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Houston trend talks

ESG and energy transition

In this episode of KPMG Houston Trend Talks, Joshua Galvan, Advisory Principal in Technology Risk Management, Brian O'Neal, Advisory Principal and Keith Jordan, Tax Partner share perspectives on energy transition and the effort it takes to make it a practical reality.

Josh (00:00):

Greetings everyone. We hope this podcast finds you well, we're coming to you from a Microsoft team's enabled studio again. Glad to be hosting some KPMG colleagues to share perspective about trending topics. And today we get to talk about the energy transition. I'm Josh Galvan, and I'm a partner in KPMG's Houston office. And again, glad to have you with us. Today in environmental, social and governance are areas of discussion for anyone it's faster passing any area of interest or hobby. And instead is a table stakes requirement for many, if not every company. It's expected by investors and regulations are popping up all over the place, including the U.S., in the not too distant future. The demands placed on companies are significant and will be an important step. I believe toward a better future. As we do more to compliment the 150 years of hydrocarbons, we've all experienced and enjoyed.

Josh (00:58):

We get to move into a brighter future and a more diverse future, perhaps for energy. KPMG works with companies across the energy value chain. We work with suppliers, producers, servicers`, and customers across all the segments. Collaborating also with leading thinkers and industry and institutions and the insights shared today, we hope will be a balanced perspective on the energy transition and the challenge ahead. We're fortunate to have two KPMG partners with me to talk things through, Brian O'Neil and Keith Jordan represent our advisory and tax practices. They're also based in Houston with me, and I'm so glad to call them colleagues. Brian, you and I have talked about how the industry itself will take us through the energy transition. With the sustained public demand capital markets, and of course, government, what are some of the things we can expect companies to do in the energy transition? What can we expect in the coming few years to a decade in their role?

Brian (01:55):

Thanks Josh. It's an interesting question. If we leave aside the issue of ESGs origins and goals, we can focus for a minute on what I think is one of the most critical components in converting those ambitions into practical reality. And that would be energy transition given that something on the order of 65% of global GHG emissions come from energy use and extraction, transitioning energy away from hydrocarbons is one of the biggest levers we have. As you mentioned earlier, the transition itself is practically here, not much to argue about on that fund I think. That's targeted by [inaudible 00:02:33] corporates, supported by broad public consensus. It's enforced at the lending level by the capital markets. And I think the global ambition for the transitions apparent. And that doesn't really matter if you look at the supplier, the demand saw either not only are the major end users clamoring for solutions, but major producing entities are sticking their futures on their ability to manage the transition.

Brian (02:57):

So what you asked was what can we expect? And I think the simple answer is that we can expect major energy companies to embrace the idea of energy transition in one form or another, that they will make major investments in strategic decisions to make it happen. I view this as a good thing. One of the most interesting challenges in emissions reduction is putting the bill. Tens of trillions of investment dollars are estimated to be needed, to reduce global warming to acceptable levels. And that's a staggering amount of money. It's hard to see how global taxpayers are going to be able to put that bill without this significant impact to their economic viability. So for me, it's especially refreshing to see major companies stepping into the gap and if companies and capital market participants are willing to invest in a better future, that makes a much, much better outcome for you.

Brian (03:48):

For me, for our listeners, would otherwise have to pay for it without the rigor that you expect from a major capital project. This is something that tends to get lost in the conversation. If major energy companies are effectively financing the transition with their operations means tax payers aren't compelled to do so. And more to the point, consumers effectively choose to pay for it via their participation in fuel and plastics and utility markets. Plus you can pull demand out of the market without forcing people to pay for others people's behaviors. So this is what I see the world doing for the next decade or so. I see investors voting with their dollars. I see companies acting with their engineering, strategic capabilities and working together as a whole to make energy transition a viable component of the overall DSG solution.

Josh (04:38):

Love it, Brian, thank you for, for sharing that and I definitely appreciate your perspective. You and I have worked together for a long time, and of course I've said for a long time as well, perhaps echoing your sentiments, but different words that this industry's solved some of the biggest life and mobility challenges we've faced for a century and a half. And I hope, and I do believe that this industry has the science, the technology, the engineering, the computational capability to create a transition for us that makes sense both from a solution perspective and a economics perspective. So real excited about that journey and like you reinforced confidence around what the energy industry can do in the transition. So Keith coming to you for a second, I made reference earlier to a topic you know a lot about, and that's kind of the business of running an energy company, the corporate functions, and in particular tax and how they play a key role in the energy transition at companies. Could you elaborate a bit on how tax functions are playing a key role?

Keith (05:47):

Yeah, happy to Josh. And I think Brian alluded to it a bit here is the role I think tax is going to play is they are going to help fund and help pay for these energy transition solutions. So what I mean by that is organizations all across the U.S., across the globe have issued their 2030 goals, their 2050 goals, as far as emissions reductions, decarbonisation efforts, net zero, et cetera. And now they're moving into what is their plan to accomplish this. And if you look at, from a government perspective across the globe, there's a bit of the stick mentality. So you've got regulations, you've got penalties, you've got fines, things of that nature to move companies in the right direction. But then you've got a lot of the carrot mentality as well. And oftentimes those carrots come in the shape and size of tax credits and incentives.

Keith (06:46):

So if you invest in this type of property, or if you do this type of activity, you can get X tax credit that you can take to reduce your corporate tax liabilities. And what we're finding is those incentives are really serving as a catalyst to help move these projects along and oftentimes get some projects that we think, Hey, we can't accomplish this for 10 years. Well, now that we layer into the cost model, the tax credit associated with that project, well, we can get started on that tomorrow. So I think taxes plays a critical role in the process and their ability to help fund and really kind of jumpstart the energy transition process.

Josh (07:32):

It's definitely clear that all parts of the enterprise need to be firing on a common mission. A common goal and tax of course, is no different and appreciate your perspective there. If there are any doubt before it's clear, the energy transition will call on companies to truly evolve. As Keith just mentioned, that includes tax. And what you've both shared, there are key threads around people and knowledge, skills, technology, and data partnerships, cutting across the value chain, your suppliers, your customers, working with governments and local communities. All the things that if I'm honest, I think energy companies already do and oil companies in particular do quite well on a global scale. And while that's true and energy companies have a legacy of doing this well, I think the energy transition will introduce new challenges. Indeed, it will be a multi-year, multi decade change journey for the company and its customers. What would you guys say will be the most critical element in that change journey? Keith, if you don't mind taking that one first.

Keith (08:42):

Happy to answer that one, Josh, I think the biggest area is going to be communication across the organization. And so let me take my tax example, those tax credits that are available if the tax department and a company knows about them, but isn't aware of the project that's happening, that they're applicable to those credits really aren't very beneficial. So you've got a tax department that needs to interact with finance, that needs to interact with operations, that needs to interact with the chief sustainability office. All of those key stakeholders together need to be communicating on what is our plan so an organization can effectively move down the road and achieve the goals they're trying to achieve. At the same time they all need to be working together and be nimble on how they react to the constantly changing environment, the constantly changing regulations and the constantly changing laws, both here in the U.S as well as international. So, they have a strategy that's nimble and flexible to continue to achieve their goals and navigate what's going on in the outside areas.

Josh (09:49):

Brian, anything you'd add to that?

Brian (09:51):

Well, for me, the biggest issue is obviously planning and operationalizing energy transition, but a close second in my mind is the reporting that goes with it. So after all it's going to be hard to point out gains if we don't have the data and the reporting rigor to support it. The idea of reporting to a broad base of stakeholders, certainly isn't new, but the platform and standards for reporting HD progress certainly is I think this is creating a bit of a challenge for the change journey that you mentioned a little bit earlier. Just to give a few examples, voluntary standards have been around for a while, but as of this recording, we're still awaiting on the finalization of the SEC's reporting rules. That's going to take some time to digest, to understand and to build appropriate action plans. And even if we had a hundred percent certainly on the new reporting standards today, there's still some serious gaps in the data space.

Brian (10:51):

Do we have access to all the data that we need? Is it verifiable? Is it in a uniform data standard location? And probably most importantly, do we have SOX's quality controls to provide the level of assurance that we've come to expect out of regulatory and capital markets reporting? These are questions that companies are dealing with right now, and it's not just a data problem. It's a behavioral challenge as well. And there are a number of vendors that are making great strides with field services software and in other solutions that are designed to generate a consistent data set a number of non-financial areas. But the fact is that there are new needs to gather timely data. And that means that we need to get operators and other field level personnel on board since they're the starting point for data acquisition. The companies need to think through the best ways to train and incentivize their workforce to drive the high quality and repeatable data sets they're going to need to report and to improve their operations. And that's, that's not a simple task.

Brian (11:56):

And finally, in my mind, there's the matter of available tools and systems to aggregate the data, embed the proper controls, facilitate reporting, and integrate all of it into existing enterprise data platforms. To developing feel, there's a lot of promise, but I think we're far from finished. I do have every confidence the companies will crack them up. I think they certainly have the incentive to do so. However, right now it's kind of sitting there waiting to be cracked. I think it's going to be a fun couple of years helping our clients get past that and get to a point of comfort. And I'm frankly looking forward to it.

Josh (12:33):

Thanks Brian and Keith both. Brian, your last few comments there certainly resonate for me, being a technology, a data, a controls and governance person. Certainly believe that's a key element to success, effectiveness in running company, energy transition activities, of course, but most importantly, around the measurement and assurance activities, that will be inevitable. Thank you so much for coming out today and sharing your important perspective. Thanks to everybody for listening in as well. You can find various thought leadership on kpmg.com about these topics. You can also connect with us personally on LinkedIn, if you'd like, or you can subscribe to KPMG podcast from the page where you found us today. Thanks again for tuning in, have a great rest of your day. Take care.

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