

Roll No.

Time allowed : 3 hours

Maximum marks : 100

Total number of questions : 6

Total number of printed pages : 8

NOTE : Answer **ALL** Questions.

1. Read and analyze the following case study and answer the questions given at the end:

On 20 April 2010, a massive explosion occurred on the Deepwater Horizon oil rig in the Gulf of Mexico. Eleven workers perished. Two days later, the rig sank, snapping the riser pipe and creating a massive oil spill. Although the Macondo well was effectively killed by 19 September 2010, the incident had tarnished BP's reputation and prompted further questions on the company's safety and environmental record. It also produced the largest accidental marine oil spill in history, at 19 times the size of the 1989 Exxon Valdez spill.

A History of Mistakes

The Deepwater Horizon spill was not the only disaster that had afflicted BP in its recent troubled history. The company had previously racked up a number of safety breaches over the years. In March 2005, a fire and explosion in its Texas City Refinery killed 15 people and injured more than 170 workers. It resulted in financial losses exceeding US\$1.5 billion.

A few months later in July, a wrongly-installed valve and shoddy welding in underwater parts of BP's Thunder Horse oil platform caused the vessel to flood and almost sink when Hurricane Dennis hit. While BP and its minority partner Exxon Mobil had to pay hundreds of millions of dollars in repairs, and with oil production being set back 3 years, it appeared BP had yet to learn its lesson. Months later, in March 2006, BP's operations in Prudhoe Bay, Alaska, experienced an oil spill, with up to 267,000 gallons of thick crude oil deposited, due to widespread corrosion in under-maintained and poorly inspected pipes – a situation which could have been prevented.

In May 2007, Tony Hayward replaced John Browne as CEO and made a commitment to focus on "safety and reliability" like a "laser". Under his reign, BP showed improvements in safety and had begun to improve its reputation.

It all came crashing down with the Deepwater Horizon incident at BP's Macondo well.

“I’d Like to Get My Life Back”

In the immediate aftermath of the incident, it was determined that the best possible solution was a relief well. However, this would take about three months to complete. BP sought a faster solution by organising a massive team of about “48,000 spill responders and deployed more than 6,900 vessels to collect and contain oil and lay out more than 13 million feet of protective boom”.

While BP was focused on containing the spill, the unfolding crisis was exacerbated by the company’s mishandling of the media and lack of communication with stakeholders. BP initially reported that the well was leaking 1,000 barrels a day; while the US government discovered that the actual rate was 12,000 to 19,000 barrels a day. That essentially was “the moment the American administration exposed BP’s crude lie [and] was the moment the company’s fate was sealed”, and the public turned on BP.

Perhaps the largest uproar was created when Hayward remarked at the height of the disaster on 30 April 2010, “I’d like my life back”, which was viewed as yet another indication of how out of touch the BP management was with the situation.

Communication with Shareholders

When the US Christian Brothers Investment Services resorted to register a protest vote, BP tried to convince them that more information would be found in the group’s financial report. However, when it was published, the situation was not much clearer. Further, BP’s method of communication through its financial report did not satisfy its shareholders as “little information is provided on issues with significant reputational and financial implications, such as the short - and long-term toxicity concerns related to BP’s substantial dispersant use, efforts to revive the Gulf Coast economy, and backlogs for claimants”.

Directors’ Remuneration

The BP’s Directors’ Remuneration Report of 2009 showed that the top level managers of BP were receiving bonuses averaging 170 per cent of their salary. 15 per cent of this was based on safety measures while about 70 per cent of the bonus was a reflection of the Group’s financial and operating performance.

Reflecting the emphasis on performance and financial results above all other operating metrics, significant efforts were made in 2009 to reduce cash costs substantially. Production increased by more than 4 per cent while unit production costs were reduced by 12 per cent. The reserves replacement ratio was 129 per cent, continuing an industry-leading performance. Refining and marketing cash costs were reduced by 15 per cent, and refining availability increased to 94 per cent. While BP now had one of the best performance figures of the big oil companies, safety seems to have become second to profit.

In Too “Deep”: Safety Measures and Whistle-blowing

A confidential survey of workers on the Deepwater Horizon in the weeks before the oil rig exploded showed that many of them were concerned about safety practices. Only about half of the workers interviewed felt they could report actions leading to a potentially “risky” situation without reprisal. “This fear was seen to be driven by decisions made in Houston, rather than those made by rig based leaders,” the report said.

During the subsequent investigations, it was found that safety documentation required by Minerals Management Service (MMS) regulations, and information on emergency procedures was not available. Furthermore, Transocean Ltd, which owned the rig and leased it to BP, would not provide detailed accounting of the Deepwater rig’s activity history. Lead federal investigator Hung Nguyen chastised BP officials after they failed to point out who was responsible for ensuring safety for the company’s deep water operations.

As Stuart Sneed, a pipeline safety technician who was removed from the company in 2006 when he ordered work to stop due to safety concerns remarked in an interview about BP’s corporate culture:

“They say it’s your duty to come forward, but then when you do come forward, they screw you. They’ll destroy your life. No one up there is ever going to say anything if there is something they see is unsafe. They are not going to say a word”.

The Aftermath

Dividend Policy

Following a meeting with President Barack Obama on 16 June 2010, BP announced an agreement with the US government where it will set aside a US\$20-billion fund to pay all legitimate claims for compensation. It also committed US\$500 million to a 10-year independent research programme that will examine the long-term environmental impact of the oil spilled and dispersants used. As a consequence of the liabilities, the BP board released a statement to cancel the previously declared first quarter dividend payment. A further announcement declared that there would be no interim dividends for the second and third quarters of 2010. The board, however, also provided a “strong commitment” in a media statement on the payment of future dividends once the long-term impact of the Deepwater Horizon spill was better assessed at the end of 2010.

Rewards for failed leadership

On 27 July 2010, the board announced Tony Hayward’s departure from his position as Group CEO with effect from 1 October 2010. This decision was made by a “mutual agreement” between the board and Hayward. The board also approved a plan to name Robert Dudley, who was already in charge of the Gulf cleanup, as CEO.

The board was legally obliged to honour Hayward's contractual terms, which entitled him to a severance payment of a year's salary at about £1million. Hayward was allowed to immediately take out £600,000 from his pension pot (valued at £11 million). His cash-based compensation alone amounted to about £12 million and he retained his rights to a long term share performance plan. Hayward would be nominated as a nonexecutive director at TNK-BP, BP's joint venture in Russia.

Commentators wondered why Hayward was rewarded for his "failed" leadership when he had put the oil giant in the midst of a severe political storm and was responsible for a 40 per cent loss in market capitalization. The potential increase in his wealth – a result of a recent share price rally which saw BP's stock price rise to 467p, driving up the value of his performance shares' value to £8 million - also revived public anger towards the issue of excessive executive payments by BP.

The BP board was thus heavily criticised. The directors' commitment and effectiveness in handling the crisis were questioned, with the lack of oversight in operational activities, slow reaction in resolving the disaster and excessive executive compensation, cited as reasons.

To reduce public dissatisfaction, it was announced that no annual cash bonus for 2010 was awarded to Dudley, Hayward and Andy Inglis, a board member who left the board on 31 October 2010. Furthermore, no shares under a long-term incentive plan would be vested for any executive director. Dudley also announced a review of all employee remuneration for the fourth quarter of the year 2010. The sole criterion for assessing employee performance and bonuses in the fourth quarter would be based on reducing operational risks and achieving excellent safety and compliance standards.

The board itself promised to improve the effectiveness of its discharge of duties. It would increase the number of its work site visits, especially for troubled Exploration & Production operations; and revamp and enhance the safety committee with new blood. The board would also play a more significant role in crisis planning and management. For example, the board would require more informative reports on the Company's operating activities to help it better oversee the likelihood of future disasters.

Storm on the Horizon

BP's constant false promises and failures to improve safety led shareholders to bring derivative suits on behalf of the company on the grounds of misrepresentation, and securities fraud suits for the loss of BP's market value. The board was also a target of these law suits as they were viewed as not having fulfilled their duties in exercising oversight over management. As at 20 January 2012, analysts at Morgan Stanley estimated that the total amount of litigation damages BP could potentially incur from all criminal and civil lawsuits could be as much as US\$25 billion.

The remedial efforts performed by the company seemed to be insufficient as executives faced angry protesters, including fishermen and women from the Gulf and climate change activists, during its annual meeting in London on 14 April 2011. The company denied entry to protesters on the grounds that it had an obligation to run an orderly AGM. Meanwhile, inside, hundreds of BP investors – individual, corporate and institutional alike – questioned board members about the excessive executive pay, a lack of transparency on safety improvements, and lack of disclosure on the full environmental impact of BP's projects.

The Journey Ahead

While BP had effectively killed the Macondo well by 19 September 2010, hundreds of ongoing lawsuits and fines could yet add billions of dollars to its already staggering liabilities, while the findings of several investigations in progress could further damage its reputation. BP has estimated that the spill would cost the company at least US\$40.9 billion and the company could ill-afford another disaster of this scale. As of 9 January 2012, BP disclosed that it had spent an estimated US\$14 billion on the response to the disaster, and that it had set aside US\$20 billion for economic claims and natural resource restoration and US\$1 billion for early restoration projects.

The funding for early restoration projects was to signal the company's commitment to mitigate its actions and the impact on the environment, and in conjunction with this, BP signed an agreement with federal and state agencies for these early restoration projects aimed at the recovery of areas along the Gulf Coast. BP also stepped up its corporate social responsibility by renewing its focus on safety and risk management. The Safety and Operational Risk (S&OR) unit created by Dudley upon his appointment as CEO went "live" on 31 March 2011 and became fully operational as of May 2011, with "sweeping powers to oversee and audit [BP's] operations around the world".

On 15 July 2011, the company made a pledge to the Bureau of Ocean Energy Management, Regulation and Enforcement (BOEMRE) to implement a "new set of deepwater oil and gas drilling standards for its operations in the US Gulf of Mexico". The pledge appeared to work, as BP was granted its first permit to drill for oil in the Gulf on 26 October 2011⁴⁴. Still, BP was issued citations by the Bureau of Safety and Environmental Enforcement on 12 October, with the very high possibility of paying "multimillion-dollar fines" for causing the spill. Should the Clean Water Act be invoked at a later date, BP would be required to pay heftier fines of up to US\$4,300 for every barrel of oil spilled or up to US\$21 billion altogether.

While BP has taken some significant steps to rebuild public trust and investor confidence and mend its tattered reputation with the award of "67 new exploration licences in 11 countries", it remains to be seen if BP will continue to project credible commitment through its actions towards improving its safety standards and preventing another "Deepwater".

Answer the following questions:

- (a) With regard to the disaster, how do you think the BP CEO behaved appropriately? (10 marks)
- (b) Should the board and its Chairman, Carl-Henric Svanberg, be held equally responsible along with the CEO? (10 marks)
- (c) BP had a comprehensive code of conduct and a whistleblower policy but did not implement them effectively. Why do you think this is so? What steps should a company like BP take to ensure that its code of conduct and whistleblower policy are effectively implemented? (5+5=10 marks)
- (d) Evaluate how BP communicated with stakeholders following the disaster. (10 marks)
- (e) What measures do you think the BP board should implement to mitigate the chances of such a catastrophic accident happening in the future? (10 marks)

2. (a) You are the Company Secretary of a large fertilizer company having five manufacturing plants in different parts of the country. Recently there was leakage of ammonia gas in one of the plants and it was hugely affected the people living in that area. Due to this impact people demonstrating and demanding to close the factory. To pacify the people and the environmentalist group the company has decided to set up corporate social responsibility committee and to assess the future risk it also decided to set up risk management committee. Therefore company asked you to help him in setting these two committees. The board has asked you to prepare paper which summarizes the main aspect of corporate social responsibility committee and risk management committee and the importance of these committees.

(10 marks)

- (b) There is lot of criticism regarding directors' remuneration even many shareholders are asking questions why so much money being paid as remuneration to the directors. The board has been having regular meetings, and at the last meeting decided it was worried about disclosures relating to directors' remuneration. Until now, remuneration has not been disclosed in the company's annual reports. Draft a report citing the key applicable provisions pertaining to Appointment & Remuneration of Managerial Personnel and Remuneration of Directors of a listed company for the next board meeting.
- (10 marks)
- (c) How Secretarial Auditor is instrumental in ensuring good Corporate Governance in a company? Explain.
- (10 marks)
3. Government is the major shareholder in public sector undertaking/central public sector enterprises (CPSE) therefore it is expected that the government should take responsibility to set high standard of governance and good governance means transparency and accountability. Analyze the government initiative regarding Corporate Governance in setting high standard in public sector enterprises.
- (5 marks)
4. SEBI requires the listed companies to include a separate report on Corporate Governance in their Annual Report. If you have been asked to prepare that report which will be attached in the company Annual Report then what are the information under disclosure norms you will give to be made available in the Corporate Governance page of Annual Report.
- (5 marks)
5. Effective board management is directly related to the outcome of better Corporate Governance in companies. In context of betterment of Corporate Governance discuss the role of Women Director, Resident Director and why SEBI is strict on Women Director issue.
- (5 marks)

Q6. It is generally understood that manufacturing companies should give importance to corporate sustainability but why the non-manufacturing companies and firms in service sector should also give equal importance to corporate sustainability and if they ignore it what will be the long term impact.

(5 marks)