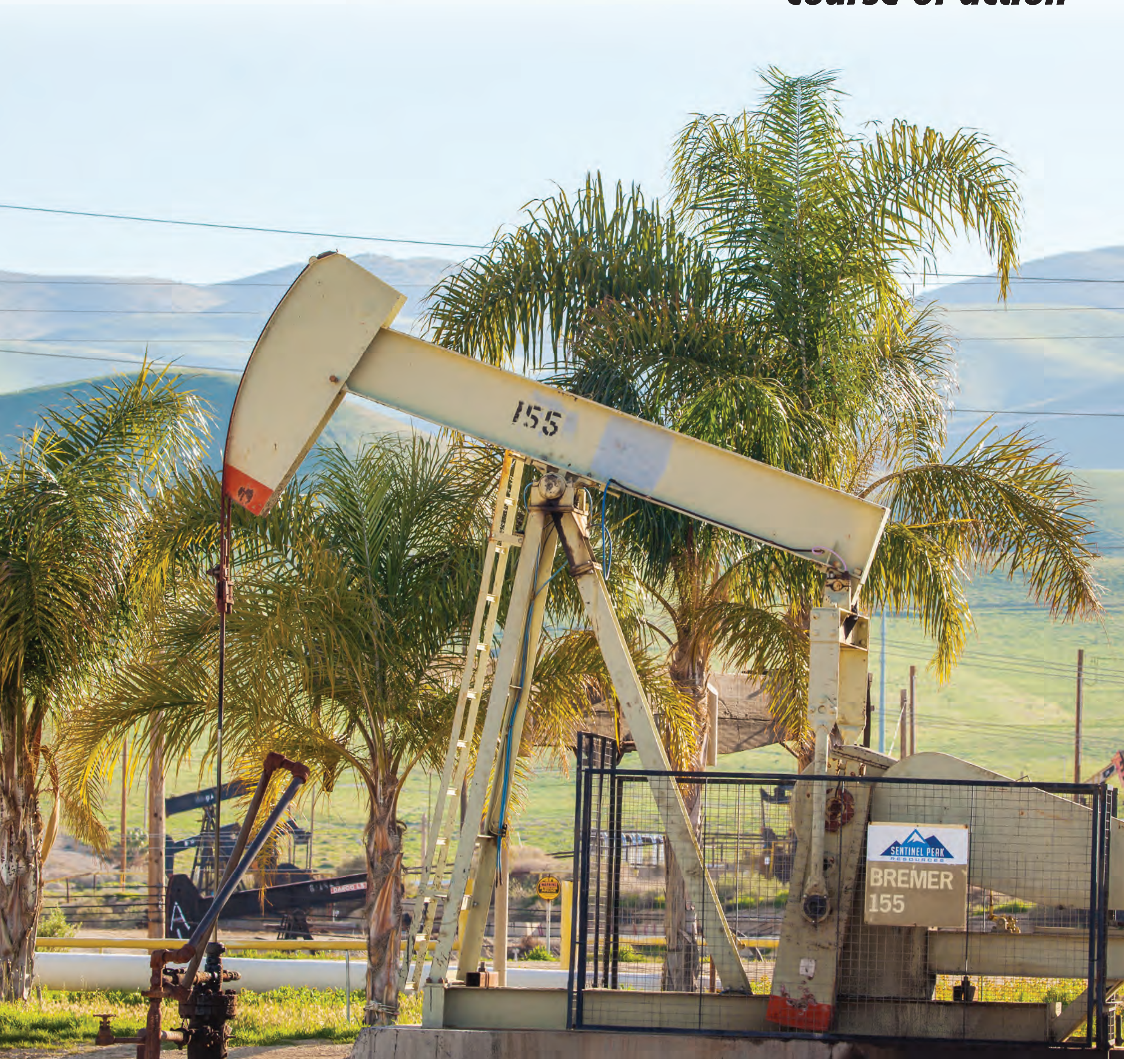
April 2022

ENERGY ESG

Demystifying the course of action



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ENERGY ESG

Demystifying the course of action

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Sentinel Peak is implementing a three-part plan to reduce its carbon footprint and achieve carbon neutrality for greenhouse-gas emissions by 2030. *(Source: Sentinel Peak Resources)*

ESG Ain't the Villain

With mounting concerns of energy security, there is a greater need for oil and gas companies to adopt a concrete ESG strategy.

By **Faiza Rizvi**
Senior Editor, ESG
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Even though Russian President Vladimir Putin has never been a big fan of U.S. shale, his recent Ukrainian invasion triggered a chain of events leading the Biden administration to ask U.S. oil and gas companies to drill more oil and gas.

As producers scramble to increase production, some industry folks are taking this chance to vilify ESG by saying "if only ESG didn't push investors away from fossil fuels," and "this is the end of the ESG era."

I beg to disagree with these statements.

ESG was never an obstacle for oil and gas, and to debunk a myth you've probably heard a lot, it's not just an "impress-the-investor scheme" either. In fact, a well-devised strategy to deal with ESG issues is a glaring opportunity, which—if used in the right way—can bring numerous benefits to the business.

Especially now, when the Biden administration has finally realized the need to ramp up domestic oil and gas production to ensure energy security, there is a greater need for producers to adopt a robust ESG strategy. This includes attracting new types of investors and promoting long-term financial outcomes as well as focusing on responsible production by promoting sustainability and slashing emissions.

Let's face it, addressing climate change remains a top priority for oil and gas companies, which is where the role of E in ESG comes into play.

Recently, a group of the world's top oil and gas companies, including Exxon Mobil and bp, announced the launch of a new fund of more than $1 billion to invest in new technologies focused on reducing greenhouse-gas emissions from energy use.

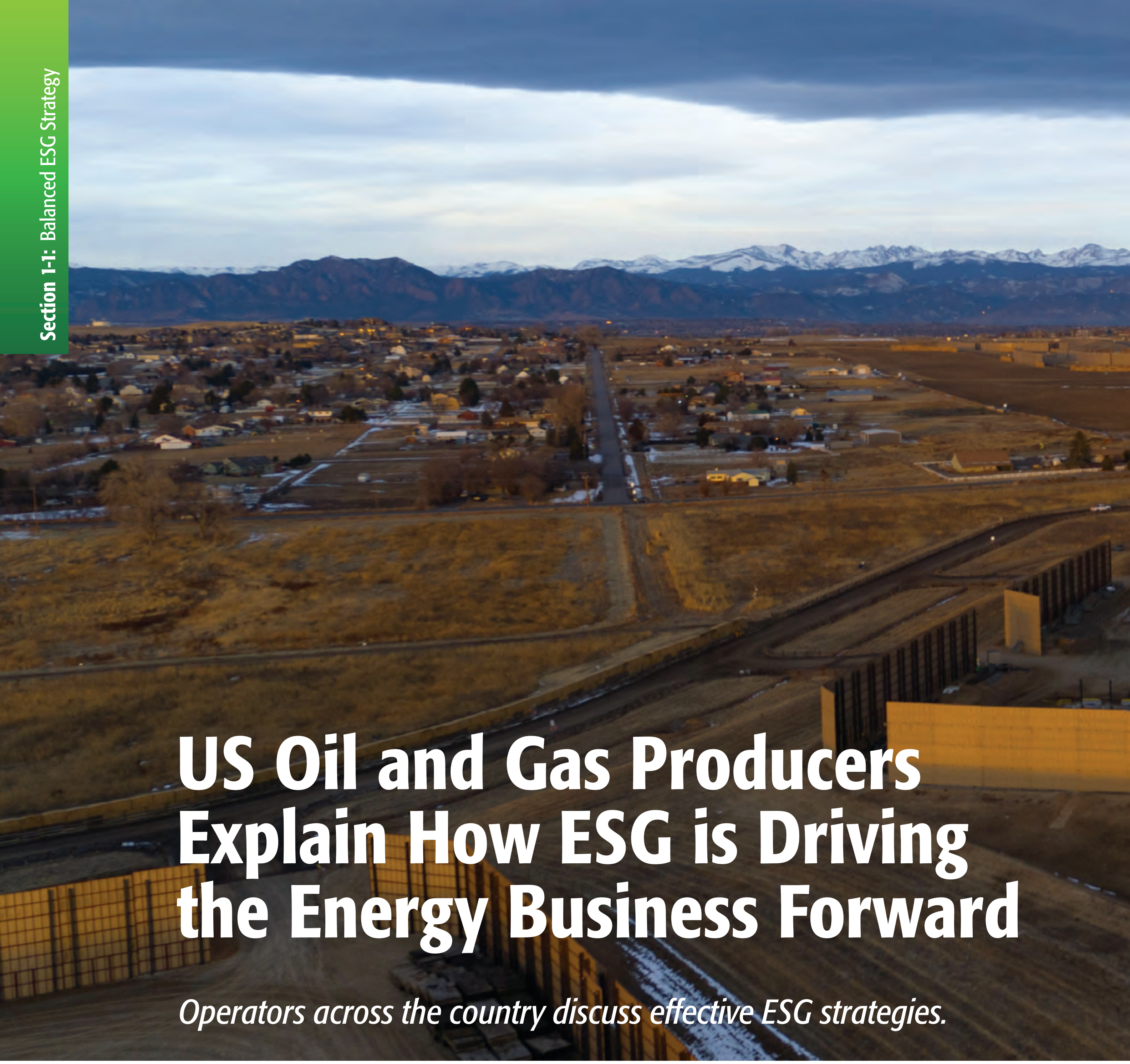
Over the past few months, I was fortunate to have some insightful conversations with leaders across the U.S. shale sector, and nearly all of them echoed the same message—a well-designed ESG strategy is helping them produce barrels responsibly, thus creating business value.

Even though reducing emissions and addressing climate change goals remain a priority for the oil and gas sector, leaders across the industry appear to be balancing the ESG equation by focusing equally, if not more, on social and governance issues. And you'll find plenty of evidence of this in Hart Energy's latest Energy ESG report, which is centered on "demystifying the course of action."

Through four strategically placed sections, the supplement takes a deep dive into the next step of ESG, which is implementation. While in the past few years, we've seen a lot on why ESG matters, companies are now taking concrete steps toward actually implementing their ESG strategies, marking a shift from ambitious planning to action.

Additionally, on April 27, Hart Energy will host its second in-person Energy ESG Conference in Dallas, where attendees will get a chance to learn from and network with top executives across the industry ranging from ESG heads of oil majors to private equity experts. Our comprehensive conference agenda sets the stage for compelling discussions on all the key topics to navigate market challenges of the energy industry by adopting a robust ESG strategy suited to different business needs amid a pressing need for energy security.

As Hart Energy continues its extensive coverage of what is being called the "megatrend of the decade," we invite you to come join us and become a part of the dialogue so that together we can ESG the right way. ■



US Oil and Gas Producers Explain How ESG is Driving the Energy Business Forward

Operators across the country discuss effective ESG strategies.

By **Faiza Rizvi**
Senior Editor, ESG

When it comes to climate action, the oil and gas industry is often blamed for not telling its side of the story and finds itself battling varying public opinions.

Over the past few years, however, the growing popularity of ESG has prompted U.S. oil and gas producers to talk publicly not just about their environmental stewardship but also societal and governance progress.

"ESG starts with an E, but definitely shouldn't end there," said Brian Cain, chief sustainability officer with Civitas Resources, adding that the oil and gas companies have a "rich history" of heavily investing in its communities.

Growing up in Houston, Cain looked up to some of the greatest philanthropists from the U.S. shale industry who have helped build the community.

"Of course, I think of George Mitchell and Rich Kinder, and I think of all those industry giants who have given back to their communities in such a meaningful and significant way. As an industry, we need to continue doing that," Cain said.

As Colorado's first carbon-neutral producer, Cain said Civitas Resources is constantly working toward a

Civitas Resources is working on electrifying its operations, moving them from Scope 1 to Scope 2, which offers numerous benefits for both the environmental and social aspects of the business. (Source: Civitas Resources)

"step change" in reducing its carbon footprint.

Last year Bonanza Creek Energy officially rebranded as Civitas Resources following Bonanza Creek's merger with Extraction Oil & Gas and subsequent acquisition of Crestone Peak Resources. Civitas is now the largest pure-play energy producer in Colorado's Denver-Julesburg Basin, operating across more than half a million net acres with an enterprise value of $4.5 billion.

Compared to its peers in the small and midcap segment, Cain noted that Civitas's ESG and carbon neutrality strategy is "much more progressive," ensuring credibility of its carbon offsets and transparency in climate disclosures, which he noted is reported in three different indices, including SASB, TCFD and AXPC formats.

So what is the company's low-carbon strategy?

"For Scope 1, first and foremost, we want to work on reducing operational emissions, and then secondarily offsetting or displacing those residual, remaining emissions that can't quite yet be operationally reduced through technology or other means," Cain explained. "We offset Scope 2 by using only green e-certified RECs [Renewable Energy Certificates], which historically we've only purchased from the Rockies sub-grid region as a best practice."

Additionally, Civitas is working on electrifying its operations, moving them from Scope 1 to Scope 2, which Cain said offers numerous benefits for both the environmental and social aspects of the business.

"As we move things from Scope 1 to Scope 2—like our drilling rigs, which we want to power on highline electricity wherever we can—we're reducing emissions by 20% to 30%, but also taking away all the backyard of generators that are creating emissions in a community and moving that emission source to the power plant," he said. "So you're taking those emissions completely out of that community or that area where you operate, which is the best thing for your landowner and for your neighbors and for the folks around it."

This also eliminates truck trips to fuel the drilling rig generators, reducing traffic and the related combustion emissions associated with the traffic, Cain added.

"Of course, I think of George Mitchell and Rich Kinder, and I think of all those industry giants who have given back to their communities in such a meaningful and significant way. As an industry, we need to continue doing that."

–**Brian Cain,**
Civitas Resources

Earlier this year, Civitas announced its commitment to voluntarily plug 42 wells that were orphaned by previous operators in Colorado. It's worth noting that the orphaned wells are unrelated to Civitas and were abandoned by their former operators and whose cleanup would otherwise be the responsibility of the state of Colorado.

Commenting on the commitment, Cain said, "We know that the state is going to get federal dollars to address the orphaned well situation, but those federal dollars won't cover all of the orphaned wells in Colorado. By plugging these wells in our operating area, we're also effectively plugging the orphaned wells that are around the populated areas of our state, around the greater Denver area and the northern Front Range of Colorado."

He continued, "From an environmental standpoint, it eliminates any emissions that could be coming from those older wells that are often in various stages of disrepair or were, frankly, irresponsibly abandoned in some cases."

This commitment not only provides environmental benefits but also checks the social aspects of ESG, Cain said.

Taking charge

When Ted Wurfel was appointed as the vice president of ESG and sustainability with Rockcliff Energy in October 2021, he was tasked with building a department that would continue to expand the company's ESG program. Within three months, Wurfel appointed two individuals to the team and set some concrete ESG goals for the company.

"One of the key ways that companies can demonstrate their commitment to ESG is to dedicate the necessary resources," Wurfel told Hart Energy.

"Rockcliff clearly understands the importance of ESG," he said, adding that the company has developed key performance indicators for 2022 focused on a variety of ESG categories including greenhouse-gas and air emissions reductions, water conservation, employee health and safety, diversity, equity and inclusion, ESG data monitoring and reporting, and cybersecurity.

While stakeholders, investors and local landowners are concerned about ESG and climate change issues and want to understand how the industry is addressing them, Wurfel believes that U.S. shale producers are "very aware" of these concerns and are taking active steps toward achieving ESG goals.

He also noted that the only way for the U.S. oil and gas industry to maintain trust and improve understanding among stakeholders is to be open and transparent about their ESG journey, which involves reporting of metrics, benchmarking with peers and continuous improvement.

The Houston-based company keeps four rigs and two frac crews busy exploiting 156,000 net acres in the Haynesville where the company has identified more than 1,000 future well sites.

To ensure responsible production across its Haynesville development, the natural gas producer has partnered with Project Canary to deploy an active emissions monitoring system at well pads. Denver-based Project Canary has developed a stringent well-by-well system of monitors that monitors methane emissions and standards of natural gas drillers.

Wurfel explained that by the end of March 2022, active emissions monitoring will be in place for all of Rockcliff's Haynesville wells, which represents 95% of Rockcliff's natural gas production, allowing them to monitor facility emissions, set alarms for operations that are outside the normal operating range and provide data to track and trend emissions over time.

Last year Rockcliff hit several ESG milestones, Wurfel said.

"On our completions side, we reduced diesel fuel use by 40% by converting to biofuel engines, and on our drilling side, all four rigs are running biofuel engines," he added.

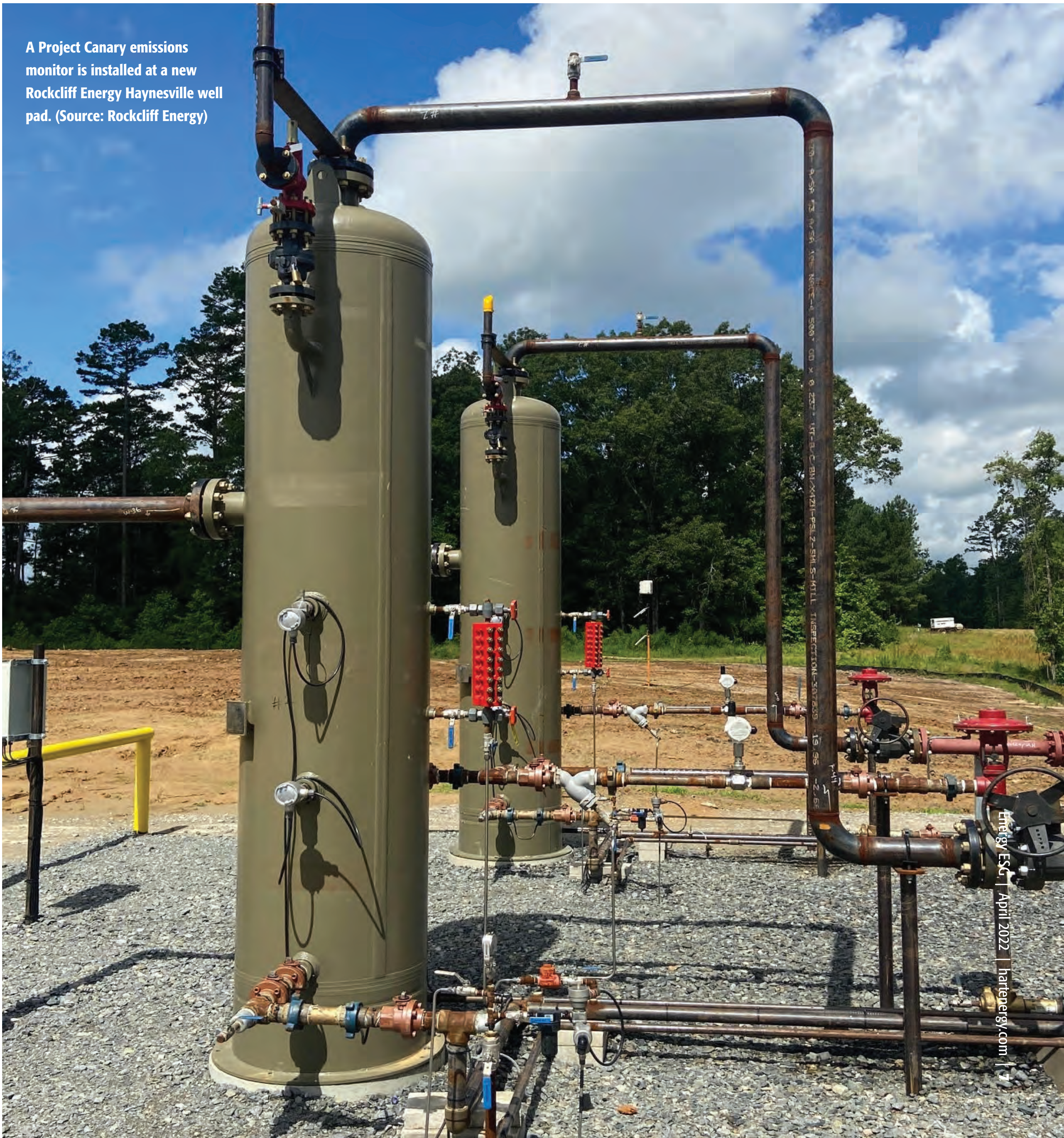
Additionally, since the company transports 97% of its produced and flowback water by pipeline, it has reduced the annual truck traffic by roughly 180,000 truckloads or about 3.5 million miles per year.

'Transformed the industry'

With more than $15 million of investments in tackling methane emissions

“One of the key ways that companies can demonstrate their commitment to ESG is to dedicate the necessary resources.”

–Ted Wurfel,
Rockcliff Energy



A Project Canary emissions monitor is installed at a new Rockcliff Energy Haynesville well pad. (Source: Rockcliff Energy)

and another $2 million set aside per year for community outreach programs, Diversified Energy CEO and founder Rusty Hutson, Jr. is certain his company is ahead of the curve in its ESG efforts.

He strongly believes that ESG has transformed the U.S. oil and gas industry and is going to impact every aspect of the business moving forward.

"If you want access to capital availability, you need to have a plan in place and show [ESG] progress," Hutson said.

Established in 2001, Alabama-based Diversified has acquired tens of thousands of mature wells from the region's biggest shale companies, beating Exxon Mobil to become the largest well owner in the country. The company operates about 69,000 oil and gas wells mainly in the Appalachian region with a heavy focus on natural gas production.

"If not Diversified, then who?" Hutson asked. "If we are not the ones acquiring these wells and making sure we spend capital on maintenance and keeping them in production for as long as we possibly can, then who will?"

Diversified Energy utilizes solar panels to power certain devices on this unconventional natural gas-producing well pad in Pennsylvania. (Source: Diversified Energy)

Diversified Energy focuses on acquiring noncore, producing oil and gas assets and investing in them to improve operational and environmental performance, such as this eight-well unconventional pad in southwestern Pennsylvania. (Source: Diversified Energy)

"We have no tolerance for methane emissions. Period. If we find emissions, we fix them."

–Rusty Hutson, Jr., Diversified Energy

He explained that extending the productive life of existing wells lessens the need for drilling and fracking of new wells to meet the country's energy needs.

"We go and acquire wells that are typically three to five years of age," he said. "We operate the wells more efficiently and enhance production on these wells."

Doing so is a key part of Diversified's ESG strategy to keep the wells in production and provide a safe and systematic way to retire them at the end of their economic life.

Being listed on the London stock exchange, Hutson said his company has zero tolerance for emissions and calls it the "stepchild in the room."

He added, "We have no tolerance for methane emissions. Period. If we find emissions, we fix them."

Last year Diversified announced plans to deploy 500 methane emissions detection devices to its Appalachian upstream field operations team as a part of the company's broader ESG initiatives. Prior to the announcement, the company had deployed 100 devices across Appalachia and proved to be effective in identifying small emissions for trained well tenders to eliminate at little-to-no incremental cost.

The company has also partnered with Bridger Photonics, a provider of methane leak detection technology, to perform multiyear aerial scans of Diversified's natural gas production and distribution assets starting with the Appalachian region.

Skills, resources amplify ESG

Sentinel Peak Resources CEO Michael Duginski believes that his company is uniquely positioned to address climate change risks because of its vast acreage position and targeted expertise.

The private equity-backed company, focused on acquisition and development of oil and gas assets in California, operates about 94,000 acres of land, out of which the company has dedicated about 1,800 acres to conservation easements and habitat conservation plans. The company also conducts biodiversity impact assessments before operating in new areas to minimize environmental impacts of development.

Additionally, Sentinel Peak has aligned its strategic goals with localized needs, creating an affordable

Sentinel Peak is implementing a three-part plan to reduce its carbon footprint and achieve carbon neutrality for greenhouse-gas emissions by 2030. (Source: Sentinel Peak Resources)

"I don't think people understand how regulated the business is here compared to the barrels that are produced in the Middle East, South America or Russia."

–Michael Duginski, Sentinel Peak

housing development in Los Angeles at the location of a former urban drill site with potential for a second future affordable student housing project in the works at a second urban drill site location that is in the final phases of abandonment, Duginski explained.

In the 500-acre Montebello oil field, located 15 miles west of Los Angeles, Sentinel has worked to redevelop the majority of the former oil field. Construction is underway on 1,200 new housing units serving a wide array of socioeconomic needs, while also offering approximately 270 acres of permanent conservation land and more than 20 acres of new public open space including 11 acres of parks and 9.5 miles of trails.

Although California is one of the world's great oil provinces, it is known for its stringent environmental regulations and policies for fossil fuel production, making oil producers in the region more focused than ever toward ESG goals, Duginski said.

"From a regulatory and governance perspective—and this is very important—California crude is the most environmentally sensitive and regulated oil production in the world," he said. "We report to dozens of regulatory agencies, comply with Assembly and Senate bills in the state of California and submit over 600 regulatory reports per year."

Explaining the company's commitment to ESG, Duginski pointed out how Sentinel Peak is actively addressing the risks that climate change poses to the planet and to its business and has been focused on that mission since its inception in 2017.

"I don't think people understand how regulated the business is here compared to the barrels that are produced in the Middle East, South America or Russia," he said.

An honoree of Hart Energy's 2021 ESG Awards in the private E&P category, Sentinel Peak is implementing a three-part plan to reduce its carbon footprint and achieve carbon neutrality for greenhouse-gas emissions by 2030 through improved efficiencies, adopting alternative energy sources and deploying new innovative technologies.

"We're very focused on the intelligent oil field," Duginski said. "We are using machine learning and artificial intelligence to improve our efficiencies, which has reduced our emissions dramatically. We have permanently reduced almost 200,000 tonnes of CO_2 annually through these initiatives."

He went on to explain how Sentinel Peak is minimizing its water use and impact, and it has made drastic improvements to the community by becoming a net supplier of water to the state of California.

The majority of water that the company uses for its operations comes from non-potable sources, including produced water from its wells. Additionally, since the beginning of last year, Sentinel Peak is providing more freshwater than it consumes through produced water reverse osmosis and ultrafiltration treatment, a process that recycles water to benefit aquatic life and support local habitat.

Additionally, the company is working on new technology for its underground carbon capture and sequestration (CCS) project.

"We have partnered with some of the leading agencies specializing in cutting-edge technology and academics to move forward with carbon capture projects and are making significant progress," Duginski said.

Despite the progress, he noted that there remains significant opportunity for the energy industry to reduce carbon emissions.

"The oil and gas industry is uniquely positioned to help states and countries meet their CO_2 reduction goals," he said. "Think about it. We not only have the engineering, the technology and systems to capture carbon, but we also have the mineral and land resources to physically store carbon permanently underground. And we have geologists and engineers to design those systems and ensure the safety of these storage methods to make a material positive environmental impact of our own operations and consumption of energy but also for a multitude of other industries that emit carbon."

As demand for oil and gas continues to increase, Duginski stressed that policymakers should embrace the oil and gas industry as both providers of transportation fuel and other products that the world is demanding while also serving as the gateway to global carbon reduction goals through CCS. ■

VortexPrime is Changing the Face of Frac

A first-of-its-kind fracturing fleet utilizes direct-drive turbine technology, powered by natural gas.

In February, Midland-based Catalyst Energy Services unveiled its newest innovative product, VortexPrime. This first-of-its-kind fracturing fleet utilizes direct-drive turbine technology, powered by natural gas.

Catalyst is dedicated to building technology that results in a cleaner future for hydraulic fracturing as well as the communities in which they serve. VortexPrime improves safety, optimizes production, decreases footprint and reduces waste and emissions.

"Catalyst brought together experts who have innovated a clear path to a cleaner future," said Bobby Chapman, Catalyst president and CEO. "I have spent more than four decades studying and innovating pressure pumping, and developing VortexPrime, which will dramatically and literally change the frac landscape, is my proudest professional achievement."

Catalyst's top priority is fostering a commitment to safety. VortexPrime uses fewer pieces of equipment—decreasing a standard footprint from roughly 20 pumps to about eight—and automated software to reduce risk. For many pads, this can reduce a site's footprint up to 55%. The smaller fleet allows for faster setup time—in hours versus days—and the implementation of fracturing technology in tight and remote spaces that have previously presented challenges for standard fleets. Additionally, VortexPrime is self-contained; no outside power source is required.

The new fleet technology enables optimized production. VortexPrime minimizes downtime and fuel burn while idle through its unique shutdown and restart technology. This reduces up/down time to three to five minutes to get back online versus the hours it takes other technologies.

A VortexPrime fleet can reduce up to 40% of CO_2-equivalent greenhouse-gas emissions over Tier 4 frac fleets. Additionally, this technology reduces the waste stream by 25,000 gallons and more than 16,000 pounds per year.

"We strive every day to innovate products that are faster, leaner and better," said Seth Moore, Catalyst COO and co-founder. "We have an incredible team that is focused

(Source: Catalyst Energy Services)

(Source: Catalyst Energy Services)

on transforming the energy industry. VortexPrime is a testament to the depth of their knowledge and their ongoing commitment to the people, technologies and industries that work to better preserve our world's resources."

New tech developed by industry veterans

While some might say that Catalyst is a relatively new stimulation service company specializing in hydraulic fracturing treatment, having emerged on the industry scene in 2018, recent performance statistics at year-end 2021 indicate significant experience in a short period of time: more than 9,000 stages and 18,000 pumping hours completed.

The energy sector leadership that came together to form Catalyst Energy Services includes 40-year veteran Bobby Chapman and 35-year veteran Seth Moore, in addition to others, who boast years of hands-on experience in the field and with engineering and business management. They term the launch of VortexPrime as "only the beginning" of the company's focus on innovation and new technology designed and built specifically to positively impact the face of hydraulic fracturing—both in terms of lowering overall systems costs and in reducing emissions. ■

"I have spent more than four decades studying and innovating pressure pumping, and developing VortexPrime, which will dramatically and literally change the frac landscape, is my proudest professional achievement."

—**Bobby Chapman**, Catalyst Energy Services

Workforce diversity, equity and inclusion are among the areas of social focus for some companies. (Source: ded pixto/Shutterstock.com)

Capturing and Maintaining the Social License to Operate

Experts share insight on effective social strategies and how oil and gas companies can effectively tell their social impact stories.

By **Velda Addison**
Senior Editor, Digital Media

Without a model to follow, they started from scratch.

"We have kind of been building this plane while we've been flying it," said Tracee Bentley, president and CEO of the Permian Strategic Partnership (PSP).

The task ahead was monumental given the wide-ranging challenges: failing schools, crumbling roads, attracting and keeping qualified employees, soaring housing prices and getting those in need access to quality health care.

None of these areas fell in the wheelhouse of energy. Still, eight oil and gas producers came together to devise a plan to help communities where they operate in Texas and New Mexico's Permian Basin. Through partnerships, collaboration and input from member companies' employees, and community leaders and residents, needs were identified, blueprints were drafted and plans unfolded.

Three years later, the PSP has more than doubled its member companies and grown its initial member contributions of nearly $90 million to almost $950 million through collaborative investments along with state and federal funds.

"It's one of the only places I've ever seen where you have some of the

"We are less interested in projects that are Band-Aids and that will just get us through for a couple of years. We're looking at what legacy will this leave for future generations in the Permian."

–Tracee Bentley,
Permian Strategic Partnership

top competitors in an industry come together to work on the 'S' in ESG," Bentley said. "They sit down at the same table, collaborate and all come to agreement. It's pretty amazing to see."

Achievements include opening a charter school, which also works with public schools, to bolster the region's academics; investing in the Texas Tech University Health Sciences Center through a number of residency and fellowship programs with focuses in Family Medicine, Surgery and Subspecialty programs; bolstering nursing programs at Odessa College and the University of Texas Permian Basin; and securing $600 million in funding for Permian Basin roads in Texas and about $100 million for the New Mexico Department of Transportation–to name a few.

"We are less interested in projects that are Band-Aids and that will just get us through for a couple of years," Bentley said. "We're looking at what legacy will this leave for future generations in the Permian."

The PSP is one example of how companies are tackling social initiatives as the ESG movement strengthens. Some are pursuing new initiatives alone. Some are building upon programs that have been aligned with company values long before ESG was a thing. Many are sharing their progress through sustainability reports, and others are trying to figure out how best to do that.

Regardless of which strategy a company chooses to pursue, transparency, consistency and a fit-for-purpose approach is essential to effectively approaching the social aspect of ESG.

Evolving trend

Experts agree that focus on the environment has dominated as companies work to reach net-zero targets and reduce emissions, partly in response to investor demands. However, social elements are entering more conversations. In reality, environment, social and governance are connected.

"An overarching theme is developing, and a lot of this is coming from feedback we're hearing from institutional investors," said Samantha Holroyd, owner of Golden Advisory Service. "That really is to be a little bit more constructive in the approach and specifically think about the fact that 'G' should be leading. Governance should lead anything that an organization is doing around 'E' and 'S,' and if the 'G' is right, shall we say, then the 'E' and the 'S' will follow suit."

The result has been more near-term effort on disclosure regarding social initiatives–at least for the companies Holroyd advises. Companies are thinking about which critical statistics they should capture and what they need to do to measure better in preparation for public disclosure, she said.

"The goal is really about integration more than balance," Zoe Thompson, principal and social strategy leader with KPMG, said on ESG. "There is a social element to the environmental, and all of ESG should really relate to the business strategy and not be seen as a standalone or a built-on."

While many oil and gas companies are taking a more philanthropic approach regarding activities in communities, other industries are beginning to integrate how social initiatives can support business strategies while also making environmental ambitions more effective, Thompson said.

Much thought is also going into how to decarbonize while minimizing the negative impact of communities and providing opportunity for growth, added Casey Herman, PwC's U.S. ESG leader.

"Climate change impacts people, and these decisions impact communities," Herman said, pointing out how some impoverished parts of the world may be affected by climate change more than others. "So mitigating those impacts is a positive social impact as well."

Finding focus

The industry will say social has always been part of the oil and gas sector,

"All of ESG should really relate to the business strategy and not be seen as a standalone or a built-on."

–Zoe Thompson,
KPMG

The Permian Strategic Partnership donated $10.6 million in February to the University of Texas Permian Basin to provide scholarships for students studying nursing or pre-health. (Source: University of Texas Permian Basin)

given its attention to workplace safety, job creation and investing in communities in areas such as education or infrastructure.

When it comes to choosing where to put company resources, there is no one area in particular that creates more value with high social impact than others. Several factors are at play. Key is understanding the company's mission, examining what is happening inside the company and the community, addressing deficiencies, setting targets, tracking progress and sharing results, according to experts.

"The short answer is to focus on those areas that connect your business, either by impacting your employees, impacting your customers or mitigating your risk," Thompson said. "Understand what audience you are trying to address. Investors are one of them. There's also regulatory matters, and there's also the general public."

Three primary areas to examine when looking at areas of risk or opportunity include assessing how the company operates today, reviewing how it plans to operate in the future, and identifying what tools it needs to get there and to execute the plan.

A few questions she suggested companies ask are: "What are the social programs that support your business strategy? How do your programs fulfill your mission as an organization?"

Different companies will integrate social initiatives in different ways, Holroyd added. Some may focus on educational programs to help children living in low-income neighborhoods. Another company may choose diversity as the flag to fly, she said, noting its efforts may be centered on diversity in employee recruitment, retention and contractors.

Social initiatives are "fit-for-purpose for your business, aligned with the culture of your organization," Holroyd said.

The PSP decided which areas to focus on by getting input from its member companies, which include Apache, bpx, Chevron, Coterra, ConocoPhillips, Devon, Diamondback, Endeavor, EOG, Halliburton, Occidental, Ovintiv, Pioneer Natural Resources, Plains All American, Schlumberger and Exxon Mobil subsidiary XTO Energy, as well as conducting research and collecting data in the Permian Basin.

The goal was to pursue initiatives where companies could "move the needle," Bentley said. "We can't focus on everything for fear that then very little would get done."

Feedback indicated needs in education, health care, roads and infrastructure, workforce development and, at the time, affordable housing. The PSP has since made behavioral health services a top priority, given the toll the coronavirus pandemic has had on the community. In 2021 PSP helped bring Permian Basin Counseling and Guidance to West Texas and southeast New Mexico and bring in counselors to staff the new offices.

"We've already heard story upon story about how having resources in a place where there once wasn't has literally saved lives," Bentley said. "The PSP stepped up to answer the call in the wake of our behavioral health crisis during COVID-19."

Measuring success

Hearing directly from people impacted gives insight on whether initiatives make a difference. For the PSP, tracking progress on initiatives also involves having quarterly meetings, including with partners and grantees, to determine whether targets are being reached and whether adjustments are needed.

Performance metrics companies can use to measure their societal impacts vary and are wide-ranging, depending on the area of focus.

"Companies need to [first] define what is important to them and their stakeholders," Herman said. "That includes having conversations with your investors, with your employees, with all of your relevant stakeholders."

After narrowing those down, understand which ones are the most important for the company and why. Herman continued, “Then the question is ‘Can I gather that data and how can I report that data in a transparent and accurate way?’”

There are several ratings tools companies can use to examine their social strategies.

These include the MSCI ESG rating, which is used to measure “a company’s resilience to long-term industry material environmental, social and governance risks.” Under the social pillar, MSCI themes include human capital (labor management, health and safety, human capital development and supply chain labor standards); product liability (including product safety and quality, privacy and data security, health and demographic risks); stakeholder opposition and social opportunities (including access to communications, finance and health care). Scores in each of these areas along with those in the environment and governance areas are compared to a company’s peers.

“There’s some aspects that are very quantifiable,” Herman said, pointing out safety records for both employees and community incidents as examples. “Product safety/quality is another area, and certainly within the human capital side, there is a growing trend to talk about and disclose quantitative factors about racial diversity, gender diversity, age diversity. … There’s plenty of data that’s being generated.”

However, getting data to help quantify, for example, the racial diversity of a company’s workforce can be challenging for some.

“Different countries around the world have different regulations about what you can even ask your employees in terms of self-identification,” Herman said. “So while it sounds easy, it’s not necessarily so easy, and it takes some investment in technology to make sure you can accumulate the right data and report it in a way that is accurate.”

With the MSCI ratings, each ESG category and subcategory carries a different weight in a company’s overall rating, depending on the subsector. With E&Ps, for example, environmental and governance issues are weighted heavier with respective percentages of about 42% and 33%, compared to about 24% for social. For refining and marketing, it’s 16.7% for social, 37% for governance and 45% for environmental.

Experts agree that the focus on the environment is justifiable given global emissions reductions goals.

“But certainly, in my conversations with investors, with stakeholders, with board members over the last six months, I think social is getting much more attention, and I think that trend is going to continue to grow,” Herman said.

Holroyd added that initiatives must

be aligned with the business and centered on something the company can control.

"We have to be flexible in these early days around what metrics and statistics are going to be used to define our social impacts and, more importantly, used to define the value proposition of our social impacts," she said.

Performance metrics used by companies are still very much focused on activities such as how many people were reached or how many services were delivered, Thompson said.

"Looking at the long-term impact is a little bit hard," she added. Again, the question is: 'Are your social programs focused on your business metrics or are they focused on activities that may be affecting the communities that aren't actually tied to your strategy?'"

The most successful companies, she said, don't look at social initiatives as a "bolt-on" to their operations. It's built into their culture. She said social programs are ways to execute their business vision.

"Social is getting much more attention, and I think that trend is going to continue to grow."

–**Casey Herman,**
PwC

Making an impact

The social story can impact the business:

- Investors want to know the risks;
- Potential employees want to work for companies with shared values and inclusive work environments that support diversity; and
- Ethical supply chains are desired.

"What they [companies] have to gain are an increased investment, reduced risk and an engaged employee base," Thompson said.

It is difficult to determine how companies' social efforts are factored into their attractiveness when it comes to valuations or, say, being a potential partner or M&A target. But there are clearly strong oil and gas players with winning ESG strategies, Holroyd said.

"The ESG strategy of an organization could become a hot topic in the boardroom when there is a discussion of an M&A target," she added. "While it may not generate in today's world a specific target for an opportunity to merge or to acquire, I do think it could be a factor in walking away from the transaction if there are poor historical statistics, lack of disclosure, anything in the history of the company or the company is lagging in terms of their ability to capture how their organization measures up on [ESG]."

Maintaining a social license to operate goes back to defining what's important to stakeholders and then consistently and transparently telling that story, Herman added. "When you cherry pick and just disclose the good stuff, people see it," he said.

Companies must also have confidence in their data, utilizing technology with built-in internal controls, and frequently engage with communities and people to understand concerns, Herman said. Having empathy, understanding issues and productively working toward solutions employees can go a long way.

Thompson advises companies to start social strategies by identifying who they are trying to reach and why, have internal conversations and determine how it's crucial to the business—"not because it makes you look good but because it helps you reach your employees or your customers or the communities that you serve."

The investment community is telling oil and gas companies to share their stories, added Holroyd, noting investors and the community will determine whether it's a good story or not.

"We actually have a good story to tell," Holroyd said. While there is always room for improvement, she said the companies she works with have great stories to tell but have never historically thought about sharing their stories.

She encouraged companies to start documenting where they are today. "If you don't measure it, you can't set a goal around it," she said. "Add it to your business process and start measuring it; be prepared to then start talking about those statistics. And once you disclose those, you can then start making future targets around

"We have to be flexible in these early days around what metrics and statistics are going to be used to define our social impacts and, more importantly, used to define the value proposition of our social impacts."

–**Samantha Holroyd,**
Golden Advisory Service

improving those specific statistics."

Companies can do amazing things individually, but much more can be accomplished by working together and thinking outside of the box, Bentley added.

"When it comes to building schools and hospitals and getting new road projects, those things are only going to happen when you work collectively and not individually," she said. "The sky really is the limit when you get a group like this together. And yes, some small things are important along the way, but think big." ■

Pictured Right:
Performance metrics companies can use to measure their societal impacts vary and are wide-ranging, depending on the area of focus. (Source: LEDOMSTOCK/ Shutterstock.com)

Why Building an ESG-effective Boardroom is Vital to Success

Governance, which is an often-overlooked aspect of ESG, is the most important of the trifecta.

By **Emily Easley**
NOVUS Energy Advisors

Early in my career, I had the opportunity to participate in our organization's board of directors meetings, which comprised 12 members from the electric utility and solar energy industries. This was during the 2000s when solar penetration into the market had started to disrupt the electric-power utility model, with customers now requesting changes to the way they procured power.

As a young associate, it was a fascinating time to see how the various members of the board navigated through what were often contentious and passionate debates. Our board was not just diverse by gender and race, but also by perspective—an often overlooked component of diversity—that surely sprang from differences in geography and plain ol' technical know-how. After all, the experience of an executive from a regulated electric investor-owned utility is very different from one whose career has been spent in solar power.

These diverse perspectives had a meaningful impact on the company's bottom line, with exponential growth occurring year after year. The discussions might have been fiery, but the results spoke for themselves. Diversity in perspective—in thought and experience—worked.

I'm reminded often about something a mentor once told me. "It takes a team," he said. "A contributing, involved board and an exemplary executive management team." No one on a team does the exact same thing as anyone else. Likewise, boards should be made up of members whose perspective and purpose varies greatly.

As ESG has become more mainstream, the "G," which stands for governance, is often the area we focus on the least. Governance is seen as boring, mechanical and something that is beneath the great big ideas behind environmental activism and social change. But, I argue, the G is the most important of the trifecta.

More recently I held a board position for a small startup in the clean energy business. While smaller, our board consisted of members from California, Colorado, Texas and Virginia, and it contained a wide range in experience in oil and gas businesses and renewables. The executive management team was young, which meant that the board had to be actively engaged to keep the operation running. In a word, governance was needed. Good governance.

In June 2021, SEC Commissioner Allison Herren Lee specifically called on companies to "consider ways to enhance the ESG competence of their boards." This included efforts to integrate ESG considerations into their nominating processes to recruit directors that would bring ESG expertise to the board, training and education efforts to enhance board members' expertise on ESG matters, and considering engagement with outside experts to provide advice and guidance to boards.

While difficult to quantify the exact relationship between diversity and

Companies that do not disclose details of their supervision of ESG risks and opportunities have the lowest ESG scores. (Source: Sharomka/Shutterstock.com)

performance, companies with standalone ESG committees at the board level or below-board committees surpass ESG scores compared to full board ESG oversight. Companies that do not disclose details of their supervision of ESG risks and opportunities have the lowest ESG scores.

Corporate governance is a component of ESG with a long history of SEC regulation, including major expansions of governance and related disclosure requirements stemming from the Sarbanes-Oxley Act of 2002 and the Dodd-Frank Act of 2010. New SEC disclosure rules may be coming soon, though, that address human capital concerns, which, some may argue, don't fall directly within those objectives.

Initial SEC proposals regarding new ESG disclosure requirements were expected in late 2021, but such a rule is now expected to be released to the public some time in 2022. Further, because any such rule proposal would need to undergo a period of public comment, it is likely that actual reporting requirements under the new rules would not take effect until 2023.

With institutional investors starting to incorporate diversity thresholds into their proxy voting policies and anticipating SEC rulemaking related to board diversity disclosures, companies proactively clarifying how environmental and social matters are governed by the entire board or expanded committees might also include key executive appointments such as chief sustainability or diversity officers as well as new management-level ESG steering committees.

What seems clear, however, is that it is not a matter of if the SEC will issue new ESG disclosure rules, but rather when it will happen and what the rules will be. The prudent thing for in-house counsel to do is begin preparing for ESG disclosure metrics now. ■

About the author: *Emily Easley is CEO of NOVUS Energy Advisors, based in McLean, Va. She is also a 2021 honoree of Oil and Gas Investor's Forty Under 40 program.*

If companies don't proactively manage and disclose key information along with financials, they can face reputational, investment and other consequences. (Source: Prostock-studio/Shutterstock.com)

How to Maneuver the ESG Standards and Ratings Qua–ire

With no universal framework for ESG reporting, find out how companies can proactively manage and disclose key information.

By **Greg Englert**, *Weaver*

When the subject of ESG reporting comes up, you're likely to encounter some head scratching or even downright confusion. ESG reporting has entered the mainstream over the past several years, but even companies that want to participate have questions.

For now, public companies aren't required to provide ESG reports along with their financials, but it's only a matter of time before SEC-registered companies will need to comply with some level of reporting or disclosure requirements related to their sustainability practices. While the impact will be felt first by public companies, private funds and private companies will likely follow. ESG disclosures and underlying data will be under a microscope, and complete and accurate data will be critical and essential.

But it is not always easy to understand what businesses are being asked to do and report. What do shareholders, institutional investors and customers expect? And how are the most successful companies responding?

To answer these questions, it's helpful to understand the ESG landscape as it is now and what to expect over the next few years.

The foundation: ESG frameworks

ESG reporting is being driven by nearly 20 organizations that have developed frameworks for what needs to be reported. The evolution of ESG is at a point where multiple players are still competing to become the reporting standard. However, this may change over the next several years as key alliances begin to emerge. A long-awaited rationalization of the many ESG reporting standard setters began in 2021.

One recent development that has made headlines is the formation of the International Sustainability Standards Board (ISSB) by the IFRS Foundation. Drawing upon the successful adoption of IFRS accounting standards on a global scale, the foundation is aiming to replicate similar adoption of sustainability disclosures for the financial markets.

Additionally, the Sustainability Accounting Standards Board (SASB) completed its merger with the International Integrated Reporting Council to form the Value Reporting Foundation (VRF). Plus, the IFRS Foundation has persuaded the VRF to join its sustainability initiative alongside the formation of the ISSB.

While framework alliances are becoming more frequent, there is still no one framework that has been universally adopted for ESG reporting. Six frameworks have emerged as the most widely adopted with the Global Reporting Initiative (GRI) Standards framework receiving widespread adoption among oil and gas companies. SASB and the Task Force on Climate-related Financial Disclosures (TCFD) adoption also has increased over the last 24 months across the energy sector.

Six Major ESG Frameworks

GRI

- Includes standards across environmental, social and economic factors, which ideally are used together to prepare sustainability reports focused on material topics
- Widely considered to be the broadest and most deeply researched framework
- GRI standards identify and describe how a company's "economic, environmental and social impacts" contribute toward sustainable development. For GRI, "material" matters are not necessarily limited to those which have a financial impact, but also include those that may become financially material over time

SASB

- Includes more than 70 standards that measure how sustainability issues affect the company and its financial performance. Includes disclosure topics, associated accounting metrics and technical protocols, and activity metrics for each covered industry
- Designed to assist businesses around the world identify, manage and report on sustainability topics that matter most to their investors
- SASB's conceptual framework contains industry-specific standards focusing on ESG matters most likely to affect a company's financial condition, operating performance and risk profile. For SASB, "material" matters are those which have a financial impact

TCFD

- Climate-related disclosure framework chaired by Michael Bloomberg
- Disclosure recommendations are structured around four thematic areas that represent core elements of how organizations operate: governance, strategy, risk management, and metrics and targets. These thematic areas are intended to interlink and inform each other

Integrated Reporting Framework

- Made up of six sources of capital: financial, manufactured, human, social and relationship, intellectual and natural. Includes guiding principles and practical content elements for reporting
- Urges companies to issue "concise" integrated reports (combining traditional, annual financial with ESG data) that detail "… the creation of value in the short, medium and long term."

CDP

- Focuses almost exclusively on climate reporting, energy strategy and climate change
- At the request of their investors, purchasers and city stakeholders, CDP supports companies, cities, states and regions in measuring and managing their risks and opportunities on climate change, water security and deforestation

Sustainable Development Goals

- Made up of 17 goals that address poverty, inequality, climate change, environmental degradation, peace and justice
- Asks companies to publicly endorse and operationally integrate a 10-point policy, covering human rights, labor standards, environmental actions and anti-corruption

Role of ratings organizations

Ratings organizations gather company ESG data either through direct surveys or through publicly available disclosures. Using a defined ratings criteria and application of qualitative and quantitative scoring, a company's ESG score is assigned based on their view of a company's risk exposure versus their industry peers. These scores are made available to the investment community as part of benchmarks and other ESG ratings data.

Some of the leading players include Sustainalytics, S&P Global and ISS (Institutional Shareholder Services). Much like ESG reporting itself, the methodologies employed by these ratings agencies are not consistently aligned with any particular ESG disclosure framework.

ESG in oil and gas

For oil and gas companies, the "E" in ESG will be one of the major areas of focus in preparing accurate reports, regardless of the framework used. However, the pandemic has heightened the focus on the "S" as investors and the public focus on how employers respond to issues like workplace safety, pay equity and other related topics. And the "G" is fundamentally important to overall operations.

While ESG reporting as a whole is

Levels of Engagement among Companies in the Oil and Gas Industry

Limited response	Reporting with basic program information, often limited to community support or legacy corporate responsibility
	Limited to no data
	Often do not address all ESG pillars
	Not aligned to an ESG reporting framework
	Good for tone but lack of data can be problematic in meeting investor expectations
Partially responsive	More information is provided on ESG programs
	ESG reporting framework used as a basis
	Data and information is presented but lacks assurance
	Covers all ESG pillars
More responsive	Robust ESG reporting, complete with ESG reporting framework indices
	Assurance is obtained by a third party
	Goals and targets are outlined

still gaining traction, there has been wide adoption within the oil and gas industry of sustainability reporting. According to a November 2021 study conducted by the Governance & Accountability Institute Inc., 92% of companies in the S&P 500 issue a sustainability report. The industry should continue to see that number grow, and the reporting is likely to get much better.

Getting started

It can be a challenge for companies to compile information for ESG reports, particularly when many divisions, geographies and business segments are required to gather and submit. The most practical way to start is to leverage a company's current processes and controls and begin to integrate ESG throughout internal controls, enterprise risk management, reporting and compliance.

Gaining assurance over key metrics is an easy and generally affordable way to bring further distinction and confidence to the most critical metrics. The same way that independent auditors provide assurance over financials, ESG metrics will follow suit.

SEC's role

The SEC's role is really about regulating the reporting and disclosure of ESG information, not requiring that companies produce this information or take other actions. The SEC cannot tell companies, for example, to reduce their carbon emissions.

What the SEC can provide is disclosure standards to drive transparency, consistency and support comparability for the market.

Under current SEC regulations and guidance, the disclosure of ESG issues is required only if "material"—meaning that information regarding an ESG issue is required to be disclosed only if it would be viewed as significantly impacting or altering information available for investors.

The time is now

For oil and gas companies and others in the energy business, being prepared and getting ahead of the curve will not only put them in a better position, it will help avoid future issues. If companies don't proactively manage and disclose key information along with financials, they can face reputational, investment and other consequences. Another benefit is that transparency and accountability should drive improvements in brand and perception.

The time to act on ESG reporting is now, even if it's just the beginning of the journey. ■

About the author: *Greg Englert is a partner of Risk Advisory Services at Weaver, a Texas-based national accounting firm. As the service leader for ESG reporting, he works with a variety of companies and investors to develop their ESG reporting programs. His practice has deep experience optimizing risk and compliance functions while solving internal control environment challenges.*

There are big expectations for 2022, internally and externally, for the SEC to push out ESG-related disclosure requirements. (Source: AevanStock/Shutterstock.com)

The ABCs of the SEC's ESG Reporting Requirements

As the SEC pushes new ESG-related disclosure requirements, find out how the move will impact reporting requirements.

By **Mike Blankenship** and **Eric Johnson**, *Winston & Strawn*

Over the last several years, stakeholder demand for ESG-related disclosures from U.S. public companies has exploded. During that time, a multitude of ESG disclosure frameworks, ratings systems, proxy voting policies and investor engagement priorities have been established, each with their own objectives, scopes, definitions and standards.

This generally voluntary and sometimes confusing ESG disclosure universe has frustrated both public companies and their stakeholders who are seeking consistent and comparable decision-useful data. However, in the absence of a unified ESG taxonomy with prescribed disclosure requirements, U.S. public companies and their stakeholders will continue to be frustrated.

Current SEC requirements

The U.S. Securities and Exchange Commission (SEC), as recently as 2020, chose not to address the growing call for standardized and prescribed ESG disclosure requirements instead continuing to rely on its existing principles-based disclosure regime and 2010 climate change guidance.

2010 climate change guidance

In February 2010, the SEC published an interpretive release to provide guidance to public companies about how to apply the SEC's existing general disclosure requirements to climate change matters. The 2010 guidance recommended that a public company consider disclosure related to the following matters, if material to the company based on its particular facts and circumstances:

- Impact of existing or pending climate change legislation and regulation;
- Impact of existing or pending international treaties or accords;
- Indirect consequences of climate change business trends, including increasing demand for new products or services or decreased demand for existing products or services (e.g., those producing significant greenhouse-gas [GHG] emissions); and
- Physical impacts of climate change.

Notably, the 2010 guidance did not establish any specific reporting requirements related to climate change and remains the SEC's only official guidance on climate change disclosures.

2020 human capital disclosure rules

The 2010 climate change guidance was the SEC's only significant ESG-related disclosure pronouncement for almost 10 years. In August 2020, the SEC amended its rules to require a public company to provide disclosure on the following topics, if material to an understanding of its business:

- Description of the company's human capital resources, including the number of persons employed; and
- Any human capital measures that the company uses in managing its business (e.g., measures that address the development, attraction and retention of personnel).

The 2020 human capital disclosure rules do provide some important topics of focus but are fairly thin and largely principles-based. As a result, in 2021, the breadth and depth of U.S. public company disclosure on human capital varied significantly across companies and industries.

SEC jumps into the fray

In 2021, under President Biden's administration, the SEC's approach to ESG and disclosure requirements changed dramatically.

On Feb. 24, 2021, the then acting SEC chair issued a statement directing the SEC's staff to enhance its focus on climate-related disclosures in public company filings, including reviewing the extent to which public companies were addressing the topics in the 2010 climate change guidance, and to begin working on updating that guidance.

On March 4, 2021, the SEC created the Climate and ESG Task Force in the SEC's Division of Enforcement. The new task force was charged with reviewing climate risk disclosures, including any material gaps or misstatements under the SEC's current guidance.

On March 15, 2021, the SEC requested public input from investors, companies and other market participants on climate change disclosure. The request acknowledged that investor demand for climate change disclosures has grown dramatically since the SEC's 2010 climate change guidance and the need for the SEC's reporting requirements to include material, decision-useful ESG information.

The request for public comment included 15 questions for consideration:

- Where and how climate change disclosures should be made (i.e., sustainability reports versus SEC filings);
- Types of climate risks that can actually be quantified and measured;
- Advantages and disadvantages of establishing different disclosure standards for different industries (e.g., oil and gas versus financial);
- Advantages and disadvantages of drawing on existing frameworks such as the Sustainability Accounting Standards Board and the Task Force on Climate-Related Financial Disclosures; and
- Whether climate-related disclosure requirements should be a part of a broader ESG disclosure framework.

It was now apparent the SEC was moving toward drafting new ESG-related disclosure requirements, with climate change disclosure as the initial focus. The majority of the public comments received strongly supported the creation of mandatory climate disclosure rules under a standardized disclosure framework.

As part of its effort to draft new climate change disclosure rules, the SEC started sending comment letters to public companies, including non-energy companies, about their current climate change disclosures. In September 2021, the SEC posted a sample comment letter so all companies could see the topics of interest to the SEC staff. The sample comment letter requested information on, among other things:

- Why the company provided more expansive disclosure in its sustainability report as compared to its SEC filings;
- Climate change "transition" risks (e.g., policy and regulatory changes, market trends, credit risks and technological changes), litigation risks and physical risks;
- Effect of material existing or pending climate change related legislation, regulations and treaties on the company's business, financial condition and results of operations; and
- Purchases and sales of carbon credits or offsets.

In the absence of a unified ESG taxonomy with prescribed disclosure requirements, U.S. public companies and their stakeholders will continue to be frustrated.

(Source: Viktoria Kurpas/Shutterstock.com)

In addition to the foregoing, ESG disclosures and related rulemaking considerations were a consistent theme in speeches by the SEC chair and commissioners in 2021. Plus, the SEC's regulatory agenda announcements in June and December 2021 identified the SEC rulemaking efforts in climate risk, human capital management, board diversity and other related matters as top priorities. In 2021 the SEC completely changed its approach to ESG disclosures and aggressively sought input on how best to construct a new, prescriptive ESG disclosure regime for U.S. public companies.

2022: SEC Rulemaking Expectations

There are big expectations for 2022, internally and externally, for the SEC to push out ESG-related disclosure requirements, and the SEC's efforts in 2021 have provided some insight on what to expect.

Climate change

The proposed rules regarding mandatory climate change disclosure are expected to cover both:

- Qualitative disclosure about how a company manages both climate risks and opportunities and how that impacts a company's strategy, both in the near term and the long term; and
- Quantitative disclosures, using consistent, comparable metrics (potentially with different or additional specific metrics depending on a company's industry), related to (i) GHG emissions, (ii) a company's climate-related goals and

pledges (e.g., net-zero commitments and other emissions intensity reduction commitments), (iii) the company's progress toward those goals and pledges, and (iv) the financial impact of climate change.

The proposed climate change disclosure rule was originally expected in late 2021, but according to reports, the SEC staff has struggled with a handful of issues, including whether and how some companies should disclose the broadest measure of GHG emissions known as Scope 3 emissions, and whether auditors should sign off on the climate change disclosures. The rule will almost certainly be challenged in court, and the SEC's focus on a legally defensible rule has slowed the proposal process. Because of these issues and the requirement that the proposed rule go through a public comment period, it appears any final rule on climate change disclosure will not go effective until 2023 at the earliest.

Human capital management and board diversity

The SEC should also issue proposed rules on human capital management (likely mandating disclosures about workforce diversity, turnover, training and compensation) and corporate board diversity (likely mandating enhanced disclosures about the diversity of current board members and board nominees). ■

About the authors*: Mike Blankenship is the managing partner with Winston & Strawn's Houston office. He focuses his practice on corporate finance, M&A, private equity, special purpose acquisition company (SPAC) offerings and securities law. He regularly counsels public companies on strategic transactions, capital markets offerings, and general corporate and securities law matters. Blankenship represents both issuers and underwriters in U.S. and international capital markets transactions, including IPOs and SPAC IPOs, and he advises on corporate governance and securities market regulation. In addition, he has advised numerous clients on many ESG matters, including ESG due diligence and developing and implementing long-term ESG strategies.*

Eric Johnson is a corporate partner with Winston & Strawn's Houston office. For more than 20 years, he has focused his practice on energy industry M&A, capital markets transactions, including SPACs, and public company governance matters, including ESG and energy transition issues. He is co-chair of Winston's worldwide ESG advisory team.

Editor's note: *In a 3-1 vote among deciding committee members, the SEC voted on March 21 to advance a set of proposed rules for climate-related disclosure statements for all SEC-registered companies. This article was written prior to this decision.*

Legal Side of ESG: Top Three Issues to Watch in 2022

The SEC's proposed rules and ESG-related litigation risk are among the key ESG themes impacting the regulatory and legal space of the energy sector this year.

By **Paul Davies, Nicola Higgs, Sophie Lamb QC, Ryan Maierson, Colleen Smith, Michael Green, Edward Kempson, James Bee and Anne Mainwaring**, *Latham & Watkins LLP*

Governments, regulators, non-governmental organizations, the private sector and other important stakeholders worldwide continued to emphasize ESG issues in 2021. The energy sector was no exception to this trend as companies and investors were confronted with a host of ESG issues including the transition to a net-zero economy, evolving emissions reporting requirements and a growing focus on supply chains. Given the societal importance that is now placed on ESG issues, Latham & Watkins LLP expect this growth trend to continue throughout 2022.

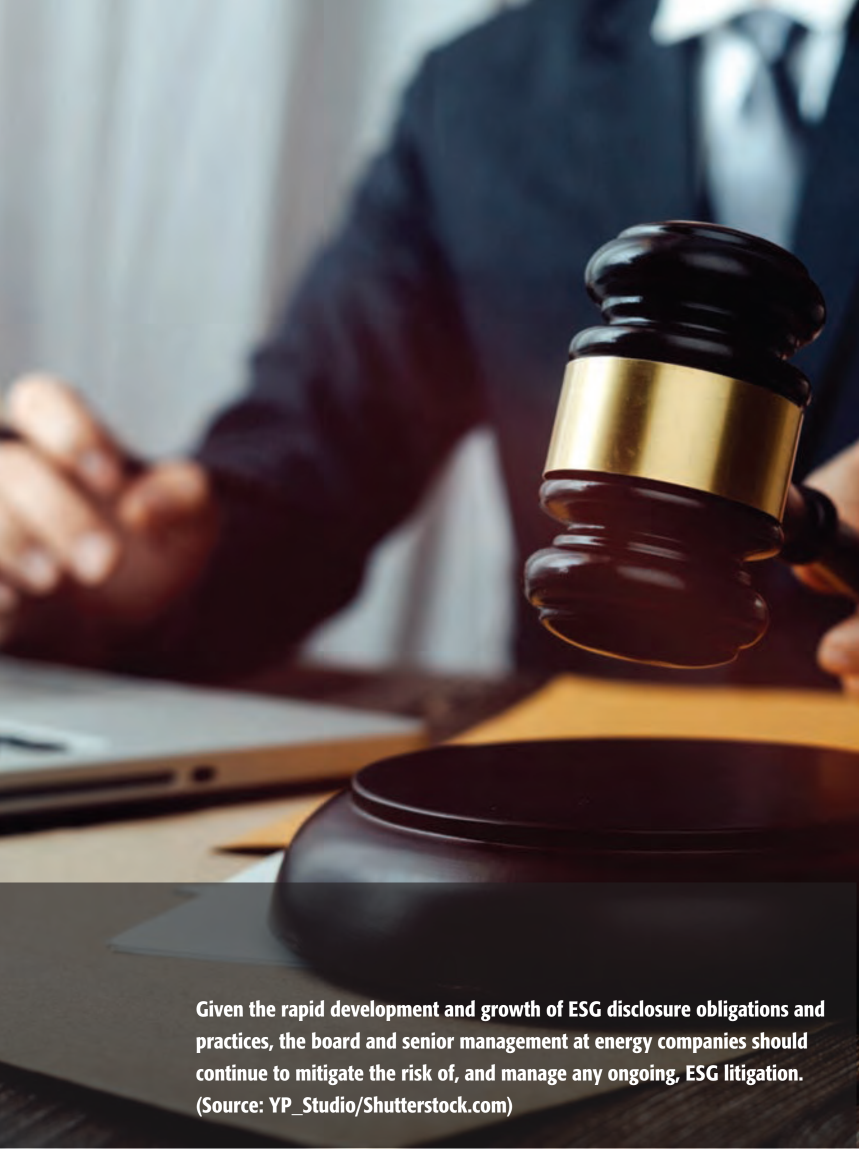
There are three ESG-related developments and trends that will likely impact the world of energy in 2022.

1. Supply chains: tracking new legal proposals

Governments and regulators are increasingly looking to require large (typically multinational) companies to take further steps to manage their value chain. The European Commission is expected to formally propose a mandatory supply chain due diligence law in early 2022.

In the U.S., on Dec. 23 2021, President Biden signed into law the Uyghur Forced Labor Prevention Act (UFLPA) in response to purported human rights abuses against Uyghurs and other ethnic minorities in the Xinjiang Uyghur Autonomous Region (XUAR).

The UFLPA represents a significant expansion of existing U.S. restrictions on items imported from, or with links



Given the rapid development and growth of ESG disclosure obligations and practices, the board and senior management at energy companies should continue to mitigate the risk of, and manage any ongoing, ESG litigation. (Source: YP_Studio/Shutterstock.com)

"While net-zero emission pledges are an important step forward, they underscore the loud, repeated and sustained calls for decision-useful metrics, That is a core purpose of the SEC's disclosure obligations."

—Caroline Crenshaw, SEC

to, the XUAR. The previous restrictions were limited to specific categories of items and items produced by specific suppliers. However, the UFLPA goes further by imposing a rebuttable presumption against imports from, or linked to, the XUAR. This effectively prohibits the import into the U.S. of such products unless the importer can clearly demonstrate that the item was produced free from forced labor or human rights abuses.

Meanwhile, Germany will continue to implement its Supply Chain Act, which will initially require German companies with more than 3,000 employees to use their best efforts to prevent human rights violations in their business operations and supply chains. The law will also require German companies to audit their direct suppliers and extend risk analyses/risk mitigation measures to indirect suppliers to the extent those companies obtain substantial knowledge of a possible human rights or environmental violation.

In addition, several cases are being pursued under the French Duty of Vigilance Act against companies that did not perform adequate diligence on their supply chains.

This regulatory shift, while placing an increased compliance burden on companies operating worldwide, is also encouraging them to consider technological solutions to perform diligence on their supply chains.

2. ESG litigation

Given the rapid development and growth of ESG disclosure obligations and practices as well as the societal focus on ESG, the board and senior management at energy companies should continue to mitigate the risk of, and manage any ongoing, ESG litigation. Latham & Watkins expects more litigation covering a broad and growing range of ESG factors.

Supply chain issues are likely to play a growing role in ESG litigation that is not related to climate change in 2022. Furthermore, greenwashing claims (from regulators, shareholders and other stakeholders) may increase as green marketing and ESG commitments become more important to consumers and investors. Climate change litigation will continue to develop in scope, as public and private entities face increased scrutiny for their role in financing high-emitting companies and/or infrastructure projects, and whether such financing aligns with their publicly stated commitments.

In addition, given the notable successes of 2021 in relation to the climate-related proxy battles, Latham & Watkins expects to see more such campaigns in 2022, with activist investors seeking to impact the ESG-related policies of high-emitting companies through shareholder action.

3. SEC: when and what to expect

The U.S. Securities and Exchange Commission (SEC) has recently placed greater emphasis on ESG and climate change issues, a trend which continued in 2021. By March 2021, the SEC had hired its first senior policy adviser for climate and ESG, created a Climate and ESG Task Force within the Division of Enforcement (the Task Force), directed the Division of Corporation Finance to enhance its focus on climate change disclosures, and requested public comments on such disclosures.

SEC Chair Gary Gensler requested that such a climate risk disclosure rule be mandated by the end of 2021. Gensler also indicated that the new rule may "learn from and be inspired by" the recommendations of the Task Force on Climate-related Financial Disclosures, although some commentators believe a proposed new rule will likely be bespoke and not use an existing framework.

The SEC has not yet released any such rule, and observers anticipate developments in early 2022. If released, such a rule could face considerable scrutiny. Notably, the public consultation saw multiple responses suggesting that climate disclosure rules will be challenged in court for being outside the SEC's statutory authority. The progress of the proposed rule and any related litigation will be closely monitored throughout 2022.

Still, the SEC will continue its work in ESG-related enforcement actions (which would not require any specific new rulemaking). In September 2021, a sample comment letter was produced on the SEC website requesting information on various ESG issues and demonstrating the type of queries that issuers could receive in relation to ESG matters. The Wall Street Journal further reported that the SEC had sent tailored comment letters to "dozens" of companies relating to their climate change disclosures.

One possible SEC focus point is combatting perceived greenwashing. Commissioner Caroline Crenshaw, on Dec. 14 2021, noted that an increasing number of companies are making public climate pledges or committing to a net-zero strategy, while providing limited or no information on how those pledges will be achieved. ■

Greenwashing is a marketing ploy in which an organization or company spends more time and money on public relations and marketing itself as more ecological and environmentally friendly than on actually minimizing its environmental impact, which deceives the public that its products, goals and policies are safe for the environment. Examples include environmental imageries or use of the color green, misleading labels, hidden trade-offs, irrelevant claims and/or misleading targets. (Source: Ivan Marc/Shutterstock.com)

A pumpjack operates in the middle of a corn field near the Denver International Airport. (Source: Arina P Habich/Shutterstock.com)

Private Equity Strongly Supports ESG Performance

What does it take to woo private equity in the age of ESG?

By **Gregory DL Morris,** *Contributing Editor*

Follow the money. In relation to private equity investment in the independent upstream sector, the classic guidance from detective stories is also the key to understanding why investors are strongly in support of ESG performance for oil and gas producers.

"Our philosophy is that good ESG contributes to good operating performance and good financial performance," said Benjamin Dell, who is a managing partner of private equity firm Kimmeridge as well as chairman and interim CEO of Civitas Resources. "You can't decouple those things. We take it very seriously that ESG performance is our license to operate. There is a natural link. ESG performance is part and parcel of operations, and we consider it an operational line item. Emissions are a line item cost no different than water disposal costs or ad-valorem taxes."

Civitas claims primacy as "Colorado's first carbon-neutral energy producer."

In that context, ESG performance is very much a factor in evaluating acquisitions.

"Net zero will become a competitive advantage. It will be a way for investors and operators to differentiate themselves."

–Benjamin Dell,
Kimmeridge and Civitas Resources

"ESG reporting is evolving," Dell said. "High-quality emissions data is difficult to document. Is it real time? Is it measured or calculated? For most people selling assets, high-quality, real-time, measured data that can be authenticated is not readily available."

ESG is also increasingly important in exit strategies.

"When we sell, we like to believe we are handing over assets that are effectively net-zero at the point of sale," Dell said. "We also think about to whom we are selling. It becomes a consideration if we are potentially selling to a company that might not be as well capitalized or committed to the same ESG standards."

Dell stressed that while Kimmeridge has not been in that situation, he is aware of others in the industry that have been.

He also noted that Kimmeridge has directionally been an acquirer of assets in recent years. Through Civitas, one of its largest investments, the company has demonstrated its ESG philosophy.

"Civitas has been consolidating the D-J [Denver-Julesburg] Basin and bringing assets under their net-zero umbrella, while also committing to plug and abandon other orphaned wells, whose cleanup would otherwise be the responsibility of the state."

From acquisition to exit and operations in between, Dell has stated categorically that "net zero will become a competitive advantage. It will be a way for investors and operators to differentiate themselves."

Looking further up the capital flow

"Our LPs generally do not have overly specific restrictions or preferences in terms of ESG performance or reporting at this point," said Doug Swanson, managing partner at EnCap Investments. "But it is clear they do want to see some type of ESG reporting feature. Our annual sustainability report provides the information that we believe is of greatest importance to our stakeholders. We have now generated two sustainability reports, and feedback thus far has been positive."

While results are far from conclusive or comprehensive, some studies have shown that companies that maintain meaningful ESG performance also yield better financial performance. Some private equity firms acknowledged an anecdotal relationship, but most suggested the linkage was axiomatic: firms that are managed soundly and operate efficiently will perform well in all areas.

"Companies that are focused on maintaining best-in-class ESG standards are also likely to be the same companies who are driven to be top quartile in every aspect of their respective business," said Swanson. "Throughout EnCap's 34-year history, we have found that partnerships with the best and most sophisticated management teams are fundamental drivers behind our success."

While current performance is important, the exit strategy is always in mind from the start of any investment.

"The ultimate acquirers of our businesses are generally large publicly traded companies," Swanson said. "When those public companies announce acquisitions, they are now not only highlighting how it is accretive from several different operational and financial metrics but are also commonly emphasizing how the acquisition affects their company-specific ESG practices. Our goal is to build companies that will be accretive to any public acquirer from an ESG standpoint."

The increase in sustainability reporting has been the biggest trend lately to establish ESG credentials.

"We believe our companies have a good story to tell," Swanson said. "So

"Companies that are focused on maintaining best-in-class ESG standards are also likely to be the same companies who are driven to be top quartile in every aspect of their respective business."

–Doug Swanson,
EnCap Investments

the onus on us is to tell this story–to choose the right metrics to report on, to report information accurately and to put reporting details in the proper context. It is also important for us to recognize that investors' need for information will change over time. We try to be flexible and to receive and incorporate feedback as we progress on our ESG journey."

More formalized but not new

There is also a case to be made that while ESG is clearly getting much attention, performance in those areas is not necessarily new.

"Our limited-partner base is made up of U.S. endowments, foundations and pension plans," said Frost W. Cochran, managing director and founding partner of Post Oak Energy Capital. "They have always done their due diligence to make sure they are investing through prudent investment managers. Over the last several years, they have wanted to better understand our policies and our portfolio company policies regarding ESG. To date, there has not been standardization around ESG reporting or performance expectations from our limited partners."

That said, Cochran added that the elements of an ESG score "have always been relevant in investment decisions based upon the institutional investor base that we represent. So

> "Many of the elements of ESG have been a part of active management for years so companies are working to formalize those procedures for measuring and reporting."

–Frost W. Cochran,
Post Oak Energy Capital

ESG considerations might be more formally identified now, but they were already part of our investment underwriting process."

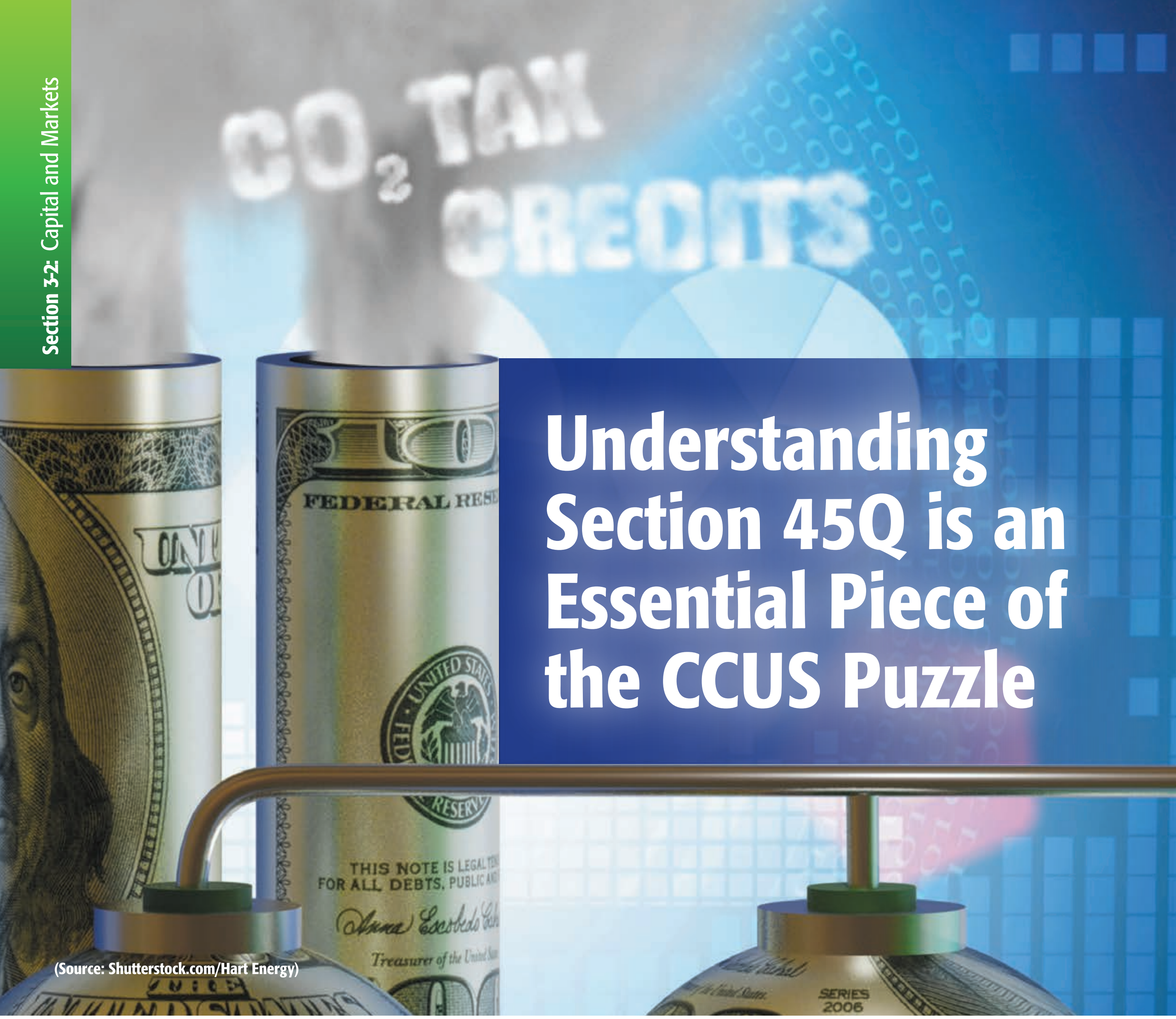
For Post Oak, ESG considerations affect entry decisions more than exit strategies.

"There are areas where we would not invest capital because the exit would be more difficult based upon the attributes of an asset," Cochran said. "We have started to see that public companies are more focused on acquiring assets that have [been] managed by portfolio companies that are top-tier operators."

Those top-tier operators are doing a better job of differentiating themselves, Cochran noted.

"Companies are putting more policies and procedures in place and beginning to benchmark against a set of key performance indicators that they can track on an annual basis," he said. "As mentioned, many of the elements of ESG have been a part of active management for years so companies are working to formalize those procedures for measuring and reporting. Most of the management teams that we invest with received extensive training at majors and [are] super independents that are safety and environmentally conscious, [and] the culture of continuous improvement is embedded in their DNA." ■

The Rifle gas field is located among the mountains of Colorado. (Source: Jake Allee/Shutterstock.com)



(Source: Shutterstock.com/Hart Energy)

Understanding Section 45Q is an Essential Piece of the CCUS Puzzle

Section 45Q tax credits can be a very effective tool for companies in the oil and gas industry that are looking to invest in and exploit the CCUS value chain.

By **Shariff Barakat** and **Matt Kapinos**, *Akin Gump*

With billions of expected investment in carbon capture, utilization and storage projects over the next decade, Section 45Q is an important tool that companies looking to invest in this space must use.

Section 45Q of the U.S. federal income tax code provides a tax credit for carbon, capture, utilization and sequestration (CCUS) of carbon. While this tax credit has been around since 2008, the credit was expanded and enhanced in 2018. Since then, a proverbial wall of capital has been inching closer to deployment in CCUS projects. The capital is flowing in from all directions; companies historically invested in hydrocarbon industries, private equity, banks, power generation and the federal government. In light of qualification for the tax credit currently requiring projects to "begin construction" by 2025 and the longer development cycles involved in bringing carbon capture projects to life, the time to start getting smart on 45Q and carbon capture generally is now.

Section 45Q provides for a tax credit per metric ton (mt) of carbon that is captured and either sequestered into a secure geologic storage site, utilized as a tertiary injectant in an enhanced oil or gas recovery project, or utilized in some other manner approved by the Departments of Treasury and Energy that produces a reduction in life-cycle greenhouse-gas emissions during the first 12 years following placement in service of the capture assets. The amount of the credit changes each year. In 2026 the credit will be at least $35/mt of carbon utilized in an EOR project, or some other Departments of Treasury and Energy approved manner, and $50/mt of carbon permanently sequestered into a secure geologic storage site.

The projects must "begin construction" as defined by the IRS before Jan. 1, 2026, which the IRS generally defines as occurring once a certain threshold of actual physical construction of a project occurs or by the owner actually incurring a certain threshold of costs. The IRS has published guidance on how projects "begin construction," and a tax professional should be consulted in qualifying a project at the onset. There are both traps for the unwary and pro-taxpayer gifts from the IRS, making expert tax advice and planning essential.

Which projects qualify?

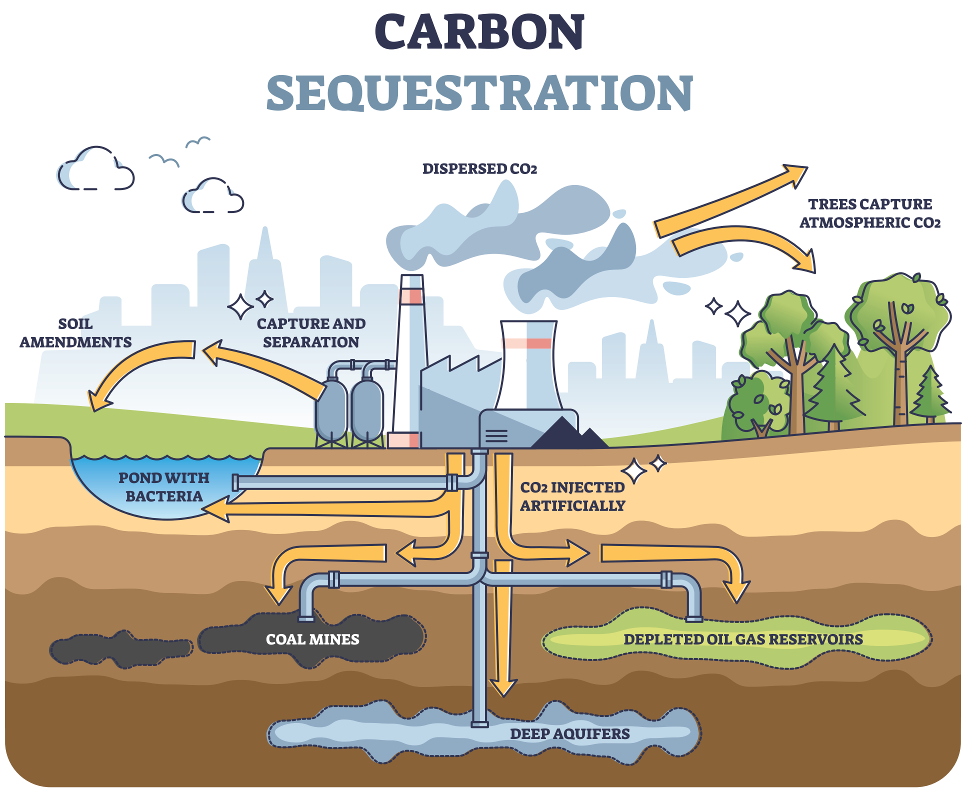
While it seems straightforward to qualify for Section 45Q tax credits, there is a bit of a catch as these projects need to be large. Section 45Q requires projects to capture a certain threshold amount of emissions to qualify for the credit at all. For example, at least 500,000 mt must be captured each year from most power plants that sell power, and at least 100,000 mt must be captured each year from almost all other types of projects. Additionally, for projects that receive approval from the Departments of Treasury and Energy for a non-EOR utilization, there is a lower 25,000-mt annual threshold for certain types of projects to qualify.

Assessing the volumetric capture potential of a project is a good first step in determining whether a proposed project can qualify for Section 45Q credits. The thresholds have proven to be a barrier to many projects qualifying for the Section 45Q credits. To overcome this barrier, one of the many adjustments that would have been made in the on-hold Build Back Better Act was to dramatically lower the annual volumetric capture thresholds for a project to qualify for the Section 45Q credits (the highest threshold after Build Back Better would have been 18,750 mt per annum; although there also would have been a new requirement to capture at least 75% of the carbon emissions in the case of a power plant that sells power). As the Build Back Better Act's prospects are uncertain, it is uncertain when (or if) the thresholds will be lowered for more projects to qualify for the Section 45Q credits.

Efficiently utilizing the tax credits

Once a project qualifies for tax credits, often the next step is figuring out how to utilize the credits most efficiently.

Looking at the minimum thresholds and credit rates, the minimum credit creation for an EOR project is $42 million (100,000 x $35 x 12 years) and for a secure geologic storage project is $60 million (100,000 x $50 x 12 years). Oftentimes, the



Pictured Above: Section 45Q of the U.S. federal income tax code provides a tax credit for CCUS of carbon. (Source: VectorMine/ Shutterstock.com)

Whether it is a knowledge of and comfort with subsurface work, ownership of an emitting asset or expertise in pipeline development, the knowledge set and infrastructure of the oil and gas industry can be and is being leveraged in the burgeoning CCUS industry.

developers of these projects do not have a sufficient tax liability to efficiently utilize these tax benefits. Other times, even if the developer does have an appetite, the funds that can be raised against those future tax benefits can be an attractive source of project capital.

In either case, enter tax equity as a capital provider. A tax equity investment is what the finance world calls an investment by a bank, financial institution or other U.S. taxpayer with a sufficient forecasted tax liability that it intends to offset by investing into a partnership with a developer to efficiently utilize the tax benefits of a project. The tax equity investor will usually become a partner in a joint venture between the developer and tax equity investor in which, in accordance with IRS guidance, the tax equity investor can be allocated 99% of the tax benefits and retain only a 5% residual interest in the project after the 12-year tax credit period.

Tax equity has existed in various forms for 50-plus years, and the major players that have dominated the solar and wind tax equity markets for the last decade are all eagerly eyeing tax equity in carbon capture projects, whether altruistically as an ESG play or as an emerging profit center for their tax equity desks.

Increased interest in carbon capture

Section 45Q tax credits can be a very effective tool for companies in the oil and gas industry that are looking to invest in and exploit the CCUS value chain. Whether it is a knowledge of and comfort with subsurface work, ownership of an emitting asset or expertise in pipeline development, the knowledge set and infrastructure of the oil and gas industry can be and is being leveraged in the burgeoning CCUS industry.

Interest from the oil and gas sector in carbon capture seems to be at an-all time high and still growing, and understanding Section 45Q is an essential piece of the puzzle and a vital tool in structuring and creating a viable and attractive CCUS project. ■

About the authors:

Akin Gump partner Shariff Barakat represents clients involved in the acquisition, development and financing of infrastructure and power generation projects, with a particular focus on tax equity financing.

Akin Gump partner Matt Kapinos guides energy and infrastructure clients through all phases of drafting and negotiating agreements for the purchase, sale, development and financing of energy and infrastructure projects.

For projects that receive approval from the Departments of Treasury and Energy for a non-EOR utilization, there is a lower 25,000-mt annual threshold for certain types of projects to qualify. (Source: JHVEPhoto/Shutterstock.com)

Leading Operators Share ESG Secrets

CNX, Devon and Laredo set environmental goals and paths for success.

By **Brian Walzel**
Senior Editor, Carbon Management

The oil and gas industry has moved well past the period of simply understanding and acknowledging the need for ESG endeavors in their operations and structure. The industry is now fully entrenched in the stages of not only implementing ESG efforts, but also setting achievable standards and establishing pathways to achieve those goals.

Whether it be to appease the sentiments of the investment community, compliance with regulations or simply pure altruism, the oil and gas industry is now at the point where ESG is a top priority rather than a box to be checked.

"You have to understand what ESG means to you as a company," said Yemi Akinkugbe, chief excellence officer with CNX. "Then you have to understand the value that it brings to you as a company, to your stakeholders and to all of the employees in your company. Once you have that solid foundation, I think it creates a very clear path for any operation, for any company, to be successful as it relates to their ESG journey."

Among the ESG leaders in the upstream operating industry have been CNX, Laredo Petroleum and Devon Energy. Each one has defined ambitious emission reductions goals to achieve over the next two decades.

Devon has set a net-zero GHG emissions reductions target for Scope 1 and Scope 2 emissions by 2050 and a goal to lower flaring intensity to .5% or lower by 2025, and eliminate routine flaring altogether by 2050.

Meanwhile, CNX aims to eliminate routine flaring by 2025 and reduce its total methane emissions as a percentage of natural gas production to less than .2% by 2025. Additionally, CNX is aiming for 12.5 $mtCO_2e$/MBOE Scope 1 greenhouse-gas (GHG) intensity by 2025. CNX has seen a 90% reduction in Scope 1 and 2 CO_2e emissions since 2011, and today operates as "net carbon negative," according to the company's 2020 Corporate Responsibility Report.

CNX's ESG targets

CNX's approach to implementing its ESG philosophy "is a reflection of our values," Akinkugbe said. "Our ESG

Laredo Petroleum has set out to achieve 12.5 mtCO2e/Mboe Scope 1 and Scope 2 intensity by 2025. (Source: Laredo Petroleum)

philosophy within CNX is tangible, impactful and local."

With its environmental aspects, Akinkugbe said CNX "continues to push the envelope" on emissions reductions.

"In our corporate responsibility report we released last year [2021], we set a target that by 2022 we want to further reduce CO_2 emissions in our Scope 1 and Scope 2 emissions by 90,000 metric tons," he said. "By the end of 2025, our goal is to have reduced Scope 1 and Scope 2 [emissions] by more than 200,000 metric tons. The big question is, how do you achieve that?"

Akinkugbe explained that the company spends about $10 million per year on methane abatement while looking for creative ways in its operations to be more efficient.

"We are reducing not just the methane emissions, but also the CO_2 signature of activity," he said. "We are reducing consumption more on the heavier hydro requirements—we're talking about different kinds of diesel and continuing to reduce [diesel usage] by looking for a much more creative way and efficient way of running our operations."

Meanwhile, CNX has invested about $30 million into the communities in which it operates in the Appalachian Basin, with plans to invest another $130 million in the next five years.

"We're looking at the health and welfare of children, the elderly and the feeble," Akinkugbe said. "We're looking at us now focusing on recidivism and criminal justice, focusing on education when it comes to water quality [as well as] technology [and] providing broadband to the localities in which we operate."

Devon's ESG objectives

Devon has established a number of environmental performance targets, with achievement goals set among the short and long term. The producer has set a net-zero GHG emissions target for Scope 1 and Scope 2 emissions by 2050, with a 50% reduction goal by 2030. Devon hopes to achieve a 65% reduction in the methane emissions intensity by 2030 and a .5% flaring intensity by 2025, completely eliminating the practice by 2030.

"When you think about net-zero 2050, that's a long time away, and you need to take steps to get there," said Garrett Jackson, Devon's vice president of ESG and EHS. "So the first step we're taking is reducing our emissions. We see a lot of focus on our GHG intensity, Scopes 1 and 2, and then also our methane intensity. Those are things we have spent a lot of time over the last several years working on, and we're continuing to try to improve in those areas."

Jackson said Devon is deploying different technologies and data to better understand its emissions, which helps the company create a "roadmap" for their employees, particularly field

CNX has outlined a seven-year financial guidance plan in line with the company's ESG principles. (Source: CNX Resources) employees, to help reach their goals along the way.

"We recognize that we're going to need advances in technology, whether that's through carbon capture or some type of offset or market-based instrument to help us ultimately get to net zero," he said.

Along with its environmental goals, Devon has placed a high priority on diversity, equity and inclusion hiring practices, ensuring that the company maintains a focus on its people, the communities in which it operates and its stakeholders.

"When you talk about having diverse backgrounds and perspectives in your employees, we want them to have equal opportunities, and we want everybody to have a fair chance and opportunity," Jackson said. " We want everybody to feel seen and heard and ultimately valued, and I think that's important for a great company culture."

Laredo's ESG focuses

Laredo Petroleum, which operates exclusively in the Permian Basin, is expecting to achieve 12.5 $mtCO_2e$/mboe Scope 1 GHG intensity, less than .20% methane emissions and zero routine flaring by 2025.

"We have a defined pathway of how we're going to achieve that 12.5 metric tons of carbon dioxide equivalent per 1,000 boes produced," said David Ferris, chief sustainability officer with Laredo. "We're going to really focus on three areas. The first is mitigating venting and flaring. The second is replacing [pneumatic] devices, and the third is electrifying portions of our field operations to eliminate or mitigate emissions from combustion."

In July 2021, Laredo completed its acquisition of Sabolo Energy. Sabolo's operators were focused in the Permian Basin's Howard County. The deal included 21,000 net acres, 100% of which was HBP. At the time of the transaction, Laredo CEO Jason Pigott said the company would be "maintaining our prior commitments to reducing greenhouse-gas intensity, methane emissions and eliminating routine flaring."

Ferris discussed the challenges of taking another company's assets and working to get it up to speed on Laredo's environmental and emissions goals.

"We are investing money to upgrade those facilities to where they are up to our standards for sustainability and environmental performance," he said. "We expect to see significant improvements on those operations as well as some of ours that needed some attention."

Although companies like Laredo, CNX and Devon are well down the path of incorporating ESG practices in their everyday operations, other companies have yet to fully embrace ESG as a priority in their own operations.

So what advice would ESG leaders offer to those just starting out their journey?

"One of the first things we talk about is understanding what your stakeholders want," Ferris said. "Who are your investors? Who are your stakeholders, and what are their top priorities? What reporting frameworks do they want? And then compare those frameworks to what you can do."

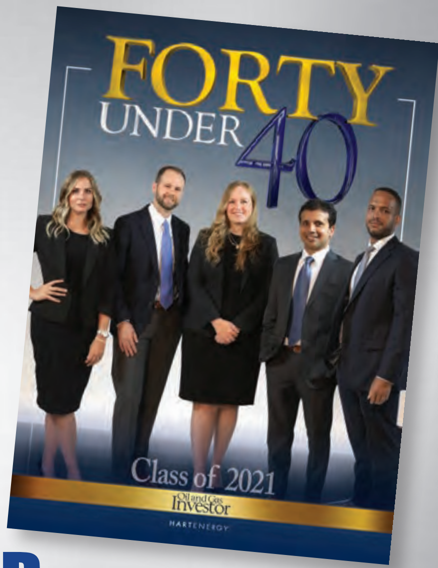
Ferris stressed understanding your own capabilities as an organization, areas of strength and, in particular, the data and expertise the company possesses.

"That's where you start, and build from there," he said. "The key is understanding where to start, getting started and then continuing to build year over year from there. It's finding the momentum, the motivation and the opportunity to get started, and it builds." ■

***Editor's note:** These interview responses were edited for clarity and meaning.*

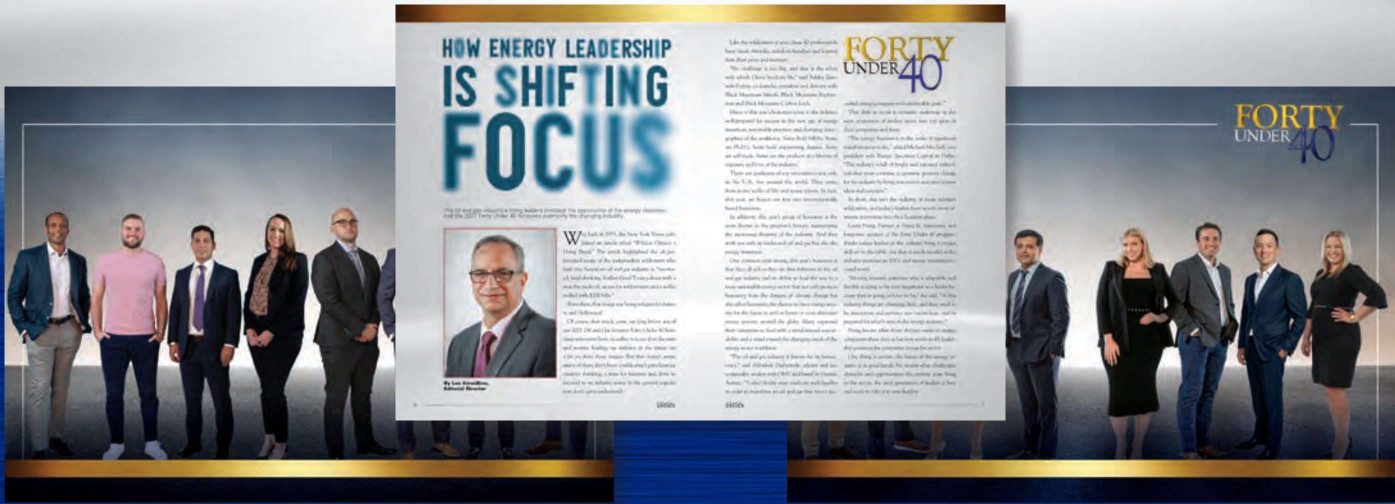
Permian-operator Laredo is expecting to achieve 12.5 $mtCO_2e$/mboe Scope 1 GHG intensity by 2025. (Source: Laredo Petroleum)

FORTY UNDER 40



We invite you to NOMINATE those that are MOVING INDUSTRY FORWARD

Oil and Gas Investor is accepting nominations for the **2022 Forty Under 40 in Energy awards**. We encourage you to nominate yourself or a colleague who exhibits entrepreneurial spirit, creative energy and intellectual skills that set them apart. Nominees can be in E&P, finance, A&D, oilfield service, or midstream. Help us honor exceptional young professionals in oil and gas.



Honorees will be profiled in a special report that ships with the November issue of *Oil and Gas Investor* and on HartEnergy.com.

Nominees should display:

- A desire to find new challenges
- Community involvement
- Leadership initiative
- Creative problem solving
- Professional excellence
- Entrepreneurial spirit

Oil and Gas Investor

Deadline for submissions is June 1, 2022

HARTENERGY


Solar panels power a Baker Hughes facility in Massa, Italy. (Source: Baker Hughes)

How is OFS Responding to the ESG Concerns of Producers?

Approaches may differ, but ultimately OFS firms' goals when it comes to balancing decarbonization with overall performance are the same.

By **Anna Kachkova,** *Contributing Editor*

The importance of ESG to the oil and gas industry continues to grow. E&P companies, in particular, are often in the spotlight because of new ESG targets, especially on the environmental side and often related to decarbonization. However, the increased focus on ESG is also playing out in the oilfield services (OFS) sector.

"Services firms face similar pressures on ESG and climate-risk concerns from investors as their upstream partners and customers, but they are slightly differently positioned," Alex Martinos, Energy Intelligence's director of energy transition research, told Hart Energy. "We see oilfield service firms as arguably being more exposed to transition pressures than other industry segments. Being acutely exposed to front-loaded, capex-intensive industry spending, OFS firms are likely to feel the squeeze from an evolution in industry priorities well before upstream/downstream segments, which could continue to profitably 'harvest' existing assets for decades to come, even if new project spending dries up."

Large and small OFS players alike are figuring out how best to respond to and anticipate producers' changing ESG concerns. Approaches may differ, but ultimately OFS firms' goals when it comes to balancing decarbonization with overall performance are the same.

"We believe there is an opportunity to streamline the reporting frameworks and agree on some basic rules, both within the oil and gas industry as well as at a macro level."

–Andres Cabada,
Halliburton

Halliburton's sustainability targets

Halliburton, one of the world's largest OFS firms along with Schlumberger and Baker Hughes, is pursuing sustainability targets including a 40% reduction in Scope 1 and 2 greenhouse-gas emissions by 2035.

"We continuously assess our targets, but we will only set targets that [are] actionable, measurable plans supported," Halliburton's director of global stewardship and sustainability, Andres Cabada, told Hart Energy. "On other ESG topics, we push ourselves to be better every year."

"We see oilfield service firms as arguably being more exposed to transition pressures than other industry segments."

–Alex Martinos,
Energy Intelligence

The company views its ESG targets and those of its customers as being complementary.

"While we have our own targets, we can help our customers achieve theirs through collaboration to implement the best solutions to their challenges," Cabada said. "Specifically, we can help reduce their carbon footprint and see opportunities to reduce their emissions beyond those generated on site by Halliburton."

The environmental component of ESG tends to dominate discussions, but Cabada cited other areas Halliburton seeks to focus on, including corporate governance, diversity, equity and inclusion, and human rights.

"We align with our customers on priorities and opportunities for collaboration in those areas," he said. "For example, we help local economies prosper by nationalizing our workforce, providing effective training and education, and engaging with local suppliers."

Halliburton sees its electric and Tier 4 dual fuel hydraulic fracturing equipment and the emission reduction it helps drive in the North American shale industry as one example of how its operations are yielding results on the ESG front.

"As a market leader, we can have an outsized positive impact on this end," Cabada said.

There are still further challenges to overcome on the ESG front, but Cabada sees them as opportunities for the industry to do better.

"We believe there is an opportunity to streamline the reporting frameworks and agree on some basic rules, both within the oil and gas industry as well as at a macro level," he said.

"We cannot achieve net-zero emissions without operationalizing sustainable business practices–across all facets of ESG."

–Allyson Book,
Baker Hughes

Baker Hughes' net-zero commitments

Baker Hughes says it is trying to lead the way in the OFS sector when it comes to ESG. This includes pursuing net-zero emissions by 2050.

"We were one of the first companies in our sector to make a net-zero carbon commitment and have defined a pathway to reduce our operational emissions," Allyson Book, Baker Hughes' vice president of energy transition, told Hart Energy. "Since then, we have actively worked to set annual performance indicators to demonstrate progress, while shoring up our data collection and reporting capabilities in this space. In 2020 we reduced our operational emissions by 15% versus prior year."

Book said Baker Hughes challenges itself to perform on a par with the most responsible companies in the world,

Pictured above and left: Evolution's electric frac fleets result in zero gallons of diesel consumed during pumping operations, reduced personnel exposure to on site hazards and a 50% smaller footprint than a conventional frac fleet. (Source: Evolution Well Services)

not necessarily just the OFS sector. She added, though, that the company also pays close attention to the goals and progress of its customers.

"One example is our recent strategic collaboration agreement with Shell, where we are providing low-carbon technology solutions to Shell in exchange for more renewable energy solutions," Book said. "In this way, we accelerate and closely support each other's net-zero carbon emissions goals."

Like Halliburton, Baker Hughes understands the importance of pursuing improvements more broadly across all areas covered by ESG.

"There is a lot of attention and coverage on the environmental component of ESG in recent times, but we cannot achieve net-zero emissions without operationalizing sustainable business practices—across all facets of ESG," Book said.

The company's approach involved embedding ESG goals into everyday actions, which Book described as "a difficult task that goes well beyond target setting." She also cautioned about the danger of viewing the energy transition as a binary concept, broken down into "good" and "bad" forms of energy.

"The true focus needs to be on emissions reductions," she said. "How do we get to a lower-carbon economy that is still safe and affordable to use, regardless of fuel type?"

Evolution Well Services' e-frac solution

The case of Evolution Well Services, a specialist in electric fracturing, illustrates how companies that specialize in a particular area of OFS are responding to producers' ESG concerns.

"Our aero-derivative turbines run on 100% field gas, offering a lower carbon fuel source to power hydraulic fracturing operations, while provid-

> “We are seeing E&Ps target electrification throughout their entire operations, not solely hydraulic fracturing.”
>
> **–Keith Myers,**
> Evolution Well Services

ing unparalleled fuel savings to our customers through the elimination of conventional diesel-powered equipment,” Evolution’s director of business development, Keith Myers, told Hart Energy. “In addition to reducing the carbon intensity of operations, our electric fracturing solution requires significantly less equipment, improves safety and provides a quieter operation when compared with conventional equipment.”

According to Myers, interest in the company’s technology is at an all-time high.

“We are seeing E&Ps target electrification throughout their entire operations, not solely hydraulic fracturing,” Myers said. “Evolution is partnered with some of the most forward-looking and innovative E&Ps in the industry, and this is highlighted by their decision to be early adopters of electric fracturing. Within these partnerships, we always seek to align both operational and ESG targets with our partners.”

Evolution sees the fact that it has spent several years honing its expertise in an industry where introducing new technologies can be challenging as a competitive advantage.

“E&Ps cannot sacrifice performance in the journey for reduced emissions, and by selecting the most experienced service company, E&Ps gain certainty with their ability to reduce emissions and operate efficiently,” Myers added.

The company sees maintaining performance standards while simultaneously reducing the environmental impact of operations as a key challenge for the OFS sector. However, it is optimistic for the future and the role ESG will play.

“As the shale revolution unlocked reserves that were previously thought to be inaccessible, the ESG revolution will spur innovation that will enable E&Ps to produce the oil and natural gas required to fuel increasing energy demand while achieving meaningful ESG targets,” Myers said.

Top priority

Looking ahead, E&Ps will need to focus increasingly on striking a balance between sustainability and meeting global energy needs.

“The wider question of how the industry balances long-run climate/ESG goals with meeting oil and gas demand—still rising in the short term—now tops the industry agenda,” Energy Intelligence’s Martinos said.

Previous forecasts of peak oil demand appear to have been premature as consumption rises again. In this environment, help from OFS firms on balancing decarbonization while meeting growing needs will be particularly welcome. ■

(Source: buffaloboy/Shutterstock.com)

Southwestern completed a Muddy Creek watershed restoration project in 2019 in West Virginia. Muddy Creek had been severely affected due to unrelated, third-party acid mine drainage from abandoned mines, but the 2019 project successfully restored Muddy Creek to its natural state. (Source: Southwestern Energy)

Using Data to Showcase Environmental Stewardship

Southwestern Energy has made strategic investments in technology to reduce its greenhouse-gas emissions.

By **Mary Holcomb,** *Contributing Editor*

Environmental sustainability is a critical pillar that makes up ESG, and at the core is good stewardship—respecting the air, land and water. In the oil and gas industry, companies are focused on delivering cost-effective energy for the industry and consumers while also being cognizant of how their operations impact the world's ecosystems and habitats.

Many energy companies are achieving this by leveraging their emissions data to invest in environmental projects and initiatives to reduce or offset future emissions. The tracking of greenhouse-gas (GHG) emissions provides operators the ability to gauge their operational efficiency to better maintain their operations.

A first-mover in seeking to reduce methane emissions, U.S. natural gas producer Southwestern Energy Co. has prioritized ESG as a core value of its business for years. As a company focused on natural gas, methane is the chief component of the product it sells. Effective ESG planning and execution has proven to be an opportunity for the company to capture more value for its shareholders while also minimizing its impact on the communities where it operates.

"We invest in ESG, because it actually delivers value to the environment and to the communities where we work and live," said Bill Way, Southwestern Energy's president and CEO. "We want to enhance our position

as a leading natural gas company by responsibly developing clean, low-carbon natural gas through the right people doing the right things."

The company's strategy focuses on responsibly developing a core position in the two premier gas basins it occupies [Appalachia and Haynesville] in the U.S., "in a way that creates sustainable value for all stakeholders, protects the financial strength [of the company] and progresses our execution ability in the company."

An example of its ESG leadership includes the implementation of emissions monitoring technology on its pads in the Appalachian Basin.

The deal with Denver-based startup Project Canary outlined a first-of-its-kind, basinwide commitment toward producing responsibly sourced natural gas, and Southwestern recently expanded the program to its recently acquired assets in the Haynesville. In Appalachia, Southwestern has 1,575 wells certified and just over 800 wells in the Haynesville shale play, he said.

"With active monitoring, we can see if something is leaking or venting," Way said. "Across the entire site, we can see the amount of methane emissions we produce so that we can reduce or eliminate them. Then we can use that data to set goals."

Way noted that the system has helped the company make additional strategic investments in the business through "technology of today and tomorrow."

"We keep all of that data, and we can do a lot of analytics with it," he said. "It helps us with predictive maintenance and can eventually cause us to have a great reduction in greenhouse gases."

The International Energy Agency found that oil production is currently responsible for about 40% of methane emissions, with leaks across the natural gas value chain accounting for the remaining 60%. The report showed that upstream oil and gas operations lead to more than three-quarters of total emissions.

Minimizing methane emissions is a key goal for the organization, which achieved a methane leak/loss rate of 0.075% in 2020. The organization has been implementing methane mitigation technologies in its facilities since the 1990s. These include reducing emissions through green completions techniques as well as carrying out leak detection and repair programs.

The ongoing remote monitoring program is used to identify potential methane leaks. This program is carried out by field personnel who are trained to detect the smell and pressure changes.

Surveys involving optical gas imaging cameras are carried out annually, and the data collected contribute to repairs and drive performance and efficiencies.

"When we get all the monitoring in place, we're able to collect the data and create a baseline of where we are," he said. "Then, as we do the analytical work, we can take that data across the board. We can look at areas where we might have leaks, take the analytics and figure out that if we do service on that unit 30 days earlier, we won't have the leak to begin with because we can begin to predict the maintenance."

In the last two years, Southwestern expanded its position with the acquisition of Montage Resources Corp. as well as private Haynesville producers Indigo Natural Resources LLC and GEP Haynesville LLC. However, the addition of these acquisitions increased the organization's GHG emissions metrics, particularly methane rose by 0.02% from 2019 to 2020.

Despite the impact on its GHG emissions profile, the acquisitions provide an opportunity for the company to illustrate its emissions leadership by implementing additional controls and improvements on the assets, according to its 2020-2021 corporate responsibility report.

"We're able to acquire companies who are not performing in the ESG space as well as we do," Way said. "With a larger enterprise, we can do more philanthropic support and support larger projects." ■

(Source: Southwestern Energy)

Do's and Don'ts of ESG Strategies

Starting now, operators in the energy sector need to turn their carbon reduction commitments into solid plans of attack, according to top energy analysts.

By **Madison Ratcliff,** *Associate Editor*

Another year closer to society-imposed carbon reduction targets means it is crunch time for oil and gas operators. To reach the 2030 and 2050 benchmarks set by the energy industry, operators need to understand that, "2020 [and] 2021 have been the years of commitments; 2022-plus will be about actions," according to Rebecca Fitz, senior director of Center for Energy Impact with BCG.

Top analytic companies have been monitoring what has and hasn't worked so far in the industry's energy transition. Among the list of improvements, they recommended making efforts to turn promises into actions and taking care not to neglect the governance aspect of ESG.

For this exclusive analyst roundtable, Fitz was joined by Nick Volkmer, vice president of ESG with Enverus; Olga Savenkova, senior analyst with Rystad Energy; and Steve Estes, advisory partner with KPMG, to discuss the effectiveness of the energy industry's ESG strategies.

Hart Energy: How have operators' ESG efforts evolved over the last year?

Fitz: To meet new commitments, strategies had to be reset, revised and fine-tuned, and what we saw was a lot of oil and gas companies coming forward with new strategies designed to explicitly reposition them to meet some of their new emissions goals. I would just, in general, say the big integrated supermajors, their commitments vary, but they have been on the leading edge, in some senses, of putting forward new climate commitments. But what really surprised me were the U.S. E&Ps also

"There's a want in the world to decarbonize, but at the same time, the world's not going to settle for energy scarcity anytime soon, so I think that getting those two different challenges aligned is going to be important and will be a focus from the regulatory side."

–Nick Volkmer,
Enverus

moved forward with new emissions commitments. And I think there's a lot of progress to be made still, but we're having a different dialogue than we were two years ago when it comes to these kinds of commitments.

Savenkova: The environmental side of ESG is under increasing spotlight for operators these days. Last year marked a turning point for the oil and gas industry as many upstream players reshaped their strategic priorities to respond to climate risk and increasing pressure from governments, regulatory authorities, investors and the public to play their part in decarbonizing the global economy. The companies' chosen path through the energy transition will, to a large extent, determine how they allocate their capital in the years ahead.

We can underline the following key trends that evolved last year: strategic shifts with sustainability at the core; redirecting budgets and setting low-carbon investment targets; carbon pricing resilience (a stress test for investments); and low-carbon solutions in field development.

"There's a lot of progress to be made still, but we're having a different dialogue than we were two years ago when it comes to these kinds of commitments."

–Rebecca Fitz,
BCG

Hart Energy: What kinds of ESG strategies have proved to be most effective thus far in lowering emissions and will help operators reach their net-zero emissions goals? Which ones have been the least effective?

Volkmer: ESG is still pretty broad, and I think the exact definition of ESG is still being worked out. I think one thing that is pretty universally agreed upon though is that the 'E' is going to be important, especially visible components of the 'E.' So where we've seen a lot of companies focus recently is around what's a little bit more visible, particularly flaring; we've seen flaring rates drop about 61% in the U.S. since 2019. Obviously that fell during COVID, but it hasn't bounced back yet, which we believe is a sign the industry is taking ESG more seriously.

I think that the technology around methane leak detection is going to improve rapidly over the next few years, either from different field level systems or from upcoming satellites that are going to be launched and bring a lot more visibility into methane. So we've seen a lot of companies put dollars into either tracking methane [or] fixing known sources of methane, so pneumatic controller and devices are a really big piece there. And then we're also seeing a lot more movement of third-party certifications on things like responsibly sourced gas.

Savenkova: We outlined three main pillars of energy transition: energy diversification, portfolio resilience and decarbonization. Using this framework, we looked at how companies are adjusting their strategies to align with the Paris Agreement's goal to limit the increased average global temperature to 1.5 C above pre-industrial levels.

The strategic priorities brought on by the energy transition differ between industry segments and regions. Direct emissions reduction together with a cost-efficient offsetting strategy seem to be essential despite company-specific priorities.

Hart Energy: How does the governance aspect of ESG play a role in boosting ESG scores?

Volkmer: When you look at oil and gas, it's a global industry, and I think in certain jurisdictions, good governance from a safety, community and corruption perspective are important. In North America, companies tend to operate in an environment where a lot of these challenges have been overcome. What I think we've seen more so in North America is a push for more oversight with respect to management compensation and incentives. We've seen payment structures shift, [and] a lot more producers tie bonuses to specific ESG criteria, whether that's emis-

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–Steve Estes,
KPMG

sions or promoting company diversity, things like that. It's a lot more explicit now than it used to be. There's also better alignment with shareholders. As a whole, better management incentives are one of the biggest changes we've seen over the past few years with respect to the governance in the energy industry in North America.

From a regulatory standpoint, [there will be] policies that directly impact things like methane emissions. We saw the EPA put out a proposal toward the end of the year with a wider mandate to regulate methane emissions. We believe these types of proposals will continue, and carbon accounting and carbon management will keep increasing in importance. I think that's where we're seeing a lot of the movement in the market. There's a want in the world to decarbonize, but at the same time, the world's not going to settle for energy scarcity anytime soon, so I think that getting those two different challenges aligned is going to be important and will be a focus from the regulatory side.

Fitz: There's a couple of near-term issues that maybe next year or two or three I would expect to see. Most of them are emissions-centric, but I would expect to see this wave of companies announcing emissions targets and gradually more comprehensive targets, so moving on from Scope 1 targets, Scope 1 and 2 to net-zero to Scope 3. I would expect that to continue.

I would expect more American companies to have Scope 3 targets; that's slow work, but I think there's pressure for that. I would expect more efforts at standardization. There is an SEC effort to force standardization in how emissions are reported overall, just to get to a place where we can benchmark targets.

"The strategic priorities brought on by the energy transition differ between industry segments and regions. Direct emissions reduction together with a cost-efficient offsetting strategy seem to be essential despite company-specific priorities."

–Olga Savenkova,
Rystad Energy

We can do it now, but it's haphazard. So I think more consistency across companies and targets is going to be showing up.

Hart Energy: What is the No. 1 thing operators can do to improve their ESG scores and satisfy investors? What potential strategies or practices are being overlooked?

Fitz: Simplistically, I'd focus on emissions, just aiming for absolute transparency and benchmark-ability on your emissions. It's not easy, but I started out benchmarking operational performance, and there's a framework where you can do that [for] any company against any company. I think we should be aiming for that on the emissions front. And then you ultimately have top-tier, second-tier, third-tier, fourth-tier quartile performers, and I think that would help, that's a necessary step that we need to get to. We're definitely a ways from that, but bringing transparency to that, calling out the best performers, calling out the worst performers—and no one likes to be the worst performer—I think that would be a good step. And there's a lot of initiatives working on that, but there's a huge number of companies that you need to bring to the table.

Estes: A lot of CFOs or people would say they don't like this answer, but from a backoffice perspective, it's creating the organizational support for creating an individual whose role is sustainability and the ESG program. In many cases, you know, there's a number of organizations out there that are rating agencies [and] organizations that are giving a score to that entity based on different criteria. That can have an impact on future financing through green bonds or reputational risk. And you need a group that's able to spend some time to understand, 'Well, what are those rating agencies and groups that do have an impact on our company or our finance role?' Understand how they're scoring your company and have a conversation with those entities, because many times they just simply read the CSR [corporate social responsibility].

Hart Energy: 2030 and 2050 are common targets among operators and countries to achieve net-zero emissions. Between now and 2050, how do you see ESG efforts evolving throughout the energy sector as a whole?

Volkmer: Figuring out the proper primary energy mix; obviously renewables are going to increase in their share of total energy, but at what expense? I think we can agree that coal is probably going to be reduced, but natural gas is likely going to play a big component in the future, so how do those different pieces relate together? Then also, from an offsetting perspective, it kind of goes back to that measurement, like if you can't effectively or properly calculate how much carbon is being taken out of the air from different projects, it's hard to have a widespread carbon offsetting market. But I think that's going to be a pretty big component to it too. Saltwater disposal, you put a ton of volumes down there, so I think just trying to sort the risks and impacts to the water question; I don't think it's talked about enough.

Estes: It could be all over the map. You see the majors, and some of those are taking some pretty aggressive claims and what they would like to see their company do by some of those decade milestones that are coming up. Some independents might not go that far. They'll have goals of where they want to reduce emissions, but I think it'll be an individual company decision based on the DNA of that organization.

I think it's fair that all companies will be responding to ESG and how it impacts their company, and they should absolutely be using that to set their individual goals and not just follow up [on a] copycat strategy of everybody else picking 2030. We also say don't put out a milestone date like that, that you really haven't thought through. How likely is that, particularly your public company? You still have profitability goals that you're out there to seek, so you still need to make sure, 'Can I meet sustainability goals in a way that meets my shareholder expectations on performance?' So I would say it's going to be all aboard. I wouldn't rush into it, but rather ease into the ESG journey. ■

Industry Will Not Abandon ESG During Crisis, Others Must not Abandon Industry

To maximize the industry's abilities, government leaders must take immediate action to embrace the security and reliability of U.S. domestic energy resources.

By **Leslie Beyer,**
Energy Workforce and Technology Council

During a crisis, such as Russian President Putin's unprovoked invasion of Ukraine, our industry will not abandon and should not forgo its ESG goals. At the same time, outside investors and interested parties must recognize this is not the time to boycott or divest in domestic energy production. This would be irresponsible and counterproductive to our economic and national security as Putin's actions have brought to the forefront the need to maximize U.S. domestic energy resources and not be beholden to world tyrants that disrupt and destabilize global energy markets.

U.S. production can ramp up production in conjunction with energy infrastructure and the pullback of excessive regulatory hurdles, while staying true to its ESG commitments.

The oil and gas industry has adopted ESG into its core values and organizational missions. ESG disclosures are on the rise and being made publicly available on websites through sustainability reports and company annual reports.

To assist industry partners in adopting ESG programs and meeting requirements, more than four years ago, Energy Workforce and Technology Council launched its ESG Committee and two years ago launched an ESG Certification program.

Through the ESG Certification program, we are supporting ESG and sustainability as integral to operations. Educating our membership base and others that a properly implemented ESG program can lead to profitability and highlighting that corporate commitment to ESG sets companies apart from their competitors.

We are working with our members to develop clear, smart, achievable and non-duplicative targets that are adaptable to address improving technology and heightened awareness of the importance of ESG issues.

Our team is also seeking reporting standardization in an effort to reduce duplicative efforts to comply with ESG requirements. Often companies face confusion and an unwillingness to engage due to multiple reporting frameworks, key performance indicators and competing metrics.

ESG is about identifying gaps, managing risk and applying what we've learned to improve our environmental performance, be a good neighbor in the communities where we operate and make the industry a desirable and equitable place to work.

Additionally, the industry is setting aggressive goals to reduce emissions and will continue to make great strides in lessening its carbon footprint through innovation, new technology development and implementation, and diversifying domestic energy resources.

Technologies like CCUS and geothermal are rapidly being improved and perfected by U.S. energy service companies. While often not yet scalable at a commercial level, government investments in this technology will help spur additional investments leading to a growing number of energy choices.

U.S. energy service companies are also working to bring more of the lithium supply chain to the U.S., which will aid in expanding the ability to locally produce solar panels and lithium batteries.

Now is not the time to hamper the U.S.' economic and national security, and that of its allies by sequestering investment in U.S. production. Vilification, boycotts and unnecessary burdensome regulations hurt workers and the workforce, not just industry giants and executives. The industry continues to support the workforce, create jobs and is ready to make a robust turnabout to pre-pandemic production that will boost the economy where we work and produce.

The industry has the expertise, technology, workforce and innovation to increase domestic supplies of oil and natural gas in a clean, environmentally safe, responsible manner. But to maximize its abilities, government leaders must take immediate action to embrace the security and reliability of domestic energy.

The domestic industry stands ready to meet global energy demand. However, this is only possible through robust investment and consistent support of U.S. oil and natural gas. ■

About the author: *Leslie Beyer is the CEO of the Energy Workforce and Technology Council, the national trade association for the energy technology and services sector, representing more than 600,000 jobs in the technology-driven energy value chain.*