Saudi Aramco

Saudi Arabia, Oil & Gas

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Report date: March 23 2021
AGM: May 2021 (TBC)</td></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td><td rowspan="2">CA 100+ company, so seen by investors as key to driving global net zero emissions</td></tr>
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<tr><td colspan="7">Summary view:
• As the world's largest crude oil producer, Saudi Aramco is both a significant contributor to carbon emissions and faces significant climate change risks. Despite this, the Audited Consolidated Financial Statements and Auditor's Report are silent on the extent, if any, to which climate change considerations impact any accounting judgements.
• On the other hand, there is some reasonable discussion of climate change risks in the narrative reporting of the annual report and there are some brief general references to Paris alignment and carbon emission measures.</td></tr>
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Background

<u>The Business</u>

- Saudi Aramco is the national oil company of Saudi Arabia. The world's largest producer of crude oil, it manages the world's largest conventional hydrocarbons reserve. At the end of 2020, proved reserves were 255.2 billion barrels of oil equivalent, with 12.4 million barrels of oil equivalent produced per day (equating to a proved reserves life of 56 years).
- In December 2019, Saudi Aramco IPO'd on the Saudi stock exchange, raising $29.4bn with a market cap of nearly $2trn. The Government of Saudi Arabia retains a 98% shareholding.
- Although primarily an upstream crude oil producer in Saudi Arabia, Aramco also owns significant downstream refining and petrochemicals assets across the world. In 2020, Aramco bought 70% of Saudi Basic Industries Corporation, marking a further downstream expansion.

<u>Approach to climate change</u>

- Saudi Aramco makes a number of high-level comments suggesting an appreciation of climate change issues, referring to the "global effort to building a low carbon economy", but lacks any specific targets or discussion of climate change assumptions or scenarios.
- There is a reasonable discussion of climate change risks to Aramco, including: the impact on the demand for, and price of, hydrocarbons; the growth and pricing of alternative energy sources, including renewables; and litigation risk, especially in the USA (where Motiva, a US refining affiliate of Aramco, is already a defendant in a case concerning climate change). Furthermore, the risk section of the annual report says that climate change "could cause Aramco to incur costs or invest additional capital". Describing these various risks in the narrative reporting only serves to underline the disconnect with the audited financials that are silent on the extent, if any, to which these risks impact accounting judgements.
- The Report from the Risk and HSE (health, safety and environment) Committee states that the Committee "discussed and evaluated several corporate risks including those relating to climate change". In contrast, the Audit Committee Report does not mention any consideration of climate change issues.
- To the extent that there is any quantification of climate issues, it is largely restricted to highlighting some of Aramco's inherent strengths in this area: namely, that it is one of the world's lowest cost producers of crude oil with one of the lowest upstream carbon intensities. This refers to scope 1 and 2 emissions, where it aims to deliver "more energy with lower emissions", but ignores the much larger scope 3 emissions. As an exceptionally low-cost producer with low carbon intensity operations, it is fair that low emissions are a competitive edge for the company. In a scenario of significantly lower crude oil prices and/or increased focus on the carbon intensity of production, Aramco would be one of the last oil companies to remain profitable.

Accounting: judgements and consistency with other reporting

Accounting judgements		Significant concerns

- Consolidated financial statement are prepared in accordance with IFRS, as well as other standards and pronouncements by the Saudi Organisation for Certified Public Accountants.
- There is no apparent reference in the notes to the financial statements that accounting judgements have been impacted by climate-related considerations – even though there are a number of judgements that might be expected to be impacted, such as proved reserves, impairments and decommissioning costs.

Consistency with other reporting		Significant concerns

- The narrative reporting states that the estimate for proved oil reserves "conforms to the SPE-PRMS (Society of Petroleum Engineers – Petroleum Resources Management System) definitions and guidelines, which is the internationally recognized industry standard". However, neither the narrative reporting nor the financials disclose the underlying oil price and economic assumptions for the calculation of proved reserves ('proved reserves' are classified as having a 90% or greater likelihood of being present *and economically viable* for extraction in current conditions).
- Separately, the narrative reporting states that an "independent petroleum consultant, D&M, independently evaluated reservoirs Aramco believes to account for 85% of its proved oil reserves" as of December 31 2019. However, it is not disclosed what climate change considerations, if any, were made by the independent consultant.
- Beyond the narrative reporting in the annual report, Aramco does not yet produce other reporting relevant to climate change. It plans to publish a Sustainability Report in 2021.

Climate assumptions in accounts: visibility and Paris alignment

Visibility of climate assumptions in accounts		Significant concerns

- There are no apparent climate-related assumptions. There is thus no sensitivity analysis.

Paris alignment		Significant concerns

- With no visibility of climate assumptions, there can be no alignment with the goals of the Paris Agreement.
- The narrative discussion of the annual report states that "Aramco supports the objectives set by the Paris Agreement … including by holding the increase in the global average temperature to below 2C above preindustrial levels". However, there is no evidence of how, if at all, this declared support impacts either the company's targets nor feeds through to the financial statements and their accounting judgements.

Audit: visibility in KAMs and consistency check

Audit firm: PricewaterhouseCoopers	Responsible partner: Baber I. Benmohareb
Audit standards: International Standards on Auditing	

Visibility in Key Audit Matters		Significant concerns

- There is no reference to climate change in the auditor's report.
- There are only two KAMs identified, both of which relate to the 2020 acquisition 70% of downstream petrochemicals company SABIC: (i) accounting for the acquisition of SABIC; and (ii) assessment of recoverability of the goodwill and brand recognised as part of the

SABIC acquisition. For (i), the audit report refers to engaging an independent valuer to determine fair value of the purchase consideration, while (ii) relates to the requirement for goodwill and intangible assets to be tested annually for impairments. Climate change considerations could reasonably be expected to impact both KAMs.

- It is surprising that these are the only two KAMs given the various other key accounting judgements inherent in the financial reporting of a company of this nature.

Consistency check		Significant concerns

- The auditor's report outlines the scope of the auditor's work, which does not cover other information beyond the consolidated financial statement.
- The auditor does not express any form of assurance conclusion on this other information, although the auditor does consider whether it is materially inconsistent with the consolidated financial statements or otherwise appears to be materially misstated. For Aramco, the auditor had nothing to report in this regard.
- There do not appear to be any other disclosures from the company that are reviewed by an audit firm or subject to any kind of assurance.

The Climate Accounting Project is an independent investor-led project to reinforce the statements of the IASB and IAASB that material climate change issues are incorporated within their standards. This analysis seeks to understand the extent to which companies and auditors are delivering against this aspect of these standards and similar local standards.		**Key**
		Good practice
		Few concerns
		Some concerns
		Significant concerns

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