

Performance Auditing in the Oil and Gas Sector

Closing Conference (18th of June, 2021)

Funded by the Netherlands Ministry of Foreign Affairs



Program overview

- 10:00 Official opening
- 10:20 Presentation by project partner SAIs
- 11:20 Parallel audit outcomes
- 11:40 *Comfort break*
- 11:50 Lessons learned by the NCA team
- 12:05 Lessons learned by SAI audit teams and the way forward
- 12:50 Closing remarks | 13:00 End

Presentations by project partner SAls
(2.1 / 2.2 / 2.3)



2.1 Presentation parallel audit report SAI Kenya



Country Context and Importance of the Audit

- Kenya is a latter discoverer of oil, having discovered commercially viable oil in 2012
- However, prospecting has been on going for over fifty years;
- Under the AFROSAI-E/NCA initiative, SAI Kenya carried out 2 audits:
 - Parallel audit with SAI Mozambique and Tanzania
 - One local audit
- Both audit reports are still under review
- The audit has been beneficial to my Office in:
 - Developing the requisite skills and competencies to conduct future performance audits in the extractive industry;
 - Sharing skills and knowledge learnt with other performance auditors;
 - Creation of partnerships and networks with auditors from participating countries which will enhance cooperation/knowledge sharing in future audits.

Parallel Audit SAI Kenya

Title of the audit:

Preparedness of The State Department for Petroleum to Monitor Costs in The Petroleum Sector

Audit questions:

- To what extent had the State Department for Petroleum put in place systems to review and approve work programmes, budgets and progress reports prepared and submitted by International Oil Companies?
- To what extent had the State Department for Petroleum put systems in place to ensure review and approval of recoverable cost claims from International Oil Companies?
- What systems had the State Department for Petroleum put in place to coordinate with the Kenya Revenue Authority, on tax related cost claims?

Audit Criteria

The audit assessment criteria were drawn from:

- The Petroleum (Exploration and Development), Act. revised Edition 2012
- Production Sharing Contracts (PSCs) in the Act. for Block 10BB and 13T
- Best practice in monitoring operations under contracts

Methods for Data Collection and Analysis

Documentary review

- The governing legislation, PSCs and various correspondences with stakeholders so as to understand the operations of SDP with regards to monitoring of costs in the petroleum sector.

Interviews

- SDP staff to gain an understanding of how SDP monitors costs, additionally KRA staff were interviewed to obtain information on collaboration and coordination with SDP.

Data analysis

- The collected data were collated, analyzed and presented in thematic areas using tables and/or discussion.

Main Conclusions and Key Recommendations

The report is at the review stage.

We will share the main conclusions and key recommendations in due course when the report is signed.

2.2 Presentation parallel audit report SAI Mozambique



Tribunal Administrativo
República de Moçambique

Country context and importance of the audit

- Background of the oil and gas sector in Mozambique
- Auditing of the Extractive Industry
- Audit results
- Importance of Extractive Industry Audit



Parallel audit SAI Mozambique

Title of the audit:

- Mozambique Government's System to monitor recoverable costs claimed by international oil companies (Auditees: Ministry of Mineral Resources and Energy; National Petroleum Institute (regulator); Tax Authority)

Audit objective:

- The objective of this audit is to assess the extent to which the Government's systems for monitoring the costs claimed by international oil companies are efficient.

Audit questions:

- The extent to which the National Petroleum Institute and the Tax Authority have systems in place to monitor the costs claimed by international oil companies for recovery and tax deductions, in order to protect future Government revenues.



Audit criteria

- Existence of filing system.
- Procedures in place to analyse and revise the oil companies´ s work plan and budget.
- Procedures in place to monitor and managing the compliance of the activities carried out by the concessionaires with the terms of the Contract.
- Procedures in place to carry out formal reviews of the performance of the concessionaires, with documented improvement plans.



Methods for data collection and analysis

- Interviews
- Document collection
- Document analyses
- Data triangulation



Main conclusions

I - Mechanism to Monitor Recoverable Costs

The National Petroleum Institute does not have an effective monitoring system to control the costs to be recovered by international oil and gas companies.

- Oil and gas companies execute their budget without prior approval of the National Petroleum Institute;
- The National Petroleum Institute does not have clear methods and procedures to challenge, review and report to the Chairman;
- The National Petroleum Institute and the Tax Authority do not have a complete filing system;
- The National Petroleum Institute does not dispute the costs claimed by companies.



Main conclusions

II - Accountability Mechanisms

The Ministry of Mineral Resources and Energy does not have an effective accountability system to track activities of the National Petroleum Institute with respect to the approval of recoverable costs.

III - Costs to be recovered by concessionaires are not approved

The National Petroleum Institute and the Tax Authority do not have a communication system in place for the Tax Authority to correctly deduct production sharing taxes.



Key recommendations

I- Mechanism to Monitor Recoverable Costs

- The National Petroleum Institute must contest the costs claimed by companies to ensure their respective eligibility, on a timely manner.
- The National Petroleum Institute must have a complete filing system that includes audit numbers, reports submitted/revised, minutes and work letters, adjustments made to costs claimed, amounts approved, etc.
- The Tax Authority should have a complete filing system that includes analysis of accounting data, claims submitted by companies and adjustments made, etc.
- The National Petroleum Institute must ensure that budgets, cost statements and progress reports are analyzed, reviewed to control costs and prevent them from being approved without any challenge, including a clear mechanism for challenging claimed costs, and timely carry-out cost audits.
- The Tax Authority should have an effective monitoring system to control the applicable tax deduction



Key recommendations

II - Accountability Mechanisms

- To exercise proper oversight, the Ministry of Mineral Resources and Energy should ensure that the National Petroleum Institute provides it with full information on the recoverable costs that must be approved.

III - Communication Mechanism between the Tax Authority and the National Petroleum Institute

- That the National Petroleum Institute coordinates with the Tax Authority to establish a clear communication mechanism where they share relevant documents (claimed and approved costs, deductible tax, etc.) to allow the Tax Authority to be fully informed and well positioned to deduct the appropriate amounts of tax.



2.3 Presentation parallel audit report SAI Tanzania



Country context and importance of the audit

- Background of Oil and Gas sector in Tanzania
- Audit Mandate
- Importance of Extractive Industry Audit
- Concluding Remarks



Parallel audit SAI Tanzania

Title of the audit:

ASSESSMENT OF THE EFFECTIVENESS OF COST RECOVERY MONITORING SYSTEM

Audit questions:

1. Does PURA and TPDC have an effective systems in place to review and approve work programmes, budgets and progress reports prepared and submitted by the IOC's?
2. Does PURA and TRA have an effective systems in place to ensure review and approval of cost claims /tax returns from IOCs?
3. Is there an effective system in place to communicate and share information on cost recovery?



Audit criteria

S/no	Audit Question	Assessment Criteria
1	Does PURA have an effective systems in place to review and approve work programmes, budgets and progress reports prepared and submitted by the IOC's?	PURA is required to analyzing, disseminating and issuing information relating to petroleum industry, including proposed exploration activities contained in the annual work program, appraisal program, production forecasts, and budget submitted by a license holder.
2	Does PURA and TRA have an effective systems in place to ensure review and approval of cost claims /tax returns from IOCs?	<p>PURA is required ascertain the cost of oil and gas due to license holder and other contractors.</p> <p>IOCs are required to file with the Commissioner not later than three months after the end of each year of income a return of income for the year of income.</p>
3	Is there an effective system in place to communicate and share information on cost recovery?	PURA and TRA shall have the responsibility of coordinating and cooperating with other Government institutions.



Methods for data collection and analysis

Interviews and documentary reviews were used as the main methods for data collection:

- Quantitative data were collected through interviews;
- Document reviews were analyzed using excel spread sheets by organizing, summarizing and compiling them and using different statistical methods for data computations.

The identified methodologies were used to respond to the audit questions and provide conclusions against audit objectives, to obtain appropriate and sufficient information to enable the audit team to come up with clear findings which were supported by collaborative evidences, to confirm matters that arose, and clarification of the issues identified during document review.



Main conclusions

The findings presented in this report endorse that there are weaknesses on the cost recovery monitoring systems that would lead to a loss of Government revenue from petroleum cost recovery. Both PURA and TPDC do not have an effective system in place to monitor the recovery of petroleum costs for the upstream operation of natural gas. We noted the following:

- There are gaps regarding guidance on the monitoring of cost recovery and information management (including ineffective data);
- There is lack of official guidance on how the submitted work program and budget are to be reviewed;
- There is lack of a standardized manner on how to present and submit accounting statements;
- There is a lack of a cost recovery information system;
- There is a lack of price cap and benchmark on the extent and nature of allowable cost recovery expenditures.



Main conclusions

- Also, we noted that there is uncertainty on the recovery of disputed disallowed recoverable cost from the IOCs. This is because both TPDC and PURA have not established a mechanism to safeguard the disputed recoverable costs against the IOCs whom are the custodian of gas sale revenue.
- On the other hand, bases on the presented findings, there is low information sharing and coordination on cost recovery monitoring. TRA and PURA are not effectively working together on auditing recoverable cost allowed by both parties. Each party monitors cost recovery through auditing in isolation and therefore TRA is not highly effective in cost recovery monitoring as they would if had worked with PURA. Furthermore, TEITI reports does not publish cost recovery information and there is no any other avenue where such information is published.



Key recommendations

Lack of Standardized Accounting Statements Submission manner and designated Cost Recovery Information System

Audit noted that, there is no formal elaborated manner on how and by which format the accounting statements should adhere to. Moreover, both PURA and TPDC do not have a designated cost recovery information system for data computation and storage.

Lack of price cap and benchmark for allowable expenditures

Audit noted that there is a loophole for the IOC to escalate recoverable costs and an environment for the IOC to dispute disallowed recoverable cost. The Petroleum (Cost Recovery Accounting) Regulation prescribed the recoverable cost limit to be allowed by referring to the prevailing market value/cost or the best cost effective judgement of the IOC. However, the regulator has not established or earmarked approved market cost and recommended best judgement.



Key recommendations

Absence of mechanism to safeguard disputed disallowed recoverable cost

For the period of audit, the IOCs from sampled PSAs disputed disallowed recoverable costs. However, audit noted that, PURA and TPDC have not established a mechanism to secure recovery of disputed disallowed recoverable costs once the conflict is resolved. The disputed amount remains at the custodianship of the IOC.

Lack of Coordination between TRA and PURA on Cost Recovery

There had been inadequate coordination between PURA and TRA in sharing information on cost recovery monitoring especially on cost recovery auditing.



3.1 Reflections on parallel audit outcomes

Consequence
Management



Governance

Communication
& Collaboration



Parallel
audit
outcomes



Consequence

4.1 Lessons learned by NCA team

Audit Team NCA / AFROSAI-E

Gijs Koop
NCA Auditor

Marike Noordhoek
*NCA project
manager*

Don Hubert
*Resources for
Development*

Marieke
Vennevertloo
NCA Auditor

Mwila Munkanta
SAI Zambia

Ewout Irgang
*NCA Vice-
President*

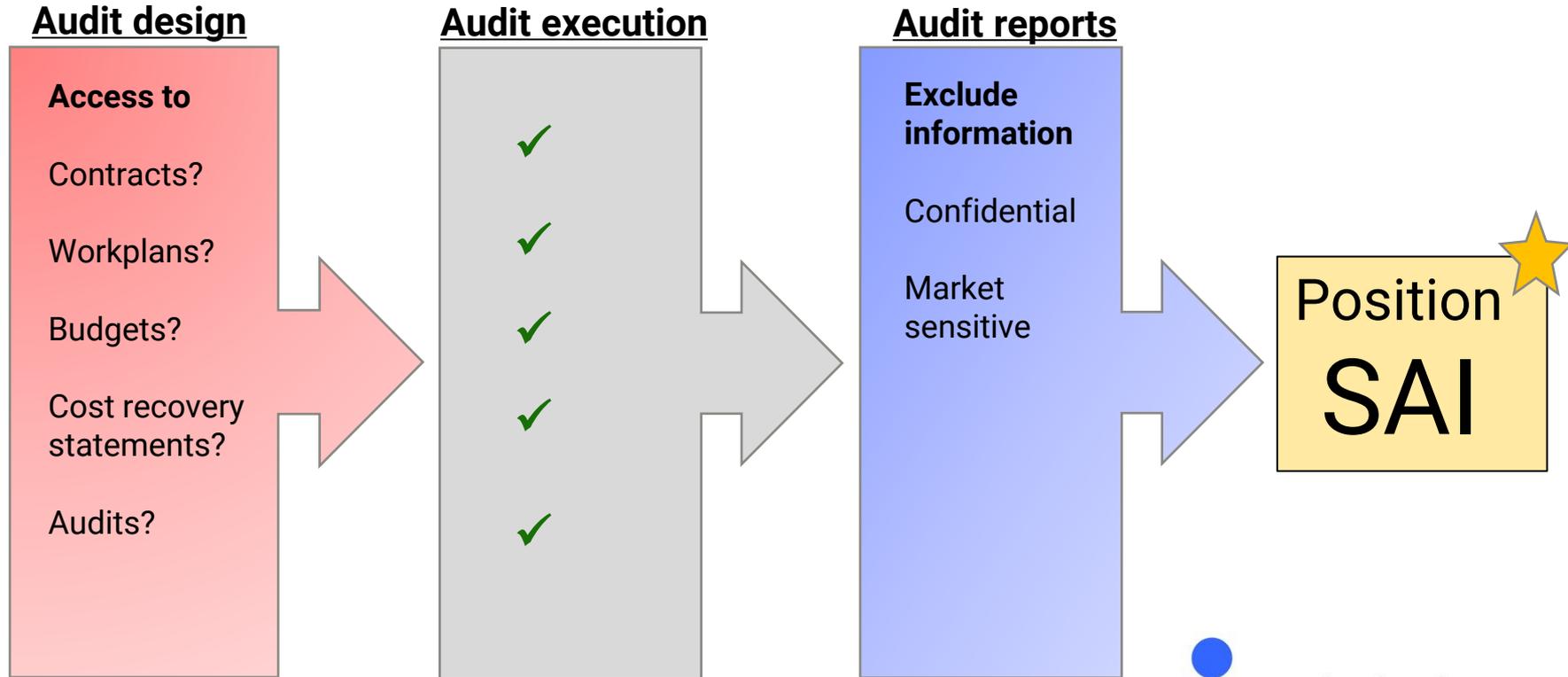


Conducting a performance audit in the oil and gas sector

Four lessons:

1. Access to information not an obstacle for SAI audits on oil/gas
2. System oriented approach useful when moving from compliance to performance audit
3. Improve system oriented performance audits: audit criteria from good practice
4. Clichés are sometimes true

Lesson 1: Access to information not an obstacle for SAI audits oil/gas



Lesson 2: System oriented approach useful when moving from financial/compliance to performance audit

System oriented approach builds on compliance audits

The ideal audit team

1. Mixed backgrounds: financial, compliance, performance auditors
2. Includes a team member with knowledge of auditee / oil-gas sector
3. An (external) resource person for specific questions

System oriented performance audit \neq compliance audit

1. Effectiveness of intra-government cooperation (tax authority and regulator)
2. Use audit criteria from international good practice

Lesson 3: Improve system oriented performance audits

Audit criteria from good practice

- SAI India: *Practice guide audit contract management (module 4, ch.2, p.5/13 -> conditions)*
- SAI UK: *Good practice contract management framework (mod. 4, ch.2, p.5/13-> conditions)*
- SAI Netherlands: *Modified evaluation framework grant management (mod.4, ch.2, p.9/13)*

Using these audit criteria was a challenge

1. Too little time to fully understand / customize to local context
2. Feeling of low-acceptability by auditee

Acceptance by auditee not necessary

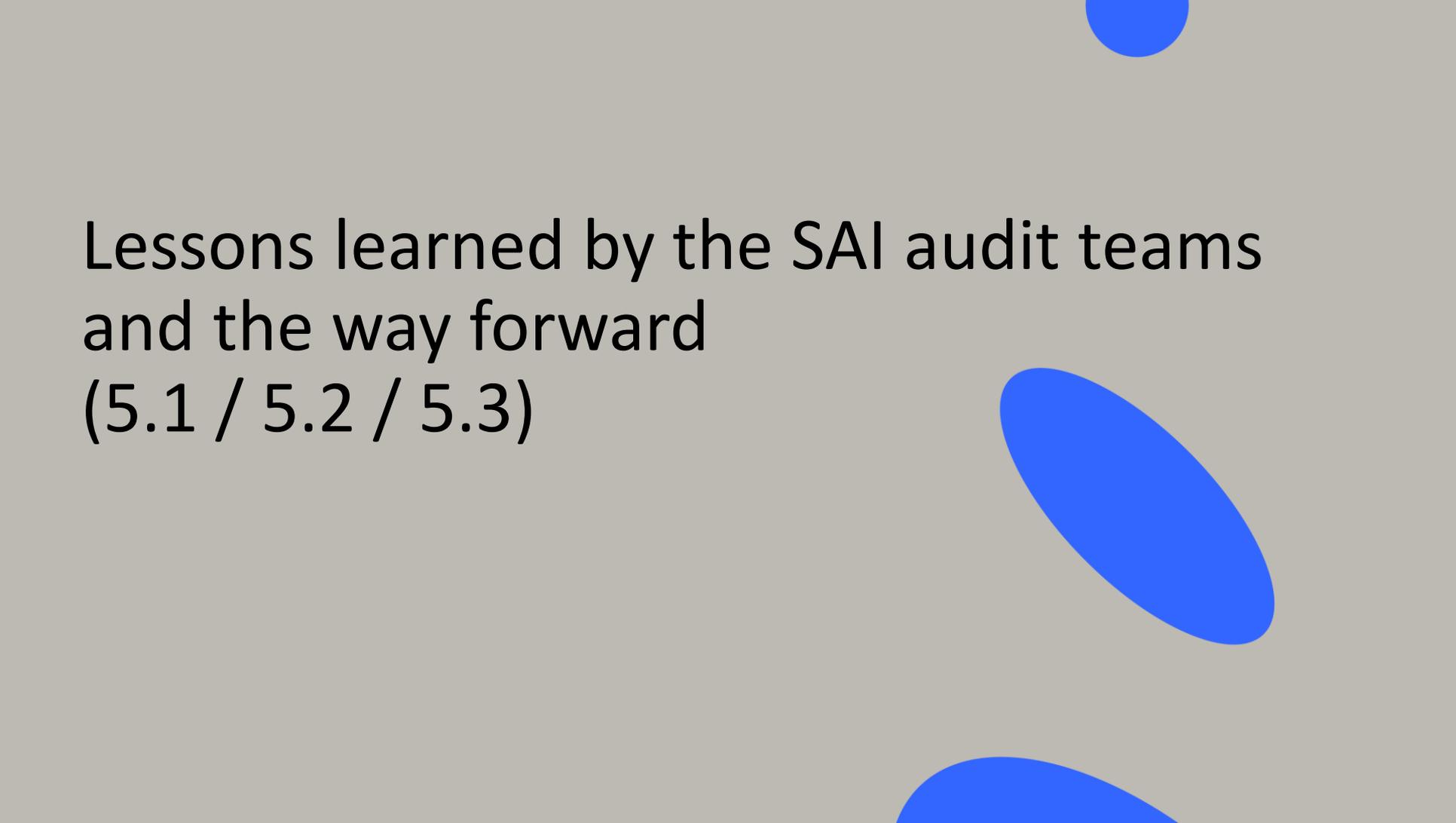
- GUID 3910 *"Audit criteria are established by the auditor"*
- Need to be discussed with auditee and stakeholders



Lesson 4: Clichés are sometimes true

Alone we go fast – together we go far





Lessons learned by the SAI audit teams
and the way forward
(5.1 / 5.2 / 5.3)

5.1 Presentation lessons learned and the way forward SAI Kenya



Conducting a performance audit in the oil and gas sector

Oil and gas audit is a highly specialized sector:

- The sector requires special skills hence the need to develop capacity in order to audit it effectively, i.e. specialized units, guiding manuals, trainings.

Accessibility of information

- Some of the information is classified as highly confidential hence affects audit evidence gathering and reporting.

Limitation of mandate

- The operators in the sector are private oil companies. SAI's may not audit their operations directly.

Conducting a parallel audit (including regional cooperation)

- **Consensus building challenges**
 - Given differences in country setups and interests, consensus building might drag before participating countries agree on common grounds for conducting the audit
- **Possibility of comparing countries' levels of performance**
 - The use of similar objectives and audit questions allows for comparative analysis of the findings and conclusions among the participating SAIs
- **Capacity enhancement**
 - Parallel audits allow for knowledge sharing among auditor hence good for capacity building of staff
- **Regional partnerships**
 - Through conducting parallel audits participating SAIs can propose partnership solution for common problems

The way forward: SAI level

- Enhancing the capacity of EI team to include multidisciplinary teams of performance and financial auditors
- Conduct more performance audits in EI sector
- Capacity/ re-skilling the EI team

The way forward: actions by other stakeholders

- AFROSAI-E should consider developing a comprehensive training programme for auditors in Extractive Industries sector
- Expand the capacity of WGEI to offer more specialized trainings in the sector
- Need for more parallel audits in the sector
- Exchange programs for countries within the region

5.2 Presentation lessons learned and the way forward SAI Mozambique



Tribunal Administrativo
República de Moçambique

Conducting a performance audit in the oil and gas sector

- Knowledge and experience about system-oriented performance auditing;
- Methods and procedures to describe in the report in order to facilitate the reader's perception, such as infographics, optimal systems for monitoring recoverable costs, data collection method, etc.;
- The structure of audit findings is grouped according to the system;
- Interactive and focused training method on the audit topic;
- Knowledge of the real costs of exploration activities and other operational expenses of these companies;
- Safeguarding the environment and ensuring safe operations;
- Revision of the extractive industry regulations;
- Importance of monitoring recoverable cost to safeguard the interests of the country;
- Types of contracts;
- Definition of recoverable costs.



Conducting a parallel audit (including regional cooperation)

- Exchange of experiences between countries on auditing extractives;
- Supreme Audit Institutions with different structure to audit oil and gas industry, while others have a specific unit, other use the performance or regularity auditors to audit extractive industries;
- Different languages;
- Understanding different audit methodologies;
- More knowledge / experience on oil and gas;
- Understanding different mandates of the SAI's.



The way forward: SAI level

- Considering the audit phases, monitoring would be essential to ascertain whether the recommendations left by the auditors have been acted upon or whether the actions taken by the entities have contributed to the achievement of the desired results.
- Ensure that TA auditors take the online course “How to audit government’s performance in managing oil and gas contracts” as has been developed as part of this regional project (available at E-Learning Platform AFROSAI-E).
- The SAI’s strategic Planning should include a description of the number of Extractive Industries audits to be carried out by year.



The way forward: actions by other stakeholders

- As to monitoring the parallel audit, it has to be done. However, in the case of Mozambique, considering that it is a Portuguese speaking country, a translator is required for a better engagement with the other countries. On the other hand, this cooperation may include countries from other continents who have experiences in auditing in the extractive industry sector;
- Sharing reports from other SAI's;
- Sharing tools for auditing;
- Providing support with specialist;
- Continuous training.



5.3 Presentation lessons learned and the way forward SAI Tanzania



Conducting a performance audit in the oil and gas sector

Lessons learned in conducting a performance audit in the oil and gas sector

- Enhance capacity building in oil and gas sector auditing

From conducting the performance audit in the sector, NAOT has improved sector understanding especially in the selected topic areas. The office has also improved its capacity in conducting performance audit in the petroleum sector.

- A need to create awareness to the auditee on performance audit

Most of the project auditees did not have a good understanding of performance audit. We had to enhance awareness on the nature and essence of performance audit to the petroleum sector.



Conducting a parallel audit (including regional cooperation)

The lessons learned from conducting parallel audit includes:

- Appreciate that SAIs are working from different environment and culture

Through the project we learned that, as SAI despite of having a common goal of conducting public audit, we work in a different environment and culture. These differences affect our audit execution and approaches. Therefore, in conducting a parallel audit in some areas an adjustment is needed in audit approach and execution.

- A need to improve cooperation during audit execution

We have learned that, the parallel audit teams have a challenge of sharing information during audit execution. Once the teams agreed on audit design and methodology, there is no effective mechanism to ensure that the team shares challenges and development encountered during audit execution.



The way forward: SAI level

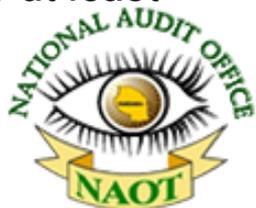
NAOT will ensure continuous conduct of performance audit in the sector through:

- **The use of Extractive Industry Strategic Plan**

The office is finalizing preparation of the extractive industry audit strategic plan. The document will prompt conduct of performance audit by ensuring that performance audit is conducted for each area along the extractive industry value chain.

- **Use of Annual Operational Plan**

For each calendar year, NAOT develops an annual operation plan for the extractive industry audit. The plan details audits to be conducted and other operation activities concerning the extractive industry audit. Through this plan the office will ensure that for each year at least one performance audit is being conducted.



The way forward: actions by other stakeholders

Suggested way forward actions by other stakeholders are:

- Create a forum or mechanism for SAIs to initiate cooperative audits

The stakeholders should establish a mechanism whereas SAIs based on sector developments within their countries could initiate and conduct cooperative audits. For example Tanzania and Uganda have a potential of conducting an audit on the constructed oil pipeline between the countries.

- Enhance online information sharing and learning

To broaden information sharing and enhance capacity building on low budget. The stakeholders should emphasize an online information sharing among the SAIs and e-learning opportunities.



5.4 Online learning:

How to audit government's performance
in managing oil and gas contracts

www.afrosai-e-learning.com

Thank you for joining!

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