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Financial Reporting Update

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Key Recent Developments

- Cybersecurity risk disclosure
- Climate change impact
- Continued SEC challenge of reserves progression

Cybersecurity Risk

- On February 20, 2018, the SEC approved new interpretative guidance that reinforces and expands its previous guidance in three key areas:
 - **Disclosure:** the 2018 Guidance highlights specific disclosure requirements that public companies must consider when evaluating cybersecurity risks and incidents;
 - **Controls & Procedures:** the 2018 Guidance emphasizes the need for disclosure controls and procedures to ensure internal reporting proper public disclosure of cybersecurity issues; and
 - **Insider Trading and Selective Disclosure:** the 2018 Guidance also focuses on public companies' responsibilities in implementing policies and procedures that prevent insider trading on, and selective disclosure of, information related to cybersecurity risks and incidents.

Cybersecurity Risk

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- Cybersecurity incidents can seriously impact
 - operating systems and infrastructure
 - process controls and safety systems
 - critical data and proprietary information

- Cybersecurity incidents entail a number of potential costs that may impact a company's financial statements, e.g.,
 - the costs of investigation, breach notification and remediation;
 - litigation related expenses;
 - loss of current revenue or diminished future cash flows;
 - warranty product liability or breach of contract claims;
 - insurance premium increases and increased financing costs;
 - recognition of losses and impairment of assets.

Cybersecurity Risk

(Continued)

- Timing and Propriety of Disclosures
 - When a company learns of a *material* cybersecurity incident or risk, it is expected to make appropriate disclosures.
 - The SEC recognizes that the disclosures may be required before an investigation has been completed and that cooperation with law enforcement may limit the disclosure that can be made in a cyber incident. However, an investigation, whether internal or external, does not alone justify withholding disclosure.
 - Companies should evaluate the processes in place for reporting cybersecurity incidents up the chain to those responsible for public disclosure decisions.
 - Companies should evaluate the cybersecurity of financial reporting systems to ensure that the systems are not themselves compromised.

Cybersecurity Risk

(Continued)

■ Board Oversight

- The 2018 Guidance emphasizes the Board's role in overseeing the management of cybersecurity risks and incidents.
- Disclosures concerning a company's cybersecurity risk management program, and how the board of directors engages with management on cybersecurity matters, are important in enabling investors to assess how effectively a board is discharging its oversight responsibilities.

■ SEC Cyber Unit

- Set up to investigate and bring enforcement actions against:
 - hackers for trading misconduct and account intrusions
 - failures to safeguard information or ensure system integrity
 - cyber-related disclosure failures by public companies

Climate Change

- Not just a regulatory issue but increasingly an investor priority
- SEC issued disclosure guidance in 2010. It encouraged companies to disclose the effect of Climate Change risk on the company's operating and financial decisions and on its financial statements.
- Various State Attorney Generals and cities such as Oakland, San Francisco and New York have instituted litigation against international oil companies alleging injury due to global warming and failure to warn of the impacts
- Companies are providing more disclosure of what they are doing to reduce their impact on climate change – taking a more proactive approach
 - Reducing emissions in operations – e.g. reduced flaring and methane emissions
 - Designing carbon capture projects
 - Producing cleaner fuels and products
 - Putting greater emphasis on renewables
 - Using carbon offsets

SEC Comment Letter issues

- PUD Reserves Progression
- Disclosures of significant changes in reserves and reasons for them
- Impairments
 - assumptions and estimates used and levels of subjectivity and uncertainty
- Independent reserves audit reports
 - disclosure of assumptions, data, methods and procedures used

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