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# Haynes Boone and EnerCom Oil & Gas ESG Tracker

August 2021

# Overview – Haynes Boone and EnerCom Oil & Gas ESG Tracker

Over the past year, environmental, social and governance (ESG) has been a transformative force in the oil and gas industry, driving company decision-making and impacting nearly every aspect of oil and gas production. In response to investor and stakeholder demands for greater disclosure, some oil and gas producers are rapidly adopting ESG policies and disclosing more information than ever regarding ESG goals and achievements. Other producers with previously established ESG policies are broadening existing disclosures, reflecting how ESG is embedded within company culture and guides long-term strategy.

Now, more than ever, company ESG achievements and commitments to sustainability are easily accessible on company websites and in U.S. Securities and Exchange Commission (SEC) filings. Companies are forming ESG committees and detailing their ESG strategies in proxy statements and letters to shareholders. Although companies generally are gravitating toward Task Force on Climate-related Financial Disclosures (TCFD) and Sustainability Accounting Standards Board (SASB) reporting metrics, many challenges remain due to the multitude of existing disclosure frameworks and standards, making an apples-to-apples comparison difficult. Further, the SEC and other federal regulators are prioritizing climate change. The SEC has indicated that it expects to issue proposed rules on climate change disclosures by the end of this year, but as of today, it is not clear what disclosure framework will be adopted by the SEC.

This second edition of the Haynes Boone and EnerCom Oil & Gas ESG Tracker summarizes the findings from our mid-year review of 30 U.S.-listed middle market onshore oil and gas producers' SEC filings and other ESG disclosures to help the market better understand the ESG policies and identify trends and takeaways across the industry. We will continue to monitor company disclosures and publish updated reports tracking changes in disclosures and identifying industry trends.

**Haynes and Boone, LLP** is an international corporate law firm that helps clients develop and implement a comprehensive approach to managing legal and business risks and addressing ESG-related issues. Click on these links to learn more about our Energy Practice Group and ESG Practice Group and access our other oil and gas reports on our Energy Roundup page.

**EnerCom, Inc.** is an internationally recognized management consulting firm advising companies on environmental, social and governance (ESG), investor relations, corporate strategy/board advisory, marketing, analysis and valuation, media, branding, and visual communications design. Learn more at enercom.com.

# Trends – Haynes Boone and EnerCom Oil & Gas ESG Tracker

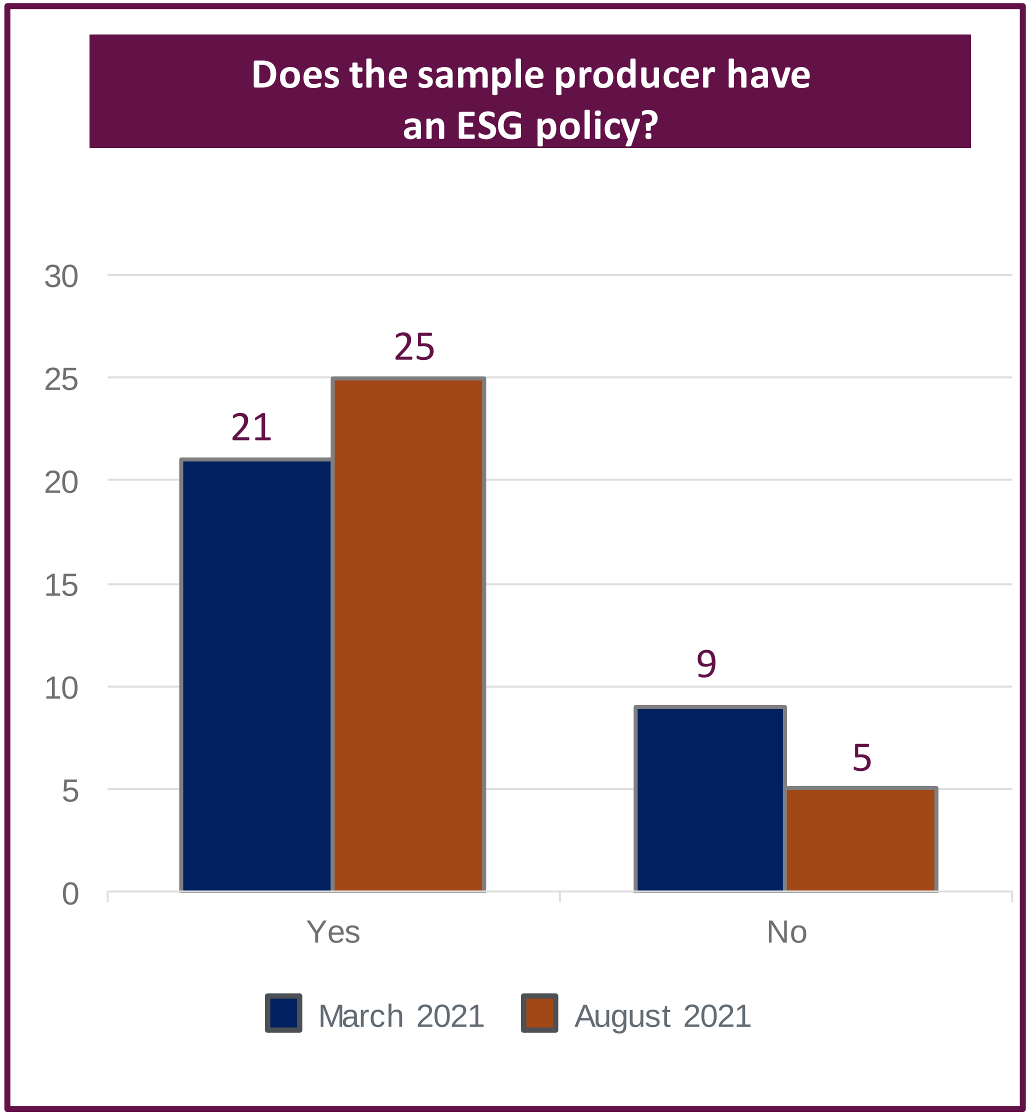
**General Trends**

1. ESG has been widely adopted and ESG principles are embedded within company culture and guide long-term planning.
2. Most companies (83%) have announced and implemented comprehensive ESG programs as of July 15, 2021.
3. More companies are disclosing GHG emissions and reporting annual reductions in direct emissions.
4. Companies with goals of “Net Zero” carbon emissions by 2025 grew by 150% since March 2021.
5. Companies are reporting more ESG achievements and announcing more goals for each ESG criterium.

**Proxy Statement Disclosure Trends**

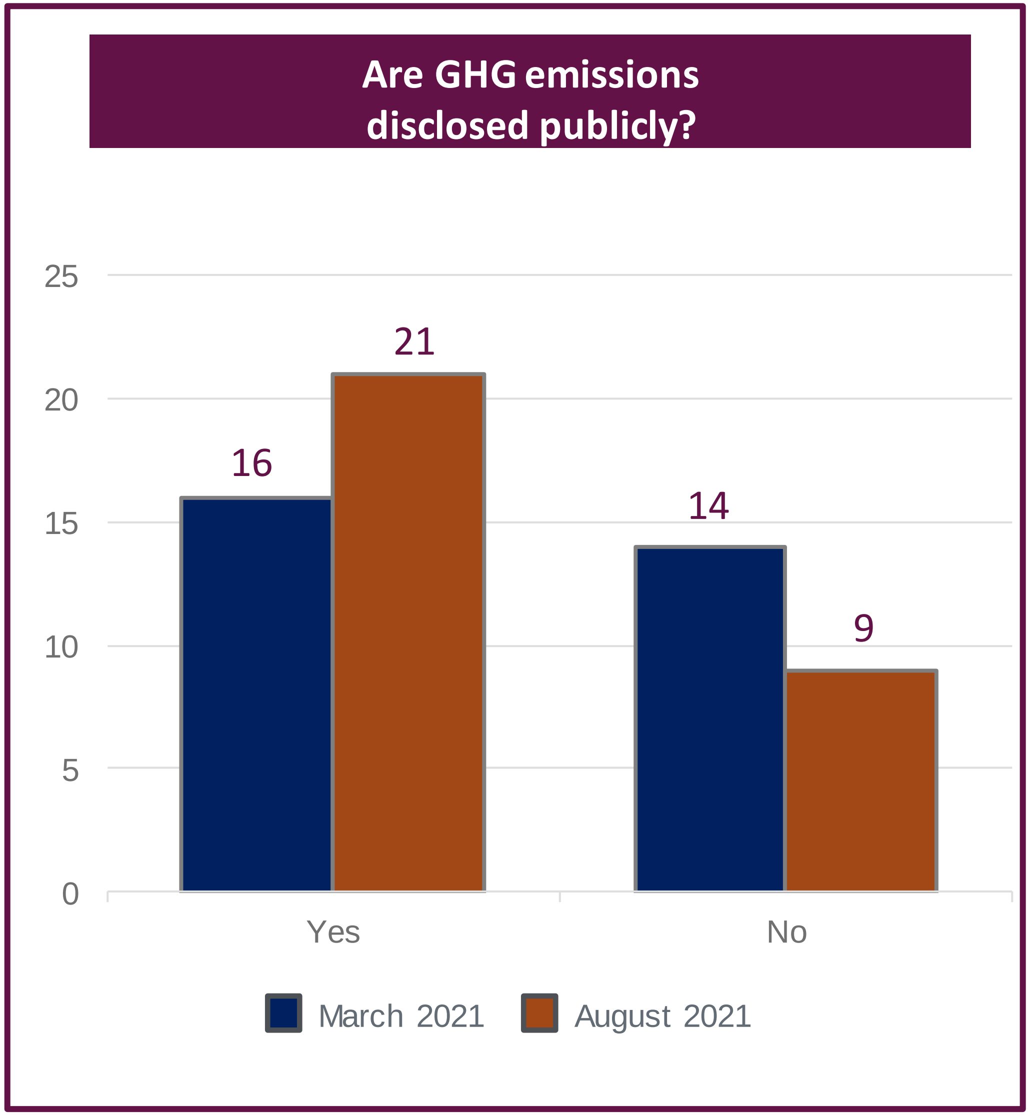
1. Companies are disclosing ESG highlights in the CEO letter and/or the proxy statement summary.
2. Companies are increasingly adding ESG goals and a discussion of ESG strategy in the proxy statement.
3. Companies are disclosing more quantitative metrics, demonstrating progress toward implementing ESG goals, and more companies are reporting metrics in alignment with TCFD and SASB standards.
4. Companies are disclosing details of stockholder engagement efforts relating to ESG.
5. More companies are forming a committee dedicated to ESG oversight and expanding disclosure on ESG oversight.
6. Companies are incorporating ESG metrics into performance targets because investors want to see that executives are incentivized to make progress toward ESG goals.
7. Companies are identifying those directors with ESG-related skills.

# Analysis of the Sample Producers




- 83% of sample producers have publicly disclosed ESG policies, up from 70% in our previous report.
- Producers are rapidly adopting and implementing ESG policies in response to both internal and external factors.
- ESG disclosures are prominently displayed on company websites and garnering more attention in SEC filings.
- Restructured companies have emerged in 2021 with ESG policies and ESG Committees.

# Analysis of the Sample Producers




- Greenhouse gas (GHG) emissions remain one of the most important topics in ESG as companies focus on monitoring and reducing GHG emissions.

- Investments in new technologies allow producers to monitor and reduce GHG emissions through:
  - use of LiDAR technologies to monitor and measure emissions;
  - installation of new field equipment;
  - electrification of operations; and
  - use of renewable energy in the field.

- SEC Chairman, Gary Gensler, noted recently that the SEC is considering mandatory quantitative disclosures on GHG emissions. However, it is unclear whether the SEC will require disclosures on Scope 3 emissions (relating to the value chain) or require different metrics based on a company's industry.

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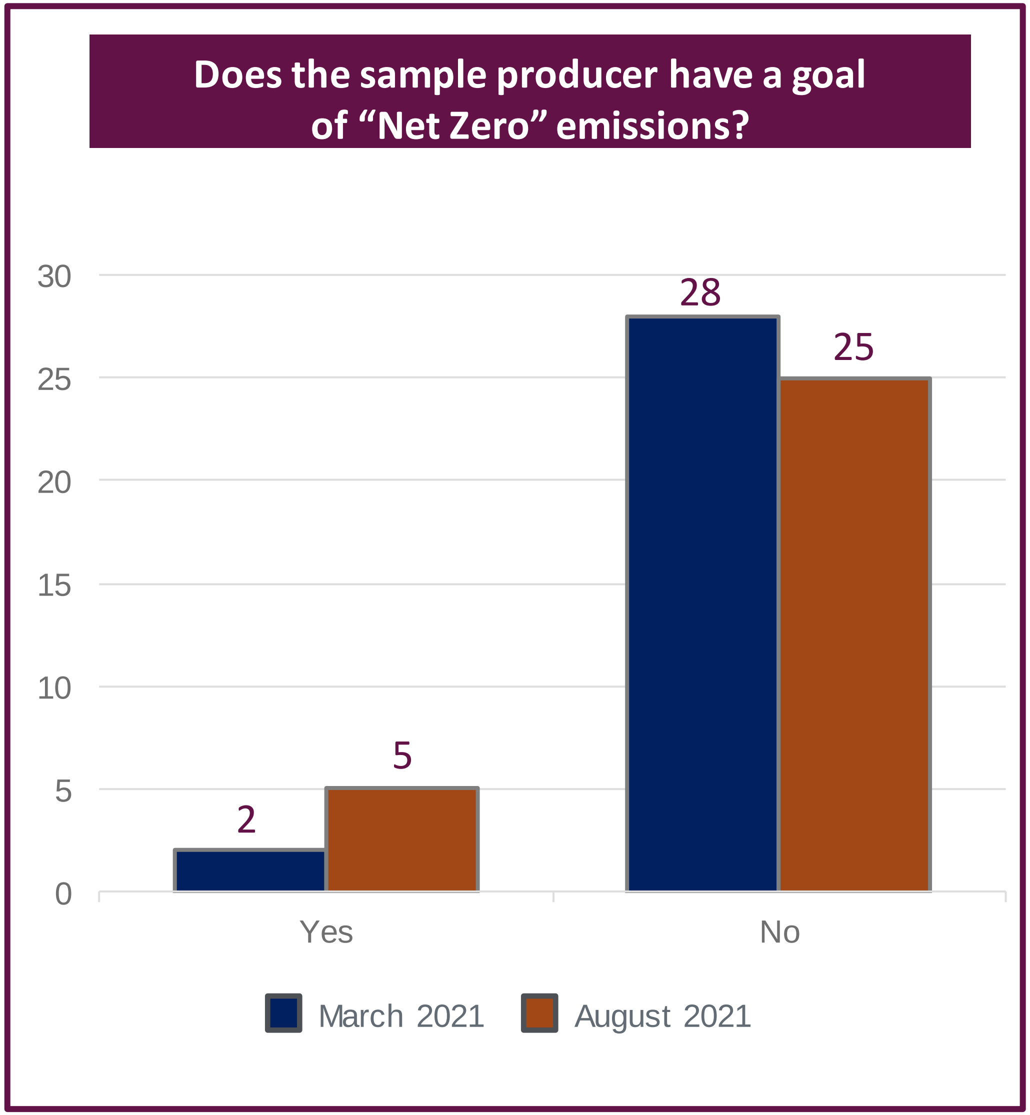
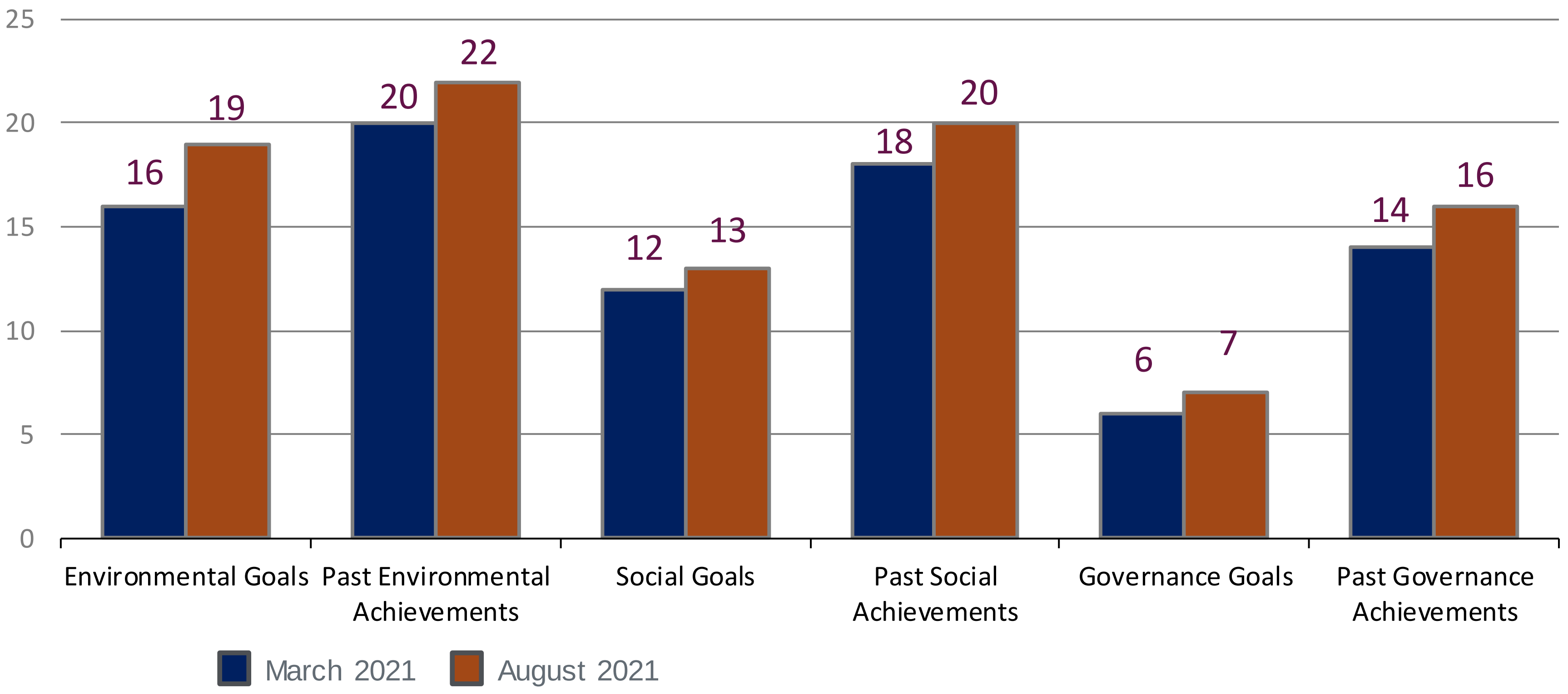
# Analysis of the Sample Producers




- The goal of "Net Zero" emissions is the most significant development, and while we saw a 150% increase in the number of sample producers who have committed to this goal since March 2021, the number remains relatively low.
- Companies generally accomplish these goals by:
  - Technological improvements and operational efficiencies; and
  - Purchase of carbon offsets (e.g., reforestation).
- In July 2021, the SEC Chairman noted that the SEC is scrutinizing "Net Zero" disclosures. The SEC is considering which data or metrics might inform investors about how a company is meeting this requirement.

# Analysis of the Sample Producers

**Does the sample producer report ESG strategies, goals or previous achievements?**

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# ESG and Access to Capital

# General Trend #1

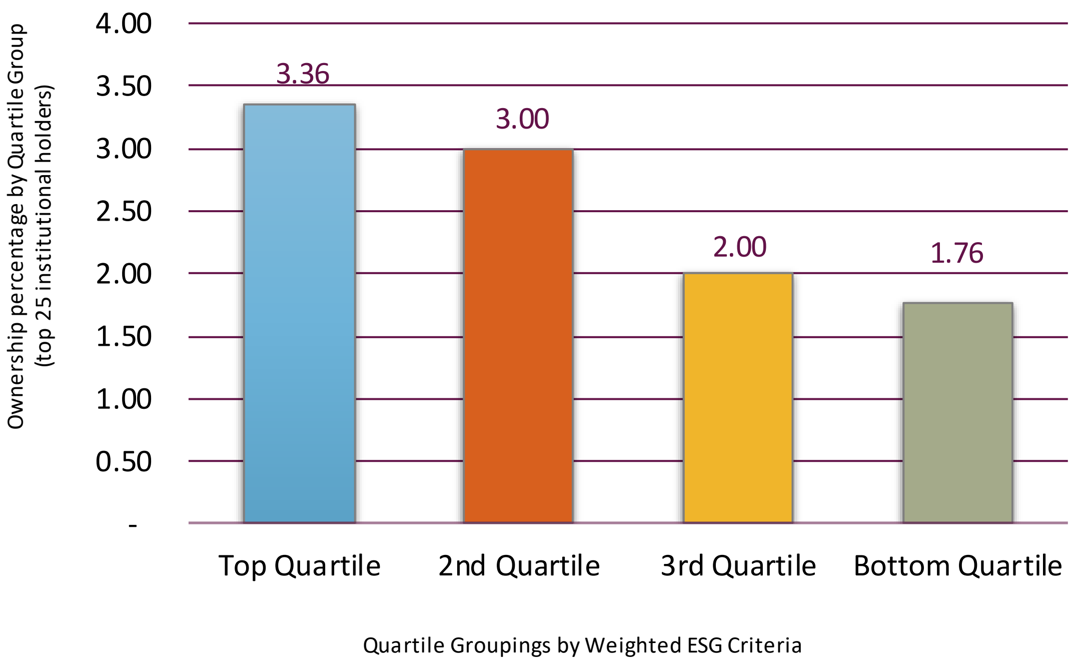
## Significant capital is being invested in funds with an ESG focus. Values increase as a result of stock prices rising.

The top 10 institutional holders of the 30 sample producers that we analyzed have an aggregate of $34.9 billion invested in the equity of the group, and they include:

| Institution | Peers owned | Value (in $ billions) |
|---|---|---|
| VANGUARD GROUP INC | 28 | $9.3 |
| BLACKROCK INC | 28 | $8.5 |
| STATE STREET CORP | 25 | $4.5 |
| CAPITAL GROUP COMPANY | 4 | $2.8 |
| FMR LLC | 18 | $2.3 |
| T ROWE PRICE GROUP INC | 6 | $1.9 |
| DIMENSIONAL FUND ADVISORS LP | 20 | $1.8 |
| GEODE CAPITAL MANAGEMENT LLC | 27 | $1.4 |
| INVESCO LTD | 8 | $1.0 |
| NORTHERN TRUST CORP | 16 | $.9 |

# Top Holders of Sample Producers – Fund Change Observations

Institutional ownership increased in 29 of the 30 equities examined since our previous report in March 2021. The Top Quartile companies are still more widely held but there was more investment in 2nd Quartile companies since our previous report as commodity prices increased.




**Notable institutions adding to positions:**

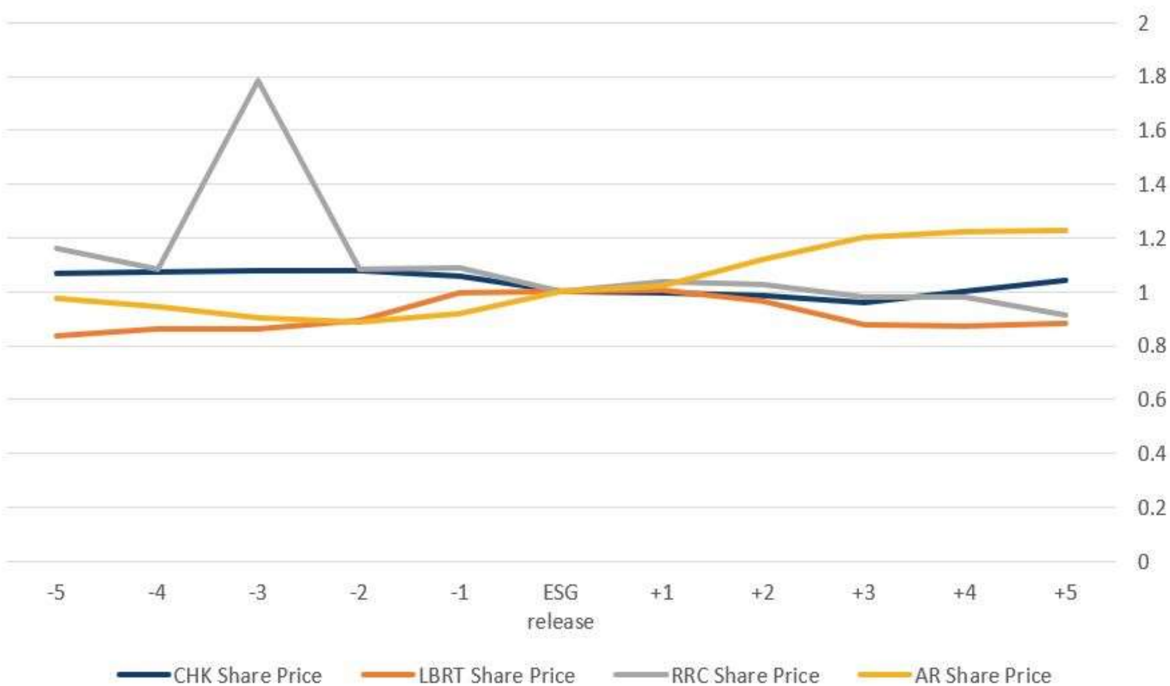
1. Vanguard Group Inc
2. BlackRock Inc
3. State Street Corp
4. T Rowe Price Group Inc
5. Capital Group Cos Inc

**Notable institutions selling positions:**

1. Dimensional Fund Advisors LP
2. FPR Partners LLC
3. JPMorgan Chase & Co
4. Arrowstreet Capital LP
5. Kopernik Global Investors LLC

# ESG is a Cost of Capital Issue

**Stock performance following the announcement of an ESG report varies widely. Releasing a report led to outperformance of a relevant index the day following the announcement in all cases examined; however, it did not always lead to continued outperformance in the five days following the announcement.**




Sample date for Chesapeake Energy (CHK), Liberty Oilfield Services (LBRT), Range Resources (RRC), and Antero Resources (AR) following announcements regarding their ESG reports and how their stock price performed for the five days before and after.

- Some private debt providers are adding ESG metrics into contracts and more attractive interest rates are being provided to companies meeting certain ESG metrics tying them to the cost of capital.
- In some cases, executive compensation is being tied to ESG metrics.
- Despite the emphasis on environmental factors, many investors say that they weight “E”, “S”, and “G” factors equally.
- Investors are sending strong messages to the effect that ESG will need to become a part of a company’s culture; solid ESG performance is an expectation and not necessarily a differentiator.
- An ESG program is not a replacement for operational performance and strong financials.

# ESG is a Cost of Capital Issue

- ESG disclosures may contribute to a company's long-term financial performance and create competitive advantages, including:
  - A broader and more stable investor base
  - A lower cost of capital
  - Improved recruiting and employee engagement
  - Enhanced social license to operate within communities
  - Deeper stakeholder loyalty
- Disclosures also mitigate regulatory costs and open doors to alternative sources of capital.
- Investors use a variety of ESG valuation metrics to evaluate companies.
  - ESG ratings can vary dramatically between rating agencies due to differences in methodology, subjective interpretation, market cap size, etc.
  - Standardizing industry ESG metrics should improve company reporting and lead to a more productive dialogue with the investment community.

# General Trend #2

## Companies looking to raise equity or debt find that investors expect some ESG disclosure.

Twelve of the 30 sample producers we analyzed included ESG highlights in their 2020 proxy statement and seven of those raised capital or engaged in a significant transaction in 2020.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# Proxy Statement Disclosure Trends

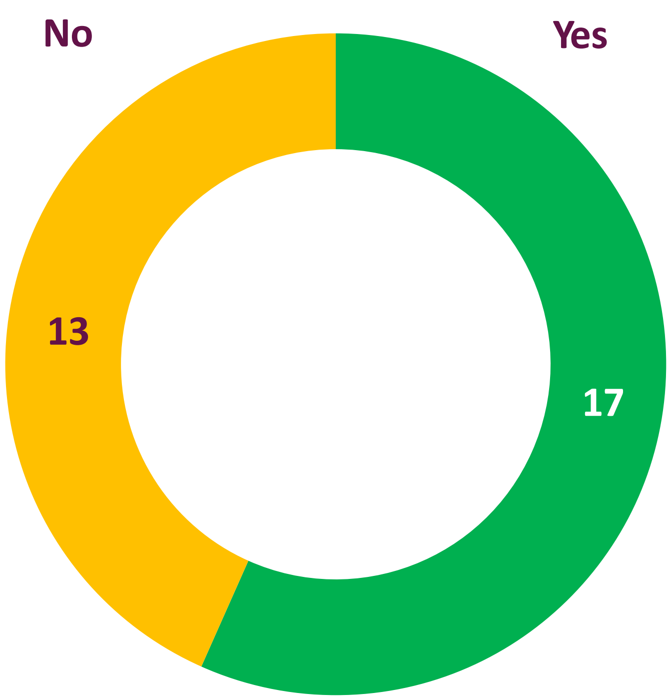
# Introduction

- ESG disclosures in proxy statements (and SEC filings generally) expanded significantly from 2020 to 2021 in line with our inaugural Haynes Boone and EnerCom Oil & Gas ESG Tracker report.
- Companies have begun including ESG disclosures in earnings releases, major announcements and other press releases – indicative that ESG has become a continuing dialogue with investors and other stakeholders.
- The expansion of ESG disclosures is evidence that investors and other stakeholders continue to push for more disclosure.
- However, companies must balance the demand for disclosure with potential liability based on ESG disclosures. Today, the SEC is ***highly*** focused on ESG disclosures:
  - In a July 2021 speech, SEC Chairman Gary Gensler noted that the SEC is scrutinizing ESG disclosures, in particular those relating to "Net Zero" goals.
  - The SEC expects to release proposed rules on climate change disclosures this year, which could include mandatory quantitative and qualitative disclosures.
  - Given the formation of the Climate Change Task Force and SEC commentary in 2021, we expect to see SEC enforcement activity relating to ESG disclosures.
  - Companies should focus carefully on the process of tracking, vetting and reporting ESG disclosures to mitigate potential liability.

# Proxy Statement Disclosure Trend #1

## Sample producers that disclosed ESG highlights did so in the CEO letter and / or the proxy statement summary.

**More than half of the sample producers included ESG highlights in either or both of them**

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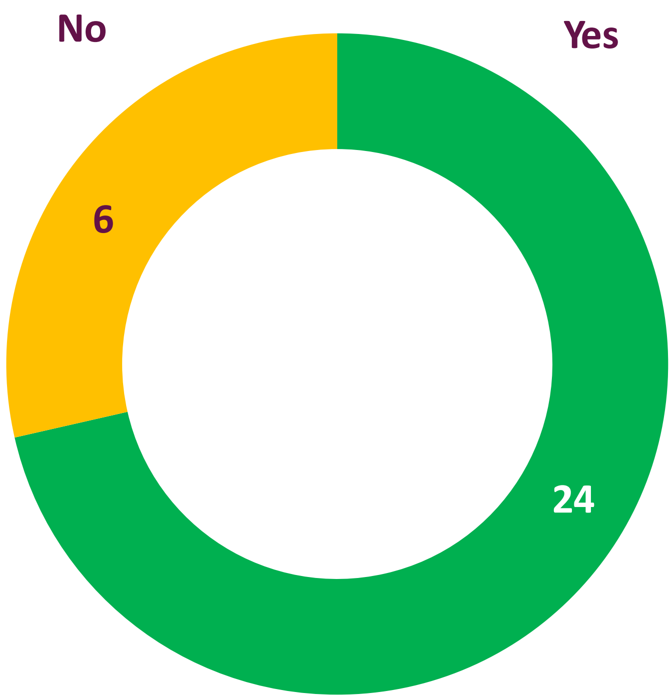
- Companies are including ESG highlights in the CEO letter and the proxy statement summary to showcase their commitment to ESG.
- Five more producers disclosed ESG highlights in these documents since our previous report in March 2021, which is an increase from 40% to 56%.
- These disclosures are given prominence similar to reporting of operating metrics.

# Proxy Statement Disclosure Trend #2

## Sample producers are increasingly disclosing ESG goals and strategies in the proxy statement.

**More than two-thirds of the sample producers included qualitative ESG disclosures in the proxy statement**

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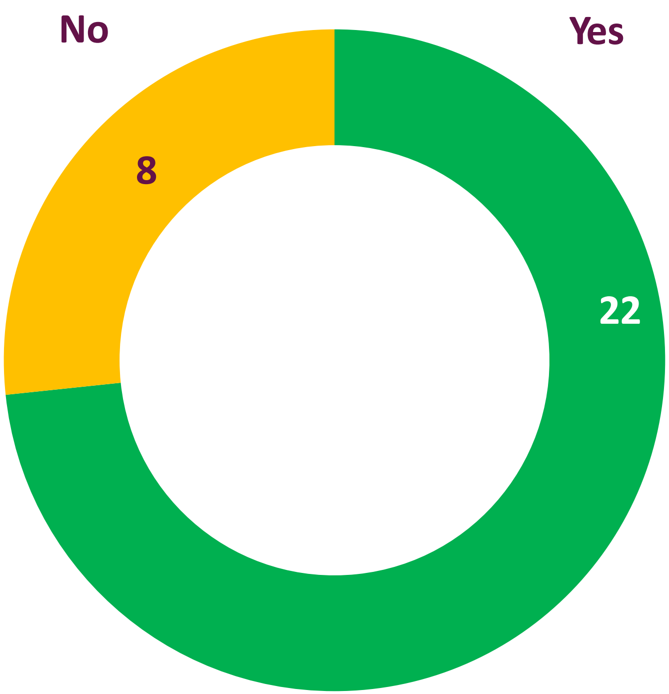
- While a company may include highlights of the ESG strategy in the proxy statement summary, companies also include further discussion of the ESG strategy in their corporate governance discussion.
- These disclosures tend to be high-level, principles-based disclosures.
- Nine more producers have disclosed ESG strategies since our previous report in March 2021, which is an increase from 50% to 80%.

# Proxy Statement Disclosure Trend #3

## Investors are demanding greater disclosure of quantitative metrics.

**More than two-thirds of the sample producers disclosed quantitative metrics in the proxy statement**

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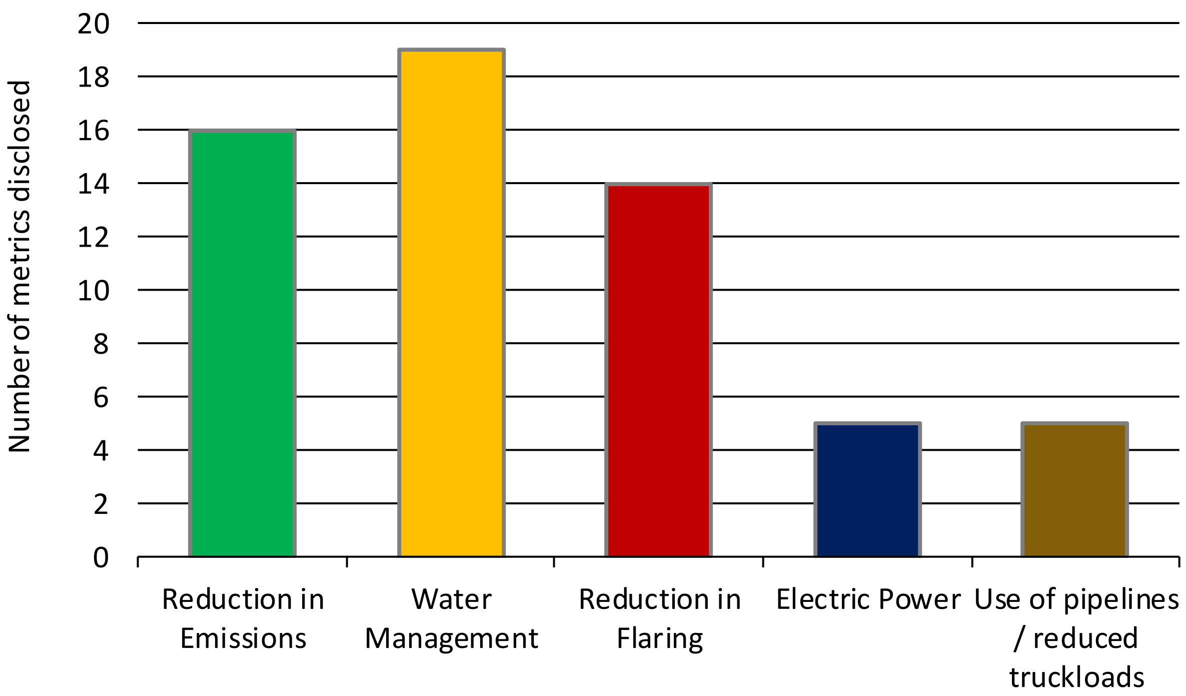
- Investors are pushing for more quantitative metrics, especially those based on a common standard so that they can compare "apples to apples" among different companies.
- This is an important disclosure trend that will evolve, especially as disclosure frameworks and principles become more standardized.
- We also are seeing more companies disclose reporting metrics aligned with TCFD and SASB.
- There has been a significant increase from 16 to 22 producers disclosing quantitative metrics since our previous report in March 2021, which is an increase from 53% to 73%.

# Proxy Statement Disclosure Trend #3 (continued)

## Investors are demanding greater disclosure of quantitative metrics.

### Environmental quantitative metrics disclosed

There was a significant increase in the number of producers reporting environmental quantitative metrics and the number of metrics disclosed, with 20 of the sample producers disclosing a total of 67 environmental metrics. The most common types of environmental metrics are summarized below.




Sample disclosures:

- "We reduced our GHG emissions by X% compared to the prior year."
- "We recycled X% of the water recovered in drilling."
- "We had zero flaring in our operations in 2020."
- "We decreased our spill rate by X% in 2020."
- "We exclusively used an electric frac fleet."

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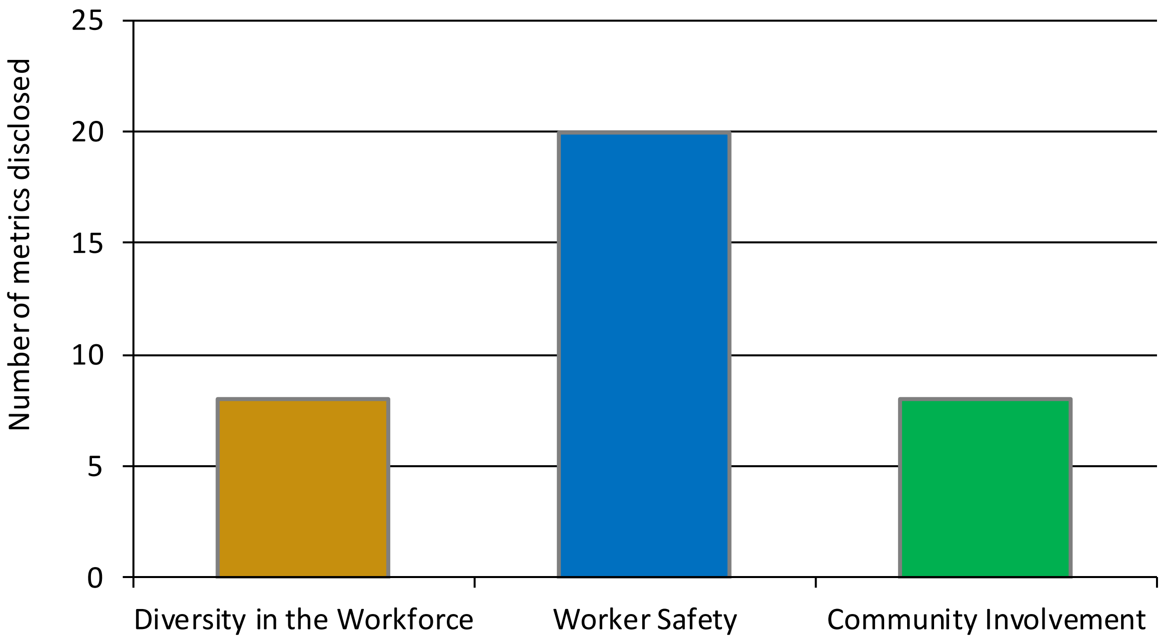
# Proxy Statement Disclosure Trend #3 (continued)

## Investors are demanding greater disclosure of quantitative metrics.

**Social quantitative metrics disclosed**

Fourteen producers disclosed an aggregate of 37 quantitative metrics in the "Social" category. The most common were worker safety, diversity in the workforce and community involvement. These metrics reflect the current focus on diversity as well as safety, especially during the COVID-19 pandemic.




Sample disclosures:

- "X% of our workforce is ethnically or racially diverse."
- "Our lost time incident rate in 2020 was X."
- "We donated $X to a charity."
- "We logged X hours in worker safety training in 2020."

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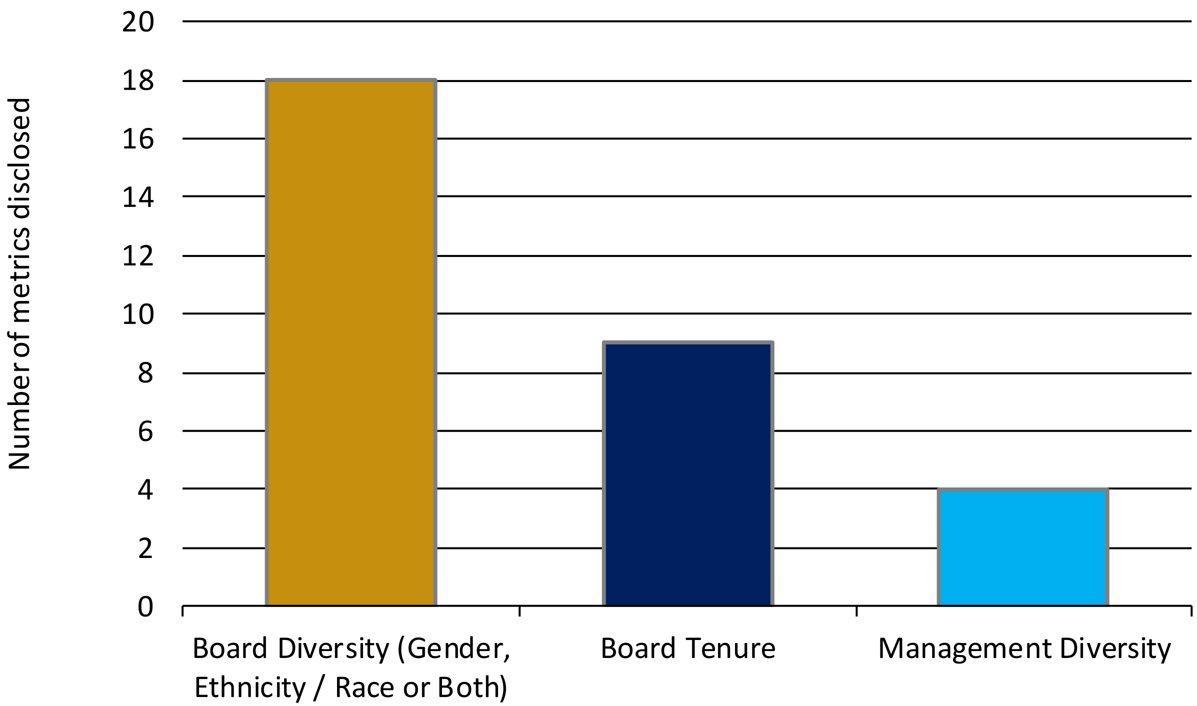
# Proxy Statement Disclosure Trend #3 (continued)

## Investors are demanding greater disclosure of quantitative metrics.

### Governance quantitative metrics disclosed

Fourteen sample producers disclosed an aggregate of 31 governance quantitative metrics. The most common metrics disclosed were related to board diversity or board tenure.




Sample disclosures:

- "X% of our directors are female."
- "X% of our directors are ethnically or racially diverse."
- "The average tenure of our directors is X years."

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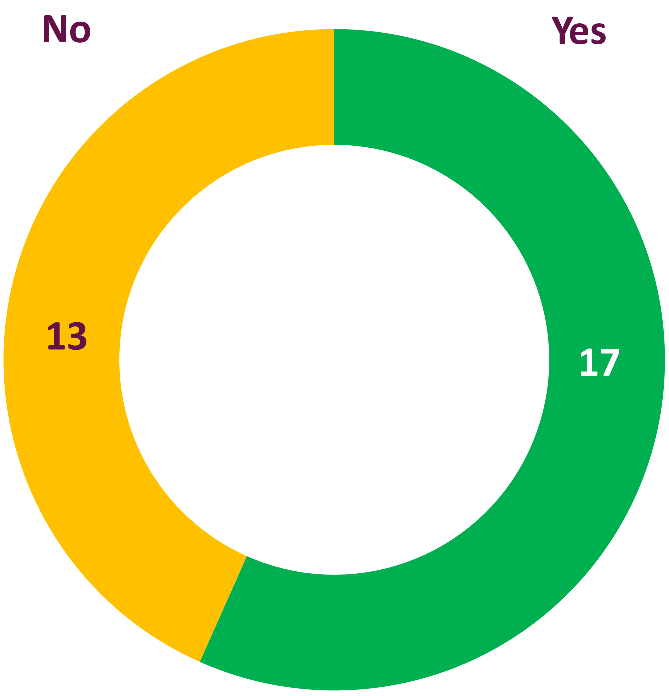
# Proxy Statement Disclosure Trend #4

## Companies are disclosing details of stockholder engagement efforts relating to ESG.

**Seventeen of the sample producers discuss engagement on ESG, with 11 of those disclosing specific changes based on stockholder concerns**

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- The majority of companies disclose specific shareholder engagement activities related to ESG.
- More than one-third of sample producers disclosed specific investor requests and the company's response.

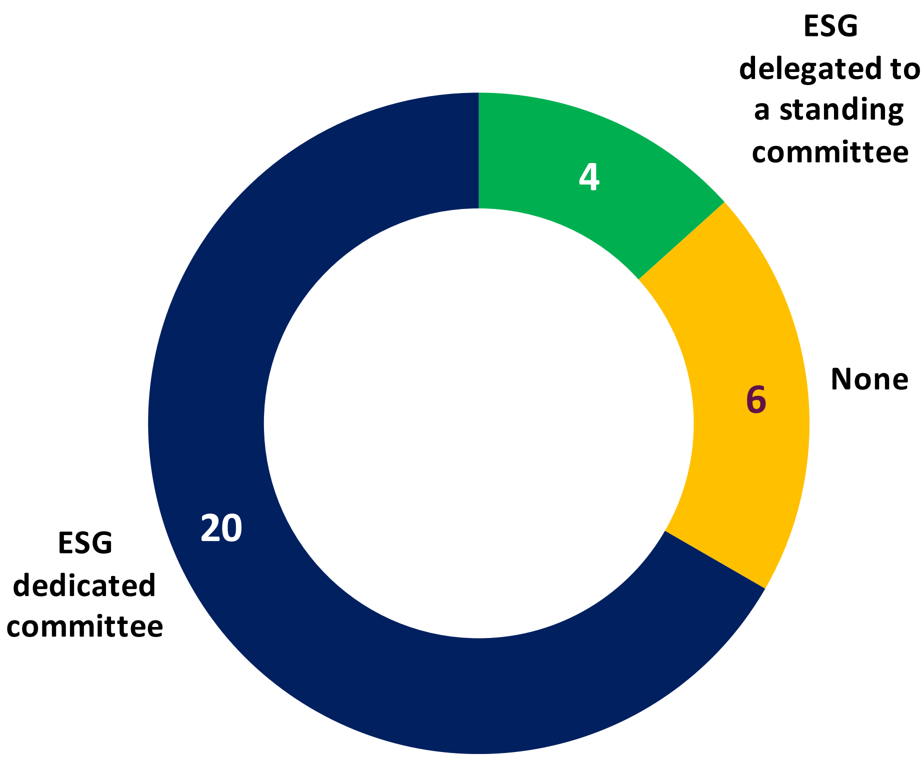
Sample responses:

- "We published our inaugural ESG report in March 2021 based on stockholder requests."
- "We formed an ESG committee in response to stockholder requests."

# Proxy Statement Disclosure Trend #5

## Boards are forming a committee dedicated to ESG oversight.

**Two-thirds of the sample producers have an ESG-dedicated board committee, which is a 100% increase from our previous report in March 2021**

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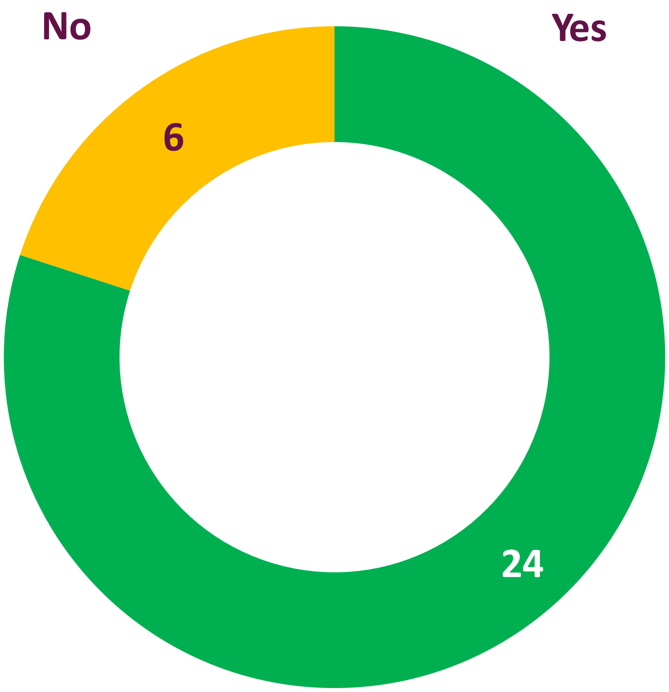
- More producers have formed a board committee dedicated to ESG matters (10 more than in our previous report).
- Four companies delegate ESG oversight to the Nominating and Governance committee.
- A few producers dedicated an entire page of their proxy statement to ESG governance and oversight.

# Proxy Statement Disclosure Trend #6

## Companies are incorporating ESG metrics into performance targets.

**More than two-thirds of the sample producers included ESG performance metrics in their proxy statement**

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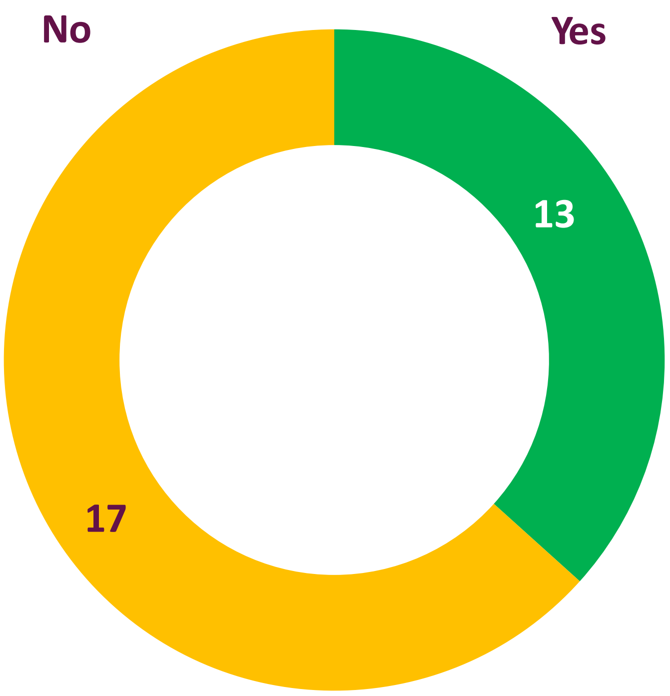
- More producers are incorporating ESG metrics into performance targets because investors want to see that executives are incentivized to make progress toward ESG goals.
- Investors are very focused on ESG-related performance metrics.
- Some companies use quantitative metrics, including a scorecard, while others measure a discretionary element.
- For example, in Compensation Discussion and Analysis (CD&A), companies may disclose that the annual performance bonus amount may be adjusted up or down within a range depending on certain ESG metrics.
- The number of sample producers including this disclosure increased from 17 to 24.

# Proxy Statement Disclosure Trend #7

## Sample producers are including ESG skills in a director skills matrix.

**Nearly half of the sample producers have a skills matrix mentioning ESG**

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- Investors have asked for more disclosure on director skills, including ESG, because they want to know that the board has the right skills to effectively manage ESG oversight.
- Although not required, many companies include a director skills matrix to the proxy statement, showing the particular skills of each director, including ESG skills.

# Key Takeaways

- We anticipate more robust ESG disclosures due to growing pressure from stakeholders, investors and regulators.
- 83% of sample producers have an ESG policy.
- Water programs, volatile organic compounds (VOC), methane and CO2 emissions are key environmental issues noted in disclosures while executive compensation and diversity are important components of corporate governance.
- Only 5 of 30 sample producers have a goal of "Net Zero" emissions but many that report GHG emissions also commit to further reductions of direct GHG emissions.
- Companies are more likely to quantify ESG accomplishments (e.g., board diversity, water usage reductions and community investments) than make express commitments to quantifiable ESG goals, but we anticipate more companies will begin disclosing specific targets and goals.
- Companies not yet disclosing ESG policies should consider the pros and cons of such disclosures and commitments moving forward.

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