Chapter 4

Environmental, Social, and Governance Matters: The Rapidly Evolving ESG Reporting Landscape

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PART I.
ESG INTRODUCTION

§ 4:1 ESG Introduction

Environmental, Social, and Governance (ESG) issues have been a mainstream business concern since 2015, when the United Nations' member nations adopted the UN Sustainable Development Goals and countries around the world adopted the Paris Climate Agreement. The financial community has seen a groundswell of investor interest in ESG factors as ESG information is increasingly viewed as significant to investment decisions. At the same time, some investors complain that corporate disclosures in filings with the Securities and Exchange Commission (SEC or Commission) frequently are confined to boilerplate language, and are of limited value to investors who seek to evaluate companies' ESG risks. Investors have called for the SEC to enhance its disclosure requirements and for the U.S. Congress to enact new laws to mandate more ESG disclosures. Some companies and other market participants have expressed concern that enhanced disclosure requirements will be costly for companies, without yielding additional material information for investors. Debate among market participants circles around such issues as whether prescriptive line-item disclosures would be superior to the current principles-based disclosure framework, whether and how the concepts of materiality and the reasonable investor are changing, and how companies might bal-

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ance liability concerns against their stakeholders' desire for more robust ESG information.

ESG disclosure is particularly challenging because it is broad in scope, touching virtually all companies, but also specific in the details, with wide variances across industries and from company to company within an industry. Furthermore, environmental and social concerns that might formerly have been viewed as fringe issues, untethered from financial returns, are now recognized as financially material, mainstream business concerns. Yet it appears that the risks and opportunities associated with ESG factors have not yet been fully integrated into some companies' critical functions, including the financial reporting process.

In the absence of definitive SEC rules, a host of voluntary reporting standards has emerged. The reporting landscape is a patchwork of disclosure regimes that reflects investors' desire for more information about companies' ESG performance, but has left some issuers with questionnaire fatigue, and others simply confused as to what guidance to follow and how to reconcile the different standards. Investors, in turn, complain that current disclosures are not decision-useful and are neither consistent nor comparable from company to company. This mismatch between investors' informational needs and companies' current disclosures has spawned a proliferation of private sector questionnaires, surveys, ratings systems, and indexes, designed to help investors to better evaluate the ESG risks and opportunities facing the companies in which they are invested.

This chapter offers an overview of the SEC reporting requirements as well as the principal voluntary reporting regimes. It explores the divide between the types of information investors desire — such as decision-useful, comparable ESG information across companies within industries — and the types of information that companies most commonly report. Finally, it offers

some thoughts as to potential paths forward for companies navigating this landscape.

§ 4:2 ESG: An overview

ESG factors cover a broad swath and touch on all companies, and yet they do not affect any two companies in precisely the same manner. *Environmental* factors include: the direct and indirect impacts and regulation of climate change; greenhouse gas (GHG) emissions; resource availability and depletion (including critical resources such as water and raw materials); waste and pollution; deforestation; and desertification. *Social* factors include: employee and supply-chain working conditions (including compliance with laws regarding slavery, child labor, health, and safety); local communities (including those of indigenous people); diversity; and economic stability. *Governance* factors include: executive pay; anti-bribery and corruption; political engagement; board diversity and structure; internal controls; corporate ethics; and shareholder rights. Governance also broadly encompasses the manner in which companies address environmental and social risks and the processes companies implement to integrate those risks into company strategy.

ESG issues are both difficult to regulate and challenging for issuers and investors, largely because they cover a broad range of risks and opportunities but also require industry-focused and company-specific information. Climate change, specifically, is a current threat that poses risks of significant concern globally. However, the potential impacts on companies' financial statements are difficult to quantify due to uncertainty concerning specific projected impacts on individual businesses. The Task Force on Climate-related Financial Disclosures (TCFD) has observed that "the large-scale and complex nature of climate

change makes it uniquely challenging, especially in the context of economic decision-making."[1]

A roundtable discussion sponsored by the Sustainability Accounting Standards Board (SASB) in July 2018 pointed to the diversity of companies and their risks, as well as the diversity of investors and their interests as a challenge for those seeking to build ESG reporting standards: "Corporate professionals, investors and other market participants cited a laundry list of obstacles holding up progress toward unlocking the full potential of ESG data for both corporate and investor decision-makers. At the root of many of these issues was the market's attempt to establish a one-size-fits-all solution to measuring ESG performance . . . no two companies — and no two investors — are exactly alike."[2]

This chapter will explore the marked increased interest in ESG matters and the various developments to meet those interests in the past several years.

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[1] 2019 Status Report, Task Force on Climate-Related Financial Disclosures (June 2019), available at https://www.fsb-tcfd.org/publications/tcfd2019-status-report/.

[2] Sustainability Accounting Standards Board, "*Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data*" (2018), available at https://libra ry.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esg-data/. For a further discussion of SASB and its work, see Voluntary Disclosure Frameworks: Sustainability Accounting Standards Board, below.

§ 4:3 ESG trends in the market

The sense of urgency around climate risks has intensified, and ESG issues have become a critical strategic and operational concern for companies across a broad range of industries. KMPG reports that, as of 2020, almost all (96%) of the world's

largest 250 companies (the G250) report on their sustainability performance.[1] The issue now transcends concerns around investor relationships and stock market performance and focuses on the major shifts in industries that have been affected by the transition to a lower-carbon economy. According to a McKinsey & Company paper:

> "We are facing two tipping points: one is economic, and one is environmental. The economic tipping point consists of industry-specific transitions that are driving decarbonization of entire sectors, where players in these industries are taking advantage of the quick pace of innovation to turn sustainability into a competitive advantage. And the environmental tipping point, of course, will determine whether our Earth remains stable—or not."[2]

In a recent study on climate risk, McKinsey found that "[e]conomic and financial systems have been designed and optimized for a certain level of risk and increasing hazards may mean that such systems are vulnerable when they reach systemic thresholds."[3] The study warned that while the direct impact of climate risk may be local, "it can have knock-on effects across regions and sectors, through interconnected socioeconomic and

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[1] KMPG, *The Time Has Come: The KPMG Survey of Sustainability Reporting 2020*, available at home.kpmg/sustainabilityreporting.

[2] Dickon Pinner, "Summit Recap Sustainability at a Tipping Point," McKinsey Insights, https://www.mckinsey.com/business-functions/sustainability/our-insights/sustainability-blog/summit-recap-sustainability-at-a-tipping-point (May 30, 2019).

[3] McKinsey & Company, "Climate Risk and Response: Physical Hazards and Socioeconomic Impacts," (Jan. 16, 2020), available at https://www.mckinsey.com/business-functions/sustainability/our-insights/climate-risk and-response-physical-hazards-and-socioeconomic-impacts?mod=article_inline.

financial systems."[4] The report further warned of "increases in socioeconomic impact of between roughly two and 20 times by 2050 versus today's levels." Further, the socioeconomic impact will increase "in a nonlinear way as hazards reach thresholds beyond which the affected physiological, human-made, or ecological systems work less well or break down and stop working altogether. This is because such systems have evolved or been optimized over time for historical climates."[5]

The World Economic Forum echoed this sense of urgency in its 2020 Global Risk Report, which found that, "[f]or the first time in the history of the Global Risks Perception Survey, environmental concerns dominate the top long-term risks by likelihood among members of the World Economic Forum's multistakeholder Community; three of the top five risks by impact are also environmental."[6] More specifically, "'[f]ailure of climate change mitigation and adaption' is the number one risk by impact and number two by likelihood over the next 10 years," and "'biodiversity loss' is the second most impactful and third most likely risk for the next decade."[7] The report found that

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[4] McKinsey & Company, "Climate Risk and Response: Physical Hazards and Socioeconomic Impacts," available at https://www.mckinsey.com/business-functions/sustainability/our-insights/climate-risk-and-response-physical-hazards-and-socioeconomic-impacts?mod=article_inline.

[5] McKinsey & Company, "Climate Risk and Response: Physical Hazards and Socioeconomic Impacts," available at https://www.mckinsey.com/business-functions/sustainability/our-insights/climate-risk-and-response-physical-hazards-and-socioeconomic-impacts?mod=article_inline.

[6] World Economic Forum, in partnership with Marsh & McLennan Companies and Zurich Insurance Group, "The Global Risks Report 2019," available at https://www3.weforum.org/docs/WEF_Global_Risk_Report_2020.pdf.

[7] World Economic Forum, in partnership with Marsh & McLennan Companies and Zurich Insurance Group, "The Global Risks Report 2019," available at https://www3.weforum.org/docs/WEF_Global_Risk_Report

"[t]he last five years are on track to be the warmest on record, natural disasters are becoming more intense and more frequent, and last year witnessed unprecedented extreme weather throughout the world."[8]

Even during the COVID-19 pandemic, climate matters continue to be a high-impact and high-likelihood risk, as found in the 2021 Global Risk Report. The report states "climate change – to which no one is immune – continues to be a catastrophic risk."[9] Further, the report highlights climate action failure and human-led environmental damage as top risks, explaining "'climate action failure' is the most impactful and second most likely long-term risk identified in the GRPS."[10]

In a September 2020 report of the Climate-Related Market Risk Subcommittee, the Market Risk Advisory Committee of the U.S. Commodity Futures Trading Commission further sounded the alarm as to the systemic threat climate change poses to the U.S. financial system. "Climate change is already impacting or is anticipated to impact nearly every facet of the

_2020.pdf. The Global Risk Report is an annual study, and this is the 14th edition of the Report.

[8] World Economic Forum, in partnership with Marsh & McLennan Companies and Zurich Insurance Group, "The Global Risks Report 2019," available at https://www3.weforum.org/docs/WEF_Global_Risk_Report_2020.pdf.

[9] World Economic Forum, in partnership with Marsh & McLennan Companies and Zurich Insurance Group, "The Global Risks Report 2021," available at http://www3.weforum.org/docs/WEF_The_Global_Risks_Report_2021.pdf.

[10] World Economic Forum, in partnership with Marsh & McLennan Companies and Zurich Insurance Group, "The Global Risks Report 2021," available at http://www3.weforum.org/docs/WEF_The_Global_Risks_Report_2021.pdf.

economy, including infrastructure, agriculture, residential and commercial property, as well as human health and labor productivity. Over time, if significant action is not taken to check rising global average temperatures, climate change impacts could impair the productive capacity of the economy and undermine its ability to generate employment, income, and opportunity."[11] The risks of paying insufficient attention to ESG issues are not lost on the business community. The U.S. Chamber of Commerce Foundation conducted a series of roundtables across the U.S. with a view to collecting information as to how market participants — CEOs, CFOs, sustainability officers, general counsels, investor relations professionals, and others — view the ESG landscape.[12] The Chamber found, "since the Securities and Exchange Commission (SEC) issued its 2010 guidance on climate change disclosure, 59% of companies reported they are disclosing more information regarding climate change. When it comes to shareholder communication, nearly two-thirds (63%) of companies are communicating with their shareholders regarding the evolving risks associated with climate change and 46% have increased the level of detail in climate change reporting due to shareholder input."[13]

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[11] Report of the Climate-Related Market Risk Subcommittee, Market Risk Advisory Committee of the U.S. Commodity Futures Trading Commission, "Managing Climate Risk in the U.S. Financial System," (Sept. 9, 2020), available at https://www.cftc.gov/sites/default/files/2020-09/9-9-20%20Report%20of%20the%20Subcommittee%20on%20Climate-Related%20Market%20Risk%20-%20Managing%20Climate%20Risk%20in%20the%20U.S.%20Financial%20System%20for%20posting.pdf.

[12] U.S. Chamber of Commerce Foundation, "Climate Change & ESG Reporting from the Public Company Perspective" (Aug. 2021) available at https://www.centerforcapitalmarkets.com/wp-content/uploads/2021/08/CCMC_ESG_Report_v4.pdf.

[13] U.S. Chamber of Commerce Foundation, "U.S. Chamber Survey on ESG and Climate Change Finds Most Companies Have Increased Amount of

In addition to increased disclosure and shareholder communication, 2021 saw an active proxy season for ESG initiatives. Climate Action 100+, a group of over 600 investors representing $55 trillion in assets under management, has engaged over 150 companies with its "Net-Zero Company Benchmark." This benchmark includes goals for emissions reductions, governance around climate-risk, and proper disclosure related to net zero efforts.[14] In addition, Climate Action 100+ flags shareholder proposals for investors' consideration that relate to climate change, lobbying, corporate governance, and other relevant topics.[15] One impact investment group made headlines in 2021 through its activist campaign against the Board of an international oil and gas conglomerate. The small activist investor firm touted its belief that long-term value is purpose-built and successfully claimed three board seats after pushing the target company to shift away from fossil fuels ahead of its annual shareholder meeting in May 2021.[16]

The 2021 proxy season also saw record-breaking support levels for environmental proposals, with an 100% increase in the number of environmental proposals that have passed year-

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Climate Change Disclosure" available at https://www.uschamber.com/press-release/us-chamber-survey-esg-and-climate-change-finds-most-companies-have-increased-amount-of (Aug. 2021).

[14] Climate Action 100+, About Climate Action 100+ available at https://www.climateaction100.org/about/.

[15] Climate Action 100+, Proxy Season available at https://www.climateaction100.org/approach/proxy-season/.

[16] Engine No. 1, "Reenergize ExxonMobil: Summary Investor Presentation (May 2021) available at https://reenergizexom.com/wp-content/uploads/2021/05/Investor-Presentation-Summary-May-2021.pdf.

over-year.[17] Social proposals on board diversity, human rights in operations and supply chains, political contributions, lobbying policies, and workforce diversity, equity, and inclusion matters have also received increased support in 2021.[18]

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[17] Georgeson, "An Early Look at the 2021 Proxy Season" available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf.

[18] Georgeson, "An Early Look at the 2021 Proxy Season" available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf.

§ 4:4 COVID-19 acceleration of ESG priorities

As the global economy began to rebuild from the COVID-19 pandemic, political initiatives to "build back better" solidified the acceleration of ESG trends.

Throughout 2021, U.S. President Joe Biden has promoted "The Build Back Better Agenda," which aims to provide COVID-19 relief funds while reducing social and economic inequalities and creating jobs in the clean energy industry.[1]

Alongside this agenda, the Biden Administration has issued a number of climate-focused executive orders. In May 2021, President Biden signed into effect an Executive Order on Climate-Related Financial Risk, which requires federal agencies and regulators to assess climate-related financial risks to the stability of the U.S. economy and to advance the disclosure of

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[1] The White House, "Build Back Better" available at https://www.whitehouse.gov/build-back-better/.

such risks.[2] This followed a January 2021 Executive Order on Tackling the Climate Crisis at Home and Abroad, which encouraged a “whole-of-government approach” for a government-wide climate-risk strategy to address environmental justice, to achieve net carbon neutrality by 2050, pursue clean energy jobs and financing, enhance global partnerships to meet the Paris Agreement goals, and other key targets.

The European Commission (EC) has also prioritized ESG initiatives to drive a portion of their COVID-19 recovery. “NextGenerationEU” directs €750 billion of stimulus towards EU Member State economies, to aid them in recovering from the pandemic while creating a greener and more resilient economy.[3] One third of the investments from the NextGenerationEU Recovery Plan will finance The European Green Deal, an EU commitment that “sets out how to make Europe the first climate neutral continent by 2050, boosting the economy, improving people’s health and quality of life, caring for nature, and leaving no one behind.”[4] The EC noted, “the European Green Deal is also our lifeline out of the COVID-19 pandemic.”[5]

In August 2021, the Intergovernmental Panel on Climate Change (IPCC), an intergovernmental body of the United Nations, released the Sixth Assessment Report (AR6). AR6 pro-

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[2] The White House, “Executive Order on Climate-Related Financial Risk” available at https://www.whitehouse.gov/briefing-room/presidential-actions/2021/05/20/executive-order-on-climate-related-financial-risk/.

[3] Official website of the European Union, “NextGenerationEU” available at https://europa.eu/next-generation-eu/index_en.

[4] Https://ec.europa.eu/commission/presscorner/detail/e%20n/ip_19_6691.

[5] European Commission, official website, “A European Green Deal” available at https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en.

vides the most up-to-date physical understanding of the climate system and climate change, noting, "It is unequivocal that human influence has warmed the atmosphere, ocean and land. Widespread and rapid changes in the atmosphere, ocean, cryosphere and biosphere have occurred."[6] UN Secretary-General António Guterres described the report as "a code red for humanity", saying, "[t]he alarm bells are deafening, and the evidence is irrefutable: greenhouse gas emissions from fossil-fuel burning and deforestation are choking our planet and putting billions of people at immediate risk."[7] The report continues to provide evidence to support the fact that, without a rapid and sustained movement away from fossil fuel burning and deforestation, the average global temperature will exceed critical thresholds of 1.5 and 2.0 degrees Celsius within the 21st century.[8] Highlighting the need for climate action on an accelerated timeframe, U.S. Special Presidential Envoy for Climate, John Kerry responded, "What the world requires now is real action. All major econo-

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[6] IPCC, 2021: Summary for Policymakers. In: Climate Change 2021: The Physical Science Basis. Contribution of Working Group I to the Sixth Assessment Report of the Intergovernmental Panel on Climate Change [Masson-Delmotte, V., P. Zhai, A. Pirani, S. L. Connors, C. Péan, S. Berger, N. Caud, Y. Chen, L. Goldfarb, M. I. Gomis, M. Huang, K. Leitzell, E. Lonnoy, J.B.R. Matthews, T. K. Maycock, T. Waterfield, O. Yelekçi, R. Yu and B. Zhou (eds.)]. Cambridge University Press. In Press.

[7] United Nations, "Secretary-General Calls Latest IPCC Climate Report 'Code Red for Humanity', Stressing 'Irrefutable' Evidence of Human Influence" available at https://www.un.org/press/en/2021/sgsm20847.doc.htm.

[8] IPCC, 2021: Summary for Policymakers. In: Climate Change 2021: The Physical Science Basis. Contribution of Working Group I to the Sixth Assessment Report of the Intergovernmental Panel on Climate Change [Masson-Delmotte, V., P. Zhai, A. Pirani, S. L. Connors, C. Péan, S. Berger, N. Caud, Y. Chen, L. Goldfarb, M. I. Gomis, M. Huang, K. Leitzell, E. Lonnoy, J.B.R. Matthews, T. K. Maycock, T. Waterfield, O. Yelekçi, R. Yu and B. Zhou (eds.)]. Cambridge University Press. In Press.

mies must commit to aggressive climate action during this critical decade."[9]

In November 2021, the 26th Conference of the Parties (COP 26) to the UN Framework Convention on Climate Change will provide an opportunity for international coordination on these fronts. From the IPCC report to COP26, the environmental and social implications of climate change have expedited the urgency for the adoption of ESG principles and actions.

Instances of social unrest have also been particularly visible during the past couple of years, prompting closer scrutiny of social issues, most keenly evidenced by the Black Lives Matter movement. Specifically, the COVID-19 pandemic highlighted, "the very issues that have been driving ESG concerns—managing resources, sustainability, community impact and employee well-being."[10] Rather than diverting attention from ESG concerns, stakeholders have observed that "the very actions companies are taking will likely bring them closer to the multi-stakeholder, long-term value principles that lie at the heart of ESG."[11] For example, a large group of nonprofit organizations — socially responsible investors, labor unions, and others — submitted a letter to then-SEC Chair Jay Clayton demanding greater disclosure concerning how "companies are acting to

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[9] Postmedia Network Inc., Reactions to landmark U.N. climate science report [K. Abnett, N. Chestney, J. Spring, K. Liffey] Postmedia Breaking News. In Press.

[10] Financial Executives International, "How ESG Issues Are Being Discussed in The Boardroom Amid The COVID-19 Pandemic," available at https://www.financialexecutives.org/FEI-Daily/June-2020/How-ESG-IssuesAre-Being-Discussed-in-The-Boardroo.aspx.

[11] Letter to SEC on Covid-19 Disclosure, available on https://our financial security.org/wp-content/uploads/2020/06/Sign-on-Letter-to-SEC-on-COVID-Disclosure.pdf.

protect workers, prevent the spread of the virus, and responsibly use any federal aid they receive."[12] The letter emphasized the importance of protecting workers' health and safety "to limit the damage to their suppliers and customers."[13]

A study conducted in response to the Black Lives Matter protests found that more than 200 of the S&P 500 companies issued one or more public statements related to racial justice.[14] The study suggests that, "customer-facing companies in the consumer goods and financial institution sectors were the first to respond."[15] Moreover, a number of global brands released statements condemning racism and injustice,[16] and many companies donated millions of dollars to nonprofit organizations.[17]

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[12] Letter to SEC on Covid-19 Disclosure, available on https://ourfinancial security.org/wp-content/uploads/2020/06/Sign-on-Letter-to-SEC-on-COVID-Disclosure.pdf.

[13] Letter to SEC on Covid-19 Disclosure, available on https://ourfinancial security.org/wp-content/uploads/2020/06/Sign-on-Letter-to-SEC-on-COVID-Disclosure.pdf.

[14] S&P Global Ratings, "Why Corporations' Responses to George Floyd Protests Matter," available at https://www.spglobal.com/ratings/en/research/articles/200723-environmental-social-and-governance-why-corporations-responses-to-george-floyd-protests-matter-11568216.

[15] S&P Global Ratings, "Why Corporations' Responses to George Floyd Protests Matter," available at https://www.spglobal.com/ratings/en/research / articles/200723-environmental-social-and-governance-why-corporations-responses-to-george-floyd-protests-matter-11568216.

[16] S&P Global Ratings, "Why Corporations' Responses to George Floyd Protests Matter," available at https://www.spglobal.com/ratings/en/research/articles/200723-environmental-social-and-governance-why-corporations-responses-to-george-floyd-protests-matter-11568216.

[17] S&P Global Ratings, "Why Corporations' Responses to George Floyd Protests Matter," available at https://www.spglobal.com/ratings/en/research /

Financial regulators hear and are responding to the calls for improved diversity, equity, and inclusion. In September 2020, Commissioner Allison Herren Lee provided remarks at the Council of Institutional Investors on how and why "Diversity Matters, Disclosure Works and the SEC Can Do More."[18] Commissioner Lee pointed to not only the lack of diversity in the corporate community, but also in the financial regulatory community. The Commissioner highlighted the shortcomings of the 2018 guidance, which encouraged the disclosure of self-identified characteristics of board candidates, saying, "While I appreciate these measures, given that women of color hold just 4.6% of board seats and less than one percent of Fortune 500 CEOs are Black, it's time to consider how to get investors the diversity information they need to allocate their capital wisely."[19]

This focus on social equity is not entirely new, indeed, corporations have increasingly focused on diversity in corporate leadership in the last several years. In 2017, State Street Global Advisors (SSGA) launched its "fearless girl" campaign, calling on 3,500 companies in which SSGA invests on behalf of clients, representing more than $30 trillion in market capitalization, to

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articles/200723-environmental-social-and-governance-why-corporations-responses-to-george-floyd-protests-matter-11568216.

[18] "Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference," Remarks by Commissioner Allison Herren Lee (Sep. 2020), available at https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922#_ftn4.

[19] "Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference," Remarks by Commissioner Allison Herren Lee (Sep. 2020), available at https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922#_ftn4.

increase the number of women on their corporate boards.[20] SSGA further announced that, starting in 2020, it "will vote against the entire slate of board members on the nominating committee if a company does not have at least one woman on its board, and has not engaged in successful dialogue on State Street Global Advisors' board gender diversity program for three consecutive years."[21] BlackRock stated that it "would normally expect to see at least two women directors on every board."[22] Further, in early 2020, Goldman Sachs' CEO averred that Goldman will take companies public only if there is "at least one diverse board candidate, with a focus on women. . . . And we're going to move towards 2021 requesting two."[23] An Institutional Shareholder Services (ISS) study found that, as of July 2019, there were no longer any all-male boards among the S&P 500 companies[24] and that women filled 45 percent of new

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[20] "State Street Global Advisors Calls on 3,500 Companies Representing More Than $30 Trillion in Market Capitalization to Increase Number of Women on Corporate Boards," available at https://www.businesswire.com/news/home/20170307005817/en/.

[21] State Street Global Advisors, "State Street Global Advisors Reports Fearless Girl's Impact: More than 300 Companies Have Added Female Directors," available at https://newsroom.statestreet.com/press-release/corporate/state-street-global-advisors-reports-fearless-girls-impactmore-300-companie.

[22] The Wall Street Journal, "BlackRock: Companies Should Have at Least Two Female Directors," available at https://www.wsj.com/articles/blackrock-companies-should-have-at-least-two-female-directors-15175984 07.

[23] CNBC, "Goldman won't take companies public without 'at least one diverse board candidate,' CEO says," available at https://www.cnbc.com/2020/01/23/goldman-wont-take-companies-public-that-dont-have-at-leastone-diverse-board-candidate-ceo-says.html.

[24] The Wall Street Journal, "The Last All-Male Board on the S&P 500 is No Longer," available at https://www.wsj.com/articles/the-last-all-maleboard-on-the-s-p-500-is-no-longer-11564003203?mod=hp_featst_pos2.

Russell 3000 board seats in 2019, compared to only 12 percent in 2008.[25]

Nasdaq made a meaningful impact in this regard when, in August 2021, the SEC approved its Board Diversity Objective. The Board Diversity Objective requires companies listed on Nasdaq to publicly disclose board-level diversity statistics using a standardized template by August 8, 2022.[26] The requirements also include a timeline by which companies should have, or explain why they do not have, at least two "diverse" directors, including at least one director who self-identifies as female and one who self-identifies as either an underrepresented minority or LGBTQ+. The requirement will not come into force immediately; under a transition period based on the listing tier of a company, the requirements will become effective in a staggered manner between 2023 and 2026. There is also some additional flexibility for smaller companies, which can meet the requirement with either (i) two female directors, or (ii) one female director and one Underrepresented Minority or LGBTQ+ director. Pre-business combination SPACs are exempt from the requirements altogether. New SEC Chair Gary Gensler, when announcing the approval of the Board Diversity Objective, stated that, "[t]hese rules will allow investors to gain a better understanding of Nasdaq-listed companies' approach to board diversity, while ensuring that those companies have the flexibility to make decisions that best serve their shareholders."

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[25] Harvard Law School Forum on Corporate Governance, "U.S. Board Diversity Trends in 2019," available at https://corpgov.law.harvard.edu/2019/06/18/u-s-board-diversity-trends-in-2019/.

[26] Latham & Watkins LLP, "SEC Approves Nasdaq's Board Diversity Proposal," available at https://www.globalelr.com/2021/08/sec-approves-nasdaqs-board-diversity-proposal/.

Companies have also been following this trend toward building greater board racial and ethnic diversity. Close to half of the Fortune 100 "explicitly disclose the board's racial and ethnic diversity, up from 23 percent three years ago."[27] In response to the COVID-19 pandemic and racial justice protests, more companies plan to incorporate environmental and social targets into their executive pay packages over the next several years. In a Willis Towers survey, 27 percent of respondents include ESG metrics in their executive incentive plans and an additional two percent plan to include ESG measures in their plans in 2021.[28] An additional 27 percent indicated that they are considering adding them by 2023.[29] "Pressure has been mounting for companies to demonstrate a commitment to ESG. . . . Some investors are becoming increasingly vocal on environmental issues while the pandemic and social unrest are accelerating the focus on social issues by many boards."[30]

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[27] Ernst & Young, "Five Takeaways from the 2019 Proxy Season," available at https://assets.ey.com/content/dam/ey-sites/ey-com/en_us/topics/cbm/ey-cbm-2019-proxy-season-preview.pdf.

[28] Globe Newswire, "More North American companies expressing interest in ESG measures for executive pay programs," available at https://www.globenewswire.com/news-release/2020/08/12/2077300/0/en/More-North-American-companies-expressing-interest-in-ESG-measuresfor-executive-pay-programs.html.

[29] Globe Newswire, "More North American companies expressing interest in ESG measures for executive pay programs," available at https://www.globenewswire.com/news-release/2020/08/12/2077300/0/en/More-North-American-companies-expressing-interest-in-ESG-measuresfor-executive-pay-programs.html.

[30] Globe Newswire, "More North American companies expressing interest in ESG measures for executive pay programs," available at https://www.globenewswire.com/news-release/2020/08/12/2077300/0/en/More-North-American-companies-expressing-interest-in-ESG-measuresfor-executive-pay-programs.html.

At a state level, California is leading efforts to advance board and executive level diversity among companies in the state. Legislation enacted in 2018 requires publicly held corporations with principal executive offices located in California to have a minimum of one female director.[31] By December 31, 2021, the minimum increases to two if the corporation has five directors, and to three women directors if the corporation has six or more directors.[32] The law also requires a report to be published on the website of the California Secretary of State providing the level of compliance with the provisions.[33] According to a *Wall Street Journal* report, the law has had a significant impact.[34] Since the law came into effect, 244 companies have added at least one woman director, and 41 companies have added two.[35] As of May 2021, the California Partners Project found that women now hold 1,483 board seats, nearly double the 766 seats held by women in 2018.[36]

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[31] California, Senate Bill No. 826, available at http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201720180SB826.

[32] California, Senate Bill No. 826, available at http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201720180SB826.

[33] California, Senate Bill No. 826, available at http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201720180SB826.

[34] *The Wall Street Journal*, "California Law Spurs Companies to Add Female Directors," available at https://www.wsj.com/articles/california-lawspurs-companies-to-add-female-directors-11576665000.

[35] *The Wall Street Journal*, "California Law Spurs Companies to Add Female Directors," available at https://www.wsj.com/articles/california-lawspurs-companies-to-add-female-directors-11576665000.

[36] California Partners Project, "Claim Your Sear: Women of Color on California's Public Company Boards," available at https://www.calpartnersproject.org/wocclaimyourseat.

In September 2020, California passed a new law designed to promote racial diversity on boards of directors.[37] Similar to the 2018 law, the new law requires a minimum of one director on boards of impacted public companies from "underrepresented communities" by the end of 2021, including directors who self-identify as African American, Hispanic, Latino, Asian, Pacific Islander, Native American, Native Hawaiian, Alaska Native, gay, lesbian, bisexual, or transgender.[38] The law requires, no later than the end of 2022, a minimum of two directors from underrepresented communities for a corporation with more than four but fewer than nine directors, and a minimum of three directors from underrepresented communities for a corporation with nine or more directors.[39]

In October 2019, the Office of the New York City Comptroller launched its Boardroom Accountability Project 3.0 to increase board and CEO diversity.[40] The third phase of the initiative calls on companies to adopt "a version of the 'Rooney Rule' pioneered by the National Football League (NFL)," which was designed to increase minority candidates for head coaching and general manager positions.[41] To launch the project, the

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[37] California, Assembly Bill No. 979, http://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201920200AB979.

[38] California, Assembly Bill No. 979, available at http://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201920200AB979.

[39] California, Assembly Bill No. 979, available at http://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201920200AB979.

[40] The City of New York, Office of the Comptroller, "Boardroom Accountability Project 3.0," available at https://comptroller.nyc.gov/services/financial-matters/boardroom-accountability-project/overview/.

[41] The City of New York, Office of the Comptroller, "Boardroom Accountability Project 3.0," available at https://comptroller.nyc.gov/services/financial-matters/boardroom-accountability-project/overview/.

Comptroller's Officer sent a letter to 56 companies in the S&P 500 to adopt a Rooney Rule policy.[42] According to the letter, the Rooney Rule would require the companies to "widen the talent pool and require the inclusion of a diverse set of candidates for consideration."[43] In April 2020, the Office of the New York City Comptroller announced the initial results of the initiative.[44] The Office has "negotiated pioneering Board and CEO diversity search policies with 13 leading companies in response to shareholder proposals."[45] Those companies "have approved, and publicly disclosed, policies requiring the consideration of qualified women and racially/ethnically diverse candidates for director and external CEO searches."[46]

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[42] The City of New York, Office of the Comptroller, available at https://comptroller.nyc.gov/wp-content/uploads/2019/10/Rooney-Rule-Sample-Letter.pdf.

[43] The City of New York, Office of the Comptroller, available at https://comptroller.nyc.gov/wp-content/uploads/2019/10/Rooney-Rule-Sample-Letter.pdf.

[44] The City of New York, Office of the Comptroller, "NYC Comptroller Stringer and Retirement Systems Announce Precedent-Setting Board/CEO Diversity Search Policies as part of Boardroom 3.0 Initiative," available at https://comptroller.nyc.gov/newsroom/nyc-comptroller-stringer-and-retirement-systems-announce-precedent-setting-board-ceo-diversity-search-policies-as-part-of-boardroom-3-0-initiative/.

[45] The City of New York, Office of the Comptroller, "NYC Comptroller Stringer and Retirement Systems Announce Precedent-Setting Board/CEO Diversity Search Policies as part of Boardroom 3.0 Initiative," available at https://comptroller.nyc.gov/newsroom/nyc-comptroller-stringer-and-retirement-systems-announce-precedent-setting-board-ceo-diversity-search-policies-as-part-of-boardroom-3-0-initiative/.

[46] The City of New York, Office of the Comptroller, "NYC Comptroller Stringer and Retirement Systems Announce Precedent-Setting Board/CEO Diversity Search Policies as part of Boardroom 3.0 Initiative," available at https://comptroller.nyc.gov/newsroom/nyc-comptroller-stringer-and-retire

At the national level, in July 2020, a group of business organizations, including the American Bankers Association, the National Association of Real Estate Investment Trusts, the National Association of Investment Companies, National Investor Relations Institute, and the U.S. Chamber of Commerce sent a letter to the Chair and Ranking Member of the U.S. Senate Committee on Banking, Housing and Urban Affairs urging the committee to pass legislation to improve corporate board diversity. Specifically, the letter asked the committee to pass H.R. 5084, the Improving Corporate Governance Through Diversity Act of 2019, which the House of Representatives passed in November 2019.[47] The bill would require certain companies to disclose the racial, ethnic, and gender composition of their boards and executive management as well as their plans to promote racial, ethnic, and gender diversity.[48]

This focus on board and executive diversity is not merely for show, indeed, studies have drawn a correlation between diversity on executive teams and financial outperformance.[49] McKinsey's 2020 study, which includes more than 1,000 large companies from 15 countries, finds that "companies in the top quartile

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ment-systems-announce-precedent-setting-board-ceo-diversity-search-polici es-as-part-of-boardroom-3-0-initiative/.

[47] Letter to the Honorable Mike Crapo, Chairman, and the Honorable Sherrod Brown, Ranking Member, Committee on Banking, Housing, and Urban Affairs, United States Senate (July 27, 2020), available at https://www.uschamber.com/sites/default/files/200727_coalition_h.r._5084_senat esmallbusiness.pdf.

[48] "Improving Corporate Governance Through Diversity Act," H.R. 5084– 116th Congress (2019-2020), available at https://www.congress.gov/bill/116th-congress/house-bill/5084.

[49] McKinsey & Company, "Diversity wins: How inclusion matters," available at https://www.mckinsey.com/featured-insights/diversity-and-inclu sion/diversity-wins-how-inclusion-matters.

for gender diversity on executive teams were 25 percent more likely to have above-average profitability than companies in the fourth quartile."[50] Moreover, "[c]ompanies with more than 30 percent women executives were more likely to outperform companies where this percentage ranged from 10 to 30."[51] Similarly, in the case of ethnic and cultural diversity, companies in the top quartile were found to have been 36 percent more profitable than those in the fourth quartile.[52]

[50] McKinsey & Company, "Diversity wins: How inclusion matters," available at https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters.

[51] McKinsey & Company, "Diversity wins: How inclusion matters," available at https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters.

[52] McKinsey & Company, "Diversity wins: How inclusion matters," available at https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters.

§ 4:5 Growing investor interest in ESG

The investor community has shown an increasingly keen focus on ESG issues in recent years. The broad adoption of the UN Principles for Responsible Investment (PRI) among investment professionals illustrates the point. The UN adopted the PRI in 2006, establishing a set of investment principles by which the signatories incorporate ESG considerations in their investment processes.[1] As of August 2021, firms that have sub-

[1] U.N. Principles for Responsible Investment, www.unpri.org.PRI signatories subscribe to six principles that guide the integration of ESG into the investment process:

scribed to the PRI control more than $121 trillion in assets under management.[2] According to the Global Sustainable Investment Alliance, "At the start of 2020, global sustainable investments reached USD35.3 trillion in the five major markets covered in this report, a 15% increase in the past two years (2018-2020)[3] and a 55% increase in the past four years (2016-2020)."[4] In the United States and Europe, the Alliance reports

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> Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes.
>
> Principle 2: We will be active owners and incorporate ESG issues into our ownership policies and practices.
>
> Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.
>
> Principle 4: We will promote acceptance and implementation of the Principles within the investment community.
>
> Principle 5: We will work together to enhance our effectiveness in implementing the Principles.
>
> Principle 6: We will each report on our activities and progress toward implementing the Principles.

[2] Principles for Responsible Investment, "PRI Growth 2006-2021 data and methodology" available at https://www.unpri.org/pri/about-the-pri.

[3] Global Sustainable Investment Alliance, "2018 Global Sustainable Investment Review," available at http://www.gsi-alliance.org/wp-content/uploads/2019/03/GSIR_Review2018.3.28.pdf.

[4] Global Sustainable Investment Alliance, "2020 Global Sustainable Investment Review," available at http://www.gsi-alliance.org/wp-content/uploads/2021/07/GSIR-2020.pdf. The five markets covered in this report are the United States, Canada, Japan, Australia and Europe. The Review defines sustainable investing as investment practices that apply any if the following strategies: (1) ESG integration, (2) corporate engagement & shareholder action, (3) norms-based screening, (4) negative/exclusionary based screening, (5) best-in-class/positive screening, (6) sustainability themed/thematic investing, and (7) impact investing and community investing.

that these regions "continue to represent more than 80% of global sustainable investing assets during 2018 to 2020."[5] Furthermore, this growth in sustainable investments does not appear to have slowed. A February 2020 Deloitte report projects that "ESG-mandated assets in the United States could grow almost three times as fast as non-ESG-mandated assets to comprise half of all professionally managed investments by 2025."[6] The report also provides that "[a]n estimated 200 new funds in the United States with an ESG investment mandate are expected to launch over the next three years, more than doubling the activity from the previous three years."[7]

BlackRock produced the following infographic as part of its own analysis of sustainable investing. The study found steady growth in investments in sustainable ETFs and mutual funds over the past five years and anticipated further growth over the coming decade.

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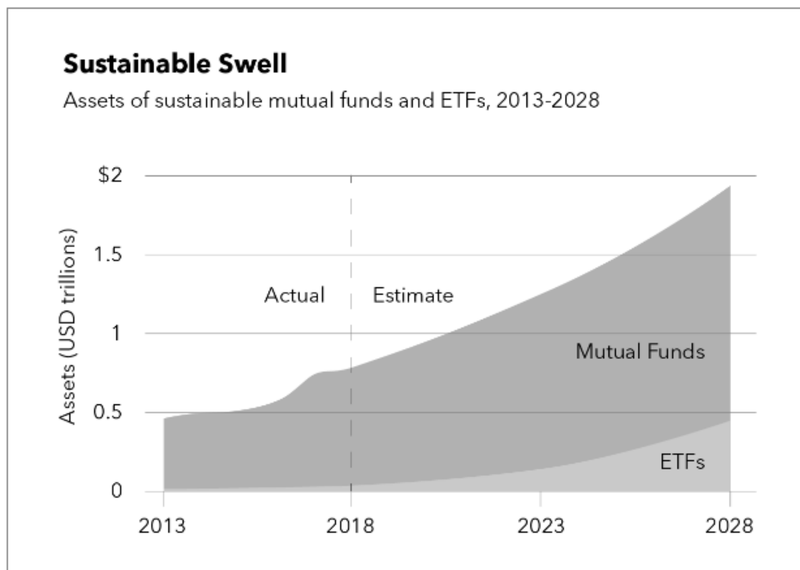
[5] Global Sustainable Investment Alliance, "2020 Global Sustainable Investment Review," available at http://www.gsi-alliance.org/wp-content/uploads/2021/07/GSIR-2020.pdf.

[6] Deloitte, "Advancing environmental, social, and governance investing" (Feb. 2020), available at https://www2.deloitte.com/us/en/insights/industry/financial-services/esg-investing-performance.html.

[7] Deloitte, "Advancing environmental, social, and governance investing" (Feb. 2020), available at https://www2.deloitte.com/us/en/insights/industry/financial-services/esg-investing-performance.html.

The growth of sustainable investing

Assets in dedicated sustainable investing strategies have grown at a rapid pace in recent years, and this trend is showing no signs of slowing.



In BlackRock's 2020 annual letter to CEOs, BlackRock's CEO, Larry Fink, announced a number of initiatives designed to put "sustainability at the center of [BlackRock's] investment approach."[8] According to the letter, "[c]limate change has become a defining factor in companies' long-term prospects," and "we are on the edge of a fundamental reshaping of finance."[9]

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[8] BlackRock, "Larry Fink's Annual Letter to CEOs" (2020), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[9] BlackRock, "Larry Fink's Annual Letter to CEOs" (2020), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

BlackRock believes that "sustainability and climate-integrated portfolios can provide better risk-adjusted returns to investors," and "sustainable investing is the strongest foundation for client portfolios going forward."[10]

To that end, BlackRock announced several new initiatives, including "making sustainability integral to portfolio construction and risk management; exiting investments that present a high sustainability-related risk, such as thermal coal producers; launching new investment products that screen fossil fuels; and strengthening our commitment to sustainability and transparency in our investment stewardship activities."[11] BlackRock advocates adoption of the SASB standards for reporting on sustainability and the TCFD for evaluating and reporting climate risks.[12] In addition, BlackRock "will be increasingly disposed to vote against management and board directors when companies are not making sufficient progress on sustainability-related disclosures and the business practices and plans underlying them."[13]

In the letter, BlackRock specifically asks companies to: (1) publish a disclosure in line with industry-specific SASB guidelines by year-end, if they have not already done so, or disclose a similar set of data in a way that is relevant to their particular business; and (2) disclose climate-related risks in line with the TCFD's recommendations, if they have not already done so. This should include the company's plan for operating under a

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[10] BlackRock, "Larry Fink's Annual Letter to CEOs" (2020), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[11] BlackRock, "Larry Fink's Annual Letter to CEOs" (2020), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[12] BlackRock, "Larry Fink's Annual Letter to CEOs" (2020), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[13] BlackRock, "Larry Fink's Annual Letter to CEOs" (2020), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

scenario in which the Paris Agreement's goal of limiting global warming to less than two degrees is fully realized, as expressed by the TCFD guidelines.[14]

In the year that followed these requests to CEOs, there was a 363 percent increase in SASB disclosures from the previous year and the support for TCFD grew in total to 1,700 organizations.[15]

In July 2020, BlackRock published a new report reemphasizing its conviction that "climate risk is investment risk," and that its approach on climate issues "is to focus [its] efforts on sectors and companies where climate change poses the greatest material risk to [the] clients' investments."[16] BlackRock stated that, in 2020, it "identified 244 companies that are making insufficient progress integrating climate risk into their business models or disclosures."[17] Of these companies, BlackRock took voting action against 53, or 22 percent, when it found "corporate leadership [was] unresponsive to investors' concerns about climate risk or assessed their disclosures to be insufficient given the importance to investors of detailed information on climate risk

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[14] BlackRock, "Larry Fink's Annual Letter to CEOs" (2020), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[15] BlackRock, "Larry Fink's 2021 Letter to CEOs" (2021), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[16] BlackRock, "Our Approach to Sustainability" (2020), available at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

[17] BlackRock, "Our Approach to Sustainability" (2020), available at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

and the transition to a low-carbon economy."[18] A majority of the companies were in the energy sector, with some in utilities, industrials, and materials, and one was in the financial industry.[19] In addition, BlackRock "put the remaining 191 companies 'on watch.' Those that do not make significant progress risk voting action against management in 2021."[20] It also identified "110 other companies across carbon-intensive sectors to initiate engagement with in the second half of 2020. These 110 companies represent over $2.7 trillion in market cap of carbon-intensive industries, nearly 1.7 billion tons of CO2 emissions and over $132 billion of our clients' exposure."[21] While the focus of the report is on climate-related issues, BlackRock advised that, in the second half of 2020, it will also "assess the impact of companies' response to COVID-19 and associated issues of racial equality" and "will continue to emphasize the importance of diversity in the board room."[22]

After BlackRock's 2020 letter was published, and the COVID-19 pandemic spread throughout the globe, climate

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[18] BlackRock, "Our Approach to Sustainability" (2020), available at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

[19] BlackRock, "Our Approach to Sustainability" (2020), available at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

[20] BlackRock, "Our Approach to Sustainability" (2020), available at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

[21] BlackRock, "Our Approach to Sustainability" (2020), available at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

[22] BlackRock, "Our Approach to Sustainability" (2020), available at https://www.blackrock.com/corporate/literature/publication/our-commitment-to-sustainability-full-report.pdf.

change still remained at the top of investors' priority lists. In BlackRock's 2021 letter to CEOs, Fink focuses on the connection between the pandemic and the risks of climate change, saying "I believe that the pandemic has presented such an existential crisis – such a stark reminder of our fragility – that it has driven us to confront the global threat of climate change more forcefully. . . . No issue ranks higher than climate change on our clients' list of priorities. They ask us about it nearly every day."[23]

BlackRock's 2021 message to CEOs strengthened the notion that the climate transition was accelerated by the continuation of the ESG and sustainable investing movement over the course of 2020, saying "in March [of 2020], the conventional wisdom was the crisis would divert attention from climate. But just the opposite took place, and the reallocation of capital accelerated even faster than I anticipated."[24] Investment in mutual funds and ETFs in sustainable assets increased by $288 billion globally from January through November 2020, marking a 96 percent increase over the whole of 2019.[25]

Notably, ESG investing has shown resilience throughout the COVID-19 crisis. According to a BlackRock study of 32 globally representative sustainable indices and their non-sustainable counterparts, throughout the whole of 2020, 81 percent of sustainable indexes outperformed their parent benchmarks.[26] Be-

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[23] BlackRock, "Larry Fink's 2021 Letter to CEOs" (2021), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[24] BlackRock, "Larry Fink's 2021 Letter to CEOs" (2021), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[25] BlackRock, "Larry Fink's 2021 Letter to CEOs" (2021), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[26] BlackRock, "Larry Fink's 2021 Letter to CEOs" (2021), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

yond outperformance, BlackRock's analysis continues to report that not only are broad-market ESG indexes outperforming their counterparts, but within industries "companies with better ESG profiles are performing better than their peers, enjoying a 'sustainability premium.'"[27]

The outperformance of ESG funds during the COVID-19 crisis appears likely to stimulate continued investment in ESG funds even after the crisis has passed. To meet the challenge of adapting to a world in which we must keep global warming well below 2 degrees Celsius, deep reductions in carbon dioxide are necessary in the coming decades. Globally, we are seeing governmental bodies and the corporate community alike setting net zero targets.

As of August 2021, over 130 countries have set or are considering net zero emissions targets and of the 191 countries party to the Paris Agreement, 110 have so far submitted a new or updated national action plan as required by the agreement.[28] As the international community and investment community prioritize the transition to a net zero economy, companies globally should prepare to incorporate plans to address this transition in their long-term ESG strategy.

Consequentially, BlackRock's 2021 letter asked public and large private companies to: (1) disclose a plan for how their business model will be compatible with a net zero economy, in which global warming is limited to 2 degrees Celsius; and (2) in their disclosures on talent strategy, provide information on long-

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[27] BlackRock, "Larry Fink's 2021 Letter to CEOs" (2021), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[28] United Nations Framework Convention on Climate Change, "NDC Synthesis Report" (Feb. 2021), available at https://unfccc.int/documents/268571.

term plans to improve diversity, equity, and inclusion, suited by region.[29]

As the scientific, economic, and social imperative for ESG strategies has become more evident, so too has the need for more comparable, decision-useful information for both setting science-based targets for emissions reductions and reporting on the progress of ESG strategies.[30]

This recent emphasis on ESG factors reflects momentum that has been building for some time. Particularly gaining steam in 2018, several studies were published which demonstrated the shifting tides on ESG matters that we are witnessing today.[31]

A September 2018 Bank of America Merrill Lynch report found ESG issues to be increasingly important to investors. Noting the expansion of the bank's ESG work over the prior several years, the report provides that "ESG is too critical to ignore. Asset potential is substantial: we conservatively estimate that flows into ESG-type funds over the next few decades could be roughly equivalent to the size of the S&P 500 today."[32] This report draws a strong correlation between good environ-

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[29] BlackRock, "Larry Fink's 2021 Letter to CEOs" (2021), available at https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter.

[30] U.S. Chamber of Commerce Foundation, "Corporate Sustainability Reporting: Past, Present, Future" (Nov. 2018), at 5.

[31] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://www.sasb.org/wp-content/uploads/2019/08/SASB-Alliance-Whitepaper-121218b.pdf.

[32] Bank of America Merrill Lynch, "Environmental, Social & Governance (ESG): The ABCs of ESG" (Sept. 10, 2018), available at https://www.bofaml.com/content/dam/boamlimages/documents/articles/ID18_0970/abcs_of_esg.pdf.

mental scores and good corporate performance. The report cites a study of S&P 500 companies between 2005 and 2017 that found that those companies with high environmental scores outperformed companies that rated lower on environmental scores by as much as three percent per year.[33] The report concludes that "ESG is a better signal of earnings risk than any other metric we have found."[34]

A 2018 survey of institutional investors by Bloomberg and the Morgan Stanley Institute for Sustainable Investing reached a similar conclusion.[35] The survey included written questions and responses from 300 U.S. asset managers with at least $50 million in assets under management, along with verbal interviews with some participants. The report concludes that "sustainable investing has gone mainstream in the United States. Asset managers surveyed foresee a rosy outlook for both client demand and competitive returns, and will continue to build their sustainable investing capabilities and product portfolios in the coming years."[36] The participants shared the view that sustainable in-

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[33] Bank of America Merrill Lynch, "Environmental, Social & Governance (ESG): The ABCs of ESG" (Sept. 10, 2018), available at https://www.bofaml.com/content/dam/boamlimages/documents/articles/ID18_0970/abcs_of_esg.pdf.

[34] Bank of America Merrill Lynch, "Environmental, Social & Governance (ESG): The ABCs of ESG" (Sept. 10, 2018), available at https://www.bofaml.com/content/dam/boamlimages/documents/articles/ID18_0970/abcs_of_esg.pdf.

[35] Bloomberg and the Morgan Stanley Institute for Sustainable Investing, "Sustainable Signals: Growth and Opportunity in Asset Management" (Feb. 19, 2019), available at https://www.morganstanley.com/assets/pdfs/2415532_Sustainable _Signals_Asset_Manager_2019_L.pdf.

[36] Bloomberg and the Morgan Stanley Institute for Sustainable Investing, "Sustainable Signals: Growth and Opportunity in Asset Management" (Feb. 19, 2019), available at https://www.morganstanley.com/assets/pdfs/2415532_Sustainable_Signals_Asset_Manager_2019_L.pdf.

vesting is "here to stay," with 89 percent indicating that it is a permanent feature of the investment landscape and 63 percent projecting growth in sustainable investments among asset managers over the next five years.[37] Eighty-two percent of respondents saw strong ESG performance as a key to improved profitability and investment returns.[38]

A similar 2018 EY survey of 260 institutional investors revealed "notable consensus that ESG information is critical to investor decision-making."[39] This survey also found a positive trajectory of institutional investors' interest in ESG information: "ESG information plays an increasingly important role in the investment decision-making process," and nearly all respondents (96 percent) said that such information had played a pivotal role.[40] According to EY, the response to the survey represents a "dramatic increase from the 2017 survey."[41] Similarly, according to a 2019 Fidelity Analyst Survey, "over 70 percent report

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[37] Bloomberg and the Morgan Stanley Institute for Sustainable Investing, "Sustainable Signals: Growth and Opportunity in Asset Management" (Feb. 19, 2019), available at https://www.morganstanley.com/assets/pdfs/2415532_Sustainable_Signals_Asset_Manager_2019_L.pdf.

[38] Bloomberg and the Morgan Stanley Institute for Sustainable Investing, "Sustainable Signals: Growth and Opportunity in Asset Management" (Feb. 19, 2019), available at https://www.morganstanley.com/assets/pdfs/2415532_Sustainable_Signals_Asset_Manager_2019_L.pdf.

[39] EY, "Does Your Non-Financial Reporting Tell Your Value Creation Story?" available at https://www.ey.com/en_gl/assurance/does-nonfinancial reporting-tell-value-creation-story.

[40] EY, "Does Your Non-Financial Reporting Tell Your Value Creation Story?" available at https://www.ey.com/en_gl/assurance/does-nonfinancial reporting-tell-value-creation-story.

[41] EY, "Does Your Non-Financial Reporting Tell Your Value Creation Story?" available at https://www.ey.com/en_gl/assurance/does-nonfinancial reporting-tell-value-creation-story.

that firms are increasing their emphasis on ESG policies, up 12 percentage points on last year."[42]

A State Street Global Advisors survey of 475 global institutional investors in the U.S., Europe, and Asia, including some of the largest pension plans, endowments, and foundations, drew similar conclusions.[43] Eighty percent of those surveyed said they incorporate ESG in their investment strategies, and 68 percent indicated that integration of ESG has significantly improved returns.[44] Furthermore, 69 percent of respondents indicated that pursuing an ESG strategy has helped them manage volatility.[45] The survey pointed to not only risk mitigation as a reason for investors' focus on ESG factors, but also opportunities for value creation and the correlation between good ESG performance and good financial returns. According to the survey, "many investors believe that effective ESG management improves company performance by helping to identify reputa-

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[42] Fidelity International, "Sustainable Investing Report," available at http://www.fidelity.com.cn/zh-cn/pdf/2018-Sustainable-Investing-Report.pdf.

[43] State Street Global Advisors, ESG Institutional Investor Survey, "Performing for the Future: ESG's place in investment portfolios. Today and tomorrow" (2018), available at https://www.ssga.com/investment-topics/environmental-social-governance/2018/04/esg-institutional-investor-survey.pdf.

[44] State Street Global Advisors, ESG Institutional Investor Survey, "Performing for the Future: ESG's place in investment portfolios. Today and tomorrow" (2018), available at https://www.ssga.com/investment-topics/environmental-social-governance/2018/04/esg-institutional-investor-survey.pdf.

[45] State Street Global Advisors, ESG Institutional Investor Survey, "Performing for the Future: ESG's place in investment portfolios. Today and tomorrow" (2018), available at https://www.ssga.com/investment-topics/environmental-social-governance/2018/04/esg-institutional-investor-survey.pdf.

tional, operational and financial risks and create commercial opportunities."[46]

In January 2020, the CEO of State Street Global Advisors sent a letter to company boards articulating State Street's 2020 Proxy Voting Agenda.[47] The letter emphasizes, "[w]e believe that addressing material ESG issues is good business practice and essential to a company's long-term financial performance — a matter of value, not values." It finds that although many directors now recognize the importance of ESG issues, "fewer than 25% of the companies we've evaluated have meaningfully identified, incorporated and disclosed material ESG issues into their strategies."[48] Interestingly, the letter also notes that "some shareholder activists continue to focus on specific or narrow ESG issues in piecemeal fashion — often creating confusion for investors, boards and company leadership without fundamentally tackling the ESG issues material to long-term shareholder performance."[49]

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[46] State Street Global Advisors, ESG Institutional Investor Survey, "Performing for the Future: ESG's place in investment portfolios. Today and tomorrow" (2018), available at https://www.ssga.com/investment-topics/environmental-social-governance/2018/04/esg-institutional-investor-survey.pdf.

[47] State Street Global Advisors, "CEO's Letter on our 2020 Proxy Voting Agenda" (2020), available at https://www.ssga.com/us/en/individual/etfs/insights/informing-better-decisions-with-esg.

[48] State Street Global Advisors, "CEO's Letter on our 2020 Proxy Voting Agenda" (2020), available at https://www.ssga.com/us/en/individual/etfs/insights/informing-better-decisions-with-esg.

[49] State Street Global Advisors, "CEO's Letter on our 2020 Proxy Voting Agenda" (2020), available at https://www.ssga.com/us/en/individual/etfs/insights/informing-better-decisions-with-esg.

In order to address ESG in a more comprehensive manner, State Street launched its proprietary "R-Factor" (the "R" stands for Responsibility), "a transparent scoring system that measures the performance of a company's business operations and governance as it relates to financially material and sector-specific ESG issues." State Street announced that it "will take appropriate voting action" against directors at companies in the S&P 500, FTSE 350, and various other indices where those companies "are laggards based on their R-Factor scores and . . . cannot articulate how they plan to improve their score. Beginning in 2022, we will expand our voting action to include those companies [that] have been consistently underperforming their peers on their R-Factor scores for multiple years, unless we see meaningful change."[50]

State Street believes that directors have a significant role to play in promoting action on ESG issues, so it provides an ESG oversight framework for directors.[51] The framework adapts current board oversight practices to ESG, and advocates that some ESG issues "be evaluated using scenario planning tools, the outputs of which should inform the company's long-term strategy."[52] In addition, financially material ESG issues, "if not managed and overseen appropriately, can negatively impact

[50] State Street Global Advisors, "CEO's Letter on our 2020 Proxy Voting Agenda" (2020), available at https://www.ssga.com/us/en/individual/etfs/insights/informing-better-decisions-with-esg.

[51] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

[52] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

company performance."[53] State Street provides a five-step roadmap to assist boards of directors in approaching and overseeing ESG issues. First, management should obtain the company's R-Factor score from State Street.[54] Second, management should determine the company's financially material ESG issues by becoming familiar with the financially material ESG issues facing the industry and other ESG issues applicable to the company's business.[55] Third, management should prioritize ESG issues on the board agenda.[56] Fourth, management should request and review periodic reporting of financially material ESG information.[57] And fifth, management should set goals and align management incentives appropriately, and communicate with investors about ESG issues.[58] Boards ultimately will bear responsibility for ensuring that management commits to these practices.

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[53] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

[54] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

[55] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

[56] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

[57] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

[58] State Street Global Advisors, "ESG Oversight Framework for Directors" (2020), available at https://www.ssga.com/library-content/pdfs/insights/esg-oversight-framework.pdf.

PART II.
CURRENT ESG DISCLOSURE

§ 4:6 Materiality

Naturally, the starting point for any discussion of the information that must be disclosed under the U.S. securities laws is materiality. The black letter definition of "materiality" as set forth by the U.S. Supreme Court in *TSC Industries v. Northway* provides the framework: "There must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information available."[1] Phrased differently, there must be "a substantial likelihood that a reasonable shareholder would consider (the omitted information) important in deciding how to vote."

The discussion of ESG issues poses the question of who the "reasonable investor" or "reasonable shareholder" is. Some years ago, activist groups raised their hands to request enhanced disclosures of environmental and social information — but those groups were not generally considered representative of the reasonable investor. If the information requested was not tied to the creation of financial value for shareholders, then it was not, as a rule, thought to be material. Times have changed, and ESG information is now important to mainstream investors. In a SustainAbility global survey of 500 investors from 17 firms conducted in 2020, 95 percent said they use ESG ratings, and 65 percent said they use them on a weekly basis.[2] Over $20 trillion in AUM is estimated to be ESG investing, representing around a quarter of all professionally managed assets around the

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[1] TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976).

[2] SustainAbility Institute, "Rate the Raters 2020," available at https://www.sustainability.com/thinking/rate-the-raters-2020/.

world.[3] FTSE Russell found that more than seven in 10 asset owners globally were evaluating and implementing sustainable investment considerations in their investment strategies in 2020.[4] BlackRock reported in 2019 that assets in sustainable mutual funds and exchange-traded funds in Europe and the United States amount to $760 billion.[5] If more than seven in 10 sophisticated asset owners are using ESG considerations and billions have been invested, nothing more needs to be said when asking if this is material information.

In many circumstances, ESG information is commonly accepted as material. Nonetheless, not all ESG information is material, nor should the range and scope of ESG information that some investors are requesting from companies necessarily be considered material. The determination as to what information is material to any particular company requires an analysis of the information and its specific relevance to that company and its prospects.

Issuers need to evaluate which ESG data are most significant for their companies. As noted below, companies complain that they are suffering from questionnaire fatigue, and investors say they are frustrated by the proliferation of information that is of little relevance. Key to bridging this divide is companies evaluating and discussing the ESG information that is most important to their performance now and in the future. A McKinsey survey of 107 executives and investors in 2019 found that investors

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[3] https://www.forbes.com/sites/georgkell/2018/07/11/the-remarkable-rise-of-esg/?sh=1adb94ed1695.

[4] https://www.ftserussell.com/press/global-rise-asset-owners-using-smart-beta-indexes-basis-sustainable-investment-strategies.

[5] BlackRock, "Sustainability: The Future of Investing," available at https://www.blackrock.com/us/individual/insights/blackrock-investment-institute/sustainability-the-future-of-investing, at 4.

cannot readily use companies' sustainability disclosures to inform investment decisions and advice accurately because of a lack of standardization and systematic data about what they consider material.[6] The SASB notes that "a given sustainability factor will not be financially material for all companies, and when it is material, it will manifest in unique ways from one industry to the next, thus requiring performance metrics tailored to the specific impact."[7] Due to the bespoke nature of sustainability risks, the SASB emphasizes that each company must make the materiality determination based on its own facts and circumstances.

The SASB roundtable highlights some corporate squeamishness over use of the word "materiality" (termed "the M word" in the roundtable report). The concern might stem in part from definitions of materiality that have emerged in the sustainability reporting world that differ from the definition in the financial world. Most companies issue sustainability reports separate and apart from their financial reports. Many include in those reports a "materiality matrix" that presents sustainability factors of significance to a variety of the companies' stakeholders. Global Reporting Initiative (GRI) developed one method for determining what information is material: the "GRI materiality process guides companies in how to identify their major sustainability impacts, and then enter into a dialogue with key stakeholders — which they define themselves — to answer the question '[w]hat

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[6] McKinsey, "More than values: The value-based sustainability reporting that investors want," available at https://www.mckinsey.com/business-functions/sustainability/our-insights/more-than-values-the-value-based-sustainability-reporting-that-investors-want.

[7] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esg data/, at 18.

are the material aspects, and to whom?' Each company designs its unique process as a reflection of its needs and in the context of its business model and sustainability strategy."[8] This definition of materiality differs from that applied under the U.S. securities laws, and this difference can lead to confusion and concern about what information is financially material and therefore subject to disclosure in financial reports versus information considered material under the GRI definition. Indeed, the GRI notes that the definition of materiality in the context of sustainability reporting is broader than that for financial reporting and therefore could well capture a broader universe of information than that which is required to be disclosed in SEC filings. "The materiality focus of sustainability reports is broader than the traditional measures of financial materiality," the GRI reports. "In financial reporting, materiality is commonly thought of as a threshold for influencing the economic decisions of those using an organization's financial statements — investors in particular. Materiality in sustainability reporting is not limited to those sustainability topics that have a significant financial impact."[9] The potential for confusion between financial materiality and the broader materiality in the context of sustainability reports has led to concern among companies. As one SASB roundtable participant notes with regard to her company's sustainability report: "We've been told by our legal team to reserve that term (materiality) for financial filings."[10]

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[8] Global Reporting Initiative, "Defining What Matters: Do Companies and Investors Agree on What Is Material?" (2016), available at https://www.globalreporting.org/resourcelibrary/GRI-DefiningMateriality2016.pdf.

[9] Global Reporting Initiative, "Materiality: What Topics Should Organizations Include in Their Reports?" (draft report), available at https://www.globalreporting.org/SiteCollectionDocuments/Materiality.pdf.

[10] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at

Inherent in the discussion of materiality is the idea that the information that is important to investors evolves over time. Indeed, we are undergoing a period of change and investors' informational needs are changing, meaning the concept of what information is material and therefore subject to the disclosure requirements of the U.S. securities laws should be expected to evolve as a result.[11] What matters to a reasonable investor can change rapidly in the short term. For instance, when the #MeToo movement gained prominence, "gender lens" investments grew to $2.4bn in assets under management by 2018.[12]

In an interesting first, Yum! Brands became the first U.S. company to agree to "double materiality" disclosure in 2022 after an activist non-profit organization, The Shareholder Commons (TSC) submitted a shareholder proposal asking that the company disclose a study detailing "the external environmental and public health costs created by the use of antibiotics in the supply chain of [the] company . . . and the manner in

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https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esgdata/, at 18.

[11] Indeed, companies' definition of their broad purpose is evolving as well. The Business Roundtable issued a statement in August 2019 defining the "Purpose of a Corporation." This statement embraces a purpose that is expansive and inclusive and that goes beyond the corporation's traditional mission of enhancing long-term shareholder value. The Business Roundtable's statement articulates its commitment to all stakeholders, including customers, employees, suppliers, and communities. The statement expresses the Business Roundtable's commitment to protecting the environment and embracing sustainability as part of the purpose of the corporation. Business Roundtable, "Statement on the Purpose of a Corporation" (Aug. 19, 2019), available at https://opportunity.businessroundtable.org/ourcommitment/.

[12] Sarah Murray, "Measuring What Matters: the Scramble to Set Standards for Sustainable Business," (May 14, 2021), The Financial Times, available at https://www.ft.com/content/92915630-c110-4364-86ee-0f6f018cba90.

which such costs affect the vast majority of its shareholders who rely on a health stock market."[13] TSC withdrew this proposal after Yum! agreed it would:

> (1) Study and disclose the system-wide costs of antimicrobial resistance (AMR) into its public sustainability reporting; (2) disclose findings regarding how antibiotic use in animal husbandry threatens global health and well-being, the global economy and diversified shareholder interests; (3) discuss a global scenario in which the food industry eliminates or internalizes AMR costs while addressing the competitive concerns that would impede such progress; and (4) describe how its policies and procedures and strategies for political influence affect the realization of the global scenario.[14]

While the concept of materiality is traditionally understood as factors that have financial impact on a company, "double materiality" and "dynamic materiality" add additional elements to the understanding. Double materiality takes into account both financial materiality (the ESG matters that would impact a company's financial performance) as well as impact materiality (the ESG matters that reflect a company's impact on the environment and people). Impact materiality works for stakeholders like consumers, citizens, and employees to understand a company's ESG-related impact. Dynamic materiality goes one step further, taking into account both financial materiality and im-

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[13] YUM! Brands, Inc: Rule 14a-8 Proposal, December 3, 2020 available at https://theshareholdercommons.com/wp-content/uploads/2021/02/YUM-Proposal-ED-AMR.pdf.

[14] The Shareholder Commons, "The Shareholder Commons Announces Withdrawal of Shareholder Proposal after Yum! Brands Commits to Disclose Systemic Costs of Antibiotic Use" (May 2021) available at https://www.prnewswire.com/news-releases/the-shareholder-commons-announces-withdrawal-of-shareholder-proposal-after-yum-brands-commits-to-disclose-systemic-costs-of-antibiotic-use-301239878.html.

pact materiality, but also financial reporting. It reflects all sustainability matters affected by or having an effect on the company. Materiality of information can shift over time, for instance if a company's impact on the climate becomes financially material.

§ 4:7 Analyst interest in ESG

Some stakeholders in the ESG space note that financial analysts appear not to be asking about sustainability disclosures on quarterly earnings calls, which seems to point to a misalignment between the financial analysts covering the quarterly earnings calls[1] and the broader investor community calling for greater disclosure of ESG factors.

One theory is that, to the extent analysts are not focused on sustainability concerns, it is because these issues are perceived to have a longer time horizon than the quarterly financial information that is the focus of the calls.[2] Sustainability issues are believed to pose risks that are understood to be significant, but might not be realized for some time, and the impacts are perhaps difficult to anticipate. As such, they don't necessarily garner the attention of analysts on quarterly calls. Furthermore, some question whether risks with a long-time horizon of perhaps five or 10 years should be considered material or, at least

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[1] SASB, Harvard Law School, "Legal Roundtable on Emerging Issues Related to Sustainability Disclosure" (Nov. 2017), available at http://www.sasb.org/wp-content/uploads/2017/12/LegalRoundtable-Paper-web.pdf.

[2] SASB, Harvard Law School, "Legal Roundtable on Emerging Issues Related to Sustainability Disclosure" (Nov. 2017), available at http://www.sasb.org/wp-content/uploads/2017/12/LegalRoundtable-Paper-web.pdf, at p.4.

from a civil liability perspective, whether their omission would be actionable.[3] That said, the idea that climate risks involve long-time horizons is not universally accepted. Indeed, the TCFD 2019 Status Report cautioned against assuming that all climate-related risks are temporally remote: "Many companies incorrectly view the implications of climate change to be relevant only in the long term and, therefore, not necessarily relevant to decisions made today. Those views, however, have begun to change."[4] A Bank of America Merrill Lynch report drew a similar conclusion, reporting that "whereas last year, ESG was more popular with long-term investors, this year, use broadened out to clients with shorter time horizons."[5]

A chicken and egg issue may also be at play. If analysts are reticent about ESG issues on quarterly earnings calls, does that cause those preparing the financial reports to pay less attention to sustainability issues than many investors might like? As one Harvard legal roundtable participant postulated, "Investors may be looking for sustainability information . . . but the people in companies who are preparing information for disclosure are not hearing it."[6] Others suggested that the chicken and egg issue

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[3] SASB, Harvard Law School, "Legal Roundtable on Emerging Issues Related to Sustainability Disclosure" (Nov. 2017), available at http://www.sasb.org/wp-content/uploads/2017/12/LegalRoundtable-Paper-web.pdf.

[4] 2019 Status Report, Task Force on Climate-Related Financial Disclosures (June 2019), available at https://www.fsb-tcfd.org/publications/tcfd 2019-status-report/, at ii.

[5] Bank of America Merrill Lynch, "Environmental, Social & Governance (ESG): The ABCs of ESG" (Sept. 10, 2018), available at https://www .bofaml.com/content/dam/boamlimages/documents/articles/ID18_0970/abcs _of_esg.pdf, at 8.

[6] SASB, Harvard Law School, "Legal Roundtable on Emerging Issues Related to Sustainability Disclosure" (Nov. 2017), available at http://

goes further. Analysts might not be asking probing questions about sustainability issues because they might not yet have a sense for how those issues are likely to impact the companies' financial results. Until there is more widespread disclosure of companies' sustainability risks within an industry, analysts might not have the information they need to ask the right questions. According to the Harvard legal roundtable, "Disclosure of sustainability information may not be useful to investors and analysts until they better understand it, but they cannot develop their understanding until the information is being widely disclosed."[7]

Conversely, the Goldman Sachs equity report suggests that the tides are shifting and that ESG issues are making their way onto quarterly earnings calls: "A common refrain from investors has been that companies rarely if ever talk about ESG topics on earnings calls. The evidence below shows that this is changing in significant ways."[8] A GS Data Works review of transcripts of quarterly earnings calls for the S&P 500 from 2000 through 2017 found a 75 percent increase in the number of companies discussing environmental and social issues on earnings calls. By the end of 2017, 230 companies (nearly half of the S&P 500)

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www.sasb.org/wp-content/uploads/2017/12/LegalRoundtable-Paper-web.pdf, at 4.

[7] SASB, Harvard Law School, "Legal Roundtable on Emerging Issues Related to Sustainability Disclosure" (Nov. 2017), available at http://www.sasb.org/wp-content/uploads/2017/12/LegalRoundtable-Paper-web.pdf, at 4.

[8] Derek R. Bingham et al., "A Revolution Rising — From Low Chatter to Loud Roar [Redacted]," Goldman Sachs Equity Research (Apr. 23, 2018), available at https://www.goldmansachs.com/insights/pages/new-energy-landscape-folder/esg-revolution-rising/report.pdf, at 4.

discussed environmental and social issues on their quarterly earnings calls.[9]

That momentum has continued into 2021, according to investment management firm, Pimco, which found that ESG mentions on corporate earnings calls have sharply increased in 2021.[10] Pimco's recent report analyzed earning call transcripts of about 10,000 global companies between May 2005 and May 2021. Their findings show that ESG mentions took place on only 0 percent to 1 percent of calls between 2005-2018. Mentions rose to 5 percent in 2019 and to 19 percent by May 2021.[11]

As further evidence of this shifting tide, a study conducted by the Center for Sustainable Business at the NYU Stern School of Business found that some companies have begun holding ESG-focused calls with investors and analysts.[12] These calls might follow the issuance of companies' sustainability reports or other ESG disclosures. And some companies are starting to build ESG discussions into their quarterly calls with analysts. By and large, however, the NYU study found that certain barri-

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[9] Derek R. Bingham et al., "A Revolution Rising — From Low Chatter to Loud Roar [Redacted]," Goldman Sachs Equity Research (Apr. 23, 2018), available at https://www.goldmansachs.com/insights/pages/new-energy-landscape-folder/esg-revolution-rising/report.pdf, at 4.

[10] Pimco, "Mid-Cycle Investing: Time to Get Selective" (July 2021), available at https://www.pimco.com/en-us/insights/economic-and-market-commentary/global-markets/asset-allocation-outlook/mid-cycle-investing-time-to-get-selective/.

[11] Pimco, "Mid-Cycle Investing: Time to Get Selective" (July 2021), available at https://www.pimco.com/en-us/insights/economic-and-market-commentary/global-markets/asset-allocation-outlook/mid-cycle-investing-time-to-get-selective/.

[12] "ESG and the Earnings Call," Harvard Law School Forum on Corporate Governance (June 17, 2020), available at https://corpgov.law.harvard.edu/2020/06/17/esg-and-the-earnings-call/.

ers interfere with broader discussion of ESG factors on quarterly earnings calls. These include a lack of knowledge about ESG factors on the part of many sell-side analysts covering companies; a limited supply of ESG information by companies; and a tension between the short-time horizon typically covered on the calls and the long-time horizons on which ESG data typically are reported.[13] Further, a focus on qualitative ESG information and a lack of uniform, quantitative disclosures of ESG information might prevent analysts from incorporating ESG data in their financial models, which are a key concern of the analysts' calls.

[13] "ESG and the Earnings Call," Harvard Law School Forum on Corporate Governance (June 17, 2020), available at https://corpgov.law.harvard.edu/2020/06/17/esg-and-the-earnings-call/.

§ 4:8 ESG reporting lines within companies

While companies commit significant resources to sustainability efforts, those resources can reside in silos, separate from the groups that control the financial reporting function, such as finance, accounting, legal, risk management, and investor relations. Such silos can potentially cause companies to fail to develop a thorough understanding of how sustainability risks might impact their financial results — which can lead to a failure to explain those risks in their financial reports. Alan Beller, former director of the SEC's Division of Corporation Finance, indicated during a SASB symposium that poor communication across functions within some companies could be impairing the disclosure process. "I don't think companies are doing as good a job as they should in vetting and coordinating across their organizations the information they're putting in those sustainability questionnaires," he said. "All too often, when I've asked disclosure lawyers at various companies for their views on

sustainability matters, the response has been something like 'Oh, that's not material.' . . . And if you then ask them, 'Well, what's in your sustainability questionnaires?,' they look at you with a blank stare and say, 'We have no idea.'"[1]

Sustainability issues have seen a rapid emergence as a key concern over the past several years, though some companies have indicated that it will take time to integrate ESG issues into their core decision-making processes. According to the Harvard legal roundtable, "Adapting to a new reality, in which sustainability is wholly integrated into a firm's strategy, operations, and reporting processes — not to mention its organizational structure — necessarily involves a certain amount of time, effort and expense."[2] A participant in the SASB roundtable reinforced this idea. The process of verifying ESG information "involves many subject matter experts across her company who 'have full-time day jobs.'"[3] Furthermore, traditional positioning of sustainability or corporate social responsibility functions in many companies reinforces the silos. Sustainability in many companies historically has resided within the public relations group, which has focused on the concerns of stakeholders other than shareholders. That legacy positioning might still contribute to the segregation of sustainability from the core business and financial operations of some companies.

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[1] The SEC and Improving Sustainability Reporting: SASB 2016 Symposium," Journal of Applied Corporate Finance, Vol. 29, No. 2 (Dec. 1, 2016).

[2] SASB, Harvard Law School, "Legal Roundtable on Emerging Issues Related to Sustainability Disclosure" (Nov. 2017), available at http://www.sasb.org/wp-content/uploads/2017/12/LegalRoundtable-Paper-web.pdf, at 5.

[3] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esg-data/, at 8.

A recent survey of corporate ESG disclosure from the Yale Initiative on Sustainable Finance in their 2020 white paper, finds that the production of ESG disclosures has become a cross-functional effort, with on average four corporate offices or functions involved at each stage of the process, with 2.5 involved for companies with less than 50 employees.[4] The survey queried over 100 corporate offices including Chief Sustainability Officers, Chief Legal Officers, investor relation staff, and strategy executives from over 20 industries and found that three business functions are consistently involved in the ESG disclosure process: Sustainability Departments; Investor Relations; and General Counsel.[5] "These teams lead the discussions regarding the selection and the release of the information while operational teams handle the collection of the data," according to their analysis. The report continues, "Perhaps not surprisingly, the Sustainability Department often serves as the "conductor" of the effort to produce sustainability data within the company – organizing and scheduling the involvement of other corporate officials and functions."[6]

One potential cause for lack of effective communication of ESG within some companies is the lack of consistent vocabu-

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[4] Yale Initiative on Sustainable Finance, "Toward Enhanced Sustainability Disclosure: Identifying Obstacles to Broader and More Actionable ESG Reporting," (Sept. 2020) available at https://pages.fiscalnote.com/rs/109-ILL-989/images/YISF%20ESG%20Reporting%20White%20Paper.pdf.

[5] Yale Initiative on Sustainable Finance, "Toward Enhanced Sustainability Disclosure: Identifying Obstacles to Broader and More Actionable ESG Reporting," (Sept. 2020) available at https://pages.fiscalnote.com/rs/109-ILL-989/images/YISF%20ESG%20Reporting%20White%20Paper.pdf.

[6] Yale Initiative on Sustainable Finance, "Toward Enhanced Sustainability Disclosure: Identifying Obstacles to Broader and More Actionable ESG Reporting," (Sept. 2020) available at https://pages.fiscalnote.com/rs/109-ILL-989/images/YISF%20ESG%20Reporting%20White%20Paper.pdf.

lary, or a "common language" in which to discuss ESG issues. The SASB roundtable emphasized the importance of fostering a productive discussion of ESG issues both within companies and between companies and investors. And in order for those discussions to be productive, the parties must speak in a common language. The roundtable participants "agreed that collaboration is key, so an important next step is overcoming language barriers within companies (e.g., between sustainability and finance), between companies and their investors (e.g., earnings calls, investor relations, etc.), and in markets more broadly."[7] Others cautioned, however, that "speaking the same language is particularly challenging when sustainability is the domain of a separate department that isn't today embedded in core business functions such as finance, operations, or risk management. . . . Establishing strong cross-departmental relationships can foster mutual respect and help bridge the communication gap."[8] Another participant agreed that embedding sustainability in the core functions of the company is critically important if companies are to move beyond "checking the box" on sustainability issues, and stressed the importance of senior-level support to establish a corporate commitment to including sustainability factors as a core concern.

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[7] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esgdata/, at 1.

[8] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esg-data/, at 13.

§ 4:9 Private sector questionnaires and voluntary disclosure standards

The apparent disconnect between investor demand for sustainability information and companies' disclosures in their financial reports has given rise to a proliferation of private sector questionnaires and voluntary reporting frameworks. The U.S. Chamber of Commerce report indicates that some companies have been asked to complete more than 250 surveys related to their ESG performance, saying:[1] "This has left many issuers 'dazed and confused' and has required them to dedicate entire teams of employees to filling out surveys or responding to third parties about ESG matters."[2]

Respondents to a 2020 Yale Initiative on Sustainable Finance survey also report "incoming requests from other stakeholders, ESG rating firms, NGOs, and others interested in sustainability performance" as a top factor affecting the production and release of ESG information.[3]

One Harvard legal roundtable participant noted that companies might be spending millions of dollars completing extensive questionnaires. It is not entirely clear, however, that the information produced is useful to investors. According to the roundtable: "Because many of these initiatives appeal to a broad

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[1] U.S. Chamber of Commerce Foundation, "Corporate Sustainability Reporting: Past, Present, Future" (Nov. 2018), at 29.

[2] U.S. Chamber of Commerce Foundation, "Corporate Sustainability Reporting: Past, Present, Future" (Nov. 2018).

[3] Yale Initiative on Sustainable Finance, "Toward Enhanced Sustainability Disclosure: Identifying Obstacles to Broader and More Actionable ESG Reporting," White Paper (Sept. 2020) available at https://pages.fiscalnote.com/rs/109-ILL-989/images/YISF%20ESG%20Reporting%20White%20Paper.pdf.

group of stakeholders (including NGOs, employees, customers, communities, and others), they lack the focus of mandatory public filings, which are guided by an investor-centric conception of materiality. As a result, such reports cast a very wide net, capturing dozens or, in many cases, hundreds of data points covering a wide swath of subjects, many of which may not be relevant to a company's business or to its investors."[4] The legal roundtable participants expressed concern that some companies are spending significant sums to provide sustainability information to stakeholders, but without rigorously assessing which part of the information is material to the company's business. As such, that information's value to investors may be diminished. In discussing how companies might sift through the sustainability data to determine what information to disclose to investors in their financial reports, one person noted the importance of tying the information to economic value. For risks that involve medium-to-long-term impacts and data whose impact is not immediately apparent, it is all the more important for companies to understand and explain how these factors affect their economic value.

The U.S. Chamber of Commerce report reveals companies' concern over the proliferation of standard-setting bodies, which have developed different recommendations as to the ESG disclosures companies should make. These recommendations have been criticized in some instances for creating more uncertainty than clarity. According to the report, "[t]he vast differences in approaches these standard setters take has created a great deal of uncertainty for companies regarding what they are expected

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[4] SASB, Harvard Law School, "Legal Roundtable on Emerging Issues Related to Sustainability Disclosure" (Nov. 2017), available at http://www.sasb.org/wp-content/uploads/2017/12/LegalRoundtable-Paper-web.pdf, at 7.

to disclose."[5] Further, the report finds that the emergence of for-profit ratings services that summarize and compare companies' ESG performance is not altogether helpful. These services, the report concludes, "do not employ any type of standardized metrics or methodologies, provide varying levels of transparency with respect to their rating methodologies, and often arrive at very different opinions regarding a company's ESG performance."[6] The State Street Global Advisors survey similarly finds, "a range of challenges that can inhibit investors' capacity to embrace ESG investing more fully. Issues around metrics and a lack of standardized performance measures can lead to confusing and contradictory results and prove particularly concerning."[7] Notably, sustainability ratings services are not universally criticized. These ratings are perceived by some to offer a valuable service to investors. "For investors, asset managers and consultants, sustainability/ESG scores (provided by sustainability rating services) allow for a quick assessment of how well a company is run. Such scores can also forecast potential risks or untapped opportunity."[8]

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[5] U.S. Chamber of Commerce Foundation, "Corporate Sustainability Reporting: Past, Present, Future" (Nov. 2018), at 3.

[6] U.S. Chamber of Commerce Foundation, "Corporate Sustainability Reporting: Past, Present, Future" (Nov. 2018).

[7] State Street Global Advisors, ESG Institutional Investor Survey, "Performing for the Future: ESG's place in investment portfolios. Today and tomorrow" (2018), available at https://www.ssga.com/investment-topics/environmental-social-governance/2018/04/esg-institutional-investor-survey.pdf, at 4.

[8] Silda Wall Spitzer and John Mandyck, "What Boards Need to Know About Sustainability Ratings," Harvard Business Review (May 30, 2019), available at https://hbr.org/2019/05/what-boards-need-to-know-about-sustainability-ratings.

The SASB roundtable participants concluded that confusion around the different standards can cause companies and investors to "talk past each other." "Coupled with the rapid pace of change, this profusion of initiatives — the 'alphabet soup,' as several participants called it — has created confusion in the marketplace that has neither benefited from nor facilitated a well-established, commonly accepted set of best practices," the SASB reports. "The result, attendees noted, has been a communication gap between companies and their investors. As one participant commented, 'They are talking past each other.'"[9]

The 2018 survey of institutional investors by Bloomberg and the Morgan Stanley Institute for Sustainable Investing draws the same conclusion: "There remains significant confusion around definitions of sustainable investing and approaches to measuring social and environmental impact. While existing efforts such as the SASB guidance continue to gain traction, no single set of metrics has fully addressed the need for comparable, high-quality ESG data. Industry engagement in efforts to create a common language of sustainability and impact remains paramount to overcoming this challenge."[10]

Similarly, a 2020 study of corporate issuers' ESG disclosure processes conducted by the Yale Initiative on Sustainable Finance study found "the proliferation of different reporting frameworks has in some cases brought confusion and uncertainty to the reporting process as companies grapple with which

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[9] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esgdata/, at 2.

[10] Bloomberg and the Morgan Stanley Institute for Sustainable Investing, "Sustainable Signals: Growth and Opportunity in Asset Management" (Feb. 19, 2019), available at https://www.morganstanley.com/assets/pdfs/2415532_Sustainable_Signals_Asset_Manager_2019_L.pdf, at p.14.

reporting frameworks to follow."[11] The respondents of the 2020 survey found these frameworks and surveys to be overwhelming the disclosure process. "About 40% spontaneously raised the proliferation of frameworks and surveys as affecting ESG disclosures – echoing the "reporting fatigue" expressed by respondents in the interviews. Others complained about the divergent requirements across ESG reporting platforms."[12]

This is not to say that the voluntary sustainability reporting frameworks are not helpful to some. Indeed, the Conference Board has emphasized that "voluntary reporting frameworks, such as the (Global Reporting Initiative) Standards, play an important role in helping companies navigate non-financial disclosure."[13] However, "check the box" exercises are thought to be less useful than disclosures that focus on the factors that are material to the particular company: "Non-financial disclosure alone does not necessarily translate into better sustainability performance as companies tick the boxes without tipping the scales . . . Existing reporting requirements are more effective

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[11] Yale Initiative on Sustainable Finance, "Toward Enhanced Sustainability Disclosure: Identifying Obstacles to Broader and More Actionable ESG Reporting" forthcoming White Paper (Sept. 2020).

[12] Yale Initiative on Sustainable Finance, "Toward Enhanced Sustainability Disclosure: Identifying Obstacles to Broader and More Actionable ESG Reporting," White Paper (Sep. 2020) available at https://pages.fiscalnote.com/rs/109-ILL-989/images/YISF%20ESG%20Reporting%20White%20Paper.pdf.

[13] Thomas Singer, Ajuj Saush, and Anke Schrader, "Sustainability Practices 2018 Edition: Trends in Corporate Sustainability Reporting in North America, Europe, and Asia-Pacific" The Conference Board, available at https://www.conference-board.org/sustainability-practices/.

when they include due diligence mechanisms to achieve not only greater disclosure but also performance improvements."[14]

[14] Thomas Singer, Ajuj Saush, and Anke Schrader, "Sustainability Practices 2018 Edition: Trends in Corporate Sustainability Reporting in North America, Europe, and Asia-Pacific" The Conference Board, available at https://www.conference-board.org/sustainability-practices/, at 5.

§ 4:10 Information misalignment

A number of market participants have noted the disconnect between the data that companies are providing and the information that many investors would find useful. The Director of Sustainability Insights for Generation Investment Management explained the challenge in a report on ESG data: "[C]overage remains patchy. Data are only currently available for some metrics, for some firms in some geographies. Indicators for social issues are relatively weak, at a time when societal challenges have never been higher on the agenda. The risk is that ESG data put a spotlight on what is available, rather than what is most important."[1] Further, the Generation report notes that "sustainability discussions focus on the need for transformation and unprecedented shifts in the way that companies operate. We think there is a disconnect here. If it is to help guide transformations underway in the economy and society, ESG data will itself need to undergo a transformation."

The World Business Council for Sustainable Development (WBCSD) conducted a study that included a series of investor roundtables and interviews to gain a better understanding of the

[1] "The Future of ESG Data," Generation Investment Management LLP. (Dec. 5, 2019), available at https://www.generationim.com/researchcentre/insights/the-future-of-esg-data/.

information that investors want in order to properly incorporate companies' sustainability performance in their capital allocation decisions.[2] The WBCSD reports:

> There is a clear appetite from investors for information outside of the financial statements. The investors interviewed said it gives important context to the financial information and insight into the long-term viability of the company. But investors can be skeptical about its relevance and reliability. Over a series of interviews and roundtables, investors explained the challenges they face in using (non-financial information) — with many of these arising from the numerous reporting frameworks and initiatives in this area, the sheer volume of information reported and the perceived lack of high-quality, consistent and comparable information.[3]

The study participants indicated the factors that would enhance their confidence in and ability to use the information provided. Investors expressed their wish that companies more clearly identify and discuss the risks specifically impacting them. Further, they expressed a desire to discern whether companies have good governance and effective internal controls, not only over financial reporting, but also over non-financial factors such as ESG risks.[4] According to the WBCSD: "Investors want

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[2] Prof. Dr. Rodney Irwin, Alan McGill, "Enhancing the Credibility of Non-Financial Information, the Investor Perspective," WBCSD and PwC (Oct. 2018), available at https://docs.wbcsd.org/2018/10/WBCSD_Enhancing_Credibility_Report.pdf.

[3] Prof. Dr. Rodney Irwin, Alan McGill, "Enhancing the Credibility of Non-Financial Information, the Investor Perspective," WBCSD and PwC (Oct. 2018), available at https://docs.wbcsd.org/2018/10/WBCSD_Enhancing_Credibility_Report.pdf, at 2.

[4] Prof. Dr. Rodney Irwin, Alan McGill, "Enhancing the Credibility of Non-Financial Information, the Investor Perspective," WBCSD and PwC

companies to show how (non-financial information) is integrated in their strategic decision-making and are looking for material information to be underpinned by controls and processes on a par with those used for financial information."[5]

The study participants also articulated the difficulty of incorporating non-financial information in their valuation models. The investors interviewed for the study emphasized the importance of providing ESG metrics for comparability across companies and within companies over time. However, the metrics alone are of limited use without narrative discussions that explain how the data are relevant to companies' performance and outlook.[6]

In May 2021, the SASB responded positively to the SEC's request for input on climate change disclosure by supporting the move and highlighting that there is need for "more effective, standardized disclosure than existing [SEC] guidance has thus far elicited from registrants."[7] The SASB further argues that "a baseline of consistent, comparable, and reliable climate disclo-

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(Oct. 2018), available at https://docs.wbcsd.org/2018/10/WBCSD_Enhancing_Credibility_Report.pdf, at 2.

[5] Prof. Dr. Rodney Irwin, Alan McGill, "Enhancing the Credibility of Non-Financial Information, the Investor Perspective," WBCSD and PwC (Oct. 2018), available at https://docs.wbcsd.org/2018/10/WBCSD_Enhancing_Credibility_Report.pdf, at 2.

[6] Prof. Dr. Rodney Irwin, Alan McGill, "Enhancing the Credibility of Non-Financial Information, the Investor Perspective," WBCSD and PwC (Oct. 2018), available at https://docs.wbcsd.org/2018/10/WBCSD_Enhancing_Credibility_Report.pdf, at 7.

[7] SASB, SEC Climate Letter, available at https://www.sasb.org/wp-content/uploads/2021/05/SASB_SEC_Climate_Letter_2021-05-19_FINAL.pdf, at 1.

sure” is a necessary “market infrastructure.”[8] The SASB analyzed the effectiveness of sustainability disclosures in SEC filings in a 2017 report, in which it reviewed sustainability disclosures in hundreds of SEC filings across industries. Consistent with the other discussions noted above, the SASB report found that there is still significant work to be done toward making disclosures in SEC reports meaningful and useful to investors. In his foreword, Alan Beller declared: “On the one hand, it is heartening that companies increasingly recognize the risks and opportunities involved in managing material sustainability factors and the requirements . . . to disclose them in communications with investors. On the other, their communication to investors on these issues remains largely designed to address liability concerns, and are thus ineffective in providing meaningful and comparable information. So much work remains to be done.”[9] The report specifically found that most sustainability disclosures rarely include sustainability performance metrics and typically consist of boilerplate language “which is largely useless to investors.”[10]

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[8] SASB, SEC Climate Letter, available at https://www.sasb.org/wp-content/uploads/2021/05/SASB_SEC_Climate_Letter_2021-05-19_FINAL.pdf, at 1.

[9] Alan Beller (SASB Foundation Board of Directors and Former Director, Division of Corporation Finance, U.S. Securities and Exchange Commission), Foreword, “The State of Disclosure: An analysis of the effectiveness of sustainability disclosure in SEC filings 2017,” available at https://www.sasb.org/wp-content/uploads/2017/12/2017State-of-Disclosure-Report-web.pdf.

[10] Alan Beller (SASB Foundation Board of Directors and Former Director, Division of Corporation Finance, U.S. Securities and Exchange Commission), Foreword, “The State of Disclosure: An analysis of the effectiveness of sustainability disclosure in SEC filings 2017,” available at https://www.sasb.org/wp-content/uploads/2017/12/2017State-of-Disclosure-Report-web.pdf, at 2.

In the 2021 Morrow Sodali Institutional Investor Survey, 42 global institutional investors were asked what could be improved in terms of the climate-related disclosure of the companies in which they analyze. The top six responses were: clear connections to financial risks/opportunities; time horizons in relation to impact on strategy; disclosure on metrics, targets and achievements; board oversight and fluency on the topic; greater clarity to identify risks and opportunities; and better alignment with reporting standards.[11]

Of the reporting standards surveyed, "TCFD was overwhelmingly the most popular ESG reporting framework, followed by SASB and then in-house proprietary frameworks focused on material topics."[12]

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[11] Morrow Sodali, "Institutional Investor Survey 2021" available at https://higherlogicdownload.s3.amazonaws.com/GOVERNANCEPROFESSIONALS/a8892c7c-6297-4149-b9fc-378577d0b150/UploadedImages/Institutional_Investor_Survey_2021.pdf.

[12] Morrow Sodali, "Institutional Investor Survey 2021" available at https://higherlogicdownload.s3.amazonaws.com/GOVERNANCEPROFESSIONALS/a8892c7c-6297-4149-b9fc-378577d0b150/UploadedImages/Institutional_Investor_Survey_2021.pdf.

PART III.
CURRENT ESG REPORTING IN THE U.S.

§ 4:11 Current SEC reporting requirements and guidance

Regulation S-K[1] underpins the reporting obligations of the Securities Act and the Exchange Act and provides the basis for required disclosure of material ESG factors in registration

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[1] 17 CFR § 229.

statements and periodic reports.[2] Specifically, disclosure of material ESG factors might be required under: Item 101 of Regulation S-K — Description of Business;[3] Item 103 — Legal Proceedings;[4] Item 105 — Risk Factors;[5] and Item 303 — Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A).[6] Further, Securities Act Rule 408 and Exchange Act Rule 12b-20 require disclosure of such material information as is necessary to make the required disclosures not misleading, in light of the circumstances in which they are made.[7]

In 2010, the Commission issued guidance regarding disclosures related to climate change that continues to inform registrants' climate change disclosures under the U.S. securities laws (2010 Interpretive Release).[8] While the 2010 Interpretive Release contains guidance and examples specifically focused on climate change, its description of disclosure taxonomy applies equally to other ESG disclosures.

In August 2020, the Commission amended Items 101, 103, and 105 of Regulation S-K, which are the provisions relating to the description of a company's business, risk factors, and legal

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[2] Additionally, Regulation S-X governs the financial statement disclosure requirements. See 17 CFR § 229.

[3] 17 CFR § 229.101.

[4] 17 CFR § 229.103.

[5] 17 CFR § 229.105.

[6] 17 CFR § 229.303.

[7] 17 CFR § 230.408 and 17 CFR § 240.12b-20.

[8] Commission Guidance Regarding Disclosure Related to Climate Change, Sec. Act Release No. 9106 (Feb. 8, 2010).

proceedings.[9] The adopting release emphasized that the amendments were designed to ease compliance burdens for companies and improve disclosures for investors. The amendments were particularly notable for their failure to address requests from many investor groups and others for enhanced rules to define the ESG information that companies should disclose.[10] While the amendments do call for new disclosures relating to companies' human capital management, some critics maintain that the rules do not go far enough in that regard (especially as they do not address disclosures of gender, racial, and ethnic diversity among companies, their boards, and senior management). Moreover, the amendments fail to address climate change disclosures, and thereby drew sharp criticism from those who saw this as an opportunity to fill a regulatory hole that many had long hoped the Commission would address.

SEC Commissioner Allison Herren Lee expressed her dismay:

> The final rules today look largely like the proposal, ignoring both overwhelming investor comment and intervening events. We have declined to include even a discussion of climate risk in the release despite significant comment on this subject. And we have declined to go beyond merely

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[9] "Modernization of Regulation S-K Items 101, 103, and 105" Final Rule, Sec. Release Nos. 33-10825 and 34-89670 (Aug. 26, 2020), available at https://www.sec.gov/rules/final/2020/33-10825.pdf.

[10] "SEC Amendments to Regulation S-K Are Silent on ESG Disclosures," Latham & Watkins Global ELR Blog (Aug. 31, 2020), available at https://www.globalelr.com/2020/08/sec-amendments-to-regulation-s-k-are-silent-on-esg-disclosures/#_edn1.

introducing the topic of human capital generally, despite investors' views that this is not nearly enough.[11]

SEC Commissioner Caroline Crenshaw noted, "[T]he rule before us today fails to deal adequately with two significant modern issues affecting financial performance: climate change risk and human capital."[12]

Since the time of the Regulation S-K amendments, the Commission has experienced an administration change following the 2020 Presidential election and the swearing in of the SEC Chair Gensler, in April 2021. In Congressional testimony, Chair Gensler stated that he has asked the SEC Staff to develop proposals for the SEC's consideration relating to climate risk disclosures, which would be subject to public comment.[13]

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[11] "Regulation S-K and ESG Disclosures: An Unsustainable Silence," Statement of Commissioner Allison Herren Lee (Aug. 26, 2020), available at https://www.sec.gov/news/public-statement/lee-regulation-s-k-2020-08-26.

[12] "Statement on the 'Modernization' of Regulation S-K Items 101, 103, and 105," Statement of Commissioner Caroline Crenshaw (Aug. 26, 2020), available at https://www.sec.gov/news/public-statement/crenshaw-statement modernization-regulation-s-k.

[13] "Testimony Before the United States Senate Committee on Banking, Housing, and Urban Affairs," Testimony of Chair Gary Gensler (Sep. 14, 2021), available at https://www.sec.gov/news/testimony/gensler-2021-09-14.

§ 4:12 Item 101 of Regulation S-K: Description of business

The August 2020 amendments to Item 101(c) modified the disclosure provisions to clarify that the provisions related to regulatory compliance apply to any governmental regulations, and are not limited to environmental regulations. The amend-

ments further added a disclosure topic related to human capital management.

Item 101(c)(2)(i) (formerly Item 101(c)(1)(xii)) provides for disclosure of the "material effects that compliance with government regulations, including environmental regulations, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries, including the estimated capital expenditures for environmental control facilities for the current fiscal year and any other material subsequent period."[1] The Commission has not indicated that its 2010 disclosure guidance related to climate change (discussed below) is any less applicable to the revised provisions of Regulation S-K. The laws or regulations that could materially impact a registrant include those enacted by the federal government, the states, local municipalities, or foreign authorities. In the 2010 Interpretive Release, the Commission pointed to the then pending cap-and-trade bills before Congress and then pending EPA rules to regulate GHG emissions, as well as the Kyoto Protocol. The Commission noted that, while the U.S. had not ratified the Kyoto Protocol, it nonetheless could materially impact U.S. registrants with operations outside the U.S. that are subject to its standards.

New Item 101(c)(2)(ii) provides for "a description of the registrant's human capital resources, including the number of persons employed by the registrant, and any human capital measures or objectives that the registrant focuses on in managing the business (such as, depending on the nature of the registrant's business and workforce, measures or objectives that address the development, attraction and retention of personnel)." A consistent theme of the amendments to Regulation S-K is a move toward more principles-based disclosure provisions. The

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[1] 17 CFR § 229.101(c)(2)(i).

intent with regard to the new human capital disclosure provisions is no different. Former Chair Clayton, in his statement supporting the adoption of the new rules, emphasized that, "our rigorous, principles-based, flexible disclosure system, where companies are required to communicate regularly and consistently with market participants, provides countless benefits to our markets, our investors and our economy more generally."[2] With regard to the human capital disclosure provisions, Clayton noted, "Experience demonstrates that these metrics, including their construction and their use, [vary] widely from industry to industry and issuer to issuer, depending of a wide array of company-specific factors and strategic judgments. It would run counter to our proven disclosure system, particularly as we first increase regulatory emphasis in an area of such wide variance, for us to attempt to prescribe specific, rigid metrics that would not capture or effectively communicate these substantial differences. That said, under the principles-based approach, I do expect to see meaningful qualitative and quantitative disclosure, including, as appropriate, disclosure of metrics that companies actually use in managing their affairs."[3]

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[2] SEC Chair Jay Clayton, "Modernizing the Framework for Business, Legal Proceedings and Risk Factor Disclosures" (Aug. 26, 2020), available at https://www.sec.gov/news/public-statement/clayton-regulation-s-k-2020-0826.

[3] SEC Chair Jay Clayton, "Modernizing the Framework for Business, Legal Proceedings and Risk Factor Disclosures" (Aug. 26, 2020), available at https://www.sec.gov/news/public-statement/clayton-regulation-s-k-2020-0826.

§ 4:13 Item 103 of Regulation S-K: Legal proceedings

Item 103 requires the registrant to describe any material pending or contemplated legal proceedings to which the regis-

trant or any of its subsidiaries is a party or to which their property is subject. Pursuant to the August 2020 amendments, companies may provide this disclosure by hyperlink or cross-reference to legal proceedings disclosures elsewhere in the disclosure document. The requirement excludes routine litigation if the business ordinarily results in such claims, except for claims that depart from the norm. Pursuant to Item 103(c)(3), an administrative or judicial proceeding arising under any federal, state, or local provisions regulating the discharge of materials into the environment or principally for the purpose of protecting the environment are *not* "ordinary routine litigation incidental to the business."

Such proceedings must be described if: (a) any such proceeding (or combined proceedings if they present largely the same issues) is material to the business or financial condition of the registrant; (b) any such proceeding (or combined proceedings if they present largely the same issues) involves primarily a claim for damages, or involves potential monetary sanctions, capital expenditures, deferred charges, or charges to income and the amount involved exceeds ten percent of the registrant's and its consolidated subsidiaries' current assets; or (c) a governmental authority is a party to the proceeding and the proceeding involves potential monetary sanctions, unless the registrant reasonably believes that the proceeding will not in fact result in monetary sanctions, or if the monetary sanctions, exclusive of interest and costs, are expected to amount to less than $300,000 or, at the company's election, such other threshold as the company determines is material (provided such threshold does not exceed the lesser of $1 million or one percent of the company's and its consolidated subsidiaries' current assets). The August 2020 amendments modified Item 103 to raise the threshold from $100,000 and to give companies discretion to establish a higher threshold, based on their materiality assessment. The Division of Corporation Finance's Office of Chief Counsel has previously provided telephone guidance indicating that the reference in

Instruction 5 to an "administrative or judicial proceeding arising under 'local provisions' is sufficiently broad to require disclosure of environmental actions brought by a foreign government."[1]

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[1] SEC Division of Corporation Finance, Manual of Publicly Available Telephone Interpretations, Section I, Question #7, available at https://www.sec.gov/interps/telephone/cftelinterps_regs-k.pdf; See also Division of Corporation Finance Compliance and Disclosure Interpretation Question 105.02 (updated Feb. 6, 2019), available at https://www.sec.gov/divisions/corpfin/guidance/regs-kinterp.htm.

§ 4:14 Item 105 (formerly Item 503(c)) of Regulation S-K: Risk factors

The Commission recently moved the Risk Factor disclosure requirements from Item 503(c) to a new Item 105.[1] The amendment emphasized its principles-based approach that encourages companies to focus on the risks that are relevant to their own specific circumstances. Item 105 requires companies, when appropriate, to disclose under the caption "Risk Factors" a discussion of "the material factors that make an investment in the registrant or offering speculative or risky." Pursuant to the August 2020 amendments, the risk factors discussion should include headings, and each risk factor should be placed under a sub-caption that adequately describes the risk. Further, if the risk factors section exceeds 15 pages, the forepart of the disclosure document must include a series of concise bulleted or numbered statements (not to exceed two pages in total) that summarize the principal risk factors.

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[1] Sec. Act Release No. 10618 (Mar. 20, 2019), available at https://www.sec.gov/rules/final/2019/33-10618.pdf.

§ 4:15 Item 303 of Regulation S-K: MD&A

Item 303 requires registrants to discuss their financial condition, changes in financial condition, and results of operations, providing the information as specified in paragraphs 303(a)(1) through (5). These items address the registrant's: (1) liquidity; (2) capital resources; (3) results of operations; (4) off balance sheet arrangements; and (5) contractual arrangements. Registrants are also required to disclose such other information that they believe to be necessary to an understanding of their financial condition, changes in financial condition, and results of operations.[1]

In the 2010 Interpretive Release, the Commission reinforced its earlier guidance that explained the objectives of the MD&A disclosure requirements, which include:

- Providing a narrative explanation of a registrant's financial statements that enables investors to see the registrant through the eyes of management
- Enhancing the overall financial disclosure and provide the context within which financial information should be analyzed
- Providing information about the quality of, and potential variability of, a registrant's earnings and cash flow, so that investors can ascertain the likelihood that past performance is indicative of future performance[2]

The Commission emphasized the flexibility of its requirements in Item 303 and its objective that the disclosures "keep

[1] 17 CFR § 229.303.

[2] Sec. Act Release No. 9106 (Feb. 8, 2010), referencing earlier guidance provided in Sec. Act Release No. 8350 (Dec. 19, 2003), 68 FR 75055.

pace with the evolving nature of business trends without the need to continuously amend the text of the rule."[3] While certain provisions of Item 303 set forth specific disclosure requirements, others are principles-based and "require management to apply the principles in the context of the registrant's particular circumstances."[4] The disclosures should be clear and should identify management's view of the company's prospects and financial condition.

In this regard, registrants are required to disclose the "known trends, events, demands, commitments and uncertainties that are reasonably likely to have a material effect on financial condition or operating performance."[5] The Commission noted that it has not quantified any specific future time period that must be considered in evaluating the events that might have a material ef-

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[3] Sec. Act Release No. 9106 (Feb. 8, 2010), at 16.

[4] Sec. Act Release No. 9106 (Feb. 8, 2010), at 16.

[5] Sec. Act Release No. 9106 (Feb. 8, 2010), at 16. The release notes that the "reasonably likely" standard is a lower standard than "more likely than not," citing Sec. Act Release No. 8056 (Jan. 22, 2002), 67 FR 3746. It is a matter of unsettled law as to whether Item 303 creates a private right of action for non-disclosure of material known trends and uncertainties. The Second Circuit broke with prior law and held in Leidos, Inc. v. Indiana Public Retirement System that a registrant may be liable for securities fraud in a private action for omitting information required under Item 303, even if the omitted information is not necessary to make affirmative statements not misleading (i.e., even if the registrant has not previously spoken on the subject). Indiana Pub. Ret. Sys. v. SAIC, Inc., 818 F.3d 85 (2d Cir. 2016). The U.S. Supreme Court was poised to address the issue when the parties settled the case and the matter was removed from the Supreme Court's docket. The issue, as posed by the Court, was "[w]hether the Second Circuit erred in holding-in direct conflict with the decisions of the Third and Ninth Circuits that Item 303 of SEC Regulation S-K creates a duty to disclose that is actionable under Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5." See https://www.supremecourt.gov//docket/docketfiles/html/qp/16-00581qp.pdf.

fect on financial condition or operating performance. "As with any other judgment required by Item 303, the necessary time period will depend on a registrant's particular circumstances and the particular trend, event or uncertainty under consideration."[6]

When assessing the materiality of any specific information, the registrant should consider both the probability and the magnitude of the event, in light of the company's circumstances.[7] This two-part test requires the registrant to consider if the event is likely to materialize. If the event is unlikely to materialize, then no disclosure is required. If the registrant cannot determine that the event is unlikely to occur, then it must assess whether the event would have a material effect on the company's financial condition and results of operations if it were to occur. This materiality analysis is intended to focus the disclosures on matters that are of particular importance to the company and to cull less meaningful disclosures. "The effectiveness of MD&A decreases with the accumulation of unnecessary detail or duplicative or uninformative disclosure that obscures material information."[8]

In January 2020, the Commission proposed amendments to Item 303.[9] This release sought to modernize and simplify the disclosure requirements but did not address the requests from

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[6] Sec. Act Release No. 9106 (Feb. 8, 2010), at 17.

[7] Basic, Inc. v. Levinson, 485 U.S. 224 (1988).

[8] Sec. Act Release No. 9106 (Feb. 8, 2010), at 18, citing Sec. Act Release No. 8350 (Dec. 19, 2003), 68 FR 75055.

[9] SEC Proposed Rule, "Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information," Sec. Act Release Nos. 33-10750; 34-88093 (Jan. 30, 2020).

the commenters on the 2016 Concept Release and other market participants who have called for enhanced ESG disclosures.

Then-Chair Clayton noted the complexity and difficulty of regulating ESG disclosures. He stressed that "the landscape around these issues is, and I expect will continue to be, complex, uncertain, multi-national/jurisdictional and dynamic."[10] The Chair noted that he has been engaged in discussions with a variety of market participants as well as with his international counterparts on the issue of ESG disclosures. Commissioner Lee issued a statement expressing her disappointment that the Commission was not proposing amendments to the disclosure rules to address ESG issues. She said, "Today's proposal is most notable for what it does not do: make any attempt to address investors' need for standardized disclosure on climate change risk . . . investors are overwhelmingly telling us, through comment letters and petitions for rulemaking, that they need consistent, reliable, and comparable disclosures of the risks and opportunities related to sustainability measures, particularly climate risk."[11]

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[10] "Statement on Proposed Amendments to Modernize and Enhance Financial Disclosures; Other Ongoing Disclosure Modernization Initiatives; Impact of the Coronavirus; Environmental and Climate-Related Disclosure," SEC Chairman Jay Clayton (Jan. 30, 2020), available at https://www.sec.gov/news/public-statement/clayton-mda-2020-01-30.

[11] "'Modernizing' Regulation S-K: Ignoring the Elephant in the Room," SEC Commissioner Allison Herren Lee (Jan. 30, 2020), available at https://www.sec.gov/news/public-statement/lee-mda-2020-01-30.

§ 4:16 2010 Interpretive Release: Impact of legislation, regulation, and international accords

The 2010 Interpretive Release provides guidance on some of the ways in which climate change risks might require disclosure under the reporting provisions discussed above. The examples provided are illustrative and not necessarily exhaustive. While the SEC is expected to propose new rules regarding disclosures of climate-related risk in late 2021 or early 2022, in the absence of any additional regulatory guidance from the Commission, the 2010 Interpretive Release remains the principal source of direction from the Commission on climate-related disclosures.

Developments in foreign, federal, state, and local laws, rules, and regulations could trigger disclosure obligations under all of the provisions outlined above. The Commission identified some examples of pending legislation, including costs to purchase or benefits from selling carbon allowances pursuant to cap-and-trade systems; costs of improving facilities or equipment to reduce emissions in order to comply with regulatory limits on emissions; and financial impacts from increased or decreased demand for goods either directly due to regulatory changes or indirectly due to increases in costs of goods sold (e.g., due to the imposition of a carbon tax on certain products).

The Commission focused on regulations governing GHG emissions, specifically. Such regulations would require disclosure in the company's business description, pursuant to Item 101 of Regulation S-K if they would require the company to make material capital expenditures for environmental control facilities. If the laws or regulations led to material legal proceedings or threatened legal proceedings, they would trigger disclosure obligations under Item 103. Further, if the laws or regulations presented material risks for the registrant specific to the company and not merely generic risks applicable to all registrants, then risk factor disclosure would be required pursuant

to Item 105. Finally, the Commission urged registrants to assess whether the laws or regulations are reasonably likely to have a material effect on the company's financial condition or results of operation, which would require MD&A disclosure under Item 303.

The Commission pointed out that companies should consider competitive benefits and other positive effects of new laws or rules as well as their negative effects. A registrant "should not limit its evaluation of disclosure of proposed laws only to negative consequences. Change in the law or in the business practices of some registrants in response to the law may provide new opportunities for the registrant. For example, if a 'cap and trade' type system is put in place, registrants may be able to profit from the sale of allowances if their emissions levels end up being below their emissions allotment."[1]

Registrants must disclose the impact on their business of treaties and international accords related to climate change if they present a material risk or benefit to the company. If the registrant's business is reasonably likely to be affected by those agreements, the company must evaluate the possible impact and provide disclosures, as appropriate, in the company's business description and MD&A. As previously noted, additional rulemaking on climate-related risks and opportunities may be forthcoming.

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[1] Sec. Act Release No. 9106 (Feb. 8, 2010), at 23.

§ 4:17 2010 Interpretive Release: Indirect consequences of regulation or business trends

The Commission noted that various developments related to climate change could indirectly create new risks and opportuni-

ties for registrants that might trigger disclosure obligations. For example, the developments could increase or decrease demand for the registrant's products or services or open new market opportunities or new competitive threats. In the context of GHG emissions, registrants whose businesses are materially impacted must consider the extent to which, for example, there might be a decreased demand for goods that have a high GHG intensity. Conversely, demand for goods that produce lower GHGs could increase. Demand for alternative energy could increase, and those supporting the production of carbon-based energy sources could see a reduction in demand.

The Commission also encouraged registrants to consider reputational impacts. If public opinion of a company's goods or services were materially affected by the perception that the company is a "good" or "bad" corporate citizen, the company should consider disclosure of that reputational effect. The Commission noted that, as always, registrants should consider their own facts and circumstances in evaluating the materiality of the indirect consequences of climate change events. When they are material, the company must consider what disclosure obligations are triggered, referring to the disclosure guidance provided, as described above. For example, the indirect consequences might require disclosure in MD&A to the extent they represent a material known trend or uncertainty impacting the company's financial condition or results of operations. If they present a material risk, they could drive risk factor disclosure. Even business description disclosure could be required if the registrant were, for example, to shift its business focus in response to changing competitive or reputational pressures.

§ 4:18 2010 Interpretive Release: Physical impacts of climate change

The physical effects of climate change, such as flooding, hurricanes, rising sea levels, rising temperatures, or impaired access to water, could present threats to a company's operations that, if material, would require disclosure. The Commission cites a 2007 Government Accountability Office report indicating that, between 1980 and 2005, 88 percent of property losses paid by insurers were related to weather.[1] If climate change exacerbates the incidence of severe weather, then it likely will be a reporting consideration for more registrants. Potential consequences of severe weather that the Commission cites include property damage and disruption to operations, including manufacturing operations and transport of products; financial and operational impacts due to disruptions to major business partners such as key customers or suppliers due to hurricanes or floods; increased insurance claims for insurance companies and reinsurance companies and higher premiums for companies with higher risks such as those in coastal areas; and decreased agricultural production and capacity in areas impacted by flooding or drought.[2]

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[1] Sec. Act Release No. 9106 (Feb. 8, 2010), at 26.

[2] Sec. Act Release No. 9106 (Feb. 8, 2010), at 27.

§ 4:19 2010 Interpretive Release: Foreign Private Issuers

The 2010 Interpretive Release emphasized that its guidance applies to not only domestic issuers but also foreign private issuers, whose specific disclosure requirements derive from Regulation S-K (as to Securities Act disclosures in registration

statements filed on Form F-1 or F-3) or Form 20-F[1] for Exchange Act reports and registration statements. The Commission noted that "most of the disclosure requirements applicable to domestic issuers under Regulation S-K that are most likely to require disclosure related to climate change have parallels under Form 20-F, although some of the requirements are not as prescriptive as the provisions applicable to domestic issuers."[2] The Commission identified the following provisions of Form 20-F as ones specifically to consider when assessing whether a foreign private issuer must disclose climate change issues:

- Item 3.D (disclosure of material risks)
- Item 4.B.8 (disclosure of material effects of government regulation on the company's business)
- Item 4.D (disclosure of any environmental issues that might affect the company's use of assets)
- Item 5 (explanation of factors that have affected the company's historical financial condition and results of operations and management's assessment of trends and factors that are expected to have a material effect on the company's future financial condition and results of operations)
- Item 8.7.A (disclosure of legal or arbitration proceedings, including those brought by the government, that have had or might in the future have significant effects on the company's financial position or profitability)[3]

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[1] 17 CFR § 249.220f.

[2] Sec. Act Release No. 9106 (Feb. 8, 2010), at 20.

[3] Sec. Act Release No. 9106 (Feb. 8, 2010), at 20-21.

PART IV.
ESG RULE-MAKING FORTHCOMING FROM THE SEC

§ 4:20 The recent evolution of the SEC on ESG

ESG has remained a regular topic of discussion among SEC officials in the wake of public comments to SEC's 2016 Concept Release and the 2019 proposed rule to modernize the S-K Regulations. Starting in the fall of 2020 through the beginning of 2021, the SEC's efforts, led in large part by Commissioner and Acting Chair Allison Herron Lee, to acknowledge and address the need for standardized ESG disclosures has picked up immense momentum as evidenced by the key events detailed below.

On September 22, 2020, Commissioner Lee delivered a speech at the Council of Institutional Investors Fall 2020 Conference, where she placed the issue of diversity and inclusion and the role of mandatory disclosure front and center.[1] Commissioner Lee acknowledged that the events of 2020 "triggered an unprecedented national conversation on racial injustice that also highlights the urgency of ensuring diverse perspectives and representation at all levels of decision-making in our country."[2] Although the SEC had taken steps to address the issue of fair representation in its 2020 amendments to Regulation S-K (which added "human capital as a broad topic for possible disclosure"), Commissioner Lee admitted that the SEC could still

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[1] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.

[2] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.

do more, noting, in part, the Commission's pending proposal for Rule 14a-8 which "affects shareholder proposals which often cover this topic."[3]

In addition to events that have pushed these important issues to the forefront, empirical studies have shown that diversity and representation in the boardroom and c-suite are better for business, which has led investors, asset managers, and proxy advisers to consider diversity in their proxy voting decisions more and more.[4] Investors want as much information about an issuer

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[3] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922. Presumably, she was referring to procedural requirements and resubmission thresholds, which were the subject of rules adopted the day after her speech. Exch. Act Release No. 89964 (Sept. 23, 2020). The SEC has placed amendments to Rule 14a-8 on its rulemaking agenda for 2021. Agency Rule List, SEC, Spring 2021, reginfo.gov.

[4] A McKinsey study found that "companies with the greatest ethnic diversity on executive teams outperformed those with the least by 36 percent in profitability." The study also found that "companies with more than 30 percent women on their executive teams are significantly more likely to outperform those with fewer or no women executives." See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.; see McKinsey & Company, *Diversity Wins, How inclusion matters* (May 2020) https://www.mckinsey.com/~/media/McKinsey/Featured %20Insights/Diversity%20and%20Inclusion/Diversity%20wins%20How%20inclusion%20matters/Diversity-wins-How-inclusion-matters-vF.pdf; see also Morgan Stanley, *Why It Pays to Invest in Gender Diversity* (May 11, 2016), https://www.morganstanley.com/ideas/gender-diversity-investment-framework (discussing a study finding that higher gender diversity companies achieve higher returns and lower volatility than their less diverse peers).

as possible and the SEC's biggest tool to help this happen is disclosure.[5]

Some proponents of diversity disclosures believe that it should be left to individual companies "to determine whether diversity information is material, and if so, what specifically to disclose."[6] In her September 2020 statement, however, Commissioner Lee made clear that she believed that approach would produce non-standardized, inconsistent information.[7] Commissioner Lee conceded that the current state of the SEC's disclosure regime "reveals the shortcomings of a principles-based materiality regime in this area."[8] Most notable, she stated, is the fact that "72 percent of companies in the Russell 1000 do not disclose any racial or ethnic data about their employees and only four percent disclose the complete information they are required to collect and maintain under EEOC rules" and "less

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[5] See Allison Herren Lee, Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.

[6] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.

[7] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.

[8] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.

than half of all Fortune 100 companies disclose data on the ethnic and gender compositions of their board."[9]

Commissioner Lee proposed a number of SEC actions aside from mandatory disclosures that could help address diversity and inclusion disparities.[10] First, she addressed the lack of diversity among financial regulators and said that all agencies — including the CFTC, FDIC, and SEC — should be "working to open opportunities in financial regulation."[11] Second, to address "the substantial disparities in access to capital markets for women and minorities due in part to a persistent wealth gap between minority and non-minority communities that can prevent minority entrepreneurs from investing their own capital in their businesses or using it as collateral," Commissioner Lee suggested tasking the SEC's Division of Economic and Risk Analysis "with assessing the extent to which [SEC] rules will have an impact on underrepresented communities."[12] She also considered "better integrating [the Commission's] Office of

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[9] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech/lee-cii-2020-conference-20200922.

[10] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech /lee-cii-2020-conference-20200922.

[11] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech /lee-cii-2020-conference-20200922.

[12] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech /lee-cii-2020-conference-20200922.

Minority and Women Inclusion (OMWI) into [its] policymaking."[13] Finally, she stated that the SEC should find a way to work better with other agencies "in their efforts to combat discrimination and support women and minority-owned small businesses."[14]

A little over a month later, on November 5, 2020, Commissioner Lee made remarks at the Practicing Law Institute's (PLI's) 52nd Annual Institute on Securities Regulation, this time focusing on climate change and its influence on the economy.[15] She began by stating that "climate change may present a systemic risk to financial markets."[16] She noted the tendency to underprice climate change risk, "particularly with respect to long-dated assets, utilities, commercial mortgage-backed securities, and potentially municipal bonds," which can "lead to abrupt and disruptive re-pricing as markets discover the anomalies."[17] Commissioner Lee stated that climate-related risks pose

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[13] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech /lee-cii-2020-conference-20200922.

[14] See Allison Herren Lee, *Diversity Matters, Disclosure Works, and the SEC Can Do More: Remarks at the Council of Institutional Investors Fall 2020 Conference* (Sept. 22, 2020) https://www.sec.gov/news/speech /lee-cii-2020-conference-20200922.

[15] See Allison Herren Lee, *Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation* (Nov. 5, 2020) https://www .sec.gov/news/speech/lee-playing-long-game-110520.

[16] See Allison Herren Lee, *Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation* (Nov. 5, 2020) https://www .sec.gov/news/speech/lee-playing-long-game-110520.

[17] See Allison Herren Lee, *Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation* (Nov. 5, 2020) https://www .sec.gov/news/speech/lee-playing-long-game-110520.

problems other types of risks do not because they "don't operate in isolation" but rather "interact with each other," and are "potentially irreversible in terms of the damage it can cause."[18]

Because of the nature of climate-related risks, Commissioner Lee acknowledged that investors are demanding information and they "require[] uniform, consistent, and reliable disclosure," particularly "by those who finance issuers."[19] Commissioner Lee proposed that "the SEC should work with market participants toward a disclosure regime specifically tailored to ensure that financial institutions produce standardized, comparable, and reliable disclosure of their exposure to climate risks, including not just direct, but also indirect, greenhouse gas emissions associated with the financing they provide, referred to as Scope 3 emissions."[20]

On the heels of these remarks, in January 2021, Commissioner Lee was designated Acting Chair of the SEC by President Biden. The first three months following her designation, Acting Chair Lee made great strides in furthering the SEC's analysis of ESG disclosures and related enforcement, starting on February 24, 2021, when she directed "Division of Corporation Finance to enhance its focus on climate-related disclosure in public company filings" stating that "[i]t is our responsibility to ensure that they have access to material information when plan-

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[18] See Allison Herren Lee, *Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation* (Nov. 5, 2020) https://www.sec.gov/news/speech/lee-playing-long-game-110520.

[19] See Allison Herren Lee, *Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation* (Nov. 5, 2020) https://www.sec.gov/news/speech/lee-playing-long-game-110520.

[20] See Allison Herren Lee, *Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation* (Nov. 5, 2020) https://www.sec.gov/news/speech/lee-playing-long-game-110520.

ning for their financial future. Ensuring compliance with the rules on the books and updating existing guidance are immediate steps the agency can take on the path to developing a more comprehensive framework that produces consistent, comparable, and reliable climate-related disclosures."[21]

This announcement fueled continued momentum into March, when the SEC made multiple announcements and remarks that laid the groundwork for the agency's ESG agenda for the year.

First, on March 3, 2021, the SEC Division of Examinations announced its 2021 priorities, stating an "Enhanced Focus on Climate-Related Risks," specifically stating that it was "enhancing its focus on climate and ESG-related risks by examining proxy voting policies and practices to ensure voting aligns with investors' best interests and expectations, as well as firms' business continuity plans in light of intensifying physical risks associated with climate change."[22] Among other things, the Division of Examinations will examine whether proxy voting policies as disclosed by investment companies, investment advisers, and private funds are consistent with how such firms actually handled proxy voting matters.

Next, on March 4, 2021, the SEC announced that it created an Enforcement Task Force Focused on Climate and ESG issues. The SEC stated that the task force's "initial focus will be to identify any material gaps or misstatements in issuers' disclosure of climate risks under existing rules.[23] The task force will also analyze disclosure and compliance issues relating to investment advisers' and funds' ESG strategies. . . . In addition,

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[21] See https://www.sec.gov/news/public-statement/lee-statement-review-climate-related-disclosure.

[22] See https://www.sec.gov/news/press-release/2021-39.

[23] See https://www.sec.gov/news/press-release/2021-42.

the Climate and ESG Task Force will evaluate and pursue tips, referrals, and whistleblower complaints on ESG-related issues, and provide expertise and insight to teams working on ESG-related matters across the Division."[24]

Then, on March 11, 2021, John Coates, while serving as Acting Director of the Division of Corporation Finance, spoke at the 33rd Annual Tulane Corporate Law Institute and advocated for developing an ESG-focused disclosure regime.[25] Coates discussed three main considerations in creating ESG disclosure requirements: (1) the costs of new ESG disclosures; (2) whether the disclosures should be mandatory or voluntary; and (3) the virtues of a global disclosure system.[26]

Coates noted that while the costs of preparing disclosures must be taken into account, "the recognition of the costs associated with *not* having ESG requirements" are just as important.[27] He said that investors are withholding investments "in the absence of information," and companies are facing "higher costs

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[24] See https://www.sec.gov/news/press-release/2021-42.

[25] John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[26] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[27] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

in responding to investor demand for ESG information because there is no consensus ESG disclosure system."[28]

With respect to whether ESG disclosures should be mandatory for all issuers, Coates said that "there is no reason an ESG disclosure system would need to be less nuanced" than the existing regime.[29] He said the current system "permits significant differences in how companies respond to a variety of 'mandatory' requirements. . . ."[30] For example, "comply and explain" requirements give companies "the ability to explain" which "makes the requirement less than rigidly mandatory and for some companies potentially more informative."[31] Furthermore, he noted that as companies "continue to disclose more in sustainability reports, they should already be evaluating those disclosures in light of existing anti-fraud obligations."[32]

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[28] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[29] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[30] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[31] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[32] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11,

On the subject of global comparability, Coates asserted that "ESG issues are global issues" that "need global solutions for our global markets."[33] He acknowledged however that establishing a global framework was complex and that "funding, governance and public accountability are all critical elements of a reliable, trusted disclosure system."[34] Coates said the SEC should "play a leading role in the development of a baseline global framework that each jurisdiction can build upon to address its individual needs."[35]

Four days later, on March 15, 2021, Acting Chair Lee made a speech titled "A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC," discussing the SEC's prioritization of areas such as ESG and climate change.[36] In her speech, Acting Chair Lee stated that climate and ESG are key to the SEC's "core mission."[37] Once again, she

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2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[33] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[34] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[35] See John Coates, *ESG Disclosure – Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets* (Mar. 11, 2021) https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.

[36] See https://www.sec.gov/news/speech/lee-climate-change.

[37] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

focused on "[ensuring] material information gets into the markets in a timely manner," claiming that "investors are demanding more and better information on climate and ESG, and that demand is not being met by the current voluntary framework."[38]

In an effort toward a comprehensive ESG disclosure framework, Commissioner Lee remarked again on her February request to the Division of Corporation Finance "to enhance its focus on climate-related disclosures."[39] She noted how she had tasked the Division with assessing "how these risks are being analyzed and disclosed by companies now to inform an update to the 2010 guidance — and to inform [] policymaking going forward."[40] With respect to shareholder proposals, she has also tasked the Division with "revising Commission or staff guidance on the no-action process, and potentially revising Rule 14a-8 itself" in an effort to "increase the number of proposals on the ballot that are well-designed for shareholder deliberation and votes, and reduce the number that are not."[41] Acting Chair Lee stated that she considered political spending disclosures as

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[38] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

[39] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

[40] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

[41] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

part of a comprehensive ESG disclosure system.[42] While she conceded that "the SEC is currently prevented from finalizing a rule in this area," she noted that "political spending disclosure is key to any discussion of sustainability."[43] All of these proposals, she said, are aimed at increasing "corporate accountability to investors through enhanced transparency and through supporting the exercise of shareholder rights."[44]

Also on March 15, 2021, Acting Chair Lee published a request for public input (RFPI) seeking public comment regarding climate change disclosure requirements "in light of demand for climate change information and questions about whether current disclosures adequately inform investors."[45] The SEC set out 15 questions to guide public comment and requested all public comment to be submitted by June 13, 2021.

In the interim, while the SEC amassed public comments on its request, it continued to move forward in its assessment of the ESG financial landscape, specifically ESG investing. On April 9, 2021, the SEC's Division of Examinations issued a risk alert (the Risk Alert) describing observations from recent examinations of investment advisers that manage and offer ESG invest-

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[42] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

[43] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

[44] See Allison Herren Lee, *A Climate for Change: Meeting Investor Demand for Climate and ESG Information at the SEC* (Mar. 15, 2021) https://www.sec.gov/news/speech/lee-climate-change.

[45] SEC, "Public Input Welcomed on Climate Change Disclosures," available at https://www.sec.gov/news/public-statement/lee-climate-change-disclosures.

ment options.[46] This Risk Alert provided observations of deficiencies and internal control weaknesses from examinations of investment advisers and funds regarding ESG investing as well as observations of effective practices from such examinations. SEC Commissioner Hester Peirce noted that the Risk Alert was a useful tool for firms that sell ESG products but cautioned that the Risk Alert should not be interpreted as a sign that ESG investment strategies were unique in the eyes of the examiners.[47]

In terms of specific deficiencies and weaknesses, staff at the Division of Examinations observed potentially misleading statements about the "ESG investing process" and about the "representations regarding the adherence to global ESG frameworks."[48] Key issues involved the fact that, while firms claimed to have processes in place for ESG investing these processes actually did not appear to be "reasonably designed to prevent violations of law."[49] Under the staff's analysis, firms' portfolio management processes did not appear to remain consistent with their disclosures about ESG approaches.[50] In addition, firm controls appeared inadequate to "maintain, monitor, and update ESG-related investing guidelines" and disclosures.[51] Moreover,

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[46] "The Division of Examinations' Review of ESG Investing," available at https://www.sec.gov/files/esg-risk-alert.pdf.

[47] "Statement on the Staff ESG Risk Alert," available at https://www.sec.gov/news/public-statement/peirce-statement-staff-esg-risk-alert#_ftn1.

[48] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[49] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[50] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

the SEC believed that the voting of proxies may have not been consistent with the stated approaches of advisors.[52] The staff also found claims of ESG investing that were not substantiated or could be possibly misleading.[53] The staff also determined that the "[c]ompliance programs did not adequately address" relevant ESG issues.[54]

With regard to effective practices, the staff pointed to clear, precise disclosures that addressed firm specific approaches, and were in line with firms' actual practices.[55] Additionally, the staff observed that some firms, helpfully, had "policies and procedures that addressed ESG investing and covered key aspects of the firms' relevant practices."[56] Finally the staff noted the importance of having compliance personnel that are knowledgeable about the ESG practices of the firm.[57]

With these initiatives and investigations as its backdrop, the SEC, on June 11, 2021, announced its Annual Regulatory Agenda, which included proposed rulemaking areas such as

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[51] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[52] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[53] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[54] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[55] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[56] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

[57] Risk Alert, Division of Examinations' Review of ESG Investing, Apr. 9, 2021, https://www.sec.gov/files/esg-risk-alert.pdf.

"[d]isclosure related to climate risk, human capital, including workforce diversity and corporate board diversity, and cybersecurity risk" and "[i]nvestment fund rules, including money market funds, private funds, and ESG funds."[58] The timeline for these proposed rulemakings spanned the fall of 2021 through the spring of 2022.

Shortly after this announcement, the deadline for public comments to the March 15, 2021 request for public input passed. In two months, the SEC received more than 550 comments, with every three out of four comments in favor of mandated climate-related disclosures.[59] Of those in favor, many generally agreed that: (1) Climate-related disclosures should be required if those disclosures are "material" to operations and would cause a rational investor to alter their investment decision; (2) Mandated climate-related disclosures should require the quantification and reporting of direct greenhouse gas (GHG) emissions (Scope 1) and certain indirect GHG emissions (Scope 2); (3) Specific applicable metrics are needed for quantifying emissions and consistency with current frameworks such as the SASB, the Climate Disclosure Standards Board, and the recommendations of the TCFD.

On June 28, 2021, Commissioner Lee (having been replaced by Gary Gensler as SEC Chair on April 14, 2021) gave the keynote address at the 2021 Society for Corporate Governance National Conference. She spoke about board obligations when it comes to ESG issues.[60] She also discussed how "boards increas-

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[58] See https://www.sec.gov/news/press-release/2021-99.

[59] Gary Gensler, Chair, Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar (July 28, 2021) https://www.sec.gov/news/speech/gensler-pri-2021-07-28

[60] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

ingly have oversight obligations related to climate and ESG risks — identification, assessment, decision-making, and disclosure of such risks," which "flow from both the federal securities laws and fiduciary duties rooted in state law."[61] These obligations, she said, require "directors to think about and consider the impact of climate change and other ESG matters on the financial statements and other corporate disclosures."[62]

Commissioner Lee noted there is a "rising expectation that boards will play a key role in managing [physical risk, transition risk, regulatory risk and reputational risk associated with climate and ESG]" and she made some suggestions as to how boards can "maximize ESG opportunities, message their commitment on these issues, and position themselves as ESG leaders."[63] Commissioner Lee proposed enhancement to board diversity "not least because investors increasingly expect them to do so."[64] She also recommended bringing adequate climate and ESG experts onto boards.[65] She advised companies to consider enhancing "the ESG competence of their boards" including "in-

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[61] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

[62] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

[63] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

[64] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

[65] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

tegrating ESG considerations into their nominating processes in order to recruit directors that will bring ESG expertise to the board; training and education efforts to enhance board members' expertise on ESG matters; and [] engagement with outside experts to provide advice and guidance to boards."[66] Finally, Commissioner Lee suggested tying executive compensation to ESG metrics, which may "offer an important way to deliver on a company's commitment to issues that matter to investors and consumers."[67]

Following the messaging of Acting Chair and Commissioner Lee — in addition to the strong public support evidenced in public comments to the March 2021 request for input as well as the 2016 Concept Release and 2019 proposed rule modernizing S-K Regulations — Chair Gensler, speaking on July 28, 2021, before a PRI "Climate and Global Financial Markets" webinar, made clear that mandatory climate-disclosure rules are on the immediate horizon. He noted that he had tasked "SEC staff to develop a mandatory climate risk disclosure rule proposal for the Commission's consideration by the end of the year," and "to consider whether these disclosures should be filed in the Form 10-K, living alongside other information that investors use to make their investment decisions."[68]

In terms of form and substance, Chair Gensler provided some color as to what a mandated climate-related disclosure

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[66] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

[67] See Allison Herren Lee, *Climate, ESG, and the Board of Directors: "You Cannot Direct the Wind, But You Can Adjust Your Sails"* (June 28, 2021) https://www.sec.gov/news/speech/lee-climate-esg-board-of-directors.

[68] https://www.sec.gov/news/speech/gensler-pri-2021-07-28.

may look like. First, he confirmed that disclosures should be "consistent and comparable" and mandatory.[69]

Second, he said the disclosures should be "decision-useful" and have "sufficient detail so investors can gain helpful information — it's not simply generic text."[70] To that end, he anticipates that disclosures will have both quantitative and qualitative components. Qualitative disclosures would "answer key questions, such as how the company's leadership manages climate-related risks and opportunities and how these factors feed into the company's strategy," while "quantitative disclosures could include metrics related to greenhouse gas emissions, financial impacts of climate change, and progress towards climate-related goals."[71]

Third, Chair Gensler noted that the disclosures may potentially be industry-specific, mentioning banking, insurance, and transportation sectors specifically.[72]

Fourth, he noted that fund managers and companies that make specific climate-related pledges or commitments could be charged with disclosing additional information to support those

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[69] See Gary Gensler, *Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar* (July 28, 2021) https://www.sec.gov/news/speech/gensler-pri-2021-07-28.

[70] See Gary Gensler, *Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar* (July 28, 2021) https://www.sec.gov/news/speech/gensler-pri-2021-07-28.

[71] See Gary Gensler, *Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar* (July 28, 2021) https://www.sec.gov/news/speech/gensler-pri-2021-07-28.

[72] See Gary Gensler, *Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar* (July 28, 2021) https://www.sec.gov/news/speech/gensler-pri-2021-07-28.

pledges or commitments.[73] In addition, companies in jurisdictions that have made climate-related commitments (such as with respect to the Paris Agreement) may be required to disclose their strategy for compliance with those jurisdictional commitments.

Finally, Chair Gensler noted that the SEC will likely develop its own disclosure requirements rather than rely on third-party standard setters, although it may look to existing frameworks such as the TCFD for guidance.

On September 22, 2021, approximately seven months after the Division of Corporation Finance received its mandate from Acting Chair Lee to ensure compliance with climate-related disclosure rules currently on the books, the Division issued a statement reminding companies that it is selectively reviewing SEC filings for climate-related disclosures and providing a sample letter that companies have been receiving regarding their climate-related disclosures or the absence thereof.[74] The letter directed specific comments to companies that provided information in Corporate Social Responsibility (CSR) reports but failed to provide similar information in their SEC filings. The letter also sought information regarding material risk factors related to climate change that may affect a company and

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[73] See Gary Gensler, *Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar* (July 28, 2021) https://www.sec.gov/news/speech/gensler-pri-2021-07-28.

[74] See *Sample Letter to Companies Regarding Climate Change Disclosures* (modified Sept. 22, 2021) https://www.sec.gov/corpfin/sample-letter-climate-change-disclosures.

what analysis the company has done regarding those risk factors.[75]

With a proposed rule on mandated climate disclosure anticipated by the end of this year or early next, and the ongoing efforts of the SEC through various divisions and initiatives to wrestle with the reporting of ESG factors through existing or new frameworks, what is clear is that ESG disclosures in public filings are the focus of SEC interest.

[75] See *Sample Letter to Companies Regarding Climate Change Disclosures* (modified Sept. 22, 2021) https://www.sec.gov/corpfin/sample-letter-climate-change-disclosures.

§ 4:21 Views of the Advisory Committees

In May 2020, the SEC's Investor Advisory Committee recommended that the SEC "set the framework" for issuers to report on material ESG information. The Committee observed that "[f]or close to 50 years, the SEC has periodically contemplated whether ESG disclosures are material and should be incorporated into its integrated disclosure regime for SEC registered Issuers." The Committee concluded that "the time has come for the SEC to address this issue."[1]

In the recommendation, the Committee defined the contours of ESG by reference to the "broad set of subjects germane to businesses as highlighted by The Business Roundtable on Au-

[1] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure" (as of May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

gust 19, 2019 in its Statement on the Purpose of a Corporation."[2] The Committee maintained that "investors consider certain ESG information material to their investment and voting decisions, regardless of whether their investment mandates include an 'ESG-specific' strategy. Our work has informed us that this information is material to investors regardless of an Issuer's business line, model or geography, and is different for every Issuer. Yet, despite a plethora of data, there is a lack of material, comparable, consistent information available upon which to base some of these decisions."[3]

In the absence of SEC regulation, different standards and criteria have emerged, which the Committee noted have imposed a "significant burden" on companies.[4] The Committee contended that "the SEC is best-placed to set the framework for Issuers to disclose material information upon which investors can rely to make investment and voting decisions."[5] As a result, the Com-

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[2] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure" (as of May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[3] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure" (as of May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[4] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure" (May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-in vestor-as-owner-subcommittee-on-esg-disclosure.pdf.

[5] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee

mittee recommended that the SEC "begin in earnest an effort to update the reporting requirements of Issuers to include material, decision-useful, ESG factors."[6]

The recommendation provided that investors and third-party data providers should have "accurate, comparable and material Issuer primary-source information upon which to base their analysis" that should be governed by "consistent standards and oversight."[7] It further suggested that the SEC's action would:

> (a) Provide investors with the material, comparable, consistent information they need to make investment and voting decisions;
>
> (b) Provide Issuers with a framework to disclose material, decision-useful, comparable and consistent information in respect of their own businesses, rather than the current situation where investors largely rely on third party ESG data providers, which may not always be reliable, consistent, or necessarily material;

Relating to ESG Disclosure" (as of May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[6] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure" (May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[7] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure" (May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-in vestor-as-owner-subcommittee-on-esg-disclosure.pdf.

(c) Level the playing field among all U.S. Issuers regardless of market cap size or capital resources;

(d) Ensure the continued flow of capital to U.S. Issuers; and

(e) Enable the SEC to take control of ESG disclosure for the U.S. capital markets before other jurisdictions impose disclosure regimes on U.S. Issuers and investors alike.[8]

At the May 2020 meeting of the Investor Advisory Committee, Chair Clayton reiterated his views on ESG disclosure.[9] He stated that his "views and support for effective disclosure on 'decision useful' information, including the modernization of financial disclosures and my views on disclosures about 'E' matters, 'S' matters and 'G' matters (I believe E, S and G are quite different baskets of disclosure matters and that lumping them together diminishes the usefulness, including investor understanding, of such disclosures), are not new to you."[10]

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[8] U.S. Securities and Exchange Commission, "Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure" (as of May 14, 2020), available at https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[9] SEC Chair Jay Clayton, "Remarks at Meeting of the Investor Advisory Committee," (May 21, 2020), available at https://www.sec.gov/news/publicstatement/clayton-statement-investor-advisory-committee-meeting-052120.

[10] SEC Chair Jay Clayton, "Remarks at Meeting of the Investor Advisory Committee," (May 21, 2020), available at https://www.sec.gov/news/publicstatement/clayton-statement-investor-advisory-committee-meeting-052120.

On December 1, 2020, the SEC Asset Management Advisory Committee provided a draft list of Potential Recommendations of the ESG subcommittee.[11] The ESG subcommittee was formed in the first quarter of 2020 with the purpose of looking into ESG practices of investment products, and exploring, within the areas of the SEC's mandate, whether any recommendations were warranted to improve practices.[12] The subcommittee was particularly focused on the extent to which ESG investment products differed from other types of investment products, and whether any intervention was needed to address these differences.[13] The subcommittee's December 1, 2020 recommendations included a set of recommendations regarding issuer disclosure of ESG risks as well as recommendations regarding ESG investment product disclosure.

With regard to issuer disclosure of ESG risks, the subcommittee recommended that:

(a) The SEC should require the adoption of standards by which corporate issuers disclose material ESG risks

(b) The SEC should utilize standard setters' frameworks to require disclosure of material ESG risks

(c) The SEC should require that material ESG risks be disclosed in a manner consistent with the presentation of other financial disclosures

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[11] See https://www.sec.gov/files/potential-recommendations-of-the-esg-subcommittee-12012020.pdf.

[12] See https://www.sec.gov/files/potential-recommendations-of-the-esg-subcommittee-12012020.pdf.

[13] See https://www.sec.gov/files/potential-recommendations-of-the-esg-subcommittee-12012020.pdf.

With regard to ESG investment product disclosures, the subcommittee recommended that:

(a) The SEC should suggest best practices to enhance ESG investment product disclosure, including alignment with the taxonomy developed by the Investment Company Institute (ICI) ESG Working Group, and clear description of each product's strategy and investment priorities, including description of non-financial objectives such as environmental impact or adherence to religious requirements

(b) The SEC should suggest best practices for investment products to describe each product's planned approach to share ownership activities in the Statement of Additional Information, and any notable recent ownership activities outside proxy voting, which is reported in Form N-PX, in shareholder reporting

In its work, the subcommittee noted that it "found that some kind of actions to support best practices would improve transparency for investors, but that more prescriptive actions were counter-productive given the early state of the evolution of ESG investing; strong rulesets might, at this point, freeze development of investment and measurement approaches in this investing style." As a result the subcommittee reported that its recommendations to improve investment product disclosure are "to provide best practice guidance rather than mandate specific approaches."

With regard to issuer disclosures, the subcommittee admitted that "if standardized, consistent issuer disclosure were available, this would allow investors and their third party service providers to verify whether investment products met their objectives, and would make performance attribution to ESG factors more consistent and reliable." Therefore, the subcommittee's recommendation regarding issuer disclosure while limited in scope, do involve the adoptions of standards for disclosure, specifically

the subcommittee proposed "mandatory, rather than voluntary, standards be established, as the current, unguided approach has not resulted in consistent, comparable, complete and meaningful disclosure."

The subcommittee stated that it does not "recommend the highly prescriptive approach that is used, for example, in Europe, as that may result in the production of metrics that are not needed to assess an issuer's material risks, and unnecessary cost." Rather, the subcommittee asserted that a "parsimonious approach" would be sufficient "to meet the needs of investor transparency, with a focus on a limited number of material metrics, tailored by industry, overseen by an independent standard setting entity such as SASB, or other similar approaches so long as they are limited to material metrics by industry."

On July 7, 2021, the SEC Asset Management Advisory Committee (AMAC) provided (1) a list of recommendations for ESG, and (2) a report and recommendations on diversity and inclusion in the asset management industry.[14] With regard to ESG, AMAC adopted wholesale the ESG subcommittee's recommendations regarding ESG investment product disclosures provided to AMAC on December 1, 2020. With regard to disclosure of material ESG matters, AMAC amended and adopted the following recommendations:

(a) The AMAC recommended the SEC take steps to foster meaningful, consistent, and comparable disclosure of material ESG matters by issuers

(b) To foster meaningful, consistent, and comparable disclosure, the SEC should encourage issuers to adopt a framework for disclosing material ESG matters and to provide an explanation if no disclosure framework is adopted

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[14] See files/amac-recommendations-di-subcommittee-070721.pdf.

(c) In addition, the AMAC recommends the SEC initiate a study of third-party ESG disclosure frameworks for the disclosure of material ESG matters to assess whether the frameworks could play a more authoritative role in the future

With regard to the recommendations on diversity and inclusion, AMAC summarized the work that the diversity and inclusion subcommittee performed, providing a brief synopsis of the findings of the committee. First, AMAC noted that the statistics are "startling" and "clear," reporting that "of the $70 trillion in global financial assets under management across the investment universe, less than 1% are managed by minority-owned or women-owned firms." AMAC further reported that "women and people of color also remain dramatically underrepresented (by all objective measures) at the board and senior management levels within asset management firms and fund complexes."

Second, AMAC reported on the widespread bias in the industry, citing to studies it deemed credible and objective to report "widespread gender and racial bias in the decisions by those in positions making asset and asset manager allocation decisions regarding who manages money for governments, universities, charities, foundations, and the institutional market in general." AMAC went on to note that these studies further confirmed that "artificial barriers that do not advance the interests of investors have been constructed and are being utilized by asset allocators under the guise of fiduciary considerations."

Third, AMAC provided full-throated support for the conclusion that "investment performance by diverse asset managers is equal to or greater than the investment performance of firms that lack diversity in ownership and senior leadership, despite differences in size and length of track record." AMAC further noted that peer-reviewed academic research indicates that diversity in life experiences is additive to investment performance.

Finally, AMAC noted the evolution of "public interest" and "materiality" reporting "a shift in both public interest in diversity in the asset management industry and the extent to which adviser's commitment to diversity is considered material to the decision of those selecting and retaining such firms." From that backdrop, AMAC then issued its recommendations on diversity and inclusion, which included the following:

(a) The SEC requiring enhanced disclosure in SEC filings by investments advisers on issues of gender and racial diversity in the workforce, officer ranks, and ownership ranks of advisory firms

(b) The SEC requiring enhanced disclosure in SEC filings for investment companies on gender and racial diversity on the fund boards of each fund, as well as issues of gender and racial diversity in the workforce, officer ranks, and ownership ranks of advisory and sub-advisory firms

(c) The SEC requiring enhanced disclosure in SEC filings (particularly, Form ADV), to provide transparency in material business practices relevant to an investor's assessment of gender and racial diversity and inclusion. Specifically, AMAC recommended that the SEC require investment advisers who serve as either asset allocators or consultants for asset aggregators and/or allocators to include disclosure on whether and to what extent the registrant's policies include diverse asset management firms in the pool of those considered and/or selected

(d) The SEC issuing guidance that clarifies that fiduciaries may consider a wide variety of factors in their selection of asset management firms and that fulfilment of one's fiduciary duty in this context does not require automatic exclusion of asset managers who are newer to the industry or do not already have a certain level of assets under management (AUM)

(e) The SEC engaging in a study of pay-to-play within the industry and how it has evolved since it's last study 10 years ago

(f) The SEC establishing a centralized and uniform practice of directing parties reporting discriminatory employment and contracting practices to the appropriate government agency for further investigation.

§ 4:22 U.S. government action supporting ESG

During 2021, other federal agencies, and the executive and legislative branches of the U.S. government have been aiming to integrate ESG factors into government initiatives, be it through agency action, executive order, or law.

On April 19, 2021 the U.S. Treasury Department announced a coordinated climate policy strategy aiming to leverage finance and financial risk mitigation to tackle the threat of climate change. The goal is to position the U.S. economy for strong and sustainable growth consistent with a future based on net zero emissions.[1] The Department has also set up a new Climate Hub and appointed a Climate Counselor to help coordinate climate-related efforts and implement Department strategy.[2]

In the Executive Order on Climate-Related Financial Risk mentioned earlier in this article,

President Biden noted that the "intensifying impacts of climate change present physical risk to assets, publicly traded securities, private investments, and companies." The President

[1] Https://home.treasury.gov/news/press-releases/jy0134.

[2] Https://home.treasury.gov/news/press-releases/jy0134.

further stated that the "failure of financial institutions to appropriately and adequately account for and measure these physical and transition risks threatens the competitiveness of US companies and markets, the life savings and pensions of US workers and families, and the ability of US financial institutions to serve communities." The Executive Order's whole-of government instruction for a government-wide climate-risk strategy calls for identifying the public and private means to achieving net carbon neutrality by 2050.

The Executive Order specifically instructs Treasury Secretary Janet Yellen to work with the Financial Stability Oversight Council (FSOC) to:

(a) Assess climate-related financial risks, both physical and transitional, to the stability of the U.S. federal government and financial system

(b) Share climate-related financial risk information among FSOC member agencies and other executive agencies, as appropriate

(c) Produce a report within 180 days of the order on the efforts of FSOC member agencies to integrate climate-related financial risk considerations, including any potential recommendations or current practices to enhance climate-related disclosures by regulated entities

The focus on creating greater transparency and consistency in climate-related financial disclosures echoes calls from investors and corporations alike for action on ESG disclosures. The Executive Order further requires consideration from Labor Secretary Marty Walsh to suspend, revise, or rescind two Trump-era rules that sought to prohibit investment firms from taking ESG considerations into account when making investment decisions, reflecting the increased demand for ESG investing globally.

On June 16, 2021, the House of Representatives passed H.R. 1187, entitled "Corporate Governance Improvement and Investor Protection Act." H.R. 1187 is a package of bills addressing everything from the simplification of ESG disclosures, to the mandating of climate risk disclosure by public companies, to the reporting and comparison of annual increases in executive compensation, to the disclosure in proxy statements of demographic information for board of director members, nominees and executive officers.[3] Many of the bills contained within H.R. 1187 are aimed at requiring the SEC "to adopt clear, consistent standards for ESG metrics and would require public companies to disclose key information to shareholders regarding political spending, worker pay, climate risk, and tax reporting[.]"[4]

Currently, this legislation has not been passed by the Senate,[5] but, as of June 17, 2021, it has been "Received in the Senate and Read twice and referred to the Committee on Banking, Housing, and Urban Affairs."[6]

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[3] In total, H.R. 1187 includes the following: (1) ESG Disclosure Simplification Act; (2) Shareholder Political Transparency Act; (3) Greater Accountability in Pay Act; (4) Climate Risk Disclosure Act; (5) Disclosure of Tax Havens and Offshoring Act; (6) Workforce Investment Disclosure Act; (7) Preventing and Responding to Workplace Harassment; (8) Cybersecurity Disclosure; (9) Improving Corporate Governance Through Diversity Act; (10) Uyghur Forced Labor Act; (11) Study and Report on Small Business and ESG Disclosure; see also https://corpgov.law.harvard.edu/2021/07/09/the-u-s-moving-toward-adopting-new-climate-disclosures/.

[4] See https://www.congress.gov/bill/117th-congress/house-bill/1187.

[5] See https://www.congress.gov/bill/117th-congress/house-bill/1187.

[6] See https://www.congress.gov/bill/117th-congress/house-bill/1187.

PART V.
INTERNATIONAL ESG

§ 4:23 ESG Disclosure frameworks outside of the U.S.

While the focus of this chapter is the disclosure framework within the U.S. under the U.S. securities laws, the broader disclosure landscape forms a critical backdrop. Globally, the reporting landscape is shifting, and an ever-growing number of countries are developing their own ESG reporting requirements. At the same time, numerous voluntary reporting regimes have emerged.

The PRI reported in 2016 that 38 of the 50 largest economies in the world either had or were in the process of developing corporate disclosure requirements addressing ESG issues,[1] and a WBCSD / Climate Disclosure Standards Board (CDSB) report suggests that the number of sustainability reporting requirements in existence globally increased ten-fold between 1992 and 2017.[2] In the 50 largest economies, the PRI has identified nearly 300 policy drivers that encouraged investors to consider long-term indicators of value, such as ESG factors. Nearly half of those 300 policy drivers were implemented between 2013 and 2016.[3]

"We found a strong correlation between responsible investment regulation and better ESG risk management by compa-

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[1] Principles for Responsible Investment, "Global Guide to Responsible Investment Regulation" (2016), available at https://www.unpri.org/download?ac=325.

[2] Https://www.cdsb.net/sites/default/files/cdsb_report_1_esg.pdf.

[3] Principles for Responsible Investment, "Global Guide to Responsible Investment Regulation" (2016), available at https://www.unpri.org/download?ac=325.

nies," the PRI reported. "This is encouraging, especially given how recent many of these policies are."[4] At the same time, the PRI reported investor skepticism as to the effectiveness of these policy measures due to their perception that the policies are poorly designed and implemented. Furthermore, "few of the investment-focused policy initiatives we analysed were clearly linked to specific sustainability objectives. However, there are signs that this is starting to change," specifically with initiatives in the European Union (the EU) and China to align sustainability and financial market objectives.[5]

In the United Kingdom, many different pieces of legislation govern ESG matters. In July 2019, the UK adopted a Green Finance Strategy,[6] following closely on the heels of legislation committing the UK to achieve net zero GHG emissions by 2050.[7] The Green Finance Strategy's objectives are "to align private sector financial flows with clean, environmentally sustainable and resilient growth, supported by Government action

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[4] Principles for Responsible Investment, "Global Guide to Responsible Investment Regulation," (2016), available at https://www.unpri.org/download?ac=325.

[5] Principles for Responsible Investment, "Global Guide to Responsible Investment Regulation," (2016), available at https://www.unpri.org/download?ac=325.

[6] HM Government, Green Finance Strategy: Transforming Finance for a Greener Future (July 2019), available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/813656/190701_BEIS_Green_Finance_Strategy_Accessible_PDF_FINAL.pdf.

[7] UK Department for Business, Energy & Industrial Strategy and Chris Skidmore MP, "UK Becomes First Major Economy to Pass Net Zero Emissions Law: New target will require the UK to bring all greenhouse gas emissions to net zero by 2050" (June 27, 2019), available at https://www.gov.uk/government/news/uk-becomes-first-major-economy-to-pass-net-zero-emissions-law.

to strengthen the competitiveness of the UK financial sector."[8] The strategies employed to meet these objectives include three pillars: Greening Finance, Financing Green, and Capturing the Opportunity. The first pillar, Greening Finance, involves ensuring that climate and environmental factors are integrated into mainstream financial decision-making, including the evaluation and incorporation of current and future financial risks and opportunities associated with climate change and other environmental factors. Greening Finance also involves ensuring a robust market for green financial products. To meet these Greening Finance objectives, the UK government stated its expectation that all listed companies and large asset owners disclose in line with the TCFD by 2022. The second pillar, Financing Green, encourages the flow of capital into projects and solutions that will help the UK meet its long-term carbon-reduction goals. The third pillar, Capturing the Opportunity, aims to capture the economic opportunities associated with the growth of the green financial markets and commercial innovations that arise through the transition to a greener economy.

As part of efforts to achieve the first pillar of the Green Finance Strategy, the UK introduced a new Listing Rule LR 9.8.6(8)[9] in December 2020, which requires companies with a premium listing in the UK to state in their annual report, for financial years beginning on or after 1 January 2021, whether they comply with the TCFD's recommendations. Any non-compliance with the TCFD will have to also be explained in the annual report. Notably, LR 9.8.6(8) does not presently require third-party verification of ESG disclosures, although the FCA

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[8] HM Government, Green Finance Strategy: Transforming Finance for a Greener Future (July 2019), available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/813656/190701_BEIS_Green_Finance_Strategy_Accessible_PDF_FINAL.pdf, at 6.

[9] Https://www.handbook.fca.org.uk/handbook/LR/9/8.html.

has identified that it considers there to be value in third-party verification, and will continue to work towards coordinating a policy response in this regard.

In a poll conducted by the members of the GC100 (the General Counsel of the FTSE100 group of companies) in June 2021, 73 percent of respondents indicated that they will include a statement of full compliance with the recommendations of the TCFD, with the remainder indicating partial compliance. 75 percent of respondents also indicated that they will be seeking independent assurance of their TCFD-aligned disclosures, to be carried out by environmental consultants, sustainability ratings providers or large accounting firms.

The promulgation of the new listing rule followed the FCA's publication of a discussion paper on green finance in October 2018, and a consultation paper seeking views on the ambit of the rule in March 2020. Moving forward, the UK government has stated its intention[10] to "introduce mandatory reporting of climate-related financial information across the economy by 2025, with a significant portion of mandatory requirements in place by 2023," and issued a roadmap for establishing these disclosure requirements in November 2020.

To further this aim, the UK government issued an additional consultation paper in March 2021 in relation to extending TCFD-based reporting requirements to all UK companies that are currently required to produce a non-financial information statement under the Companies Act 2006 (broadly this includes UK companies and LLPs that have more than 500 employees and are listed or have an annual turnover of greater than £500 million). The government proposes that this requirement would enter into effect for financial years beginning on or after 6 April

[10] Https://www.gov.uk/government/publications/uk-joint-regulator-and-government-tcfd-taskforce-interim-report-and-roadmap.

2022, and that relevant companies and LLPs would have to report in line with the four overarching pillars of the TCFD recommendations. However, the current consultation paper proposals would not require certain scenario analyses to be undertaken, or the disclosure of information in line with TCFD's 11, more detailed recommendations. Separate consultations have also been issued on potential TCFD-alignment for issuers of standard listed equity shares and UK-authorised asset managers, life insurers, and regulated pension providers, with staggered implementation dates proposed for the various entity types. While these proposals are still in the consultation stage, the direction of regulatory travel and UK government support would suggest that they are likely to be adopted in substantially their current form.

The UK's Financial Conduct Authority issued a consultation paper in March 2020, primarily focused on enhancing requirements for premium listed companies and certain sovereign controlled companies to make climate-related disclosures.[11] The consultation draft proposes the introduction of a new listing rule requiring impacted companies to disclose whether and where they report in line with the TCFD's recommendations, or to explain why they do not report. While these proposals are still in the consultation stage, the direction of regulatory travel and UK government support suggests that they are likely to be adopted in substantially their current form.

The UK has also adopted regulations requiring certain companies to conduct energy efficiency audits and to disclose their energy consumption and GHG emissions. The Companies (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulation requires the disclosure of GHG

[11] Https://www.fca.org.uk/publications/consultation-papers/cp20-3-proposals-enhance-climate-related-disclosures-listed-issuers-and-clarification-existing.

emissions by quoted companies, large unquoted companies and large limited liability partnerships.[12] The Energy Savings Opportunity Scheme requires companies in the UK to carry out mandatory energy savings assessments by calculating their total energy consumption, carrying out energy audits and identifying where energy savings can be made.[13]

The UK Corporate Governance Code (the Code), issued by the Financial Reporting Council (the FRC), forms another piece of the ESG framework.[14] The Code consists of a set of principles of good governance in the areas of board leadership and company purpose, division of responsibilities between the board and the company's executive leadership, board composition, succession and evaluation, audit, risk and internal control, and executive and board remuneration. The Code does not impose rigid rules but rather provides flexibility through a set of principles for boards to use. It operates on the basis of "comply or explain" and applies to all companies with a premium listing, whether incorporated in the UK or elsewhere. Finally, the Code requires companies to include in their annual corporate reports and accounts a disclosure statement setting out how they have applied the principles.

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[12] Companies (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulation, available at https://www.legislation.gov.uk/uksi/2018/1155/pdfs/uksi_20181155_en.pdf.

[13] Https://www.gov.uk/guidance/energy-savings-opportunity-scheme-esos.

[14] UK Corporate Governance Code, available at https://www.frc.org.uk/directors/corporate-governance-and-stewardship/uk-corporate-governance-code.

The Companies Act imposes on directors a similar, but more general, duty to promote the success of a company.[15] In doing so, company directors must have regard to the impact of the company's operations on the community and the environment, and the likely consequences of any decision in the long term. The Chartered Governance Institute recently confirmed the increased attention that directors must pay to the company's employees, relationships with suppliers and customers, and their impact on the community and the environment.[16] The board should consider how the company is, and will be, contributing to environmental concerns relating to its operations and its supply chain. Directors should also contemplate how the company has engaged with the local community in which it operates.

The Companies Act[17] also mandates the directors of large- and medium-sized UK companies to prepare strategic reports for each financial year. These reports are required to contain, alongside the general risks and uncertainties facing the company, information about environmental matters (including the impact of the company's operations on the environment), the company's employees and social, community, and human rights issues. The strategic report also must contain (in the case of certain large companies)[18] a non-financial statement providing information relating to environmental matters (including the

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[15] Companies Act 2006 c.46, available at https://www.legislation.gov.uk/ukpga/2006/46/contents.

[16] Directors' General Duties under the Companies Act 2006: Guidance note, available at https://www.icsa.org.uk/knowledge/resources/directors-general-duties.

[17] Chapter 4A.

[18] (i) Large companies with over 500 employees and which are either (i) a traded company, (ii) a banking company, (iii) an authorised insurance company, or (iv) an insurance company.

impact of the company's operations on the environment), the company's employees, social matters, respect for human rights, and anti-corruption and anti-bribery matters.

The UK has also been proactive in addressing the "S" element of ESG in its disclosure regulations. The Equality Act 2010 mandates gender pay gap reporting in the UK for large employers (more than 250 relevant employees), and voluntary for smaller companies.[19] In addition, the voluntary "Think, Act, Report" framework prompts companies to collect data, take action to address gender pay gaps, and publish information on their progress.[20] The Modern Slavery Act of 2015 requires large commercial organizations to publicly state each year what actions they have taken to ensure their business and supply chains are slavery free.[21]

Looking to possible developments in the UK, in July 2021 the FRC published a statement of intent on ESG challenges.[22] The statement identifies measures that the FRC plans to take to attain a fully effective and efficient system of ESG reporting in the UK, and notes that the FRC will continue to monitor the approaches of boards with respect to ESG reporting, and will highlight whether changes need to be made to accounting standards to reflect the impact of ESG (specifically climate) issues on companies' financial statements.

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[19] Equality Act 2010, Ch.3 Equality of terms, Sec. 78 Gender pay gap information, available at https://www.legislation.gov.uk /ukpga/2010/15/contents.

[20] https://www.gov.uk/government/publications/think-act-report/think-act-report.

[21] Modern Slavery Act 2015, available at https://www.legislation.gov.uk/ukpga/2015/30/contents/enacted.

[22] Https://www.frc.org.uk/getattachment/691f28fa-4af4-49d7-a4f5-49ad7a2db532/FRC-LAB-ESG-Paper_2021.pdf.

The EU and EC's ESG efforts have accelerated in the past year, with the announcement of the European Green Deal prompting a wave of legislative and policy actions geared toward meeting its goals. In January 2020, the EC unveiled the European Investment Plan, with the goal to mobilizing at least €1 trillion of public and private investment over the next decade to enable Europe to transition to a climate neutral economy.[23] As part of the transition to carbon neutrality, the EU plan incorporates the "Just Transition Mechanism," a tool to ensure that the transition takes place in a fair and inclusive manner.

In March 2020, the EC proposed a new European Climate Law to ensure a climate neutral EU by 2050[24] and, in September 2020, presented its 2030 Climate Target Plan.[25] The Climate Target Plan proposes to reduce GHG emissions by at least 55 percent below 1990 levels by 2030, as a first step on the path to becoming climate neutral by 2050. In July 2021, the Commission adopted a package of proposals intended to help achieve that 55 percent target, known as the "Fit for 55"[26] package, which includes, amongst other policies, the introduction of a carbon border adjustment mechanism and reduced emissions

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[23] European Commission, "Financing the green transition: The European Green Deal Investment Plan and Just Transition Mechanism," (Jan. 14, 2020), available at https://ec.europa.eu/commission/presscorner/detail/en/ip_20_17.

[24] European Commission, "Proposal for a Regulation of the European Parliament and of the Council establishing the framework for achieving climate neutrality and amending Regulation (EU) 2018/1999 (European Climate Law)" (Mar. 4, 2020), available at https://eur-lex.europa.eu/legalcontent/EN/TXT/?qid=1588581905912&uri=CELEX:52020PC0080.

[25] European Commission, "2030 Climate Target Plan" (Sept. 17, 2020), available at https://ec.europa.eu/clima/policies/eu-climate-action/2030_ctp_en.

[26] Https://ec.europa.eu/commission/presscorner/detail/en/IP_21_3541.

allowances as part of the EU Emissions Trading Scheme. The EC will next begin to prepare more detailed legislative proposals to define how the goal can be achieved. In 2020, the Commission also issued a number of other strategies and plans in support of the Green Deal, including the European Industrial Strategy[27] and the Circular Economy Action Plan[28] (both in March), the Farm to Fork Strategy[29] and the EU Biodiversity Strategy[30] (both in May), and the EU combined strategies for energy system transformation to decarbonize the energy sector in July.[31]

One of the key workstreams to support the ambitions of the European Green Deal focuses on sustainable finance. Specifically, "the EU is examining how to integrate sustainability considerations into its financial policy framework in order to mobi-

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[27] European Commission, "European Industrial Strategy" (Mar. 10, 2020), available at https://ec.europa.eu/info/strategy/priorities-2019-2024/europe-fit-digital-age/european-industrial-strategy_en.

[28] European Commission, "Circular Economy Action Plan" (Mar. 11, 2020), available at https://ec.europa.eu/commission/presscorner/detail/en/fs_20_437.

[29] European Commission, "From Farm to Fork" (May 20, 2020), available at https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal/actions-being-taken-eu/farm-fork_en.

[30] European Commission, "EU Biodiversity Strategy for 2030" (May 20, 2020), available at https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal/actions-being-taken-eu/eu-biodiversity-strategy-2030_en.

[31] European Commission, "EU Energy System Integration Strategy" (July 8, 2020), available at https://ec.europa.eu/commission/presscorner/detail/en/fs_20_1295; "A Hydrogen Strategy for a climate neutral Europe" (July 8, 2020), available at https://ec.europa.eu/commission/presscorner/detail/en/fs_20_1296; and "European Clean Hydrogen Alliance" (July 8, 2020), available at https://ec.europa.eu/commission/presscorner/detail/en/fs_20_1297.

lise finance for sustainable growth."[32] In this regard, the EC announced its Strategy for Financing the Transition to a Sustainable Economy (Sustainable Finance Strategy)[33] in July 2021, which builds on the previously existing Action Plan on Financing Sustainable Growth (Action Plan) and the reports of the Technical Expert Group on Sustainable Finance (TEG). One of the core building blocks of the Sustainable Finance Strategy focuses on corporate disclosure of climate-related information, expanding on the proposals of the technical expert group on sustainable finance (TEG). TEG was formed in 2018 to assist the EC in evaluating certain key issues around sustainable finance. TEG published its final report on climate-related disclosures in January 2019,[34] and the European Commission then adopted new non-binding climate reporting guidelines based on the TEG report.[35] These guidelines include disclosure of the impact of a company's activities on the environment and society, as well as the business and financial risks a company faces due to its sustainability exposures (double materiality). The use of double materiality marks a potential contrast with the approach being considered by regulators in the U.S., where the materiality threshold for disclosures is usually discussed purely

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[32] European Commission, "Sustainable Finance" available at https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance_en.

[33] https://eur-lex.europa.eu/resource.html?uri=cellar:9f5e7e95-df06-11eb-895a-01aa75ed71a1.0001.02/DOC_1&format=PDF.

[34] European Commission, "Technical expert group on sustainable finance report on climate-related disclosures" (Jan. 10, 2019), available at https://ec.europa.eu/info/files/190110-sustainable-finance-teg-report-climate-relateddisclosures_en.

[35] European Commission, "Guidelines on reporting climate-related information" available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52019XC0620(01).

by reference to the business and financial risks a company faces.

The climate reporting guidelines "recognise that the content of climate-related disclosures may vary between companies according to a number of factors, including the sector of activity, geographical location and the nature and scale of climate-related risks and opportunities" and, as such, "a flexible approach is necessary. Companies and other organizations are strongly encouraged to continue to innovate and further improve climate-related reporting beyond the content of these guidelines."[36] The guidelines integrate the TCFD's recommendations and encourage companies to report on the risks that they face due to climate change and the risks that they pose to the climate resulting from their activities. Companies should also disclose their dependencies on natural, human, and social capitals, which might include natural resources such as water and minerals, as well as employees, suppliers, and other stakeholders. Companies are also encouraged to disclose climate-related opportunities.[37]

The Sustainable Finance Strategy identifies three key sources of mandatory disclosure requirements. The first of these is the Corporate Sustainability Reporting Directive (CSRD) proposal,[38] which seeks to build on the EU Non-Financial Disclosure Directive (NFRD). The NFRD came into force in Decem-

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[36] European Commission, "Guidelines on reporting climate-related information" available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52019XC0620(01).

[37] European Commission, "Guidelines on reporting climate-related information" available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52019XC0620(01).

[38] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52021PC0189&from=EN.

ber 2014 and Member States were required to transpose it into national law by 2016.[39] The NFRD imposes requirements on large public interest entities (namely EU-listed companies, insurance companies, and banks) to include a non-financial statement in their annual report. At a minimum, the non-financial information should cover environmental, social, and employee matters, human rights, anti-corruption, and bribery issues. In January 2020, the EC published a consultation seeking opinions on whether it should revise the non-financial reporting framework, including the NFRD. In February 2020, the Commission published a further consultation, and a majority of respondents support extending the application of the NFRD to a broader range of companies and establishing a common reporting standard for companies. The EC is expected to adopt legislation in line with the consultation report and adopted a proposal for the CSRD in April 2021. Under the proposal, the scope of sustainability reporting requirements would be extended to include all large companies, whether listed or not, and listed SMEs (who will face simpler standards). Affected companies will have to report sustainability issues from a variety of topics on a double materiality basis, with the introduction of a general EU-wide third party assurance requirement for reported sustainability information. The proposal would require reporting in accordance with EU-wide standards, which the Commission intends to adopt by October 2022.

Second, the EC's Action Plan on Financing Sustainable Growth (Action Plan) lays out the strategy for connecting finance with sustainability.[40] An important component of the Ac-

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[39] For more details on the Directive, including the text of the legislation: https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en.

[40] European Commission, "Action Plan: Financing Sustainable Growth" (Mar. 8, 2018), available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097.

tion Plan is the EU Taxonomy Regulation, which came into effect in July 2020.[41] The Taxonomy Regulation tasks the EC with establishing a list of environmentally sustainable activities, and defining technical screening criteria for each of six environmental objectives.[42] These criteria for the climate change adaptation and mitigation objectives were formally adopted for consideration by legislators by the EC in June 2021, and criteria for the remaining objectives will be established through a further delegated acts, which are due to be adopted by the EC by December 31, 2020 and published in 2022. Article 8 of the Taxonomy Regulation in particular requires certain companies (namely financial market participants and those subject to CSRD) to provide information to investors about the environmental performance of their assets and economic activities. In this regard, the EC adopted a delegated act in July 2021, which specifies the content, methodology, and presentation of information to be disclosed by large companies on their activities' alignments with the Taxonomy.

The third and final pillar identified in the Sustainable Finance Strategy is the Sustainable Finance Disclosure Regulation (SFDR). The SFDR imposes certain disclosure and transparency obligations on financial market participants in the EU, including certain content that firms must maintain on their website, information to be provided to investors, and periodic reporting requirements. The SFDR entered into force in De-

[41] Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (June 18, 2020), available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32020R0852.

[42] For more details on the Regulation, including the legislative text: https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/eu-taxonomy-sustainable-activities_en.

cember 2019, and most of its provisions became applicable on 10 March 2021. However, the publication of regulatory technical standards detailing the reporting requirements of the SFDR has been delayed, with a new target date set for the second half of 2021.

Alongside the publication of the Sustainable Finance Strategy in July 2021, the EC proposed a regulation for the creation of a voluntary EU Green Bond Standard (EU GBS) following a targeted consultation document.[43] The EC first proposed an EU GBS in 2018 as part of the Action Plan.[44]. In June 2021, the EC published the standard, and the European Parliament and European Council proposed a regulation to implement the EU GBS in August 2021. The consultation sought to assess the potential alignment of the EU GBS with the EU Taxonomy regulation and proposed mandatory reporting on the use of proceeds and on environmental impact. The EU GBS contains a concrete list of substantive activities that can be categorized as green. The proposed framework would also require mandatory post-issuance verification of the use of proceeds and external verification by reviewers who are registered with and supervised by the European Securities Markets Authority (ESMA). The EU GBS is not proposed to enter into legal effect until 2022 at the earliest, and, notably, the EU's own €250 billion green bond offering in 2021 will not be EU GBS compliant.

The Sustainable Finance Strategy, and its forerunner the Action Plan (together, the Action Plan), promotes the EC's goals of financing sustainable growth through a number of additional initiatives. The Action Plan encourages investment in sustainable projects through the Sustainable Europe Investment Plan

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[43] Https://ec.europa.eu/commission/presscorner/detail/en/ip_21_3405.

[44] Https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/eu-green-bond-standard_en.

(otherwise known as the European Green Deal Investment Plan),[45] Invest EU,[46] and other EU funds. The EC has also issued draft rules to clarify investment firms' duties to provide clients with clear advice on the social and environmental risks and opportunities associated with their investments.[47] The Action Plan calls for the development of amended sustainability benchmarks[48] and on July 17, 2020, the EC adopted new rules setting out minimum technical requirements for the methodology of EU climate benchmarks.[49] The benchmarks are designed

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[45] European Commission, "The European Green Deal Investment Plan and Just Transition Mechanism explained" (Jan. 14, 2020), available at https://ec.europa.eu/commission/presscorner/detail/en/qanda_20_24.

[46] European Commission, "What's next? The InvestEU Programme (2021-2027)" available at https://ec.europa.eu/commission/priorities/jobs growth-and-investment/investment-plan-europe-juncker-plan/whats-next-inv esteu-programme-2021-2027_en.

[47] European Commission, "Sustainable finance – obligation for investment firms to advise clients on social and environmental aspects of financial products" available at https://ec.europa.eu/info/law/better-regulation/have your-say/initiatives/12068-Strengthening-the-consideration-of-sustainability risks-and-factors-for-financial-products-Regulation-EU-2017-565. For an overview of the frameworks applicable to financial institutions and a discussion of a suggested roadmap for firms in the financial services sector making the transition to sustainable finance, see AFME and Latham & Watkins, "Governance, Conduct and Compliance in the Transition to Sustainable Finance" (Sept. 2020), available at https://www.lw.com/admin/Upload/Docu ments/AFME-Sustainable-Finance-Paper.pdf.

[48] Regulation (EU) 2019/2089 of the European Parliament and of the Council of 27 November 2019 amending Regulation (EU) 2016/1011 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks" (Nov. 27, 2019), available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX :32019R2089.

[49] European Commission, "Commission Delegated Regulation supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards the explanation in the benchmark statement of how envi-

to reduce the risk of "greenwashing" and to improve the transparency and comparability of information across benchmarks concerning climate-related information and a variety of ESG factors.

These examples are not isolated. Indeed, regulators and markets around the world are focused on the impact of climate change and other ESG factors, which in turn can be expected to impact their growth and the strength of their capital markets. For example, in September 2020, China's President Xi Jinping announced to the UN General Assembly China's commitment to become carbon neutral by 2060.[50] Other countries, including Austria, Bhutan, Canada, Chile, Costa Rica, Denmark, Fiji, Finland, France, Germany, Hungary, Iceland, Ireland, Japan, New Zealand, Norway, Portugal, Singapore, Slovakia, South Africa, South Korea, Spain, Sweden, Switzerland, and Uruguay have all made carbon neutrality pledges.[51] Certain jurisdictions, including Japan[52] and France,[53] have introduced further legislation aimed at increasing ESG disclosures, particularly for financial

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ronmental, social and governance factors are reflected in each benchmark provided and published" (July 17, 2020), available at https://ec.europa.eu/finance/docs/level-2-measures/benchmarks-delegated-act-2020-4744_en.pdf.

[50] Paul A. Davies, Michael D. Green, R. Andrew Westgate, and Jacqueline J. Yap, "China Pledges to Become Carbon Neutral by 2060" (Sept. 30, 2020), available at https://www.globalelr.com/2020/09/china-pledges-to-become-carbon-neutral-by-2060/#more-4354.

[51] Megan Darby and Isabelle Gerretsen, "Which countries have a net zero carbon goal?" Climate Home News (Sept. 17, 2020), available at https://www.climatechangenews.com/2020/09/17/countries-net-zero-climate-goal/.

[52] Https://www.environmental-finance.com/content/news/japans-fsa-to-launch-mandatory-esg-disclosures.html.

[53] Https://www.reuters.com/article/uk-climate-change-france-disclosure-idUKKCN2DY1KB.

institutions**.** As the focus on climate change and the broader array of ESG issues continues to grow around the world, the pressure will continue to build in the U.S. to take action on ESG issues. This pressure can be expected to increase the focus on ESG investments and associated disclosures.

§ 4:24 ESG and the role of stock exchanges and securities regulators globally

Stock exchanges around the world and the International Organization of Securities Commissions (IOSCO) are focused on sustainability challenges. In 2009, then-UN Secretary-General Ban Ki-moon formed the Sustainable Stock Exchanges Initiative (SSE), and in 2012 the New York Stock Exchange and Nasdaq signed on as partner exchanges. The SSE is a partnership among the UN Partnership Program of the PRI, the UN Conference on Trade and Development, the UN Global Compact, and the UN Environment Program Finance Initiative.[1] The SSE works with partner exchanges around the world that publicly commit to the SSE's mission "to build the capacity of stock exchanges and securities market regulators to promote responsible investment in sustainable development and advance corporate performance on environmental, social and governance issues."

The SSE has developed an action plan that articulates how securities regulators can work together in support of the UN Sustainable Development Goals and the creation of stronger, more resilient markets. The action plan recognizes that "sustainability issues can create financially material risks and opportunities for investors and may affect the resilience of the finan-

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[1] Sustainable Stock Exchanges Initiative, About the SSE, https://sseinitiative.org/about/about-the-sse/.

cial system as a whole."[2] It includes five action areas: training market participants on sustainability topics, facilitating enhanced board governance around environmental and social factors, guiding investors on ESG integration, strengthening disclosures of environmental and social information, and aiding the flow of investment toward the achievement of the UN Sustainable Development Goals. The action plan also includes five supporting actions to facilitate achievement of the action areas' goals: analysis, development of roadmaps for national or regional sustainable finance plans, sharing of information among securities regulators, development of standardized guidelines and frameworks, and collaborating with other relevant organizations in support of the UN Sustainable Development Goals.

IOSCO issued a Statement on Disclosure of ESG Matters by Issuers in January 2019 to stress the purposes of securities regulation, including protecting investors; ensuring the fairness, transparency, and efficiency of the markets, and reducing systemic risk.[3] The statement emphasizes the potential significance of ESG factors: "ESG matters, though sometimes characterized as non-financial, may have a material short-term and long-term impact on the business operations of the issuers as well as on risks and returns for investors and their investment and voting decisions."[4] The statement urges issuers to assess the materiality of ESG factors to their businesses and, when material, to dis-

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[2] SSE, "Securities Regulators and Sustainable Development" https://sseinitiative.org/securities-regulators/.

[3] International Organization of Securities Commissions, "Statement on Disclosure of ESG Matters by Issuers" (Jan. 18, 2019), available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD619.pdf.

[4] International Organization of Securities Commissions, "Statement on Disclosure of ESG Matters by Issuers" (Jan. 18, 2019), available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD619.pdf.

close the impact or potential impact on financial performance as well as the potential for value creation.

In June 2019, IOSCO hosted its first Sustainable Finance Network Stakeholder Meeting, which focused on four topics: the impact of sustainability on corporate risk management, sustainability factors in the investment decision-making process, sustainability in corporate reporting, and the role of security regulators with regard to all of these issues.[5] In June 2021, IOSCO issued a consultation[6] requesting feedback on proposed recommendations about sustainability-related regulatory and supervisory expectations for asset managers. The recommendations for securities regulators included the setting of clear and mandatory regulatory and supervisory expectations of asset managers in the sustainability sphere, increasing the enforcement capabilities of regulators, and the development of common sustainable finance related terms and definitions. The consultation also highlighted the current issues that face investors due to a lack of easily comparable ESG data, which was a factor behind IOSCO's public support for the work of the IFRS Foundation's International Sustainability Standards Board in the continued development of a globally accepted climate reporting standard (see below). The World Federation of Exchanges (WFE) responded to IOSCO's efforts, emphasizing the importance of ESG factors to the member exchanges: "ESG is one of the WFE's strategic priorities for 2019, and we have been proactively tackling the topic since 2014. We are pleased to see the importance placed on sustainability by IOSCO in recent months. We believe that securities regulators, in line with their

[5] IOSCO Holds First Sustainable Finance Network Stakeholder Meeting," Sustainable Stock Exchanges Initiative (June 19, 2019), available at https://sseinitiative.org/home-slider/iosco-holds-first-sustainable-finance-network-stakeholder-meeting/.

[6] Https://www.iosco.org/library/pubdocs/pdf/IOSCOPD679.pdf.

mandate of investor protection, can assist in moving towards the adoption of globally applicable, consistent standards, which are necessary to ensure effective, comparable disclosure and ESG labelling."[7]

A month prior, in May 2019, Nasdaq published its ESG Reporting Guide 2.0.[8] Nasdaq does not have specific ESG listing standards, but agrees with the SEC position that principles-based disclosure requirements will best serve investors: "Nasdaq believes that principles-based disclosure grounded in materiality allows reporting companies the degree of flexibility needed to provide investors with the proper amount and mix of information."[9] The reporting guide summarizes some of the key voluntary reporting frameworks and offers a roadmap for disclosure of the different ESG factors.[10] The roadmap provides

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[7] World Federation of Exchanges, "The World Federation of Exchanges Responds to IOSCO's Sustainable Finance Network" (June 11, 2019), quoting Nandini Sukumar, Chief Executive Officer, WFE, available at https://www.world-exchanges.org/news/articles/world-federation-exchangesresponds-ioscos-sustainable-finance-network.

[8] Nasdaq "ESG Reporting Guide 2.0: A Support Resource for Companies" (May 2019), available at https://business.nasdaq.com/marketinsite / 2019/Corp/Introducing-Nasdaq-ESG-Reporting-Guide-2.html.

[9] Nasdaq "ESG Reporting Guide 2.0: A Support Resource for Companies" (May 2019), available at https://business.nasdaq.com/marketinsite/2019/Corp/Introducing-Nasdaq-ESG-Reporting-Guide-2.html, quoting Ed Knight, Nasdaq EVP and General Counsel, Comment Letter to the SEC on Concept Release (Sept. 16, 2016).

[10] For example, under "Environmental," the road map identifies the following factors as potentially material and describes how they could be measured and disclosed: GHG emissions, emissions intensity, energy usage, energy intensity, energy mix, water usage, environmental operations, climate oversight by the board and by management, and climate risk mitigation. Under "Social," the road map identifies CEO pay ratio, gender pay ratio, employee turnover, gender diversity, temporary worker ratio, nondiscrimination, injury rates, global health and safety, child and forced labor, and human

context to explain what is measured, why, and how it is measured; why and how it is disclosed; and how it connects to the principal voluntary reporting frameworks. The reporting guide is an acknowledgement of the dynamic nature of ESG data collection and reporting and the rapid pace of change. Nasdaq issued its first ESG Reporting Guide in 2017. In explaining its reasons for issuing a second guide, Nasdaq stated, "The most important has to do with the evolving nature of the data itself. Not only is the ESG data set growing more robust, definitive, and 'mainstream' every day, but we are finding better ways to measure performance. In some ways, the ESG data universe is still expanding at an astounding rate. New topics are still emerging, and the connections between company operation and downstream impact are being made clear."[11]

As discussed previously, the SEC voted to approve Nasdaq's changes to its listing rules in August 2021, which mandates greater transparency at board level of diversity statistics Additional requirements were also placed on companies to either have, or offer a public explanation in a proxy statement or on the company website as to why they do not have, multiple "diverse" directors. The rule was opposed by SEC Commissioners Peirce and Elad Roisman, who suggested that it was outside the scope of the SEC's authority, and was quickly subject to legal challenges by private organizations. Commissioner Elad Roisman stated that while he "supports the goal of having more diverse and inclusive boards," he did not feel that the SEC had

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rights. Under "Governance," the factors identified are board diversity, board independence, incentivized pay, collective bargaining, supplier codes of conduct, ethics and anti-corruption, data privacy, ESG reporting, disclosure practices, and external assurance.

[11] Nasdaq "ESG Reporting Guide 2.0: A Support Resource for Companies" (May 2019), available at https://business.nasdaq.com/marketinsite/2019/Corp/Introducing-Nasdaq-ESG-Reporting-Guide-2.html, at 13.

undertaken its own "reasoned analysis" to evaluate the merits of the proposal.[12] Nevertheless, the changes were approved and SEC Chair Gensler stated that "[t]hese rules will allow investors to gain a better understanding of Nasdaq-listed companies' approach to board diversity, while ensuring that those companies have the flexibility to make decisions that best serve their shareholders." Indeed, the rules allows for flexibility for smaller companies which can meet the requirement with either (i) two female directors, or (ii) one female director and one Underrepresented Minority or LGBTQ+ director. Similarly, foreign issuers can meet the Board Diversity Objective with (i) two female directors, or (ii) one female director and one director who is from an underrepresented minority in the company's principal location or LGBTQ+. Pre-business combination SPACs are exempt from the requirements altogether.

[12] Latham & Watkins LLP, "SEC Approves Nasdaq's Board Diversity Proposal," available at https://www.globalelr.com/2021/08/sec-approves-nasdaqs-board-diversity-proposal/.

PART VI.
THE PRACTICAL POINTS OF ESG

§ 4:25 Shareholder activism

Shareholder proposals related to environmental and social issues have been a prominent feature of the proxy season landscape for the past several years. Between 2011 and 2016, governance-focused shareholder proposals outpaced environmental and social proposals. In contrast, in 2017, 2018, and 2019, the number of environmental and social proposals has exceeded governance proposals, according to an analysis published by

ISS in June 2019.[1] In 2020, for the fourth consecutive year, the majority of U.S. shareholder proposals (55 percent) filed were environmental and social-related.[2] ISS found the 30-plus majority vote count on core governance proposals "low by historical standards," while the 18 majority votes on environmental and social proposal was "historic."[3] Meanwhile, an early analysis of the 2021 proxy season by Georgeson found that a record-setting number of environmental and social proposals passed, a 50 percent increase compared to the total number of such proposals receiving majority support during the 2020 proxy season.[4]

The increased shareholder support for environmental and social proposals appears to reflect the growing mainstream interest in and support of environmental and social issues. According to ISS:

> Historically, investors treated environmental and social issues very differently compared to governance proposals, with many abstaining from voting on these matters, and even more being very reluctant to support such proposals

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[1] Kosmas Papadopoulos, "Early Review of 2019 US Proxy Season Vote Results," ISS Analytics (June 5, 2019), available at https://www.issgovernance.com/file/publications/ISS_Early_Review_of_2019_US_Proxy_Season_Vote_Results.pdf.

[2] ISS, "2020 U.S. Environmental & Social Shareholder Proposals Proxy Season Review," available at https://insights.issgovernance.com/posts/2020-u-s-environmental-social-shareholder-proposals-proxy-season-review/.

[3] Patrick McGurn, "Key Highlights from the 2020 U.S. Proxy Season," ISS Analytics (June 19, 2020), available at https://www.issgovernance.com/file/publications/ISS-Key-Highlights-from-the-2020-US-Proxy-Season.pdf

[4] Hannah Orowitz, "And Early Look at the 2021 Proxy Season," Georgeson, available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf

> that may have appeared disconnected from investment management fundamentals. However, as ESG integration takes hold, recent voting trends indicate that we are entering a new era, whereby investors no longer compartmentalize environmental and social issues as a separate category from governance shareholder proposals. We are now dealing with ESG shareholder proposals, and every proposal type is evaluated based on its merits and relative to company and industry practice, without the mental barrier of the "E&S" moniker blocking investors' view from these matters.[5]

ISS reports that companies appear more likely to engage with proponents of environmental and social shareholder proposals than they were several years ago. Starting with increasing trends in 2019, many companies agreed to implement environmental and social proposals in 2019, leading to proponents' withdrawal of a record number of such proposals at that time.[6] Also in 2019, the number of Fortune 100 companies voluntarily reporting on their sustainability commitments increased from 29 percent in 2016 to 69 percent in 2019.[7] This increased shareholder focus on environmental and social issues and companies' corresponding responses reflects the growing agreement that

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[5] Kosmas Papadopoulos, "Early Review of 2019 US Proxy Season Vote Results," ISS Analytics (June 5, 2019), available at https://www.issgovernance.com/file/publications/ISS_Early_Review_of_2019_US_Proxy_Season_Vote_Results.pdf, at 5.

[6] Kosmas Papadopoulos, "Early Review of 2019 US Proxy Season Vote Results," ISS Analytics (June 5, 2019), available at https://www.issgovernance.com/file/publications/ISS_Early_Review_of_2019_US_Proxy_Season_Vote_Results.pdf.

[7] EY Center for Board Matters, "Five takeaways from the 2019 proxy season" (July 2019), available at https://assets.ey.com/content/dam/ey-sites/ey-com/en_us/topics/cbm/ey-cbm-2019-proxy-season-preview.pdf.

environmental and social issues were becoming mainstream business concerns. Indeed, the discussion of environmental and social issues does not end with the annual meeting. According to a Harvard Law School forum addressing the 2019 proxy season, "Investor conversations around board oversight and company management of environmental and social (E&S) risks and opportunities have become a year-round dialogue."[8]

The 2020 proxy season saw a further uptick in shareholder proposals focused on environmental and social issues. In 2020, for the fourth consecutive year, the majority of U.S. shareholder proposals (55 percent) filed were environmental and social-related.[9] According to Broadridge and PwC, overall shareholder support for social and environmental proposals increased from 25 percent in 2019 to 27 percent in 2020.[10]

Among majority-supported shareholder proposals in 2020, 66.7 percent were governance-related and nearly all of the remaining were environmental- and social-related.[11] Specifically, 22.2 percent of the majority-supported proposals were social-

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[8] Erica Lukoski et al., 2019 Proxy Season Takeaways," Harvard Law School Forum on Corporate Governance and Financial Regulation (July 27, 2019), available at https://corpgov.law.harvard.edu/2019/07/27/2019-proxyseason-takeaways/.

[9] ISS, "2020 U.S. Environmental & Social Shareholder Proposals Proxy Season Review," available at https://insights.issgovernance.com/posts/2020-u-s-environmental-social-shareholder-proposals-proxy-season-review/.

[10] Broadridge and PwC, "2020 Proxy Season Review," available at https://www.pwc.com/us/en/governance-insights-center/publications/assets/pwc-and-broadridge-2020-proxy-season-review.pdf.

[11] Brianna Castro et. al., "2020 Proxy Season Review," Glass Lewis (2020), available at https://www.glasslewis.com/wp-content/uploads/2020/09 /2020-Proxy-Season-Review-United-States.pdf, at 29.

related and 9.3% were environmental.[12] This level of support for environmental proposals is significant because in the 2019 season, no such proposals received majority support.[13] In the 2020 season, a proposal submitted to a major energy company "seeking reporting on climate lobbying aligned with Paris Agreement goals" received 53.9 percent support.[14] A proposal to another energy company "seeking a report assessing the public health risks of expanding petrochemical operations and investments in areas increasingly prone to climate change-induced storms, flooding and sea level rise" also received 53.9 percent support.[15]

ESG proposals, and support for those proposals, grew even further in 2021, in large part bolstered by signals of support for ESG issues from major investors, including BlackRock, Vanguard, and State Street as well as pressure from organizations such as As You Sow, Climate Action + and the Net Zero Asset Managers Initiative. Early disclosures by BlackRock and Van-

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[12] *Ibid.* In total, 54 shareholder proposals received majority shareholder support, 17 of which were environmental or social in nature.

[13] Hannah Orowitz et al., "An Early Look at the 2020 Proxy Season," Harvard Law School Forum on Corporate Governance and Financial Regulation (July 10, 2020), available at https://corpgov.law.harvard.edu/2020/06/10/an-early-look-at-the-2020-proxy-season/#7b.

[14] Hannah Orowitz et al., "An Early Look at the 2020 Proxy Season," Harvard Law School Forum on Corporate Governance and Financial Regulation (July 10, 2020), available at https://corpgov.law.harvard.edu/2020/06/10/an-early-look-at-the-2020-proxy-season/#7b.

[15] Hannah Orowitz et al., "An Early Look at the 2020 Proxy Season," Harvard Law School Forum on Corporate Governance and Financial Regulation (July 10, 2020), available at https://corpgov.law.harvard.edu/2020/06/10/an-early-look-at-the-2020-proxy-season/#7b.

guard indicate a significant level of support for environmental and social proposals during the first quarter of 2021.[16]

As of August 2021, over 30 environmental and social proposals had received majority support, exceeding last year's record by roughly 50 percent.[17] A shareholder proposal regarding plastic pollution received 81 percent at Dupont, which is one of the highest records seen to date. Additionally, at least six of these proposals were unopposed by the boards, such as those of General Electric and Bunge Limited.[18]

Climate change was at the forefront of shareholder proposals, with nearly a third directed at oil and natural gas companies, electric utilities, and the transportation sector.[19] Approximately 36 percent of environmental proposals that reach a vote passed, representing a 50 percent increase in the previous year's passage rate. An additional 92 environmentally focused proposals were withdrawn, compared to 39 in 2020,[20] potentially as

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[16] BlackRock's stewardship report is available at https://www.blackrock.com/corporate/literature/publication/blk-qrtly-stewardship-report-q1-2021.pdf; Vanguard Investment Stewardship Insights; available at https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/INSCHART_052021.pdf.

[17] "An early look at the 2021 proxy season," Georgeson, available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf.

[18] 2021 Proxy Season Review, Shirley Westcott, Alliance Advisors, available at https://corpgov.law.harvard.edu/2021/08/05/2021-proxy-season-review/.

[19] 2021 Proxy Season Review, available at https://corpgov.law.harvard.edu/2021/08/05/2021-proxy-season-review/#1.

[20] 021 Proxy Season Review, available at https://corpgov.law.harvard.edu/2021/08/05/2021-proxy-season-review/#1; "2021 Proxy Season Review: Shareholder Proposals on Environmental Matters," https://corpgov

a result of companies favoring direct engagement with the shareholder rather than taking the proposal to a vote. A new initiative known as Say on Climate, advanced by the The Children's Investment Fund Management (TCI), proposed providing shareholders with the opportunity to approve or disapprove of a company's publicly available climate policies and strategies. While no Say on Climate proposals received majority support this season, Moody's Investor Service and S&P Global supported TCI's campaign by holding votes on their climate transition plans, which received over 90% support.[21] While BlackRock expressed support for Say on Climate initiatives on the basis that it would accelerate companies' progress on climate risk management, Vanguard rejected the proposal on the grounds that it displayed short-term thinking to a long-term issue and it delegated oversight responsibilities to shareholders.[22] This type of proposal will likely make another appearance in future proxy seasons.

This year, as referenced above, the proxy battle victory of a small activist investor firm made headlines when it successfully installed new directors on the Board of an international oil and

.law.harvard.edu/2021/08/11/2021-proxy-season-review-shareholder-proposals-on-environmental-matters/.

[21] "An early look at the 2021 proxy season," Georgeson, available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf.

[22] See BlackRock's 2021 vote bulletins on Charter Communications and Moody's at https://www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-charter-communications-may-2021.pdf and https://www.blackrock.com/corporate/literature/press-release/blk-vote-bulletin-moodys-apr-2021.pdf; Vanguard Investment Stewardship Insights; available at https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/INSCHART_052021.pdf.

gas conglomerate to reduce its carbon footprints.[23] With only 0.02 percent of the company's shares, the activist convinced the three largest institutional shareholders BlackRock, Vanguard and State Street — who collectively held nearly 20 percent of voting shares — to back up its campaign.[24] In its investor presentation, the activist argued that the oil and gas company "still has no credible plan to protect value in an energy transition" and that therefore it requires new directors to "Gradually but purposefully [reposition] the company to succeed in a decarbonizing world."[25] The campaign's success was hailed as a "sea change" and "a new course for ESG advocates."[26] However, it remains to be seen whether large companies will drastically change courses after activist campaigns such as this.[27]

Board diversity was another important focus which started to take root during the 2020 proxy season. The New York City Comptroller's Office launched its Board Accountability Project 3.0 campaign. The Comptroller's Office submitted shareholder

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[23] Matt Phillips, "Exxon's Board Defeat Signals the Rise of Social-Good Activists," (June 9, 2021), The New York Times, available at https://www.nytimes.com/2021/06/09/business/exxon-mobil-engine-no1-activist.html. See also Billy Nauman et al., "Exxon Shareholder Victory Charts New Course for ESG Advocates" (May 28, 2021), Financial Times, available at https://www.ft.com/content/965ecd0d-821c-4f76-89f7-7f8cb4a649f6.

[24] Matt Phillips, "Exxon's Board Defeat Signals the Rise of Social-Good Activists" (June 9, 2021), The New York Times, available at https://www.nytimes.com/2021/06/09/business/exxon-mobil-engine-no1-activist.html.

[25] Engine No. 1, "Reenergizing ExxonMobil – Investor Presentation," (May 2021), available at https://reenergizexom.com/wp-content/uploads/2021/05/Investor-Presentation-May-2021-v2.pdf.

[26] Billy Nauman et. al., "Exxon Shareholder Victory Charts New Course for ESG Advocates" (May 28, 2021), Financial Times, available at https://www.ft.com/content/965ecd0d-821c-4f76-89f7-7f8cb4a649f6.

[27] Ibid.

proposals to 17 companies, and upon receipt of the shareholder proposals, 13 of the 17 companies implemented Rooney Rule policies.[28] Those 13 companies also extended such a policy to external CEO searches.[29]

The Social pillar of ESG, particularly as it relates to diversity, equity and inclusion featured prominently among shareholder proposals. The New York City Comptroller spearheaded the campaign for diverse director candidates as part of its Boardroom Accountability Project 3.0 with a letter requesting 67 S&P 100 companies to publicly disclose the company's EEO-1 report. The comptroller withdrew its proposals due to company compliance with the request.[30] Of the four proposals voted on relating to board and executive diversity, three received over 70 percent support with the fourth occurring at a controlled company. Various investors, including Vanguard, State Street, JPMorgan Asset Management, and Alliance Bernstein, indicated that they would begin to hold nominating committee chairs accountable this year or next if their boards fail to disclose or lack racial/ethnic diversity. As discussed below, proxy advisory firms voiced a similar approach. As of August 2021, of the S&P

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[28] Hannah Orowitz et al., "An Early Look at the 2020 Proxy Season," Harvard Law School Forum on Corporate Governance and Financial Regulation (July 10, 2020), available at https://corpgov.law.harvard.edu/2020/06/10/an-early-look-at-the-2020-proxy-season/#7b. Concerning the "Rooney Rule,"

[29] Hannah Orowitz et al., "An Early Look at the 2020 Proxy Season," Harvard Law School Forum on Corporate Governance and Financial Regulation (July 10, 2020), available at https://corpgov.law.harvard.edu/2020/06/10/an-early-look-at-the-2020-proxy-season/#7b.

[30] "An early look at the 2021 proxy season," Georgeson, available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf; "An early look at the 2021 proxy season," 2021 Proxy Season Review, available at https://corpgov.law.harvard.edu/2021/08/05/2021-proxy-season-review/#1.

500 firms that filed 2021 proxy statements, 71 percent disclosed the racial/ethnic composition of their boards.[31] Four proposals relating to reporting on workforce diversity, equity and inclusion practices also passed, with the proposal submitted at First Solar receiving 91.2 percent support.[32] [33]

A novel request for racial equity audits were introduced during this proxy season. Of the 12 proposals submitted, 8 voted on received an average of 31 percent support. Glass, Lewis & Co. (Glass Lewis) generally voted in favor of these proposals based on their ability to reduce high-profile controversies, while ISS found that the companies had taken other meaningful action to address racial inequities.[34]

Shareholder proposals relating to political contributions increased to 74 from 70 in 2020. Support for those proposal grew to 48.1 percent from 38.6 percent in 2020 and included six majority votes. In somewhat of a departure from past practice, BlackRock and Vanguard stated that they would consider voting in favor of these proposals where company practice was inconsistent with the company's publicly stated strategies.[35]

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[31] 2021 Proxy Season Review, available at https://corpgov.law.harvard.edu/2021/08/05/2021-proxy-season-review/#1.

[32] "An early look at the 2021 proxy season," Georgeson, available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf.

[33] "Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8," SEC Release No. 34-89964 (Sept. 23, 2020), available at https://www.sec.gov/rules/final/2020/34-89964.pdf.

[34] 2021 Proxy Season Review, available at https://corpgov.law.harvard.edu/2021/08/05/2021-proxy-season-review/#1.

[35] 2021 Proxy Season Review, available at https://corpgov.law.harvard.edu/2021/08/05/2021-proxy-season-review/#1.

Governance-related proposals did not see any significant changes or novel approaches as compared to last year.[36] 36 of the 237 proposals voted upon as of June 2021 passed, the majority of which related to written consent, special meetings, proxy access, and independent board chairs.

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[36] "An early look at the 2021 proxy season," Georgeson, available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf; "An early look at the 2021 proxy season," Georgeson, available at https://www.georgeson.com/us/Documents/Georgeson-Early-Proxy-Season-Review.pdf.

§ 4:26 ESG guidelines by proxy advisory firms

Proxy advisory firms play an important role in promoting ESG issues by providing "recommendations to institutional investors on how to vote at shareholder meetings on issues such as climate change, executive pay and board composition."[1] Two proxy advisory firms command an estimated 97 percent of the U.S. market share: ISS and Glass Lewis.[2] Of the two, ISS holds about 61 percent of the market.[3]

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[1] ShareAction and Charities Responsible Investment Network, "Another Link in the Chain: Uncovering the Role of Proxy Advisors," (Aug. 2019), available at https://shareaction.org/wp-content/uploads/2020/02/Another-Link-in-the-Chain-Uncovering-the-Role-of-Proxy-Advisors.pdf.

[2] ShareAction and Charities Responsible Investment Network, "Another Link in the Chain: Uncovering the Role of Proxy Advisors," (Aug. 2019), available at https://shareaction.org/wp-content/uploads/2020/02/Another-Link-in-the-Chain-Uncovering-the-Role-of-Proxy-Advisors.pdf.

[3] ShareAction and Charities Responsible Investment Network, "Another Link in the Chain: Uncovering the Role of Proxy Advisors," (Aug. 2019), available at https://shareaction.org/wp-content/uploads/2020/02/Another-Link-in-the-Chain-Uncovering-the-Role-of-Proxy-Advisors.pdf.

ISS recently acquired several research firms to further its ESG efforts, including the investment arm of environmental advisory firm South Pole Group and the ESG research and consulting firm IW Financial.[4] It also acquired leading ESG rating and research agency Oekom Research AG in 2018.[5]

ISS launched an Environmental & Social Quality Score in 2018, which it describes as "a data-driven approach to measuring the quality of corporate disclosures on environmental and social issues, including sustainability governance, and to identify key disclosure omissions."[6] The Quality Score covers approximately 4,700 companies across 24 industries that ISS views "as being most exposed to E&S risks, including: Energy, Materials, Capital Goods, Transportation, Automobiles & Components, and Consumer Durables & Apparel."[7] The Quality Score evaluates "ESG risks via the level of corporate disclo-

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[4] ShareAction and Charities Responsible Investment Network, "Another Link in the Chain: Uncovering the Role of Proxy Advisors," (Aug. 2019), available at https://shareaction.org/wp-content/uploads/2020/02/Another-Link-in-the-Chain-Uncovering-the-Role-of-Proxy-Advisors.pdf.

[5] ShareAction and Charities Responsible Investment Network, "Another Link in the Chain: Uncovering the Role of Proxy Advisors," (Aug. 2019), available at https://shareaction.org/wp-content/uploads/2020/02/Another-Link-in-the-Chain-Uncovering-the-Role-of-Proxy-Advisors.pdf.

[6] Institutional Shareholder Services, "Environmental & Social Disclosure QualityScore FAQ," available at https://www.issgovernance.com/file/faq/Environmental-Social-QualityScore-FAQ.pdf.

[7] Institutional Shareholder Services, "Environmental & Social Disclosure QualityScore FAQ," available at https://www.issgovernance.com/file/faq/Environmental-Social-QualityScore-FAQ.pdf.

sures, utilizing 380 industry-specific factors and 10 relative scores developed for easy comparison."[8]

ISS' current U.S. Proxy Voting Guidelines focus on social and environmental issues, which include "consumer and product safety, environment and energy, labor standards and human rights, workplace and board diversity, and corporate political issues."[9] For climate change, ISS generally recommends voting for "resolutions requesting that a company disclose information on the financial, physical, or regulatory risks it faces related to climate change on its operations and investments or on how the company identifies, measures, and manages such risks."[10] It also recommends voting for "proposals requesting that a company report on its energy efficiency," "requests for reports on the feasibility of developing renewable energy resources," and "requests for reports on policies and/or the potential (community) social and/or environmental impact of company operations."[11]

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[8] Open: Factset, "ISS ESG Environmental & Social Disclosure QualityScore," available at https://open.factset.com/products/iss-esg-environmental-and-social-disclosure-qualityscore/en-us.

[9] Institutional Shareholder Services, "United States Proxy Voting Guidelines Benchmark Policy Recommendations" (effective for meetings on or after Feb. 1, 2021), available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[10] Institutional Shareholder Services, "United States Proxy Voting Guidelines Benchmark Policy Recommendations" (effective for meetings on or after Feb. 1, 2021), available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[11] Institutional Shareholder Services, "United States Proxy Voting Guidelines Benchmark Policy Recommendations" (effective for meetings on or after Feb. 1, 2021), available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

The Proxy Voting Guidelines generally recommend voting in favor of "requests for reports on a company's efforts to diversify the board."[12] Similarly, they generally recommend affirmative votes on proposals "asking a company to increase the gender and racial minority representation on its board," and vote case by case for "requests for reports on a company's pay data by gender or race/ethnicity, or a report on a company's policies and goals to reduce any gender, race, or ethnicity pay gap."[13] Furthermore, the Guidelines generally recommend voting for "proposals to link, or report on linking, executive compensation to sustainability (environmental and social) criteria."[14]

ISS has published specialty policies on socially responsible investment, sustainability, and climate. The Socially Responsible Investment Proxy Voting Guidelines emphasize that investors are recognizing that "sustainability or environmental, social, and corporate governance (ESG) factors could present material risks to portfolio investments."[15] It provides a frame-

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[12] Institutional Shareholder Services, "United States Proxy Voting Guidelines Benchmark Policy Recommendations" (effective for meetings on or after Feb. 1, 2021), available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[13] Institutional Shareholder Services, "United States Proxy Voting Guidelines Benchmark Policy Recommendations" (effective for meetings on or after Feb. 1, 2021), available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[14] Institutional Shareholder Services, "United States Proxy Voting Guidelines Benchmark Policy Recommendations" (effective for meetings on or after Feb. 1, 2021), available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[15] Institutional Shareholder Services, "United States Socially Responsible Investment Proxy Voting Guidelines 2021 Policy Recommendations," available at https://www.issgovernance.com/file/policy/active/specialty/Sustainability-US-Voting-Guidelines.pdf.

work "that are consistence with the objectives of sustainability-minded investors and fiduciaries."[16]

The Sustainability Proxy Voting Guidelines provide a framework that "seeks to promote support for recognized global governing bodies promoting sustainable business practices advocating for stewardship of environment, fair labor practices, nondiscrimination, and the protection of human rights."[17] The ISS Sustainability Advisory Services will generally "vote against or withhold from directors individually, committee members, or the entire board" for "failure to adequately guard against or manage ESG risks" or for "a lack of sustainability reporting in the company's public documents and/or website in conjunction with a failure to adequately manage or mitigate ESG risks."[18] It will also vote against or withhold votes from certain incumbent nominees who serve as the chair of the board or of the nominating committee if the board lacks at least one female director.[19]

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[16] Institutional Shareholder Services, "United States Socially Responsible Investment Proxy Voting Guidelines 2021 Policy Recommendations," available at https://www.issgovernance.com/file/policy/active/specialty/Sustainability-US-Voting-Guidelines.pdf.

[17] Institutional Shareholder Services, "United States Sustainability Proxy Voting Guidelines 2021 Policy Recommendations," available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[18] Institutional Shareholder Services, "United States Sustainability Proxy Voting Guidelines 2021 Policy Recommendations," available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

[19] Institutional Shareholder Services, "United States Sustainability Proxy Voting Guidelines 2021 Policy Recommendations," available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

In March 2020, ISS published the U.S. Climate Voting Policy.[20] The Climate Voting Policy uses a scorecard approach to provide "an actionable, transparent framework for investors to exercise their voting rights with reference to their portfolio companies' climate disclosures and performance."[21] The Climate Voting Policy is "based on principles developed from widely recognized international frameworks, such as the TCFD's disclosure requirements."[22] If a board fails to sufficiently oversee, manage, or guard against material climate risk, the policy may recommend adverse votes on the reelection of board members.[23]

Glass Lewis uses data and ratings from Sustainalytics — a provider of ESG research — in the ESG Profile section of its standard Proxy Paper reports for large cap companies or in instances where it has identified "material oversight issues."[24] The

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[20] Institutional Shareholder Services, "United States Climate Proxy Voting Guidelines 2020 Policy Recommendations," available at https://www.issgovernance.com/file/policy/active/specialty/Climate-US-Voting-Guidelines.pdf.

[21] Institutional Shareholder Services, "Policy Supports Investors Choosing to Integrate Climate Performance & Disclosure into their Proxy Voting," available at https://www.issgovernance.com/iss-launches-climate-voting-policy/.

[22] Institutional Shareholder Services, "Policy Supports Investors Choosing to Integrate Climate Performance & Disclosure into their Proxy Voting," available at https://www.issgovernance.com/iss-launches-climate-voting-policy/.

[23] Institutional Shareholder Services, "United States Climate Proxy Voting Guidelines 2020 Policy Recommendations," available at https://www.issgovernance.com/file/policy/active/specialty/Climate-US-Voting-Guidelines.pdf.

[24] Harvard Law School Forum on Corporate Governance, "Glass Lewis, ISS, and ESG," (July 3, 2019), available at https://corpgov.law.harvard.edu/2019/07/03/glass-lewis-iss-and-esg/.

goal is "to provide summary data and insights that can be used by Glass Lewis clients as part of their investment decision-making, including aligning proxy voting and engagement practices with ESG risk management considerations."[25] The Glass Lewis evaluation rates companies on a matrix that balances overall "ESG Performance" against the highest level of "ESG Controversy."[26] The evaluation model notes that "some companies involved in particular product areas are naturally deemed higher risk."[27]

Glass Lewis released a practical guide to address investor concerns after COVID-19.[28] For boards, "there is particular risk in the lack of age and gender diversity among company directors" due to the health concerns.[29] The pandemic may inspire more companies to look harder at "emerging, black-swan and

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[25] Harvard Law School Forum on Corporate Governance, "Glass Lewis, ISS, and ESG," (July 3, 2019), available at https://corpgov.law.harvard.edu/2019/07/03/glass-lewis-iss-and-esg/.

[26] Harvard Law School Forum on Corporate Governance, "Glass Lewis, ISS, and ESG," (July 3, 2019), available at https://corpgov.law.harvard.edu/2019/07/03/glass-lewis-iss-and-esg/.

[27] Harvard Law School Forum on Corporate Governance, "Glass Lewis, ISS, and ESG," (July 3, 2019), available at https://corpgov.law.harvard.edu/2019/07/03/glass-lewis-iss-and-esg/.

[28] Glass Lewis, "COVID-19: The New Rules for ESG," (May 18, 2020), available at https://higherlogicdownload.s3.amazonaws.com/GOVERNANCEPROFESSIONALS/a8892c7c-6297-4149-b9fc-378577d0b150/UploadedImages/COVI D_New_Rules_for_ESG.pdf.

[29] Glass Lewis, "COVID-19: The New Rules for ESG," (May 18, 2020), available at https://higherlogicdownload.s3.amazonaws.com/GOVERNANCEPROFESSIONALS/a8892c7c-6297-4149-b9fc-378577d0b150/UploadedImages/COVI D_New_Rules_for_ESG.pdf.

long-term risks."[30] Glass Lewis predicted a sharp increase in shareholder proposals on ESG in 2020, and said that "[c]ompanies should prepare for shareholder concerns and questions around climate risk to reach record levels next year."[31]

Previously, proxy advisory firms like ISS and Glass Lewis enjoyed a broad exemption with respect to whether their advice would be subject to the full panoply of the SEC's rules relating to proxy solicitations. In July 2020, the SEC adopted amendments to the proxy rules that subject proxy voting advice to the proxy solicitation rules.[32] The amendments condition exemptions from those rules for proxy advisory firms — such as ISS and Glass Lewis — on disclosure of conflicts of interest and adoption of principles-based policies to make proxy voting advice available to the subject companies and to notify clients of company responses.[33] The amendments also include two nonexclusive safe harbors to satisfy the conditions of the exemptions.[34] In response to this rule, Glass Lewis announced that it

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[30] Glass Lewis, "COVID-19: The New Rules for ESG," (May 18, 2020), available at https://higherlogicdownload.s3.amazonaws.com/GOVERNANCEPROFESSIONALS/a8892c7c-6297-4149-b9fc-378577d0b150/UploadedImages/COVI D_New_Rules_for_ESG.pdf.

[31] Glass Lewis, "COVID-19: The New Rules for ESG," (May 18, 2020), available at https://higherlogicdownload.s3.amazonaws.com/GOVERNANCEPROFESSIONALS/a8892c7c-6297-4149-b9fc-378577d0b150/UploadedImages/COVI D_New_Rules_for_ESG.pdf.

[32] Securities and Exchange Commission, "Exemptions from the Proxy Rules for Proxy Voting Advice (Conformed to Federal register version)," available at https://www.sec.gov/rules/final/2020/34-89372.pdf.

[33] Securities and Exchange Commission, "Exemptions from the Proxy Rules for Proxy Voting Advice (Conformed to Federal register version)," available at https://www.sec.gov/rules/final/2020/34-89372.pdf.

[34] Securities and Exchange Commission, "Exemptions from the Proxy Rules for Proxy Voting Advice (Conformed to Federal register version)," available at https://www.sec.gov/rules/final/2020/34-89372.pdf.

would include "unedited company feedback on its research . . . with all its proxy research papers" and will deliver that information "directly to the voting decision makers at every investor client."[35] Glass Lewis stated that the new report will allow companies to "directly express their differences and unfiltered opinions on Glass Lewis' research and recommendations."[36]

ISS, by contrast, brought a suit against the SEC challenging the new amendments.[37]

The 2021 voting guidelines published by ISS and Glass Lewis in November 2020 (as referred to above) reflect an increased focus on social and environmental matters. With respect to board-level ethnic and racial diversity, ISS adopted a two-step approach to highlight the lack of diversity in its 2021 research reports on U.S. companies, as was already its practice in respect of board-level gender diversity. ISS will begin recommending against the chair of the nominating committee of a board that has not identified ethnic or racially diverse board members in the absence of any mitigating circumstances such as a firm commitment to diversity. With respect to environmental risks, the ISS revised voting guidelines also recommend, in extraordinary circumstances, voting against individual directors, specific

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[35] Glass Lewis, "Glass Lewis Announces that Company Opinions are Now Included with Research and Voting Recommendations," available at https://www.glasslewis.com/report-feedback-statement-included-withresearch/.

[36] Glass Lewis, "Glass Lewis Announces that Company Opinions are Now Included with Research and Voting Recommendations," available at https://www.glasslewis.com/report-feedback-statement-included-with-research/.

[37] Reuters, "Proxy Adviser ISS to Push Ahead with Lawsuit Against SEC over New Rule," available at https://www.reuters.com/article/us-isssec/proxy-adviser-iss-to-push-ahead-with-lawsuit-against-sec-over-new-ruleid USKCN25934B.

board committee members, or the whole board due to material failures of risk oversight, including "demonstrably poor risk oversight of environmental and social issues, including climate change."[38]

The ISS voting guidelines recommend a case-by-case approach on proposals that relate to linking executive compensation to sustainability (environmental or social) criteria, considering factors such as:

- The scope and prescriptive nature of the proposal
- Whether the company has significant and/or persistent controversies or regulatory violations regarding social and/or environmental issues
- Whether the company has management systems and oversight mechanisms in place regarding its social and environmental performance
- The degree to which industry peers have incorporated similar non-financial performance criteria in their executive compensation practices
- The company's current level of disclosure regarding its environmental and social performance

In regard to board-level gender diversity, Glass Lewis' revised voting guidelines recommend voting against the nominating committee chair of a board that has fewer than one female director in 2021 and two female directors, starting with shareholder meetings held after January 1, 2022. Glass Lewis will also flag companies if their boards have fewer than two female

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[38] ISS 2021 United States Proxy Voting Guidelines, p.12, available at https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf.

directors. Glass Lewis did not issue a recommendation regarding board-level ethnic or racial diversity, but instead indicated that it would begin tracking company disclosures on board diversity, including the ethnic and racial composition of the board.

Additionally, the guidelines stipulate that as of 2021, Glass Lewis will highlight any lack of clear disclosure regarding board-level oversight of material environmental and social issues and as of 2022 will begin recommending votes against the governance committee chair of companies that fail to provide explicit disclosure on these issues.[39]

Glass Lewis 2021 ESG Initiatives also contained revised recommendations on certain proposals involving diversity reporting, management-proposed ESG strategies and climate change, which Glass Lewis would evaluate on a case-by-case basis but would typically vote in favor of proposals requiring enhanced disclosures.[40]

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[39] Glass Lewis, 2021 Proxy Paper Guidelines, An Overview of the Glass Lewis Approach to Proxy Advice, United States, available at https://www.glasslewis.com/wp-content/uploads/2020/11/US-Voting-Guidelines-GL.pdf?hsCtaTracking=7c712e31-24fb-4a3a-b396-9e8568fa0685%7C86255695-f1f4-47cb-8dc0-e919a9a5cf5b.

[40] Glass Lewis, 2021 Proxy Paper Guidelines, An Overview of the Glass Lewis Approach to Proxy Advice, Environmental, Social & Governance (“ESG”) Initiatives, available at https://www.glasslewis.com/wp-content/uploads/2020/11/ESG-Initiatives-Voting-Guidelines-GL.pdf.

§ 4:27 Voluntary disclosure frameworks: Global reporting initiative

Against the backdrop of mandatory reporting regimes around the world, many voluntary disclosure frameworks have evolved

in response to investors' desire for more ESG information. Some of the more prominent frameworks are outlined in this section. The Global Reporting Initiative (GRI) was formed in 1997 to help companies and governments better understand and communicate their impact on sustainability issues such as climate change, human rights, governance, and social well-being.[1] Companies around the world now use the GRI's Sustainability Reporting Standards to report on key sustainability issues. According to the GRI, "of the world's largest 250 corporations, 92 percent report on their sustainability performance and 74 percent of these use GRI's Standards."[2] The GRI published a revised version of the Standards on October 5, 2021, alongside a new oil and gas sector reporting standard; the first sector-specific reporting standard intended for relevant entities to use alongside the universal GRI Standards. The revised version of the GRI Standards seeks to address perceived gaps between existing disclosure frameworks and intergovernmental expectations for responsible business, including in human rights reporting and environmental due diligence, and aligns with the OECD standards of responsible business conduct. The GRI also provides training, information, and support for issuers and other market participants, and works to promote the broad implementation of the GRI Standards, which offer specific metrics and measurement criteria to guide reporting on a host of ESG factors.[3] In July 2021, a statement of cooperation was announced

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[1] See GRI website https://www.globalreporting.org/Information/aboutgri/Pages/default.aspx.

[2] Https://www.globalreporting.org/information/sustainability-reporting/Pages/gri-standards.aspx.

[3] For example, the environmental standards include standards on materials, energy, water and effluents, biodiversity, emissions, effluents and waste, environmental compliance, and supplier environmental assessments. The social standards include standards on employment, labor/management relations, occupational health and safety, training and education, diversity and

between the GRI and the European Financial Reporting Advisory Group (EFRAG), whereby the GRI will assist EFRAG in developing the new EU sustainability reporting standards as set out in the CSRD proposal (discussed above).[4]

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equal opportunity, non-discrimination, freedom of association and collective bargaining, child labor, forced labor, security practices, rights of indigenous people, human rights, local communities, supplier social assessment, and consumer health and safety.

[4] Https://www.globalreporting.org/about-gri/news-center/gri-welcomes-role-as-co-constructor-of-new-eu-sustainability-reporting-standards/.

§ 4:28 Voluntary disclosure frameworks: The TCFD

The TCFD provides a consistent framework for companies to voluntarily make climate-related financial disclosures for investors, lenders, and others.[1] The TCFD, as its name suggests, focuses specifically on climate-related disclosures, as compared with the GRI and SASB frameworks, which cover ESG factors more broadly. Moreover, the TCFD's framework addresses the establishment of sound governance and reporting processes and practices, rather than specific reporting metrics.

In June 2017, the TCFD issued its final report, which made broad recommendations with regard to climate-related disclosures. The TCFD explained that the report was a response to the FSB's request that the TCFD "develop voluntary, consistent climate-related financial disclosures that would be useful to investors, lenders, and insurance underwriters in understanding

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material risks."[2] The TCFD stressed that the recommendations were designed so that all organizations, regardless of industry, sector, or geography, should be able to adopt the recommendations. It also emphasized that climate-related financial disclosures should be incorporated in mainstream financial filings and should provide decision-useful, forward-looking information on the financial impacts of climate change. Further, the TCFD stressed its intent that the disclosures emphasize the risks and opportunities in transitioning to a lower-carbon economy.

In a 2019 update, the TCFD reiterated its purpose: "Now more than ever it is critical for companies to consider the impact of climate change and associated mitigation and adaptation efforts on their strategies and operations and disclose related material information. Companies that invest in activities that may not be viable in the longer term may be less resilient to risks related to climate change; and their investors may experience lower financial returns."[3]

The TCFD incorporates four core themes in its recommendations with regard to climate-related financial disclosures. First, disclosures should describe an organization's governance with regard to climate-related risks and opportunities. Second, disclosures should explain how climate-related risks and opportunities could impact an organization's business, financial condition, and strategy. Third, disclosures should explain how an organization identifies, assesses, and manages climate-related risks, including through scenario analyses. Fourth, disclosures

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[2] Final Report, Recommendations of the Task Force on Climate-Related Financial Disclosures (June 2017), available at https://www.fsb-tcfd.org/wpcontent/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf.

[3] TCFD: 2019 Status Report (June 2019), available at https://www.fsbtcfd.org/publications/tcfd-2019-status-report/.

should use metrics and targets to evaluate and manage these risks and opportunities.[4]

The TCFD elaborates on the types of climate-related risks organizations might face. These fall broadly in two categories: transition risks and risks associated with the physical impacts of climate change. Transition risks might include policy and legal developments, such as implementation of carbon pricing, emissions caps, shifts to alternative energy sources, legal and regulatory compliance costs, and exposure to litigation. Other transition risks could relate to technological improvements that displace old systems, market risks, and reputational risks associated with changing customer perceptions of an organization's business. Physical risks might include damage to property due to rising sea levels or extreme weather in addition to resource scarcity and supply-chain risks. The TCFD report also outlines opportunities that companies might enjoy as a result of their climate strategies, including opportunities around energy efficiency, resource reuse, and the development of new products and markets.

Since the publication of its final report in 2017, the TCFD recommendations have proven relatively popular with policymakers and companies worldwide. The TCFD reported in October 2020 that over 1,500 organizations globally had expressed their support for the TCFD recommendations, including companies with a market capitalization of $12.6 trillion, and nearly 60 percent of the world's 100 largest public companies support

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[4] Final Report, Recommendations of the Task Force on Climate-Related Financial Disclosures (June 2017), available at https://www.fsb-tcfd.org/wpcontent/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf, at 176.

the TCFD, report in line with the TCFD recommendations, or both.[5]

The TCFD recommendations have served as a key pillar of much of the work to harmonize ESG disclosure requirements globally. Moreover, the G20 publicly welcomed the FSB's July 2021 roadmap for addressing climate-related financial risks, alongside a pledge to work to promote implementation of disclosure requirements or guidance, which will build on the TCFD framework.[6]

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[5] Https://www.fsb.org/wp-content/uploads/P291020-1.pdf.

[6] Https://www.g20.org/wp-content/uploads/2021/07/Communique-Third-G20-FMCBG-meeting-9-10-July-2021.pdf.

§ 4:29 Voluntary disclosure frameworks: The SASB

The Value Reporting Foundation was formed in a 2021 merger between the SASB and the International Integrated Reporting Council (IIRC), as part of a larger effort to simplify the current ESG disclosure landscape.

The SASB, founded in 2011, is a standards-setting organization formed to help businesses to identify, manage, and report on the sustainability topics that are most important to investors.[1] The SASB's approach closely follows the concept of materiality as articulated by the U.S. Supreme Court, and it seeks to facilitate the identification and disclosure of that information related to sustainability factors that have a material impact on companies' financial condition and prospects. The SASB has developed a set of 77 industry-specific standards that target the sus-

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[1] See https://www.sasb.org/.

tainability issues that generally are most important within an industry. These standards were developed based on surveys and interviews with investors, companies, and other market participants. The industry focus helps companies identify and address the issues most salient to their businesses and cut through the confusion that can sometimes result from the use of more general questionnaires. The industry focus can also facilitate comparison across companies within an industry, as their disclosures are more likely to be comparable as to general sustainability topics. The SASB also regularly publishes guidance and conducts research to advance the thinking on best practices for sustainability reporting.

The IIRC launched the International <IR> Framework[2] in December 2013. The Framework aimed to link financial and non-financial business strategies, risks, and performance to provide a single value of a company's performance over a long-time horizon.

Despite the merger, the SASB standards and <IR> Framework are both still in operation and are seen as mutually compatible, which provides companies with the option of complying with either one, or both, depending on preference.

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[2] Https://www.valuereportingfoundation.org/.

§ 4:30 Voluntary disclosure frameworks: Climate Disclosure Standards Board

The International Financial Reporting Standards Foundation (IFRS Foundation), which has for a number of years overseen the globally accepted set of accounting standards, published a consultation in September 2020 to determine the appetite for a similar set of global sustainability standards, and whether the

IFRS Foundation is well placed to develop and oversee such standards.

Having received support for the promulgation of a global standard from IOSCO[1] in March 2021, the IFRS Foundation Trustees (the Trustees) issued a public statement[2] on the strategic direction of the proposed international sustainability reporting standards board (ISSB). This approach outlined that the ISSB should focus initially on climate-related reporting, while also working towards providing information on other ESG matters. It also signaled an intention to build on existing frameworks, in particular the TCFD recommendations, and to work with existing organizations in the field.

The Trustees aim to make a final determination on the creation of the ISSB in advance of the November 2021 COP26 conference in Glasgow, and have already received support in principle from G7 finance ministers in the form of a June 2021 communiqué.[3]

The Climate Disclosure Standards Board (CDSB) was founded in 2007 and is composed of a consortium of NGOs and businesses that focus on incorporating environmental effects in mainstream financial reporting. The CDSB's goal is to drive decision-useful environmental information to market participants through mainstream reports.[4] While the SASB and the GRI target ESG factors broadly, the CDSB addresses the envi-

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[1] https://www.iosco.org/news/pdf/IOSCONEWS594.pdf.

[2] Https://www.ifrs.org/news-and-events/news/2021/03/trustees-announce-strategic-direction-based-on-feedback-to-sustainability-reporting-consultation/.

[3] Https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/991640/FMCBGs_communique_-_5_June.pdf.

[4] See https://www.cdsb.net/our-story.

ronmental impacts and the treatment of "natural capital" alongside financial capital. The CDSB is "committed to advancing and aligning the global mainstream corporate reporting model to equate natural capital with financial capital."[5] The CDSB offers companies a Climate Change Reporting Framework, by which to report environmental information with a level of rigor comparable to that applied to financial information. The framework enables companies to "provide investors with decision-useful environmental information via the mainstream corporate report, enhancing the efficient allocation of capital."[6] The CDSB's framework is designed to filter the information that investors, issuers, and regulators require in order to understand how climate change affects a company's financial condition and prospects.

The framework provides a detailed description of the methodology that the CDSB urges companies to apply in assessing and reporting on their climate change impacts.[7] The guidance falls in three categories: Determination, Preparation, and Presentation. Determination requires companies to determine what information is most useful to investors based on the company's thorough assessment of how climate change has or might affect the company's strategic goals. Preparation requires companies to prepare disclosures on a consistent basis that include such information as is necessary to optimize its utility to investors. Presentation requires companies to present disclosures in a

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[5] See https://www.cdsb.net/our-story.

[6] See https://www.cdsb.net/our-story.

[7] Climate Disclosure Standards Board, "Climate Change Reporting Framework: Advancing and aligning disclosure of climate change-related information in mainstream reports" (Oct. 2012), available at https://www.cdsb.net/sites/default/files/cdsb_climate_change_reporting_framework_edition_1.1_0.pdf.

manner that makes the climate-related risks clear and understandable to investors.

§ 4:31 Voluntary disclosure frameworks: CDP

The CDP (formerly the Carbon Disclosure Project) operates a disclosure system that enables companies, municipalities, and others to measure and manage the environmental impact of their activities.[1] According to its website, the CDP has built the most comprehensive set of self-reported environmental data in the world, with more than 7,000 companies and 620 cities reporting environmental data through the CDP in 2019.[2] The CDP requests detailed information of companies, cities, and states on their environmental performance, GHG emissions, and environmental governance. The CDP then analyzes that data with reference to critical environmental risks and opportunities and shares the analyses and resulting scores with investors and others with an interest in the information. The CDP data are designed to facilitate better-informed decision-making by investors and policymakers.

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[1] See https://www.cdp.net.

[2] See https://www.cdp.net.

§ 4:32 Voluntary disclosure frameworks: UN sustainable development goals

In 2015, the UN member nations unanimously adopted the 2030 Agenda for Sustainable Development. The 17 Sustainable Development Goals (SDGs),[1] and 169 specific targets embed-

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[1] The 17 Sustainable Development Goals are:

Goal 1: End poverty in all its forms everywhere

Goal 2: End hunger, achieve food security and improved nutrition, and promote sustainable agriculture

Goal 3: Ensure healthy lives and promote well-being for all at all ages

Goal 4: Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all

Goal 5: Achieve gender equality and empower all women and girls

Goal 6: Ensure availability and sustainable management of water and sanitation for all

Goal 7: Ensure access to affordable, reliable, sustainable, and modern energy for all

Goal 8: Promote sustained, inclusive, and sustainable economic growth, full and productive employment and decent work for all

Goal 9: Build resilient infrastructure, promote inclusive and sustainable industrialization, and foster innovation

Goal 10: Reduce inequality within and among countries

Goal 11: Make cities and human settlements inclusive, safe, resilient, and sustainable

Goal 12: Ensure sustainable consumption and production patterns

Goal 13: Take urgent action to combat climate change and its impacts

Goal 14: Conserve and sustainably use the oceans, seas, and marine resources for sustainable development

Goal 15: Protect, restore, and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss

Goal 16: Promote peaceful and inclusive societies for sustainable development, provide access to justice for all, and build effective, accountable, and inclusive institutions for all levels

ded within the 17 goals, "are an urgent call for action by all countries — developed and developing — in a global partnership. They recognize that ending poverty and other deprivations must go hand-in-hand with strategies that improve health and education, reduce inequality, and spur economic growth — all while tackling climate change and working to preserve our oceans and forests."[2] The UN agenda is ambitious, global, and inclusive. All UN member nations have agreed to work toward the goals, which flow down into states, cities, businesses, schools, and other organizations. As organizations map their activities to the SDGs, they are encouraged to identify the goals that are most relevant to their businesses and establish suitable targets that will advance progress on the selected SDGs. Companies are not expected to map all 17 of the SDGs, but rather identify the ones they can most directly impact. The SDGs are voluntary and leave companies with substantial freedom to define which goals they will disclose. The real significance of the SDGs lies in the provision of a common framework within which companies, governments, and others can work toward solutions to the problems that the UN has identified as most critical for the future.

Goal 17: Strengthen the means of implementation and revitalize the Global Partnership for Sustainable Development

[2] See https://sustainabledevelopment.un.org/?menu=1300.

§ 4:33 Integrated ESG reporting

The IIRC was, and as part of the Value Reporting Foundation, remains, a global coalition composed of investors, corpora-

tions, NGOs, regulators, accountants, and standards setters.[1] The IIRC's (and now the Value Reporting Foundation's) vision is "a world in which integrated thinking is embedded within mainstream business practice in the public and private sectors, facilitated by Integrated Reporting as the corporate reporting norm."[2] A goal of integrated reporting is to explain the relationship of the resources or "capitals" an organization uses to create value over time. The six capitals are categorized as financial, manufactured, intellectual, human, social, and natural. According to the IIRC, "An integrated report is a concise communication about how an organization's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value over the short, medium and long term."[3] Integrated reporting takes a prominent position in the ESG reporting discussion because it has been offered as a framework through which to integrate ESG factors with financial analysis and disclosures. Further, it embraces the proposition that companies, investors, and other stakeholders would benefit if ESG factors were discussed alongside financial factors in financial reports rather than in separate reports. In January 2021, prior to becoming a part of the Value Reporting Foundation, the IIRC released an updated version of Interna-

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[1] International Integrated Reporting Council, "The International <IR> Framework" (Dec. 2013), available at http://integratedreporting.org/wp content/uploads/2015/03/13-12-08-THE-INTERNATIONAL-IR-FRAME WORK-2-1.pdf.

[2] International Integrated Reporting Council, "The International <IR> Framework" (Dec. 2013), available at http://integratedreporting.org/wp-content/uploads/2015/03/13-12-08-THE-INTERNATIONAL-IR-FRAME WORK-2-1.pdf.

[3] International Integrated Reporting Council, "The International <IR> Framework" (Dec. 2013), available at http://integratedreporting.org/wpcontent/uploads/2015/03/13-12-08-THE-INTERNATIONAL-IR-FRAME WORK-2-1.pdf.

tional <IR> Framework, reflecting the results of a market consultation with 1,470 individuals in 55 jurisdictions.[4]

In 2018, the Conference Board assembled an Integrated Reporting Working Group composed of investors, corporations, and professional services providers, who analyzed key trends in and challenges with regard to the implementation of integrated reporting.[5] The Conference Board report observes the economic shift toward intangible assets that the Commission notes in its August 2019 proposing release, as discussed above: "The dynamics of how business value is created are changing, moving from a system based largely on tangible assets to one that favors intangible ones."[6] In considering ESG factors in their investment processes, many investors want companies to take a more holistic approach to reporting that accounts for not only traditional financial assets, but also the six capitals identified by the IIRC Value Reporting Foundation.[7] According to the Conference Board report, "How value is calculated is changing, and it would be helpful for reporting norms to change accordingly." The report notes that investors strongly support an integrated approach as evidenced by a survey of institutional investors

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[4] Https://integratedreporting.org/wp-content/uploads/2021/03/Framework-comparison-2013-to-2021.pdf.

[5] The Conference Board, "Integrated Reporting Working Group: The Emergence of Integrated Reporting" (July 15, 2019), available at https://www.conference-board.org/publications/publicationdetail.cfm?publicationid=8635.

[6] The Conference Board, "Integrated Reporting Working Group: The Emergence of Integrated Reporting" (July 15, 2019), available at https://www.conference-board.org/publications/publicationdetail.cfm?publicationid=8635, at 3.

[7] The six capitals identified by the IIRC are: financial capital, manufactured capital, intellectual capital, human capital, social and relationship capital and natural capital.

with a collective $33 trillion in assets under management. Eighty percent of the survey's respondents support integrated reporting.[8] The Conference Board explains:

> While investors still find financial performance disclosure important, they increasingly believe a holistic view of the way a company creates and sustains value is also crucial for insight. Investors want to understand not only a company's immediate financial performance, but also the strategy of the business, the key resources, the assets (tangible and intangible) to which it has access, and how it intends to maintain access to these resources and maintain or improve its assets while appropriately controlling its liabilities. Companies are beginning to rethink their approach to managing and reporting on their intangible assets, many aspects of which don't show up on their balance sheet.[9]

The Conference Board views integrated reporting as a mechanism to provide investors with the holistic understanding that they seek. Integrated reporting encourages companies to "more comprehensively explain how the company creates value in the short, medium, and long term through the eyes of management."[10] The focus is not solely on a company's reporting to

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[8] The Conference Board, "Integrated Reporting Working Group: The Emergence of Integrated Reporting" (July 15, 2019), available at https://www.conference-board.org/publications/publicationdetail.cfm?publicationid=8635, at 25.

[9] The Conference Board, "Integrated Reporting Working Group: The Emergence of Integrated Reporting" (July 15, 2019), available at https://www.conference-board.org/publications/publicationdetail.cfm?publicationid=8635, at 9.

[10] The Conference Board, "Integrated Reporting Working Group: The Emergence of Integrated Reporting" (July 15, 2019), available at https://www.conference-board.org/publications/publicationdetail.cfm?publicationid=8635, at 3.

external stakeholders, but also on responding to the informational needs of other stakeholders and building a more integrated approach within the company. "While integrated reporting is often thought of as a framework for external reporting," the Conference Board notes, "its greatest benefit may be its ability to foster 'integrated thinking,' enabling a better understanding within companies of the factors that materially affect their ability to create value over time."[11]

The Conference Board report stresses that integrated reporting is still in its infancy for most public companies, and that there is no one correct way to prepare an integrated report. It indicates that the most useful reports generally briefly discuss the company's business model, the material issues that impact value creation, and stakeholder engagement. The report provides several helpful examples of integrated reports, which use graphical representations to illustrate how companies can apply the six capitals to create value.

The IIRC and the Conference Board note that integrated reports can be merged with a company's Form 10-K and include both required information and voluntary disclosures. Alternatively, companies are free to reserve their periodic reports for required disclosures and separately produce an integrated report — perhaps to replace the sustainability report that many companies currently publish. This leads to the question of whether ESG disclosures should appear in financial reports or separate sustainability reports.

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[11] The Conference Board, "Integrated Reporting Working Group: The Emergence of Integrated Reporting" (July 15, 2019), available at https://www.conference-board.org/publications/publicationdetail.cfm?publicationid=8635, at 3.

§ 4:34 Where ESG information should appear

The SASB roundtable addressed the question of where sustainability information should be disclosed: "No clear consensus emerged on where companies should report their sustainability performance. The current reporting practices of corporate participants run the gamut, with most disclosing ESG information in sustainability reports, others in mainstream financial filings, and still others in annual reports, on website, or through some combination of channels. Likewise, investors' opinions were mixed."[1] Some investors indicated that sustainability reports can be bloated with information that is less helpful to the investor community and would prefer that financially material ESG information be included in companies' 10-Ks or other financial filings. According to the roundtable, "[a]t the end of the day, however, most investors generally agreed they don't care where the information is reported as long as it's high-quality." Said one asset manager: "What we're looking for is how any ESG theme or metric is tied to a company's value proposition . . . Whether the company conveys that in its 10-K or sustainability report — we don't care that much."[2]

More recently, the SASB announced that it is rethinking its initial assumption that its standards would be incorporated in SEC filings. According to a Harvard Law School forum on those standards and filings, "SASB's outreach to investors con-

[1] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esgdata/, at 9.

[2] Sustainability Accounting Standards Board, "Dead Cobras and Faberge Eggs: Unlocking the Potential of ESG Data" (2018), available at https://library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esgdata/, at 10.

vinced it to become less focused on SEC filings as the primary location for disclosures; most investors were found to care more about obtaining sustainability disclosure that is readily available, reliable, and comparable than they do about where it is located."[3] The SASB endorsed the idea that companies should be free to determine where to report ESG information provided that they implement appropriate disclosure controls to ensure the information is reliable.

The SASB explained that its change in thinking was informed by the concerns that companies expressed over use of the SASB standards in their SEC filings. Companies noted that the level of detail or extent of the disclosures that the SASB contemplates may go beyond what is required. They also noted the potential liability that could result from inclusion of more detailed ESG information in SEC filings. At the same time, as the SASB points out, companies frequently provide more detailed disclosures outside their SEC filings in separate sustainability reports or on their websites, which are subject to the antifraud provisions of the U.S. securities laws even if they do not appear in the company's SEC filings. As such, this concern over enhanced liability is perhaps somewhat overstated. On the other hand, ESG disclosures in Form 10-K filings could expose companies to liability under Section 11 of the Securities Act if the 10-K is incorporated by reference in a registration statement. As such, companies' nervousness is not without justification.[4] Fi-

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[3] Tom Riesenberg and Alan Beller, "Sustainability Accounting Standards and SEC Filings," Harvard Law School Forum on Corporate Governance and Financial Regulation (June 5, 2019), available at https://corpgov.law.harvard.edu/2019/06/05/sustainability-accounting-standards-and-sec-filings/.

[4] Tom Riesenberg and Alan Beller, "Sustainability Accounting Standards and SEC Filings," Harvard Law School Forum on Corporate Governance and Financial Regulation (June 5, 2019), available at https://

nally, companies have expressed a reluctance to accept increased reporting burdens in light of the time pressures they currently face to produce and file their periodic SEC filings.

The SASB discussion highlighted some recent innovative thinking with regard to the manner of filing ESG information with the SEC. It noted that one company recently filed its sustainability report on a Current Report on Form 8-K. The sustainability report was filed as an attachment to a press release and technically was "furnished" pursuant to Item 7.01 of Form 8-K rather than "filed."[5] As such, the report would not be incorporated by reference into the registrant's registration statements and would not, therefore, give rise to Section 11 liability.

If companies do provide ESG disclosures in separate reports outside of their SEC filings, they of course still must consider what disclosures are required in the SEC filings. Ideally, companies will harmonize the disclosure processes internally to ensure consistency between the sustainability reports and financial reports, and ensure the sustainability reports are subjected to similar oversight and rigor as that applied to financial disclosures. These measures should help ensure consistency in reporting, and lead to a deeper analysis and scrutiny of ESG disclosures within companies.

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corpgov.law.harvard.edu/2019/06/05/sustainability-accounting-standards-and-sec-filings/.

[5] Disclosures pursuant to Item 7.01 are made to satisfy public disclosure obligations under Regulation FD relating to selective disclosure. See Form 8-K, Item 7.01, available at https://www.sec.gov/files/form8-k.pdf.

§ 4:35 Calls for the harmonization of reporting frameworks

The SEC's disclosure requirements typically are only the starting point in companies' assessment of what ESG information to disclose. As noted above, most companies also follow other reporting standards and respond to private-sector questionnaires that draw out information beyond that disclosed in the financial reports.

A number of initiatives have attempted to help market participants navigate the different reporting frameworks. The WBCSD has developed a comprehensive tool, the Reporting Exchange, which aggregates reporting requirements around the world. The Reporting Exchange is an online platform that offers a roadmap to nearly 2,000 mandatory and voluntary ESG reporting standards and frameworks in 70 countries.[1] The WBCSD developed the Reporting Exchange to address the fragmentation in the reporting landscape and the resulting confusion and frustration among market participants. The WBCSD notes: "Because there isn't standard terminology for describing and defining the components of the reporting world, confusion and complexity continues to grow. The resulting variability in the quality, quantity and relevance of disclosures prevents investors and stakeholders from getting the information they need."[2] In May 2021, the WBSCD transferred the Reporting Exchange to artificial intelligence company Arabesque in order

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[1] See https://www.wbcsd.org/Programs/Redefining-Value/External-Disclosure/The-Reporting-Exchange.

[2] See https://www.wbcsd.org/Programs/Redefining-Value/External-Disclosure/The-Reporting-Exchange.

to ensure the system is continually able to leverage the latest technology.[3]

The WBCSD's ESG Disclosure Handbook provides further guidance for companies as they approach their ESG reporting processes.[4] The ESG Disclosure Handbook is designed to help companies navigate the disclosure process, considering the informational demands of multiple stakeholders and the array of reporting standards. It offers a process by which companies are encouraged to consider their internal and external reasons for reporting, and to synthesize their reports to provide the key information that their stakeholders need. The guidance aims to help companies "when considering what to report, where, why, to whom and how" in response to the various mandatory and voluntary disclosure frameworks.[5]

The Corporate Reporting Dialogue also aims to rationalize the ESG reporting landscape.[6] Organized initially by the IIRC and now the Value Reporting Foundation, the Corporate Reporting Dialogue's participants include the CDP, CDSB, GRI, International Organization for Standardization, SASB, International Financial Reporting Standards, and the Financial Accounting Standards Board (FASB). The Corporate Reporting Dialogue has endeavored to reconcile the different reporting regimes by providing comparisons and summaries of the princi-

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[3] Https://www.reportingexchange.com/the-reporting-exchange-transferred-to-new-host-arabesque-to-take-advantage-of-the-latest-technology/?trevar=1.

[4] See https://www.wbcsd.org/Programs/Redefining-Value/External-Disclosure/Purpose-driven-disclosure/Resources/ESG-Disclosure-Handbook.

[5] Https://www.wbcsd.org/Programs/Redefining-Value/External-Disclosure/Purpose-driven-disclosure/Resources/ESG-Disclosure-Handbook.

[6] See https://corporatereportingdialogue.com/.

pal reporting frameworks, including a “landscape map” that compares the member organizations’ disclosure standards.[7] The goal of the Corporate Reporting Dialogue’s tools is “to promote greater coherence, consistency and comparability between corporate reporting frameworks, standards and related requirements.”

The Corporate Reporting Dialogue is a sponsor of the Better Alignment Project, a two-year project that aimed to map the key provisions of the CDP, CDSB, GRI, IIRC, SASB, and TCFD to find points of overlap that can be harmonized.[8] The project leaders conducted roundtables with stakeholders around the globe between April and June 2019 in order to identify opportunities for better alignment in sustainability reporting and to understand the impediments to effective ESG reporting, with a particular focus on efforts to adopt the TCFD recommendations. The Corporate Reporting Dialogue announced a forthcoming publication in Q3 2019 published a report titled “Driving Alignment in Climate-related Reporting” in September 2019, which demonstrated the linkages and high levels of alignment of the TCFD recommendations with the CDP, CDSB, GRI, IIRC, and SASB standards.[9] Consistent with the IIRC’s objectives, the Better Alignment Project aims to facilitate integrated disclosure of financial and non-financial information, and the findings of its final report suggest that existing conflicts between TCFD and standards currently used in the market are substantively limited.

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[7] See https://corporatereportingdialogue.com/landscape-map/.

[8] Https://corporatereportingdialogue.com/better-alignment-project/.

[9] Https://corporatereportingdialogue.com/publication/driving-alignment-in-climate-related-reporting/. This website indicates that the report will be posted at https://corpo ratereportingdialogue.com/better-alignment-project/.

In the spring of 2019, SASB and the CDSB published a TCFD Implementation Guide designed to help companies apply the TCFD recommendations in harmony with the SASB and CDSB standards in order to improve companies' climate-related disclosures.[10] This guide recognizes that, despite the TCFD's broad support since its formation in 2015, comparatively few organizations apply its reporting guidance to address climate impacts in their disclosure documents. The guide was designed as a practical roadmap to remedy this disclosure gap and explains how the three frameworks complement each other. The CDSB principles "sit on top" of the TCFD framework and provide guidance as to how companies can effectively incorporate environmental and climate information in their mainstream reports and craft decision-useful disclosures. The SASB standards further augment the disclosure process by providing industry-specific criteria to help companies deliver material, decision-useful information to investors. The guide also emphasizes that a company's disclosures must first be guided by the relevant reporting requirements of the jurisdiction in which it operates, such as the SEC reporting framework.

The TCFD Implementation Guide offers a practical roadmap to ESG disclosures following the TCFD, CDSB, and SASB guidance. The steps guide companies on how to: (1) obtain executive and board-level support; (2) integrate climate change issues into key company governance with board-level oversight;

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[10] Sustainability Accounting Standards Board and Climate Disclosures Standards Board, "TCFD Implementation Guide: Using SASB Standards and the CDSB Framework to Enhance Climate-Related Financial Disclosures in Mainstream Reporting" (2019), available at https://library.sasb.org/tcfd-implementation-guide/. See also Paul A. Davies and Kristina S. Wyatt, "SASB and CDSB Issue TCFD Implementation Guide," Latham & Watkins Environment, Land & Resources Blog (May 13, 2019), available at https://www.globalelr.com/2019/05/tcfd-issues-implementation-guide-incorporating-sasb-and-cdsb-frameworks/.

(3) connect key functions within the company — sustainability, governance, finance, and compliance; (4) evaluate the financial impacts of climate risk; (5) apply scenario analyses to assess climate risks; (6) apply existing risk-management processes to climate risks; (7) seek feedback from investors as to what information they find most important; (8) leverage existing tools to collect and report climate information, rather than reinvent the wheel; (9) repurpose the same quality assurance and compliance systems for climate-related financial information as for other disclosures; (10) obtain external assurance of climate-related information or, at least, prepare the information as if it were going to be subject to assurance; and (11) evaluate the structure of annual reports and how the recommendations would fit within Risk Factors, MD&A, and the governance disclosures.[11]

The TCFD Implementation Guide provides sample disclosures that illustrate "TCFD-Aligned" disclosures. These examples are a response to requests from market participants for "real-world, good-practice examples of what decision-useful, climate-related financial disclosures could look like."[12] The sample disclosures are analyzed against the four principal elements of the TCFD recommendations: governance, strategy, risk management, and metrics and targets to illustrate how these elements can be applied in practice. Finally, the guide provides

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[11] Sustainability Accounting Standards Board and Climate Disclosures Standards Board, "TCFD Implementation Guide: Using SASB Standards and the CDSB Framework to Enhance Climate-Related Financial Disclosures in Mainstream Reporting" (2019), available at https://library.sasb.org/tcfd-implementation-guide/, at 8-10.

[12] Sustainability Accounting Standards Board and Climate Disclosures Standards Board, "TCFD Implementation Guide: Using SASB Standards and the CDSB Framework to Enhance Climate-Related Financial Disclosures in Mainstream Reporting" (2019), available at https://library.sasb.org/tcfd-implementation-guide/, at 12.

a matrix that maps the disclosure standards of the CDSB and the SASB to the TCFD recommendations to help companies see how the frameworks line up. The guide goes a long way toward providing actionable guidance to facilitate reporting, yet it also respects the dynamic nature of this field. The guide acknowledges, "as the TCFD recommendations are more broadly adopted and the management and reporting of climate-related risks and opportunities evolves, what is considered realistic and achievable will likely change."[13]

Since the publication of the TCFD Implementation Guide, the CDSB, SASB, and CDP have produced a number of other publications. These include a checklist[14] that sets out 11 preliminary steps that an organisation should take to ensure the TCFD recommendations are effectively implemented, a TCFD Good Practice Handbook,[15] and a TCFD to-do list.[16]

While TCFD is a voluntary framework, the UN PRI announced that, starting from 2020, its signatories would be required to report to the TCFD.[17] In July 2020, the PRI published

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[13] Sustainability Accounting Standards Board and Climate Disclosures Standards Board, "TCFD Implementation Guide: Using SASB Standards and the CDSB Framework to Enhance Climate-Related Financial Disclosures in Mainstream Reporting" (2019), available at https://library.sasb.org/tcfd-implementation-guide/, at 16.

[14] Https://www.cdsb.net/task-force/895/checklist-laying-groundwork-effective-tcfd-aligned-disclosures.

[15] Https://www.Cdsb.Net/Sites/Default/Files/Tcfd_Good_Practice _Handbook _web _a4.pdf.

[16] Https://www.cdsb.net/uncategorized/1032/tcfd-do-list-how-do-i-know-i%E2%80%99ve-met-tcfd-recommendations.

[17] United Nations Principles for Responsible Investment, "TCFD-based Reporting to Become mandatory for PRI Signatories in 2020," available at https://www.unpri.org/tcfd-based-reporting-to-become-mandatory-for-prisignatories-in-2020/4116.article.

a report on the first year of mandatory reporting, finding that the "increase in the volume of responses is in-line with the mandatory requirement for investor signatories to report 2,097 investors (443 asset owners, 1654 asset managers) representing $97 trillion in assets report this year as opposed to 591 investors last year."[18] By countries, the U.S. was "the largest market with 382 investors reporting."[19] The report noted that "79% of asset owners have reported board oversight of climate change," and in some markets "the percentage was as high as 100%."[20]

The calls to develop a globally recognized ESG disclosure framework have continued to intensify. The European Central Bank (ECB) remarked that "internationally consistent standards on climate-related and environmental information disclosure would foster comparable high-quality information and provide greater clarity to the industry on how to align their reporting internationally."[21] In September 2020, the IFRS Foundation, a not-for-profit organization that develops global accounting

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[18] United Nations Principles for Responsible Investment, "Top Four Takeaways from the PRI's First Year Mandatory TCFD-based Reporting," available at https://www.unpri.org/pri-blogs/top-four-takeaways-from-thepris-first-year-of-mandatory-tcfd-based-reporting/6097.article.

[19] United Nations Principles for Responsible Investment, "Top Four Takeaways from the PRI's First Year Mandatory TCFD-based Reporting," available at https://www.unpri.org/pri-blogs/top-four-takeaways-from-thepris-first-year-of-mandatory-tcfd-based-reporting/6097.article.

[20] United Nations Principles for Responsible Investment, "Top Four Takeaways from the PRI's First Year Mandatory TCFD-based Reporting," available at https://www.unpri.org/pri-blogs/top-four-takeaways-from-thepris-first-year-of-mandatory-tcfd-based-reporting/6097.article.

[21] European Central Bank, "Eurosystem Reply to the European Commission's Public Consultations on the Renewed Sustainable Finance Strategy and the Revision of the Non-Financial Reporting Directive," available at https://www.ecb.europa.eu/pub/pdf/other/ecb.eurosystemreplyeuropeancom missionpublicconsultations_20200608~cf01a984aa.en.pdf.

standards, issued a consultation draft to solicit input on the development of global ESG reporting standards.[22] The IFRS Foundation established a task force that consulted informally with a cross section of stakeholders involved with sustainability reporting, who agreed that "there is an urgent need to improve the consistency and comparability in sustainability reporting."[23] The consultation draft proposed the establishment of an International Sustainability Standards Board that would develop a global set of sustainability reporting standards (see further information above).

The calls to develop a globally recognized ESG disclosure framework have continued to intensify. The ECB remarked that "internationally consistent standards on climate-related and environmental information disclosure would foster comparable high-quality information and provide greater clarity to the industry on how to align their reporting internationally."[24] Moreover, in April 2020, the IOSCO published a report titled "Sustainable Finance and the Role of Securities Regulators and IOSCO," to "help achieve a degree of international consistency

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[22] IFRS Foundation, "Consultation Paper on Sustainability Reporting" (Sept. 30, 2020), available at https://cdn.ifrs.org/-/media/project/sustainability- reporting/consultation-paper-on-sustainability-reporting.pdf?la=en.

[23] IFRS Foundation, "Consultation Paper on Sustainability Reporting" (Sept. 30, 2020), available at https://cdn.ifrs.org/-/media/project/sustainability- reporting/consultation-paper-on-sustainability-reporting.pdf?la=en.

[24] European Central Bank, "Eurosystem Reply to the European Commission's Public Consultations on the Renewed Sustainable Finance Strategy and the Revision of the Non-Financial Reporting Directive," available at https://www.ecb.europa.eu/pub/pdf/other/ecb.eurosystemreplyeuropeancommissionpublicconsultations_20200608~cf01a984aa.en.pdf.

and harmonization, thereby assisting investors and issuers with the cross-border and global nature of sustainable instruments."[25]

IOSCO followed up in August 2020 with a further commitment to drive convergence of disclosure standards.[26] In response to the "plethora" of reporting standards that can make it difficult to compare companies and sustainable financial products, IOSCO created a taskforce that will work to harmonize the different standards around the world. That commitment was further echoed by a report[27] published by IOSCO in June 2021, which took the opportunity to reiterate IOSCO's view that there is an urgent need to improve the consistency, reliability, and comparability of issuers' ESG disclosures. The report highlights IOSCO's engagement with the IFRS Foundation, and provides further detail on what IOSCO would like the proposed ISSB to address. The report notes that IOSCO plans to consider endorsing the future ISSB standards, but such endorsement would require that IOSCO's expectations regarding strong governance and decision-useful content are satisfied.

However, in July 2021, SEC Commissioner Peirce submitted a comment letter[28] responding to an IFRS Foundation proposal to amend its constitution so that it could continue work on the ISSB. In her comment letter, Commissioner Peirce urged the IFRS Foundation to stop work on the proposed ISSB and desist

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[25] International Organization of Securities Commission, "Sustainable Finance and the Role of Securities Regulators and IOSCO," available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD652.pdf.

[26] "Global Regulatory Body to Harmonize 'plethora' of ESG Standards," Financial Times (Sept. 7, 2020), available at https://www.ft.com/content/4d7accf7-5431-4ebb-a528-87db3cca1eb7.

[27] Https://www.iosco.org/library/pubdocs/pdf/IOSCOPD678.pdf.

[28] Https://www.sec.gov/news/public-statement/peirce-ifrs-2021-07-01.

from work on sustainability standards, given their differences to financial and accounting reporting standards.

The International Monetary Fund (IMF) addressed climate change disclosures in its Global Financial Stability Report in April 2021. The report highlighted that:

> [D]eveloping global mandatory disclosures on material climate change risks would be an important step to sustain financial stability. In the short term, mandatory climate change risk disclosure could be based on globally agreed principles. In the longer term, climate change risk disclosure standards could be incorporated into financial statements compliant with International Financial Reporting Standards. Markets for assets that follow ESG standards have boomed since the beginning of the recovery phase of the pandemic. In the run-up to the UN COP26 in November 2021, the IMF is working with other international financial institutions, standard-setting organizations, and the Network for Greening the Financial System to establish climate disclosure standards, defined climate taxonomy and improve climate date."[29]

Similarly, the Organisation for Economic Co-operation and Development (OECD) dedicated its 2020 Business and Finance Outlook Report to ESG.[30] It explains, "the COVID-19 pandemic has highlighted an urgent need to consider resilience in fi-

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[29] Https://www.imf.org/en/Publications/GFSR/Issues/2021/04/06/global-financial-stability-report-april-2021International Monetary Fund Global Financial Stability Report, Chapter 5 "Climate Change: Physical Risks and Equity Prices," available at https://www.imf.org/en/Publications/GFSR/Issues/2020/04/14/global-financial-stability-report-april-2020#Chapter5.

[30] OECD, "Sustainable and Resilient Finance: OECD Business and Finance Outlook 2020" (Sept. 2020), available at http://www.oecd.org/daf/Sustainable-and-Resilient-Finance.pdf.

nance, both in the financial system itself and in the role played by capital and investors in making economic and social systems more dynamic and able to withstand external shocks. Using analysis from a wide range of perspectives, this year's edition focuses on the environmental, social and governance (ESG) factors that are rapidly becoming a part of mainstream finance."[31] The report notes the growth in ESG investing, but observes that investors are not receiving the information they need to inform their investment decisions: "[M]arket participants often lack the tools they need, such as consistent data, comparable metrics, and transparent methodologies, to properly inform value-based decision-making through a sustainability risk lens. This is despite a proliferation of ratings, methodologies, and metrics on ESG performance."[32]

The CFA Institute also released a consultation paper in August 2020 that highlights the need for consistent standards with regard to ESG investment products.[33] "In the face of growing interest in ESG investing, we found widespread support from the investment community for the development of a standard to reduce confusion and facilitate better alignment of investor objectives with product intent."[34]

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[31] OECD, "Sustainable and Resilient Finance: OECD Business and Finance Outlook 2020" (Sept. 2020), available at http://www.oecd.org/daf/Sustainable-and-Resilient-Finance.pdf.

[32] OECD, "Sustainable and Resilient Finance: OECD Business and Finance Outlook 2020" (Sept. 2020), available at http://www.oecd.org/daf/Sustainable-and-Resilient-Finance.pdf.

[33] CFA Institute "CFA Institute Publishes Consultation Paper on ESG Disclosure Standards for Investment Products" (Aug. 19, 2020), available at https://www.cfainstitute.org/en/about/press-releases/2020/cfa-institute-publishes-consultation-paper.

[34] CFA Institute "CFA Institute Publishes Consultation Paper on ESG Disclosure Standards for Investment Products" (Aug. 19, 2020), available at

Then, in September 2020, a group of standard-setters, including the CDSB, GRI, CDP, IIRC, and SASB issued a Statement of Intent to Work Together Towards Comprehensive Corporate Reporting, designed to advance the goal of alignment of ESG reporting standards.[35] The document emphasizes the importance of streamlining sustainability standards to improve the utility of sustainability information for companies and investors. The statement articulates three overarching goals:

1. To provide joint market guidance on how the different reporting frameworks can be applied in a complementary and additive fashion

2. To provide a shared vision of how the ESG disclosure elements might complement financial accounting principles and act as a starting point to advance the creation of a more "coherent" and comprehensive corporate reporting system

3. To provide a joint commitment by the participants to advance the work through ongoing deeper collaboration and a willingness to work with other interested parties[36]

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https://www.cfainstitute.org/en/about/press-releases/2020/cfa-institute-publishes-consultation-paper.

[35] Statement of Intent to Work Together Towards Comprehensive Corporate Reporting" (Sept. 2020), available at https://29kjwb3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Statement-of-Intentto-Work-Together-Towards-Comprehensive-Corporate-Reporting.pdf. See also "Setters of Sustainability Standards Pledge to Collaborate on Comprehensive Corporate Reporting" Latham & Watkins ELR Blog (Sept. 23, 2020), available at https://www.globalelr.com/2020/09/setters-of-sustainability-standards-pledge-to-collaborate-on-comprehensive-corporate-reporting/.

[36] "Statement of Intent to Work Together Towards Comprehensive Corporate Reporting" (Sept. 2020), available at https://29kjwb3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Statement-

In January 2020, the International Business Council of the World Economic Forum (IBC-WEF), in collaboration with the Big Four accounting firms, released a consultation draft, "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation."[37] The consultation draft was part of an effort "to develop a core set of common metrics to track environmental and social responsibility."[38] In September 2020, the IBC-WEF published a white paper that recommended a common set of ESG reporting standards designed to help companies across industries and across the world in building sustainable value.[39] In January 2021, a coalition of over 60 business leaders committed to these standards, specifically vowing to "[r]eflect the core metrics in their reporting to investors and other stakeholders . . . or briefly explaining why a different approach is more appropriate" and to "[p]romote the further convergence of existing ESG standards, frameworks and principles."[40]

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ofIntent-to-Work-Together-Towards-Comprehensive-Corporate-Reporting .pdf.

[37] World Economic Forum (Prepared in collaboration with Deloitte, EY, KPMG, and PwC), "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation," available at http://www3.weforum.org/docs/ WEF_IBC_ESG_Metrics_Discussion_Paper.pdf.

[38] World Economic Forum (Prepared in collaboration with Deloitte, EY, KPMG, and PwC), "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation," available at http://www3.weforum.org/docs/ WEF_IBC_ESG_Metrics_Discussion_Paper.pdf.

[39] International Business Council of the World Economic Forum, "Measuring Stakeholder Capitalism: Towards Common Metrics and Consistent Reporting of Sustainable Value Creation," (Sept, 22, 2020), available at http://www3.weforum.org/docs/ WEF_IBC_Measuring_Stakeholder_Capitalism _Report_2020.pdf.

[40] IBC-WEF, "Global Business Leaders Support ESG Convergence by Committing to Stakeholder Capitalism Metrics," (Jan. 26, 2021), available at

The IBC-WEF initiative adopts a different approach from that taken by the SASB framework, which provides separate sustainability accounting standards for 77 industries. The IBC-WEF seeks to identify a common set of ESG metrics for all companies to report on, regardless of sector or geography.[41] The consultation draft noted that these metrics and the recommended disclosures "should be capable of verification and assurance, further helping to raise the level of transparency and alignment among corporations, investors and all stakeholders with the goal of building a more sustainable and inclusive global economy."[42]

The IBC-WEF white paper draws on existing ESG reporting frameworks, including CDP, CDSB, GRI, IIRC, and SASB, and establishes 21 core and 34 expanded metrics and disclosures that map to the UN SDGs. The white paper organizes these core and expanded metrics in four pillars:

1. **Principles of governance:** governing purpose; governance body composition; material issues to stakeholders; anti-corruption; ethics and reporting mechanisms; and risk and opportunity oversight

2. **Planet:** greenhouse gas emissions from Scopes 1, 2, and 3; TCFD implementation; land use and ecological sensitivity; water consumption; and withdrawal

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https://www.weforum.org/press/2021/01/global-business-leaders-support-esg-convergence-by-committing-to-stakeholder-capitalism-metrics-73b5e9f13d.

[41] World Economic Forum (Prepared in collaboration with Deloitte, EY, KPMG, and PwC), "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation," available at http://www3.weforum.org/docs/WEF_IBC_ESG_Metrics_Discussion_Paper.pdf.

[42] World Economic Forum (Prepared in collaboration with Deloitte, EY, KPMG, and PwC), "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation," available at http://www3.weforum.org/docs/WEF_IBC_ESG_Metrics_Discussion_Paper.pdf.

3. **People:** diversity and inclusion; pay equality; wage levels; executive compensation; supplier and employee health and well-being; and employee training

4. **Prosperity:** employment and wealth generation; investment in innovation; and tax strategy[43]

The 21 core metrics are mostly "quantitative metrics for which information is already being reported by many firms (albeit often in different formats) or can be obtained with reasonable effort."[44] They focus "primarily on activities within an organization's own boundaries."[45]

The 34 expanded metrics, on the other hand, "tend to be less well established in existing practice and standards and have a wider value chain scope or convey impact in a more sophisticated or tangible way, such as in monetary terms."[46] The white paper encourages companies reporting on their ESG perfor-

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[43] International Business Council of the World Economic Forum, "Measuring Stakeholder Capitalism: Towards Common Metrics and Consistent Reporting of Sustainable Value Creation," (Sept. 22, 2020), available at http://www3.weforum.org/docs/WEF_IBC_Measuring_StakeholderCapitalism_Report_2020.pdf.

[44] World Economic Forum (Prepared in collaboration with Deloitte, EY, KPMG, and PwC), "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation," available at http://www3.weforum.org/docs/WEF_IBC_ESG_Metrics_Discussion_Paper.pdf.

[45] World Economic Forum (Prepared in collaboration with Deloitte, EY, KPMG, and PwC), "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation," available at http://www3.weforum.org/docs/WEF_IBC_ESG_Metrics_Discussion_Paper.pdf.

[46] World Economic Forum (Prepared in collaboration with Deloitte, EY, KPMG, and PwC), "Toward Common Metrics and Consistent Reporting of Sustainable Value Creation," available at http://www3.weforum.org/docs/WEF_IBC_ESG_Metrics_Discussion_Paper.pdf.

mance to consider the impact of their operations on the planet and in society "across the full value chain, in more tangible, sophisticated ways, including the monetary value of impacts."[47]

[47] International Business Council of the World Economic Forum, "Measuring Stakeholder Capitalism: Towards Common Metrics and Consistent Reporting of Sustainable Value Creation," (Sept. 22, 2020), available at http://www3.weforum.org/docs/WEF_IBC_Measuring_Stakeholder_Capitalism_Report_2020.pdf.

§ 4:36 ESG indexes and ratings

The financial industry has seen a surge in ESG rating and indexing services that score companies on the basis of their ESG performance, governance, and disclosures.[1] According to a 2020 SustainAbility "rate the raters" survey of several thousand sustainability professionals, the number of ESG ratings services has increased by more than 500 percent since 2010, with the number currently estimated at well over 600 percent.[2]

While ratings services can be helpful in the comparison of ESG risks across companies and industries, they do not appear to be a silver bullet. Ratings firms use a variety of criteria and

[1] Betty Moy Huber and Michael Comstock, "ESG Reports and Ratings: What They Are, Why They Matter," Harvard Law School Forum on Corporate Governance and Financial Regulation (July 27, 2017), available at https://corpgov.law.harvard.edu/2017/07/27/esg-reports-and-ratings-what they-are-why-they-matter/.

[2] SustainAbility, "Rate the Raters 2019: Expert Views on ESG Ratings" (Feb. 2019), p.4, available at http://sustainability.com/our-work/reports/rateraters-2019/. Some of the prominent ESG rating services include MSCI ESG Rating, RobecoSAM, CDP, Sustainalytics, RepRisk, ISS Environment and Social Quality, and the Dow Jones Sustainability Index.

methodologies to derive their ratings, including both publicly available information and answers to questions asked directly to companies, and there is no overarching regulatory structure governing the ratings methodologies. As a result, while many investors and companies place a high value on ESG ratings services as a path to greater clarity and comparability, some have criticized the ratings as subjective.[3]

In response to this criticism, and the potential risks that an overreliance of unregulated ESG ratings poses to investors, IOSCO launched a consultation report in July 2021 proposing a set of recommendations to mitigate the risks flowing from the activities of ESG ratings and data providers.[4] The recommendations in the report are aimed at a cross section of relevant industry players, including regulators, ESG ratings providers themselves, and assessed entities. One of the key recommendations includes a suggestion to regulators to consider focusing more on the use of ESG ratings and their providers, potentially leading the way for a regulated sector. This would echo the approach of the EU GBS, which introduced a requirement for providers of external verification to be approved by the European regulator.

Other key recommendations from the report include that rating agencies should seek to use publicly disclosed data sources when possible, and that financial market participants conduct diligence on any ESG rating product they use, to ensure a greater understanding of that rating's components. Globally, the EU's Sustainable Finance Strategy (discussed above), also contains plans to improve the reliability, comparability, and trans-

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[3] James Mackintosh, "Is Tesla or Exxon More Sustainable? It Depends Whom You Ask," Wall St. J. (Sept. 17, 2018), available at https://www.wsj.com/articles/is-tesla-or-exxon-more-sustainable-it-depends-whom-youask-1537199931.

[4] Https://www.iosco.org/library/pubdocs/pdf/IOSCOPD681.pdf.

parency of ESG ratings, as a result of strong demand within the European market. However, EU action is not expected until 2023 at the earliest. Last year, five major framework- and standard-setting institutions came together to help resolve the confusion and lack of standardization across ratings and to show a commitment to working towards a comprehensive corporate reporting system.[5]

SustainAbility's 2020 survey notes that not all ratings systems are the same, and investors and companies are still discerning where they find value in ratings: "Although many investors and companies see the value ratings have in engaging, informing and helping to change companies, they still question the overall quality, effectiveness and impact of corporate ESG ratings."[6] For their part, some companies expressed concern that the proliferation of ratings firms has accelerated the flow of information requests.[7] On the other hand, the survey found that close to two-thirds of the corporate respondents reported using ESG ratings to help inform their internal corporate decision-making were the top source of ESG information for investors, with 55 percent of those surveyed stating their reliance upon ratings. Ratings are often used as just one data point in a more

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[5] These institutions were GRI, the most widely used rating institution, SASB, CDP, and CDSB. See "Statement of Intent to Work Together Towards Comprehensive Corporate Reporting," (Sept. 2020) available at https://29kjwb3armds2g3gi4lq2sx1-wpengine.netdna-ssl.com/wp-content/uploads/Statement-of-Intent-to-Work-Together-Towards-Comprehensive-Corporate-Reporting.pdf.

[6] SustainAbility, "Rate the Raters 2019: Expert Views on ESG Ratings" (Feb. 2019), p.4, available at https://www.sustainability.com/globalassets/sustainability.com/thinking/pdfs/sa-ratetheraters-2019-1.pdf.

[7] SustainAbility, "Rate the Raters 2018: Ratings Revisited" (Mar. 2018), available at http://sustainability.com/our-work/reports/rate-raters-2018-white-paper/.

widespread ESG analysis undertaken by investors, and respondents were far more likely to report using the underlying data to provide material information (71 percent of respondents) compared to using the final score itself as a source of information (35 percent). "In open-ended responses, sustainability experts most often mentioned using ratings for internal assessments and strategy, to help inform what data to disclose, identify trends and support stakeholder engagement. This sentiment is reflected in SustainAbility's 2020 report, saying, "Those that have their own internal. . . . KPIs do not need the scores. What they do need is a way to efficiently gather ESG data to feed these internal analysis mechanisms."[8]

Traditional credit rating agencies are also increasing their focus on ESG factors. The S&P Global Ratings announced the launch of its ESG Evaluation in April 2019[9] and published its first ESG Evaluation in June 2019.[10] S&P Global Ratings explains its rationale to help investors manage and rationalize the ESG information that they are trying to integrate in their investment analyses: "Today, investors who deliberately apply an ESG lens to investing are growing rapidly worldwide as more come to realize the risks of separating such issues from business

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[8] SustainAbility, "Rate the Raters 2020: Investor Survey and Interview Results" (Mar. 2020), p.24, available at https://www.sustainability.com/globalassets/sustainability.com/thinking/pdfs/sustainability-ratetheraters2020-report.pdf.

[9] S&P Global Ratings Media Release, "New market offering seeks to improve transparency, disclosure and private-sector engagement with rising environmental, social, and governance risk concerns" (Apr. 11, 2019), available at https://www.spratings.com/en_US/media-releases/-/asset_publisher/cebizYBoiIER/content/s-p-global-ratings-launches-its-esg-evaluation?inheritRedirect=false.

[10] "S&P Global Ratings Publishes Its First ESG Evaluation," MarketWatch (June 17, 2019), available at https://www.marketwatch.com/pressrelease/sp-global-ratings-publishes-its-first-esg-evaluation-2019-06-17.

fundamentals. The lack of consistency, standards, and forward view of the majority of ESG information providers result in widespread difficulties for investors looking to integrate ESG factors into their investment decisions."[11] In December 2019, S&P Global acquired SAM ESG ratings and Benchmarking from RobecoSAM, a long running sustainable investment research and ESG rating provider, to bolster its offering in the ratings space.

In May 2019, Moody's Investors Service solicited feedback on a new carbon transition risk-assessment tool for rated companies.[12] The proposed carbon transition assessments (CTAs) are not traditional credit ratings, but rather tools to provide market participants with greater clarity as to carbon transition risks for companies in selected sectors as well as rankings of issuers within sectors. The CTAs will apply a materiality, risk, and mitigation assessment. The key risks that will be scrutinized are a company's current carbon profile, its medium-term exposure to technology risk, near- and medium-term mitigation strategies, and long-term risks associated with a rapid transition to a low-carbon economy.[13] Similar to S&P, Moody's has also looked to grow via acquisition in the ESG space, with the 2019 purchase

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[11] S&P Global, "ESG Evaluation: Sustainable Practices. Sustainable Returns," available at https://www.spglobal.com/en/capabilities/esg-evaluation.

[12] Moody's Investors Service, "Research Announcement: Moody's requests feedback on a new carbon transition risk assessment tool for rated companies" (May 7, 2019), available at https://m.moodys.com/research/Moodys-requests-feedback-on-a-new-carbon-transition-risk-assessment--PBC_1171112.

[13] Moody's Investors Service, "Research Announcement: Moody's requests feedback on a new carbon transition risk assessment tool for rated companies" (May 7, 2019), available at https://m.moodys.com/research/Moodys-requests-feedback-on-a-new-carbon-transition-risk-assessment--PBC_1171112.

of VigeoEiris and August 2021 acquisition of RMS providing increased ESG ratings capability.

Similarly, Fitch launched its ESG Relevance Scores in January 2019.[14] Fitch applies a sector-based standardized scoring system that began with 1,500 non-financial corporate ratings across asset classes. Fitch's announcement of the ESG Relevance Scores explained that it planned to follow the initial non-financial sector ESG scoring with similar scoring for banks, non-bank financial institutions, insurance companies, sovereigns, public finance, global infrastructure, and structured finance.[15] The initiative results from market feedback Fitch received that indicated the importance of ESG information to credit risk: "We actively engaged with investors and other market participants to understand what they want to see from CRAs before devising the new relevance scores. Our focus is purely on fundamental credit analysis and so our ESG Relevance Scores are solely aimed at addressing ESG in that context. The scores do not make value judgements on whether an entity engages in good or bad ESG practices, but draw out which E, S, and G risk elements are influencing the credit rating decision."[16]

PRI launched its ESG in Credit Risk and Ratings Initiative "to enhance the transparent and systematic integration of ESG

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[14] Fitch Ratings, "Fitch Ratings Launches ESG Relevance Scores to Show Impact of ESG on Credit" (Jan. 7, 2019), available at https://www.fitchratings.com/site/pr/10058528.

[15] Fitch Ratings, "Fitch Ratings Launches ESG Relevance Scores to Show Impact of ESG on Credit" (Jan. 7, 2019), available at https://www.fitchratings.com/site/pr/10058528.

[16] Fitch Ratings, "Fitch Ratings Launches ESG Relevance Scores to Show Impact of ESG on Credit" (Jan. 7, 2019), available at https://www.fitchratings.com/site/pr/10058528, quoting Andrew Steel, Fitch Ratings Global Head of Sustainable Finance.

factors in credit risk analysis."[17] The effort highlights the fact that credit risks are evolving and the incorporation of material ESG factors into the credit risk analysis is critical to properly evaluating a company's default risk. The ESG Credit Risk and Ratings Initiative brings together fixed-income investors and credit rating agencies to promote understanding and identify areas in which ESG factors are not being taken into account in the credit rating process. The discussion between fixed-income investors and credit rating agencies has illustrated that "ESG consideration in credit risk analysis is still not addressed consistently and systematically by all (fixed income) market participants."[18] Nonetheless, a recent 2020 report from the initiative pointed to a positive trajectory with increased transparency as to how ESG factors are incorporated in investors' and credit rating agencies' analyses and better alignment between investors and credit rating agencies. Furthermore, ESG factors are viewed not merely as sources of risk but also as opportunities: "Perceptions are shifting and ESG signals are beginning to be used not only to manage downside risks but also to spot investment opportunities."[19]

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[17] PRI, "ESG, Credit Risk and Ratings: Part 1 — The State of Play. Investors and credit rating agencies (CRAs) are ramping up efforts to consider environmental, social and governance (ESG) factors in credit risk analysis" (July 3, 2017), available at https://www.unpri.org/credit-ratings/esg-creditrisk-and-ratings-part-1-the-state-of-play/78.article.

[18] PRI, "Shifting Perceptions: ESG, Credit Risk and Ratings: Part 3 — From Disconnects to Action Areas" available at https://www.unpri.org/download?ac=5819.

[19] PRI, "Shifting Perceptions: ESG, Credit Risk and Ratings: Part 3 — From Disconnects to Action Areas" available at https://www.unpri.org/download?ac=5819.

§ 4:37 Some practical guidance

ESG reporting requirements and voluntary reporting regimes are propagating at a dizzying pace, and the SEC appears to be patiently watching as these developments unfold. As William Hinman has noted, "[t]he marketplace evolution of sustainability disclosures is ongoing."[1] The process of regulation will likely be long, and companies and investors are likely to face ongoing challenges as they sort what information is most useful, in what format, and in what forum.

In the interim, the guidelines outlined below might be useful for companies to consider as they navigate their ESG disclosures.

Understand that materiality is dynamic. The concept of what is material is evolving. While the U.S. Supreme Court's black letter law is the law of the land and guides what information should be disclosed, the question of what information is significant to the reasonable investor in making its investment decision is changing. ESG issues are increasingly prominent in the minds of investors and are recognized as significant to financial results. At the same time, there is no one-size-fits-all materiality analysis. Each company should assess what information would be considered important to its investors in light of the total mix of information for that company.

Break down silos. Companies must understand how ESG factors present risks and opportunities. Ideally, companies will integrate ESG factors across and through all relevant functions to enable a meaningful understanding of the risks and opportunities that ESG factors present. This understanding will facili-

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[1] William Hinman, "Applying a Principles-Based Approach to Disclosing Complex, Uncertain and Evolving Risks," Remarks at the 18th Annual Institute on Securities Regulation in Europe (Mar. 15, 2019).

tate risk mitigation, contingency planning, new market opportunities, and ultimately more meaningful reporting on companies' ESG risks and opportunities.

Treat material ESG risks like financial information. To ensure information is accurate and presented in a complete and trustworthy manner, companies are advised to treat material ESG information as if it were financial information, applying internal controls processes to their management and reporting, regardless of whether formal assurance processes are used. Ideally, ESG disclosures should be crafted in conjunction not only with a company's sustainability team, but also the legal, finance, and other relevant groups, and with executive and board-level oversight.

Explain the relevance of ESG factors to investors. Companies should disclose ESG factors in a manner that highlights material information and explains why the information is material to the company. Companies should avoid boilerplate disclosures and give meaningful context to the information disclosed.

Take a longer view. ESG risks and opportunities might not play out over quarterly or annual reporting cycles. If the risks and opportunities are material to investors, companies should consider providing disclosures that look further into the future.

Reconcile and harmonize disclosures in different locations. If a company elects to disclose ESG information in its financial reports and in separate sustainability reports or websites, it should be careful to harmonize those disclosures so they are consistent. If information is required to be reported in the company's financial reports, then the disclosure must appear there even if the information is separately disclosed in a sustainability report. Companies should be mindful that the anti-fraud provisions of the U.S. securities laws apply to disclosures outside the filed reports, including in sustainability reports or on websites. Those disclosures should be scrutinized to ensure they don't

contain materially false or misleading information or omit information necessary to make the statements made not misleading.

Use voluntary disclosure standards as tools to augment disclosures. The starting point for companies reporting under the U.S. securities laws is the law itself and the forms, rules, and regulations under the Securities and Exchange Act. The various voluntary disclosure standards can augment the SEC reporting obligations and provide guidance and structure for disclosures in the company's financial or sustainability reports, whether presented in integrated reports or separately. When considering reporting under other frameworks such as the TCFD, CDSB, SASB, and UN SDGs, companies should continue to consult the required SEC disclosure requirements as the foundation. The TCFD Implementation Guide provides a useful map that illustrates how the TCFD, SASB, and CDSB guidance can operate in concert. The WBCSD ESG Disclosure Handbook and the Corporate Reporting Dialogue, among other resources, also provide useful guidance to companies trying to reconcile the various voluntary reporting frameworks. These different standards will evolve, as will the efforts to harmonize and reconcile them, and inevitably. this landscape will continue to change over time.

§ 4:38 Conclusion

The ESG reporting landscape is dynamic, fragmented, and evolving. Companies operate in an environment in which the SEC reporting framework has remained essentially unchanged, even as much of the rest of the world is taking action to require enhanced ESG reporting. This is not to say that U.S. public companies' ESG disclosures have remained static. On the contrary, disclosures under the existing principles-based framework change as the issues material to companies evolve. However,

investors complain that the ESG information they currently receive in many companies' financial reports is too generic and is riddled with boilerplate language. These concerns have led investor groups to call for more meaningful disclosure requirements from the SEC and the U.S. Congress. Investors also have attempted to fill the informational gaps by issuing questionnaires to companies seeking further ESG data. At the same time, ESG surveys, ratings, and rankings have proliferated to meet investors' informational needs. The landscape remains crowded and confusing and marked with dissatisfaction among investors and companies. This disclosure landscape is changing and will require close attention over the coming months and years as regulatory requirements and guidance take shape, and as disclosure practices evolve.