CHAPTER: 6
CORPORATE GOVERNANCE IN OIL PSUs

6.1 Introduction

Corporate governance is the system by which Companies are directed and controlled by the management in the best interest of the stakeholders and others ensuring greater transparency and better and timely financial reporting. The objectives of corporate governance are fulfilled by setting up appropriate structure and functioning mechanisms for the Board of Directors and Audit Committees, as laid down by the Companies Act, 1956.

6.2 Audit Scope and Objectives

This study aims to ascertain whether the Public Sector Undertakings (PSUs) in the Petroleum Sector have an effective corporate governance mechanism. This objective has been further split to examine the setup and functioning of the Board of Directors and of the Audit Committees in the following PSUs in the petroleum sector:

1. Oil and Natural Gas Corporation Limited (ONGC),
2. ONGC Videsh Limited,
3. Indian Oil Corporation Limited (IOC),
4. Bharat Petroleum Corporation Limited (BPCL),
5. Bongaigaon Refinery and Petrochemicals Limited (BRPL)
6. Chennai Petroleum Corporation Limited (CPCL),
7. Hindustan Petroleum Corporation Limited (HPCL),
8. Kochi Refinery Limited (KRL),
9. Guru Gobind Singh Refineries Limited (GGSR),
10. Mangalore Refinery and Petrochemicals Limited (MRPL),
11. IBP Company Limited (IBP).
12. Gas Authority India Limited (GAIL)

6.3 *Audit Findings*

The audit findings vis-a-vis the audit objectives of this study are detailed below:

6.4 Setting up of proper and effective Audit Committee Mechanism

In order to ensure transparency and accountability, clause 49 of the Listing Agreements read with Section 292A of the Companies Act, 1956 lays down the provisions for constitution of Audit Committee. Audit examined whether the Companies covered by the current study had complied with the above-mentioned provisions.

6.4.1 Formation of Audit Committee

In all the PSUs examined by Audit, the Audit Committee had been formed as per requirements of Clause 49 of the Listing Agreement and Section 292A of the Companies

Act, 1956. The Audit Committee in ONGC had been renamed as Audit and Ethics Committee (November 2002).

6.4.2 Functioning of Audit Committee

In all the Companies the Audit Committee was functioning effectively. The Board had also specified the terms of reference of the Audit Committee in the PSUs. The Audit Committees in most of the PSUs had the power to investigate any activity within its terms of reference. In respect of IOC, a new Whistle Blower Policy had been approved by the Board, under which any individual coming across an unethical or improper practice would be able to approach the Audit Committee for protection from unfair termination or unfair and prejudicial practices adopted by the Management. However, the following deviations were observed in the functioning of the Audit Committee in respect of BPCL, CPCL, GGSR, HPCL, KRL, MRPL and ONGC:

- The Audit Committee of BPCL, CPCL, KRL, HPCL and ONGC had not undertaken any investigation into the matter in relation to the items specified in section 292A. Nor had any such item been referred to the Committee by the Board. However, the Audit Committee of BPCL, HPCL and ONGC had full access to the records of the Company;
- In the case of ONGC and BPCL, the Chairman of the Audit Committee had been appointed by their Board of Directors instead of being elected by the members from amongst themselves;
- In respect of MRPL the follow up action taken on investigation by the Audit Committee was not discussed by the Board;
- In GGSR and KRL the Chairman of the Audit Committee did not attend the Annual General Meeting.

6.4.3 Role of Audit Committee in reviewing with the Management, external and internal auditors

In all the PSUs the adequacy of the internal control system was reviewed by the Audit Committee from time to time and the Management was advised, wherever required, to take necessary action for strengthening the internal control system. In ONGC Videsh Limited, the Audit Committee observed that the Internal Audit system required strengthening and that it was continuously watching the progress in this regard. In case of GAIL the Audit Committee had observed the following deficiencies in Internal Audit:

- Frequency of Internal Audit was inadequate;
- Internal Audit was not technically sound in the absence of technical staff in the Internal Audit Department;
- The Internal Audit system was not commensurate with the size and nature of the Company and its activities;
- Internal Audit could not obtain time bound replies from the Company.

6.5 Effective functioning of Board of Directors

One of the main pillars of Corporate Governance is a Board of Directors controlling and managing the Company in the best interests of the stakeholders. Detailed provisions have been laid down under clause 49 of the Listing Agreement for achieving this objective. An appraisal of the compliance of various provisions under this parameter was made in Audit:

6.5.1 Constitution of the Board of Directors

In all the PSUs the Board was constituted as per the requirements of Corporate Governance. The Board had an optimum combination of executive and non executive directors with not less than fifty per cent of the Board of Directors comprising non executive directors. However, in the case of KRL, out of 11 directors on the Board, only two were independent directors as against the requirement of one-third. Induction of more number of independent directors was under consideration. In no PSU was the director found to be a member in more than ten committees or acting as a Chairman of more than five committees across all Companies in which he was a director.

6.5.2 Vacancy position in the Board of Directors

The Board of Directors was generally found to be adequately staffed. Deviations were noticed, however, in respect of ONGC, BPCL, BRPL and IBP. While in ONGC during 2003-04 posts of two executive directors and two non official directors remained vacant from time to time, in respect of IBP the Director (Marketing) in IOC was holding the additional charge of the posts of Managing Director and Director (Marketing). In BPCL one post of Director was vacant. In respect of BRPL there were only nine Directors against 15 as per the Articles of Association.

6.5.3 Holding of Board Meetings

In all the PSUs the Board Meetings were being held regularly and the requisite information placed before the Board. The quality of the minutes of the Board Meetings was also found to be adequate in all the PSUs.

6.5.4 Attendance at the Board of Directors' Meetings

The attendance at the Board of Directors' Meetings was found to be adequate in all the PSUs except for the following three PSUs:

- In GAIL the attendance of non-executive directors was not regular. Similarly, the Government nominee director attended only seven out of a total of 11 meetings held.
- In IOC three to four directors did not attend eight meetings out of 14 meetings.
- In ONGC Videsh three non-executive directors did not attend the meetings regularly.
- Board of Directors of GGSR held five meetings during 2003-04. One independent director attended only one meeting and the Government nominees attended only two meetings.

6.6 Setting up of a Strategy

In all the PSUs the Board had set up a strategy for the Company which was consistent with its vision except for MRPL which had so far not prepared its 'Vision and Mission' statement stating its recent takeover by ONGC as one of the reasons. The Company was in the process of preparing the same.

6.7 Disclosure in the Annual Reports

All the PSUs were making adequate disclosures on Corporate Governance in the Annual Reports except for GGSR, which did not make a mention about Corporate Governance in its Annual report.

6.8 Conclusion

Audit found that the PSUs in the petroleum sector were generally functioning as per requirement of the Companies Act and clause 49 of the listing agreement for the achievement of the objectives of Corporate Governance.

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The April 2005