Testimony of

Dan K. Eberhart, CEO, Canary, LLC

Before the United States Senate Committee on Banking, Housing, and Urban Affairs

"Borrowed Time: The Economic Costs of Climate Change"

538 Dirksen Senate Office Building

August 4, 2022

Introduction

Chairman Brown, Ranking Member Toomey, and members of the Committee, thank you for inviting me to testify today on the economic costs of climate change. Climate change is one of the most significant issues of our time, and I am proud of the continuing role of the energy sector in reducing the carbon intensity of the energy Americans rely on every day.

As CEO of Canary, one of the largest privately held oilfield services companies in the United States, I am familiar with the positive impact business can have on communities, providing good paying jobs and benefits to the hundreds of workers who are proud to call us their employer. These are folks who proudly come to work every day committed to building our reputation of trust, quality service, and commitment to excellence. Today, however, we are increasingly challenged by the mountains of red tape imposed by regulators, which has disproportionately impacted our industry, one of the most heavily regulated in the country.

As CEO, I also understand the important role of business in addressing the environmental impacts of energy production and helping mitigate climate change. Canary is already required to operate in a manner that protects the environment and human health, responsibilities we take seriously. We are also one of the nation's most innovative industries, with billions of dollars invested industrywide to develop technologies that allow us to produce the abundant and affordable energy that Americans have come to depend on every day.

I firmly believe the oil and natural gas industry can be our nation's most formidable ally in the fight against climate change. But to do so, we need the government as a partner, not an adversary.

That is why I am concerned that the U.S. Securities and Exchange Commission's proposal mandating public companies report their emissions and exposure to climate risks is a major move in the wrong direction.

Proponents argue the SEC's proposed rule on "The Enhancement and Standardization of Climate-Related Disclosures for Investors" will provide investors with useful information on a company's exposure to climate risks, but the practical effect will be to drive capital away from badly needed conventional energy and infrastructure projects, making energy more expensive and denying America of a natural competitive advantage against other countries.

In a parallel trend in the capital markets, the growing popularity of environmental, social and governance (ESG) investment funds, are steadily strangling domestic oil production, which now sits at around 11.6 million barrels per day compared to its peak in 2019 of 13 million per day.

A report last year from the International Energy Forum estimates that 2021 oil and gas production remained 23 percent below the pre-pandemic level of $525 billion, while investment slumped by 30 percent in 2020. The report identified ESG as one of three principal drivers of underinvestment. That is a predictable result of the nearly $2.7 trillion in ESG funds that restrict investment in conventional energy producing companies.

As Committee members are undoubtedly aware, our economy faces an historic energy supply challenge. After a decade of underinvestment in the oil and gas sector, current domestic output sits well below pre-pandemic levels while demand continues to return. Unfortunately, much of this shortage is driven by domestic energy policy that has frozen new federal leasing and prohibited pipeline construction, discouraging the investment necessary to explore, develop, and produce the energy America needs to prosper.

Our industry requires capital and investor confidence to thrive. Investor confidence follows from reasonable and predictable regulation. Without those prerequisites, companies will not risk the capital needed to ensure we have a secure supply of energy. Decapitalizing the oil and gas industry in the fight against climate change will increase energy prices, restrict innovation, and shrink our economy.

Structural underinvestment has hampered capital-intensive activities across the upstream, midstream, and downstream sectors of our industry. Less than a decade ago, there were 1,600 active drilling rigs in the country. Today, there are roughly 500.

And while the SEC rule and adjacent policies undermine U.S. energy security and destabilize the economy, the administration has done little to nothing to address consumer demand for the underlying products. As an industry, we are responding to the market and projected increases in demand. By comparison, the mixed signals coming out of the administration are clearly discouraging new investment.

Regulatory burdens carry real costs that effect everyday Americans. As prices rise across energy categories that consumers rely on, I strongly urge the Committee to reconsider its current reliance on regulations, and instead pursue a viable and durable path forward on climate policy that protects the environment, consumers, the economy, and our national security.

Authority

Perhaps the most significant concern raised by the proposed rule is that the SEC is exceeding its statutory authority.

The SEC's rules, as clarified in its 2010 interpretative guidance, already require publicly traded companies to disclose a wide range of climate information to the extent that it is financially material.

These rules are principles-based and grounded in the materiality standard, which has long underpinned U.S. capital markets and ensured that federal securities regulation fulfills the Commission's tripartite mission. That standard, which is generally defined by Congress and the courts as requiring disclosure of information necessary to protect investors from inflated prices and fraud, has long instilled confidence, promoted market efficiency, and competition and is thus tied to advancing the goals of federal securities laws, as reflected in the SEC's mission.

Furthermore, much of the emissions data the Commission seeks is already publicly available under the Environmental Protection Agency's (EPA) Greenhouse Gas (GHG) Reporting Program, which captures roughly 90 percent of U.S. GHG emissions from the largest emitters.[1] Combined with the U.S. Inventory of GHG emissions, investors have more than enough data about a companies' emissions profile to make informed investment decisions.

Like other service companies, Canary adheres to the EPA's regulations on this topic and encourages regulation from just one agency to limit duplicative rules, or worse, inconsistencies that increase costs and the risk of unintended consequences.

Unfortunately, the SEC's proposal goes well beyond requiring information that provides an objective picture of a company's financial situation. Instead, it seeks to impose an unnecessarily burdensome and costly reporting structure that requires disclosure of a wide range of information, much of which is non-investor-oriented, and that is largely immaterial to a company's financial health.

Compelling public companies to report different kinds of costly environmental data, including Scope 1, 2, and 3 emissions data, climate scenario analyses, transition plans, climate-related financial impacts on corporate financial statements, and emissions reductions plans will have a practical effect on markets beyond just "disclosure."

If there is concern regarding companies' disclosures, they might be more readily, and cost effectively addressed through updated guidance regarding its materiality standards and by cross referencing EPA's GHG Reporting Program.

The Scope 3 reporting requirement proposed in the rule will place the responsibility and pressure to mitigate economy-wide emissions solely on the oil and gas industry.

For many companies, those costs are significant and could contribute to a decision to forego participating in public markets. On an annual basis, companies are projected to spend more than $10 billion cumulatively and burn more than 43 million workhours to meet the demands of this proposal. These direct compliance costs are likely underestimated, however, and say nothing of

[1] https://www.epa.gov/ghgreporting

the broader costs to the economy, due to the proposal's impact on capital allocation, markets, and energy prices.

Notwithstanding the SEC's stated goal of establishing a reporting framework that provides more "consistent, comparable, and reliable information," the Commission should not attempt to expand its authority simply because a subset of investors is interested in compelling corporate adherence to aspirational policy objectives, regardless of their merit. In fact, given the well documented political opposition the proposal has already garnered, it is likely that the rule will result in market instability and confusion, as the rules become a continued source of controversy and subject to repeal once a new Administration takes office or the complexion of the Commission itself changes.

Excessive Costs

Most important to companies like Canary is the impact this proposal will have on the bottom line. In this regard, the proposal fails to reasonably arrive at an accurate assessment of the cost for companies to comply. The SEC provides its first-year cost of compliance estimate at $640,000 for non-SEC registrants and $490,000 for SEC registrants. But on page 372, the SEC admits that these estimates may be "limited in scope and may not directly reflect registrants' compliance costs." From my vantage point as a CEO, I find this estimate suspect given the immense financial, account, and legal hours that the proposal will require. This compels me to question if the SEC has arrived at a reasonable estimate for companies to comply with the full scope of the rule. One economist from the University of Wisconsin, found that "by the late 2020s, the enduring economic impact will be approximately $25 billion in U.S. GDP foregone each year and 200,000 fewer jobs."[2]

Mandatory disclosure will drive the shift in investment flows by providing ESG funds regulatory cover to prioritize "environmental sustainability" over economic returns for investors when ranking funds.

The proposed rule will further cripple the oil and gas sector and our ability to meet the energy needs of consumers. The requirement that a company accounts for greenhouse gases emitted anywhere along its supply chain, called Scope 3 emissions, and the use of its products is a burdensome standard that will disproportionally affect domestic energy producers, including the financial institutions that underwrite the sector.

As CEO of a private company, this Scope 3 requirement amounts to one of my biggest concerns with the proposal. As an oilfield services company, Canary's Scope 1 emissions would be the Scope 3 emissions for a company who procures our services. This unprecedented mandate for Scope 3 has rightly concerned many private companies, as many lack the capability to collect this data. This is particularly the case for smaller companies, like Canary, who will be required to expend a disproportionate amount of resources to comply. While it may be true that certain large

[2] https://www.sec.gov/comments/s7-10-22/s71022-20132304-302836.pdf

incumbent firms might have sufficient resources to begin a Scope 3 data collection process – that will only involve those large firms asking smaller companies, like Canary, for their emissions estimates, which are much too costly for us to collect.

In addition, the industrial sector has expressed concern about increased liability for companies that must suddenly predict risks 10 to 20 years into the future as global temperatures rise. Chevron, ConocoPhillips and the American Petroleum Institute were among those asking the SEC to stipulate so-called “safe harbor” protections to shield them from legal or regulatory penalties related to the new climate-risk disclosures.

Conclusion

Throughout my testimony, I’ve described in detail the various reasons why companies like Canary are concerned about this proposal. If implemented as proposed, the rule will severely impact the ability of the oil and gas sector to meet present energy demand. The energy crisis facing the country today will be further exacerbated as costs pile onto energy producers and present difficulties to find labor, materials, and capital needed for exploration and production efforts.

A weakened U.S. oil and gas sector will not, however, stop forthcoming rising global energy demand, which the EIA projects will rise nearly 50 percent by 2050. Instead, current policy initiatives look more likely to bring about scenarios in which the U.S. settles into a role as a net importer of petroleum and natural gas products despite our abundant resources here at home.

Financial regulators’ shift toward prioritizing climate change over returns will end badly for the U.S. economy and consumers. It’s bound to restrict investment into finding and producing conventional energy supplies and usher in a more extreme version of the demand shock we’re experiencing today. Regulators make poor capital allocators. Free markets that can react to sudden supply and demand changes are much better at channeling investment.

The proposed rule’s prescriptive regime for emissions disclosures for public companies is unnecessary, will weaken our country’s energy security, and undermine our climate goals. As prices rise across energy categories that consumers rely on, the SEC, in its role as a financial regulator, cannot and should not move forward with a major environmental initiative without the direction of elected policymakers and agencies with environmental and energy expertise.

With two quarters of negative economic growth, and alarming inflationary trends in our future, I implore Congress to save American energy independence and oppose this rule.