

SUMMARY

As long-term investors in Valero Energy (“Valero” or “the Company”), we are concerned that the Company is not adequately managing the risks that climate change and the energy transition pose to its core business of refining and selling fossil fuels. Without ambitious and clearly defined targets and stated plans to ensure that the Company is reducing the greenhouse gas (GHG) emissions of both operations and products, investors are unable to evaluate whether Valero is adequately taking advantage of opportunities to expand investments in innovative, lower-emissions alternatives and managing its long-term climate risks. Accordingly, investors are encouraged to vote “FOR” this proposal.

RESOLVED CLAUSE

RESOLVED, shareholders request Valero issue a report, at reasonable expense and excluding confidential information, within a year and updated annually thereafter, on its climate transition plan to align operations and value chain emissions with a well-below 2 degrees Celsius scenario, including short-, medium- and long-term reduction targets for Valero’s full GHG emissions (scopes 1, 2, and 3).

RATIONALE FOR A YES VOTE

- 1) Valero’s existing GHG emissions reduction targets and lack of climate transition plan provide insufficient details for shareholders to properly assess whether the Company’s short-, medium- and long-term strategy is consistently aligned with a well-below 2°C scenario.
- 2) In contrast, Valero’s peers have taken more ambitious steps to address the risks and to embrace the opportunities that climate change presents, making Valero a laggard in both an absolute and relative sense.

DISCUSSION

Introduction

In its Statement of Opposition, Valero’s Board claims that our proposal seeks targets that “*can only come from refinery closures.*” This is inaccurate—we seek targets that reflect a consistently constructed trajectory to lower emissions, and a transition plan that demonstrates that Valero is positioning its assets to take full advantage of new opportunities that will arise in the energy transition.

Investors ranging from State Streetⁱ to Legal and Generalⁱⁱ to Avivaⁱⁱⁱ have underscored the critical role that climate transition plans play in helping companies manage the risks and opportunities of the energy transition. As CDP notes, a good transition plan should “*clearly [outline] how an organization will achieve its strategy to pivot its existing assets, operations and entire business model towards a trajectory that aligns with the latest and most ambitious climate science recommendations.*”^{iv} The Task Force on Climate-related Financial Disclosures (TCFD) has further recognized that an organization's transition plan and its adaptation plan are important components of a company's strategy to address its climate-related risks and opportunities.^v Simply put, a clear transition plan is a basic building block of any company's climate strategy.

The IEA has estimated that under a net zero scenario, global oil use will need to decline 75% by 2050 compared to 2020, with even larger declines in refined products like gasoline and diesel.^{vi} Major markets like the EU and California have begun to mandate the phase-out of internal combustion engines, and jurisdictions globally are putting a price on carbon emissions.^{vii} Wood Mackenzie found in its 2°C and 1.5°C ‘accelerated energy transition’ scenarios that refining faces continued rationalization as oil demand collapses, with gross refining margin indicators all negative by 2050.^{viii}

Valero’s existing GHG emissions reduction targets and lack of climate transition plan provide insufficient details for shareholders to properly assess whether the Company’s short-, medium- and long-term strategy is consistently aligned with a well-below 2°C scenario.

While Valero has adopted 2025 and 2035 GHG reduction targets, those targets lack ambition as well as the details that investors would need to evaluate their feasibility and impact. Specifically, the targets:

- Count scope 3 emissions reductions (e.g., from low-carbon products) against the company’s scope 1 and 2 targets. For a refiner, scope 3 emissions are largely a measure of a company’s exposure to climate transition risk, and are influenced by product slate, and diversification into lower-carbon fuels. Scope 1 emissions are largely a measure of refinery energy and process efficiency, and are linked to a company’s exposure to regulatory risk. While both are important, using one to offset the other is at best confusing and at worst misleading, and suggests that the company does not really understand the material financial impact of these metrics.
- Lack the details needed for investors to properly evaluate them. Specifically, the company doesn’t make clear (a) how 100% absolute scope 1 and 2 emissions reduction can be achieved in the medium and long term, (b) how it will reduce its scope 3 emissions, and (c) how the Company plans to achieve its publicly-stated targets and adequately manage the risks posed by the energy transition to its business, in the absence of a properly defined climate transition plan.

- a) **We are asking Valero to include credible scope 1 and 2 emissions reduction targets in its climate transition plan.** The 2035 GHG Emissions Target chart provided in the Board’s Statement of Opposition, as well as in the Company’s TCFD report^{ix}, provides insufficient details and citations to global frameworks to explain how Valero can reduce its absolute scope 1 and 2 emissions, to move beyond the 7.4% absolute emissions reduction, which the Company achieved in 2019 and surpassed in 2020 and 2021. The following categories are particularly problematic:
- i. *Emissions Displaced by Valero’s Ethanol and Renewable Diesel Production, and by Global Blending of and Credits from Low-carbon Fuels* – These three types of displacements are not absolute scope 1 and 2 emissions reductions. Rather, they reduce emissions *in the value chain* of the Company; hence, these displacements should normally be tracked as scope 3 (use of sold product) emissions reduction.^x Valero is also double counting these emissions reductions in its “net scope 3 intensity” calculation where reported GHG emissions are “*netted for avoided emissions and emissions reductions from low-carbon fuels displacement of petroleum-based fuels.*”^{xi} In an example of better disclosure, industry peer Neste reports displaced emissions from renewable diesel^{xii} in a way that complies with industry standards.^{xiii}

ii. *2035 GHG Emissions Reduced by CCS* – While we agree with the IPCC's and IEA's evaluations that net zero by 2050 ambitions will require a "rapid acceleration in the deployment of CCS", our concern with Valero's scope 1 and 2 emissions target and CCS transition planning is that the company does not disclose sufficient detail for shareholders to properly assess whether the associated emissions reductions should be accounted for as scope 1 or as scope 3 emissions reductions. CCS-related emissions reduction classification is indeed case-dependent.^{xiv} It appears that Valero is currently double counting these emissions reductions in its "net scope 3 intensity" calculation, where reported GHG emissions are "netted for avoided emissions and emissions reductions from (...) carbon capture."^{xv}

b) **We are asking Valero to include a credible scope 3 emissions target in its climate transition plan.** Scope 3 emissions represent the vast majority of any refiner's carbon footprint and, therefore, constitute most of its climate risk exposure. As noted below, for peers Marathon Petroleum and Phillips 66, scope 3 emissions represent at least 90% of total GHG emissions. Setting a scope 3 emissions reduction target, using existing guidance,^{xvi} would enable Valero's shareholders to assess how the company is managing its climate-related risks and opportunities.

In addition, Valero does not report its absolute scope 3 emissions, but instead last year began reporting "net scope 3 intensity" using a non-externally validated methodology and concluding that its net scope 3 intensity leads its peers.^{xvii} In its Statement of Opposition, Valero's Board mentions that the GHG Protocol contemplates scope 3 intensity disclosures. It is true that the GHG Protocol enables *optional* reporting of intensity metrics (e.g., average GHG intensity of sold products). However, it also *requires* the reporting, for each scope 3 category, of total GHG emissions in metric tons of CO₂ equivalent (i.e., absolute emissions reporting), which Valero does not provide.^{xviii} When it comes to netting off emissions, the GHG Protocol states "*companies should report internal emissions in separate accounts from offsets used to meet the target, rather than providing a net figure*"; contrary to this global guidance, Valero only discloses *net* scope 3 intensity.^{xix} Disclosure of absolute scope 3 emissions using existing recognized methodologies^{xx} would be more useful to Valero's shareholders and other stakeholders, allowing direct comparison of Valero's absolute scope 3 emissions with its peers. It is also a prerequisite for the company to set a credible scope 3 emissions reduction target.

c) **We are asking that Valero issue a climate transition plan to align operations and value chain emissions with a well-below 2°C scenario.** This plan should make clear how Valero plans to achieve its publicly stated targets, and adequately manage the risks posed by the energy transition to its business. It should include timing, specific activities that will be undertaken as well as their scope and expected impact, and capital expenditure plans to carry out these activities.^{xxi} In its opposition statement and in other reporting, Valero has provided some details of low-carbon projects it has undertaken,^{xxii} but these stories, without more, do not constitute a transition plan.

In contrast, Valero’s peers have taken more ambitious steps to address the risks and to embrace the opportunities that climate change presents, making Valero a laggard in both an absolute and relative sense.

We believe that the creation of long-term shareholder value will be enhanced if the Company follows its peers in taking a more transparent and ambitious approach to addressing climate risks and opportunities, by regularly updating its climate transition plan and including full GHG emissions reduction targets.

As set forth in the table below, Valero’s industry peers have more ambitious disclosures and emissions reduction targets, on shorter timelines.

Company	Scope 1&2 reduction targets (true emissions reductions)	Incorporates “displaced emissions” into scope 1&2 targets	Scope 3 reduction targets	Total absolute scope 3 emissions disclosure (estimated percentage of total GHG emissions)	Scope 3 emissions disclosure using standard, comparable methods
Valero	7.4% by 2035 (vs 2011, absolute) <i>Rest of target made up of displaced emissions and carbon capture and storage</i>	Yes	No	No	No
Phillips 66^{xxiii}	30% by 2030, 50% by 2050 (vs 2019, intensity)	No	15% by 2030 (vs 2019, intensity)	Yes (~91%)	Yes
Marathon Petroleum^{xxiv}	30% by 2030 (vs 2014, intensity)*	No	15% by 2030 (vs 2019, absolute)*	Yes (~90%)	Yes (provides emissions from refining throughput and production volume data)
ExxonMobil^{xxv} Ex	20% by 2030, net zero by 2050 (vs 2016 absolute)	No	No	Yes (~86%)	Yes (provides emissions from refining throughput and production volume data)
Chevron^{xxvi}	Net zero upstream by 2050	No - reports them separately as required by GHG Protocol	Yes	Yes (~87%)	Yes
Neste^{xxvii}	50% by 2030 (vs 2019, absolute), carbon neutral production by 2035	No - reports them separately as required by GHG Protocol	50% by 2040 (vs 2020, intensity)	Yes (~94%)	Yes

*It is worth noting that Marathon Petroleum developed its targets using guidance from the Science Based Targets Initiative (SBTi) and Ipeca.^{xxviii}

Valero maintains that it leads the industry in producing low-carbon renewable fuels.^{xxix} However, according to Carbon Tracker: “*without an extremely aggressive [low carbon fuels] ramp up, sufficient feedstocks and technological advancements, it’s hard to see how [low carbon fuels] will make a dent in the company’s wider (...) processing capacity*”.^{xxx} Ramping up the scale, pace and rigor of Valero’s climate-related initiatives could unlock further opportunities for growth in new renewable fuels, help strengthen financial resilience, and avoid investments in assets that will lose value as the global economy transitions away from fossil fuels.

Recent reports from peer companies Phillips 66 and Marathon Petroleum show investments in multiple low-carbon technologies and fuels and provide more detail than Valero of their plans to achieve more ambitious GHG reduction targets.^{xxxi}

Investors, including Mercy and our co-filers, increasingly expect companies to set targets and strategies to indicate that they are anticipating and managing the risks of climate change to their business and to help ensure the world is on track to meet the goals of the Paris Climate Agreement. The Climate Action 100+ initiative, including investors with more than \$68 trillion in assets under management, has established a Net-Zero Company Benchmark, evaluating whether companies report all emissions in their value chains (*i.e.*, including scope 3 emissions) and set short-, medium- and long-term targets aligned with the 1.5°C goal of the Paris Climate Agreement. Valero failed to meet any of the benchmark’s requirements for setting targets or for articulating a transition plan.^{xxxii} In addition, the largest investors in the global market are increasingly asking companies to report all value chain emissions and set targets to reduce them, including BlackRock, Vanguard and State Street Global Advisors.^{xxxiii}

Not only does Valero’s reporting of emissions fail to meet these investor expectations and lag its peers, but also the Company’s current, limited target does not align with the net zero goals being set by many of its investors and lenders. In addition, Valero does not articulate a clear climate transition plan. As a result, Valero risks losing market share and access to capital as more institutions commit to align their lending and investments to net zero goals.

CONCLUSION

Vote “YES” on this Shareholder Proposal

As long-term investors in Valero, we are concerned that the Company is not adequately managing the risks that climate change and the energy transition pose to its core business of refining and selling fossil fuels. Without ambitious and clearly defined targets and stated plans to ensure that the Company is reducing the GHG emissions of both operations and products, investors are unable to evaluate whether Valero is adequately taking advantage of opportunities to expand investments in innovative, lower-emissions alternatives and managing its long-term climate risks. **Accordingly, investors are encouraged to vote “FOR” this proposal.**

THE FOREGOING INFORMATION MAY BE DISSEMINATED TO SHAREHOLDERS VIA TELEPHONE, U.S. MAIL, E-MAIL, CERTAIN WEBSITES AND CERTAIN SOCIAL MEDIA VENUES, AND SHOULD NOT BE CONSTRUED AS INVESTMENT ADVICE OR AS A SOLICITATION OF AUTHORITY TO VOTE YOUR PROXY. THE COST OF DISSEMINATING THE FOREGOING INFORMATION TO SHAREHOLDERS IS BEING BORNE ENTIRELY BY ONE OR MORE OF THE CO-FILERS. PROXY CARDS WILL NOT BE ACCEPTED BY ANY CO-FILER. PLEASE DO NOT SEND YOUR PROXY TO ANY CO-FILER. TO VOTE YOUR PROXY, PLEASE FOLLOW THE INSTRUCTIONS ON YOUR PROXY CARD.

ⁱ See <https://www.ssga.com/library-content/pdfs/asset-stewardship/disclosure-expectations-for-effective-climate-transition-plans.pdf>.

ⁱⁱ See https://www.lgim.com/landg-assets/lgim/_document-library/capabilities/climate-governance-guide-tagged.pdf.

ⁱⁱⁱ See <https://www.avivainvestors.com/en-us/views/aiq-investment-thinking/2023/01/company-chairpersons/>.

^{iv} See <https://www.cdp.net/en/guidance/guidance-for-companies/climate-transition-plans>.

^v See https://assets.bbhub.io/company/sites/60/2021/07/2021-Metrics_Targets_Guidance-1.pdf, pgs. 39-41.

^{vi} See https://iea.blob.core.windows.net/assets/deebef5d-0c34-4539-9d0c-10b13d840027/NetZeroBy2050-ARoadmapfortheGlobalEnergySector_CORR.pdf, pgs. 21 and 102.

^{vii} See for example <https://www.europarl.europa.eu/news/en/headlines/economy/20221019STO44572/eu-ban-on-sale-of-new-petrol-and-diesel-cars-from-2035-explained>; <https://www.nytimes.com/2022/08/24/climate/california-gas-cars-emissions.html>; and <https://www.oecd-ilibrary.org/sites/e9778969-en/index.html?itemId=/content/publication/e9778969-en#execsumm-d1e47>.

^{viii} See <https://www.woodmac.com/news/the-edge/what-different-scenarios-tell-us-about-the-future-of-oil-and-gas/>.

^{ix} See <https://www.valero.com/sites/default/files/valero-documents/2022-TCFD-Report-FINAL-digital-spreads.pdf>, p. 38.

^x See the GHG Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard: https://ghgprotocol.org/sites/default/files/standards/Corporate-Value-Chain-Accounting-Reporting-Standard-EReader_041613_0.pdf. According to CDP, "Scope 3 encompasses 15 distinct categories covering all emissions along the corporate value chain. The use of sold products falls under category 11 of Scope 3 and typically represents over 90% of total emissions relating to oil and gas companies", see https://cdn.cdp.net/cdp-production/cms/guidance_docs/pdfs/000/000/469/original/CDP-Scope-3-Category11-Guidance-Oil-Gas.pdf?1643046888, p. 7. According to the API, "Scope 3 emissions are emissions that result from value chain activities that are not captured by company scope 1 and scope 2 emissions, such as emissions that result from company-produced fuel used by end-use customers", see <https://www.api.org/~media/Files/EHS/climate-change/Scope-3-emissions-reporting-guidance-2016.pdf>, p. 10.

^{xi} See <https://www.valero.com/sites/default/files/valero-documents/2022-TCFD-Report-FINAL-digital-spreads.pdf>, p. 43.

^{xii} See https://www.neste.com/sites/neste.com/files/attachments/corporate/investors/corporate_governance/neste_sustainability_report_2021.pdf, p. 51.

^{xiii} See <https://www.chevron.com/~media/chevron/sustainability/documents/2021-climate-change-resilience-report.pdf>, p. 58, methodology explained p. 62.

^{xiv} According to the GHG Protocol, “[d]irect (scope 1) removals result where the reporting company owns or controls *both* the sink that transferred CO₂ from the atmosphere *and* the pool where the carbon is stored. Indirect (scope 3) removals result where the reporting company does not own or control both the sink and the associated storage pools.” Further, “[i]n a fossil CCS pathway, CO₂ from industrial and energy-related sources is captured on site at a point source. (...) Geologic storage pathways where carbon is derived from fossil fuels (...) are not accounted for as CO₂ removals. Instead, capture of fossil CO₂ from a point source prevents emissions by capturing and storing the CO₂. All GHG emissions from fugitive losses and processes associated with the geologic storage pathway must be accounted for.” See https://ghgprotocol.org/sites/default/files/standards_supporting/Land-Sector-and-Removals-Guidance-Pilot-Testing-and-Review-Draft-Part-1.pdf, Chapter 3, p. 27, Chapter 5, p. 68., Chapter 10, pgs. 175-177. See also https://ghgprotocol.org/sites/default/files/standards/Corporate-Value-Chain-Accounting-Reporting-Standard_041613_2.pdf.

^{xv} See <https://www.valero.com/sites/default/files/valero-documents/2022-TCFD-Report-FINAL-digital-spreads.pdf>, p. 43.

^{xvi} By the GHG Protocol, Ipieca or the Science Based Target Initiative, for example.

^{xvii} See <https://www.valero.com/sites/default/files/valero-documents/2022-TCFD-Report-FINAL-digital-spreads.pdf>, pgs. 39 and 43.

^{xviii} See https://ghgprotocol.org/sites/default/files/standards/Corporate-Value-Chain-Accounting-Reporting-Standard-EReader_041613_0.pdf, Chapter 11, pgs. 123-124.

^{xix} See https://ghgprotocol.org/sites/default/files/standards/Corporate-Value-Chain-Accounting-Reporting-Standard-EReader_041613_0.pdf, Chapter 9, p. 103.

^{xx} See, e.g., https://ghgprotocol.org/sites/default/files/standards/Corporate-Value-Chain-Accounting-Reporting-Standard_041613_2.pdf, p. 119; or <https://www.api.org/~media/Files/EHS/climate-change/Scope-3-emissions-reporting-guidance-2016.pdf>.

^{xxi} See for example the key characteristics of effective transition plans and the transition plan elements from TCFD, https://assets.bbhub.io/company/sites/60/2021/07/2021-Metrics_Targets_Guidance-1.pdf, pgs. 40-42). See guidance from CDP, <https://www.cdp.net/en/guidance/guidance-for-companies/climate-transition-plans>. See guidance from We Mean Business, <https://www.wemeanbusinesscoalition.org/wp-content/uploads/2022/10/WMBC-Climate-Transition-Action-Plans.pdf>.

^{xxii} See <https://www.valero.com/sites/default/files/valero-documents/2022-TCFD-Report-FINAL-digital-spreads.pdf>.

^{xxiii} See <https://www.phillips66.com/sustainability/our-targets/> and <https://issuu.com/philips66co/docs/2022sustainabilityreport?fr=sYTYwYzUxMzk1MDc>, pgs. 53 and 63.

^{xxiv} See <https://www.marathonpetroleum.com/content/documents/Responsibility/2022-MPC-MPLX-ClimateReport.pdf>, p. 10, and <https://www.marathonpetroleum.com/content/documents/Responsibility/2022-MPC-MPLX-ClimateReport.pdf>, pgs. 12 and 37.

^{xxv} See <https://corporate.exxonmobil.com/-/media/global/files/advancing-climate-solutions-progress-report/2023/2023-acs-progress-report.pdf>, pgs. 6, 47, 92.

^{xxvi} See <https://www.chevron.com/-/media/shared-media/documents/chevron-sustainability-report-2021.pdf>, pgs. 15, 17, 61-64, 80.

^{xxvii} See https://www.neste.com/sites/neste.com/files/attachments/corporate/investors/corporate_governance/neste_sustainability_report_2021.pdf, pgs. 22, 26, 51, 54 and 96.

^{xxviii} See <https://www.marathonpetroleum.com/content/documents/Responsibility/2022-MPC-MPLX-ClimateReport.pdf>, p. 10.

^{xxix} See <https://www.valero.com/renewables>.

^{xxx} See Refining exposure to an accelerating energy transition, <https://carbontracker.org/reports/refining-exposure-to-an-accelerating-energy-transition/>, p. 6. Carbon Tracker specifies that “the contribution to Valero’s processing capacity from renewable diesel and ethanol is limited to under 50kb/d”. This is minimal compared to “the company’s wider >3Mb/d processing capacity.”

^{xxxi} See <https://www.marathonpetroleum.com/Sustainability/Reducing-Our-Carbon-Footprint/> and <https://www.phillips66.com/sustainability/our-targets/>.

^{xxxii} See <https://www.climateaction100.org/company/valero-energy-corporation/>.

^{xxxiii} Blackrock: “We encourage companies to discuss in their reporting how their business model is aligned to a scenario in which global warming is limited to well below 2°C, moving towards global net zero emissions by 2050. Companies help investors understand their approach when they provide disclosures aligned with the four pillars of the TCFD.” See <https://www.blackrock.com/us/individual/literature/publication/blk-stewardship-priorities-final.pdf>. Vanguard: “Where climate change is a material risk, Vanguard encourages companies to set targets that align with [the Paris Agreement’s] goals and to disclose them clearly.” See https://corporate.vanguard.com/content/dam/corp/research/pdf/Global%20investment%20stewardship%20principles_final_112021.pdf. State Street, see <https://www.ssga.com/library-content/pdfs/asset-stewardship/guidance-on-climate-related-disclosures.pdf>.