Natural Resource Governance Institute

Carbon Tracker Initiative

Responsible Exit Principles for Oil and Gas Companies



Acknowledgements

These Principles have been prepared by Mike Coffin on behalf of Carbon Tracker Initiative, Nicola Woodroffe and Erica Westenberg on behalf of the Natural Resource Governance Institute, and Karina Litvack.

They have benefited from consultation with over 100 stakeholders from the oil and gas industry, investors, the financial, legal and accounting professions, the insurance industry, standard-setting bodies, academia and civil society.

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Preamble

These Responsible Exit Principles for Upstream oil and gas operators have been produced with one very clear objective: to respond to regulatory gaps left by inconsistencies between different jurisdictions regarding the operational and governance standards that sellers and buyers must uphold when assets change hands. These Principles, which are necessarily not one-size-fits-all, are intended to guide best practice and serve the shared interests of industry and a broad array of stakeholders, including host governments and communities, in ensuring an orderly transition to a low-GHG and climate-resilient economy.

Our hope and intention are that these Principles serve as a constructive starting point for regulatory reform, by articulating a set of best practice standards to manage operational, legal, regulatory and reputational risk. We therefore invite oil and gas companies, their shareholders, lenders, insurers, legal advisors, as well as governments, civil society and broader stakeholders, to come together to critique and offer improvements to this framework where needed.

Why Now?

Asset disposals have taken place for as long as the industry has existed, and yet their relevance has gained heightened attention of late as oil and gas companies, spurred by their financial and other stakeholders to reinvent themselves in the face of the climate crisis and the energy transition, increasingly rely on M&A to meet greenhouse gas reduction targets, sometimes with the virtuous intention of redeploying capital towards a strategic pivot into clean energy technologies.

Why might this be a concern? Quite simply because while transferring assets, and the emissions associated with them, may eliminate them from the seller's balance sheet, they have not disappeared: they have merely been displaced – often to operators who can evade the harsh scrutiny imposed on the large, listed majors. And it is here that the race to curb emissions can go off track, as new owners often increase production and may take risks that their previous owners would not tolerate.

This poses a risk to sellers as well—in some jurisdictions they retain legal obligations to decommission transferred assets when current operators fail to; other jurisdictions where such requirements do not exist are considering imposing such liability.

Important research by Ceres and the Environmental Defense Fund[1] has documented how operational standards have tended to decline and emissions to increase in the wake of such transfers. These Principles therefore seek to set out a clear set of minimum best practice standards to avert this risk and give responsible buyers and sellers confidence in transferring assets consistent with reducing economy-wide emissions and protecting and enhancing long-term value. At the same time, the Principles seek to establish a basis for harmonizing regulatory practice across the global industry.

1. Gabriel Malek, Andrew Baxter, Dominic Watson and Andrew Howell, "Transferred Emissions: How Risks in Oil and Gas M&A Could Hamper the Energy Transition," *Environmental Defense Fund* (2022), https://business.edf.org/insights/transferred-emissions-risks-in-oil-gas-ma-could-hamper-the-energy-transition/.

A Tool for Improved Practice

Sellers and their financial advisors have rightly warned that the market for asset disposals is often not a deep one to begin with, and that overly stringent standards may therefore further harm liquidity by disqualifying potential buyers and thereby harming sellers. Valid though such concerns are, this cannot be a reason to accept that weak transfer/sales conditions compromise the integrity of either day-to-day operational standards or the pathway to achieving Net Zero Emissions by 2050. The overriding goal of these Principles is therefore to drive the adoption of better practices across the industry, by incentivising buyers to lift standards in order to compete more effectively for assets.

Moreover, a drive to profit from short-term transactions may leave ageing infrastructure abandoned and spur calls for further regulatory reform, resulting in potential trailing liabilities being enforced or imposed on previous owners. Adhering to such standards will therefore reduce operational, legal and reputational risk for both parties to the transfer, which prudent managers and boards will value. But such commitments also cost money upfront, and as such, may result in lower asset valuations as the full cost of clean-up and alignment with a Net Zero Emissions pathway are internalised in the sale price: boards will need to take stock of these changing dynamics, and, consistent with their fiduciary duty to act in the long-term best interest of their companies and shareholders, be prepared to support their management in making the right decisions.

These Principles therefore aim to serve as the *de facto* best practice standard that sellers should seek of their counterparties via their contracts of sale, and buyers should strive to adopt across their operations; that shareholders, lenders and insurers should expect of their investee companies and clients; that independent auditors should assess in their audits of both processes and financial reporting; that legal and other professional advisors should incorporate into their advice, including by building them into the contractual provisions contained in Sales and Purchase Agreements; and that national governments can use to strengthen existing laws and regulations governing asset transfers and decommissioning, where needed.

Until such time, that is, that regulations catch up and build such standards into the rule book, thereby making these voluntary Principles obsolete.

Karina Litvack



Photo by Berkut_34 for Getty Images (via Canva)

Introduction

The Climate Emergency and the Risk of Unintended Consequences

Meeting the goal of the Paris Agreement[2] of "holding the increase in global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C" requires global emissions to fall rapidly from today, reducing by about 45% from 2010 levels by 2030 and reaching net zero around 2050. Accordingly, companies, particularly large emitters, are under pressure to decarbonise, by setting – and subsequently pursuing – "net zero" targets and Paris-aligned corporate transition plans.

A key component of reducing emissions and stabilising temperature rise is significantly reducing fossil fuel consumption, with energy systems transitioning to low- or zero-carbon alternatives. Technology development, supported by hard and soft climate policy measures, including the UAE Consensus[3] at COP28 to transition away from fossil fuels, should therefore see increased displacement of fossil fuels.

Achieving the Paris Agreement's goal thus sees oil and gas consumption volume falling significantly over the next decade. With reduced demand for new developments, individual producers will likely be differentially impacted given the relative competitiveness of their project options;[4] most producers would see their production fall under such a scenario.

Limiting warming to 1.5°C and avoiding the worst impacts of climate change requires this transition to happen rapidly, with little, if any, space for new oil and gas developments (e.g. as detailed in the IEA's Net Zero Emissions by 2050 Scenario, NZE), with production from existing projects declining naturally without further extension.

Yet many oil and gas companies continue to invest in developing new projects, either because of a view that demand will remain sustained despite the strengthening headwinds of science-driven policy and technology evolution; or because despite acknowledging the general downward trend in demand, they believe ongoing investment in new fields is still compatible with overall emissions reduction targets, so long as older, more carbon-intensive assets are swapped out.

However, if Upstream assets (described in Box 1) are transferred to producers with a less ambitious emissions reduction strategy, whether on operational CO2 and methane emissions or production volumes, then such transfers could result in an increase in emissions at the global level, in addition to the additional emissions locked-in by the new developments.[5]

2. This is the original language of the Paris Agreement (November 2015), which we note included a commitment to further research the temperature limit. That research, published by the IPCC in October 2018 highlighted the need to limit warming to 1.5°C, with the goals of the Paris Agreement generally accepted to be updated accordingly to focus on limiting warming to 1.5°C.
3. The UAE Consensus was set at COP28 to keep 1.5°C "within reach" incorporating the first Global Stocktake. See: "The UAE Consensus Foreword," *COP28 UAE*, accessed 13 September, 2024, https://www.cop28.com/en/the-uae-consensus-foreword.
4. Carbon Tracker has published a series of reports looking at the relative competitiveness of companies' portfolio of project options, using its least-cost methodology, most recently in: Maeve O'Connor, "Paris Maligned II," (2024), https://carbontracker.org/reports/paris-maligned-2/.
5. See: Malek et al., "Transferred Emissions: How Risks in Oil and Gas M&A Could Hamper the Energy Transition".

Box 1

Oil and gas asset overview

Upstream

- **Exploration acreage** which gives the licence to explore for oil and gas, and may include existing exploration and appraisal wells, which may or may not have been fully decommissioned ("abandoned") despite potential legal obligations to do so.
- **Production assets**, including platforms/facilities and associated wells and pipelines.

Midstream:

- Pipelines for crude oil, natural gas and refined products.
- Crude and product tankers.

Downstream

- **Refining** assets, which may be co-located with chemicals plants as part of a petrochemical complex, producing a range of products including fuels, lubricants, chemical feedstocks.
- **Marketing** assets, including petrol/gasoline stations and aviation supply assets.

In addition, some companies may own **power generation** assets.

The Need for Responsible Exit Principles[6]

As the energy transition progresses, oil and gas companies are increasingly being challenged by investors to reposition their business models, for two main reasons.[7]

First, to maintain and enhance value through the transition to a decarbonised global economy, by reducing exposure to energy transition risks; particularly declining long-term oil and gas demand, and associated declining commodity prices, and the consequent impact to both the viability of new developments and expected revenues from existing production assets.

Second, to reduce the negative spillover impacts on the rest of their portfolios arising from oil companies' activities on nature and the environment – particularly in relation to extreme climate-driven weather events. This concern is particularly felt by investors with large highly-diversified portfolios – i.e. so-called *Universal Owners* – which are exposed to systemic climate-related risks affecting the broad economy, insofar as the medium- and long-term negative economic impacts of unabated climate change have been consistently found to far exceed the near-term costs of investing in mitigation.[8] And is especially a concern for those with obligations to guarantee a stable retirement and other long-term payouts, e.g. pension plans and life assurance providers.

6. We note that the international normative framework for Business and Human Rights (BHR)/Responsible Business Conduct (RBC) (e.g. OECD Guidelines and UNGPs) requires "responsible exit". However, these requirements are focused on human rights and other social factors, rather than the extent to which actions are Paris-aligned. Here we take a broader view of what constitutes "responsible exit".
7. See: Mike Coffin, "Oil and Gas Transition Plans: A User Guide," *Carbon Tracker* (2024), https://carbontracker.org/reports/oil-and-gas-transition-plans-user-guide/.
8. See: Nicholas Stern, *The Economics of Climate Change: The Stern Review* (Cambridge University Press, 2007).

To address these and other pressures, some companies are currently seeking, or may seek, to exit from Upstream assets through a number of different ways, including:

1. Surrendering assets to the resource owner (usually the host country government)

2. Selling assets to a third party, including[9]:

- Other operators, which may be smaller companies
- In-country operators, which may be private companies
- Host-country National Oil Companies (NOCs)
- NOCs from other countries
- Private equity companies

3. Selling shares in a third party/Joint-Venture company

4. Retiring assets sooner than had previously been intended

The transfer of ageing assets from larger to smaller Upstream operators has long been common industry practice. Yet as sellers increasingly turn to divestment of "dirtier" assets as one lever (among others) to meet their emissions reduction targets and reduce corporate climate impact, or to seek to reduce transition risk exposure,[10] such asset transfers give rise to additional investor concerns. These concerns include the climate implications of asset sales (Box 2) and increasing risk exposure related to decommissioning obligations.[11,12]

9. See: Nicola Woodroffe, "Responsible Change: How Governments Can Address Environmental, Social and Governance Challenges When Petroleum Assets Change Hands," *Natural Resource Governance Institute* (2024): 10-28, https://resourcegovernance.org/publications/responsible-change-how-governments-can-address-environmental-social-and-governance.
10. See, for example: Stakeholder Democracy Network (SDN), "Divesting from the Delta: Implications for the Niger Delta as international oil companies exit onshore production" (2021), https://www.stakeholderdemocracy.org/report-divestment/. See also: Rick Steiner, "Just Transition: Reforming Oil Industry Divestment, Decommissioning & Abandonment in the Niger Delta, Nigeria," *Centre for Research on Multinational Corporations* (2023), www.oasis-earth.com/_files/ugd/92a90d_25043ffd87f7434f9b6b58f0c17baf96.pdf; and Audrey Gaughran, Nabie Nubari Francis and Emeka Duruigbo, "Selling out the Niger Delta," *SOMO* (2024), www.somo.nl/selling-out-the-niger-delta/.
11. In some jurisdictions, e.g. the Outer Continental Shelf (OCS) in the Gulf of Mexico, decommissioning liability will automatically be reassigned to predecessor owners in cases where the current owners fail to meet decommissioning obligations, and potentially senior to other liabilities. For example, Chevron Corporation recognised an after-tax loss of $1.9 billion related to abandonment and decommissioning obligations from previously sold oil and gas assets in the U.S. Gulf of Mexico after the companies that purchased the assets filed for bankruptcy, stating it was "probable and estimable that a portion of these obligations will revert to the company." See: Chevron, "2023 Annual Report": 29, https://www.chevron.com/-/media/chevron/annual-report/2023/documents/2023-Annual-Report.pdf. In other jurisdictions where such legislation is not in effect, assets that are not decommissioned properly and cause environmental damage (e.g. oil leaks from incorrectly "abandoned" wells) could cause compliance, litigation and/or financial damage to transferees, and reputational damage to transferors. See, for example: "Colorado landowners and farmers sue oil and gas companies in landmark lawsuit over industry's toxic 'zombie wells'," *ClientEarth*, 23 February, 2024, https://www.clientearth.org/latest/press-office/press/colorado-landowners-and-farmers-sue-oil-and-gas-companies-in-landmark-lawsuit-over-industry-s-toxic-zombie-wells/; and Stephen Greenslade, "Feet to the Fire: An analysis of potential outcomes of the Colorado 700-Series Rulemaking," *Carbon Tracker* (2022), https://carbontracker.org/reports/feet-to-the-fire-an-analysis-of-potential-outcomes-of-the-colorado-700-series-rulemaking/.
12. It is important to note the systemic under-provisioning of decommissioning liabilities. This is detailed in: Dwayne Purvis and Rob Schuwerk, "Event Horizon: A Case Study of Holdback and the Point of No Return for Decommissioning Upstream Oil and Gas "Assets"," *Carbon Tracker* (2022), https://carbontracker.org/reports/event-horizon-a-case-study-of-holdback-analysis/; and "Offshore oil and gas asset decommissioning", *Australasian Centre for Corporate Responsibility* (2023), https://www.accr.org.au/research/offshore-oil-and-gas-asset-decommissioning/.

Box 2

Climate-related financial implications of asset sales

While exiting unwanted Upstream assets may reduce direct exposure to energy transition/climate risk for selling companies and their investors, it may actually be detrimental to the climate.[13] For example:

- Transferring assets to a company with comparatively weak operational emissions standards – particularly around methane (leaks, flaring and venting) – may increase production-related (Scope 1) emissions over the remaining asset lifetime, particularly if such operating standards reduce costs and thus extend asset lifetimes.[14]
- Depending on financial terms and attribution of decommissioning obligations, transferring assets to a more thinly-capitalised company may mean reduced ability to sustain costs associated with decommissioning assets to an appropriate standard.[15]
- Unless clear commitments are embedded in the Sales and Purchase Agreement ("SPA") to ensure that target production volumes are consistent with a Paris-aligned climate transition strategy, there is a distinct probability that the buyer will seek to maximise production volumes and extend production life beyond what the seller may have originally projected as part of its own climate transition strategy, where such a strategy exists, thereby undermining the seller's Scope 3 reduction targets. However, adopting such commitments in the SPA inevitably has implications for the financial and other terms of the asset transfer, in particular the financial consideration that can be paid by the buyer to the seller to ensure that the economics of the deal sustain decommissioning at the right time and to the right standard.
- Without the above safeguards, seeking to meet corporate emissions reduction targets simply through asset sales may therefore result in no net reduction in emissions, and could even result in an increase in overall emissions, both Scope 1 and Scope 3.
  - This is particularly so if sellers seek to "create space" within their target emissions budget for the development of new production assets.[16]
  - This also applies for companies that focus on reducing the *emissions intensity* of their portfolios rather than setting absolute reduction targets, as swapping out of older, more carbon-intensive assets in favour of cleaner ones will flatter intensity figures while potentially allowing the company's absolute emissions to increase, while merely displacing rather than cancelling the emissions associated with its disposed legacy assets.
- Ultimately, no producer strategy can credibly be considered *Paris-aligned* if it is not anchored in plans for production reduction over time – a focus on emissions alone is insufficient.

13. We also note the work undertaken by Rethinking Capital, and others, around accounting practice related to emission reduction commitments, noting that current accounting practice has been not to recognise historical emission reduction commitments as obligations nor to recognise investments purposed to meet them as assets, creating perverse incentives. They propose "normative accounting" to enable an informed financial analysis of the true returns from retention and greening versus disposal. Rethinking Capital and the Impact Weighted Accounts Initiative at Harvard Business School first wrote about the insight of '*upside down incentives*' in: Andrew Watson, Thaddeus Zochowski and Robert D. McGarvey, "Constrained by Accounting: Examining How Current Accounting Practice is Constraining the Net Zero Transition," *SSRN* (2021), http://dx.doi.org/10.2139/ssrn.3811577.
14. See: Malek et al., "Transferred Emissions: How Risks in Oil and Gas M&A Could Hamper the Energy Transition".
15. See: Rob Schuwerk and Greg Rogers, "Billion Dollar Orphans: Why millions of oil and gas wells could become wards of the state," *Carbon Tracker* (2020), https://carbontracker.org/reports/billion-dollar-orphans/.
16. Carbon Tracker has written on the need for companies' approaches to emissions reduction to be *credible* in its *Absolute Impact* series. See: Mike Coffin and Saidrasul Ashrafkhanov, "Absolute Impact 2023: Progress on oil and gas emissions targets has stalled," *Carbon Tracker* (2023), https://carbontracker.org/reports/absolute-impact-2023/.

A failure to conduct exits responsibly risks further exposing local communities in oil and gas producing countries to long-term social and environmental harm, including impacts to health, livelihoods, local development and biodiversity,[17] particularly for lower-income countries. There is thus a need for exits to be conducted in a way that takes government interests into account (Box 3), and considers both local regulations on workers and communities alongside related legislation in corporates' domiciles, and the need to maintain a social licence to operate.

As a result, it is in sellers' interests to exit responsibly, as failure to do so exposes them, and their shareholders, to increased regulatory, legal and reputational risks arising from their buyers' inadequate operational standards. Depending on jurisdiction, these could translate into compliance and litigation risks that extend well beyond the period of asset ownership, in addition to posing a reputational risk from being seen to have knowingly sold to a less responsible operator. In addition, when selling assets to operators on terms that compel them to extend the productive life of the acquired assets in order to finance the decommissioning, sellers risk undermining the credibility of their own climate strategy by enabling a transaction that directly increases production and emissions.

Accordingly, we have developed a set of "Responsible Exit" Principles for oil and gas companies that are primarily aimed at correcting the perverse incentive that induces owners of high-carbon assets to dispose of such assets to third parties in order to meet carbon emissions reduction targets, and to mitigate the unintended consequences of divestment and best manage operational, legal, regulatory and reputational risk.

While these Principles are focused on Upstream operations and assets, many of these same considerations can be applied to Midstream and Downstream operations (Box 1), as well as asset transfers of carbon-intensive and highly polluting industrial assets in other sectors.[18]

Additional aims include to support investors to deliver their fiduciary duty, by increasing transparency around asset transfers and exposure to future financial risks, and by supporting an orderly transition, which likely reduces systemic risks (both physical and financial) versus a disorderly transition, and are thus of benefit to Universal Owners.

As part of a responsible exit, these Principles also call for sellers to obtain a commitment from the buyer not to extend the life or production targets of the acquired assets beyond those agreed at time of sale. Host governments will have a central role to play, along with sellers and buyers, in defining and implementing these commitments because, in many jurisdictions, governments are the owner of the oil and gas resource and must make ultimate decisions on production, not just with respect to the closure of a particular asset, but with respect to the future of their country's oil and gas sector. Moreover, in some jurisdictions asset transfers, and the terms of such transfers, are subject to government approval and/or companies are legally or contractually bound to maximise oil recovery (see Box 3 on government interests).

Existing international normative standards on responsible business conduct include expectations that companies contribute to addressing climate change—including through the adoption of, and reporting on, transition plans[19]—and disengage responsibly from countries and communities in which they operate.[20] These Principles build on such standards and provide specific detail on how oil and gas companies can fulfil obligations when exiting Upstream oil and gas assets.

17. See: Rick Steiner, "Just Transition: Reforming Oil Industry Divestment, Decommissioning & Abandonment in the Niger Delta, Nigeria".
18. See: Julien Halfon, Vincent Mayot, Annie Omojola and James Sheen, "Decommissioning Stranded Energy Assets – A USD 8 trillion Challenge," *BNP Paribas Asset Management* (2023), https://docfinder.bnpparibas-am.com/api/files/774827C2-0FC0-40E4-B442-6945018B54DF.
19. For further discussion on the assessment of corporate transition plans for oil and gas companies, see: Coffin, "Oil and Gas Transition Plans: A User Guide".
20. For example, the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct provide that: "[e]nterprises have an important role in contributing towards net-zero greenhouse gas emissions and a climate-resilient economy, necessary for achieving internationally agreed goals on climate change mitigation and adaptation. During the process of transitioning to net-zero greenhouse gas emissions, many business activities will involve some level of emissions of greenhouse gases or reduction of carbon sinks. Enterprises should ensure that their greenhouse gas emissions and impact on carbon sinks are consistent with internationally agreed global temperature goals based on best available science, including as assessed by the Intergovernmental Panel on Climate Change (IPCC)" and states that it "set[s] out expectations on how enterprises should avoid and address adverse environmental impacts and contribute to reaching the goals of climate change mitigation and adaptation". See: OECD, *OECD Guidelines for Multinational Enterprises on Responsible Business Conduct* (OECD Publishing, 2023): 35 and 37, https://www.oecd-ilibrary.org/finance-and-investment/oecd-guidelines-for-multinational-enterprises-on-responsible-business-conduct_81f92357-en.

Box 3

Government interests

It is in the strong interest of all governments to ensure that companies clear up after themselves, particularly regarding ensuring costs are fully provided for, so that assets are not abandoned in a poor state, and thus effectively place those costs on the state purse.

Newly sanctioned fields can take seven to ten years to come onstream, and with oil and gas demand expected to peak by the end of the decade, many are at risk of failing to deliver returns as expected. Equally, further development of oil and gas producing assets makes achieving national climate goals considerably harder.

It is also important to acknowledge a particular challenge to effecting a transition away from fossil fuels, i.e. that some nations with significant remaining oil and gas resources, especially those in the **Global South**[21], are often heavily dependent on the fiscal proceeds of such resources. As the transition gathers pace, and against a backdrop of rising global concerns about climate change, they have a strong incentive to maximise potential earnings *before* their window of opportunity closes.

Few will likely willingly forego such earnings unless and until market forces compel them, or funding and technological assistance from the Global North can be mobilised to incentivise and accelerate diversification away from their dependence on fossil fuels. A failure to invest in such actions risks not only severely undermining global efforts to transition away from fossil fuels, as called for by the COP28 UAE Consensus, in a manner that averts the worst effects of extreme climate change for North and South alike, but also leaves fossil fuel-dependent emerging nations vulnerable to the risk of overinvestment, costly write-downs and socially disruptive contraction.[22]

By ensuring that asset disposals take place with suitable safeguards regarding operational and stewardship standards as well as production volumes, the measures in this guidance therefore seek to enable a phaseout of the industry that is more orderly and reduces social and environmental harms in host countries and specifically host communities, which is a critical aspect of enabling a just and equitable transition. While we do not seek to resolve issues of global equity regarding fossil fuel phaseout in this document, we acknowledge that actions taken under these principles will take place in the broader context of Global North and Global South Just Transition dynamics.

For all countries, governments should review and align their oil and gas legal framework with their climate action plans and consider whether current licence obligations are appropriate given the climate crisis and the unfolding energy transition. For example, in the UK, the current general requirement for companies to maximise the value of economically recoverable oil and gas potentially prevents companies seeking to exit the sector through closure of assets.[23]

21. Our intent here is to recognise that nations' historic contribution to climate change is not equal, and nations face the different challenges, physically, economically and socially.

22. As argued in Carbon Tracker, 2021, *Beyond Petrostates* - Beyond Petrostates - Carbon Tracker Initiative, Carbon Tracker, 2023, *Petrostates of Decline* - PetroStates of Decline: oil and gas producers face growing fiscal risks as the energy transition unfolds - Carbon Tracker Initiative, David Manley and Patrick R.P. Heller, *Risky Bet: National Oil Companies in the Energy Transition* (Natural Resource Governance Institute (NRGI), 2021). https://resourcegovernance.org/publications/risky-bet-national-oil-companies-energy-transition; David Manley, Andrea Furnaro and Patrick R.P. Heller, *Riskier Bets, Smaller Pockets: How National Oil Companies Are Spending Public Money Amid the Energy Transition* (NRGI, 2023), www.resourcegovernance.org/publications/riskier-bets-smaller-pockets-national-oil-companies-public-money-energy-transition) there is a big opportunity cost in continuing to invest state money into 1) the acquisition of existing production assets, and 2) the development of new oil and gas infrastructure, particularly seeking export revenues.

23. See: "The OGA Strategy," *Oil and Gas Authority* (2021), https://www.nstauthority.co.uk/media/7105/the-oga-strategy.pdf.

These principles:

1) Define a set of credible, widely recognised best practice standards governing the operation and eventual closure of such assets, by informing how sellers, buyers and their financial stakeholders can mitigate financial, environmental, governance and reputational risks related to such transfers.

2) Are relevant to different stakeholders, including:

- **Buyers and sellers** (public / state-owned / private) of Upstream oil and gas assets.
- **Financial institutions** (asset managers, banks, insurers, advisors), who can refer to these Principles when determining whether and under what conditions to lend to, invest in, underwrite, advise or insure a company in the oil and gas sector.[24]
- **Professional advisors** (legal counsel, who can refer to these Principles when drawing up contracts of sale; external auditors, who can assess the quality of optional disclosures in the notes to the financial statements and narrative disclosure; and consultants, who can weigh up the implications of these Principles when advising on strategic priorities, including using M&A as a tool to accelerate business model transformation).
- **Governments and financial regulators,** who can use these principles to consider how best to regulate both decommissioning activities[25] and asset transfers within their jurisdictions, including the impact such transfers may have on Nationally Determined Contributions (NDCs), and the implications for fiscal policy.[26]
- **Host communities, civil society and other accountability actors** who can monitor the terms and implementation of asset transfers to hold sellers and buyers accountable for their compliance (or non-compliance) with these Principles, including as part of broader just transition considerations.

3) Build on other work, such as that of the Environmental Defense Fund and Ceres,[27] **by proposing:**

- **That companies consider their emissions reduction plans** from the perspective of alignment with Paris Agreement goals (see Appendix 1)
- **Additional safeguards** for ensuring adequate financing for decommissioning of assets, including transparency and third-party auditing of companies' decommissioning cost estimations and buyer covenants.
- **That due diligence on prospective buyers should also include an assessment of their governance strength, social impacts management and community engagement practices,** which, alongside financial and technical capabilities, is critical for ensuring delivery against the principles contained in this guidance.
- **Additional disclosures** with respect to each asset transfer on emissions reduction targets, environmental liabilities and the terms of the asset transfer to enable relevant stakeholders to assess the transfer of risks and the alignment between the terms agreed and companies' transition strategy.
- **Engagement with governments, civil society and host communities** to minimize negative impacts and support sustainable development.

These Principles are meant to supplement laws of the jurisdictions in which oil and gas companies operate by filling in regulatory gaps or calling for companies to exceed existing legal requirements on asset transfers and environmental and social impact management. Under these Principles, companies are expected to comply with or exceed country laws and regulations in all cases.

24. Additionally, these principles support financial institutions to determine whether such a relationship is compatible with their own climate or net-zero commitments; as well as transaction assessments (e.g. on decommissioning provisions) when considering "managed phaseout transition finance" in cases where a buyer has committed to retire the asset early. GFANZ has proposed transition financing strategies and transaction attributes on Managed Phaseout here: "Scaling Transition Finance and Real-economy Decarbonization," *GFANZ* (2023), https://assets.bbhub.io/company/sites/63/2023/11/Transition-Finance-and-Real-Economy-Decarbonization-December-2023.pdf.
25. This should include paying particular attention to a) the tax treatment afforded to decommissioning activities, ensuring where necessary that fiscal policies enable, rather than penalise, the closure of assets, e.g. by allowing full deductibility of decommissioning cost as operating expenses, and b) funding/bonding set aside for decommissioning activities.
26. See: Woodroffe, "Responsible Change: How Governments Can Address Environmental, Social and Governance Challenges When Petroleum Assets Change Hands".
27. See: Andrew Baxter, Laetitia Pirson, Chris Amandes and Elizabeth Arenz, "Tackling Transferred Emissions: Climate Principles for Oil and Gas Mergers and Acquisitions," *Environmental Defense Fund* and *Ceres*, (2022), https://business.edf.org/insights/transferred-emissions-climate-principles/.

Principle 1: Decommissioning Obligations and Sales & Purchase Agreements

The following recommendations related to decommissioning obligations, a.k.a. asset retirement obligations (AROs), should be seen to apply on a voluntary basis, to the extent that they do not place either the Seller or Buyer in breach of applicable law. Where local law imposes certain requirements that are more stringent than this guidance, such requirements should take precedence. As a general principle, Sellers and Buyers are encouraged to commit voluntarily and as a matter of best practice to adopt the protections required in the most stringent jurisdictions (see Box 1).

Companies should ensure that in addition to the minimum required disclosures, they make certain voluntary disclosures:

1.1. Decommissioning obligations, are valued, fully provisioned for and disclosed, as per the following:

- **Obligations are accounted for and fully disclosed in the Seller's audited financial statements under the relevant accounting standards**, for example International Financial Reporting Standards (IFRS) or US Generally Accepted Accounting Principles (US GAAP).[28]
  - Sufficient disclosure is made to fully make understandable how decommissioning obligations have been considered, whether recorded on the balance sheet (as liabilities or provisions) or remaining off-balance sheet, including consideration of the relevant facts and circumstances, uncertainties, and assumptions made.[29] This would include the quantitative assumptions and estimates that companies used to account for these obligations (see Box 2).
- **Full discounted present value, and total undiscounted estimated costs and estimated settlement dates,[30] of such decommissioning obligations are calculated by the Seller, consistent with adherence to global best technical standards**, e.g. as embodied in ISO 19900[31] and related standards.
  - Estimated undiscounted costs of retirement for all unrecorded obligations ("off-balance sheet liabilities") and the reasons for not recording such items, such as those that relate to any assets whose *remaining economic lives* are regarded by management as "indeterminate", even though non-disclosure would be permissible under relevant accounting standards[32] (see Box 4).

28. When the seller and buyer are both private companies, apply principles-based standards, such as IFRS, to ensure interpretations of requirements that would result in the most useful disclosures.
29. This may include voluntary disclosures that provide information beyond those mandated under the relevant accounting standards, and are not prohibited by IFRS or US GAAP.
30. For example, bp plc disclosed the total expected payments (undiscounted) for recorded decommissioning liabilities (see: "Annual Report and Form 20-F 2023," *bp:* 341, https://www.bp.com/content/dam/bp/business-sites/en/global/corporate/pdfs/investors/bp-annual-report-and-form-20f-2023.pdf). Additional disclosures provided by bp in FY2023 include: 1) undiscounted amounts and estimated timing for Upstream decommissioning (p. 184): "The estimated phasing of undiscounted cash flows in real terms for upstream decommissioning is approximately $5.5 billion (2022 $5.6 billion) within the next 10 years, $5.8 billion (2022 $5.3 billion) in 10 to 20 years and the remainder of approximately $6.6 billion (2022 $6.0 billion) after 20 years.", and 2) (p. 337): "2021 includes adjustments relating to the change in discount rate on retained decommissioning provisions and the recognition of a decommissioning provision in relation to certain assets previously sold to a third party where the decommissioning obligation transferred may revert to bp due to the financial condition of the current owner." Shell plc, in the notes to its FY2023 financial statements, indicated that it reflected "acceleration of decommissioning and restoration activities" in the discount rate used for decommissioning provisions which it revised in FY2021 from a 30-year term to a 20-year term in "line with the average remaining life of Integrated Gas and Upstream assets." (A subsequent increase to the FY2023 rate resulted in a decrease to decommissioning and restoration provisions of $2.8bn). It disclosed the undiscounted amount of its decommissioning and restoration provisions, and the amount of decommissioning and other provisions related to assets held for sale. See: "Annual Report and Accounts 2023," *Shell*: 268, 287 and 301, https://reports.shell.com/annual-report/2023/_assets/downloads/shell-annual-report-2023.pdf.
31. References here to additional relevant international standards, as per recommendation by ISO – forthcoming. ISO 19900 details technical standards that operators should adhere to when undertaking decommissioning, but does not take a view on the costs attributed to such activities, nor does it opine on accounting or governance practices.

- **Changes in the assumptions and/or estimates by the Seller that resulted in significant changes to liabilities/provisions on the balance sheet in the period reported or immediately prior to the exit/transfer are disclosed.** This should include the impacts of the energy transition on the estimated costs and expected timing of asset retirement by the Seller or Buyer.
- **Any re-estimations of decommissioning costs by the Buyer are disclosed to the Seller, along with the assumptions that underpin these and justification for their use.**
- **In instances where the net present value (NPV) of the asset is negative because of the decommissioning cost, the amount of consideration paid by the Seller to the Buyer to take ownership of the asset and related liabilities.** The use of an escrow account should be considered in such circumstances (See 1.2).

Box 4

Selected national standards

The standards for addressing the decommissioning of assets vary by jurisdiction. The following are provided by way of example; see *Decommissioning Liability at the End of Offshore Oil and Gas* published by the **Columbia Center for Sustainable Investment** (CCSI) for a broader review of selected jurisdictions.[33]

- **The state of Queensland in Australia** has recently overhauled its approach to rehabilitation for resource projects – this covers oil and gas projects as well as mines. The new regime requires operators to pay into a government fund and in some circumstances obtain a surety. This is intended to be a comprehensive way of ensuring that rehabilitation/decommissioning costs are provided for, and do not become a liability for taxpayers.
- **Norway's regulatory requirements**[34] state that: "a decommissioning plan must be submitted to the Ministry of Energy within two to five years prior to a licence expiring or being relinquished, or when use of a facility ceases". The decommissioning plan consists of two main parts, a disposal part and an impact assessment part. The disposal part describes the technical and financial aspects of the cessation project. The impact assessment part provides an overview of expected consequences of the disposal, e.g., for the environment and other users of the sea."
- **UK Decommissioning securities requirements** state that in field partnerships, the owners are jointly and severally liable: if one owner defaults, the other owner must become liable for the failed partner's share of decommissioning liabilities. Additionally, under the UK Petroleum Act, the government has the right to require a previous owner and affiliates to pay for decommissioning in the event the current owners are unable to do so. As a result, most field partnerships insist on decommissioning security from each owner, in the form of a PCG or a letter of credit – which is usually done through a Decommissioning Security Agreement (DSA).
- **Nigeria's decommissioning regulations** require companies to set up a decommissioning fund no later than 90 days from the date of commencement of production for new licenses and 90 days from the date of commencement of the regulations for existing licenses.[35]

32. For example, see auditor guidance about providing more information: "Financial statement presentation – Partially updated April 2023," *PwC,* Chapter 11, 24, https://viewpoint.pwc.com/dt/us/en/pwc/accounting_guides/financial_statement_/assets/pwcfinlstmtpresentn0423.pdf.
33. See: Martin Lockman, Martin Dietrich Brauch, Esteban F. Fresno Rodríguez and José Luis Gallardo Torres, "Decommissioning Liability at the End of Offshore Oil and Gas: A Review of International Obligations, National Laws, and Contractual Approaches in Ten Jurisdictions," *Columbia Center on Sustainable Investment* (2023), https://scholarship.law.columbia.edu/sabin_climate_change/205/.
34. See: "Cessation and decommissioning," *Norwegian Petroleum*, accessed 13 September, 2024, https://www.norskpetroleum.no/en/developments-and-operations/cessation-and-decommissioning/.

Box 5

Assumptions and estimates underpinning decommissioning obligations and contextual information

Disclosures related to decommissioning obligations should be disaggregated at a level that provides useful information to the reader; at a minimum, by cash generating unit (e.g., provide separate information for Upstream, Midstream and Downstream activities). Such disclosures may include, but should not be limited to, the following.

The relevant asset (or group of assets):

- Asset value on the balance sheet
- Estimated remaining asset lives (or estimated units of production in relation to annual production) and residual value, assumed for depreciation calculations

Assets set aside to fund obligations:

- Information including the nature of the restriction and value of the assets set aside.
- Remedial measures taken in the event the decommissioning fund falls behind required outlays, and extent to which Seller and Buyer bear responsibility

For all instances in which constructive or legal decommissioning obligations are present:

- Whether contingencies are included in the cost estimate (i.e., risk of cost overruns, e.g. engineer salary inflation, materials, supply chain bottlenecks, foreign exchange risk)
- Explanation of significant gaps between remaining economic lives and the start of decommissioning. For example, instances involving a decision to "idle" and, where permissible, pay an "idle well fee" as a means of indefinitely delaying the start of shutdown operations and thereby minimising the present value of decommissioning obligations;

For the on-balance sheet (recorded) liabilities/ provisions:

- Current estimate of the total cost of meeting the obligations – at the balance sheet date
- Estimated expected timing of future cash flows (payments) to meet the obligations
- Inflation rate applicable for the timing of expected cash flows
- Undiscounted cash flows (current costs, increased for inflation to expected timing)
- Discount rate(s) applied;
- Discounted present value – liability/provision on the balance sheet.

Off-balance sheet obligations:

- In addition to amounts that must be carried on the balance sheet per existing accounting requirements, both parties should voluntarily disclose the current estimate of the cost of meeting the obligations – at the balance sheet date, again disaggregated to a level that is useful for the reader.[36]

Guarantees of decommissioning obligations relating to exited assets (contingent liabilities)

- Information on the guarantees historically made by asset/group of assets, and an assessment of the potential costs and probability of the need to fulfil such guarantees. (e.g. in the event of bankruptcy of the purchaser).

35. See: "Nigeria Upstream Petroleum Decommissioning and Abandonment Regulations, 2023," *Federal Republic of Nigeria Official Gazette*, https://www.nuprc.gov.ng/wp-content/uploads/2023/07/DECOMMISSIONING-REGULATIONS.pdf.

1.2. Sales and Purchase Agreements (SPAs) include contractually-binding obligations for Sellers and Buyers, to ensure that:

- **Sufficient monies are placed in escrow with a reputable financial institution to fund decommissioning** to a standard that is in line with the above-noted ISO 19900 and climate commitments (e.g. to be Paris-aligned);
  - To the extent that such a fund is either non-existent or insufficient to cover the full value of expected outlays, additional provisions are made via the SPA to ensure funding is increased to an adequate extent, with appropriately robust safeguards governing its drawdown;
  - The establishment of a sinking fund is encouraged, to be funded over the Seller's expected life of the project.
- **Where not already required by local law, the Seller undertakes to retain responsibility over the Buyer's performance until such time as decommissioning is complete** to ensure the above-noted technical and climate transition performance standards are met post-transfer[37]. This may take the form of the Seller having recourse over the Buyer via one, or more, of:
  - Financial protection, e.g. in the form of a decommissioning security provided by both parties, in the form of a PCG or a letter of credit through a Decommissioning Security Agreement (DSA);
  - Retention of a partial ownership stake by the Seller, with joint and several liability over delivery of the shutdown;
  - Responsibility for completion of the decommissioning phase reverting to the Seller;
- The Buyer will uphold, and report annually on delivery against, commitments governing long-term monitoring of leaks and other environmental impacts[38];
- The Buyer will uphold an investment-grade credit rating, or purchase adequate credit enhancements to secure the deal;
- The Buyer will purchase Reps and Warranties Insurance coverage to guarantee delivery against decommissioning obligations;
- The Buyer undertakes to avoid availing itself of the option, where permissible under local law, to "idle" a well or field without commencing decommissioning as a means of reducing the present value of decommissioning obligations (irrespective of the accounting treatment of idled wells in calculating present value);
- The Buyer is precluded from making dividend payments or other shareholder distributions that, through excessive cash withdrawals, risk impairing its ability to maintain sufficient funding for decommissioning liabilities;
- Parent companies of both Sellers and Buyers guarantee decommissioning obligations, i.e. take full responsibility for the standards and commitments of their subsidiaries and affiliates.

36. See: PwC, "Financial statement presentation – Partially updated April 2023".
37. This provision intends to replicate on a voluntary basis, by mutual agreement between Seller and Buyer, the predecessor liability regime that applies in certain jurisdictions whereby decommissioning liability that in normal circumstances sits with the current owner (in this context, the Buyer post-transfer) would revert to the previous owner (in this context, the Seller) in the event the Buyer is technically or financially unable to meet its decommissioning obligations to a standard consistent with the terms of the contract.
38. In the absence of an existing industry standard, we propose to place a time-limited guarantee, e.g. of five years following completion.

1.3. These financial provisions within the SPA are subject to robust governance oversight, including:

- **Regular monitoring, reporting and, where necessary, re-valuing of decommissioning obligations**, to ensure ongoing consistency between ringfenced amounts and the expected value of outlays and timing of successive stages of the asset retirement programme, actual progress achieved against milestones, as well as consistency of the assumptions and estimates used in accounting for the liability with the latest climate change impact and energy transition scenarios.[39]
- **Climate commitments** - to the extent that the Buyer already has group-level climate transition policies, operating standards and targets that are consistent with a Paris-aligned scenario, such as the International Energy Agency's Net Zero Emissions by 2050 Scenario (NZE), ensure that it has, or commits to adopt, the following standards across its groupwide portfolio; where it does not have such a groupwide commitment, ensure, at a very minimum, that for purposes of operating the acquired assets, the Buyer commits to align with the following:
  - Internationally-recognised measurement and reporting framework(s) such as the Greenhouse Gas Protocol, The Oil & Gas Methane Partnership 2.0 (OGMP 2.0), and the Global Reporting Initiative including improvements / enhancements to these standards (e.g. moving from calculated to directly-measured methane emissions).
  - The Oil and Gas Decarbonization Charter issued at COP28;
  - The Seller's pre-existing standard, if more ambitious than the above;
  - A commitment not to extend the life or production targets of the acquired assets beyond those agreed at time of sale.
- **Transparency and audit** – the nature, amount and sufficiency of decommissioning provisions should be subject to annual verification, whether via assurance or audit, by an independent third party, and the terms of such oversight processes disclosed, including compliance with Greenhouse Gas (GHG) emissions commitments.
  - For listed companies, these provisions should be disclosed within financial statements and subject to the relevant audit requirements.
  - For private companies, the audit of financial provisions should follow the accounting standards agreed upon in the SPA.
  - For both listed and private companies, auditors should question the assumptions used in the calculation of provisions, both that numbers are not materially misstated or disclosure is misleading.
  - Compliance with climate commitments should be subject to assurance by an independent third party.

39. This is to ensure that decommissioning costs are adequately funded in the event of a rapid phase-out of oil and gas necessitating earlier decommissioning.

Box 6

Illustrative example

From the BNP Paribas Asset Management report on decommissioning: *"The transition to a lower carbon economy requires business models to be reviewed and adapted. In recent years, oil & gas companies such as Shell and BP have begun to acknowledge the acceleration of the energy transition, resulting in earlier-than-anticipated decommissioning work and thereby increasing the current value of the associated liabilities."*

They have included references in recent annual reports

- Shell annual report 2021 (page 222): "The timing of estimated future decommissioning activity is also a key judgement with the energy transition increasing the risk that oil and gas fields will be decommissioned earlier than anticipated...."
- BP annual report 2021 (Page 148): "The timing of expected future decommissioning expenditures in respect of oil and gas assets may need to be brought forward with a resulting increase in the present value of the associated liabilities due to the impact of climate change."[40]



Photo by David McNew via Getty Images

40. See: Halfon et al., "Decommissioning Stranded Energy Assets – A USD 8 trillion Challenge".

Principle 2: Counterparty Due Diligence

The Seller should, in line with standards outlined in Principle 1 above, and in keeping with existing host country laws and regulations governing asset transfers,[41] conduct effective due diligence on potential Buyers, and work proactively with those with insufficient capacity in order to bring them up to standard, as follows. This should include a review of the Buyer's track record in successfully completing prior decommissioning projects to the appropriate technical standard, on time and within budget. Where a prospective Buyer lacks the requisite track record, the Seller should insist on the additional measures outline below to mitigate the risks of underperformance. **Per Principle 3 that follows, Sellers should, moreover, disclose the results of this due diligence** when announcing the disposal of the asset(s) to the Buyer, as well as state clearly what legal commitments have been taken by both parties in the Sales and Purchase Agreement to ensure delivery on commitments taken and over what timeline.

Counterparty due diligence should therefore consist of the following:

2.1. Technical strength assessment: ensure that the Buyer has a strong track record of successfully completing prior decommissioning project – or is partnered with an established service company with such a track record – backed up by evidence of technical capability to:

- Safely and efficiently operate the asset until closure;
- Carry out, or appropriately supervise if conducted by third-party contractor, the decommissioning process in line with ISO 19900 and related standards;
- Measure, reduce and disclose GHG emissions in line with contractually-agreed standards and relevant commitments;
- Maintain strong supply chain and circularity practices.

2.2. Financial strength assessment: ensure that the Buyer has the financial strength and appropriate management processes to:

- Maintain operational standards through completion of production phase;
- Meet decommissioning obligations, as detailed in Principle 1, including undergoing annual audit or assurance by external auditors regarding the sufficiency of relevant financial provisions;
- Maintain an investment-grade credit rating, if necessary, via purchase of an appropriate credit enhancement product;
- Where obligations for transferred assets are not ring-fenced by individual project, additional due diligence should be conducted on the decommissioning obligations related to all of the Buyer's other assets, in order to identify, and if need be, mitigate, any potential financial and operational risks posed by the Buyer's wider portfolio exposure.

2.3. Climate and environmental standards assessment: ensure Buyer has, or commits to adopt:

- Emissions reduction, measurement and reporting aligned with:
  - Internationally-recognised measurement and reporting framework(s) such as The Oil & Gas Methane Partnership 2.0 (OGMP 2.0),[42] the Greenhouse Gas Protocol,[43] the Global Reporting Initiative,[44] including evolutions to such frameworks.
  - The Oil and Gas Decarbonization Charter issued at COP28;
  - The Seller's pre-existing standard, if more ambitious than the above.
- A commitment not to extend the life or production targets of the acquired assets beyond those agreed at time of sale.[45]

41. For example, companies may be required under law or contract to seek approval for an asset transfer and must demonstrate the buyer's technical and financial capacity as a condition for approval. Companies are expected to conduct due diligence and engage with host governments to meet or exceed requirements to demonstrate the buyer's technical and financial competence. See: Woodroffe, "Responsible Change: How Governments Can Address Environmental, Social and Governance Challenges When Petroleum Assets Change Hands".
42. "Homepage," *Oil & Gas Methane Partnership 2.0*, accessed 13 September, 2024, https://ogmpartnership.com/.
43. "Homepage," *Greenhouse Gas Protocol*, accessed 13 September, 2024, https://ghgprotocol.org/.
44. "Homepage," *Global Reporting Initiative*, accessed 13 September, 2024, https://www.globalreporting.org/.
45. Subject to host government approval.

- Emissions targets relating to the asset; all actors are encouraged to set emissions targets on a scope 1, 2 and 3 basis.
- Environmental management record, including oil spills management.

2.4. Governance strength assessment: ensure that the Buyer has appropriate governance systems in place, and a strong track record in these areas:

- Strong board oversight to guarantee ongoing delivery against the high standards contained in this guidance;
- Risk management practices, including on health, safety, security, environmental (including GHGs), and transition-related risks;
- Anti-bribery and corruption;
- Lobbying transparency and alignment with publicly-stated commitments;
- Executive remuneration policies that support delivery of high operational standards and a Paris-aligned strategy;
- Audit practices, including review by the company's Audit Committee (or equivalent) and external auditors, that ensure the company's financial reporting practices are consistent with its public commitments to ensure a Paris-aligned climate transition.

2.5. Social impacts management and community engagement assessment – ensure that the Buyer has appropriate systems in place, and a strong track record in the following areas[46]:

- Employee consultation, employee training and re-skilling, early employee retirement plans, including a fully-costed plan to re-deploy production workers, where possible, to roles in the closure of existing installations and the development and execution of new low- and zero-carbon technologies, where applicable;
- Supplier engagement, capacity-building and re-skilling;
- Human rights and social impacts management record;
- Community relations and social investment, including actions to assess and mitigate impacts on the local tax base and local economy; transparent commitments and assurance on investment in local economic diversification opportunities.

46. See also: Principle 4 Engagement.

Principle 3: Transparency

Sellers should be transparent to governments and other key stakeholders—including rights holders, financial stakeholders, host communities and civil society— about the role of asset transfers in their transition strategy. This specifically relates to reduction of total emissions and emissions intensity across their portfolio of assets and how commitments enshrined in the SPA are reflected in anticipated lifetime emissions of sold assets. They should also publicly disclose sufficient information to enable stakeholders to assess the transfer of risk and, in particular, to provide clarity around responsibility for environmental and social responsibilities post-transfer.

Sellers and Buyers (where relevant below) should disclose:

3.1. The commitments in the SPA to ensure sufficient decommissioning funding as itemised under Principle 1;

3.2. The emissions reduction, measurement and reporting commitments the Buyer has or has undertaken to adopt under Principle 2;

3.3. To the extent that the Seller has set company-wide emissions reduction targets, **Seller should disclose how the transfer affects changes in its absolute and intensity-based emissions and progress towards emissions targets**. Sellers should rebase their climate transition targets, and related disclosures, to avoid counting asset disposals towards meeting climate targets using standards such as the Greenhouse Gas Protocol and the Environmental Defense Fund and Ceres' Climate Principles; [47]

3.4. To the extent that the Seller has set company-wide emissions reduction targets, **Sellers should include total anticipated lifetime scopes 1, 2 and 3 emissions of transferred asset as part of their Scope 3 disclosures in the year in which the asset is transferred**, to reflect commitments made between the Buyer and Seller on emissions reduction and production for the asset;[48]

3.5. A full list of the assets included in the transfer and the environmental and social responsibilities associated with the assets, including pending litigation;[49]

3.6. At the time of disposal and transaction completion, Sellers are recommended to be transparent about the likely deployment of funds from the disposal, specifically whether these will be used to fund further development of Upstream oil and gas.

3.7. The provisions of the SPA addressing Buyer's commitments with respect to local benefits and employment after the transfer, per Principle 4;

3.8. The engagement they have conducted with the above-noted stakeholders (per Principle 4), and the outcomes of such dialogues.

47. See: Baxter et al., "Tackling Transferred Emissions: Climate Principles for Oil and Gas Mergers and Acquisitions".

48. Companies are encouraged to consider a new proposal for carbon accounting to reflect an expanded notion of indirect or Scope 3 emissions which, "are a consequence of the activities of the company but occur at sources owned or controlled by another company" as defined by the Greenhouse Gas Protocol (25). Such proposal would require that "[i]n each reporting period, scope 3 emissions must include the reasonably anticipated lifetime emissions resulting from the operation of capital assets and lines of business that are sold during that reporting period [, excluding emissions from sold assets that have been excluded from the reporting company's emissions inventory following a base year emissions recalculation]. For the purposes of this requirement, "lifetime emissions" consist of the aggregated scope 1, 2, and 3 emissions over the working life of any sold capital assets." See: Jack Arnold, Martin Lockman, Perrine Toledano, Martin Dietrich Brauch, Shraman Sen and Michael Burger, "Transferred Emissions Are Still Emissions: Why Fossil Fuel Asset Sales Need Enhanced Transparency and Carbon Accounting," *Columbia Center on Sustainable Investment*, (2023): 57, https://ccsi.columbia.edu/sites/default/files/content/docs/Fossil-Fuel-Asset-Sales-Enhanced-Transparency-Carbon-Accounting.pdf.

49. Clarity around responsibility for environmental and social liabilities associated with transferred assets is of great concern to affected communities, taking into account the seller's responsibility to remediate environmental harms it caused or contributed to. Apart from remediation requirements that may exist under the laws of the jurisdiction in which the asset is located, environmental remediation obligations are well established in international standards. See: OECD, *OECD Guidelines for Multinational Enterprises on Responsible Business Conduct*. Failure to provide this clarity and to ensure buyers have the capacity to responsibly manage environmental and social impacts and engage with communities risk reputational damage. See: Audrey Gaughran, "Selling out Nigeria: Shell's irresponsible divestment," *The Centre for Research on Multinational Corporations*, 27 February, 2024, https://www.somo.nl/shells-reckless-divestment-from-niger-delta/.

Principle 4: Engagement

Before sales and divestments take place, both Seller and Buyer should engage with national and subnational governments (referred to collectively as "host governments" in this Principle), Indigenous Peoples, local communities, and broader civil society (referred to as "relevant stakeholders" in this Principle). Sellers and Buyers should include responsible exit policies and practices in their corporate just transition plans, including explaining how the company has integrated and acted on feedback from various stakeholders in connection with exiting assets.

Such plans should be created and implemented in line with best practices on content and stakeholder engagement,[50] and should include key issues to inform priority actions in line with just transition principles, minimise negative impacts on communities, and support sustainable development.

Sellers and Buyers should engage with stakeholders on the following key issues:

4.1. Domestic demand for oil and gas – Seller and Buyer should liaise with host governments and relevant stakeholders on policies to balance domestic demand for, and supply of, resources;[51]

4.2. Changes in host government policy – Seller and Buyer should engage with government officials and relevant stakeholders on potential policy changes that host governments may initiate in response to the unfolding energy transition, especially regarding the impact of such shifts on project economics and abilities to meet decommissioning obligations.[52] When entering into new agreements, companies should refrain from using stabilization clauses that constrain host government abilities to respond to energy transition shifts and should adhere to, or exceed, host government laws.

4.3. Decommissioning requirements – Buyer and Seller should engage with governments around decommissioning, to share best practice and to ensure consistency across exits/transfers, and ensuring financial provisions are fully met, and accountability actors fulfil their duties.

4.4. Lobbying/Litigation – Sellers and Buyers should ensure compliance with best practices regarding lobbying, including on climate-related policies[53], and at all times publicly disclose any lobbying and litigation activities that they and the trade associations of which they are members undertake with respect to climate and energy transition policies and host country policies, and ensure consistency between their climate- and energy transition-related commitments, and the public policy positions they and their proxies promote;

4.5. Local Benefits – Sellers should ensure, as part of the SPA and taking into account their legal/contractual obligations and voluntary practices before the transfer, that Buyers will minimize reductions in any previously planned local and national benefits following the asset transfer, by continuing or implementing local content and community development activities, including with respect to local skills development, employment and procurement, and will adhere to any previous agreements with communities on compensation;

50. Examples include the Just Transition Indicators in: "Climate Action 100+ Net Zero Company Benchmark Disclosure Framework Assessment Methodology V2.0 – 2023," *Climate Action 100+*, https://www.climateaction100.org/wp-content/uploads/2023/10/CA100-Benchmark-2.0-Disclosure-Framework-Methodology-Confidential-October-2023.pdf; and: "World Benchmarking Alliance Just Transition Methodology," *World Benchmarking Alliance* (2021), https://assets.worldbenchmarkingalliance.org/app/uploads/2021/07/Just-Transition-Methodology.pdf.

51. Where governments seek to decarbonise domestic industries, including power generation, to meet NDCs, this may result in lower-than-anticipated domestic demand, particularly for gas, with implications, for example, for domestic supply agreements.

52. As the energy transition unfolds, with likely implications for commodity prices, governments may seek to change licence terms and/or taxation in order to minimize reduction to government revenues and support fiscal sustainability.

53. Examples include: "Global Standard on Responsible Corporate Climate Lobbying," *Responsible climate lobbying: The global standard* (2022), https://climate-lobbying.com/wp-content/uploads/2022/03/2022_global-standard-responsible-climate-lobbying_APPENDIX.pdf.

4.6. Employment – Sellers should ensure, as part of the SPA and taking into account their legal/contractual obligations and voluntary practices before the transfer, that Buyers will uphold workers' rights and employee safety measures, and commit to retrain, retain, redeploy and/or compensate employees whose jobs are impacted as a result of the sale or eventual wind-down;

4.7. Diversification opportunities – where oil and gas companies have a strategy of transitioning/diversifying into new business sectors (as opposed to going into harvest/wind down mode) or are considering alternatives to decommissioning (e.g. converting offshore and onshore fields to wind farms), they should explore and engage host governments and relevant stakeholders on opportunities for such plans to contribute to domestic economic diversification and clean energy needs, especially in low- and middle-income host countries. For further discussion of the merits of pursuing a wind-down or diversification strategy, see Carbon Tracker's report *Navigating Peak Demand*.[54]

4.8. Socio-environmental impacts – Sellers and Buyers should ensure that all transfer and exit planning and implementation is conducted in line with the inclusive assessment and mitigation of social and environmental impacts, including with respect to biodiversity, nature, water, health, gender, and Indigenous Peoples and Free Prior Informed Consent.

4.9. Investor engagement – Investors can also play a role in pushing for transfers and divestments to be done responsibly. Sellers and Buyers should disclose their process of engagement with investors, including the conditions under which a transaction will be put to a shareholder vote.

54. See: Mike Coffin and Guy Prince, "Navigating Peak Demand," *Carbon Tracker* (2024), https://carbontracker.org/reports/navigating-peak-demand/ and Coffin, "Oil and Gas Transition Plans: A User Guide".

Natural Resource Governance Institute

Carbon Tracker Initiative

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The Natural Resource Governance Institute is an independent, non-profit organization that supports informed, inclusive decision-making about natural resources and the energy transition. We partner with reformers in government and civil society to design and implement just policies based on evidence and the priorities of citizens in resource-rich developing countries. Learn more at **www.resourcegovernance.org**

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The Carbon Tracker Initiative is a team of financial specialists making climate risk real in today's capital markets. Our research to date on unburnable carbon and stranded assets has started a new debate on how to align the financial system in the transition to a low carbon economy. **www.carbontracker.org**

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