Marathon Petroleum Corporation (MPC)
Proposal No. 10 – Shareholder proposal seeking an audited report on asset retirement obligations
Proponent: State of New Jersey Common Pension Fund D
Memo submitted by: KBI Global Investors. Contact Jeanne Collins (jeanne.collins@kbigi.com)

SUMMARY
Expansive goals to reach net zero emissions by 2050 will radically alter the global energy profile. Consequently, oil and gas assets built at a time when they could be expected to operate indefinitely must be reevaluated to consider this shift. If those assets cease to provide sufficient revenue, they will need to be retired and the associated legal liabilities could be material yet are unknown to investors. Disclosure of what those costs would be today, gives investors actionable information to assess long term value. KBI Global Investors, as shareholders of Marathon Petroleum Corporation, submit this memo as it aligns with our engagement priorities with the Company.

RESOLVED CLAUSE
Shareholders request Marathon Petroleum Corporation's Board of Directors issue an audited report to shareholders that contains the undiscounted expected costs to settle obligations for AROs with indeterminate settlement dates. The Board should obtain and ensure publication of the report by February 2024 at reasonable cost and omitting proprietary information. To allow maximum flexibility, nothing in this resolution shall serve to micromanage the company by seeking to impose methods for implementing complex policies in place of the ongoing judgment of management as overseen by its Board of Directors.

SUPPORTING STATEMENT
In the Board and management's reasonable discretion, we recommend such report also include: (1) a range of potential settlement dates based on each asset's estimated economic life, (2) probabilities associated with the potential settlement dates, with due consideration given to the potential impact of the energy transition away from fossil fuels, and (3) whether, based on known information, it is reasonably possible that these assumptions and estimates will change in the near term.

RATIONALE FOR SUPPORT OF THIS RESOLUTION
1. Asset Retirement Obligations could present a material risk to investors in the energy transition. This disclosure will provide insight that is decision useful as investors assess long term value and is consistent with U.S. GAAP.
2. Information related to AROs (aka decommissioning) is reported by peers.
3. Disclosure of this information is consistent with TCFD guidance and has strong investor support.

Asset Retirement Obligations could present a material risk to investors in the energy transition. This disclosure will provide insight that is decision useful as investors assess long term value and is consistent with U.S. GAAP.

The energy transition underway necessitates that energy companies re-evaluate assets to understand how each asset will contribute to a low carbon economy. Marathon Petroleum Corporation relies on substantial revenues from products related to transportation, a sector which is undergoing a rapid transformation to electrify, likely dampening the market for gasoline, diesel, and motor oil.

This resolution is seeking the disclosure of the <u>undiscounted value</u> of AROs, which can be assessed separately from any assumption relating to the asset life. There are widely different views of how the energy transition may unfold, and this information will allow investors to make their own assessment of the timing for when those liabilities may come due, which may differ from the company's projections. The resolution is not asking the company to change judgements on timing, but to disclose information that the Company (and its auditors) should be prudently scrutinizing as a matter of course.

While the Company maintains that reporting of the undiscounted cost to settle ARO's is contrary to US GAAP, guidance from leading audit firms, including the Company's own auditor, differ and indicate that this information "should be accounted for".

The Company states that the disclosure sought is:

> "(A)n alternate accounting standard advocated by the proponent that our management and independent auditors have determined would be contrary to US GAAP in the context of the specific facts and circumstances applicable to us."[1]

To the contrary, the Company auditor, PwC furnishes guidance on disclosure of AROs:

> "ASC 410-20-25-7 states that the legal obligation to perform an asset retirement activity is unconditional even when uncertainty exists about the timing or method of settlement. For example, the settlement date and method of settlement for an obligation may have been specified by others through law, regulation, or contract that gives rise to the legal obligation but provides various methods of settlement, each of which would be acceptable. Therefore, **even if the timing or method of settlement is uncertain and may be conditional on a future event, an unconditional obligation exists and should be accounted for in accordance with ASC 410-20**. See PPE 3.4.3.2 for guidance on the recognition and measurement of conditional AROs."[2] (emphasis added)

Deloitte as well notes the responsibility of companies to measure asset retirement obligations, regardless of uncertainty of timing:

Deloitte:

> "An obligation to perform asset retirement activities in unconditional, and an ARO should be measured and recognized regardless of whether (1) there is uncertainty about the timing or method of settlement or (2) such timing and method of settlement are conditional on a future event. "[3]
>
> "We believe that entities would typically have sufficient information to estimate a range of potential settlement dates, the potential methods of settlement, and the related probabilities on the basis on an analysis of the factors listed above. It would not be appropriate for an entity to delay recognition of the liability merely on the basis that management does not intend to perform the asset retirement activities in the foreseeable future. ASC 410-20-25-8 clarifies that the timing of liability recognition under ASC 410-20 should not be based on when the retirement activities are probable of being performed (as ASC 450 approach); rather, any uncertainty with respect to timing of settlement should be incorporated into the measurement of the obligation. An entity that believes that it lacks sufficient information to reasonably estimate the fair value of an ARO liability must have evidence to support that assertion. For example, evidence may include a history of indefinitely extending the economic lives of other long-lived assets that are the same as or similar to the assets under the related ARO by regularly repairing and maintaining the assets. In the rare circumstances in which sufficient information does not exist, and entity must disclose that fact and the reasons why an estimate could not be made, in accordance with ASC 410-20-50-2.
>
> Under ASC 410-20-25-6, an entity is also required to identify all ARO's. Therefore, it would be inappropriate for an entity to assert that the information to reasonably estimate fair value is insufficient simply because a thorough inventory of existing AROs has not been compiled."[4]

While the fair value of an ARO cannot be reasonably estimated in the context of the unknown duration of the useful life of the asset, the *current undiscounted value* of AROs should be a value the company is monitoring and can provide to investors.

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[1] MCP 2023 Proxy, p.81. https://www.sec.gov/ix?doc=/Archives/edgar/data/1510295/000151029523000028/mpc-20230313.htm

[2] PwC Viewpoint, https://viewpoint.pwc.com/dt/us/en/pwc/accounting_guides/property_plant_equip/property_plant_equip_US/Chapter_3_Asset_retirement_obligations/3_2_Scope_of_the_ARO_guidance.html#pwc-topic.dita_b16e2d34-c61f-4b3a-943e-0b019f40c534-tOp-S

[3] Deloitte Roadmap: Environmental Obligations and Asset Retirement Obligations (September 2022), p. 81. https://dart.deloitte.com/USDART/home/publications/roadmap/environmental-obligations-aro

[4] Deloitte Roadmap: Environmental Obligations and Asset Retirement Obligations (September 2022) p.83

Information related to AROs (aka decommissioning) is reported by peers.

The foundation of this request is that asset lives that were once considered indeterminate may, with the energy transition, have finite lives. The legal obligation to retire those assets would in that case come due. The resolution does not ask for the Company to determine an end life date, but instead asks for an “audited report to shareholders that contains the undiscounted expected costs to settle obligations for AROs with indeterminate settlement dates” which would be the amount to settle those liabilities today. Investors could then make their own assessment of when those liabilities might come due.

The Company maintains that “industry practice” is that AROs for assets with indeterminate lives are unreported. We agree and maintain this practice is an accounting loophole that has been exploited to obscure off balance sheet liabilities that may be material. Some companies are reporting the undiscounted cost of asset retirement obligations, and some jurisdictions are requiring bonding provisions[5] [6] for reported upstream AROs to avoid shouldering the burden of these liabilities in the future.

bp, in the 2021 Annual Report includes undiscounted estimates of decommissioning and environmental liabilities as shown in this excerpt[7]:

			$ million
			Payments due by period
Expected payments by period under contractual obligations	Less than 1 year	More than 1 year	Total
Balance sheet obligations			
Borrowings[a]	6,867	64,698	71,565
Lease liabilities[b]	1,949	8,076	10,025
Decommissioning liabilities[c]	615	23,182	23,797
Environmental liabilities[c]	273	1,659	1,932
Gulf of Mexico oil spill liabilities[d]	1,287	11,883	13,170
Pensions and other post-retirement benefits[e]	822	13,208	14,030
	11,813	122,706	134,519

than 1 year $1,178 million)

[c] The amounts presented are undiscounted.

[d] The amounts presented are undiscounted. Gulf of Mexico oil spill liabilities are included in the group balance sheet, on a discounted basis, within other payables. See Financial statements – Note 21 for further information.

[e] Represents the expected future contributions to funded pension plans and payments by the

In addition, the bp 2021 Annual Report describes the process for assessing recoverability[8], and how the audit committee considered decommissioning liabilities:

> “The committee reviewed the process for estimating decommissioning liabilities for our operation, in particular for oil and gas property, plant and equipment, and challenged the assumptions used in

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[5] https://cogcc.state.co.us/documents/media/Fact_Sheet_FA_Rulemaking_20220301.pdf

[6] https://carbontracker.org/shining-a-light-on-colorados-financial-assurance-plans/

[7] bp Annual Report and Form 20-F, 2021, p. 343, https://otp.tools.investis.com/clients/uk/bp_plc1/SEC1/sec-show.aspx?Type=html&FilingId=15669032&CIK=0000313807&Index=10000

[8] bp annual report and Form 20-F 2021 https://www.bp.com/content/dam/bp/business-sites/en/global/corporate/pdfs/investors/bp-annual-report-and-form-20f-2021.pdf (p. 112)

determining the same, including the anticipated time period over which decommissioning liabilities were expected to be incurred in respect of the pace of transition to a low carbon economy and the alignment of bp's aims and ambitions to 2030, particularly with respect to refineries. The committee also assessed the process for monitoring decommissioning reversion risk."[9]

bp's independent auditor, Deloitte, noted decommissioning costs as a key audit matter, challenging managements judgment that decommissioning provisions are not required for refineries as their decommissioning date is indeterminate.[10]

Shell's 2022 financial report recognizes that the energy transition may impact decommissioning and restoration assumptions. Shell accelerated the assessment of the discount rate from a 30-year term to a 20-year term and recognizes the undiscounted provision at $33 billion.

> "The energy transition may result in decommissioning and restoration occurring earlier than expected. The risk on the timing of decommissioning and restoration activities for Integrated Gas and Upstream fields is limited, supported by production plans in the foreseeable future (see "Estimated useful life" above). Acceleration of decommissioning and restoration activities has also been reflected in the assessment of the appropriate discount rate. In 2021, the discount rate was revised from a 30-year to a 20-year term in line with the average remaining life of Integrated Gas and Upstream assets. On an undiscounted basis the provision for decommissioning and restoration as at December 31, 2022 was $33 billion, recognised on a discounted basis in the Consolidated Balance Sheet as at December 31, 2022 at $20 billion (2021: $22 billion). Sensitivity to changes in the discount rate is provided in Note 24. In Chemicals and Products, it was industry practice not to recognise decommissioning and restoration provisions associated with manufacturing facilities. This was on the basis that these assets were considered to have indefinite lives, so it was considered remote that an outflow of economic benefits would be required. In 2020, Shell considered the changed macroeconomic fundamentals, together with Shell's plans to rationalise the Group's manufacturing portfolio. Shell also reconsidered whether it remained appropriate not to recognise decommissioning and restoration provisions for manufacturing facilities. Since 2020, decommissioning and restoration provisions are recognised for certain shorter-lived manufacturing facilities (see Notes 24 and 31). The remaining five energy and chemicals parks are considered longer-lived facilities that are expected to be resilient in the energy transition, and decommissioning would generally be more than 50 years away."11

Marathon Oil's 2021 Sustainability Report explains that a sensitivity analysis on current ARO liability which reduced asset lives for 10 years, revealed a potential increase in liability from 2% to 3% of net PP&E.[12]

Eni's 2021 Annual Report includes estimates of future development and decommissioning costs of €32.2 billion, undiscounted.[13]

Disclosure of this information is consistent with TCFD guidance and has strong investor support.

The request to disclose this information is also consistent with guidance from Task Force on Climate-related Financial Disclosures (TCFD). The Company notes that its reporting is guided by the TCFD framework, which many investors support. TCFD guidance suggests that companies disclose the potential impacts of climate-related risks on the organizations business where such information is material including a description of the "climate-related issues on their financial performance (e.g., revenues, costs) and financial position (e.g., assets, liabilities)."[14] Supplemental

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[9] bp 2021 (p. 110)

[10] bp 2021 (p. 147)

[11] Shell Annual Report and Accounts 2022, https://reports.shell.com/annual-report/2022/_assets/downloads/shell-annual-report-2022.pdf. p. 260.

[12] MRO 2021 Sustainability Report, p. 4. https://cdn.sanity.io/files/ghcnw9z2/website/12352ad93f64eb31f82b3e7cc0ba445a65879eba.pdf

[13] Eni Annual Report 2021, p. 132, https://www.eni.com/assets/documents/eng/reports/2021/Annual-Report-2021.pdf

[14] TCFD 2021 https://assets.bbhub.io/company/sites/60/2021/07/2021-TCFD-Implementing_Guidance.pdf (p. 58)

guidance for non-financial groups encourages disclosure around climate-related future activities such as restructuring, write downs, or impairment of assets; critical planning assumptions around legacy assets; and flexibility in positioning/repositioning capital to address emerging climate-related risks and opportunities.[15] For energy companies, the TCFD notes that transparent and decision-useful climate-related disclosures including "exposure to regulatory changes or changing consumer and investor expectations (e.g., expansion of renewable energy in the mix of energy supply)" are crucial to understanding climate impacts.[16]

In 2022 shareholders at ExxonMobil[17] and Chevron[18] showed solid support for a resolution seeking an audited report assessing the financial impact of the IEA NZE assumptions, including future asset retirement obligations, underscoring the importance of this disclosure to investors.

Disclosure of ARO costs is consistent with current accounting standards, peer practice and investor expectations, and should be addressed by companies such as Marathon Petroleum Corporation who are not currently transparent about this off balance sheet liability.

Accordingly, we urge you to vote FOR proposal No. 10 – shareholder proposal seeking an audited report on asset retirement obligations on Marathon Petroleum Corporation's proxy card.

[15] TCFD (p.59)

[16] TCFD (p. 64)

[17] ExxonMobil 8-k, Proposal #8, votes cast For = 51.0%.
https://www.sec.gov/ix?doc=/Archives/edgar/data/0000034088/000003408822000034/xom-20220525.htm

[18] Chevron 8-k, proposal #6, votes cast For = 38.7%. https://www.sec.gov/ix?doc=/Archives/edgar/data/93410/000009341022000035/cvx-20220525.htm