Mr. Erik Gerding
Director, Division of Corporation Finance

Mr. Paul Munter
Chief Accountant, Office of the Chief Accountant

Securities and Exchange Commission
100 F St NE, Washington, DC 20549

14 October 2024

Dear Mr. Gerding and Mr. Munter,

Re: Inadequate critical accounting assumption disclosures

We are writing as a group of forty institutional investors representing $3.75 trillion in assets to raise concerns about inadequate disclosures on critical accounting assumptions and associated sensitivities by listed US energy companies[1]. This inhibits our ability to interpret and compare companies' financial condition and operating performance, undermining our ability to allocate capital effectively. Beyond the immediate risks to investment returns, impaired market efficiency would tend to hamper economic growth and thus long-term investment returns.

In view of the SEC's mission to protect investors, maintain fair, orderly, and efficient markets, and to facilitate capital formation, we would welcome your attention to this matter. We note that the lack of disclosure has persisted despite amendments to Regulation S-K, Item 303, in 2021 to make clear the requirement for the disclosure of critical accounting estimates and assumptions[2]. We believe there would be merit in further clarifying guidance to reinforce existing disclosure requirements across both Regulations S-X and S-K, as well as emphasising such requirements in the reviews of company filings and ultimately, enforcement action where existing requirements are not being followed.

The problem: poor disclosure of critical accounting estimates and assumptions

Based on a review of US-listed energy companies' 2023 Form 10-K (10K) disclosures, covering both the "front end" (e.g. Management Discussion and Analysis (MD&A) and Risk Factors) and the notes to the financial statements, we have found that these companies typically provide qualitative disclosures relating to critical accounting assumptions but limited or no quantitative disclosure[3]. These include the following critical accounting assumptions[4]:

- long-term oil and gas price and demand assumptions (used for impairment testing of upstream assets);

[1] We focus here on energy companies. However, the core concerns raised may be relevant in other sectors, particularly those facing structural change and thus more uncertain future outlooks.
[2] https://www.sec.gov/files/rules/final/2020/33-10890.pdf
[3] As highlighted in footnote 1, inadequate disclosures of quantitative accounting assumptions and estimates is unlikely to impact exclusively the energy sector. We focus on energy here as we perceive the situation to be particularly acute.
[4] This is not a comprehensive list of critical accounting assumptions but those we view to be particularly material. Carbon tax / price assumption disclosures are also important, and we would expect these to be factored into forecasting of longer-term commodity price and estimated refining margin assumptions that are used in impairment testing of the relevant assets.

- estimated refining margins (used for impairment testing of downstream assets);
- key quantitative assumptions used to calculate liabilities for asset retirement obligations (AROs) and considered in relation to off-balance sheet amounts[5]; and
- discount rates used in impairment and ARO calculations.

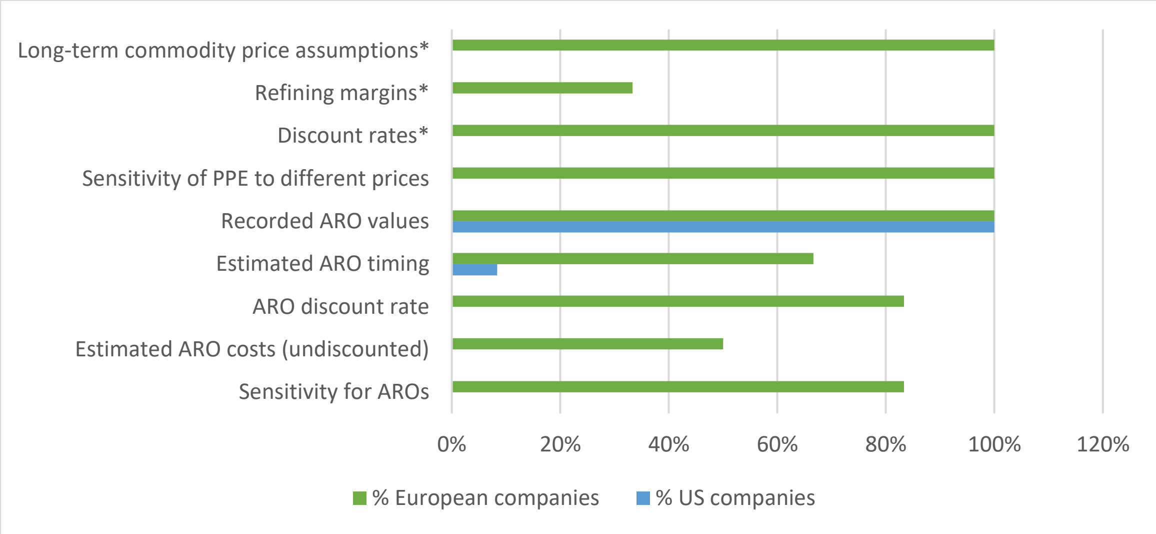
This picture contrasts with European oil and gas company accounting disclosures. Based on a review of seven listed US and six European (including UK) energy companies' annual filings, Carbon Tracker finds US companies lag far behind their European peers in the disclosure of quantitative critical accounting assumptions and estimates (see summary bar chart below)[6].

For instance, in the case of long-term commodity price assumptions used for impairment testing, discount rates and sensitivities to different prices, all of the European companies reviewed provide quantitative assumptions, while none of their US counterparts do. Similarly, over 80 percent of European companies provide quantitative disclosures on discount rates used to calculate AROs as well as sensitivities to different assumptions, whereas none of the US companies do. Company-specific results are provided in an Addendum to this letter.

[5] Energy companies do provide some ARO related assumptions in line with explicit requirements in US GAAP ASC 410-20-50-1 (Asset Retirement and Environmental Obligations), including a general description of the ARO and associated long-lived assets; the fair value of assets that are legally restricted for purposes of settling AROs; a reconciliation of the beginning and ending aggregate carrying amount of AROs showing separately the significant changes attributable to liabilities incurred, liabilities settled, accretion expense, and revisions in estimated cash flows. However, the following key assumptions that are critical to investor understanding of AROs are often missing: the expected value of the undiscounted AROs and timing; key assumptions used in valuing the liabilities such as costs, inflation and discount rates; sensitivities of AROs to key underpinning assumptions, and similar information for unrecognised AROs (e.g. left out due to indeterminate settlement dates). See Rogers and Schuwerk (Dec 2023) for fuller discussion of missing information. https://carbontracker.org/reports/overlooked-why-oil-and-gas-decommissioning-liabilities-pose-overlooked-financial-stability-risk/

[6] Per analyses by Carbon Tracker's Accounting, Audit and Disclosure team for select Climate Action 100+ focus companies. The results of the 152 assessments will be published in Q4 2024. Please see Addendum with the results from a preliminary review of 2023 annual filings in these categories for seven US energy companies (Occidental Petroleum, Exxon Mobil, Chevron, ConocoPhillips, Marathon Petroleum, Phillips 66, and Valero Energy), as well as six European energy companies (bp, Shell, Eni, Repsol, TotalEnergies, Equinor).

Figure 1: Percentage of US and European energy companies reviewed providing quantitative accounting assumptions / estimates in annual filings for 2023[7]



Source: Chart based on Carbon Tracker analysis, August 2024.

*For impairment testing; where applicable (e.g. commodity price assumptions for upstream activities and estimated refining margins for downstream activities)

Why non-disclosure matters

The lack of quantitative disclosures of critical accounting assumptions and estimates impedes market efficiency by undermining investors' ability to assess the reliability of the financial statements; to determine companies' resilience to plausible economic headwinds such as lower long-term oil and gas prices; or to compare companies' financial statements.

This point is particularly pertinent today as energy companies are facing structural reductions in long-term demand driven by global policies to deliver decarbonisation as well as the rapid development (and falling costs) of alternative lower-carbon energy sources, such as renewables. These changes are expected by independent experts to continue, if not accelerate[8].

The lack of disclosure of quantitative sensitivities furthermore means investors have little visibility around how resilient companies would be to plausible scenarios such as faster decarbonisation or more extreme global warming, potentially associated with a more precipitous decline in commodity prices / demand, changing discount rates, and rising AROs. Depending on the scale of the downside risks, there could be ramifications for dividend paying capacity under relevant state laws[9].

[7] Notes on methodology: Disclosure of assumptions/estimates is scored 1; no disclosure 0 and partial disclosure 0.5. Scores removed from calculation where not applicable – e.g., refining margin estimates are only relevant when refining activities undertaken by the entity. In addition, this analysis focuses only on assumptions and estimates related to recorded AROs, not unrecorded AROs which arise where issuers assume, for instance, indeterminate lives for relevant assets. We have concerns over the transparency of such unrecognised AROs but do not consider this here.

[8] The International Energy Agency (IEA) provides one of the most widely used references for energy market modelling applied in listed energy companies' financial statements. Their central Stated Policies (STEPS) scenario projects peak oil and gas demand by 2030, with more rapid reductions in demand in their Announced Policies (APS) and Net Zero by 2050 (NZE) scenarios (https://www.iea.org/news/slowing-demand-growth-and-surging-supply-put-global-oil-markets-on-course-for-major-surplus-this-decade). Oil price projections for 2030 vary between each, ranging from $85/bbl to $42/bbl. For gas the range in 2030 in the US is $4/MBtu to $2.4/MBtu. https://iea.blob.core.windows.net/assets/86ede39e-4436-42d7-ba2a-edf61467e070/WorldEnergyOutlook2023.pdf

[9] For instance, dividend rules under Delaware General Corporation Law, Section 170 and 173, prohibits dividend payments where surplus capital does not exist, taking into account expected liabilities:

Given the risks and uncertainties facing energy companies, the importance of ensuring accounting transparency is paramount[10]. The longer the market lacks clarity on critical accounting assumptions, the greater the danger of capital misallocation and instability in the sector.

Regulation S-K, Item 303, requires disclosure of critical accounting estimates and assumptions (as does US GAAP)

The lack of company disclosure of the above-mentioned critical accounting estimates and assumptions appears to be at odds with the SEC's Regulation S-K, Item 303[11], which makes clear that companies must disclose in their MD&A the critical accounting estimates and assumptions that underpin their financial statements and are important to understanding the company's financial position. Management is also required to disclose changes to these assumptions, as well as sensitivities to reasonable alternative assumptions, where this information is material.

In the energy sector, each of the above noted assumptions (long-term commodity prices; refining margins; inputs for calculating AROs and discount rates) involve significant estimation uncertainty and are identified by energy companies themselves as critical accounting estimates in their 10Ks[12]. Despite this, the companies frequently do not provide the numerical assumptions used.

The lack of critical quantitative accounting estimate disclosure is not a new problem. In an amendment to the Regulation introduced in February 2021, the SEC outlined its intention to ensure disclosure of critical accounting estimates and sensitivities of the reported numbers to different assumptions[13].

US Generally Accepted Accounting Policies (GAAP) aligns with Regulation S-K, requiring the disclosure of material critical accounting assumptions in several standards, notably: ASC 360 (Impairment of long-lived assets), ASC 350 (Impairment of Goodwill), ASC 410-20 (AROs) and ASC 820 (Fair value measurement).

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https://delcode.delaware.gov/title8/c001/sc05/index.html#170. Section 548 of the US Bankruptcy Code (and similar state laws), make clear that dividend payments made when a company is insolvent or that render the company insolvent can be clawed back if the company later files for bankruptcy.

[10] We note the SEC has provided specific guidance around climate-related disclosures under existing rules, including the 2010 Guidance Regarding Disclosure Related to Climate Change, Release No. 33-9106 (https://www.sec.gov/files/rules/interp/2010/33-9106.pdf), as well as a sample 'Dear issuer' letter in 2021 (https://www.sec.gov/rules-regulations/staff-guidance/disclosure-guidance/sample-letter-companies-regarding-climate). In March 2024, the SEC adopted a new Climate Disclosure Rule to tackle weak implementation (https://www.sec.gov/newsroom/press-releases/2024-31), which has been stayed pending litigation. In all cases, the SEC has pointed to the need to treat climate-related risks and opportunities, whether related to physical, regulatory or technological factors, as economic phenomenon that must be captured under the existing disclosures rules and requirements. In this letter we are specifically focused on accounting related disclosures as vital to investor decision-making.

[11] https://www.law.cornell.edu/cfr/text/17/229.303 - See specifically paragraph (b)(3)

[12] See, for instance, Occidental's 2023 10K, Note 1 to the Financial Statements "Summary of significant accounting policies".

[13] https://www.sec.gov/files/rules/final/2020/33-10890.pdf - Section C 8 (emphasis added): "*The Commission proposed amending Item 303 to add new Item 303(b)(4) [later adopted as to 303(b)(3)], which would explicitly require disclosure of critical accounting estimates in order to clarify the required disclosures of critical accounting estimates, facilitate compliance, and improve the resulting disclosure…For each critical accounting estimate, the proposal would require registrants to disclose, to the extent material, why the estimate is subject to uncertainty, how much each estimate has changed during the reporting period, and the sensitivity of the reported amounts to the methods, assumptions, and estimates underlying the estimate's calculation. Lastly, the proposal specified that the discussion should provide quantitative as well as qualitative information when quantitative information is reasonably available and will provide material information to investors.*"

Materiality
A key qualifier applied by the SEC to the disclosures of critical accounting estimates (both quantitative and qualitative) is that the information is 'material', defined in the Code of Federal Regulations (CFR), Part 270, as "*those matters as to which an average prudent investor ought reasonably to be informed before buying or selling any security of the particular company.*"[14]

The SEC's Staff Accounting Bulletin 99 (SAB 99) further clarifies the importance of considering qualitative factors alongside quantitative factors in determining materiality, and that companies should avoid over-reliance on quantitative thresholds, such as 5% sales, in determining materiality[15]:

> *"… The staff reminds registrants and the auditors of their financial statements that exclusive reliance on this [5% threshold] or any percentage or numerical threshold has no basis in the accounting literature or the law…. A matter is "material" if there is a substantial likelihood that a reasonable person would consider it important."*

The investor signatories to this letter view the assumptions identified above (long-term commodity prices, refining margins, assumptions underpinning ARO calculations and discount rates) to be material to their decision-making due to their importance in determining the reported financial results[16]. As noted previously, the energy companies reviewed appear to agree that the assumptions listed are material as they are often identified by these companies under their 'Critical accounting policies and estimates'.

The issue, therefore, does not appear to be whether or not these critical accounting assumptions are material. Rather, there seems to be a view that, even where assumptions are material, there is no requirement to disclose the quantitative assumptions. We cannot see how this can be reconciled with the requirements.

The information investors seek is 'reasonably available'

A second qualifier alongside 'materiality' for disclosure of critical accounting estimates is that the information is 'reasonably available'[17]. On this point we would simply say that, given these assumptions are necessary for drawing up companies' financial statements, there is no additional information gathering required. Investors merely ask for companies to publish the estimates they are using.

Another argument that we have heard for not disclosing the requested assumptions has been that the information is commercially sensitive. We would make two points in response.

First, in a generally competitive market, individual US energy companies are price-takers, not price-setters[18]. Therefore, in their forward-looking assumptions they should be using established and

[14] See Item 8b-2 (Definitions) (g) (https://www.law.cornell.edu/cfr/text/17/270.8b-2)
[15] https://www.sec.gov/interps/account/sab99.htm
[16] Shareholder resolutions filed at Exxon and Chevron between 2021 and 2023 seeking the disclosure of critical accounting assumptions and sensitivities to faster decarbonisation pathways provide further evidence that this information is material to investors. For instance, see resolutions filed at Exxon in 2022 (https://cbisonline.com/us/vote-for-cbis-shareholder-proposal-at-exxonmobil/) and 2023 (https://www.sec.gov/Archives/edgar/data/34088/000121465923007809/x525230px14a6g.htm)
[17] See Regulation S-K, Item 303, Para (b)(3) - https://www.law.cornell.edu/cfr/text/17/229.303
[18] Recent statements by the Federal Trade Commission (FTC) point to concerns over potential anti-competitive behaviour by US oil and gas majors (https://www.ftc.gov/news-events/news/press-releases/2024/05/ftc-order-bans-former-pioneer-

independent benchmarks. Whether or not one company decides to assume a higher or lower oil price in 2030, for instance, is unlikely to influence the market, but is important information to inform investor decision-making.

Second, we would question the commercial sensitivity of these assumptions given that most listed European oil and gas companies provide the requested disclosures, without any evident harm to their businesses (see Addendum).

Conclusion
Market efficiency contributes to healthy economic growth. Both require transparency. We believe that the current practice by many US-listed energy companies of not disclosing critical forward-looking accounting assumptions and estimates creates opacity in the market, resulting in uncertainty and potential capital misallocation. As noted above, the points we raise may well justify a broader examination of critical accounting assumptions and estimate disclosure across other industries facing structural change.

We would welcome the SEC's attention to this matter and would be pleased to meet to discuss possible ways forward. Please contact Natasha Landell-Mills, Partner, Sarasin & Partners LLP (Natasha.landell-mills@sarasin.co.uk) for any follow up.

We are copying this letter to the Public Company Accounting Oversight Board and the Financial Accounting Standards Board given the relevance of the points raised for auditors in fulfilling their duty to provide an opinion on the reliability of companies' financial statements, and compliance with existing accounting requirements.

Yours sincerely,

Sarasin & Partners LLP
AkademikerPension
Barrow Cadbury Trust
Brunel Pension Partnership
Cardano
Carnegie UK Trust
CCLA Investment Management
Christian Brothers Investment Services
Corra Foundation
Diocese of Westminster
DPAM
Ellison-Cliffe Charitable Trust
Francis Scott Trust
Gloucestershire Community Foundation
Impax
KBI Global Investors
LGIM
Local Authorities' Pension Fund Forum
Mercy Investment Services, Inc.
Miller/Howard Investments, Inc.
Monday Charitable Trust
Nest Pensions
Peter Minet Trust
Railpen
Royal College of Music
Royal College of Obstetricians & Gynaecologists
Ruffer LLP
Sampension Administrationsselskab A/S
Schroders
Scottish Widows
Seventh Generation Interfaith Coalition for Responsible Investment
Society of the Holy Child Jesus – European Province
St. Hilda's College
The Lucy Cavendish College
The People's Pension

ceo-exxon-board-seat-exxon-pioneer-deal). The industry maintains that its behaviour is not in violation of anti-trust rules and the market is competitive.

The Sisters of St. Joseph of Peace Charity
University of Bradford
University of Leeds
Vermont Pension Investment Commission
West Yorkshire Pension Scheme

cc:
Erica Williams, Chair, Public Company Accounting Oversight Board
Richard Jones, Chair, Financial Accounting Standards Board

Addendum – Review of energy company financial disclosures

Source: Carbon Tracker analysis of oil and gas companies' FY2023 Form 10-K or annual reports. US company quantitative information is collected from 10K filings; EU/UK information is from financial statements (including the notes) (FS) (unless stated otherwise).

Company	Source document	Long-term commodity price assump-tions used in impair-ment tests	Estimated refining margins used in impairment tests	Discount rates (WACC) used in impairment tests	Sensitivity of PPE to different prices / margins	Recorded ARO values	Estimated ARO timing	ARO discount rate	Estimated ARO costs (un-discounted)	Sensitivity for AROs
US-listed companies										
Exxon	2023 Form 10-K	Not provided	Not provided	Not provided	Not provided	Provided in the FS	Not provided	Not provided	Not provided	Not provided
Chevron	2023 Form 10-K	Not provided	Not provided	Not provided	Not provided	Provided in the FS	Not provided	Not provided	Not provided	Not provided
Conoco-Phillips	2023 Form 10-K	Not provided	N/A	Not provided	Not provided	Provided in the FS	Not provided	Not provided	Not provided	Not provided
Occidental Petroleum	2023 Form 10-K	Not provided	N/A	Not provided	Not provided	Provided in the FS	Some provided in FS	Not provided	Not provided	Not provided
Marathon Petroleum	2023 Form 10-K	N/A	Not provided	Not provided	Not provided	Provided in the FS	Not provided	Not provided	Not provided	Not provided
Phillips 66	2023 Form 10-K	N/A	Not provided	Not provided	Not provided	Provided in the FS	Not provided	Not provided	Not provided	Not provided
Valero	2023 Form 10-K	N/A	Not provided	Not provided	Not provided	N/A[19]	N/A[20]	N/A[21]	N/A	N/A
	Source document	**Long-term commodity price assumptio**	**Estimated refining margins used in impairment tests**	**Discount rates (WACC) used in**	**Sensitivity of PPE to different**	**Recorded ARO values**	**Estimated ARO timing**	**ARO discount rate**	**Estimated ARO costs (undiscounted)**	**Sensitivity for AROs**

[19] Valero has *"...obligations with respect to certain of our assets at our refineries and plants to clean and/or dispose of various component parts of the assets at the time they are retired..."*. However, it believes that "assets at our refineries and plants have indeterminate lives for purposes of estimating asset retirement obligations because dates or ranges of dates upon which we would retire such assets cannot reasonably be estimated at this time." Accordingly, it has not recorded any AROs at year-end so none of the ARO-related assumptions are applicable here. Valero 2023 Form 10-K, p. 81.

[20] *Ibid*.

[21] *Ibid*.

		ns used in impairmen t tests		impairment tests	prices / margins					
European (inc UK)-listed companies										
bp	2023 Annual Report and Form 20-F	Provided in the FS	Provided outside the FS	Provided in the FS	Provided in the FS	Provided in the FS	Provided in the FS	Provided in the FS	Provided in the FS	Provided in the FS
Eni	2023 Annual Report	Provided in the FS	Not provided	Provided in the FS	Provided in the FS	Provided in the FS	Some provided in the FS	Provided in the FS	Provided in the FS	Not provided
Equinor	2023 Integrated Annual Report	Provided in the FS	Not provided	Provided in the FS	Provided in the FS	Provided in the FS	Provided in the FS	Not provided	Not provided	Provided in the FS
Repsol	2023 Group Annual Financial Report	Provided in the FS	Not provided	Provided in the FS	Provided in the FS	Provided in the FS	Some provided in FS	Provided in the FS	Not provided	Provided in the FS
Shell	2023 Annual Report and Accounts	Provided in the FS	Provided in the FS	Provided in the FS	Provided in the FS	Provided in the FS	Some provided in FS	Provided in the FS	Provided in the FS	Provided in the FS
Total-Energies	2023 Universal Registration Document	Provided in the FS	Not provided	Provided in the FS	Provided in the FS	Provided in the FS	Some provided in FS	Provided in the FS	Not provided	Provided in the FS