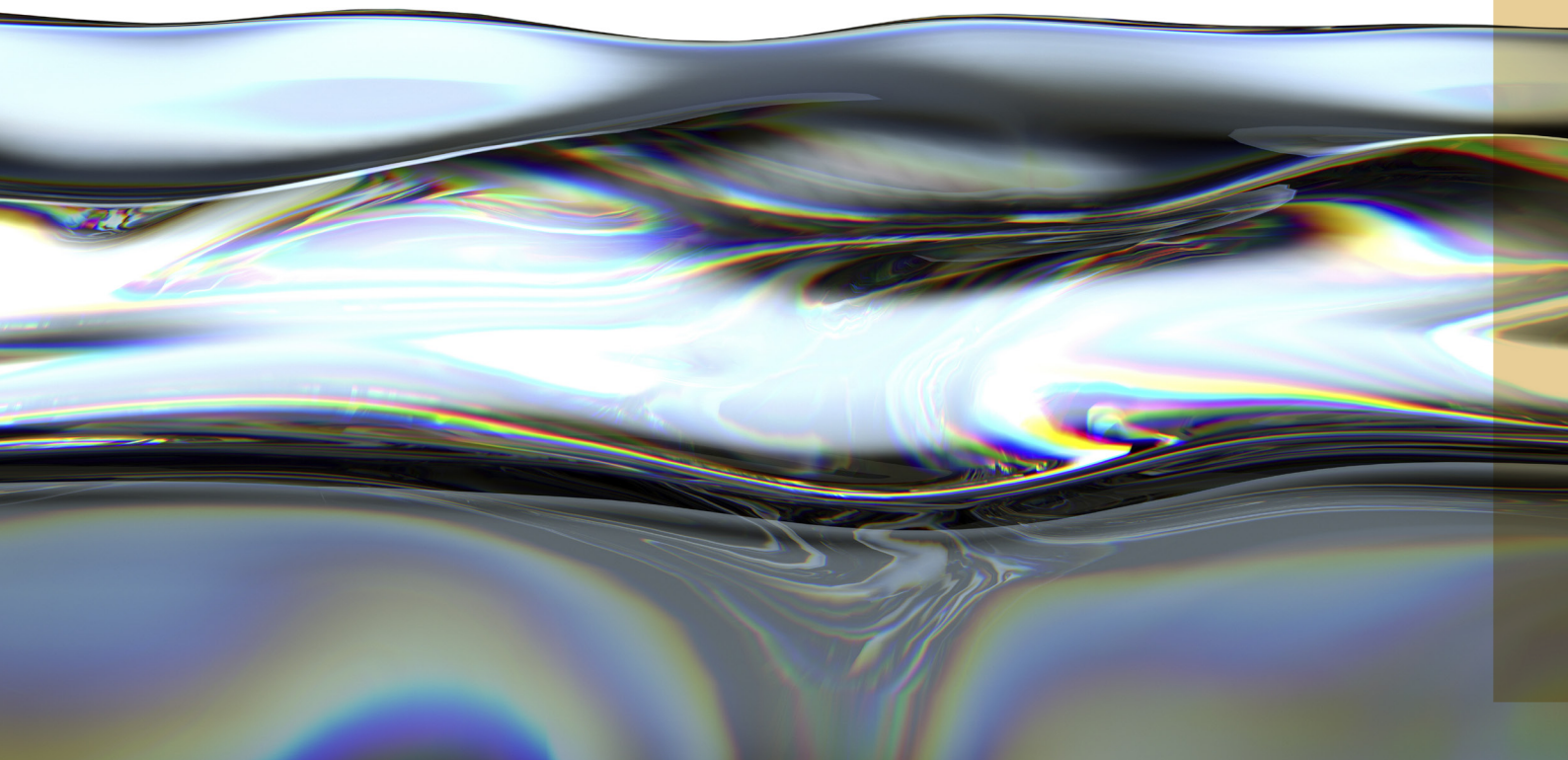


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RESOURCES, RIGHTS AND RESPONSIBILITIES:

THE ROLE OF THE PRIVATE
SECTOR IN PUBLIC
DEVELOPMENT. A VIEW BY
LORD BROWNE OF MADINGLEY



RESOURCES, RIGHTS AND RESPONSIBILITIES: THE ROLE OF THE PRIVATE SECTOR IN PUBLIC DEVELOPMENT. A VIEW BY LORD BROWNE OF MADINGLEY

Lord Browne of Madingley, former chief executive of BP and now co-head of Renewable Energy Funds at energy and power private investment firm, Riverstone, gave the inaugural annual lecture at the Energy and Natural Resources Law Institute (ENRLI) at Queen Mary University of London, which was sponsored by Clifford Chance. In this extract from his lecture he talks about the future of the energy industry and the need for companies to contribute constructively to public development, and engage with the rest of society.

I have spent much of my time outside of business working with higher education institutions. As you become more senior in business, it is a way to keep in touch with the leaders of tomorrow, and to pass on some of what you have learned.

So it is a great pleasure to be here this evening, supporting those who seek to train brilliant legal minds and to encourage excellence in the extractive industries.

When I agreed to deliver this lecture six months ago, a barrel of oil cost 110 dollars, and the world's attention was focused on the risk posed to supplies from sanctions on Russia and terrorism in the Middle East. But 110 dollars turned out to be a peak. The price of oil has subsequently fallen to less than 50 dollars, below its forty-year real average and a level last seen almost six years ago. This feels like a shock to the contemporary industry which has become accustomed to high

prices, and which was already experiencing rising costs and falling returns.

This rapid change is partly a result of higher-than-expected production in countries like Iraq and Russia, as well as long-term structural changes in energy demand. But it is also the result of the revolutionary impact of hydraulic fracturing and horizontal drilling technologies in North America. Today's environment is unlikely to be a short-term phenomenon. Technology continues to improve, making it cheaper to extract oil from existing wells, and easier to drill new ones. And the evidence suggests that stocks of crude oil and petroleum products are at a historically high level compared to the past two decades, and growing¹. It seems to me that



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¹ EIA: US stock average over past 20 years was 53.34 days of demand and on Jan 2nd there were 58.53 days of demand in stocks. Stocks have increased by 0.5 days since Oct 2014

production and demand must return to balance before we can contemplate an upturn.

I expect that some producers will have great difficulty in this environment, but the energy industry as a whole will emerge stronger than before. Costs are likely to come down, and companies will have to develop new strategies as they search for barrels which make commercial sense in a more moderately priced environment. But the long-term fortunes of the industry will depend on much more than fluctuations in the price of oil, which are important but ephemeral.

Rather, the industry's future will depend on companies' ability to contribute constructively to public development, and to engage successfully with the rest of society. That is the focus of the rest of my remarks this evening. Based on my own business experience, I want to make four points about the relationship between the energy industry and the societies in which it operates.

First, the energy industry has a decidedly mixed track record when it comes to engaging with society. Second, it has taken some important steps to learn from its mistakes. Third, these achievements must not lead to complacency. And fourth, future progress will depend on action from the leaders of tomorrow.

Let me begin with the relationship between the energy industry and the rest of society. Looking from the inside, it is sometimes easy to forget the remarkable contribution this industry makes to humanity. Companies go into far-off lands, often in the most inhospitable climates imaginable, and drill miles down through the earth, in an

attempt to reach a reservoir that they can only see through the magic of seismic imaging. If they are successful, they have to hold back thousands of pounds of pressure, get the oil or gas to the surface and transform it into a useful fuel, bringing it to a consistent standard the world over. The product is then delivered to millions of consumers around the globe, exactly when and where it is needed. For less than the cost of a loaf of bread, we can provide enough fuel to move a two-tonne car for 30 miles. For just a few pence more, we can provide enough gas to heat a home for a day. It is a remarkable feat of science, engineering and entrepreneurship.

But surveys suggest that around the world, barely half the population trust energy companies to do the right thing. In the UK, that figure drops to less than a third, and the vast majority of people think that the government fails to keep a close enough watch on the industry's activity².

In the short term, suspicion of business activity imposes hidden costs on companies and consumers. In the long term, it can pose an existential threat to an industry, and greatly reduce the contribution businesses can make society.

Suspicion of the energy industry is partly the result of technological progress. As companies gain the ability to operate in higher-risk environments such as ultra-deep water and the Arctic, people understandably become more concerned about the possibility and consequences of catastrophes. But mistrust has also come from a history of bad practice. Environmental hazards, corruption and a

² Edelman Trust Barometer 2014

disregard for local communities are rare, but in my experience, bad news stands the test of time while good news tends to be forgotten. It is up to the energy industry to repair its fractious relationship with society. And it is encouraging that there have already been steps in the right direction. This is my second point this evening.

A decade after I joined BP, the company's main operations were in the US and the UK, countries with high development standards and long liberal traditions in which the rights of citizens were protected and enshrined. But by the time I left BP, it was operating all over the world, in much less well developed countries. We operated across the globe, from Colombia to Azerbaijan, and from Angola to Indonesia. The potential benefits were clear: new markets, greater social development and growing wealth in the countries that needed it most. What was unclear was the huge impact that we would have on people in nations lacking a traditional commitment to human rights and without strong governance.

BP's experience in Angola is a good example. We were accused by NGOs of making payments to the government without demanding any accountability for where the money was spent. Against a backdrop of civil war and ethnic conflict, these payments were construed as propping up a government with an indefensible record on human rights. Whether in the form of concession payments, production royalties or signature bonuses, such payments have been common in the oil industry since its earliest day. These substantial transfers of wealth can aid

development in resource-rich nations and the potential social benefits can be substantial. But we recognised that without greater transparency, benefits were not trickling down to the ordinary citizen. That is why we decided to publish details of the payments we made to the Angolan government and to the state oil company. The Angolan President was angry, and threatened to eject BP from the country. Other oil companies did not follow our lead, and continued to hide behind confidentiality clauses in case the President made good on his threats.

It was clear that a unilateral approach was unworkable, so BP cooperated with companies, governments and NGOs to form the Extractive Industries Transparency Initiative. By providing clear guidance to both businesses and governments, and creating an open standard on which all parties can be judged, the initiative aims to increase trust on how payments are made and to improve their impact on society. Almost fifty governments and one hundred of the world's largest oil, gas and mining companies have now signed up, taking measurable steps towards greater transparency. And some of the EITI's standards are even being transposed into American, Canadian and European Union law. In a world of sometimes vague but well-meaning initiatives, the EITI is proving a practical success in rebuilding the relationship between energy companies and the societies in which they

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operate. The EITI has proved to be resilient so far, and indeed has become more influential over time.

But I am not sure that the same can be said for the industry's efforts to address another risk to its long-term sustainability: the risk posed by climate change. That brings me to my third point this evening: constant vigilance is needed, because progress can be undone as quickly as it is made. In the late 1990s, the extractive industries were at the forefront of society's response to addressing climate change. Since then, the scientific consensus around climate change has solidified. The potential costs of inaction have become clearer, and public attention has turned to the costs of mitigation and adaptation. People now want to talk about practical solutions to meet this challenge. But as public opinion has evolved, it seems that industry has been left behind, conspicuous in its absence from this contemporary debate.

Coal, oil and gas companies are yet to fully recognise the existential threat posed to their business if a more powerful consensus develops that something must be done. By ignoring

this, these companies demonstrate a failure to grasp the opportunities created by changing circumstances. New policies and regulations will be written by governments whether business likes it or not. If companies engage constructively in the regulatory process, they can help to ensure that policy makes sense on the ground, and that incentives are designed to deliver the intended aims of policy. That is why I committed BP to taking action on climate change. Our efforts won us respect, along with a seat at the negotiating table when new rules were being written. They also meant that our customers could see us planning for change, rather than seeking to preserve the status quo. And they meant that we had the upper hand in the market for talented young people with a vision for the future.

In the past, extractive industries have demonstrated an understanding of the implications of climate change. But it is time to renew and refresh that understanding, as part of a wider effort to reconnect with society. That brings me to my final point: the future. I am an optimist, and believe it is possible for the extractive industries to improve permanently their relationship with the rest of society. For



business leaders preoccupied with quarterly results, it is tempting simply to let things take their course. Trust in business ebbs and flows, and the urgent has a habit of driving out the important on the corporate agenda. But complacency will only take us so far. As the problem of climate change shows, things can go backwards as well as forwards.

Fixing a longstanding problem will not be easy, but I think there are four things business leaders can do to help. I think they apply not just to the extractive industries, but to all sectors of business. The first is to acknowledge and to study failure. It is the most effective mechanism for learning, but companies are often too reluctant to admit that things have gone wrong. The evidence suggests that the public wants authentic corporate leaders who tell the truth about their companies, regardless of how complex or unpopular it is³.

The second is to embrace strong and smart regulation. In my experience at BP and as Chairman of the shale gas company Cuadrilla, intelligent regulation shuts out free-riders, and protects an industry's reputation from the actions of a cavalier minority. The reputation of an industry is only as strong as its weakest member and regulation designed with care and collaboration can in fact reduce the long-term costs of doing business.

The third is to communicate openly with society. History shows us that people do not automatically embrace change. They have concerns about new technology - how safe it is and how disruptive

it will be to their lives. Companies rely on the public's support for their continued licence to operate, so every business needs to engage with people's fears and accept their concerns if they are to succeed.

And fourthly, leaders should examine deeply the purpose of their business activity. Every company should clearly define the contribution it makes to society, which extends beyond the merely financial. In the case of the energy industry that should not be a difficult task, but it is rarely done well. In my view, the next generation of corporate leaders will have to spend more time than ever on defining, communicating and enacting their companies' core purpose.

If business leaders are bold enough to take those steps, then the prize for both parties could be enormous. The profits from business lift whole nations out of poverty, they make philanthropy possible, and they support the next wave of transformative human progress. In my own career I am aware that when I was successful, it was the result of engaging effectively and sustainably with the wider society. When I failed it was usually because I got this wrong. Business is the engine of human progress, but it can only fulfil that role if it has a harmonious relationship with those it serves.

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³ Edelman Trust Barometer



Lord Browne of Madingley

Lord Browne of Madingley joined BP in 1966 and joined the board in 1991. He was appointed Group Chief Executive in 1995 and held that position until May 2007. He is a Partner of Riverstone Holdings LLC and a Fellow and former President of the Royal Academy of Engineering (2006-2011). He was Chairman of the Advisory Board of Apax Partners LLC from 2006 - 2007. He was a non-executive director of Goldman Sachs from 1999 to 2007, a non-executive director of Intel Corporation from 1997 - 2006, a Trustee of The British Museum from 1995-2005, a member of the Supervisory Board of DaimlerChrysler AG from 1998 - 2001 and a non-executive director of SmithKline Beecham from 1996-1999. He was knighted in 1998 and made a life peer in 2001.



Centre for Commercial Law Studies

The Energy and Natural Resources Law Institute is a London based Institute providing focus for the development of energy and natural resources law. The Institute provides practical and academic training of energy lawyers through its specialist Energy and Natural Resources Law LLM, practitioner training and events, and promotes discussion through its Forum. Within the Centre for Commercial Law Studies at Queen Mary University of London, the Institute's aim is to be an international centre of academic excellence.

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