



FRAMEWORK OF GOVERNMENT AUDITING STANDARDS FOR OIL COMPANIES UNDER SERVICE CONTRACTS

2022



FRAMEWORK OF GOVERNMENT
AUDITING STANDARDS
STANDARDS FOR OIL
COMPANIES UNDER SERVICE
CONTRACTS



Table of Contents

Quality Assurance Certificate Of The Goal Chair	01
Quality Assurance Certificate of the Chair of the Working Group	02
List of Acronyms	04
Foreword	05
Introduction	06
Chapter One: Theoretical Aspect Of The Guide	07
Chapter Two: Oil Service Contracts	22
Chapter Three: The Procedures Of Supreme Audit Institutions (Sais) To Audit And Control The Costs Of Oil Service Contracts.	43





INTOSAI

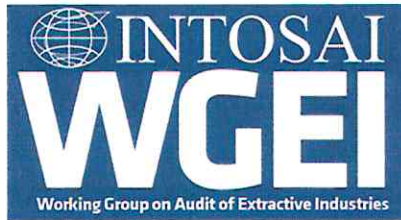
Goal Chairs
Collaboration
PSC - CBC - KSC

**Quality Assurance Certificate of the Chair of the Knowledge Sharing and
Knowledge Services Committee**

Based on the assurance provided by the **INTOSAI Working Group on Audit of Extractive Industries (WGEI)** and the assessment by the Goal Chair, it is certified that the **Extractive Industries Auditor Toolkit**, which is placed at level **3 (three)** of Quality Assurance as defined in the paper on "Quality Assurance on public goods developed outside Due Process" approved by the INTOSAI Governing Board in November 2017, has been developed by following the Quality Assurance processes as detailed in the Quality Assurance Certificate given by the Working Group Chair.

The product is valid till **30 November 2025** and if it is not reviewed and updated by **30 November 2025**, it will cease to be a public good of INTOSAI developed outside the Due Process.

Girish Chandra Murmu
Chair of Knowledge Sharing and
Knowledge Services Committee



Quality Assurance Certificate

Chair of the Working Group on Audit of Extractive Industries (WGEI)

This is to certify that ***the Extractive Industries Auditor Toolkit*** which is placed at level ***three*** of Quality Assurance as defined in the paper on "Quality Assurance on Public goods developed outside Due Process" approved by the INTOSAI Governing Board in November 2017 has been developed by following the Quality Assurance processes as detailed below:

- I. Extractive Industry (EI) team made proposal to develop EI Auditor Toolkit at 2016 WGEI meeting in Kenya*
- II. WGEI Steering Committee agreed to develop Extractive Industries (EI) Toolkit under Activity 4 of the WGEI Workplan (2017 – 2019) at the 2017 WGEI Annual Steering Committee Meeting in the United States.*
- III. EI Toolkit Team presented EI Toolkit progress at 2018 Annual Steering Committee Meeting in South Africa seeking their comments.*
- IV. EI Toolkit Team presented English version of draft EI Toolkit to WGEI members at 2019 WGEI All Members' Meeting the Philippines seeking comments.*
- V. EI Toolkit Team translated the EI Toolkit into Spanish and French in 2020 and into Arabic in 2021.*
- VI. WGEI Secretariat transmitted EI Toolkit feedback surveys in English, Spanish, and French to 39 Members in June 2021 seeking their comments*
- VII. EI Toolkit Team received feedback from 19 Members in July 2021, compiled their comments, prioritized and then addressed the comments.*

VIII. Final draft presented to WGEI Steering Committee for discussion and approval in August 2022. EI Toolkit approved at WGEI Steering Committee meeting in August 2022

The product developed is consistent with relevant INTOSAI Principles and Standards. The structure of the product is in line with the drafting convention of non-IFPP documents.

The product is valid until November 2025 and if it is not reviewed and updated by November 2025, it will cease to be a public good of INTOSAI developed outside the Due Process.



JOHN F.S. MUWANGA

CHAIR OF THE WORKING GROUP WORKING GROUP ON AUDIT OF EXTRACTIVE INDUSTRIES

LIST OF ACRONYMS

AFROSAI-E	African Organisation of English Speaking Supreme Audit Institutions
EI	Extractive Industries
EITI	Extractive Industries Transparency Initiative
IDI	INTOSAI Development Initiative
INTOSAI	International Organisation of Supreme Audit Institutions
SAI	Supreme Audit Institution
WGEI	Working Group on Audit of Extractive Industries

FOREWORD

The Working Group on Audit of Extractive Industries (WGEI) was established by the International Organisation of Supreme Audit Institutions (INTOSAI) in 2013. Currently, the WGEI has 43 Supreme Audit Institutions (SAIs) as its registered members and two observer members namely the INTOSAI Development Initiative (IDI) and AFROSAI-E. The WGEI in its mandate to build the capacity of SAIs intends to develop tools and guidance for the use in the audit of extractive industries based on WGEI members' needs, and thereby promote transparency, accountability and good governance of the sector.

During the Annual WGEI Steering Committee meeting that took place in September 2017 in the United States, SAI Iraq was appointed to prepare a Framework of Government Auditing Standards for Oil Companies under Service Contracts. It worked from 2018 through 2022 and presented regular updates to the Steering Committee and WGEI members. We acknowledge the contribution of SAI members to developing this Framework of Government Auditing Standards for Oil Companies under Service Contracts.

SAI Iraq developed this Framework based on needs of SAIs in countries that employ the service contract model in their oil and gas industry. A survey questionnaire was also developed and circulated among member SAIs by the INTOSAI- WGEI secretariat about the profile of Extractive Industries, audit mandate, experience in audit of Extractive Industries, capacity and learning needs of INTOSAI- WGEI member SAIs to make this Framework relevant and comprehensive.

We feel that it is desirable that member SAIs appoint focal persons in their respective SAIs. These focal persons are expected to bring out needs that will further contribute to improvement of the Framework. We welcome feedback on this Framework from the member SAIs.

INTOSAI-WGEI acknowledges the support and resources provided SAI Iraq, ARABOSAI and all member SAIs for their contribution in preparing this Framework of Government Auditing Standards for Oil Companies under Service Contracts.

The objective of the Framework is to enable Supreme Audit Institutions (SAIs) to audit the most important industrial sectors represented by the extractive industry, specifically oil service contracts concluded between governments and foreign companies. The Framework will be used as a guide by SAIs and interested stakeholders, within and outside the INTOSAI, to develop audit and control procedures for oil service contracts. This Framework is a living document that will be periodically updated.

INTRODUCTION

Proceeding from the objectives of International Organization of Supreme Audit Institutions (INTOSAI), in strengthening control procedures on oil service contracts concluded between crude oil-owning governments and specialized foreign companies, and to enhance the basic factors of good management by ensuring the efficiency and effectiveness of external audit procedures on those contracts, this guide has been prepared to consist of three chapters. The first chapter is concerned with the theoretical aspect of extractive oil industry activities as well as the oil service contracts, the second chapter is concerned with oil service contracts, and the third chapter is concerned with the control and audit procedures on the oil service contracts.

CHAPTER I

**THEORETICAL ASPECT OF THE
GUIDE**

CHAPTER ONE: THEORETICAL ASPECT OF THE GUIDE

1-1 OBJECTIVE OF THE GUIDE

The pilot guide to (audit and control procedures on oil service contracts) contributes to enabling the Supreme Audit Institutions (SAIs) to carry out their tasks in auditing the most important industrial sectors represented by the extractive industry, specifically regarding the audit of oil service contracts concluded between governments and foreign companies. This guide also contributes to achieve other goals are as following: -

1- Providing users with information, data, and the findings of audit and control of oil service contracts.

2- Continuous improvement in the application of the terms of the oil service contracts by discovering deviation in implementation by relying on the procedures provided by this guide.

3- Providing information and data appropriate for future aspirations for the purpose of introducing appropriate improvements for future service contracts by addressing the errors discovered through the application of these procedures over previous decades.

4- Enhancing the effectiveness of the departments and bodies of the Supreme Audit Institutions through the exercise of their supervisory work by relying on the procedures provided by this guide in implementing the types of audits that fall within their functional tasks.

5- Enabling the Supreme Audit Institutions to achieve the concept of sustainable development in managing the most important economic sector for all countries in the world represented by the oil sector and the reflection of its concept on achieving the unified goals related to social, economic, and environmental aspects.

6- The guide aims to achieve the efficiency of supervision operations over the performance of control and audit work on oil service contracts to ensure that the best results are achieved and that they were implemented in accordance with recognized standards as the following: -

A - Follow up on the audit process in all its stages (planning - implementation - preparing the report - follow-up).

B - Reducing the causes of low and unacceptable performance in the audit process.

C - Ensuring the continuity of audit work within the required quality levels.

1-2 IMPORTANCE OF THE GUIDE

IMPORTANCE OF THE GUIDE IS REPRESENTED BY THREE MAIN AXES:-

- FIRST AXIS: IMPORTANCE OF THE GUIDE BASED ON THE IMPORTANCE OF SUPREME AUDIT INSTITUTIONS.

- SECOND AXIS: IMPORTANCE OF THE GUIDE BASED ON THE IMPORTANCE OF OIL SECTOR ACTIVITY.

- THIRD AXIS: IMPORTANCE OF THE GUIDE BASED ON THE IMPORTANCE OF OIL SERVICE CONTRACTS.

FIRST AXIS: IMPORTANCE OF THE GUIDE BASED ON THE IMPORTANCE OF SUPREME AUDIT INSTITUTIONS.

The supreme audit institutions are the highest auditing institutions in any country. These institutions are known for their role in supervising the management of public financial resources. Many of the supreme audit institutions also monitor the compliance of government institutions with the rules and regulations in force and the performance of government programs and policies by auditing the management and performance of public financial and providing an assurance of the use of public resources wisely and efficiently for the benefit of community.

SECOND AXIS: IMPORTANCE OF THE GUIDE BASED ON THE IMPORTANCE OF OIL SERVICE CONTRACTS.

Oil is one of the important extractive minerals, and this importance entails the development of plans and policy formulation for most countries of the world, and the importance of oil in the world is increasing day by day according to its multiple uses, which are no longer limited to lighting, cooling and heating, as was the case in the past, but rather scientific and cognitive progress led to the expansion in its uses, oil has become a source of energy, heat, lighting, the production of chemical and medical compounds and countless other industries. Hence, oil has played a major role in our household and other consumer uses, in transportation and industry. Oil is used as a raw material in many industries such as cosmetics, textile industry and building

materials. In sum, there are more than three thousand products derived from oil, thus providing humanity through these uses with more economic prosperity.

The importance of oil does not need to be emphasized. Oil is of economic and political importance and is of interest to all producing and consuming countries alike. Oil is the main source of national income. The oil-producing countries depend on it to advance their economic and social development, as well as the increasing importance of oil for the developed countries, is due to their dependence on oil for their progress and industrial development.

Accordingly, oil has become a feature of the age, and the twentieth century has been associated with the name of oil, as it was called the age of petroleum, after the use of oil in all areas of life. Despite the continuous changes in scientific discoveries in the research and development of alternative sources, the facts indicate that oil will remain the first strategic commodity in the field of economy and development and in times of war and peace alike.

Therefore, there was a need to provide healthy working conditions and agree to the conditions of occupational safety and health that pertain to the work and workers environment in the extractive industries and mining sector to provide protection for workers from the risks inherent in work sites and the application of occupational health procedures that are concerned with studying the occupational risks resulting from the work environment and finding ways to reduce those risks, unsafe conditions and behaviors from accidents and reducing the danger of equipment and machines to workers, as well as the safety of the work environment from environmental pollution and the causing factors by controlling emissions of toxic gases, liquids and work requirements that are carcinogenic and polluting to the environment resulting from the extraction process, in addition to reducing pollution of the external environment is one of those factors, which requires commitment and serious application of work parameters, guidelines and instructions issued by institutes or centers concerned with occupational health and safety such as (National Institute for Occupational Safety and Health (NIOSH), Environmental Protection Agency (EPA), Safety and Mining Management System (MSHA) and Health System and Environmental Safety (HSE), as well as specifications of the Occupational Safety and Health Administration's standard represented by the latest versions of ISO (ISO: 45001) and environmental management system standards represented by (ISO: 14001) to protect the external environment and improve its conditions which includes (air - water - soil - human - plant - natural resources).

THIRD AXIS: IMPORTANCE OF THE GUIDE BASED ON THE IMPORTANCE OF OIL SERVICE CONTRACTS.

As a result of the great importance of oil, it is imperative for the producing countries to develop administrative, legal, and technical systems to keep pace with the process of optimizing the exploitation of oil, and to deal with international oil companies for the purpose of contributing to the oil-producing countries investing their national wealth in an efficient manner that

guarantees the general national interests and to achieve prosperity for their people. Hence, oil-producing countries should work on developing the administrative and legal system for oil investment contracts (oil licensing contracts) and for the purpose of achieving a balance between production and oil markets controlled by largest companies in the world. These countries tended to develop mechanisms for concluding oil contracts with foreign companies to achieve the best possible profits, with taking the necessary precautions to ensure that the oil reservoirs are not exhausted. The oil-producing countries are the most important party to the oil investment contracts, as they are the owners of the oil wealth, and therefore the producing governments must exercise their legal powers to follow up and monitor those contracts.

1.3 WHAT DO THE INVESTMENT CONTRACTS MEAN IN THE OIL SECTOR?

They are contracts concluded between the contracting countries or one of the companies or institutions and public bodies affiliated with them, and between oil companies, often foreign, for the purpose of searching for and prospecting for oil and then producing it or developing oil fields to reach the highest production capacity in certain places, and for a specific period and for an agreed fees in the contract.

1-4 TYPES OF INVESTMENT CONTRACTS IN THE OIL SECTOR

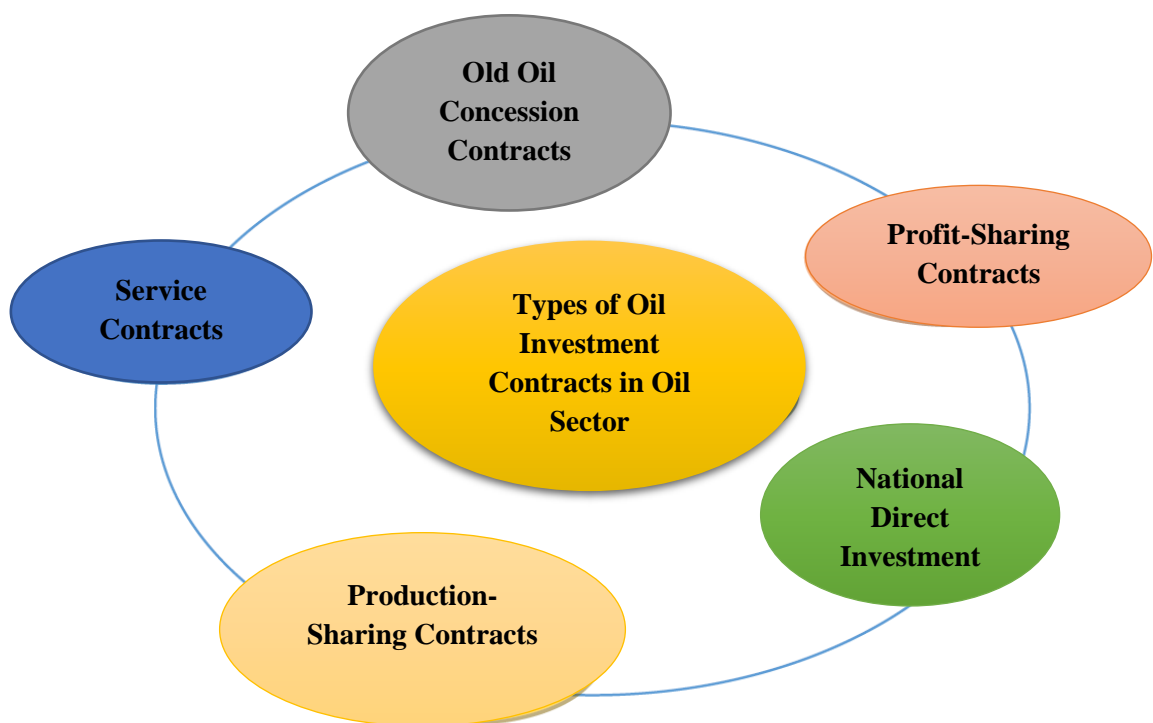


Figure (1) Types of oil investment contracts

1-4-1 Old Oil Concession Contracts:

Concession contracts are the oldest form of petroleum (oil) contracts and can be defined broadly as ((Contracts concluded between oil-producing countries and foreign companies under which those companies are granted the right to invest oil for their own account, with the right to own the oil that they discover in return for some money to be paid to those countries)). And concession agreements, like any contract between two parties, regulate the relationship between the producing country and the oil companies. It defines the rights and duties of each of them. These contracts are classified as one of the old or classic patterns or forms in oil investment.

This type of contracts prevailed in the oil industry under specific political and economic conditions as the giant international companies controlled most of the oil investments in the producing countries.

The international companies that obtained these contracts were able to achieve great, economic advantages due to the positive characteristics in their favor in the content of those contracts, which are represented by: -

- 1- It is the first pattern known to the oil industry that began to be applied in the 1920s and continued until the end of the sixties and the beginning of the seventies.
- 2 - These contracts give concession companies the right to search for and produce oil in large geographical areas for a long period of up to (75) years, without oblige of these companies to the total or partial waive of the contract area specified during the contract period.
- 3-The classic patterns represent the most persistent form in terms of time in the global oil industry.
- 4- The parties benefiting from concession contracts are the foreign companies that enjoy the rights of disposal and ownership in all the circles of the oil industry and the absolute control of these companies over the oil industry in the host countries.
- 5- non-compliance of companies to refining oil locally or investing part of their profits in the host countries, as well as these companies are not subject to the local judiciary in most matters related to the exercise of their activities.
- 6- The concession companies work on discovering, producing, and marketing the oil for their own account, as well as determining the prices without interference of the host country.

7- The stability of the tax rate by making this rate a contractual element so that the legislator in the host country cannot amend it without the approval of the concessionaire.

8- The companies pay certain amounts to the host country in exchange for obtaining the concession contract, and the companies pledge under these contracts to pay specific amounts of cash for each barrel produced of crude oil, without the participation of the host countries in the profits generated from the sale of oil.

9- Concession contracts represent the highest forms of monopolistic exploitation of the oil producing countries.

1-4-2 Profit-Sharing Contracts

These contracts are based on the concept of two parties' participation in the exploitation of the oil wealth inherent in the land or area of the granting party to the oil agreement. These contracts are better than concession contracts because of the clarity of their clauses and the host country's access to some advantages, this type of contracts are known as (Profit-Sharing Contract). The results of this type of contracts are an increase in the revenues of the host countries for each barrel exported, and then an increase in the total oil revenues. Despite this, the companies have retained for themselves the full right to determine prices and methods of earning profits and the right to grant discounts when selling oil to other companies, and this type of oil investment contracts is distinguished with the following characteristics: -

- 1- Adoption of a system of equal profits between the companies and countries granting the concession or contract.
- 2- The two parties (the company and the government) participate in the operations of exploiting the oil wealth, and the term of the contract is up to (25) years after the commercial discovery of oil.
- 3- The area of the lands granted in the contract is limited and the non-invested lands are abandoned.
- 4- The foreign and national party's share of the oil production shall be divided equally with the foreign party paying the government's dues of taxes and fees, and the government's revenues shall be calculated according to the declared or realized prices or as agreed upon.
- 4- The foreign party shall bear the necessary investments for the development and discovery of oil fields until the stage of commercial exploitation of oil.

1-4-3 Direct National Investment

This type of investment is based on the government or one of its national companies exploiting the country's oil wealth independently or by benefiting from some foreign and national expertise, and this type of investment is formed through the total or partial transfer of ownership of the oil industry from foreign companies to oil companies. The direct national investment can achieve the following advantages:

- 1- Total ownership of all oil industrial activities.
- 2- The material and technical advantages achieved by the oil country.
- 3- High flexibility in dealing with international parties in the oil industry.
- 4- Getting rid of the control of global oil monopolies.
- 5- Putting oil at the service of economic development.

1-4-4 Production Sharing Contracts

It means an agreement between a country that grants a concession on the one hand with another investor on the other hand, whether foreign or local, for discovery and exploration or for the exploitation of oil wealth in certain areas in the oil state for a specific period. The risks are the main idea on which those contracts are based. If this type appeared in areas where expectations were weak for the presence of oil, or the presence of oil requires high costs to reach the oil reservoirs, so the contracting company spends free of charge until the discovery of oil, then the company's costs and what it spent are calculated, and a new relationship begins, represented by a partnership contract in the event that the discovered quantities are valid for investment.

In the absence of oil, the investing company is the one who bears the loss because it risked those costs to obtain future profits, which is a formula for each party to exploit the other. As the company wants to exploit the oil of the state on its territory, and the state wants to exploit the company's money and capabilities because it needs them for the security of obtaining oil resources, which is the result of the objections to the concession contracts and their negative aspects against the oil state, the formulas of these contracts have been developed to avoid the wave of objections to the previous one.

The partnership contract extends between (20-40) years, and the specialists believe that the partnership contracts cannot be relied upon in the country where the expectations of the presence of oil are high. An example of this is Iraq, as it is considered part of a sedimentary basin in the geological aspect, and its lands contain oil rock layers. All studies confirm the existence of large oil reservoirs with different depths.

In essence, production-sharing contracts do not differ from concession contracts except to show state control, as they give the impression of state ownership and control over its oil resources while remaining the essence of oil-sharing contracts for the benefit of foreign companies. In terms of their parties, these contracts take one of three forms either the contract is concluded between the producing country and the foreign company. Provided that a company

is established in which the state or one of its institutions contributes a share in its capital, after the discovery of oil in commercial quantities, such as the contract of the French company (OKcira ap) with the Saudi government, or the contracts are concluded between the oil producing state and its national institutions from one hand, and the foreign company on the other hand. Examples of this are the contracts of the Republic of Egypt with the Egyptian Petroleum Corporation and Saint American and Phillips in 1964. The other form is that the contract is concluded between one of the national companies of the producing state and the foreign companies by authorizing the government to the national company, as was the case in the Iranian contracts in 1957 AD.

Participation contracts may provide for the establishment of a company in the producing countries to carry out the works agreed upon in the contract, or the contracts may include some obligations on the foreign company, such as establishing a factory, laying a pipeline, or otherwise.

The production sharing contracts are distinguished by the fact that they allow the producing country to exercise control over the foreign company's activities, and it has the right to participate in the marketing of oil. It also contributes to acquiring the experiences and avoiding the loss by making the foreign company bears the financing operations until the discovery of commercial oil and the start of production, and the foreign company will be a partner in accordance with the concluded contract.

1-4-5 Service Contracts

This type of contract is called by several names, such as the contract, the contracting, the rent of services, the mandate, or the work contract, as the oil-producing countries continued to seek formulas for oil contracts that give them greater guarantee of national control in order to develop their oil industry on the one hand and limit from the control of the interference of foreign companies from the other side. In the second half of the twentieth century and with the emergence of wealth liberation movements, service contracts appeared, but they were not widely used. This type of contracts is based on a national party contracting with a foreign company to do some work in the oil sector for a certain amount to be agreed upon, and upon the end of its tasks, its connection with the project ends. The service contracts are defined as (a contractual pattern to organize the relationship between the oil-producing country on the one hand, and the specialized international oil companies on the other hand, to explore and develop oil and natural gas fields for a specified fee). This type of contract will be discussed in detail in the second chapter of this guide.

1-5 The Concept of Value Chain

It is a term used in the field of business management to express the group of activities performed by a company operating in a specific industry in order to provide a product of value in other words (a good and/or service to the market), and it can be used in industrial service establishments in which the activities are divided into basic activities and supporting activities or subsidiary, the basic activities are the set of activities, procedures and actions carried out by the institution that lead to the realization of value. The supporting activities are those that lead to add the effectiveness, efficiency, and economy of value production. Below are the seven steps of the extractive industries value chain: -



Figure (2) Steps in the Value Chain of Extractive Industries

1-5-1- Legal Framework

The assessment of the legal framework across the value chain of the Extractives Industries (EI) requires the application of specific legislation regulating the activities of each component of the EI value chain. The auditor must understand all applicable legislation to identify any gaps, inconsistencies, and areas to which different interpretations apply. As explained above, auditors should not expect to find all these elements included in legislation, as some Supreme Audit Institutions (SAIs) are competent to evaluate specific legislation, while others do not have such powers.

Legal tools such as international treaties, national laws and other regulations and contracts constitute a framework for extractive industries, and the responsibilities of government and non-governmental entities related to their work in extractive industries can contribute to assisting SAIs in measuring the institutional capacity of the government to supervise the extractive industries sector.

1-5-2 Resource Exploration

The constitution or law in most countries states that the government owns what lies beneath the surface of land from resources, and the government, in turn, grants private companies or other parties the right to explore and extract resources, so that that country can benefit from the

emerging capital. The legislature shall make political decisions regarding the opening of exploration areas, based on recommendations from the executive branch. There should be indications of potential reserves, environmental impact assessments and the establishment of relevant government institutions. If exploration indicates the presence of significant natural resources, the government may proceed with a decision of extraction.

1-5-3 Award of Contracts and Licenses

Through negotiations with petroleum companies, contracts are contracted according to the legislation in force, the auditor must determine the discretionary authority granted to individuals and even public service employees regarding the quorum for the purpose of signing contracts with petroleum companies, with a focus on tax incentives or tax exemptions. Experience shows that granting tax incentives significantly reduces the tax base, creates scope for bribery and corruption, and increases the emergence of tax evasion loopholes.

1-5-4 Monitoring of Operations

The legislative framework should provide for the supervisory authorities entrusted with monitoring operations, and the terms of reference of these authorities should also include useful information about their tasks. Regulations usually deal with quality controls and measurement, the quantities produced and the quantities sold or exported, and aspects of human resources, safety, and environment.

1-5-4 Collection of Revenue

Receipts from the extractive industry are often the most important revenues, and tax legislation must be updated to match the large profits obtained from extracting these resources, and special tax rates must be applied. Revenues from petroleum production agreements/contracts often constitute the largest revenue from the petroleum sector, and auditors can assess the clarity of tax legislation and petroleum production agreements/contracts on how to calculate the exploration costs that can be deducted from the total revenue. Specific provisions must also be established in legislation and agreements on purely commercial basis. It is also necessary to study the possibility of applying a general rule to combat tax evasion, and specific requirements should be established for the preparation of reports on the quantity and quality of extractive industry production and exports so that revenues auditors can compare audited financial statements and tax returns with actual and relevant production and sales figures.

1-5-6 Revenue Management

Legislation should clearly define how the revenues from the extractive industry are managed and allocated to ensure that the revenues are used for the purposes of diversifying the economy,

and clear procedures should be applied to invest the collected revenues and ensure the distribution of the greatest number of profits.

1-5-7 Implementing Sustainable Policies

Given the impact of natural resource extraction and production on the environmental, social, and economic aspects of the concerned country, therefore the legal framework for the extractive industry must include regulations governing these aspects at every step of the entire extractive value chain. These are environmental laws, local content law, labor law, as well as environmental, social, health and safety regulations. The steps related to policy, the legal framework, and the implementations of sustainable policies are issues of importance in the extractive industry.

The extractive industry value chain illustrates seven different steps when converting natural resources into national income and ultimately economic growth for the citizens of any country. The value chain is used repeatedly to clarify the potential impact of the government in each step. The steps represent a critical distinctive and necessary area to generate the value (revenue, employment, capacity building, etc.) for the population of the country. The following table describes each step in the value chain and potential audit topics along the same lines, as well as examples of relevant audit reports conducted by the various SAIs:

Table (1): The Value Chain of Extractive Industries and Audit Areas

The value of the extractive industries	Activity type	Description	Examples of areas of audit	Examples of audit reports
1 - Legal framework	The supportive activities	The existence of updated laws, regulations and policies represents the basis for the proper management of the extractive industries sector, with the need for a clear separation of duties and responsibilities.	The SAI shall audit whether the laws are supported by the relevant regulations and instructions and indicate an overlap or a lack of clarity in the lines of responsibility between institutions.	The results of the compliance audit as well as that the reports provide reasonable assurance of the existence of an appropriate and appropriate legislative framework for all stages of the extractive industry.

2- Resource Exploration	The basic activities	The development of the extractive industry to meet the needs of the government to draw a map of its reserves, data are collected from oil and gas resources mainly through seismic surveys and drilling, and data on mineral resources are collected from geological samples.	The SAI shall audit whether the relevant data is properly managed and secured.	Performance audit of hydrocarbon exploration efforts in the oil and gas industry.
3 - Award of Contracts and Licenses	The basic activities	The government awards contracts or licenses to companies to explore, develop and produce extractive industries resources. This process is supposed to follow competitive rules, and instructions to ensure that the most efficient and cost-effective companies are selected.	The SAI shall audit whether the process of handing over contracts and licenses is transparent and designed to attract companies that are efficient and adhere to government policies. SAI may also audit whether the process is in line with the laws and regulations.	The SAI conducts the administrative practice with regard to the granting of production licenses in the oil sector.
4- Monitoring of operations	The basic activities	The government monitors the	The SAI shall audit whether the government	

		<p>activities of extractive industries companies in a number of areas, production numbers must be verified in terms of quality and quantity, by independent control units, health, safety and environmental risks must be addressed and followed up through inspections.</p> <p>Reviewing the safety procedures, impact assessments, etc.</p>	<p>is complying with its roles as an extractive industry regulator. SAI also can assess how the government performs inspections and obtain confirmation of the quality of information reported by extractive industries companies.</p>	<p>Making ensure that reports of oil and gas production provide a reasonable guarantee of an accurate measurement of the volume of production.</p>
<p>5- Collection of Revenue</p>	<p>The basic activities</p>	<p>The government has several tax tools at its disposal for the purposes of revenue collection, royalty, production sharing, bonuses, taxes, and others, all of which aim to give the government its fair share of revenue.</p> <p>Risks may be associated with a</p>	<p>The Supreme Audit Institution follows up checking the estimated and actual revenues, comparing them, and finding out the reasons for deviations.</p>	<p>consistent audit on the oversight of public revenues from exploration, production and signing of service contracts.</p>

		wrong calculation of revenues based on wrong input data or inflated costs by companies.		
6- Revenue Management	The basic activities	<p>After the revenue is collected, the next step is to allocate the funds. Using revenues to support public budget, and reserve, etc., and there might be a potential for mishandling of revenues.</p> <p>Revenues may be distributed to foreign bank accounts that have not been disclosed and the investment rules are not being followed.</p>	The SAI shall follow the audit of estimated and actual revenues, and their comparison. And knowing the reasons behind their deviations.	Audit of the financial management of the oil fund, as well as performance and compliance audit.
7-Implementing Sustainable Policies	The supportive activity	It is important to consider the potential negative impacts of the extractive industries sector, such as environmental damage and the dependence of extractive industries on eco-friendly resources.	The SAI reviews how to implement laws and regulations aimed at limiting the negative impact of the extractive industries sector, and whether the government's control system is effective.	<p>Report on the environmental impact and implementation of local content policies.</p> <p>Environmental audit report on the regulation and control of drilling waste management.</p>

Chapter II

Oil Service Contracts

Chapter Two: Oil Service Contracts

The host countries or (the national company) leases under service contracts the services of a foreign oil company that takes the legal status as a contractor and according to the service contracts, the national company enters a contract with a foreign oil company (contractor) when it wants to benefit from additional experience or ability to perform technical service or, development and production service under this contract. The contractor undertakes to provide certain services within a specified period and in return for fees and rewards fixed in the contract. The foreign company bears the capital costs required for all investment, financing, implementation of development, and production operations. And when production begins, its investments are recovered in return for a lump sum fee for each produced barrel paid in cash or in kind with oil, and this lump sum fees covers all costs and profits. This company also manages oil operations for the duration of the contract, which usually ranges between (5-10) years. A joint management committee is formed between them to coordinate and follow up on common matters. One of the advantages from the oil service contracts is getting rid from the problem of agreeing on the price of crude oil.

2-1 The mechanism of payment of financial dues under service contracts:

The amounts due to foreign companies and their interests are paid either in direct cash or by delivering crude oil from the fields that will be developed and produced under those contracts or other producing fields, meaning that the foreign investor can be considered a contractor working on behalf of the national oil company in the producing country without having rights, ownership or participation of this ownership, provided that the foreign investor bears all the investment risks in the event of its failure, while the national companies bear the full cost of the risks in the event of their success.

Usually, national oil companies with extensive experience and experienced national technical staff for many years benefit from these services in some specific oil fields and oil businesses to rehabilitate and develop the oil sector, and it is preferable that financing this method be possible for works, complementary projects, and development projects to develop oil fields of small size. It is noticeable that the advantage from this method of oil investment is the recognition of the oil state's ownership whether before oil production or in its later stages because the contractor is considered an entrepreneur working for the host country and all works done by that contractor returns to this country.

2-2 Types of Service Contracts:

First: Classifying service contracts in terms of risks into two types: -

The first type: is for the foreign company to provide the capital required to implement the contract on condition that it is recoverable with interest during a specified period after the production stage, either in cash, or in-kind, or by giving the foreign company the right to purchase part of the production for a specified period, at a specified reduced price. Thus, the amount spent by the foreign company is a loan with interest to be repaid in the shortest period. The profits of the foreign company may be subject to tax, according to the agreement and the terms of the contract. Examples of this are patterns of contracts in the Republic of Iraq.

The second type: This type of service contract is that the producing country bears all or some of the risks associated with the discovery, and the foreign company is hired for implementation, and that reduces what the producing country pays to the foreign company for its services provided. These contracts were developed as technical contracts. As some countries don't suffer from a scarcity of capital, but rather a lack of technology and technical expertise, so technical service contracts are used, and in the light of this contract, the foreign company carries out specific tasks such as exploration, development, or any other services for specific fees.

Second: Classification of service contracts in terms of petroleum activities.

It is also worth noting that there is another classification of these contracts according to the petroleum activities covered by these contracts, as follows: -

No.	Types of Contracts	Abbreviation
1	TECHNICAL SERVICE CONTRACT	TSC
2	DEVELOPMENT AND PRODUCTION SERVICE CONTRACT	DPSC
3	GAS DEVELOPMENT AND PRODUCTION SERVICE CONTRACT	GDPS
4	EXPLORATION, DEVELOPMENT AND PRODUCTION SERVICE CONTRACT	EDPSC

Table (2) Types of Contracts according to the petroleum activities

2-3 Reasons for resorting to oil service contracts

1. When national governments are faced with the high costs of extracting crude oil or the desire to obtain a high level of advanced technical progress in the oil industry, which

is reflected in reducing the costs of extraction per barrel of crude oil, and this in turn leads to an increase in the revenues of the oil industry in those countries.

2. When the national governments in the oil-producing countries wish to provide large production capacities to ensure the high flexibility of the oil supply to keep pace with any increase in the local and global demand for crude oil.
3. When the oil industry in the oil-producing countries faces a rise in the rates of uncertainty and risks in extractive oil activities. The oil industry always faces risk factors related to traditional risks, such as not finding crude oil in economic quantities in oil reservoirs, and local governments in these countries resort to service contracts to charge foreign oil companies the costs of exploration considering the high risks of not extracting oil in economic quantities.
4. Increasing the quantities of production of crude oil to achieve the strength of the forward links of the oil industry, meaning the contribution of the oil industry to transforming and equipping existing and new industries to ensure the sustainability of the refining and chemical industries and the rest of the economic industries.
5. To address some of the technical and environmental problems faced by the oil-producing countries in their extractive industries, such as reduced reservoir pressures or burning large quantities of associated natural gas so national governments in those countries resorted to sign service contracts to address those problems.

2-4 Common characteristics of oil service contracts

Service contracts vary among themselves, but the common characteristics between them are as following: -

A- The sole owner of the oil is the national party, as well as the land and fixed assets within the operations of the project belong to the oil state.

B- The revenue of the foreign company shall be in return for the obligations that have been undertaken, either a cash or in-kind, or giving the right to purchase a specific percentage of the produced oil at a reduced price and according to the agreement.

C- A joint management for the project is formed for coordination and follow-up.

One of the advantages of these contracts is that they contribute to the development and training of national cadres, to work with foreign companies, as well as succeed in complementary projects to develop the small-sized oil fields.

2.5 Petroleum activities targeted by petroleum service contracts

The process of the oil industry includes several operations and activities and passes through several stages before it reaches the final consumer. It is possible to sign services contracts with international oil companies specialized in all the stages, which areas following: -

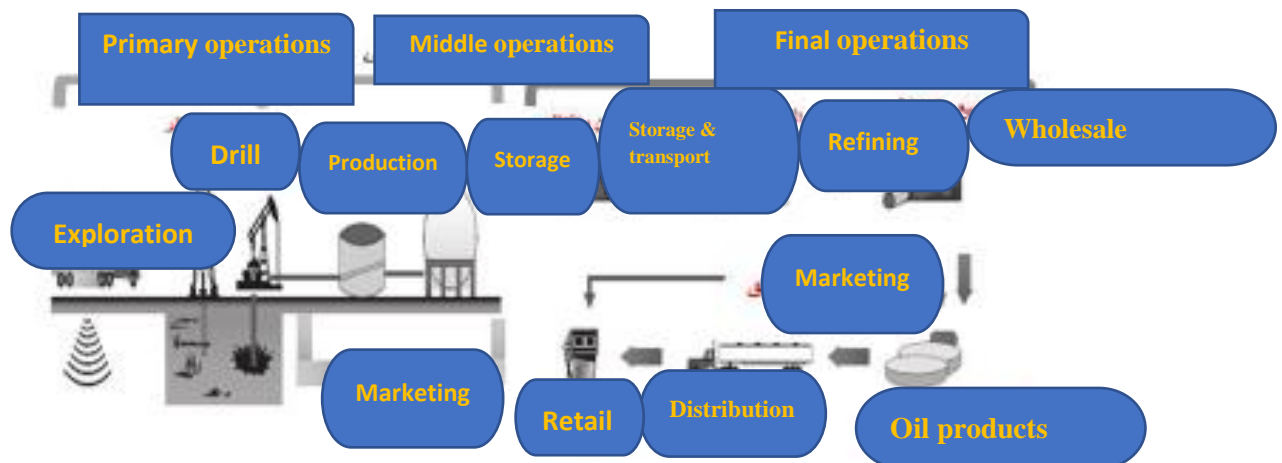


Figure (3) Stages of Oil Industry in Iraqi Ministry of Oil

2.5-1 The stage of drilling and exploration.

It is considered the first step in the process of exploring for crude oil, which is concerned with defining the geographical area in which the search activities will be conducted after obtaining a field called the exploration field, then analyzing the layers of the earth in preparation for determining the place where there are likely oil reserves and thus drilling exploratory wells and exploration according to a contract with the owner of the land. For defining the area, geological information about the geographical area is used and after determining the area and the company obtaining permission to conduct exploration operations, the part, or parts of the area in which drilling, and exploration operations will be concentrated is determined.

Research and oil exploration also requires large material investments, advanced technological expertise, and continuous financing for the exploration plans, and the integration of oil mining, manufacturing, transportation, and marketing elements. Onshore drilling is more expensive and dangerous than offshore drilling.

The obvious goal of exploration is to search for reservoirs of oil gathering using various types of survey, and aerial, ground, and subsurface detection. Oil leaching is considered a positive indicator for identifying most of the exploration areas, as well as searching for oil in certain structural contours, such as convex folds and domes.

Despite the tremendous technological development in the field of oil drilling and exploration, drilling is the only sure way to ascertain the presence of oil, and it is necessary to drill, as it is the decisive factor in oil exploration, and its success is linked to the accurate determination of the locations of the wells, the assessment of the potential depth for the presence of oil, and the efficiency of drilling programming and information systems, however, drilling wells has become of high cost, and if the drilling company is not in a good financial position, drilling a number of dry wells may lead to bankruptcy.

The border wells, which are dug to discover oil concentrations, are called exploratory wells. If the exploratory wells achieve success, they are called (discovery wells); otherwise, they are dry or empty wells. The first wells that are drilled to know the boundaries of the oil field after the discovery of oil are called designation wells or border wells, they are either successful or dry wells.

As for the wells that are drilled to exploit the oil field, they are called development wells, although drilling the initial well gives evidence of the presence of oil, the composition of the oil reservoir, and the depths of the container layers. However, defining the oil field, calculating the quantities of oil expected to be produced, and estimating the likely reserves of oil in the field require drilling other exploratory wells around the initial well, and in many cases, deep “bottom wells” are drilled in places suitable for oil gathering to study the geological structure and hydrological conditions for the formation of sedimentary layers, as well as ((parametric wells)) to check information on the geological structures of rocks in the exploratory research area.

2-5-2 Evaluation stage

At this stage, the technical feasibility, and the possibility of the presence of oil in commercial quantities are evaluated at the area in which oil reserve was obtained. Accordingly, the capital costs required for development and production are being known if it becomes clear that there is oil in commercial quantities.

2-5-3 Development stage

Once it is confirmed that the oil is in commercial quantities, the necessary arrangements are made for development, starting with preparing the sites for drilling development wells, installing drilling and production equipment, and even making the oil suitable for transportation and marketing.

2-5-4 Production stage

This stage includes extracting the oil to the surface of the earth and preparing it until it is ready for shipment or marketing. This includes raising the oil to the surface, assembling the products of the various wells to a specific collection area in the field and working on the necessary field treatment. This stage begins after the producing company has taken all the necessary steps in the stages of survey, discovery, exploration, and drilling exploratory wells. And based on the results of the evaluation and testing of exploratory wells, either the construction of surface facilities, the drilling of developmental wells, and the installation of equipment to complete the well, the most important of which is the wellhead, which is in the form of a (Christmas tree) that consisting of a number of valves to control the quantities of oil flowing, Or locking / abandoning the well due to the lack of reserves in the necessary commercial quantities.

The production process includes all the necessary steps to withdraw oil from the wells until it is delivered to the marketing or export sites, although the order of the necessary steps may differ according to the production sites in each field. However, these steps can be summarized as follows:

1- Withdrawal from the wells

This is represented in the flow of oil from wells through pipes to the surface of the earth, and this may be done in a natural way depending on the high degree of the reservoir pressure than the pressure at the bottom of the well and the viscosity of the oil due to the presence of a large amount of dissolved gas or the presence of a water layer below the oil layers and between the rocky pores (restrained water) the natural production may be the result of more of these factors. The reservoir pressure may be low, so industrial methods are used to help increase the pressure in the reservoir, such as pumps, gas injection, or water injection. With considering, the extraction factor at production.

2- Separation and treatment

Oil is extracted from wells and collected in separation and treatment stations, where it is subjected to a series of operations that result in obtaining oil and gas separately after getting rid of the brine, and despite the separation and treatment processes, the crude oil still retains a quantity of water and some impurities. The producing companies work on carrying out the necessary laboratory tests to ensure that the percentage of water and impurities does not exceed the universally permissible in oil industry. This stage requires identifying and preparing successful oil wells and establishing extraction facilities from pipelines, tanks, etc., and the period for this stage ranges between 3-4 years, the oil extraction process is done by one of the following two ways:

A - Natural Method

It means the natural flow of crude oil from the ground under the influence of the natural forces inherent in the oil well, as the oil flows with the natural thrust inherent in the depths and resulting from the following reasons:

- Gas dissolved in petroleum.
- Free gas in the oil reservoir.
- Mixed water.
- Gravity thrust in pressurized warehouses.

And all of them may be in the reservoir and lead to the flow of oil automatically. This method is one of the methods with low costs and is characterized by short time required to complete the extraction operations. The natural flow of oil is in the early periods of the life of the oil well, and if these pressures decrease, they are resorting to the means of industrial lifting to raise the oil to the surface of the earth.

B-Industrial Method

This method depends on industrial means for the purpose of increasing the reservoir pressure in the oil well, which leads to an increase in the flow of crude oil.

- (WATER INJECTION) the water is pumped from the wells at lower level in the oil reservoir to raise the pressure inside it and continue the flow of oil from other wells around it.
- (GAS INJECTION) Natural gas is pumped from one of the wells at the highest point in the oil reservoir to raise the pressure inside it and continue the flow of oil from other wells around the injection well.
- Suction pumps (PUMPS) a pump is lowered to withdraw oil from the bottom of the well and raise it to the surface.
- Chemical treatment (CHEMICAL TREATMENT) Chemical acids are injected to improve the properties of the rock (permeability) so that the oil is easily allowed through.
- Dissolving Oil (MISCIBLE FLOOD) An oil solvent of the same type (hydrogenated carbonate) such as (propane) is injected to reduce the viscosity of the oil, which helps to increase its flow.

- **Heating (FIRE FLOOD)** The oil is heated if it is of a heavy type to reduce its viscosity, either by injecting hot water vapor or by injecting air into the reservoir and setting fire to part of the petroleum in it.

The extraction of crude oil also requires large expenses that vary depending on the nature of the area covered by the oil extraction, the quantities of crude oil, the nature of the prevailing technical and economic conditions, and the approved extraction method.

The ratio of the oil that can be extracted to the oil in one of the reservoirs is called the extractive ratio. This ratio depends on the nature of the oil-bearing rock and on the type of crude oil itself.

And when all industrial means are unable to extract more oil so that it does not cover the production costs, it is said that the reservoir has been depleted, and the field is abandoned, and the wells are closed.

Oil engineers work to extend the life of oil reservoirs (oil reserves) to extract the highest percentage of the oil contained within them. They direct their attention to studying the properties of the producing layer, determining the locations of wells, and calculating the ideal production rates. We must point out the fact that exceeding the withdrawn production quantities may accelerate the end of the reservoir life (oil reserves). Consequently, large quantities of oil remain underground, and it is impossible to extract them despite the presence of wells.

2-5-5 Stage of Storage, Transportation and Sale

After the crude oil is separated from gas and treated from water and other impurities, it is stored in tanks for the purpose of shipping to investors, which is the last activity in the crude oil industry. At this stage, the process of shipping and marketing the crude oil is finally done to consumers. The process of shipping crude oil from assembly warehouses is carried out according to issuance documents prepared by the shipper's warehouse to be sent to customers and marketed through different outlets, or to refinery plants. Crude oil transportation is one of the important stages through which crude oil is transported from production areas to consumption areas by specialized means of transport that can be identified as follows: -

1- **Means of Land Transport:** including pipelines, railways and large truckloads.

2- **Maritime and River Transportation:** These include tankers, river ships and floating containers. Pipeline transportation is linked to the history of the oil industry, and pipeline transportation has spread throughout the world, as the increasing oil production and the expansion of markets require the presence of important and reliable extraction and distribution

means, and the expansion of pipeline networks to transport oil over long distances that may sometimes exceed thousands of miles inside or outside the political borders of the state.

In recent years, there has been a significant increase in the lengths of the pipelines that transport crude oil from the producing fields to the docks for oil tankers or directly to refineries, as well as the pipes that transport petroleum products to the main distribution centers.

Interest is increasing towards the use of pipelines to transport crude oil, as well as pipeline networks that connect wells to separation centers and collection stations. Pipeline networks consist of main and subsidiary pipelines, oil storage tanks, pump stations, and receivers, wired and wireless transmissions, television circuits and electronic systems.

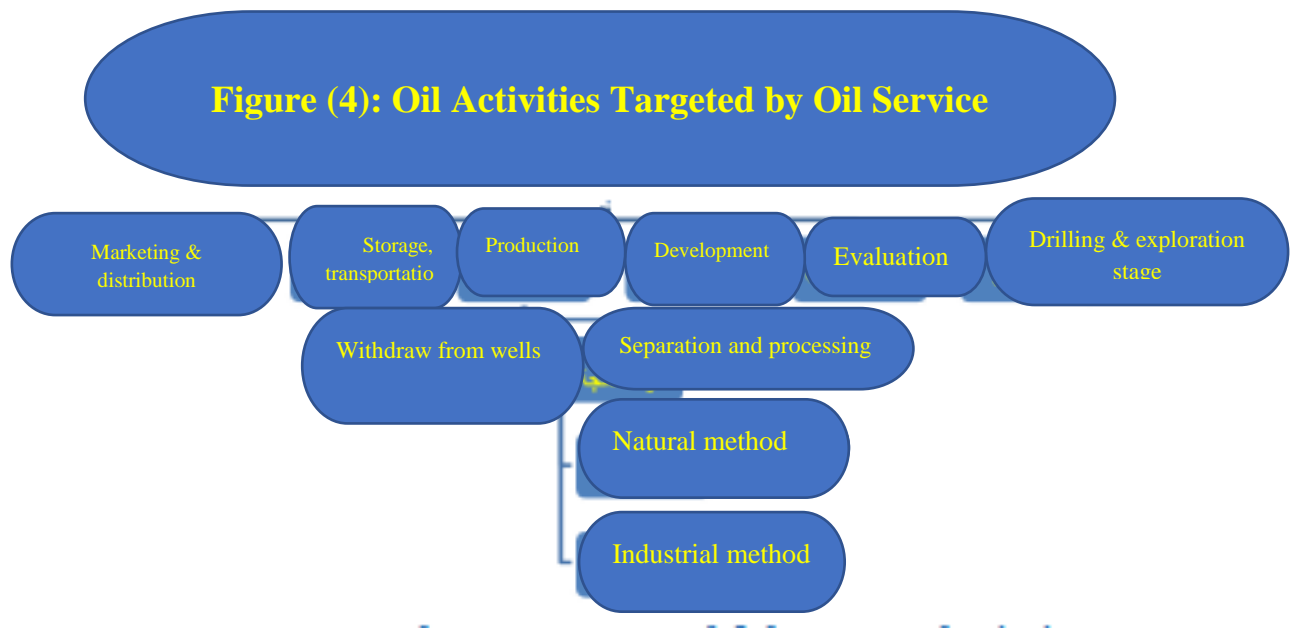
The oil is transported from each of the oil wells by a pipe to the nearest tank and then pushed to the collection tanks in the fields to complete the primary treatment process, and then pushed to the refineries directly or to shipping ports for export.

Conducting market studies to determine the size and nature of demand and supply for crude oil or derivatives. Most of the oil travels through pipelines for at least part of its journey, and some pipelines can transport more than one million barrels of oil per day, and pipelines can be built in almost any terrain and climate.

2-5-6 Marketing and Distribution Stage

It includes the link between the producer and the consumer, and aims to deliver crude oil or oil products to the local or foreign market through various distribution activities represented by a group of means, capabilities and fixed and mobile stations, and this stage needs a set of economic activities to determine the required quantities of crude oil or refined products in the domestic and foreign market, this is done through the following: -

- 1- Performing market studies to determine the size and nature of demand and supply of crude oil or the petroleum derivatives over different timescales in the short and long term.
- 2- Identifying the parties dealing in the oil market and providing the necessary capabilities and procedures to implement contracts of buying and selling in the oil market.
- 3- Preparing specialized means of transportation and all associated loading and unloading operations.
- 4- Providing administrative facilities for marketing and distribution operations.
- 5- Providing advertising media to promote refined petroleum products.



2-6 Parties to signing service contracts and the mechanism for collecting cash claims:

Because of the high cost of exploration and development of oil fields, as well as the high costs of extracting crude oil from the ground and the seas, oil service contracts are signed between the government side and a consortium of foreign oil companies. Considering this, these companies can be classified into:

- 1- The contractor\operator undertakes the implementation of the contracted oil activities.
 1. Other operating companies with the contractor\operator.
 2. The company of local and foreign subcontractor.

Based on that, the relationship between these companies is organized according to the following:

-The contractor\operator shall, within a period (a month or a quarter) as agreed under the service contract, specify the cash or liquidity required to fulfill the obligations of that period.

- The contractor\operator puts estimates of the needs of a whole year or every three months in advance. In most cases, estimates are prepared for a whole year and are divided into quarters to allow the partners to make the necessary arrangements on their part and schedule the payment of the required amounts.

- If any of the companies, which participate with the operator, do not pay their share of the costs, then the contractor\operator has the right to calculate the delay interest on the delayed partner using the prevailing interest rate in the market.

And considering service contracts, we find that the situation of the host country is not affected by these payments, but these monetary claims are made between the contractor\operator and other partners.

There are two ways in which the contractor\operator collects cash claims from partners as following: -

- Advance payments.
- Pay and then claim payment.

2-7 Preparing the necessary estimates for the implementation of the activities within the service contracts:

When submitting the annual work program and budget for the purpose of approval by the authorized body under the terms of the service contract, the operating company must write down the following details related to employees, specific services and customs tariffs related to petroleum operations to be calculated during the relevant year and as follows: -

1- With regard to personnel costs

- First: Estimate the total amount of the costs of salaries and wages of employees and workers.
- Second: Analyzing and clarifying the applicable personnel policy and the practice of the operating company and its subsidiaries or companies involved with it in implementing the service contract (allied with it).
- Third: Reasonable suspension of the above-mentioned expenses.
- Fourth: The ratios and/or methods of apportioning those costs.

2- With regard to services costs

- First: Estimate the total amount of service costs.
- Second: Reasonable suspension of such services.
- Third: Customs tariffs and rates expected to be applied in relation to those services.

3- Regarding Tariffs

First: estimate the total amount to be paid.

Second: Reasonable cessation of customs tariff expenditures.

4- Purchase Costs

A- All materials related to petroleum operations are purchased at a competitive price from well-known factories or suppliers, and the materials purchased from the third party are calculated at the net cost paid by the contractor after deducting all discounts received. The net cost includes transportation, insurance, license fees, purchase, and dispatch costs.

B- The parties may supply the new materials from their own warehouses, provided that the new materials are transferred from the warehouses to other facilities of the establishments where the contractor or his related subsidiaries are concerned, and they should be priced at cost, provided that it does not exceed the price of new materials of the same quality, which are obtained according to the terms and conditions of procurement from global markets while supplying new materials to the contractor and operator.

5- Direct and Indirect Costs

The costs are calculated at the operating account using fixed methods from one year to another, and the parties should agree to these methods according to the following bases:

A- Calculating the costs that can be calculated directly on any classification of the operating account.

B- The costs that cannot be calculated directly shall be divided into any classification of the operating account according to time or other appropriate bases.

C- The costs of services that cannot be accurately estimated may be calculated according to standard rates and adjusted to become actual costs at the end of the year.

For the purpose of using any equipment or facilities completely owned by the contractor's facilities, the operating account is calculated according to the rental bases, which are commensurate with the costs of ownership. It also requires the approval of the authorized body under the contract on those estimates, such as (Joint Management Committee JMC or Board of Directors) in each calendar year on the rental rates, which will not include any element of profit and that such ratios should be linked with those ratios currently prevailing in the area in which the petroleum operations are located for the purpose of suitability of equipment and facilities with regard to their availability, safety, adequacy and its quality.

6- Settlements

In the event that one of the non-operating companies (partners who are not operating) objects to a specific item mentioned in the claim list, it will be dissolved in accordance with the provisions of the contract. Generally, with the exception of rare cases, the non-operating partner must continue to pay to fulfill the operator's obligations until the dispute is resolved.

7- Distribution of Joint Costs

The operating company may have employees or equipment that serves more than one contract, and therefore the necessary distribution must be made in accordance with internationally accepted accounting practices. However, the problem is that there are no acceptable international practices for distributing the common costs in the oil industry.

Accordingly, the operating company must confirm and clarify the fairness of the method be followed in distributing the joint costs.

2-8 The submission of the operating company to the invoice of petroleum costs, supplementary costs and service fees

The operating company must submit to the government side, during the period specified under the service contract, such as after the end of the last month of each quarter, the invoice for petroleum costs, supplementary costs, and due service fees (to be paid) for each quarter (every three months) and based on the operational account, indicating the following: -

1. Petroleum costs, supplementary costs and due service fees carried forward from the previous quarter, if any.
2. Petroleum costs, supplementary costs, and service fees during the quarter.
3. Total petroleum costs, supplementary costs, and service fees for the quarter.
4. Petroleum costs, supplementary costs and service fees required during the quarter.
5. Amounts of petroleum costs, supplementary costs, and service fees to be carried forward into the succeeding quarter, if any.
6. Specifying the petroleum costs according to their sub-accounts whose details included in the accounting system adopted for the

generally accepted accounting policies. These costs shall be studied in the light of the total production of crude oil during the quarter and baseline production quantities in the oil field under the service contract.

2-9 The costs excluded from the claimed invoice as non-recoverable costs

1. The costs incurred because of any willful negligence or mismanagement by the contractor/operator shall be established including any amounts paid to settle any complaint alleging total negligence or willful mismanagement.
2. Exchanging contractor and/or repairing costs related to assets or other property that are not insured or not covered by insurance and obligations incurred to third parties on a strict obligation basis and when the contractor and operator agree with the host country's oil company to insure against such loss, but they fail to do so.
3. Any expenditure incurred directly or indirectly in connection with the raising of money to finance Petroleum Operations and other incidental costs and charges related thereto by whatever method raised; such expenditure includes, but is not limited to, interest, commissions, fees, and brokerage.
4. Any costs, expenses, or expenditures, including grants related to public relations or the promotion of interests and common concepts of the contractor.
5. Any incurred expenses that are not related to petroleum operations or related to them or activities beyond a delivery point.
6. Corporate income tax.
7. Training, technology, and scholarship funds.
8. Signature bonus.

9. Payments made more than taxes to the host country's oil company under contract.
10. Any other costs mentioned in the service contract as non-recoverable costs.

2-10 Payment by the government side of the invoice for petroleum costs, supplementary costs and service fees

- A- Approval of the committees or authorized body under the terms of the service contract on the claimed invoice.
- B- Approval of the internal audit department at the government side to verify the correctness of calculating the recoverable costs contained in the claim list and that they are in accordance with the provisions and the terms of the service contract.
- C- When the petroleum costs, supplementary costs and service fees received by the contractor exceeds the oil costs, supplementary costs, and service fees due during the quarter, this excess has been compensated in the following calculation in the immediately following quarter in accordance with the contract.

2-11 Accounting treatments in the government records when paying the amount of the claimed invoice

After completing the audit procedures and approving the invoice by the authorized body to service contract, which includes two types of costs (capital and operating), the government side records the accounting treatments, and these treatments are different by various payment patterns of the recoverable costs as following: -

- 1- When The government pays the capital and the operating costs in cash, the accounting entry shall be recorded as below: -

Debtor	Creditor	Details
****		Account/ capital costs (as classified under the approved accounting system)
***		Account/ Operating costs (according to its terms under the approved accounting system)

	****	to Account/ cash
--	------	------------------

2- When the government side pays in kind (amounts of crude oil) equivalent to the financial entitlements for capital and operating costs, the accounting entries shall be recorded as below: -

A- The quantities of crude oil paid are considered sales at the prevailing prices and the following entry shall be recorded: -

Debtor	Creditor	Details
****		from Account/ cash
	****	to Account/ sales

B- When the capital and operating costs of the contract area are paid, the following entry shall be recorded: -

Debtor	Creditor	Details
****		Account/ capital costs (as classified under the accounting system).
	***	Account/ capital costs (as classified under the accounting system).
****		To Account/cash

3- When another party pays the operating costs of the service contract area on behalf of the government, the entry shall be recorded as below: -

A. Accounting entry for the payment of operating costs:-

Debtor	Creditor	Details
****		Account/ capital costs (as classified under the accounting system).
	***	To Account/ revenues

B. The accounting entry for the payment of capital costs: -

Debtor	Creditor	Details
****		Account/ capital costs (as classified under the accounting system).
	***	To Account/ capital or reserves

2-12 Inventory of fixed assets and warehouse:

At all times, the Contractor shall undertake to carry out inventories of fixed assets and materials at the best levels required for petroleum operations, and they shall be subject to the following procedures:

1- Periodic Inventories, Notes and Representation.

The working company (operating) shall prepare a written notice for the purpose of carrying out the inventory process, and this notice shall be submitted before an appropriate period from the date of the start of any inventory process, and that the inventory operations shall be carried out at reasonable intervals and at least once annually. The host country company may provide clarifications when conducting an inventory process.

2- Reconciliation and Adjustment of Inventory operations.

The inventory process must be settled with the operating account and a list of increases and decreases should be submitted to the (host country) company, and adjustments to the inventory process should be made by the contractor and operator to the operating account if required provided that in the event that any adjustment to the inventory exceeds an amount specified under the terms The contract should inform the host country company accordingly.

3- Details of Inventory Lists.

Inventory lists must include all detailed information of inventory assets and materials such as (type of asset or material, quantity, costs, date of purchase, date of use), and the numbers of assets, equipment and stock materials contained in the inventory must be matched with the records maintained by the operating company, identifying differences, and making the related settlements.

2-13 The accounting systems applied by foreign companies under oil service contracts

Companies use accounting systems that are consistent in their work with the Enterprise Resources Planning (ERP) system, which depends mainly on the Internet. These systems are designed specifically for the work of companies, and their costs that are deemed as recoverable oil costs, below a presentation of the mostly used systems by the international oil companies operating in the Republic of Iraq.

First: The Italian company (ENI) operating at Zubair oil field uses the (SAP) system.

Second: The British Petroleum company (BP), the operator of the Rumaila oil field, is using the Maxisun system.

Third: The American company (Exxon), which operates at West Qurna field, uses the (IDEAS) system.

1- Cost aggregation according to (SAP) system:

The (Systems Application And Products) system is one of the applications of the (ERP) system issued by (SAP) company, as this company issues management software that helps companies improve their business and connect them to one comprehensive system that ensures interconnection and performance efficiency without the need to use several software and systems from different companies, which may lead to the emergence of differences in the type of inputs and outputs. Thus, SAP Company sought to find an integrated system suitable for all applications and all types of companies. SAP system consists of several applications called (SAP Modules), which are always interconnected with each other, and companies using the system can choose one or more applications according to their needs and for each application a special license and a specific price, and these applications are as follows: -

Financial Accounting	FI
Controlling	Co
Fixed Asset Management	AM
Project System	PS
Sales And Distribution	SD
Materials Management	MM
Product Planning	PP
Human Resources	HR
Quality Management	QM
Plant Maintenance	PM
Customer Relationship Management	CRM
Supply Chain Management	SCM

One of the most widely used applications is (CRM, FI, CO, SD, HR, SCM) and (SAP) has two main parts:

A- Functional Section: This section is concerned with functional operation, such as operations management in the system, such as financial or accounting operations.

B-Technical Section: This section is concerned with technical operations such as software or system control.

The main records in (SAP) system are: -

- 1- **(Customer Master)**: consists of all the data related to customers such as (addresses, contact numbers, historical data for the previous transactions).
- 2- **(Material Master)**: contains a definition of all materials that are manufactured.
- 3- **(Vendors Master)**: includes all vendors' data and their specialties in supplying of materials.
- 4- **(Prices Master)**: It is a record of all prices and for all products or service sold.

2-Cost aggregation according to (MaxiSun system):

The MaxiSun system consists of two main systems that are connected to form the integrated electronic system, namely the Maximo system and the Sun system. The synthesis between the two systems is done through the main control unit. Sapphire company has combined the Maximo system designed by IBM and the Sun system designed by Sun, and each system is concerned with a number of the main activities in the company using the system.

The integrated system aims to transform a lot of disparate data into relevant information. It is noticeable that many information technology systems work in isolation from each other in the company's units and departments and that lead to the occurrence of multiple problems, including (data duplication, information gaps, inconsistencies or contradictions in registration, different versions of the same information) and other problems in addition to that these systems designed according to a fixed database and the programming language is often outdated or inflexible, MaxiSun came with a set of application interfaces , powerful and interconnected modules that lead to financial, commercial and administrative solutions for applications and business system of the third-party (the user) and other key benefits of the system:

1. Big shortcuts in data processing.
2. Accuracy in data processing in the areas of business systems and finance.
3. 3- Presenting business operations in a timely manner.
4. 4 - Easy to use and requires only a few hours of training.
5. 5- Ensure data recovery in the event of a system malfunction.

The MaxiSun system differs from the ERP system in that the latter is designed to include all the procedures carried out by companies and governed all the work details. In other word, ERP system is designed as a big frame includes the work procedures, while MaxiSun is designed to be consistent with specific procedures to regulate and make them interconnected.

Regarding financial operations, the (Maximo) system is specialized in the following:

- Management of purchases and contracts (since purchasing till payment).
- Managing invoices and suppliers.
- Currency conversion rates.
- Inventory management (receipt, withdrawal and return operations).
- Issuing reports.

The (SUN) system is concerned with the following:

- Ledger Accounts Manual.
- Finance Reports.
- Currency conversion rates.
- Daily entries (accrual and adjustments).
- Accounts payable.
- Supplier management.

3- Collection of costs according to the IDEAS system.

An IDEA is an acronym for (Improved International and Domestic Accounting System). (International Domestic Enhanced Accounting System) IDEAS system uses the applications of (Maximo) system extensively, whose details are clarified in previous paragraph.

Chapter III

Procedures of Supreme Audit Institutions (SAIs) to audit and control the costs of oil service contracts

Chapter III

The procedures of the Supreme Audit Institutions to monitor and audit the expenditures of oil service contracts

3-1 The first axis: the basic requirements for the control and auditing of oil service contracts:

The governmental audit of the costs of oil companies is carried out in a manner that meets the privacy of that audit. To achieve this, it is necessary to know the basic requirements for the implementation of audit and control work on these costs, which are represented in the following: -

No.	Basic requirements	Basic requirements details
1-	Define the objective of audit and control.	The goal of the government side is represented by auditing the costs of oil companies for the purpose of determining the recoverable costs, in the light of the list prepared by oil companies and submitted by the governmental aspect, in order to reach the costs of oil products produced by them within the limits of the contracted oil fields on its management and operation within service contracts, which leads to a measurement of the state's share of oil resources, and achieving the general objective of audit, which is to preserve property and efficient use of the available resources.
2-	Study and understand the contents of the oil service contract.	Based on the service contract, the government side periodically implements control and audit procedures on the transactions and books of the service contract prepared by the operating foreign oil companies. There is usually a lot of items that are focus of discussions and negotiations between the government side and the companies which must be considered when reviewing. The government side's control over the expenses of the operating oil companies is primarily a review to ensure the company's commitment to implement what is stated in the service contract. Therefore, it is important for the employees of the higher agencies in the government

		<p>side to become familiar with all the clauses and clauses of the contract, the meanings of each of them and their relationship to each other, and the potential gaps that exist, and that Before starting the implementation of control and audit work, especially with regard to those aspects that are the subject of discussions and negotiations with the foreign oil company during the audit, and to achieve the above, the following is required:-</p> <p>A - Studying the agreement in general.</p> <p>B - Studying the accounting aspects contained in the agreement.</p> <p>C-Familiarity with the terms included in the contract agreement and its impact on accounting work.</p> <p>D-Knowing any other non-accounting aspects related to the audit process and ensuring that they are properly understood.</p> <p>E- Focusing on studying the provisions of service contracts and knowing the scientific methods for applying these provisions in addition to understanding the views on the interpretation of the clauses contained in those contracts.</p>
3-	<p>Knowing the agreements of Oil Service contracts in previous decades.</p> <p>(Appendix of service Contracts) .</p>	<p>Usually, the government side agrees with the oil company operating under service contracts to organize many aspects that aim in the latter to clarify how to implement some aspects mentioned in the contract or other aspects not included in those agreements. The government side Knowledge and familiarity with the details of subsequent agreements before starting the process of preparing and implementing the audit process.</p>

4-	Knowledge of the nature of the activity of oil industry.	<p>The control procedures under service contracts are implemented on the foreign company's expenses and determine the extent of their recoverability or not. Of course, it requires the auditors of the government side to understand the types of expenses and the nature of business in the various stages of oil extraction.</p> <p>On the other hand, being familiar with the nature of oil extraction activity helps to link the amounts of expenditures allocated in the discretionary budgets with those recorded in the records, and this helps the effectiveness of the control process.</p>
5-	Knowing the details and components of the lists of costs prepared by the oil company.	<p>Since the operating oil companies are foreign companies that arrive in the country to explore and produce oil, and this entails that the oil companies adapt themselves in the face of many administrative and accounting aspects, as the companies prepare a list of costs for each quarter submitted to the government side and include the costs that the oil company considers Refundable, and this list is prepared according to the service contract, but the way it is presented and the level of detail differs from one company to another, and there is no recognized standard form for the list of costs. (Exploration - development - production) costs are also displayed in those lists according to their respective accounts, for the purpose of providing the possibility of comparing them with the estimated budget and identifying deviations as well as showing additional costs.</p>
6-	Definition of the operating oil company in the role of the Supreme Audit Institutions(SAI).	<p>Expenditures are reviewed at the headquarters of the operating company or the place where the documents are available, which requires the auditors of the governmental side to define the operating oil company as the role of the supreme body for financial or accounting control in order to determine the framework in which the oil company subject to control is dealt with in accordance with the service contracts to ensure the flow of work and implementation The task is according to the specified times.</p>

3-2 The second axis: the bases of audit and control of the costs of foreign companies under oil service contracts:

The government audit of the costs of oil companies under service contracts is carried out according to special principles (standards or rules) that distinguish them from other types of audit. As the audit procedures of the costs of oil companies aim at verifying the recoverable costs and determining the rejected costs. The general basic rule on which cost is accepted or not is as follows:

For the costs to be recoverable, it must be a valid legal costs in accordance with Generally Accepted Accounting Standards (GAAP), or International Accounting Standards (IAS), or International Financial Reporting Standards (IFRS), provided that that cost is in accordance with the contractual terms of service contracts, and it has been claimed according to the accounting annex to the service contract, and must be within the limits of the amount allowed in accordance with the work program and budget approved by the government.

It is possible to rewrite the previous rule in the form of two sets of bases that are relied upon in order to accept or reject the costs, for the various costs items represented in the administrative and general expenditures, the various salaries, and their burdens, and the costs of extraction for different stages:-

No.	Bases Type	Bases Details
1-	General set of bases.	<p>A- The costs should be legal and correct in accordance with the accounting standards generally or internationally accepted.</p> <p>B- The costs are stated in the service contract and in light of the procedures that included in the accounting annex to the contract.</p> <p>C- The costs are mentioned in the work program related to the scope of the service contract and the planning budget approved by the government side.</p>
2-	Subsidiary and Analytical Bases.	<p>In order to check the availability of the general bases, obtaining many supporting documents, making sure of the implementation of procedures, and obtaining the necessary approvals from the concerned authorities, which is what we call in general the subsidiary and analytical bases that are different depending on the nature of costs. Among those sub-bases are the following:-</p>

		<p>A- What agreements have been reached or concluded with the oil company under audit and control.</p> <p>B-The nature of the disbursed amount and its connection to the oil operations of the contract area.</p> <p>C- The authenticity of the documents supporting and corroborating the validity of the disbursed amounts related to the contract area.</p> <p>D- Sound and customary procedures regarding tenders and the necessity of obtaining the prior approval of the government side on those tenders.</p> <p>E - Observations of the government on the company's policy regarding recruitment from abroad considering the approved salaries and benefits for foreign workers.</p> <p>F- The approval of the government to carry out the work that needs to be done, such as the technical works that take place in the company's head office.</p>
--	--	--

Considering subjecting the costs to the previous main and subsidiary basics, any of the following alternatives will be obtained for the results of the audit process:

NO.	Alternative	Alternative details
1-	The first	Cost acceptance.
2-	The second	<p>Refusal of the cost completely if the list of costs is charged with an amount greater than it should or duplicated, or if the expense is for the operating company and its benefits, and the oil operations have no direct relationship with it or other reasons due to the absence of the main or subsidiary bases for accepting them as recoverable costs.</p> <p>The decision to accept the cost or not is left to the authorized senior management officials on the governmental side (who are authorized to approve the lists of costs) for costs that are either not supported by documents or were not properly and completely documented, as the</p>

	<p>government side follows up on such cases with the oil company, which in turn It provides documents and clarifications to the government side, in the light of which the appropriate decision is taken.</p>
--	---

3-3 The third axis: preparing a program or programs for the purpose of implementing audit and control procedures on service contracts:

Audit and control procedures are implemented legally by the government side and are usually carried out once a year, unless there are other audit procedures implemented for special purposes determined by the legally authorized bodies, and due to the specificity of this type of audit procedures and the lack of clarity of what must be observed as is the case of other audit procedures, so in the preparation stage the following must be done: -

1- Examining all the correspondences that took place between the foreign company and the government side during the period subject to audit to know the aspects included in the correspondences and their impact on the audit process and the need for follow-up during field work.

2- Examining the reports of the technicians of the government side and those working in the sites of the contract area, as this clarifies the aspects that have disagreement or objection to their implementation, which requires follow-up during the review to know the possibility of rejecting the costs associated with those aspects.

3- Contacting with the company under audit to make the necessary arrangements for field work, through a letter that includes many aspects, including:

- Date of commencement of field work, year of audit, names of the audit team and their job titles.
- Directing correspondence regarding the request to provide information and data for the purpose of facilitating the audit process and shortening the time of its implementation, directing those correspondence and following up on oil companies for the purpose of answering them before starting field work is one of the most important aspects that lead to the smooth flow of the audit process, shortening the time and linking data and information with each other to ensure the introduction of many amendments and additions to the scope of the control and audit program on costs, and from that information and data that is due requested for the purpose of completing the oversight process the following:-

- ✓ Tender File.
- ✓ Reports and minutes of the initial and final receipt of the work completed during the period under control.
- ✓ Well abandon Reports.
- ✓ Original documents supporting various transactions.
- ✓ Daily drilling reports.
- ✓ Geological, engineering and production data.
- ✓ Minutes of meetings of the operating committees prepared based on the terms of the contract.
- ✓ A list that includes a comparison of actual expenditures with those included in the budget, with an explanation of the causes of deviations.
- ✓ The settlement made by the company in preparing the lists of costs from the financial records, general ledger, or trial balance.
- ✓ A complete copy of the general ledger to be used during the audit.
- ✓ A list of cost centers, which represent the approved exchange orders during the period under audit or those approved from the previous year, showing the actual expenditures with an explanation of deviations, if any.
- ✓ A list of purchase orders made during the period under audit and that fall within the framework of what was agreed to be reviewed with the government side, with the details of all suppliers' accounts being provided.
- ✓ Inventory reports that show the turnover and spoilage rate and the accounting procedures followed by the company in Inventory control.
- ✓ List of all insurance policies.
- ✓ List of exploration and development wells.
- ✓ Fixed assets inventories and the results of matching them with records.
- ✓ Trial balance at the end of the period under control and audit.
- ✓ A list of allied companies that were dealt with during the period under control and audit.
- ✓ A list of all the expenses included in the lists of costs for the main accounts.

- ✓ Documents related to salaries and wages, including files of foreign workers, documents of performance evaluation, and proof of receipt workers for their entitlements.
- ✓ The company's policy regarding foreigners' salaries and the amendments made to them.
- ✓ A file of all correspondences made with the government side that is related to audit.
- ✓ A copy of the budget and work programs approved by the government side.
- ✓ List of local and international suppliers that were dealt with during the period under audit.

3-4 Fourth Axis: Scope and program of audit and control of service contracts

3-4-1 Scope of control and audit work:

The scope of the control and audit process is the period for which costs will be audited, and the aspects that will be audited. When determining the scope of the process of controlling the costs of foreign oil companies under service contracts, the following factors must be considered:

No.	The details
1-	Study the lists of costs, to find out the aspects that should be focused on, which are usually in dispute between the government side and the oil company on the one hand, and to know the size and concentration of the amounts spent and other details.
2-	Conducting a preliminary survey by conducting a field visit to the accounting unit of the company under control to determine the number of documents and other details that the head of the audit team deems important and directly related to the scope of control and auditing.
3-	Examining the observations made by the results of the audit during the previous years, to verify that they were addressed and that their effects did not continue during the period under scrutiny
4-	Reviewing some important documents, meeting with officials, and identifying the extent of commitment to implement what was stated in the budget approved by the government.

5-	Determining the period whose costs will be monitored and determining the amounts that will be examined, bearing in mind that there are many items that are covered by (100%) during the implementation of field audits according to what the government side sees.
----	--

3-4-2 Program of Control and Audit Procedures:

The audit program is detailed steps for how to achieve the goal of controlling and auditing costs considering oil service contracts, and it explains the audit steps in detail, provided that the program is modified according to the actual results during field work.

The audit program is prepared considering what is stated in the scope of control and audit, provided that the program covers all the items of the cost list in a balanced manner to ensure coverage of all aspects within the framework of the same group. The audit program and preparation for field work; it requires the government side's observers to know how to implement the control work for each item of the cost list.

Fifth axis: Implementation of control and audit procedures on the costs of oil companies under service contracts

There are aspects related to the government side's relationship with the operating company, which needs a special method to be audited and reviewed. It can be said that these aspects are represented in the accounts or aspects that have to do with the recoverable costs in both parts (operational and capital), the quality of the oil produced and the environmental effects of the extractive operations of the oil fields within the scope of service contracts Accordingly, this axis will be concerned with presenting the control and audit procedures according to these aspects, as follows:

- 1- Preliminary control and audit procedures for signing oil service contracts.**
- 2 - Procedures for controlling and auditing operating costs.**
- 3- Procedures for controlling and auditing capital costs.**
- 4- Procedures for controlling and auditing production.**
- 5- Procedures for controlling and auditing the social and environmental impacts and the requirements of sustainable development.**

In the following paragraphs, the most important control and audit procedures related to the items of the costs list for oil service contracts will be identified, which is considered the minimum requirement for each member in the audit team of the government side to understand, before starting the field work.

3-5-1 Preliminary control and audit procedures for signing oil service contracts (procedures of auditing service contracts for the first time).

When the service contract is audited for the first time by government auditors, the following procedures must be observed when auditing:-

No.	Control and Audit Procedures
1-	Verify the government's use of the information obtained during the implementation of the evaluation of explorations for resources or production in choosing the method of licensing or contracting, whether it is the competitive or non-competitive method.
2-	According to scientific and practical sources for the extractive industries, there are two main ways to grant oil and gas rights: the competitive method and the non-competitive method (the open door), which requires studying and evaluating the method used by the government side in soliciting technical and commercial offers for foreign companies, as shown in sequences (3 and 4) from this table.
3-	<p>Control and audit procedures when the competitive method is used:</p> <p>A- This method is consistent with government policies, and it encourages effective participation, and the selection of applicants is made on the basis of competence and to be from solid (strong) companies in the global oil and gas markets.</p> <p>B-Verify the availability of protection measures against practicing pressures to spoil the contract award process. It should also reflect the technical, legal and administrative ability of the governmental authority responsible for awarding contracts and licenses. In addition, the award system must be equitable and transparent to reduce corruption risks.</p> <p>C-Verification of setting specific criteria with standards relative weights and be available to the public and sharing them with investors to be adopted in selecting the best bids.</p> <p>D- Use this method when the information about potential resources is available, along with the availability of interest of high number of investors.</p> <p>E - Ensuring that transparency is achieved by providing all information to bidders, while verifying that the same information is provided to all bidders?</p>

	<p>F- Ensure that integrity is achieved in the selection by selecting the oil company with the highest bid submitted, and this is done by comparing the bid details of the contracted company with the criteria and specified standard weights.</p> <p>G- Verification of pre-qualification of the financial and technical capabilities of potential bidders and the program of schedule-based work to reduce speculation.</p> <p>H- It is necessary having technical, professional, legal and other capabilities to evaluate bids.</p> <p>I- Provide information to the government about the value of the resources in the view of bidders.</p> <p>J- Rights are transferred on the basis of specific criteria established in administrative procedures.</p>
	<p>2- Control and audit procedures when the non-competitive method (open door) is used:</p> <p>A-Transfer of rights according to priority is given in a non-competitive manner.</p> <p>B- Verify the use of this method when the geological information on potential resources is limited or the contract area is not explored, or if the government wants to stimulate operations of minerals development.</p> <p>C- Verify that there are no errors in the judgments issued and that there are no cases of corruption due to limited information and increased discretion.</p> <p>D - Verify that transparency requirements are provided by pre-defining clear criteria for grants and publishing the results.</p>
5-	<p>Ensuring that the contract is effective when:</p> <p>A- Signed by the two parties, the government, and the oil company.</p> <p>B- Approval of the contract by the authorized body by virtue of the constitution or laws in force.</p> <p>C- The government has informed the contractor in writing of the ratification of the contract and its effective date.</p>
6-	<p>When the government has documented geological information about the contract area, the contract area must be announced as a competitive tender - through which the government ensures that foreign companies submit their bids in a competitive manner - and this is the best option for the government to get the most benefit.</p>

7-	Verifying the efficiency and effectiveness of the procedures for granting licenses for exploration operations and verifying that the government observes the requirements of transparency in these procedures, as they represent the first step in achieving economic gains, and this matter may also contribute to reducing the risks of corruption.
8-	When the service contract stipulates that the foreign company pays a certain amount as final revenue, such as a signature bonus, and tenders. It is necessary to verify paying the amount mentioned in the contract and recording it as final revenue to the state treasury or any other amounts paid by the foreign companies upon awarding and before signing the contract.
9-	Ensuring the presence of a branch of the foreign company contracted with in the country of the main contracting government side during the period specified by the laws and instructions in force, as well as defining the branch's tasks, numbers of employees and details of the costs of opening and operating the branch as they are reimbursable costs. The foreign company is also required to inform the government side of the address of the branch and the names of its representatives (authorized persons) with permanent residence and any change that occurs to the address of the branch or its representatives.
10-	Verify that the relevant parties to the service contract have formed the Joint Management Committee (JMC) for the purposes of general supervision and control of petroleum operations in the oil field that falls within the scope of the contract. JMC consists of representatives of the national oil company, the foreign company, and any other party related to the implementation of the contract area, as stated in the service contract.
11-	<p>Verify that the Joint Management Committee (JMC) has the following tasks and authorities in relation to petroleum operations:</p> <p>A- Review and recommendations for plans or any required modifications.</p> <p>B- Reviewing and approving the annual work program, budgets, production schedules, and any other amendments.</p> <p>C- Reviewing and approving the schedules of procedures prepared for the implementation of petroleum operations.</p> <p>D- Reviewing and approving the award of secondary contracts and purchase orders.</p> <p>E- Approval of training programs and plans prepared by the National Oil Company for the development of local employment.</p>

	<p>F- Supervising and controlling the implementation of the approved plans, work programs and the overall policy of the operator.</p> <p>G- Reviewing and approving the employer's employment programs, which show the number of workers, their specializations, and nationalities.</p> <p>H- Reviewing and approving the numbers of workers planned by the operator.</p> <p>I- Reviewing the quarterly statement, annual accounts, and other financial statements.</p> <p>J- Conducting the periodic review and reviewing other reports submitted by the contractor or operator and make recommendations to ensure an adequate implementation of petroleum operations.</p> <p>K - Recommending the appointment of independent international auditors.</p>
12-	<p><u>Development plans and work programs</u></p> <p>A- Verify that the operator has submitted plans related to development operations and estimated budgets and approved them by the national oil company before an appropriate period from the beginning of each year.</p> <p>B- Not to carry out any petroleum operations unless the work program, budget, development plans, or their revised copies have been duly approved.</p> <p>C. The operator shall prepare and submit the proposals related to plans or revised copies and any other administrative, accounting, or operational procedures including supporting studies, data, and information to the Joint Management Committee (JMC) for the purpose of approval.</p> <p>D. The operator shall implement the annual work program and budget after being approved by JMC and under its general supervision and control.</p> <p>E- The operator may make minor changes to the details of the approved work programs or budget, provided that they do not affect the amounts specified in the main items of the budget.</p> <p>F- Comparing the amount of the change in the total approved budget with the authorities specified in the service contract, while determining its negative impact on achieving the general objectives of the work program.</p>

	<p>G- Any amendment to the approved plan that leads to a change in the general objectives of that plan or changes the total estimated cost is considered a revision that must be subject to approval.</p> <p>H- The state oil company reviewing the production level of any proposed or approved work program.</p> <p>I- When the contractor/operator takes a decision to increase or reduce (reduce) the rate of production from the contract area, this procedure requires a written notice to the National Oil Company with a statement of the compelling reasons for taking the decision to increase or decrease as follows: -</p> <p>J- When the contractor/operator takes a decision to increase or reduce (reduce) the rate of production from the contract area, this procedure requires a written notice to the National Oil Company with a statement of the compelling reasons for taking the decision to increase or decrease as follows: -</p> <p>First- to avoid basic damage to the reservoirs.</p> <p>Second - for short-term operational requirements.</p> <p>Third- the curtailment imposed by the government.</p> <p>Fourth - for healthy, safety or environmental considerations.</p> <p>Fifth - Reduction due to the carrier's failure to receive the net production or products of the gas processing plant at the transfer point.</p> <p>K-The contractor submits and revises the rehabilitation plan, the enhanced rehabilitation plan, and all the annual work programs, budgets and their revision to the oil company for approval.</p> <p>L- The operator, during the period specified under the provisions of the service contract, provides the national oil company with a detailed written report of the total cash requirements for the subsequent calendar month and in the currency agreed upon in the contract in accordance with the approved work programs and budgets.</p>
13-	<p>The operator, in accordance with the law and the provisions of the contract, shall take all the appropriate and necessary measures to protect the environment and to prevent or reduce the impact of any pollution that may result from petroleum operations.</p>

14-	Ensuring the conclusion of service contracts in accordance with the current requirements and needs, and this can be measured through the revenues generated by those contracts to meet the needs of citizens at the present time without compromising the interest of future generations.
15-	Verify the development of strategic plans to ensure the modernization of the infrastructure and technology used in the service contract to make it sustainable, such as the use of renewable energy in the implementation of some extractive activities.
16-	Verify the development of social, environmental, safety and quality standards for inputs provided by suppliers and contractors throughout their supply chain.
17-	Verify the development of human rights standards within the operational and strategic risks and environmental impact assessments.
18-	Verify the status of anti-corruption policies and compliance programs within the provisions of service contracts, in addition to encouraging stakeholders and subcontractors to implement their anti-corruption policy.

3-5-2 Procedures for controlling and auditing operational costs:

Considering service contracts, there are many aspects of operating costs according to the concept of recoverable costs. In this paragraph, procedures will be proposed to audit those costs by the government, as follows:

A- Procedures for controlling and auditing the contracts of foreign oil companies with subcontractors (subcontracts):

In executing most of their work in various fields, companies depend on contracts made with sub-contractors. In most cases, the amounts of these contracts represent the largest part of the amounts of the companies' lists of costs. Therefore, these contracts have a high relative importance, and there is a strong justification for focusing on them in setting the procedures of audit and control, to highlight the various issues that usually appear during auditing the costs of oil companies that are carried out through subcontracts.

First: the procedures taken to verify the integrity of contractual procedures:-

The extent to which, the most important contracting procedures made by foreign oil companies with subcontractors have been implemented, shall be audited based on the basics that were agreed upon with the government and how the government auditors see it. Below are the most important measures to be taken to verify what was previously addressed as following:-

No.	Actions to be Taken
1-	Adequate knowledge of the effective contracting procedures and the procedures agreed upon by the governmental with foreign companies regarding the implementation of those contracts to ensure their implementation and compliance.
2-	Determining the contracts to be audited, and this helps in knowing many aspects, including (the extent of the opportunity for the largest possible number of contractors to implement those contracts and not limiting contracts to specific contractors, giving local contractors the opportunity to contract, and this is one of the aspects that distinguish service contracts, which It usually stipulates that priority should be given in contracts to local contractors, even if the cost is greater than that provided by the foreign contractor in a certain percentage agreed upon).
3-	Verify that more than one contract is not referred to one company before implementing its previous contractual obligations, and more than one contract can be referred to one company, only in the case of ensuring its financial efficiency represented by {the financial efficiency of the bidders, through determining the approved capital and cash liquidity}.
4-	The contracts to be audited must be diversified according to the type of activity, sectors, or other basics to ensure that audit procedures are not focused on a particular activity.
5-	Evaluating the way of selecting the contractor and the extent of commitment to follow the rules and principles agreed upon in the service contract and subsequent correspondence.
6-	Checking the amendments, renewal or extension of contracts to ascertain the extent of the need for them and verifying the approval of the government on that.
7-	Familiarize with the concept of the terminology contained in the contract, as they are not repeated in invoices of costs or other documents.
8-	Getting to know the two parties of the contract, defining the duties and obligations of each of them, and focusing on knowing the party that provides implementation requirements such as equipment and personnel.
9-	Verify that the subcontracted companies are not granted additional periods without an actual need for that. In the event that additional periods are granted, it is ascertained that there are real and realistic justifications for the reasons for the delay in implementation, and it is necessary to match the additional period with the delay period of implementation and the original duration of the contract.

10-	Verify the deduction of all amounts owed by the subcontracting company, such as taxes, fees, etc., and the conformity of the deduction amounts with the laws and instructions in force.
11-	Verify the approval of the authorized bodies to certify the awarding of contracts.
12-	Include clauses in the contracts to clarify the procedures and cases that fall under the so-called force majeure, as this must be clearly specified in the contract to avoid paying sums to the contractor that are added at the end to the production cost, and this is one of the aspects that frequently appear between the government and the operating company.
13-	In some cases, it may be decided that one of the subcontractors is entitled to a certain amount, according to that an accounting entry is made, but the actual payment has not been made yet. In this case, it must be ensured that the appropriate accounting treatment is carried out and that the amount is excluded from the list of costs, in application of the cash basis that must be followed in preparing the lists of costs. And this is one of the aspects that distinguish the audit of service contracts from the regular audit procedures, which are based on the accrual basis.
14-	If the invoices submitted by the contractors are in dollars and are converted into the local currency at a price higher or lower than the official price, and payment was made on this basis, this means that there is a price difference that must be added or excluded from the list of costs.

Second: Control and audit procedures for the implementation of sub-contracts:

No.	Details of control and audit procedures for execution contracts (construction)
1-	Verification of obtaining the approval of the authorized bodies to ratify the contracting procedures in accordance with the limits of the spending powers specified under the service contract.
2-	Verify that the contractual terms, technical specifications, bills of quantities and maps are prepared accurately to avoid making changes and additions during execution.
3-	The existence of an estimated cost prepared by a competent technical authority for adoption in measuring the balance between the amounts of the contract with the prices prevailing in the local or international markets.

4-	Ensure that the contracts include clauses related to determining the delay fines in a proportion proportional to the contract amount.
5-	Comparing the percentages of actual (material) completion with the percentages of planned completion for all contracts, identifying the dilatory contracts, and verifying that administrative and legal decisions are taken in this regard.
6-	Comparing the percentages of physical implementation with the percentages of financial implementation of the contract and verifying that there is no excess of the percentage of financial implementation over the percentage of physical implementation.
7-	Verify that new contracts are not assigned to dilatory companies in implementing previous contracts.
8-	Verify the efficiency and suitability of the qualifications of the technical and specialist staff working in the project. In the event of the lack of cadres for experience or qualification, it will need longer hours to carry out the work, and then its negative impact on the increase in costs.
9-	Verify the efficiency and validity of the specialized equipment and mechanisms used in the implementation of the project.
10-	Verify that the executing company submits a work plan (work method) that shows the order of the stages and the method to be followed when executing the works and its approval by the authorized (authorized) body to monitor the implementation.
11-	Ensuring that there are periodic tests for the materials used in the execution of the project and reviewing the results of those tests to make sure of not using materials that do not conform to specifications in the implementation of the project.
12-	Reviewing the periodic reports of the engineer supervising the project to verify the progress of the project implementation in accordance with the technical specifications and the schedule of the work program and identifying the items executed in contrary with the technical specifications and to verify their treatment.
13-	<p><u>Hidden business arguments:</u></p> <p>When the items or stages of project implementation include the presence of excuses for hidden works (which will disappear during the implementation of the subsequent project items), the auditors of the ASI must verify that foreign companies take the following measures:</p> <p>A - When starting the implementation of the project, a technical committee for hidden works must be formed, consisting of:-</p> <ul style="list-style-type: none"> -A representative of the foreign oil company from outside the resident engineer department. -A representative of the National Oil Company from outside the resident engineer department. -A representative of the resident engineer department. -A representative of the implementing agency (contracting company). <p>B - The resident engineer department must open a special record for the hidden project works that will disappear later. The committee referred to in paragraph (A) Above, confirming the amounts and details of those works, and it is approved by the committee.</p>

14-	Verify that the final entitlement to the project has not been disbursed only after the formation of a receiving committee that supports the conformity of the executed work with the conditions agreed upon in the contract.
15-	Comparing the actual contract implementation period with the contractual period and verifying that this period has not been exceeded by the company, which executes the project and in the case of an overstepping, verifying the accuracy of calculating the overstepping period. The number of fines imposed on the company shall be deducted from its financial dues.
16-	Comparing the actual contract implementation period with the contractual period and verifying that this period has not been exceeded by the project executing company. In case of existence of overstepping it should be verifying the accuracy of accounting the period of overstepping and the amount of the delay fines imposed on the executed company and deducting this amount from its financial dues.
17-	The contract may stipulate for the payment of fees for using the equipment based on the operating rates (the daily rate, the weekly rate, or the monthly rate). In this case, it must be verified that the calculation mechanism was determined based on the best benefit to the company.
18-	Verify that the contracts include a clause referring to the obligation of the subcontractor to the presence of its workers within (24) hours in the work sites throughout the implementation period to avoid carrying any amounts of production costs if a strike occurs by the contractor's workers.
	Ensure that the subcontractor has hired local workers in accordance with the provisions of the contract.

B- Control and Audit Procedures for Salaries and Wages Costs:

As a result of the specificity of auditing salaries and wages costs in light of service contracts, the matter is required when reviewing the expenses and workers' salaries to judge the correctness of their calculation from being a recoverable costs, taking into account:-

NO.	Control and Audit Procedures
1-	verifying the employment procedures, and preparing a fundamental system for the recruitment of local staff including (salaries, wages, benefits and all applicable allocations, related to staff and users) as well as employment requirements such as (functional description and standard qualifications for job occupancy) in accordance with the law and domestic market conditions and must be taken into account the equality of salaries and employment conditions for local and foreign workers.
2-	Knowing the settlement made by the company on the account appeared in the trial balance in order to reach the amounts of salaries and wages contained in

	the list of costs, and this is one of the aspects that are distinguished by reviewing the costs under service contracts, as we find that the salary and wages item mentioned in the general ledger includes amounts that do not belong to the service contract, which requires excluding them to reach to the recoverable salaries and wages.
3-	Ensure that the government agrees to the rates of disbursement of salaries, wages, and benefits that are supposed to be within a special guide to be presented to the government for being studied and discussed with the company before approval, provided that equality and fairness in salaries, and employment requirements between locals and foreigners with similar qualifications and experience are taken into account. With the granting of allocations and special benefits suitable for foreigners.
4-	Taking into account the individuals who are included in the percentage of additional expenses and individuals who are not directly related to the contract under audit, because the matter requires rejecting any expense related to them if it has been included in the list of costs, and verifying the logical distribution of the time of individuals who work for more than one contract and more than one party.
5-	Some companies use in the head office, estimated hours and costs at the beginning of the period, so they are charged to the list of costs, provided that they are settled at the actual cost at the end of the period. This is what must be noted so that the list of costs does not include amounts that exceed the actual, which results in inflating the cost of production.
6-	In auditing, connection must be made when checking the number of working hours per day during successive work periods and making sure that the reasonable hours of rest per day are calculated for each person separately and not considered among the actual working hours. Taking into account the case of rotation, according to which a person usually works for a specific period, such as (28) days in the oil field and giving him/her (28) days off to travel to his/her country, and therefore the matter requires making sure that this system (28/28) is given only to workers in the fields, because, as it is clear, the company bears double burdens.
7-	In the event that the salaries of seconded employees from a third party, it must be ensured that what is burdened as a salary, is done in accordance with the contracts and documents regulating this, and any disbursement otherwise must be excluded from the list of costs.
8-	In the event that the wages are related to technical works at the head office, the validity of the wage rates are checked, and all attachments of the voucher are checked, to ensure that there is a task assignment, and a summary of the work, including the job of the person who carried out the task, the hourly wage rate, the type of the task, and the period in which the work was carried out.
9-	The costs associated with redistributing the employees to and from the site of the service contract are considered recoverable costs if the service contract

	<p>includes a text indicating that they are considered recoverable costs in addition to the transfer of the employees, their family members and their home furniture, provided that the transfer is mainly for the purposes of the service contract, whether the employees are permanent or temporary. Mostly, the costs of foreign workers are large, and the extent to which the costs of their transportation are considered recoverable can be judged by being guided:-</p> <p>A- The costs of transporting laid-off foreign workers are not recoverable. B - The salaries and wages of transferring foreign workers to work in the oil field for the purpose of training are considered non-recoverable costs. C- The burdens incurred as a result of transferring (foreign workers, their families and their furniture) from the oil field area to another oil field area are considered non-recoverable costs as they will be charged on the service contract for the oil field to which the foreign worker would go.</p>
10-	<p>When there are foreign cadres working within the scope of the service contract, the foreign company must employ qualified cadres and keep pace with modern technological developments related to their scientific specializations. In light of this, the costs of technical training are not considered recoverable costs, and the costs of training local cadres are considered recoverable unless the following conditions are met:-</p> <p>a- The fields and topics of training are directly related to the contract in which the trainee works. B - The trainee will continue within the limits of his previous work. C- Verify that the technical trainee's efficiency has been raised as a result of the training.</p>
11-	<p>The operator shall provide the necessary personnel for petroleum operations and give priority to local citizens who have the required experience and qualifications.</p>
12-	<p>Verify the ratio of local employment to the total number of workers in development and compare it with the percentages specified under the service contract.</p>

C- Procedures for Auditing Purchase orders:

Usually, materials are purchased or services are obtained through purchase orders issued to suppliers or service supply contracts, and this would affect costs, which requires auditing procedures for issuing purchase orders and contracts, to ensure control over a large part of the costs that are considered as recoverable costs. The purchase orders and service supply contracts are audited in light of the procedures that are approved by the government and the oil company, and this is achieved through the following:

No.	Details of control and audit procedures of supply contracts for goods and services
1-	The government auditors should be familiar with the procurement procedures agreed upon with the oil company to ensure that they are implemented, including the procedures that require the oil company to obtain the approval of the government on any purchase order whose value exceeds a certain amount, verifying the suitability of the purchase order to the approved work programs, and obtaining prior approval from the concerned authorities in accordance with the provisions of the contract.
2-	Ensure that business and services contracts are awarded on a competitive basis and give preference for local entities and companies.
3-	Ensure that priority is given to merchandise, materials, equipment and manufactured consumables materials that are available locally as long as their technical specifications, availability, prices and date of delivery is similar to what is available in the international markets.
4-	<p>Verify that the subcontracting companies are solid companies. To achieve this, the following procedures must be observed:</p> <p>A- Verifying the contracting with the manufacturers or their authorized agents to avoid spending additional costs when contracting with intermediary companies.</p> <p>B - The products of the contracting companies are of high quality.</p> <p>C- The contracted company has continued in its specialized activity for the past five years by requiring it to submit statements that include the details of its contracts for the last five years.</p> <p>D- The indicator of activity result included in the final accounts for the past five years shall be positive.</p> <p>E- The contracting company is distinguished for its good performance in the implementation of its previous obligations.</p> <p>F-And making sure that the contracting company is not included in the blacklist during the period of signing contracts with it.</p>
5-	Checking any amendment or renewal in purchase orders and making sure that the oil company obtains the approval of the government.
6-	Ensuring that the purchase was not made from the same source (single source of supply) and if it does, make sure that there are convincing justifications.

7-	<p>Familiarity with the procurement procedures followed by the oil company under audit, in accordance with its regulations, as it is required to ensure that the oil company follows the recognized procurement cycle. To achieve this, the following must be taking into account:</p> <p>A- The presence of a purchase order from the requesting party in accordance with the established principles.</p> <p>B. The presence of a copy of the request for price quotations from the suppliers, or the presence of a copy of the advertisement or tender.</p> <p>C. Providing lists of bids opening in the presence of the concerned committee.</p> <p>D. Providing bid evaluation documents and selecting the appropriate bid.</p> <p>E. In case of selecting a specific supplier without following the aforementioned procedures, the justifications followed by the company must be ascertained, which might be due to monopoly or otherwise.</p>
8-	Verify that the contracts include technical and accurate specifications that guarantee the identification of the technical characteristics of the goods and services to be supplied.
9-	When the contracts include a clause of post-supply services, the provision of those services is verified according to the agreed contractual terms.
10-	Verify the place of delivery of the materials contracted to be supplied with the selection of places that do not charge the government additional amounts, such as the delivery of goods at the oil company's warehouses according to (CIF) method.
11-	Verify the accuracy in determining the duration of supplying or providing services in proportion to the nature of the supplied materials or the type of service provided.
12-	Verify the existence of a curriculum (method) or dates for delivery of materials and provision of services required under the contract.
13-	Ensure that the contractor pays all taxes and fees imposed under the laws.
14-	Verify that the contracts include the method of calculating delay penalties in accordance with the terms of the contract (shipping delay fines, delivery delay fines) and others.
15-	Determining the name of the party that has the authority to finally accept the goods or services after being delivered from the contracting party, checking the minutes of receipt and test to verify the conformity of the supplied goods or services to the contractual clauses.
16-	Provisions of contract drafting procedures, including specifying the following clauses (names and addresses of the two parties to the contract, subject of the contract, contract number and date, contract scope, contract amount and

	currency, implementation period, dates of completion, dates of payment, effective date, demurrage, , provisions for contract termination, certified certificate of origin, dispute resolution method).
17-	<p>When signing contracts to transport the employees of foreign company by planes or any other means of transportation .The following procedures must be observed in audit:-</p> <p>A- Verify the existence of a shift work system to ensure the implementation of transport flights by aircraft on time.</p> <p>B- Comparing the number of trips carried out with the shift system by comparing the trip history with the start and end date of the shift.</p> <p>C –Determine the number of trips carried out that in contrary with the work regulations and determine the costs of these trips to be regarded as non-recoverable costs.</p> <p>D. In the event that there are a number of transport contracts for a number of oil fields, the contract amounts are compared with each other, and the differences are identified and their reasons are searched for. In case of lack of any scientific and logical reasons for these differences, they will be classified as non-recoverable costs.</p> <p>E- Verify that there is no exaggeration in the cost of transporting a single worker by comparing the contract amount with the number of trips carried out and the number of workers transferred and comparing the transport cost per worker for one of the oil fields with the contracts of other oil fields.</p>
18-	Ensuring the benefit of the cash discount, if any. For example, the contract may stipulate that the invoices submitted by the contractor are paid within a certain period from the date of using the invoice. If it becomes clear that the payment was made early, the amount of the expense must be reduced by the amount of the discount.
19-	<p>Oil companies may resort to signing contracts for supplying and providing services according to the (Call Off) method, and when there is such type of contracts, the following procedures are taken into account when carrying out control and audit of those contracts:-</p> <p>A - Verify that the contracts include a text that includes retail supply.</p>

	<p>B - Verify that this method is adopted in the implementation of supply contracts only.</p> <p>C- Verify that those contracts include a clause specifying the technical specifications of the materials to be supplied and the obligations of the supplying company to supply them within the specified period.</p> <p>D- Verify that the required materials have been prepared according to the specified timings by comparing the time specified for supply based on the company's request with the actual supply date.</p> <p>E - Verify that the contracts include a clause related to delay fines when companies supplying the required materials are delayed, identify cases of delays in supply and deduct the amounts of delay fines, taking into consideration the comparison of the amounts of delay fines with the damage caused by the delay in supply to the progress of the oil company's business, such as losses caused by disruption the company's activity or the amount of lost opportunity in generating additional revenues when supplying is delayed.</p>
--	---

D- Procedures for Auditing Costs of Inventory Items:

The inventory audit procedures depend on the provisions of the service contract. Some contracts stipulate that purchases of materials and spare parts are considered costs on the date of purchase and not when used. Some contracts stipulate that the expense of inventory is not considered costs except when used, and accordingly, the inventory audit procedures shall include the following:

No.	Audit Procedures
1-	When the contract stipulates that the expense of inventory is not considered an cost except when used, it must be verified that the list of costs is not loaded with a stock that has not yet been used, which is achieved through auditing the disbursement operations from warehouses, and it must be ensured that the company's inventory value is incurred according to the list of actual costs or according to the inventory pricing system followed by the oil company.
2-	<p>In the event that the service contract stipulates that the cost of inventory is considered as a recoverable costs, as soon as for the purchase process to take place, the audit is conducted as follows:</p> <p>A- Ensuring the purchase of warehouse materials according to the actual need for the progress of the production process.</p> <p>B - Making sure that there are committees specialized in receiving and examining the purchased warehouse materials to verify their conformity with the specifications.</p>

	<p>C- Ensure that the value of the end-of-term inventory is not added to any item of costs, because that leads to inflated costs.</p>
3-	<p>Many indicators that demonstrate good management of inventory are used in achieving inventory audit, including some of the following:-</p> <p>D- The regularity of the movement of the stock and carrying forward to the warehouse records without delay.</p> <p>E - Disbursement of warehouse materials to production departments is carried out in accordance with the authorities.</p> <p>F- Ensuring that there is no damage to the warehouse materials, and in case of their presence, the operator bears the financial impact, while specifying the reasons that led to their damage and treating them.</p> <p>G - Verify that there are no slow or motionless warehouse materials, and in the event of such types, the operator must be charged with purchasing them and recommending the purchase of warehouse materials according to the actual need by setting the minimum and maximum for each item.</p>
4-	<p>Any taxes recovered by the contractor when purchasing from abroad shall be excluded from the value of the purchased materials (inventory), and all discounts or deductions that were obtained or that the contractor should have been obtained if the payment occurs during the discount period, shall be excluded from the value of the purchased materials.</p>
5-	<p>The government auditors must evaluate the warehouse system, and the procedures for auditing it, and reinforce this by conducting an interview with the company's warehouse officials, knowing their views on the internal control procedures, obtaining and studying the latest inventory list, and verifying the conformity of the actual inventory in the stores with their balances in the records.</p>
6-	<p>Request the sufficient confirmations (certifications) for the inventory items that have been sold, and ensure that proper procedures are followed in this regard.</p>
7-	<p>Ensure that the government participates in the procedures that take place when some purchases are re-exported (purchase revenues).</p>
8-	<p>Verify the conformity of inventory materials deposited with third parties and obtain approvals from those parties.</p>
9-	<p>Verify the validity of the stores and their compliance with the conditions of public safety.</p>
10-	<p>Verify the organization of entry and exit documents of the incoming and outgoing warehouse materials.</p>

E- Control and audit procedures for the services provided by the head office:

The oil companies operating in the host country depend on their head office to obtain many services and carry out many tasks, but it is not easy to link those services, and their costs directly with the operation of the contract, and they usually represent the costs of business of a general nature, which are at the general administrative level, that means those general costs associated with executive and administrative functions, which are due to companies operating in their head offices, branch offices, or the like, which are above the level of direct operating of the contract, and which are carried out for the purpose of supervising or managing private development or production operations of the service contract, vis-a-vis the accounting costs, legal support provided by the head office of the operating company located outside the host country, and other costs that indirectly benefit the contract.

The supervision services provided by the head office of the operating company, at the country level, that occur during drilling and production, which is of a general nature, and is considered among the additional burdens.

Here, we find that this type of services is one of the biggest problems that appear during the implementation of control and audit work of service contracts, and in fact, the costs associated with those services are the most controversial between the government and the oil company, and accordingly the following procedures are adopted when reviewing those costs:-

No.	Audit Procedures
1-	For the lack of clarity of the items that is covered through the percentage of additional costs or what is sometimes called the fixed burdens. In general, what is calculated in the list of costs, through the percentage of additional costs, is in exchange for what the headquarters of the company provides to its branch at the host country such as works of an administrative, accounting, legal, technical nature, technical supervision, and senior management work.
2-	As for the technical services provided by the head office, the salaries, wages and costs associated with the employee working in the offices of the working company, are considered direct costs and therefore recoverable. For example, geologists residing in the offices of the company operating outside the host country and working for the benefit of the oil field, or the contract in the host country. This is reinforced by a record of time in the assigned lists so that the cost of that time is considered direct costs.
3-	In the event that technical services are provided by a third party through the head office, in this case its costs are direct, and therefore recoverable. And this party may be an affiliate company of the operating company. In this case, the actual value is only considered as recoverable costs, excluding any profits that may be added, and the amount should not exceed the value of the service, if it

	was obtained from other party not related to the operating company, and this will be achieved through comparison with what others ask for costs of the same service.
4-	<p>There are many items, which are usually the focus of discussions and negotiations between the host country and the oil company, as a result of audit. Questions are usually raised, and by answering them the possibility of considering the costs within the recoverable costs or not is determined. So the government auditors should realize:</p> <p>A set of questions about additional costs:</p> <p>A- What are the types of additional costs in the head office that are recoverable?</p> <p>B - Are these costs within reasonable limits, and are they supportive and directly related to oil operations?</p> <p>C-What is the basis for charging the operating company at the host country with the additional costs?</p> <p>D-Are the charging bases fixed from year to year, and are they applied on a continuous basis to other similar interests of the company.</p> <p>E- How to determine the amounts in the invoice submitted by the head office?</p> <p>F- What are the procedures to be followed in determining the time the technicians spend on different work in favor of the contract?</p>

The answer to the previous inquiries represents the axis of viewpoints discrepancy between the oil company and the government, and what makes the matter more difficult is that the service contract does not clearly answer those inquiries.

In order to ascertain the extent of the recoverability of costs or not, it is necessary doing as follows:

No.	Audit Procedures
1-	Obtaining details of the amounts charged to the branch directly by the head office abroad.
2-	Obtaining an order to task assignment. It is assumed that there should be a prior agreement between the government represented by the technicians and the operating company on the type of task to be carried out in the head office and the issuance of a written approval so that the costs is considered recoverable.

3-	Obtaining (Time Sheet) for individuals who have executed the work assigned to obtain time lists to them.
4-	Obtaining a report on the result of the work, as proof of the implementation of the task.
5-	Obtain accurate details about the nature of the assignment, in order to be sure that the costs are considered direct. If the work is in exchange for a precisely defined technical work for the benefit of the oil operations in the country, then the cost is accepted, unless the cost is included within the overhead and therefore it must be excluded from the list of costs.
6-	It should be noted that if, during the fieldwork of the audit, a refusal of a specific cost from the expenditures charged directly by the head office became apparent, this must be documented by including a copy of all the documents issued by the head office, with the company officials being informed of the reason for the refusal with its discussion. If the discussion Or the conviction resulted that a certain amount has been excluded from those costs, then it must be followed by decreasing the of the additional costs, which is calculated on the basis of the percentage agreed upon in the service contract, to the extent of the effect of the excluded cost, which is calculated by multiplying the amount of the cost that was excluded by the percentage of the additional cost. This point is extremely important, due to the lack of awareness in many cases during the review and preparation of the oversight report on the expenditures of oil companies in accordance with the service contract.

F- Procedures for controlling and auditing the distribution of joint costs:

Joint costs can be divided into two types:-

The first type: joint costs between more than one contract:

This happens in those cases in which the operating company manages more than one contract, using the common assets and staffs among those contracts:-

No.	Audit Procedures
1-	In this case, the auditor must verify the correctness of the distribution of the joint costs between the beneficiary contracts, as in the event of an error in the distribution between productive and non-productive contracts, it will have a negative and significant impact on the cost of crude oil production within the producing field area, because there is an interest in the operating oil company to load the productive contracts by a large percentage of costs to ensure the recovery of their amounts, with a low percentage of those costs allocated to contracts that are still in the exploration

stage, as oil may not be obtained, and therefore oil companies bear all the amounts according to the provisions of service contracts and some other contracts.

The second type: joint costs between the stages of extraction in the same contract:

It is known that there are some of joint costs, which are made for the benefit of the different stages of oil extraction, and these costs are distributed to the beneficiary business according to certain bases.

And in light of service contracts, this aspect must be given great attention by the auditors, as the distribution of joint costs affects the cost of the produced oil recovered by the oil companies, based on service contracts that guarantee the recovery of operating costs at a rate of (100%) during the year in which disbursement was made. While only certain percentages are determined to recover for each of the exploration and development costs. For this reason, the following procedures are taken into account when auditing the joint costs:-

No.	Audit Procedures
1-	Determining the joint costs to be distributed and providing documents supporting the correctness of their calculation.
2-	Knowing the principles followed in the distribution and their compatibility with the bases agreed upon in the contract or in the correspondence that takes place between the governmental and the oil company, or in the accepted accounting standards in the oil sector.
3-	Verifying the distribution of costs between different petroleum industries of (exploration phase, development phase, production phase) with agreed fundamentals in the contract or correspondences between the government and the oil company or in the accepted accounting standards in the oil sector.

G - Procedures for auditing the service fees (remuneration fees) of foreign oil companies:-

The service contracts include granting foreign companies service fees (remuneration fees) paid to the contractor for the purposes of supplementary production calculated according to the provisions of the contract, as well as granting these companies the administrative charges calculated on the total capital and operating costs. The service fees and the administrative charges are deemed as recoverable costs on the government, the auditors shall take into account the following aspect during audit:-

No.	Audit Procedures
1-	<p>When auditing the amounts of service fees (remuneration fees) granted to the foreign company, the following shall be taken into account: -</p> <p>A-Verification of the calculation and payment of service fees to the contractor. The operating account begins after the due date of service fees for each calendar quarter, commencing from the quarter that follows the quarter in which the due date of service fees occurs, the amount of service fees will be equal to the sum of the service fees for each barrels in each quarter, with multiplied by the incremental production applicable to such quarter and subject to performance adjustments from the stage of operating account- after the date of entitlement of service fees.</p> <p>B-Determining the quantity of the total production of the oil field and the quantity of the baseline production of the field for the purpose of determining the quantity of the net production that will be adopted in calculating the service fees as in the following formula:-</p> <p>(Total Production during the quarter- Baseline Production= Net Production)</p> <p>C- Determining the service fees for each barrel and according to the terms of the contract</p> <p>D- Calculating the due service fees through (the amount of net production × the service fees per barrel) and comparing the results of the calculation with the service fees mentioned in the list of costs approved by the government to verify the correctness of the calculation and the absence of differences.</p> <p>The auditors of the governmental must determine the tax rate imposed on the service fees of foreign companies in accordance with the laws in force.</p> <p>E- Verify that the foreign company pays the tax arising from service fees paid to the companies, in accordance with the laws in force, on a timely basis, and without delay.</p> <p>F-When there are several foreign oil companies contracting with the government, verify that there are no differences in calculating the service fees for each produced barrel of oil, and when there are differences, it is necessary to search for their causes and express an opinion regarding that.</p>
2-	<p>When auditing the amounts of administrative charges granted to the foreign company, the following shall be taken into account:-</p> <p>A- Determining the percentage of the administrative charges contained in the service contract.</p>

	<p>B- Determining the total operating costs approved by the authorized bodies in the governmental.</p> <p>C-Ensure the accuracy of calculating the administrative charges calculated on the operating costs included in the list of costs through the following equation {total operating costs x the percentage of administrative charges} under the contract and comparing the results of the calculation with the administrative charges in the list of costs approved by the government to make sure of the calculation correctness and absence of differences.</p> <p>D- Ensure the correctness of classification of the amounts of administrative charges calculated on the operating costs on their related operating accounts.</p> <p>E- Ensuring the accuracy of calculating the administrative charges calculated on the capital costs included in the list of costs through the following equation {total capital costs x percentage of administrative charges under the contract} and comparing the results of the calculation with the administrative charges included in the list of costs approved by the government to verify the correctness of the calculation and the absence of differences.</p> <p>F- Ensure the correctness of classification of the amounts of administrative charges calculated on the capital costs on their related fixed assets accounts.</p>
--	--

H- Procedures for auditing the differences of currency rates:

Amounts of economic events of monetary nature related to the oil field, such as purchases and payment of salaries and wages, are recorded according to the currency specified in the service contract, and the following procedures are taken into account in auditing:-

No.	Audit Procedures
1-	If the purchase was made in different currencies, and the registration in the books is in US dollars, in this case, the impact of this on the list of costs is taken into account, and the government auditors must ensure that the exchange rates for other currencies with their equivalent in US dollars are based on the exchange rate contained in the bulletin approved in the service contracts and the date of the transaction.
2-	If the purchase and payment of salaries are in the local currency, it shall be converted into US dollars on the basis of the official purchase exchange rate determined by the central bank in the country.

I- Audit procedures to verify that non-recoverable costs are not included in the list of costs:

Service contracts must include a clear and explicit description of the non-recoverable costs. The government auditor must verify that these costs are excluded from the list of recoverable costs. The exclusion of those costs is verified through the following:

No. Details of control and audit procedures for non- recoverable costs	
1-	The costs incurred as a result of any negligence, default or willful mismanagement by the operator/ contractor shall be established and shall include any amounts paid to settle any complaint alleging total negligence or willful mismanagement, and shall be paid without consideration or on a similar basis.
2-	Costs arising directly or indirectly from petroleum operations by financing the petroleum operations and other incidental costs, for example interest, commissions, wages and brokerage.
3-	Costs or expenditures of grants related to public relations or promotion of the contractor's common interests and concepts, and social benefits that are not related to petroleum activities.
4-	Any costs not related to petroleum operations or activities beyond a delivery point as: - Corporate income tax. -Training, technology and scholarship fund. -Any other expenses mentioned in this contract to be non-recoverable.

3-5-3 Control and audit procedures of the capital costs.

A- Procedures for controlling and auditing costs related to fixed assets:

The nature of costs related to fixed assets in light of service contracts and the consequent accounting treatments are different from what is known from the procedures followed in the normal control, as the costs of purchasing those assets are charged to the costs that are recoverable during the period in which the purchase is made.

A list of financial position is not prepared in light of the service contracts by the operating oil company, through which the assets appear, as those assets appear in the list of period costs only, and therefore the government audit is conducted to verify whether that the costs of assets are recoverable or not. The asset continues to be used by the oil company until it is disposed of or returned to the government, and therefore the asset is considered the property of the government once the oil company recovers its value according to what is stated in the contract.

And what distinguishes dealing with fixed assets under service contracts that depreciation is not calculated for them, as is common because, as mentioned above, since the goal of audit and control is to reach to the activity result not to determine the recoverable costs. Subsequently, it is reached to calculate the recoverable production costs and in light of the foregoing, the costs of fixed assets are audited by the government under service contracts according to the following:-

No.	Audit Procedures
1-	Request lists of all fixed assets purchased during the period under audit and ensure that they are classified on their respective accounts.
2-	Ensure that the audited oil company maintains a special record of fixed assets that includes the asset's name, details, location and the movements made on it.
3-	Request a list of all assets that have been disposed of during the period under audit, the list includes (type of asset, number, type of disposal either written off or gift, or other areas of disposal, date of its use in the activity, date of disposal).
4-	Ensure that the contractor keeps records of all types of fixed assets that include full information about all assets.
5-	Verify that all assets acquired or insured by the contractor related to petroleum operations, as well as costs subject to recovery in accordance with the provisions of the contract, are recorded from the property of the national oil company.
6-	Verify that the national oil company or the contractor don't sell or dispose of the assets for the purposes of the contract and for the duration of its validity (fixed and/or movable assets) except in the case of a joint agreement.
7-	Ensure that the government is informed in a timely manner of any lost asset and the measures taken about that.
8-	Any taxes recovered by the contractor when purchasing from abroad shall be excluded from the value of the purchased asset, and all deductions or discounts that were obtained or that the contractor should have obtained if payment had been made during the discount period shall be excluded from the value of the purchased assets.
9-	Ensuring that the operating company has the necessary insurance on the fixed assets. If there are claims for compensation, this must be reviewed and the necessary compensation is verified and recorded in the correct manner.
10-	Ensure the proper registration of the purchased assets and that the registration is made in the assets account and not within the purchases of materials and supplies, as this means that the asset does not appear within the fixed assets and therefore considers it as an expense in the year of purchase. Therefore, it is difficult to follow up on that asset from a year to another and it may be lost or disposed of without any impact on the accounting books and is even difficult to detect. In the event that a specific asset is considered within a specific item

	of costs, the matter requires making the appropriate correction in the accounting books, as well as making the consequent adjustment of that correction in the list of costs.
11-	Ensuring that the oil company uses the assets correctly and that they are maintained in accordance with periodic maintenance programs and in the correct manner.
12-	Verify that there is a real need to purchase assets, and that there is no exaggeration in determining the types and numbers of assets that have been purchased, specifically means of transportation and computers, which leads to inflation of the costs of oil production.
13-	Verifying the commitment to purchase fixed assets in accordance with what was stated in the purchase budget approved by the Joint Management Committee. And verifying the purchase lists and all enhanced documents for purchase.
14-	Ensure that the inventory process of fixed assets is carried out during the audit period and that the numbers received according to the actual inventory process are matched with the records; identify the differences (if any) and their causes and work to address them.
15-	Verify that all assets acquired and/or supplied by the contractor or operator connected to or related to petroleum operations and whose costs considered recoverable costs are according to the provisions of the service contract. And also verify the integrity of the property registration of the purchased means of transportation of all kinds in the name of the government at the official authorities.
16-	The government shall inform the foreign contractor of all the laws and instructions in force regulating cases of purchase of fixed assets, for example, the instructions specifying the year of manufacture of the means of transportation upon purchase and other instructions.

3-5-4 Control and Audit Procedures for Production:

The procedures for controlling and auditing the production quantities of crude oil in the oil fields under the oil service contracts are taken into consideration:

No.	The details
1-	This audit is achieved through technical observers representing the government in the production sites and fields for each oil company.
2-	Technicians play a direct role in monitoring the quantity delivered and the shipments that take place in oil tanks. The reports prepared by government technicians and monitors are considered an essential means in the control process over the delivered quantities.

3-	Measuring the produced and shipped quantities, which the government observers must be aware of, to ensure that the control procedures are applied correctly.
4-	The tank counters, tests and various measurements are read, and the reports for measuring quantities are studied and reviewed and matched with the delivered quantity.
5-	Does the government check and test volumetric devices at regular intervals and in accordance with regulations?
6-	<p>Does the government review the company's reports and documents against supporting information or other sources?</p> <p>-Auditing production volumes usually entails regular review and examination of documentation, such as project reports and supporting information, as well as physical inspections of extraction operations and accuracy of production measuring equipment.</p> <p>- Although some cases of uncertainty is inherent in any measurement, it is important to avoid -bias -systematic error that constantly increases or decreases size.</p> <p>- Checking the production separation of each field separately in case the foreign partner (contractor) owns more than one field in the region, in order not to overlap the production of those fields, which may differ in proportions and recovery rates.</p>
7-	<p>Verify the existence of independent warehouses for each field in which production is aggregated and pumped to the main warehouses or (refineries), provided that the following is reviewed:</p> <ul style="list-style-type: none"> - Existence of measurement meters to measure the pumped products. - Conducting the required tests to measure the product quality. - Making daily reports of the quantities pumped to the main warehouses, which are supervised by government representatives and signed by the officials of the plant, storage and production units.
8-	The shipping documents in the field are compared with the reports of adding the main warehouses and verifying the conformity of the quantities, technical specifications, and percentages of wastage and water in the product according to the recognized ratios.
9-	Matching the quantities delivered to the main warehouses with the quantities listed in the recovery lists and verifying the correctness of their calculation.
10-	Verifying the presence of meters in the production, receiving and delivery sites, their adequacy, and the safety of their calibration procedures. Does the government check and test volume measuring equipment at regular intervals and in accordance with the rules and provisions? It is also verified that the government compares the company's reports and documents with supporting information or other sources.
11-	Verify that auditors monitor government entities and oversight bodies to ensure compliance with laws and agreements regulating oil and gas exploration,

	<p>development and production. In addition, verifying that the national oil company monitors operations throughout the entire project cycle. the auditors shall assess the following:-</p> <p>-Are the oversight roles and responsibilities of each party in the regulatory framework clearly defined?</p> <p>-What accountability and verification systems have been put in place to monitor the company performance, such as accounting procedures and periodic independent audits?</p>
12-	Verify that the foreign company has taken the procedures and measures for maintaining the proportion of reservoir pressures within its standard limits and for all oil reservoirs within the contract area. In the event of its decline, measuring the impact of this decline on the production process, and measuring the action taken to treat it, with the additional costs that have been charged to the production process as a result.
13-	Verify the contractor's commitment to achieving the target of plateau production, net production rate and the first commercial production rate of crude oil specified in each round of licensing.
14-	Verify that the contractor estimates and determines the maximum volume of reserves and petroleum resources annually in the contract area.
15-	Exploitation of the associated gas by the national oil company and the operating company, and it is not permissible to burn it except in accordance with the law and as stipulated in the contract.
16-	Verifying the quality of the produced quantities by comparing the percentage of water, impurities and actual salts of the quantities of crude oil inside the warehouses with their standard ratios specified under the service contract.

3-5-5 Procedures for auditing the extent to which social and environmental standards and sustainable development requirements are met:

Reviewing of executive procedures to verify the extent to which social and environmental standards and sustainable development goals have been achieved as a result of the implementation of the service contract, as in the following:

No.	The details
1-	Verifying the contribution of the concluded contracts to achieving a good standard of living and assuring the quality of life and welfare by providing adequate income, careers, and jobs opportunities for the members of the community.

2-	Ensuring a high level of economic growth that contributes to improving the quality of life and ensuring the well-being of all citizens.
3-	Verify that climate change and disaster risks are reduced.
4-	Verify the existence of cooperation between the extractive activities management with local communities and neighboring and farmers
5-	Verifying the contribution of extractive industries to improving energy efficiency and reducing gas emissions.
6-	Verify that health impact assessments are conducted to enhance the ability to manage health risks as well as environmental and occupational risks.
7-	Verify the existence of a strategy for the full impact of the extractive operations within the oil field boundaries on the local water resources and the potential impact of water scarcity on its extractive operations.
8-	<p>Ensure that the operator implements everything related to the protection of the environment and the sustainability of natural resources specifically, as follows:</p> <p>A- Adopting the best practices of the international petroleum industry in managing and monitoring operations, and taking appropriate and sufficient steps to:</p> <p>First - Avoiding environmental damages and minimizing them if these damages and effects will occur inevitably on people and property.</p> <p>Second - Preventing damage to livelihoods or the quality of life in the surrounding communities or spoiling them and reduce it to a minimum if it will inevitably occur to ensure adequate compensation for an injury persons or property damage caused by the impact of petroleum operations.</p> <p>B - Develop detailed guidelines for environmental protection, monitoring and community interaction as a prerequisite for petroleum operations, these guidelines must meet the internationally applicable industry standards in the following areas:</p> <p>First - air pollution.</p> <p>Second - Protection of water bodies from oil leaks and spills, including preparing a plan for injection all produced water and a plan to prevent and control the occurrence of oil spills and ways to treat them.</p> <p>Third - protection of groundwater.</p> <p>Fourth - Waste management such as solid waste and hazardous waste, with a focus on waste reduction.</p> <p>Fifth - Reducing the sites of drilling operations to a minimum, especially in sensitive areas such as the marshes.</p>

	<p>Sixth - optimum utilization of the boreholes of the reserve wells.</p> <p>Seventh: Protection of plant and animal life.</p> <p>Eighth: Protecting archaeological and cultural sites.</p> <p>Ninth: Plans to end the assignment and abandon petroleum facilities.</p> <p>Tenth - compensation for land and resettlement of local communities within the petroleum operations.</p> <p>Eleventh - Implementing the grievance mechanism between the contractor and the communities affected by petroleum operations.</p> <p>Twelve. Preserving the livelihoods of indigenous communities in the contract area.</p> <p>Thirteen - Work to achieve prosperity for communities wherever operations are carried out in cooperation with the local authority and civil society organizations.</p> <p>B- Ensure that the contractor team, should include professional environmental specialists, to conduct two environmental impact studies for the purpose of :-</p> <p>First: Determine the prevailing conditions (in the period of studies related to the environment, humans, local communities and local wildlife, plants and animals) in the contract area and the adjacent areas.</p> <p>Second: Providing the necessary solutions and measures to reduce environmental damage and implementing activities of site repair.</p>
9-	<p>Ensure that the contractor and operator comply with the provisions of the law in all respects, and the contractor must indemnify the state oil company and avoid it from damage in return for all penalties, fines and other responsibilities of all kinds for violating the law by the contractor or Operator.</p>
10-	<p>Verify that the government is monitoring the achievement and comparing it with the company's environmental and social impact assessment and related administrative plans, as well as verifying that penalties have been identified or taken other measures to hold companies accountable for negative social or environmental impacts.</p>

FRAMEWORK OF GOVERNMENT
AUDITING STANDARDS



