 August 2008, subject to receipt of approval of regulatory authorities of the Russian Federation to the acquisition. Further, as mentioned in the earlier para, OVL had no plan to farm out any stake of the target asset and hence on refusal of Rosneft, there was no further effort by OVL to divest any participating interest(PI) in the venture. Post-acquisition, through focused efforts Imperial Energy was successful in ramping up the production from approximately 6000 bopd at the time of acquisition to 19200 bopd in mid-2011. However, unlocking the oil in place from the tight reservoirs with infusion of the right exploitation technology in a cost efficient manner has been the major technical challenges to the company. The company is currently engaged in pilot scale application of horizontal drilling and fracing with partnership of a US based independent E&P company having expertise in this area to exploit these reservoirs. The full-fledged application of the new technology to enhance production from the asset shall follow the ongoing pilot program based on its results. It may be noted that the earlier submission of OVL that such reservoirs elsewhere in the world have been successfully exploited with appropriate technology, had reference to the very recent technological breakthroughs made in the area of exploitation of tight oil / gas reservoirs especially the shale oil / gas reservoirs of North America. The Company believes that application of similar technology, supported by the tax breaks offered by the host government, will help in turning around the performance of the Imperial Energy asset. The company is closely monitoring the current technology application endeavor, the results of which will decide the future action plan for the asset and the Committee will be apprised of the developments on the issue. Lessons learn would be used in future acquisition.

Remarks of office of C&AG on the reply of the Government

The assurance given by the Government regarding review of the acquisition and performance of IEC asset will be watched in future.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Comments of the Committee

Please see para 20 of Chapter I.

Recommendation Serial No. 17

NN Block, Qatar

The Committee note that OVL acquired 100% participation interest in Najwat Najem Block, (NN) Qatar and estimated the volume of Original Oil in Place (OOIP) at 187.72 million metric barrel of oil equivalent (MMBO) in spite of risk of pre-existing poor event continuity attached with its reserves estimations. Further, OVL decided to appraise the Block by itself despite knowing that about 12-16 leading E&P international oil companies were interested in the Block. This go alone decision not only deprived the Company of mitigating the impact of risk known to it, by leveraging the combined financial strength and sharing experience of the JV partners but also resulted in financial loss.

Reply of the Government

The Company has reiterated its stand that in view of NN Block being a discovered asset, sharing of risk with Partner (s) was not in the strategic consideration of the Company. Though many Companies had shown interest for the same block, no Company has approached OVL for partnership.

Remarks of office of C&AG on the reply of the Government

The Government has reiterated its earlier reply. Hence, no further comments.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

Recommendation Serial No. 18

OVL has submitted to the Committee that being a discovered field it decided to do the field appraisal on its own. It has also submitted that it did not receive any expression of interest to farm-in in the Block from the 12 to 16 leading E&P companies which were interested in the project and decided to appraise the discovery by itself in expectation of associated reward which did not materialise. OVL has also contended that even if it had decided to take partners there could have been criticism if the project would have been successful. The Committee take exception to this convoluted set of logics extended by the Company to cover up the errors in its commercial judgement. Had the Company made any serious efforts to rope in partners, the risk factor involved in the project would have been mitigated to a considerable extent. The Committee recommend that given the high risk nature of exploration and production industry, the Company should exercise more prudence when faced with similar situations in future.

Reply of the Government

While agreeing to the Committee's recommendation, the Company has introduced many new measures to further strengthen the acquisition process of high risk overseas E&P assets.

Remarks of office of C&AG on the reply of the Government

The measures adopted by the Company for strengthening its in-house capabilities for evaluation of investment opportunities will be watched during future audits.

(Ministry of Petroleum & Natural Gas)
(O.M. No. O-22019/8/2011-ONG-III(pt.) dated 27.10.2014)

CHAPTER V

**RECOMMENDATIONS IN RESPECT OF WHICH FINAL REPLIES OF THE
GOVERNMENT ARE STILL AWAITED**

- NIL -

**New Delhi,
6 August 2015
15 Shrawana, 1937(S)**

**SHANTA KUMAR
Chairperson,
Committee on Public Undertakings.**

COMMITTEE ON PUBLIC UNDERTAKINGS
(2015-16)

MINUTES OF THE THIRD SITTING OF THE COMMITTEE

The Committee sat on Tuesday, the 9th June 2015 from 1100 hrs. to 1200 hrs. in Room No. 53, First Floor, Parliament House, New Delhi.

PRESENT

Shri Shanta Kumar - Chairperson

MEMBERS

Lok Sabha

2. Shri Lal Krishna Advani
3. Shri Prahlad Patel
4. Shri Rayapati Sambasiva Rao
5. Shri Sushil Kumar Singh

Rajya Sabha

6. Shri Narendra Budania
7. Shri Praful Patel
8. Shri C.M. Ramesh
9. Shri Tapan Kumar Sen

SECRETARIAT

1. Shri M.C. Sharma Joint Secretary
2. Shri M.K. Madhusudhan Director
3. Shri G. C. Prasad Deputy Secretary

OFFICE OF C&AG

Shri P. Sesh Kumar Director General (Commercial)-I

WITNESSES

NHPC LIMITED

1. Shri R.S.T. Sai CMD
2. Shri D.P. Bhargava Director (Technical)

2. XXXX

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3. The Committee, then, considered the draft Action Taken Report on the action taken by the Government on the observations/recommendations contained in the Twenty-seventh Report of Committee on Public Undertakings (Fifteenth Lok Sabha) on Joint Venture Operations of ONGC Videsh Limited based on Audit Report No. 28 of 2010-11 (Performance Audit) and adopted the same without any change. The Committee also authorised the Chairperson to present the Report to Parliament on their behalf, after obtaining factual verification.

A verbatim record of the proceedings has been kept separately.

The Committee then adjourned.

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Matter not related to this Report.

APPENDIX - II

(Vide para 3 of the Introduction)

Analysis of the action taken by Government on the Observations / Recommendations contained in the Twenty-seventh Report of the Committee on Public Undertakings (Fifteenth Lok Sabha) on “Joint Venture Operations of ONGC Videsh Limited based on Audit Report No. 28 of 2010-11 (Performance Audit)”.

I	Total number of Recommendations	21
II	Recommendations that have been accepted by the Government [vide Recommendations at Sl. Nos. 1, 5, 6, 7, 8, 9, 10, 11, 13, 14, 19, 20 and 21] Percentage of total	13 62%
III	Recommendation which the Committee do not desire to pursue in view of Government’s replies [vide Recommendations at Sl. Nos. 2, 3, 4 and 12] Percentage of total	04 19%
IV	Recommendations in respect of which replies of the Government have not been accepted by the Committee [vide Recommendations at Sl. Nos. 15, 16, 17 and 18] Percentage of total	04 19%
V	Recommendations in respect of which final replies of Government are still awaited.	Nil