SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

In the Matter of the Application of the PEOPLE OF THE STATE OF NEW YORK, by BARBARA D. UNDERWOOD, Attorney General of the State of New York, Petitioner, – against – PRICEWATERHOUSECOOPERS LLP and EXXON MOBIL CORPORATION, Respondents.	Index No. 451962/2016 IAS Part 61 Hon. Barry R. Ostrager Motion Sequence No. 7

AFFIRMATION OF JOHN OLESKE IN SUPPORT OF THE OFFICE OF THE ATTORNEY GENERAL'S MOTION TO COMPEL COMPLIANCE WITH INVESTIGATORY SUBPOENAS

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JOHN OLESKE, under penalty of perjury, affirms:

1. I am Senior Enforcement Counsel to the Office of the Attorney General of the State of New York ("OAG"), counsel for petitioner. I make this affirmation in support of OAG's motion to compel Exxon Mobil Corporation ("Exxon") to produce (i) the cash flow projections in the form of spreadsheets and their backup materials (hereafter "cash flow spreadsheets") for 26 of its major oil, gas and petrochemical projects and assets, as specified in Exhibit A to the proposed order annexed to the accompanying notice of motion, and (ii) the documents previously provided by Exxon to the Securities & Exchange Commission ("SEC") relating to impairment evaluations, reserves assessments, and climate change.

2. I make this affirmation to describe the factual basis of OAG's investigation, and the relationship between the information and documents sought on this motion and that investigation, based on personal knowledge and my review of the court docket and referenced documents and testimony.

I. <u>Factual Basis for OAG's Investigation</u>

3. The evidence obtained in this investigation establishes a factual basis for OAG's continuing investigation into whether Exxon has made false and misleading public representations about its use of projected costs of greenhouse gas ("GHG") emissions as a proxy for the effects of future GHG-related regulations on Exxon's business ("proxy costs"). Exxon represented that it applied proxy costs as set forth in its annual Outlook for Energy reports ("Outlook Reports") in its investment decisions, business planning, and financial reporting. The evidence shows, however, that Exxon maintained an undisclosed internal corporate policy, documented in its internal Corporate Plan Appendices to the Dataguide ("Corporate Plan"), which directed its business units to use a second set of proxy costs ("Corporate Plan Proxy Costs") that were significantly lower and less protective against climate change risk than the

proxy costs set forth in Exxon's public Outlook Reports ("Outlook Proxy Costs") for several years. Additionally, the evidence indicates that after Exxon aligned the long-term Corporate Plan Proxy Costs with the relevant Outlook Proxy Costs, the company nevertheless directed its planners to use substantially lower, existing legislated cost figures in their cash flow spreadsheets rather than the rising proxy costs Exxon represented to investors it would use. Further, the evidence indicates that Exxon did not include proxy costs in the cost projections that it used in impairment evaluations prior to 2016.

A. Exxon's Public Representations Regarding Proxy Costs

4. Since at least 2010, in its annual Outlook Reports and elsewhere, Exxon has set forth its expectations concerning costs resulting from future government policies regarding climate change. Over time, these representations grew increasingly specific with respect to both the costs Exxon expected to incur and the company's use of a proxy cost to implement these assumptions in its decision-making and business planning.

5. In March 2014, Exxon issued two public reports, entitled *Energy and Climate* and *Energy and Carbon—Managing the Risks* ("*Managing the Risks*"), which provided further details about the company's purported use of proxy costs. These reports were issued in exchange for the withdrawal of two proposed shareholder resolutions that requested detailed financial analysis of the company's resilience to increased regulatory costs relating to global efforts to combat climate change. Attached as Exhibits 1 and 2 are *Energy and Climate* and *Managing the Risks*, respectively.[1]

6. In *Energy and Climate*, in a section entitled "The Outlook for Energy: A View to 2040," Exxon explained that "for our Outlook we use a cost of carbon as a proxy to model a

[1] All exhibits attached to this affirmation are true and correct copies of the document described.

wide variety of potential policies that might be adopted by governments to help stem GHG emissions." (Ex. 1, *Energy and Climate* at 5-6.) Exxon stated that "[t]his GHG proxy cost is integral to ExxonMobil's planning." (*Id.* at 6.) Later in the report, under the subheading "Evaluating climate risk in our planning," Exxon expounded on its "robust process for evaluating investment opportunities" by touting the fact that it "requires that all business units use a consistent corporate planning basis, including the proxy cost of carbon discussed above, in evaluating capital expenditures and developing business plans." (*Id.* at 20.)

7. The report also included a color-coded map of the world from the 2013 Outlook Report entitled "CO2 'proxy' cost" that purported to show the "assumed cost of CO2 emissions associated with public policies in 2040 in 2012 dollars." The map divided the world into three categories for purposes of proxy cost application: "More than $40 per ton" (most of the OECD countries), "$20-40 per ton" (mostly non-OECD countries, including China, Indonesia, and Russia, among others); and "Less than $20 per ton" (the remaining non-OECD countries).[2] (*Id.* at 6.) The report stated that it expected "OECD nations to continue to lead the way" in adopting regulatory policies to limit GHG emissions, "with developing nations gradually following, led by countries like China and Mexico." (*Id.* at 5.)

8. In the other March 2014 report, *Managing the Risks*, Exxon claimed to "address the potential of future climate-related controls, including the potential for restriction on emissions, through the use of a proxy cost of carbon." (Ex. 2, *Managing the Risks* at 17.) Exxon represented that it "require[s] that investment proposals reflect the climate-related policy decisions [the company] anticipate[s] governments making during the Outlook period and therefore incorporate[s] them as a factor in [its] specific investment decisions." (*Id.* at 18.)

[2] "OECD" refers to the Organisation for Economic Co-operation and Development, which includes 35 developed and emerging countries as members.

Along much the same lines, Exxon represented that it "require[s] that all significant proposed projects include a cost of carbon – which reflects our best assessment of costs associated with potential GHG regulations over the Outlook period – when being evaluated for investment." (*Id.* at 21.) Exxon further represented that proxy costs would increase over time as a result of the fact that "[g]overnments' constraints on use of carbon-based energy sources and limits on greenhouse gas emissions are expected to increase throughout the Outlook period." (*Id.* at 15.) In conclusion, Exxon claimed that its use of a proxy cost in its investment decision-making, business planning, and financial reporting allowed the company to assure investors that it was "confident that none of [its] hydrocarbon reserves are now or will become 'stranded.'" (*Id.* at 1.)

9. Exxon's March 2014 reports did not disclose that, as discussed below (*see infra* ¶¶ 23-44), the company maintained two sets of proxy costs, and that one of these sets of proxy costs was lower than those disclosed in the Outlook Reports.

10. Exxon has repeatedly quoted from and referred investors to the proxy cost-related representations in its two March 2014 reports, including in media interviews, on its external website (including in Corporate Citizenship Reports), in filings with the SEC, in Carbon Disclosure Project submissions, and in other communications to market analysts, concerned investors, and the general public. For example, in its 2017 Proxy Statement opposing a shareholder proposal that sought to address "climate change related risks of stranded carbon assets," Exxon referred concerned shareholders to *Managing the Risks*, which it claimed "describes how the Company integrates consideration of climate change risks into planning processes and investment evaluation." Attached as Exhibit 3 is Exxon's 2017 Proxy Statement. (*See id.* at 61.)

11. Exxon has also pointed to its application of proxy costs in attempting to avoid

further disclosure to investors. In a 2016 letter to the SEC opposing a shareholder proposal for additional company disclosures regarding climate change risk, Exxon explained that its proxy cost "represents the Company's estimate of the cost of expected policy actions to reduce carbon emissions over the Company's business planning horizon," and that it "has tied its analysis of a proxy cost of carbon and that cost's effect on the company's oil and gas reserves to the time period between now and 2040." Attached as Exhibit 4 is Exxon's February 29, 2016 letter to the SEC. (*See id.* at 6.)

12. Moreover, Exxon has publicly claimed that its Outlook Proxy Cost has been in use since 2007. For example, in a December 2, 2015 publication on Exxon's corporate website, entitled *ExxonMobil and the carbon tax*, Exxon specified that the company "ha[d] included a proxy price on carbon in [its] business planning since 2007," in order "to analyze the impact of a price on carbon on various investment opportunities." Attached as Exhibit 5 is *ExxonMobil and the carbon tax*. (*See id.* at 3-4.)

13. In May 2016, at Exxon's annual shareholder meeting, the company's then-Chairman and CEO, Rex Tillerson, provided the following response to a concerned investor's inquiry about the company's management of climate-change risks:

> We have, unlike many of our competitors, we have for many years included a price of carbon in our outlook. ***And that price of carbon gets put into all of our economic models when we make investment decisions as well***. ***It's a proxy.*** We don't know how else to model what future policy impacts might be. But whatever policies are, ultimately they come back to either your revenues or your cost. So we choose to put it in ***as a cost***. So we have accommodated that uncertainty in the future, and ***everything gets tested against it***.

Attached as Exhibit 6 is a transcript of the 2016 Annual Meeting. (*See id.* at 26.) (Emphasis added.) Mr. Tillerson's assertion that Exxon's Outlook Proxy Costs are incorporated "as a cost," rather than as a factor affecting revenues, is directly contrary to Exxon's current position that Outlook Proxy Costs relate only to Exxon's demand and revenue projections. (*See infra* ¶ 41.)

B. Exxon's Public Representations Regarding Reserves

14. Exxon's representations about its use of a proxy cost also implicate its representations about the size and value of its resource base and company reserves, as the company has implied that its estimates of the amount of those resources and reserves include the application of proxy costs. Specifically, Exxon has represented that the total size of its resource base is roughly 90 billion oil-equivalent barrels and that "The size and diversity of [its] global resource base, the largest held by an international oil and gas company, provide [Exxon] with unequaled investment flexibility to profitably develop new supplies of energy to meet future demand." Attached as Exhibit 7 is the 2014 ExxonMobil Financial & Operating Review. (*See id.* at 17, 24.) Exxon's resource base, which is calculated as part of the company reserves process, "includes quantities of oil and gas that are not yet classified as proved reserves under SEC definitions, but that [Exxon] believe[s] will ultimately be developed." (Ex. 2, *Managing the Risks* at 25.)

15. Unlike Exxon's estimates of proved reserves pursuant to SEC regulations, which require the use of historical price assumptions and cost assumptions under the existing regulatory regime, company reserves estimates are based on Exxon's own price and cost assumptions, which purportedly include proxy cost assumptions. [redacted] Attached as Exhibit 8 is PNYAG0342309 [redacted]. (*See id.* at 1.)

16. Exxon has also told investors repeatedly, including in its *2016 Energy and Carbon Summary*, that its company reserves and resource base estimates are "aligned with"

industry guidelines for calculating reserves and resources – called the Petroleum Resources Management System ("PRMS") – which are maintained by the Society of Petroleum Engineers and other industry groups. Attached as Exhibit 9 is the *2016 Energy and Carbon Summary*. (*See id.* at 2.)

17. Those PRMS guidelines require a company to apply "a consistent set of forecast conditions, including assumed future costs and prices." Attached as Exhibit 10 is the Petroleum Resources Management System. (*See id.* at § 2.2.2.) A proxy cost for GHG emissions is a quintessential "assumed future cost." The guidelines further specify that the "estimated costs associated with the project . . . including environmental . . . costs charged to the project, [should be] based on the [company's] view of the costs expected to apply in future periods." (*Id.* § 3.1.1.)

18. [redacted] Attached as Exhibit 11 is EMC 003030973, a copy of that email. (*See id.* at 4.) [redacted]

19. If Exxon failed to include applicable proxy costs in these company reserves calculations, then Exxon potentially misled investors about the size of its total resource base. [redacted] Attached as Exhibit 12 is a transcript of [redacted] testimony. (*See id.* at 96-98.)

C. Exxon's Public Representations Regarding Impairment

20. Exxon also repeatedly assured its investors in its annual securities filings that it

followed generally accepted accounting principles ("GAAP"). Per GAAP, in evaluating whether its assets may be impaired (*i.e.*, whether they must be written down on its balance sheet), Exxon represented that it used assumptions – like the inclusion of proxy costs in relevant calculations – consistent with those it used in its investment and planning decisions. For example, in its 2015 Form 10-K, Exxon stated: "Cash flows used in impairment evaluations . . . make use of the Corporation's price, margin, volume, and cost assumptions developed in the annual planning and budgeting process, and are consistent with the criteria management uses to evaluate investment opportunities." Attached as Exhibit 13 is Exxon's 2015 Form 10-K. (*See id.* at 56-57, 70.) This representation may be misleading to the extent that Exxon was not incorporating the proxy cost assumptions it publicly described in its impairment evaluations.

21. Exxon's use of consistent assumptions in its impairment evaluations is also called into question by its reserves estimation practices, as discussed above, because documents and testimony indicate that Exxon's company reserves estimates are an input into its impairment evaluations. [redacted] Attached as Exhibit 14 is a transcript of [redacted] testimony. (*See id.* at 42, 297-99.) [redacted] (Ex. 12, [redacted] Tr. 281.)

22. [redacted]

Attached as Exhibit 15 is PNYAG0001270, a copy of this memorandum. (*See id.* at 41.)

D. Exxon's Internal Practices

1. Exxon's Apparent Use of Undisclosed Corporate Plan Proxy Costs

23. While Exxon publicly disclosed only a single set of proxy costs, Exxon in fact maintained two distinct sets of proxy costs internally—the Outlook Proxy Costs and the undisclosed Corporate Plan Proxy Costs. Exxon's undisclosed Corporate Plan Proxy Costs deviated from the public Outlook Proxy Costs in at least two distinct ways, over two separate, but overlapping timespans.

24. *First*, from at least 2010 through mid-2014, the Corporate Plan directed the use of proxy cost figures for projects in OECD countries that were significantly lower than the long-term Outlook Proxy Costs assigned to those jurisdictions. For example:

- In 2010, Exxon publicly represented that its Outlook Proxy Cost for OECD countries was $60/ton of emissions in 2030, while internally, its undisclosed Corporate Plan Proxy Cost was only $40/ton in 2030. Attached as Exhibits 16 and 17 are the 2010 Outlook Report and 2010 Corporate Plan, respectively. (*See* Ex. 16 at 29; Ex. 17 at 37.)
- In 2012 and 2013, Exxon publicly represented that its Outlook Proxy Cost was $60/ton in 2030, as before, and $80/ton in 2040. Internally, Exxon's Corporate Plan Proxy Cost still reached only $40/ton by 2030 for OECD countries, and did not extend to 2040. Attached as Exhibits 18 and 19 are the 2012 Outlook Report and 2012 Corporate Plan, respectively. (*See* Ex. 18 at 29-30; Ex. 19 at 34.)

25. In the speaker notes of a May 2014 presentation to Mr. Tillerson, Exxon's GHG Manager, Guy Powell, recommended aligning the figures in the Corporate Plan instructions with those in the Outlook Reports on the basis that Exxon's March 2014 reports to shareholders had "implied that we use the [Outlook] basis for proxy cost of carbon when evaluating investments."[3] Mr. Powell also noted that the lower Corporate Plan Proxy Costs were "non-conservative" (*i.e.*,

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[3] [redacted] (Ex. 21, [redacted] Tr. 362:6-8.)

risky) in comparison to the Outlook Proxy Costs for projects that created GHG emissions. Attached as Exhibit 20 is EMC 000539903, a copy of this presentation with speaker notes.

26. [redacted] Attached as Exhibit 21 is the transcript of [redacted] testimony. (*See id.* at 358-73.)

27. In June 2014, one month after the May 2014 presentation in which Exxon's GHG Manager effectively acknowledged that Exxon's representations were misleading, Exxon aligned the long-term Corporate Plan Proxy Costs with the proxy costs in the Outlook Reports, but for OECD countries only. Attached as Exhibits 22 and 23 are Exxon's 2014 Outlook Report and 2014 Corporate Plan, respectively. (*See* Ex. 22 at 32; Ex. 23 at 31.)

28. It appears that Mr. Tillerson had known about and expressly approved of this discrepancy for at least the prior three years. For example, on April 22, 2011, Robert Bailes, Exxon's then-GHG Manager, raised the question of "whether to harmonize" the Corporate Plan Proxy Costs with the Outlook Proxy Costs, and noted that doing so would "provide more clarity and alignment throughout organization" and would be "rational." Tom Eizember, an Exxon Planning Manager, responded the same day by stating: "Rex [Tillerson] has seemed happy with the difference previously – appeared to feel it provides a 'conservative' basis (but only if viewed from the perspective of claiming economics credits to reduce emissions; it is not conservative vs EO [the Outlook Report] from the perspective of debiting actions that increase emissions)." Attached as Exhibit 24 is EMC 000354827, a copy of this email thread.

29. *Second*, between at least 2012 and 2016, the Corporate Plan directed Exxon planners not to use *any* proxy costs in the cost projections in their base economic models (as opposed to sensitivity analyses) for projects in non-OECD countries, despite the fact that the

Outlook Reports set forth proxy costs in non-OECD jurisdictions. (*See, e.g*., Ex. 19, 2012 Corporate Plan at 34; Ex. 18, 2012 Outlook Report at 30.)

30. The direction in the Corporate Plan to apply proxy costs only in sensitivity analyses for non-OECD countries, and not in base economic models, is significant, as base economic models are typically considered more important for planning purposes than sensitivity analyses, which test a range of hypotheticals that are considered less likely to occur. [redacted] Attached as Exhibit 25 is a transcript of [redacted] testimony. (*See id.* at 183-84.)

31. [redacted] Attached as Exhibit 26 is a transcript of [redacted] testimony. (*See id.* at 644, 648-50.)

32. Exxon did not resolve the discrepancy between the Outlook Proxy Costs and Corporate Plan Proxy Costs with respect to non-OECD countries until June 2016 [redacted] Attached as Exhibit 27 is Exxon's 2016 Corporate Plan. (*See id.* at 29.)

33. Any Exxon planner following the Corporate Plan would have generated forecasts that were less protective against climate change risk than those they would have generated had they applied the proxy costs described to investors. Indeed, Mr. Bailes wrote in an internal email

on April 30, 2010, that he "[r]ecognize[d]" that the "2030 cost of $40/T [ton]" in the Corporate Plan "is a conservative (low) estimate" of costs likely to be incurred, and that the Outlook Report's "assumption of $60/T is likely more realistic." Attached as Exhibit 28 is EMC 000339155, a copy of this email.

34. Exxon's witnesses have been unable to explain any reason for the divergence between the Outlook Proxy Costs and the Corporate Plan Proxy Costs that is consistent with the evidence. [redacted] Attached as Exhibit 29 is a transcript of [redacted] testimony. (*See id.* at 183-84, 267-78.)

35. In response to OAG's motion papers highlighting these issues, Exxon asserted in in its June 9, 2017 papers that there is no disconnect between the company's public representations and its internal policy, because (i) the Outlook Proxy Cost described in its public representations is used only for purposes of projecting oil and gas demand, which influences oil and gas price projections and ultimately projected revenues, while (ii) the Corporate Plan Proxy Cost is actually a separate "GHG cost" that applies only to projecting Exxon's expenses in connection with its capital investments in oil and gas projects.

36. Notably, however, Exxon's public representations prior to its June 9, 2017 papers, as set forth *supra* at ¶¶ 4-22, did not disclose that Exxon used a different, lower proxy cost for

calculating its projected expenses. To the contrary, these representations described "proxy cost" as a single concept, and highlighted Exxon's purported use of a "consistent corporate planning basis." (*See supra* ¶ 6.) Indeed, an Exxon employee admitted that Exxon's representations were inconsistent with its use of two different costs, stating internally that "we have implied that we use the [publicly disclosed] basis for proxy cost of carbon when evaluating investments." (*See supra* ¶ 25.)

37. The evidence to date also indicates that, notwithstanding the purposes for which they were used, Exxon's Outlook Proxy Cost and Corporate Plan Proxy Cost both were intended to represent a best estimate of the additional costs likely to be imposed as a result of climate change-related regulation over the coming decades, in jurisdictions around the world. As such, both figures are a "proxy" for projected "GHG costs," and Exxon never explained to the public that these apparently interchangeable terms referred to two different sets of costs.

38. Exxon has also used the term "proxy" to refer internally to the costs in its Corporate Plan that it now insists can only be described as "GHG costs." [redacted] Attached as Exhibit 30 is EMC 003354181, a copy of this email. (Emphasis added.)

39. The inverse is also true; Exxon has used the term "GHG costs" to refer internally to Outlook Proxy Costs. [redacted] Attached as Exhibit 31 is EMC 003203448,

a copy of this email. (*See id.* at 1-2.) (Emphasis added.)

40. Likewise, after discussions with Exxon personnel, PwC used the terms "proxy costs" and "GHG costs" interchangeably to refer to Corporate Plan Proxy Costs in a February 2017 memorandum. Attached as Exhibit 32 is PNYAG0199237, a copy of this memorandum.

41. Additionally, as set forth above, Exxon's then-Chairman and CEO Rex Tillerson stated at Exxon's annual shareholder meeting in 2016 that (i) generally, a company can assume that future GHG-related costs will affect either its revenues or its costs, and that (ii) Exxon "choose[s] to put" its "proxy" cost "in as a cost." (*See supra* ¶ 13.) This directly contradicts Exxon's current position that proxy costs, as described in its public representations, affect only Exxon's demand and revenue projections, rather than its cost projections.

42. Further, prior to OAG's motion papers highlighting the deviations between Exxon's public statements and its internal policies, Exxon's counsel not only did not disclose to OAG or the Court any distinction between proxy costs and so-called "GHG costs," but in fact affirmatively asserted to OAG and the Court that the Corporate Plan contains Exxon's "proxy cost"-related policies. For example:

- On January 6, 2017, Exxon represented to the Court that OAG's requests for documents "reflect[ing] Exxon's actual incorporation of the proxy cost of carbon into specific oil and gas projects" was "simply asking for duplicative information," because "[t]he Corporate Plan Dataguides and Appendices, produced to [OAG] on December 31, 2016, contain the information that [OAG] purports to seek." Attached as Exhibit 33 is Exxon's January 6, 2017 letter to the Court. (*See id.* at II-1 & n.5.)

- Similarly, on February 11, 2017, Exxon wrote to OAG asserting that there was no need for it to produce "further documentation showing how the Company applies a proxy cost of carbon," because Exxon had already produced the "ExxonMobil [Corporate Plan] Dataguide Appendices, *i.e.*, internal policy documents that specify precisely how ExxonMobil applies its proxy cost of carbon in every jurisdiction worldwide through the year 2040." Attached as Exhibit 34 is Exxon's February 11, 2017 letter to OAG. (*See id.* at 2.)

- On March 16, 2017 and April 27, 2017, Exxon repeated this argument verbatim in letters to the Court and OAG. Attached as Exhibits 35 and 36 are Exxon's March 16, 2017 letter to the Court and April 27, 2017 letter to OAG respectively. (Ex. 35 at 4; Ex. 36 at 3 n.5.)

43. After being confronted with significant differences between its Corporate Plan and its public representations, Exxon asserted that its Corporate Plan does *not* specify how it applies its "proxy" cost of carbon, but rather its "GHG costs." (*See supra* ¶ 35.)

44. Exxon recently published a new climate change report directed at investors and the public entitled *2018 Energy & Carbon Summary*. For the first time, Exxon appears to have attempted to assert outside of court papers the new purported distinction between the scope and use of its public "proxy costs" and its internal "GHG costs." Attached as Exhibit 37 is Exxon's *2018 Energy & Carbon Summary*. (*See id.* at 21.) However, the company made no effort to explain or remedy its conflation (at best) of the two costs in numerous communications to investors over the prior years.

2. Exxon's Apparent Use of Existing Legislated Costs in Lieu of Proxy Costs

45. According to Exxon's recently produced documents, after Exxon aligned the instructions in its Corporate Plan with the Outlook Proxy Costs for OECD countries in June 2014, planners from Exxon's Imperial Oil Limited subsidiary ("Imperial") responsible for the company's oil sands projects in Alberta, Canada encountered adverse results when they tried to apply the applicable proxy cost figures from the Corporate Plan in the cash flow spreadsheets for these high-emissions projects. Facing high projected costs, these planners were apparently directed by management *not* to apply proxy costs, and instead to apply lower, existing legislated costs, and to hold those costs flat indefinitely into the future.

46. Assuming that existing costs will remain in place indefinitely directly contradicts Exxon's public statements that it expects the GHG-related costs imposed by governments to rise over time, and that it uses a proxy cost to take into account those projected rising costs. (*See*

supra ¶¶ 6-8.) The evidence indicates that instead of using a proxy cost mechanism to model, for economic evaluation and decision-making purposes, the increasingly stringent projected policies that Exxon discussed publicly, Exxon frequently acted in a manner directly contrary to its representations by assuming that carbon policies would not become more stringent, but instead would remain the same decades into the future.

47. [redacted] Attached as Exhibit 38 is EMC 002875747, a copy of this email thread.

48. Under this "alternate methodology," Exxon appears to have instructed the planners in business units responsible for the Alberta projects not to use the Outlook or the Corporate Plan Proxy Costs in their cash flow spreadsheets, and instead to use figures reflecting only the existing costs imposed by Alberta law then in place at the time the cash flow spreadsheets were being used. [redacted] Attached as Exhibit 39 is EMC 002879540, a copy of this email thread.

49. This is confirmed by a cash flow spreadsheet Exxon produced for [redacted]. Attached as Exhibit 40 is EMC 003697717, a copy of this cash flow spreadsheet.

50. [redacted]

[redacted] Attached as Exhibit 41 is EMC 003010467, a copy of this invitation.

51. In addition to apparently directing the planners to assume that then-current regulatory costs would remain in place and be held flat, without escalation, for all future years, Exxon management also apparently directed planners to assume that only a very limited percentage of GHG emissions would be taxed, indefinitely into the future. [redacted] Attached as Exhibit 42 is EMC 001850584, a copy of this email thread.

52. [redacted] Attached as Exhibit 43 is EMC 001850439, a copy of this email. (Emphasis added.) In other words, Exxon decided to apply a projection that (i) no new GHG costs would be imposed throughout the life of the project, and (ii) only [redacted]% of GHG emissions

would be taxed (*i.e.*, a "legislated intensity" of [redacted]%), indefinitely into the future.

53. There is no evidence that Exxon ever generated or distributed any justification or explanation of how such an assumption could be squared with Exxon's stated assumption in the Outlook Reports that governments would impose *increasing* costs on GHG emissions over time, with "OECD nations [such as Canada] to continue to lead the way." (Ex. 1, *Energy and Climate* at 5.)

54. Moreover, a flat cost assumption in Alberta is contrary to the company's experience in that province, as Alberta's carbon tax has increased in recent years. For example:

- In 2007, the price set by the Alberta government was $15 per ton of carbon dioxide equivalent. Attached as Exhibit 44 is a 2007 Alberta government report showing the initial price of carbon under Alberta Regulation 139/2007. (*See id.* at 2.)
- In 2015, the price was raised to $20 per ton for the year 2016, and to $30 per ton for the year 2017. Attached as Exhibit 45 is Alberta Ministerial Order 13/2015, which mandated this increase in the price of carbon.

55. Exxon has produced a few examples of cash flow spreadsheets relating to Alberta oil sands projects that were attached to emails or located in files in [redacted] custody, including the [redacted] spreadsheet discussed *supra* at ¶ 49. Based on OAG's preliminary analysis of those spreadsheets and related communications, the use of existing regulatory costs for Alberta oil sands projects in 2015 undercounted the applicable long-term operating expenses expected to be imposed by future regulation by as much as 93% on a per-barrel basis, as compared to the results that would have been computed if the Outlook Proxy Costs were applied in accordance with Exxon's representations to investors. [redacted] This indicates that applying existing, legislated GHG costs in Alberta, rather than the proxy costs set out in Exxon's internal guidance, resulted in a reduction in projected GHG costs from approximately $[redacted] per

barrel to $[redacted] per barrel, a reduction of over 93%. Attached as Exhibit 46 is EMC 002881265, a copy of this email.

56. The most complete example of a cash flow spreadsheet Exxon has produced is related to the [redacted] project, in which Exxon had invested more than $[redacted] billion in capital expenditures by 2015[redacted] Attached as Exhibit 47 is an article describing costs associated with [redacted]. By using its "alternate methodology," which was to apply a flat legislated cost instead of the rising Outlook Proxy Costs in the 2015 cash flow spreadsheet for [redacted] (*see supra* ¶ 49), Exxon appears (based on OAG's preliminary analysis) to have undercounted the projected lifetime operating expenses of [redacted], as enhanced by a potential future investment, by more than $[redacted] billion. Depending on Exxon's assumptions about the price of oil, this decision may have made the difference between positive cash flows and negative cash flow projections, and potential reductions in associated reserves.

57. According to Exxon's employees, the use of lower cost assumptions would be expected to inflate projected profitability, and consequently, the expected field life of the relevant projects and the associated estimates of the company's resource base. [redacted] Attached as Exhibit 48 is EMC 001427003, a copy of this email.

58. [redacted]

[redacted] In other words, by not applying the Corporate Plan and Outlook Proxy Costs, Exxon projected that it would be profitable for the company to continue producing at [redacted] for a significantly longer period of time. Attached as Exhibit 49 is EMC 001098246, a copy of this email.

59. [redacted] (Ex. 12, [redacted] Tr. 517-18.)

60. Beyond Alberta, OAG is investigating whether, in similar fashion, Exxon deviated from its Outlook and Corporate Plan directing the use of proxy costs in other countries and regions.

3. Exxon's Apparent Failure to Use Proxy Costs in Impairment Evaluations

61. Documents and testimony from Exxon and PwC indicate that the Outlook and Corporate Plan Proxy Costs were not included prior to 2016 in the cost projections in cash flow spreadsheets used for Exxon's evaluations of its long-lived assets for potential impairment and write-down or removal from its balance sheet.

62. [redacted] Attached as Exhibit 50 is a transcript of [redacted] testimony. (*See id.* at 128-29, 136-37.) [redacted] In this way, Exxon may have acted inconsistently with its representations that, per

GAAP, it used economic assumptions for impairment evaluation purposes that were consistent with those it used in its investment and planning decisions. (*See supra* ¶ 20.)

II. OAG's Requests Are Reasonably Related to Its Investigation of Exxon's Representations Concerning Its Use of Proxy Costs

A. Cash Flow Spreadsheets

63. Cash flow spreadsheets, referred to by company planners as economic models, set forth Exxon's projections with respect to the revenues and profitability of its projects and assets, and the factors that influence revenues and profits. These factors include, for example, projected oil and gas production, oil and gas prices, capital expenditures, operating expenditures, and, to the extent they were incorporated, proxy costs. These projections generally represent Exxon's best estimates of future economic conditions, and are central to core decision-making, planning, and reporting processes at Exxon.

64. According to Exxon's documents and witness testimony, the company's planners and managers routinely created, used, and updated these cash flow spreadsheets for purposes of: evaluating new investments (Ex. 50, [redacted] Tr. 55-56); conducting ongoing corporate planning for projects that the company had already invested in (Ex. 51, [redacted] Tr. 60-61); estimating company hydrocarbon reserves and resources (Ex. 12, [redacted] Tr. 87, 96-97, 105-09, 184-87); and evaluating whether its long-lived assets were impaired (Ex. 14, [redacted] Tr. 255-56, 261-62, 266-68). Attached as Exhibit 51 is a transcript of [redacted] testimony.

65. Exxon's witnesses have explained that these cash flow spreadsheets are likely to provide direct evidence of whether and to what extent Exxon used proxy costs. For example:

- [redacted] (Ex. 25, [redacted] Tr. 383-84.)
- [redacted]

[redacted] (Ex. 29, [redacted] 72-73.)

- [redacted] Ex. 21, [redacted] Tr. 148-49.)

66. In testimony, Exxon's witnesses have been unable to recall what proxy costs, if any, were used in any specific projects, making it essential for OAG to review the final cash flow spreadsheets themselves to see the final numbers Exxon actually used to make decisions. [redacted] (Ex. 26, [redacted] Tr. 367.) [redacted] (*Id.* at 396-397.) [redacted] (Ex. 51, [redacted] Tr. 101-02.) [redacted] (*Id.* at 102-04.)

67. OAG selected the 26 projects and assets subject to its requests for cash flow spreadsheets used since 2010 to capture a reasonable cross-section of Exxon's largest projects and assets. Each of those selected involved Exxon's investment of many millions, if not billions, of dollars in capital. Each is notable for generating (or being forecasted to generate) significant GHG emissions. Together, they reflect the geographic diversity of Exxon's worldwide operations, the functional diversity of the principal subsidiaries responsible for supervising

Exxon's major projects and assets, and the diversity in commercial maturity of the projects and assets themselves, including some still under consideration for investment, some that have only recently been approved for investment, and some more established projects and assets. In particular, OAG's list of 26 projects and assets includes:

- Four Canadian oil sands projects and assets (Aspen, Cold Lake, Kearl, Syncrude) and two additional upstream Canadian projects and assets (Hebron, Horn River).
- Four additional upstream projects and assets in OECD countries (Julia, Mobile Bay, and Point Thomson in the United States; Gorgon in Australia).
- Six upstream projects and assets in non-OECD countries (Cepu, Indonesia; Guyana; Kara Sea, Russia; Kashagan, Kazakhstan; Sakhalin, Russia; Tapis, Malaysia).
- Three United States downstream and/or petrochemical projects and assets (Baton Rouge, Baytown, Beaumont), two such facilities in Europe (Antwerp, Rotterdam) and one in Canada (Strathcona).
- Exxon's 2010 acquisition of XTO for approximately $44 billion.[4]
- Three upstream XTO projects and assets in the United States (Bakken, Barnett, Uintah).

68. These 26 projects and assets represent a fraction of Exxon's operations around the world. For example, [redacted] Attached as Exhibit 52 is PNYAG0500870, a copy of this list.

69. As noted in the proposed order submitted with this motion, OAG's request calls for Exxon to produce the cash flow spreadsheets in native format, without redaction, and to provide any backup materials necessary to determine whether any proxy costs were in fact included. The spreadsheets OAG has received to date contain complex, interrelated data, and understanding how they function requires production in a format that preserves that data.

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[4] [redacted] (Ex. 14, [redacted] Tr. 247-49.)

Exxon's witnesses have testified that proxy costs may in some cases be broken out as a separate line item within cash flow spreadsheets, but in other cases may be subsumed within another line item, which will require the production of backup materials such as input files in order to identify the relevant figures. (*See, e.g.*, Ex. 51, [redacted] Tr. 123-24; Ex. 26, [redacted] Tr. 281; Ex. 29, [redacted] Tr. 77-78.)

70. With respect to impairment evaluations in particular, Exxon's own cash flow spreadsheets are key evidence of whether the economic assumptions that Exxon used in these evaluations comported with those that it used in its other business functions. [redacted] (Ex. 14, [redacted] Tr. 255-56, 261-62, 266-68; *see also* Ex. 29, [redacted] Tr. 77-78).

71. [redacted] Exxon, by contrast, faces no such obstacle to producing the cash flow spreadsheets it relied on in performing its impairment evaluations.

B. Documents Provided to the SEC

72. According to public reports, the SEC is investigating how Exxon incorporates climate change into its reserves and impairment accounting. Attached as Exhibit 53 is a September 20, 2016 article on this topic from the Wall Street Journal.

73. [redacted] Attached as Exhibit 54 is PNYAG0579453, a February 8, 2017 letter from Exxon's outside counsel to PwC summarizing the SEC's requests for documents and Exxon's responses.

74. The subject matter of the SEC's investigation, like this investigation, concerns the intersection of climate change, financial reporting, and reserves estimation. As such, documents that Exxon has provided to the SEC are likely to be highly relevant to OAG's investigation. Exxon has not denied that its productions to the SEC concern relevant topics that are responsive to OAG's Subpoenas, but continues to resist OAG's request on federal preemption grounds.

Conclusion

75. OAG respectfully requests that the Court compel Exxon to produce the cash flow spreadsheets identified in the proposed order submitted herewith, as well as the documents it has provided to the SEC, and make other and further orders as the Court deems just and proper.

Dated: June 19, 2018
New York, New York

John Oleske