Sustainable Investments Institute

# Climate Change

## Marathon Petroleum

**April 5, 2017**

| Ticker | Exchange | Meeting Date | Record Date | Annual Meeting Location |
|---|---|---|---|---|
| MPC | NYSE | 4-26-17 | 2-27-17 | Findlay, Ohio |

## Agenda

| Item | Proposal |
|---|---|
| 1 | MGT: Elect directors |
| 2 | MGT: Ratify selection of auditors |
| 3 | MGT: Advisory vote on executive compensation |
| 4 | MGT: Approve amended executive compensation plan |
| 5 | SH: Report on indigenous peoples' policy |
| **6** | **SH: Report on climate change strategy** |
| 7 | SH: Adopt simple majority vote |

**Si2 Briefing** Environment (Climate Change); Social (Human Rights)

**Report Authors** Sara E. Murphy and Heidi Welsh

**Links** 2017 Proxy Statement; 2016 Form 10-K

### Item 5: Report on indigenous peoples' policy

**Resolved Clause**

RESOLVED: Marathon prepare a report to shareholders, at reasonable cost and omitting proprietary information, that describes the due diligence process used to identify and address environmental and social risks, including Indigenous rights risk, in reviewing potential acquisitions. Such a report should consider:

- Which committees, departments and/or managers are responsible for review, oversight and verification;
- How social and environmental risks are identified and assessed;
- Which international standards are used to define the company's due diligence procedures;
- How this information informs and is weighted in acquisition decisions;
- If and how risks identified were disclosed to shareholders;
- Whether MPLX has an exit option in DAPL;
- Whether Marathon will adjust its policies and practices so as to not become entangled with such situations in the future.

**Lead Proponent** New York State Common Retirement Fund (NYSCRF)

**Vote History** None. The company unsuccessfully challenged the resolution at the SEC, which disagreed with the company's arguments that it could be excluded because it consti-

| | |
|---|---|
| | tuted multiple proposals, was false and misleading and was related to ordinary business. The company did succeed in knocking out one proponent on ownership grounds and NYSCRF modified the language slightly after negotiations. |
| **Summary** | The proponents believe that the controversies connected to the Dakota Access Pipeline, in which the company holds an indirect minority stake, illustrate that Marathon Petroleum needs a more in-depth policy to avoid pitfalls associated with projects that may violate the rights of indigenous peoples. From the company's perspective, it has in place appropriate policies that give due regard to human rights because it has expressed support for the UN Universal Declaration of Human Rights. Management believes the requested report would be too detailed and not provide a full picture of what it says is "a complex process" for project-specific decision-making. |

**Item 6: Climate Change Risk**

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| **Resolved Clause** | RESOLVED: Shareholders request that Marathon Petroleum issue a report by December 30, 2017 with board oversight, at reasonable cost and omitting proprietary information, on the Company's strategy for aligning its business plan with the well below 2-degree Celsius goal of the Paris Agreement, while continuing to provide safe, affordable and reliable energy. |
| **Lead Proponent** | Mercy Investment Services |
| **Vote History** | This is a new formulation from Mercy Investment Services at this company. In the three prior years, the proponent had filed a resolution requesting that Marathon Petroleum adopt greenhouse gas emissions reduction targets. That proposal garnered 35.8 percent support in 2014, 12.7 percent support in 2015 and 14.7 percent support in 2016. |
| **Summary** | Mercy Investments believes that although Marathon Petroleum does not disclose enough information for investors to evaluate investment decisions. The proposal calls for a study of the potential future impact of changes in the oil and gas industry arising from efforts to limit global warming to 2 degrees Celsius, as agreed in the Paris climate treaty in December 2015. Marathon Petroleum says it already reviews the impacts of regulatory changes and provides suitable disclosure. The company has decreased its greenhouse gas emissions in recent years, both absolute and relative. Peer companies have made specific efforts to set emission reduction targets in line with a 2-degree scenario. |

## I. Marathon Petroleum, Climate Change and Human Rights

| Financials | | | |
|---|---|---|---|
| *($ millions)* | **2016** | **2015** | **% Change** |
| **Total Revenue** | $63,339 | $72,051 | (12.1%) |
| **Net Income** | $1,174 | $2,852 | (58.8%) |

Marathon Petroleum refines, markets, retails and transports petroleum products primarily in the United States. It operates through three segments: Refining & Marketing, Speedway and Midstream. The company refines crude oil and other feed stocks at its seven refineries in the Gulf Coast and Midwest regions of the United States, and purchases ethanol and refined products for resale. Its refined products include gasoline, distillates, propane, feed stocks and petrochemicals, heavy fuel oil and asphalt. The company also sells transportation fuels and convenience products in the retail market through Speedway convenience stores; gathers, transports, fractionates, stores and markets natural gas liquids (NGLs); and transports and stores crude oil and refined products. Marathon Petroleum markets its refined products to resellers, consumers, independent retailers, wholesale customers, its Marathon brand jobbers and Speedway brand convenience stores, airlines, transportation companies and utilities. The company also exports its refined products. As of February 2, 2017, the company owned, leased and had ownership interests in approximately 8,400 miles of crude and light product pipelines, as well as 5,600 miles of gas gathering and NGL pipelines, and owned and operated approximately 5,500 independently owned retail outlets in 19 states, and 2,730 convenience stores in 21 states.

Marathon Petroleum's Midstream segment includes the operations of MPLX, its midstream master limited partnership (MLP). An MLP is a type of business organization that exists in the form of a publicly traded limited partnership. MLPs are most commonly present in the energy industry, providing and managing resources such as oil and gas pipelines. These types of business endeavors are conducive to producing regular income, thus enabling MLPs to offer attractive income yields, because they earn stable income that is often based on long-term service contracts. Essentially, MLPs are tax-exempt, publicly traded companies that own pipelines, storage tanks and other cash-generating energy infrastructure, and transfer the bulk of their income to shareholders in the form of distributions. However, some analysts see unique risk in this structure associated with declining income from pipeline assets.

Many of Marathon Petroleum's assets have long planned lifespans and represent major capital investments. For example, the company has spent $900 million on performance upgrades at its Galveston Bay and Garyville refineries since 2013. The company acquired the Galveston Bay refinery and related assets from **BP** in 2013 for $1.49 billion, and an additional $400 million in environmental upgrades to the facility in the coming years.

**Pipeline projects:** On February 15, 2017, MPLX closed on a previously announced transaction to acquire a partial, indirect equity interest in the controversial Dakota Access Pipeline and Energy Transfer Crude Oil Company Pipeline projects, collectively referred to as the Bakken Pipeline system, through a joint venture with Enbridge Energy Partners. MPLX contributed $500 million of the $2 billion purchase price to acquire a 36.75 percent indirect equity interest in the Bakken Pipeline system from Energy Transfer Partners and Sunoco Logistics Partners. MPLX holds, through a subsidiary, a 25 percent interest in the joint venture, which equates to an approximate 9.2 percent indirect equity interest in the Bakken Pipeline system. The Bakken Pipeline system is currently expected to deliver more than 470 million barrels per day (mbpd) of crude oil from the Bakken/Three Forks production area in North Dakota to the Midwest through Patoka, Illinois, and ultimately to the Gulf Coast. Marathon Petroleum expects to become a committed shipper on the Bakken Pipeline system.

In the proxy statement, the proponents note Marathon Petroleum's "agreement to acquire its ownership in DAPL was reached on August 2, 2016, five days after the project was approved by the US Army Corps of Engineers and eight days before the Standing Rock Sioux Tribe (SRST) began its blockade to stop construction." *(See box for more on the DAPL controversy.)*

The 10-K also notes that Marathon was involved in a different project with Enbridge Energy Partners, one of the Bakken pipeline system partners. That venture, the Sandpiper pipeline, was cancelled during 2016 and Marathon recognized a related $267 million charge in the third quarter of the year. But given its new investment in DAPL, Enbridge released Marathon from paying any termination fees in Sandpiper.

Otherwise, Marathon Petroleum mentions that it owns 35 percent of Enbridge's Southern Access Extension pipeline, between the towns of Flanagan and Patoka, Illinois—near St. Louis, Missouri. As McClatchy newspapers noted in December, pipelines from Patoka "radiate in every direction."

### *Climate Change Risk*

Marathon Petroleum says in its 2016 Form 10-K that it expects "the scientific and political attention to issues concerning the extent and causes of climate change" to continue. The company asserts that laws and regulations associated with limiting climate change can impose that, while significant, cannot be estimated. However, it also notes the regulatory uncertainty that accompanies the new Trump administration and its stated intent to roll back flagship environmental regulations. On that basis, the company asserts that the potential impact of regulation is "unknown at this time." Marathon Petroleum does acknowledge that states may become more active in regulating greenhouse gas emissions in the absence of federal regulation or legislation.

**Emissions performance and management:** The company's 2016 Citizenship Report outlines some of its environmental initiatives. The term "climate change" appears nowhere in the report, nor is there any discussion of the contribution of the oil and gas sector to a warming planet. The report emphasizes improvements in efficiencies, noting that production throughputs doubled between 2002 and 2015 while criteria pollutant emissions (a category that encompasses greenhouse gas emissions, among others) decreased by 43 percent over the same period. The company says this constitutes a 70 percent decrease in criteria pollutant emissions intensity, but does not provide explicit intensity figures over time. Marathon Petroleum says that it reduced refinery greenhouse gas emissions intensity from 2002 to 2015 by more than 15 percent at the six refineries it owned for the entire period. At its Galveston Bay refinery, the company reports an emissions intensity decline of 10 percent since it bought the refinery in 2013.

The report also highlights the company's role as an industry leader in energy efficiency, noting that it has earned 36 Energy Star designations for its refineries—75 percent of the total awarded—despite only owning and operating 10 percent of refining capacity in the country.

Marathon Petroleum cites figures from the 2015 U.S. Refining Survey, the Oil & Gas Journal and the U.S. Environmental Protection Agency's 2015 greenhouse gas emissions inventory to provide a comparison of its emissions to the industry average. It shows that while Marathon Petroleum represents 9.6 percent of U.S. refining capacity, the company emits 8.3 percent of the total direct greenhouse gas emissions for the refining industry, thus emitting less than the industry average.

In an apparent attempt to undermine the concept of the "Social Cost of Carbon"—a calculation of the economic cost of climate change impacts that underpinned a major Obama-era climate initiative—Marathon Petroleum in its 2015 Citizenship Report chose to introduce its concept of the "Social Benefits of Carbon," suggesting that each additional metric ton of carbon dioxide emissions was responsible for an increase in global gross domestic product of $4,400. The company made other completely unsupported claims, such as one that linked poverty reduction to emissions increases, suggesting causation. One can only surmise that this line of reasoning was received unfavorably, as the company dropped it from its 2016 Citizenship Report.

In one or both years' reports, Marathon Petroleum also highlighted its advocacy work in attempting to repeal legislation such as the Renewable Fuel Standard, methane reporting requirements, the Clean Power Plan Proposed Rule, the National Ambient Air Quality Standard and the crude oil export ban. In some cases, the company's arguments have merit, but it is notable that Marathon Petroleum reports only on environmental standards it opposes, and none that it favors.

**Physical impacts of climate change:** In its 2016 Form 10-K, Marathon Petroleum makes brief mention of the potential for severe weather events to adversely affect its operations. In doing so, the company appears to cast doubt on the established science of anthropogenic climate change:

> For a variety of reasons, natural and/or anthropogenic, some members of the scientific community believe that climate changes could occur that could have significant physical effects, such as increased frequency and severity of storms, droughts and floods and other climatic events; if any such effects were to occur, they could have an adverse effect on our assets and operations.

The Union of Concerned Scientists (UCS) published *Stormy Seas, Rising Risks: What Investors Should Know About Climate Change Impacts at Oil Refineries* in February 2015. In the report, UCS notes that Marathon Petroleum's Texas City refinery sits adjacent to its Galveston refinery to the west and **Valero's** Texas City refinery to the south. Modeling shows that with sea level rise to date, the Marathon Petroleum Texas City refinery and those around it could see storm surge impacts from a Category 3 storm or higher, with operations closest to the coast being inundated. In the future, sea level rise and changes in storm intensity could put the facility at greater risk for storm damages. UCS says that the close proximity of refineries in this area means that damage at one facility could also affect operations at others.

UCS and a group of investors sent a letter to Marathon Petroleum in February 2015, expressing the organization's concerns about the company's lack of disclosure of physical risks from climate change impacts. UCS expressed its view that Marathon Petroleum has a duty to shareholders and taxpayers to address this issue more comprehensively:

> As you are aware, Marathon Petroleum received a loan of one million barrels of crude oil from the federal government's emergency reserves to support its refining operations after Hurricane Isaac caused a reduction in operating capacity at the Garyville, Louisiana refinery. Risk of such events in the future is likely to grow. Diminished refining utilization rates, downtime or closure of facilities due to direct damage, danger to employees, releases of environmental contamination, disruption in supply chains and distribution centers, and/ or power supply due to storm surges or sea level rise could have a material impact on production and related cash flows.

**Renewables development:** Marathon Petroleum has made small recent investments in solar and wind power. Both the solar array and the wind turbine the company has installed are for the purposes of studying the technologies, and do not currently contribute to the company's operations. Indeed, the words "wind" and "solar" do not appear in the company's 2016 Form 10-K. The company does not offer metrics that would allow a calculation of renewables' significance in its overall portfolio.

Marathon Petroleum owns a biofuel production facility in Cincinnati, Ohio, that produces biodiesel, glycerin and other by-products. The capacity of the plant is approximately 60 million gallons per year. The company also holds interests in three ethanol production facilities. These plants have a combined ethanol production capacity of 275 million gallons per year and are managed by a co-owner. The company says the ethanol plants' annual capacity is equivalent to 18 mbpd, a minuscule quantity compared to the rest of its portfolio.

Twelve percent of Speedway's retail facilities sell biofuels, and three of its locations have begun to offer compressed natural gas. The company provides no revenue figures, but these would appear to compose a very small portion of its overall sales.

## *Industry and Investor Initiatives*

On December 14, 2016, a 20-nation task force released guidelines for voluntary climate risk disclosure by companies and investors in financial filings. The Task Force on Climate-Related Financial Disclosures (TCFD), set up by Bank of England Governor Mark Carney in his role as head of the G20's Financial Stability Board, recommends that all companies "describe the potential impact of different scenarios, including a 2°C scenario, on the organization's businesses, strategy, and financial planning," and provides more specific guidance for companies in the oil and gas, coal and electric utilities sectors due to the unique vulnerabilities of these industries. The TCFD offered 11 specific recommendations for all industries, divided into four topics: governance, strategy, risk management and metrics and targets. They include:

- All companies should benchmark strategic and financial planning using a 2-degrees Celsius economic scenario as their baseline for analyzing climate risks and opportunities. (As discussed in our briefing paper on climate change, scientists now say that even two degrees Celsius of average global temperature increase could be too much to prevent catastrophic impacts.)

- All companies should disclose information related to water, energy usage and efficiency, land use and revenues from products and services designed for a low carbon economy.

**BHP Billiton**, a global mining, metals and petroleum company, has adopted a planning process that "uses scenario analysis to encompass a wide spectrum of potential outcomes for key global uncertainties." In a 2015 report, BHP Billiton outlined four possible scenarios ranging from an orderly transition to a 2-degree world to a shock event that leads to a much more rapid transition to a 2-degree Celsius world by 2030.

Other oil and gas companies have begun using scenario analysis to assess the direction of their businesses and to assure investors that they are poised to take advantage of new opportunities. For example, **Total** issued a report in 2016 that discusses how a 2-degree scenario affects the company's decision-making process, discusses its targets for reducing the carbon intensity of its operations over time and includes the endorsement of its board of directors for this approach. Other companies beginning to use a 2-degree scenario analysis in their business planning include **ConocoPhillips**, **Statoil** and **Shell**.

### *Potential Disruptions to the Oil & Gas Industry*

According to the International Energy Agency (IEA), transportation accounts for more than one-fifth of global carbon dioxide emissions and that percentage is likely to rise, requiring rapid adoption of new technologies to keep temperatures within the 2-degree Celsius limit set by the Paris Agreement. The IEA and the International Council on Clean Transportation forecast that transport electrification will play a critical role in achieving required greenhouse gas reductions by 2050. Sales of electric vehicles (EV) are on the rise: in 2016, U.S. EV sales rose by 37 percent in the United States and 41 percent globally. **Statoil's** CEO recently predicted that oil demand would peak in 2020 with "a shrinking oil industry" as vehicles are electrified. A recent report from Carbon Tracker and the Grantham Institute calls "business as usual" predictions of slow growth in the market for EVs a "high risk strategy," and urges use of a range of scenarios to evaluate future demand.

An October 2016 Fitch Ratings report warned that oil companies faced a "resoundingly negative" threat from the recent and growing proliferation of electric cars. "Widespread adoption of battery-powered vehicles is a serious threat to the oil industry," says the report, which urges energy companies to plan for "radical change" spurred by new technologies that could arrive more quickly than expected. Ratings agency Moody's announced in June 2016 that it would begin analyzing carbon transition risk based on the 2-degree scenario. Moody's noted the particular risk exposure of the energy sector. In February 2017, Moody's published a subsequent report asserting that future shifts in U.S. climate policy—which are likely under the new Trump administration—would not stall global emissions reduction efforts.

Increased fuel efficiency for internal combustion engines could reduce demand for gasoline and diesel fuels. According to Obama-era regulations, efficiency requirements for light-duty vehicles are slated to increase to 54.5 miles per gallon by 2025, and agencies under the previous administration had been considering standards leading to significant reductions in fuel consumption for medium and heavy-duty trucks. President Trump has expressed his intention to roll back fuel efficiency standards. At the same time, California has the clout to enforce its own more stringent standards, and has stated its willingness to go up against the new administration. California's market share is so significant that vehicle manufacturers typically find it more efficient to conform their entire U.S. production to the state's requirements, rather than to produce separate vehicles for the rest of the country. It remains uncertain how this will play out.

### *Human Rights and Indigenous Peoples' Policies*

The company's 25-page Code of Business Conduct makes one mention of human rights. It says, "The Company respects the human, cultural and legal rights of individuals and communities and promotes, within its sphere of influence and legitimate business role, the goals and principles of the United Nations Universal Declaration of Human Rights." No policy about indigenous rights appears on the website or in the company's securities filings.

### *Dakota Access Pipe Line Controversy*

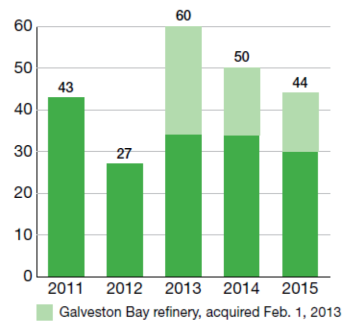
The Dakota Access Pipeline (DAPL) refers to the 1,172-mile underground 30" pipeline extending from the Bakken/Three Forks production area in North Dakota to Patoka, Illinois. Dakota Access is a subsidiary of Energy Transfer Partners (NYSE:ETP), a Texas-based natural gas company. The $3.78 billion project is expected to bring domestic crude oil from the Bakken fields to refineries in the Midwest and the Gulf Coast more safely than train or trucks; proponents of DAPL have also touted the number of jobs it would create and tax revenues to states. The project was announced to the public in June 2014 and, according to the company's website on the project, hundreds of public hearings were held between late 2014 and early 2015. The vast majority of the pipeline—99.98 percent—is on private property, however, and the companies negotiated directly with private landowners to obtain easements to begin building. The U.S. Army Corps of Engineers was charged with granting easement for the remaining federal lands, which are located north of the Standing Rock Sioux Tribe territory and the subject of this controversy; it subsequently determined that the project will not be "injurious to public interest" and a more extensive environmental review would be unnecessary.

**Controversy:** Opposition from Native Indian tribes—led by the Standing Rock Sioux Tribe—has been documented as early as 2014, almost from the beginning of the project. Grounds for their opposition are many. They say that the Army Corps of Engineers, which for its part maintains that it engaged the tribes sufficiently, failed to consult with the tribes before making its judgments. They also say that the Corps relied solely on information provided by the company and came to hasty conclusions; they want a full environmental assessment as required by law. Also at issue is the fact that the federal lands in question had been forcibly taken from the Sioux tribes by the U.S. government, a point that the U.S. Supreme Court acknowledged in its 1980 decision on *United States v. Sioux Nation of Indians*. Sacred burial grounds and other historical sites would be affected by the construction, the tribes have noted, and they are concerned about possible contamination of their drinking water in case of a pipeline rupture.

The Standing Rock Sioux first set up camp to oppose DAPL at the confluence of Missouri and Cannonball Rivers in North Dakota in April 2016. The camp grew as tribal and environmental activists from near and far came to protest what they saw as government and big oil infringing upon the rights of indigenous people. Throughout the legal and public relations back and forth the scene at the grounds turned violent, as demonstrators clashed with construction workers, security hired by the companies and, eventually, the police and National Guard. Uses of pepper spray, bean bag firing, tear gas, rubber bullets and hosing water in 20 degree weather have been reported against protesters; North Dakota is said to have run up more than $10 million in line of credit in law enforcement costs related to DAPL.

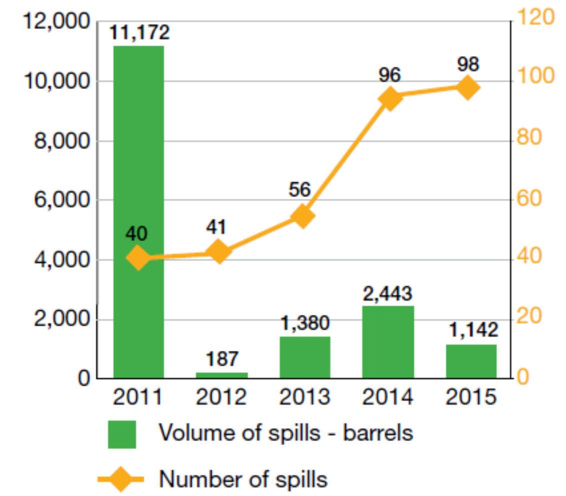
Temporary relief came when the departing Obama administration granted the protesters their full environmental assessment in December 2016, effectively pausing construction of the pipeline. But the incoming Trump administration quickly reversed course when it signed an executive order to let DAPL finish. A federal judge subsequently denied the protesters' legal challenge in March, finally allowing the companies to forge ahead.

TIER 3 AND TIER 4 DESIGNATED ENVIRONMENTAL INCIDENTS (DEIs)*




*DEIs include three categories of environmental incidents: releases to the environment (air, land or water), environmental permit exceedances and agency enforcement actions. These include both MPC and Speedway. Tier 3 and 4 DEIs are the most severe types of DEIs.*

OIL SPILLS




For the purposes of this metric, oil spills include crude oil and refined products on land or water, and we report spills here that are, in some cases, as small as a few drops.

**Community engagement:** The company posts its *Citizenship Report* (CR) on its website; the most recent version was released in 2016 with prior year data. It describes what Marathon calls its "deep involvement in the communities where we are privileged to do business." The report includes as an example discussion of its plan to cut sulfur dioxide at a plant near Detroit, to which it agreed after community engagement—which it says it should have initiated earlier in the permitting process.

**Safety:** The CR covers health and safety and says Marathon aims to have "no injuries, no incidents and no harm to the environment." Further, "For a manufacturing company that processes, transports and markets volatile substances, that means we never allow ourselves to be satisfied with how safe we are. We are constantly on the lookout for better ways to protect our employees, contractors and communities." It points out it is member of the Occupational Health and Safety Administration's Voluntary Protection Program, which requires lower than industry average injury and illness rates, and has received commendations in the program. The report includes annual data on its total recordable incident rates, which have increased each year since 2012.

**Environmental impacts:** The CR also provides information on oil spills and shows that the number has more than doubled since 2011. However, the company also reports that the number of serious "Designated Environmental Incidents" (DEIs) has dropped during this period. *(See charts, this page, from the CR.)*

## II. Proponent Positions

### *Item 5: Indigenous Peoples*

The New York State Common Retirement Fund and co-filers (the Unitarian Universalists, the Oneida Trust of the Oneida Tribe of Indians of Wisconsin, Trillium Asset Management and As You Sow) want more information about how the company is taking into account the rights of indigenous peoples who are affected by projects in which the company is involved. They were prompted to file the resolution because of the controversy over the Dakota Access Pipeline (DAPL) but have broader concerns about climate-related risks. In this proposal, they are focused on the construction and operation of energy infrastructure in North America.

The resolution argues that due diligence about environmental and human rights risks is "essential to assessing the full risk of an asset acquisition. Where such risks are not adequately considered, decisions can be made that lead to reputational, regulatory and financial loss."

It references The UN Declaration on the Rights of Indigenous Peoples and its standards for indigenous rights, including "free, prior, and informed consent for…any projects affecting their traditional territory," noting that the UN Guiding Principles on Business and Human Rights expectations are contained in that document's principles 17 through 21.

The proponents argue that the $500 million MPLX investment "pales…in the face of potential environmental liability and loss of reputation from a catastrophic pipeline failure." They point out, "The pipeline's operator, Energy Transfer Partners (ETP), has a poor environmental record, with pending water contamination lawsuits in New Jersey, Vermont, Pennsylvania, Louisiana, and Puerto Rico."

They also argue that before MPLX invested in the DAPL project, the Standing Rock Sioux Tribe and three federal agencies "raised concerns about the lack of tribal consultation and the inadequacy of the environmental impact review. At the time of this agreement, proponents believe that Marathon and its shareholders should have been aware of the risks posed by these concerns."

The resolution goes on to note the escalating controversy over the pipeline's construction, despite requests from the Obama administration to "voluntarily pause construction within 20 miles of Lake Oahe." It says, "The alleged use of force towards peaceful protesters is generating negative media coverage while further jeopardizing DAPL's social license to operate. ETP reports losses of $1.4 billion in a year if delays continue."

The resolution then asks for a report that would describe the company's "due diligence process used to identify and address environmental and social risks, including Indigenous rights risk, in reviewing potential acquisitions." It says the report should "should consider" the following:

- Which committees, departments and/or managers are responsible for review, oversight and verification;
- How social and environmental risks are identified and assessed;
- Which international standards are used to define the company's due diligence procedures;
- How this information informs and is weighted in acquisition decisions;
- If and how risks identified were disclosed to shareholders;
- Whether MPLX has an exit option in DAPL;
- Whether Marathon will adjust its policies and practices so as to not become entangled with such situations in the future.

**Exempt solicitation:** In a filing at the SEC on March 28, New York State Comptroller DiNapoli expanded on the resolution and provided updated information on the proponents' views. He noted NYSCRF owns shares worth about $79 million and said, "Given the nationwide protests and controversy that surrounded the Dakota Access Pipeline, we assume Marathon would have undertaken robust due diligence before getting involved with that project….Risks to the environment and to human rights create risks for our pension fund's investments and should be addressed as part of a sustainable business plan."

The resolution notes that risks associated with DAPL were apparent well before the deal closed on its subsidiary's investment this February. It points to the blockage begun on August 10 by the Standing Rock Sioux Tribe and its supporters, which aimed "to halt construction of the pipeline as a danger to the environment and to its culture for cutting through its ancestral lands." As the proponents observe, "Protests, and the use of force to deter them, escalated, resulting in negative media coverage for the companies involved in the project."

In addition to the blockade, landowners in Iowa sued to delay the use of eminent domain to acquire their lands for the pipeline project over their protests.

The exempt solicitation then reiterates the resolution's call for an explanation from Marathon Petroleum about how it assesses and "to explain how these and similar risks are assessed and weighed, who is responsible for such oversight in its review of potential acquisitions, if and how those risks were disclosed, and whether it will adjust its policies to avoid becoming entangled in such situations in the future."

### *Item 6: Climate Change*

Mercy Investment Services believes shareholders will benefit from increased disclosure by Marathon Petroleum and a more detailed analysis evaluating the impacts of achieving the 2-degree scenario put forth by the Paris agreement. Mercy believes that current disclosure is inadequate and that the requested analysis would help the company and its investors by contributing to improved financial risk assessment. The proponent notes that the Moody's credit rating agency now analyzes carbon transition risk, and highlights the high carbon risk exposure of the power sector, and highlights Fitch Ratings' warnings of the threat vehicle electrification poses to the oil and gas industry, as described earlier in this report.

Mercy points to the IEA's assertion that rapid new technology adoption is required to constrain global warming within safe limits. The proponent also notes the IEA's forecast that transport electrification will be critical to achieving emissions reductions, and thus could adversely affect oil demand, as described earlier, and highlights the fuel economy standards promulgated under the Obama administration. The proponent views the disruptive transportation angle as critical:

> Expansion of electric and hybrid vehicles, growth in autonomous vehicles and ride sharing, innovations in low carbon fuels, and increased fuel efficiency and battery range hold the potential to reduce demand for petroleum-based fuels and transform the marketing and retail business lines for refiners. According to the Sustainable Accounting Standards Board, market changes driven by climate change regulations can provide not only challenges for existing refining and retail business models but also opportunities for growth and brand enhancement. For example, many large corporations are actively seeking to reduce transportation emissions, with significant market opportunities for forward-thinking downstream companies.

Mercy emphasizes Marathon Petroleum's high capital expenditures, and the likelihood that these will continue to characterize its business model. The proponent acknowledges the company's "investments in renewable energy projects" and increased energy efficiency at its refineries, but expresses concern that Marathon Petroleum does not communicate:

> how the 2 degree challenge is being accounted for in its short and long term capital investment decisions, predictions of future demand, plans for growth, or strategies to manage risks from climate change regulations or related market changes. Such information would allow investors to better assess the risks that climate change regulations may pose to the company and shareholder value.

The proponent seeks a report from management on a 2-degree scenario risk analysis and business plan alignment, and suggests that Marathon Petroleum could include a discussion of its plans to integrate "technological, regulatory and business model innovations such as advanced biofuels, fuel cells, and electric vehicle charging infrastructure."

**Exempt Solicitation**: On March 27, 2017, the California Public Employees Retirement System (CalPERS) announced that it would vote in favor of the climate change proposal and encouraged other shareholders to follow suit. CalPERS is the largest state public pension fund in the United States with $311 billion in total assets under management, and owns approximately 2,012,000 shares in Marathon Petroleum. CalPERS explained its reasoning in an SEC filing:

> After completing a review of the CalPERS global equity portfolio, we identified 100 companies as significant carbon emitters responsible for over 50% of the portfolio's total carbon emissions. CalPERS defines these companies as systemically important carbon emitters (SICEs) – with Marathon Petroleum Corporation being one of them. Further, we believe proposal #6 is of particular significance in light of the global consensus regarding climate change and emission reduction targets reflected in the Paris Agreement. The importance of the proposal's request is also underscored by the efforts of Financial Stability Board (FSB), an international body mandated by G-20 leaders to develop efficient climate-related financial risk disclosures.
>
> Consistent with the CalPERS Investment Beliefs, we believe effective management of environmental factors, including those related to climate change risk increase the likelihood that companies will perform well over the long-term.

## III. Management Positions

### *Item 5: Indigenous Peoples*

Before going into its reason for opposing the shareholder resolution in the proxy statement, Marathon Petroleum underscores what it says is an "indirect ownership interest in the Bakken Pipeline Project…by MPLX, the midstream master limited partnership," in which it owns an approximate 28 percent interest. (This works out to an approximate 9 percent interest in the DAPL project.)

Marathon asserts that it "respects the human, cultural and legal rights of individuals and communities and promotes, within its sphere of influence and business role, the goals and principles of the United Nations Universal Declaration of Human Rights." It says its support for these principles lines up with its "dedication to enriching the workplace, preserving the environment, strengthening the communities where we operate and engaging with our stakeholders to pursue progress toward these goals."

However, management says the requested report would not serve shareholder interests because a due diligence analysis "is a complex process and one that is highly customized to the transaction involved." If the company were to provide the information requested, the resulting report would give "an incomplete and potentially misleading picture of prospective strategic transactions to its shareholders and to the public generally." Also, the "rigorous permitting processes" in its "highly regulated industry" provide for "stakeholder engagement through public comment and other means," obviating the need for a separate report.

The company reports that its board of directors "continually identifies, evaluates and monitors social, political and environmental trends, issues and concerns" relevant to its "business activities and performance." It asserts that this process has shown it has an ongoing "commitment to human dignity, human rights and fairness in our employment practices, non-discrimination policies, fair compensation policies and our policies on health, environment, safety and security," as set out in its Code of Business Conduct, described above in this report.

Management notes it recognizes its operations "affect many stakeholders" and says it affirms "our responsibility and commitment to promote social, environmental and economic benefits everywhere we operate." It asserts it will "remain accountable for our actions in the operation of our business with a spirit of respect, collaboration, stewardship and responsible investment" wherever it operates.

The company's membership in the American Chemistry Council includes a pledge to do business according to that organization's Guiding Principles of Responsible Care®, Marathon says—including that it operate ethically in a way that "benefits society, the economy and the environment." This means that a business plan "requires not only manufacturing great products and providing exemplary services, but also taking responsibility for the potential impacts of the business on local communities and the environment." Marathon argues it does this through its community engagement efforts and communications strategies for communities affected by its plants and transportation infrastructure.

The company, in closing, points to its sustainability reporting, which it says provide "an important tool for measuring the Company's progress and advancing our dialogue with stakeholders." It says its Citizenship Report and promotion of the Universal Declaration of Human Rights in its Code of Business Conduct and policies are "ample disclosures regarding environmental and human rights matters" about its business and urges a vote against the proposal.

**SEC challenge:** Marathon Petroleum unsuccessfully challenged the proposal at the SEC in a voluminous filing, arguing it could be excluded because constituted multiple proposals, was false and misleading and was related to ordinary business. The SEC rejected all the arguments, saying in part, "We are unable to conclude that you have demonstrated objectively that the proposal is materially false or misleading."

### *Item 6: Climate Change*

Management responds that the requested report is unnecessary, in that the company is already a leader in emissions reduction, and not in shareholders' best interests, as it would reveal its competitive strategy. The board says:

> Prevailing market conditions, forecasted demand for our products and the risks and opportunities associated with public policy are all factors we consider, and have long considered, in our planning, investment decisions and development of our corporate strategy, including as that strategy relates to our peer-leading performance in greenhouse gas (GHG) emission reductions and our investments in renewable energy sources and renewable fuels.

Notably, the above statement does not acknowledge climate change explicitly, nor does management do so at any point in its rebuttal, except to say that it reports on "risks associated with changing market conditions, including those that may be driven by GHG regulation or climate change mitigation commitments such as the Paris Agreement" in its SEC filings.

The board goes on to describe its various steps to diversify its business and enhance its competitive position, including its expansion of its midstream business and its presence in prolific shale plays, which management argues position the company to benefit from "rising commodity prices" and increased demand for natural gas and NGLs. The board believes "these strategic moves illustrate our commitment to adapting to a changing marketplace, supplying products and services demanded by our customers and remaining competitive for the benefit of our shareholders." Further, management believes it is already well positioned for possible future shifts:

> To the extent public policy results in regulations limiting GHG emissions in the jurisdictions where we operate, similarly situated industry participants will compete under common requirements, and MPC is well positioned as an established industry leader in energy efficiency to adapt to such requirements, just as we have adapted to other dynamic conditions.

The board goes on to detail its various energy efficiency and greenhouse gas emissions reduction initiatives, as well as its below-industry-average greenhouse gas emissions, and enumerates the various places where it discloses this information, as described earlier in this report. Management concludes by affirming the great benefit the petroleum business confers on society, and asserts that it does so in a safe and responsible manner. It further contends that it has already demonstrated its "ability to adapt to changing market and other conditions," and concludes that it views "the request for [Marathon Petroleum] to disclose elements of its competitive strategy and business plan as not in the best interests of our shareholders."

## IV. Analysis

### *Item 5: Human Rights and Indigenous Peoples – Key Points at Issue*

- What is Marathon Petroleum's current policy on human rights?
- Do investors have enough information to judge the company's commitment to the protection of indigenous peoples?
- Should the company provide more information to investors about how it weighs the potential costs and benefits of its projects' community impacts?

The proponents believe that the controversies connected to the Dakota Access Pipeline, in which the company holds an indirect minority stake, illustrate that Marathon Petroleum needs a more in-depth policy to avoid pitfalls associated with projects that may violate the rights of indigenous peoples. They also suggest the company has not provided investors with enough information about how it decided to purchase a stake in DAPL, and whether the company has sufficient safeguards in place to avoid environmental and social problems going forward. In particular, the proponents say the safety record of the DAPL project partner, Energy Transfer Partners, raises concerns given that firm's record.

As discussed above, the DAPL project engendered significant controversy given protests led by the Standing Rock Sioux Tribe and was put on hold by the Obama administration, then given a green light by the Trump administration. It is about to commence carrying oil from the Dakotas to a terminal near St. Louis, and thence to refining and export facilities.

From the company's perspective, it has in place appropriate policies that give due regard to human rights because it has expressed support for the UN Universal Declaration of Human Rights. Management believes the requested report would be too detailed and not provide a full picture of what it says is "a complex process" for project-specific decision-making. It also says that existing regulations and permitting provide a sufficient conduit for feedback from interested stakeholders.

**Current practice:** The company does not appear to have a human rights policy that specifically takes into account the rights of indigenous peoples. It also does not go into any detail about how it implements its current human rights policy, which is mentioned just once in the Code of Business Conduct and not referenced in the most recent iteration of the Citizenship Report. There is no mention of human rights in the company's Form 10-K discussion of risk factors, either, although it mentions environmental issues that are typical for the industry.

Marathon's stance contrasts to that of the banks that received a resolution with a similar focus, which took the view that they should carefully examine their conditions for financing projects that may affect indigenous peoples. **Goldman Sachs** and **Morgan Stanley** settled with the proponents and beefed up their policies, and agreed to continue discussions about the issue; Marathon did not. The other energy company to receive this same proposal, with its focus on regard for indigenous peoples' rights in project acquisitions, was **Phillips 66;** it also reached an accord with the proponents, who included the Presbyterian Church (USA), and according to the church agreed to "work towards disclosing and strengthening the company's human rights and Indigenous rights policies" and to participate in further dialogue this year.

**Cost/benefit:** The direct costs of implementing this policy would be minimal, for a company with annual revenue of over $63 billion, involving staff time and making the result formal and public—particularly since the company says it already undertook a complex evaluation process for its acquisition of the DAPL stake. Indirect costs might be more significant, if the policy prompted Marathon to consider selling its stake in the project, although at this point such a move seems very unlikely.

The potential benefits of implementing the resolution could help ease criticism of the company and flesh out its assertion that it has appropriate regard for the human rights concerns raised by the proponents. Existing reporting by Marathon on this subject is quite thin and has provided little detail to investors on any of the issues raised in the resolution. There are a number of multi-stakeholder initiatives that set out model policies and procedures, and related disclosures, that address human rights generally and indigenous rights more particularly. These include the International Finance Corporation (IFC) Performance Standard 7 on Indigenous Peoples, which defines the circumstances requiring Free, Prior and Informed Consent. Marathon at present is silent on this standard.

A more detailed examination of the fraught issues surrounding pipeline siting could help the company to identify previously unseen human rights-related risks, including policy and/or implementation gaps. Such a review might also help the company evolve and improve its current policies, and might help it avoid being ensnarled in similar controversies in the future.

For some investors, these issues may be of less concern given the trajectory of the company's recent financial results. Marathon Petroleum's fortunes have been hit, like other energy companies, by the current low world oil price, and its revenues have dropped from a recent high of about $100 billion in 2013 to just $63.4 billion in 2016—with a revenue drop of 12 percent in the last year alone. Net income is at a five-year low, just $1.2 billion, down from $3.4 billion in 2012 despite an increase last year. Diluted net earnings per share this year were $2.21, down from nearly $5 five years ago. The company clearly is betting that its pipeline project will help it unlock a new revenue stream and boost the bottom line. For those less interested in social policy and human rights and more concerned about financial results, and for those who believe substantial push-back on projects such as the Dakota Access Pipeline are unlikely for the immediate future given the current orientation of the federal government, the resolution may not be a major concern.

**Environmental record:** Some investors may want to consider the company's current environmental record when they decide how to vote on the issue. According to its most recent sustainability report, the number of oil spills has more than doubled in the last five years, although the *volume* of spills is lower. For some, this may be mitigated by a reduction in serious environmental incidents.

**Voting Considerations**

**Voting in favor:** Investors who believe that Marathon Petroleum's current human rights policy and lack of a statement on indigenous peoples leave much room for improvement are likely to support the proposal. They are likely to be especially interested in receiving more information given that the company has offered little to flesh out how it implements current commitments. Investors who believe that Marathon Petroleum will benefit in the long-run from investing more in the human rights impacts of its projects also will want to vote for the resolution. Investors who believe that the rights of Native Indian tribes are being violated by DAPL and want Marathon Petroleum to explain more about how it addresses this concern also will support the resolution.

**Voting against:** Investors who believe that the company's current statement about human rights sufficiently addresses the intent of the resolution will want to vote against the resolution. Investors who believe that implementing the resolution will impose overly burdensome costs on the company also will vote against. They may be joined by those concerned about the company's recent poor financial results; these investors may believe the risk of any immediate government curbs on pipeline projects is low because of the orientation of the Trump administration and its plan to boost domestic energy production and loosen regulatory burdens on industry.

### *Item 6: Climate Change - Key Points at Issue*

- Is Marathon Petroleum reporting sufficiently on how it is positioning the company in response to climate-related risks?

*Si2's 2017 Briefing Paper on Climate Change contains a general analysis of issues investors may want to consider. The following information is specific to Marathon Petroleum.*

Marathon Petroleum is a major crude oil refiner in the United States, and one of the biggest petroleum pipeline companies in the country. Many of the company's assets have long planned lifespans and represent major capital investments, which may not pay off if demand for its products were to drop significantly.

The proposal is based on concerns about growing evidence that anthropogenic climate change is already having serious impacts on the environment and society, that these impacts are highly likely to increase in severity and that global regulatory bodies will take increasingly stringent steps to constrain the greenhouse gas emissions that are responsible for the majority of atmospheric warming. The proponent specifically raises the 2-degree scenario, which reflects what had been a general scientific consensus that average global temperatures must not increase more than 2 degrees Celsius in order for catastrophic impacts to be averted. Recent research, however, strongly suggests that even 2 degrees of warming would be devastating, and the most recent discourse is turning toward a 1.5-degree scenario. Within this context, the proponent wants to know more about how Marathon Petroleum is planning for a transition to this new, low-carbon future.

The company cursorily acknowledges that climate change could pose a risk to its operations, chiefly through regulatory initiatives that management now sees as more remote in the face of shifting U.S. policy. The board briefly acknowledges the possibility of an increase in extreme weather events and the threat that these would pose, but makes no further consideration of the physical risks of climate change. The proponent perceives recent developments, chiefly the proliferation of electric and hybrid vehicles and projections that they, innovation in low-carbon fuels and increased fuel efficiency will markedly disrupt the oil and gas industry, as an existential threat that management should address with scenario analysis. Management sees no such threat, and believes it has already positioned itself well for future growth. The board also says that any regulatory threats would affect its industry uniformly, and that it is well positioned to absorb tightened legislation owing to its efficiency and emissions reduction programs. Shareholders will have to evaluate potential risks to the fossil fuel industry as a whole, and whether management's apparent argument that a falling tide drops all boats feels reassuring. Marathon has seen falling revenues for that past three years, and declining net income for the last two. It is not alone in its industry in this regard. It does, however, go against the prevailing view that the current low oil price environment will likely persist for some time.

The Paris climate treaty reached in December 2015 initially prompted optimism from many about new prospects for a real shift in global government action to address climate change. The outcome of the 2016 presidential election and the new Trump administration's stated intention to abandon many of the U.S. existing climate initiatives may delay some movement at the federal level. Nonetheless, many large institutional investors are convinced that companies and governments must take urgent action to address climate risks; they are paying ever closer attention to how their portfolio companies are strategically situated to handle climate-related risks and opportunities, despite the continuing U.S. political dysfunction that puts meaningful national energy legislation out of reach in the short term.

Many analysts believe that regulation is inevitable, given the scope and impact of the problem, and that if such regulation is delayed, it will constitute a greater shock when it is ultimately passed. They argue that companies would create a strategic advantage by adjusting their business models now. Indeed, many leading global asset managers are now advocating for greater climate change risk management and disclosure, and do not believe that a temporary shift in U.S. policy will derail decarbonization efforts. Marathon Petroleum acknowledges that states may step up climate change mitigation efforts in the face of federal inaction, and California may undermine the Trump administration's efforts to roll back fuel economy standards, as noted earlier.

That Marathon Petroleum is successfully taking steps to reduce its absolute and relative greenhouse gas emissions is not in question. The company has demonstrated declines in both absolute and relative greenhouse gas emissions—possibly because of the proponent's three-year campaign—and has stepped up its reporting on these subjects. But Marathon Petroleum has provided limited information on the issues the proponent specifically raises. Mercy is not looking for information on actions the company has already taken; it wants to understand how Marathon Petroleum is incorporating different climate change scenarios into its business plan. However, Marathon Petroleum appears not even to acknowledge the established science of anthropogenic climate change.

In comparison, a number of energy companies including **Shell, BP, Statoil, BHP Billiton** and **Total**, have endorsed requests for stress-testing portfolios for resilience to a 2-degree scenario. In addition, ten oil and gas companies support achieving the 2-degree target as part of the Oil and Gas Climate Initiative. **ConocoPhillips**, Statoil, Total, Shell and BHP Billiton have conducted 2-degree scenario analysis, with Conoco's action prompting the withdrawal of a shareholder resolution on the subject last year. Marathon Petroleum has not joined in these efforts.

While the requested report would incur costs for Marathon, it is unlikely that it would be materially significant to a company of this size. Given that the company has already acknowledged impacts from greenhouse gas emissions and climate change regulation, this report could help it prepare for future impacts globally.

**Voting Considerations**

**Votes in favor:** Investors who share the proponent's view that the company should provide further analysis of potential scenarios that could both limit demand for its fossil fuel products and increase their costs of production will vote in favor of the resolution. They are likely to agree that future restrictions are probably, irrespective of near-term policy shifts, and could have a material effect on the company. They also may believe the company's oil and gas reserves could see a significant drop in value under certain low-carbon scenarios and that management's related analyses and action plans are key to assessing their investment in the company and could help the company to plan for a more profitable future.

**Votes against:** Investors who are satisfied with the company's existing reporting on climate change and related risks will vote against the resolution. They are likely to find sufficient disclosure in the company's securities filings and citizenship reports. These investors also are likely to be satisfied with the company's assurances that it is positioning itself well for a dynamic future. Investors who agree that Marathon Petroleum would expose competitively sensitive information by publishing a 2-degree scenario report will also reject this resolution. Finally, investors who believe the recent U.S. policy shift defangs the projected risks to Marathon Petroleum's operations are also likely to reject this resolution.

## Resources

- Marathon Petroleum's 2017 Proxy Statement
  https://www.sec.gov/Archives/ed-gar/data/1510295/000119312517083730/d275049ddef14a.htm#toc275049_15
- Marathon Petroleum's 2016 Company 10-K
  https://www.sec.gov/Archives/edgar/data/1510295/000151029517000017/mpc-20161231x10k.htm
- Marathon Petroleum's *2016 Corporate Citizenship Report*
  http://www.marathonpetroleum.com/Corporate_Citizenship/Citizenship_Report/
- Exempt Solicitations
  - New York State Common Retirement System, regarding indigenous peoples
    https://www.sec.gov/Archives/edgar/data/810265/000081026517000005/MarathonPR-FI-NAL-03.27.2017.htm
  - California Public Employees' Retirement System, regarding climate risk report
    https://www.sec.gov/Archives/edgar/data/919079/000114036117013416/formpx14a6g.htm
- Marathon Petroleum Code of Business Conduct
  http://www.marathonpetroleum.com/content/documents/investor_center/corporate_govern-ance/MPC_Code_of_Business_Conduct_2017.pdf
- International Finance Corporation (IFC) Performance Standard 7 on Indigenous Peoples
  https://www.ifc.org/wps/wcm/connect/1ee7038049a79139b845faa8c6a8312a/PS7_Eng-lish_2012.pdf?MOD=AJPERES
- Union of Concerned Scientists: Stormy Seas, Rising Risks: What Investors Should Know About Climate Change Impacts at Oil Refineries
  http://www.ucsusa.org/sites/default/files/attach/2015/02/stormy-seas-rising-risks-ucs-2015.pdf