Chapter 6

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

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§ 6:1 Introduction

Environmental, Social, and Governance (ESG) issues have been a mainstream business concern since 2015, when the Unit-

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ed 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, 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 balance liability concerns against their stakeholders' desire for more robust ESG information.

ESG disclosure is particularly challenging because it is both broad in scope, touching virtually all companies, and 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, increasingly are 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 rules from the SEC, a host of voluntary reporting standards has emerged. The reporting landscape is a patchwork of disclosure regimes that has left some issuers with questionnaire fatigue and others simply confused as to what guidance to follow and how to reconcile the different standards. These reporting frameworks reflect investors' desire for more information as to companies' ESG performance and risks. Still the lack of standardization around the frameworks leaves companies with the challenge of determining which regimes to follow and how to reconcile the different guidance. 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.

§ 6:2 ESG: An overview

ESG factors cover a broad swath and touch on all companies, and yet they do not touch on 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, because they cover a broad range of risks and opportunities and at the same time require industry-focused and company-specific information. Climate change, specifically, is a current threat that poses risks that are of significant concern. However, the potential impacts on companies' financial statements are difficult to quantify due to uncertainty concerning specific projected impacts. 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 obsta-

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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/tcfd-2019-status-report/.

cles 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]

[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-esg-data/. For a further discussion of SASB and its work, see *Voluntary Disclosure Frameworks*: Sustainability Accounting Standards Board, below.

§ 6:3 ESG issues are top of mind for many companies

The sense of urgency around climate risks is intensifying, and ESG issues have become a critical strategic and operational concern of companies across industries. McKinsey reports that its May 2019 Global Sustainability Summit was at capacity: "The crowd was the largest and most senior we've seen, which is no surprise given sustainability is now on the top of every leader's agenda."[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 McKinsey:

> We are facing two tipping points: one is economic, and one is environmental. The economic tipping point consists

[1] 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).

> 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]

The World Economic Forum echoes this sense of urgency in its 2019 Global Risk Report, which finds that "environmental risks continue to dominate the results of our annual Global Risks Perception Survey (GRPS). This year, they accounted for three of the top five risks by likelihood and four by impact. Extreme weather was the risk of greatest concern."[3] The report describes 2018 as a year of fires, storms, and floods. In addition, the report cites the acceleration of biodiversity loss as a significant concern, with compounding effects on ecosystems, climate change, and food security: "Of all risks, it is in relation to the environment that the world is most clearly sleepwalking into catastrophe."[4]

The risks are not lost on the business community. The U.S. Chamber of Commerce Foundation recently conducted a series of roundtables across the United States with a view to collecting

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[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] World Economic Forum, in partnership with Marsh & McLennan Companies and Zurich Insurance Group, "The Global Risks Report 2019," available at http://www3.weforum.org/docs/WEF_Global_Risks_Report_2019.pdf.

[4] World Economic Forum, in partnership with Marsh & McLennan Companies and Zurich Insurance Group, "The Global Risks Report 2019," available at http://www3.weforum.org/docs/WEF_Global_Risks_Report_2019.pdf.

information as to how market participants — public company board members, sustainability officers, corporate executives, institutional investors, and others — view the ESG landscape.[5] The Chamber reports, "[t]oday, more than 80% of companies in the S&P 500 publish an annual sustainability report, a roughly four-fold increase over the past decade. The broad consensus is that heightened attention to ESG topics offers value to the business community, investors, and the public, and is not expected to recede anytime soon."[6]

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

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

§ 6:4 Growing investor interest in ESG

The investor community is keenly focused on ESG issues. 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

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[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:

> 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.

2019, firms that have subscribed to the PRI control nearly $90 trillion in assets under management. According to the Global Sustainable Investment Alliance: "Globally, sustainable investing assets in the five major markets stood at $30.7 trillion at the start of 2018, a 34 percent increase in two years."[2] In the United States, the Alliance reports, "total US-domiciled assets under management using sustainable strategies grew from $8.7 trillion at the start of 2016 to $12.0 trillion at the start of 2018, an increase of 38 percent."[3]

BlackRock produced the following infographic as part of a recent study on 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.[4]

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.

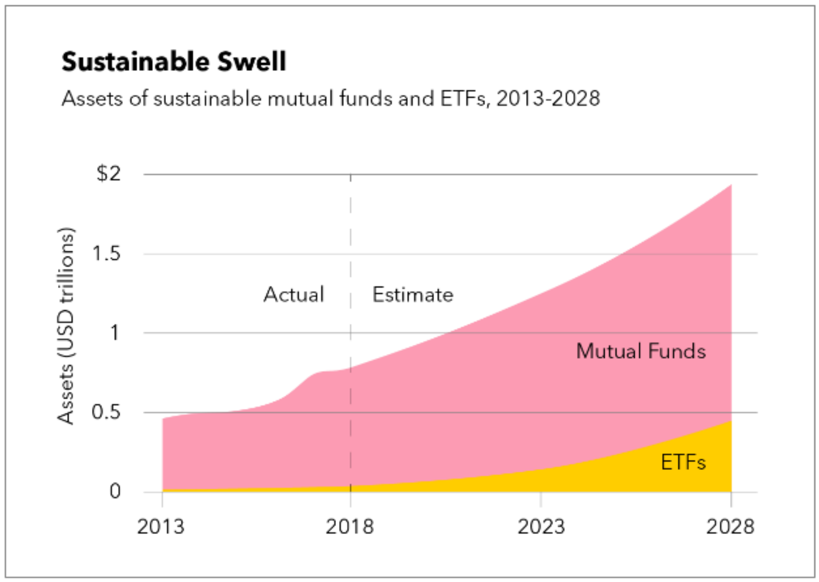
[2] Global Sustainable Investment Alliance, "2018 Global Sustainable Investment Review," available at http://www.gsi-alliance.org/wp-content/uploads/2019/03/GSIR_Review2018.3.28.pdf. The Review defines sustainable investing as investment practices that apply any of the following strategies: (1) negative/exclusionary screening, (2) positive/best-in-class screening, (3) norms-based screening, (4) ESG integration, (5) sustainability themed investing, (6) impact/community investing, and (7) corporate engagement and shareholder action.

[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] Https://www.blackrock.com/ch/individual/en/themes/sustainable-investing#esg-integration.

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.



The U.S. Chamber of Commerce report concludes that "both publicly held and private companies in the United States face increased pressure not only from investors but also from customers, employees, and others to publish more (ESG) information. For a variety of reasons, this pressure is likely to intensify."[5] The participants in the SASB roundtable agreed, citing the importance of ESG factors in helping shareholders under-

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

stand companies' risk profiles, particularly when ESG risks relate to intangible assets.[6]

Another report, issued in September 2018 by Bank of America Merrill Lynch, finds 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."[7] This report draws a strong correlation between good environmental 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.[8] The report concludes that "ESG is a better signal of earnings risk than any other metric we have found."[9]

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[6] 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/, 2.

[7] 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.

[8] 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.

[9] 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.

A 2018 survey of institutional investors by Bloomberg and the Morgan Stanley Institute for Sustainable Investing reaches a similar conclusion.[10] The survey includes 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."[11] The participants shared the view that sustainable investing 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.[12] Eighty-two percent of respondents saw strong ESG performance as a key to improved profitability and investment returns.[13] A similar 2018 survey of 260 institutional investors by EY reveals "notable consensus

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[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.

[11] 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.

[12] 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.

[13] 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.

that ESG information is critical to investor decision-making."[14] This survey also finds 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.[15] According to EY, the response to the survey represents a "dramatic increase from the 2017 survey."

A State Street Global Advisors survey of 475 global institutional investors in the United States, Europe, and Asia, including some of the largest pension plans, endowments, and foundations, draws similar conclusions.[16] 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.[17] Furthermore, 69 percent of respondents indicated that pursuing an ESG strategy has helped them manage volatility.[18] The survey points to not only risk

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[14] 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.

[15] 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.

[16] 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.

[17] 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.

[18] State Street Global Advisors, ESG Institutional Investor Survey, "Performing for the Future: ESG's place in investment portfolios. Today and

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 reputational, operational and financial risks and create commercial opportunities." State Street's Lori Heinel explains that "increasingly, there is a broader appreciation of the idea that good governance translates into better management of areas such as carbon footprint and workforce engagement. This creates better quality companies that provide better performance over the long-term."[19] The survey notes the rapid rise of ESG investments in the United States and attributes that rise in part to U.S. Department of Labor guidance that in 2015 acknowledged that ERISA-governed pension plans may properly take ESG considerations into account.[20]

The TCFD's 2019 status report finds that "there is a growing demand for decision-useful, climate-related financial information by investors. There likely are many factors driving investor demand, ranging from European regulations requiring certain investors to disclose climate-related information to weather-driven events resulting in significant financial impacts and leading investors to seek better information on their expo-

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tomorrow" (2018), available at https://www.ssga.com/investment-topics/environmental-social-governance/2018/04/esg-institutional-investor-survey.pdf.

19 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.

20 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.

sure to climate-related risks. As evidence of this demand, more than 340 investors with nearly $34 trillion in assets under management have committed to engage the world's largest corporate greenhouse gas emitters to strengthen their climate-related disclosures by implementing the TCFD recommendations as part of Climate Action 100+."[21]

A recent Goldman Sachs equity report emphasizes the investment value of ESG integration and the still untapped potential in applying ESG factors in the investment process: "We believe the potential benefits of ESG are underutilized by asset managers. In our view, ESG integration offers a differentiated and alpha-additive complement to fundamental analysis with the added benefit of helping to attract and retain a growing pool of assets. As corporate disclosures and dialog continues to improve, investors will be better able to assess ESG's influence on a company and stock performance, helping to further deliver alpha and refine engagement."[22]

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[21] 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 iii.

[22] 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.

§ 6:5 Current state of disclosures in financial reports: Perspectives from the trenches

The SASB and the Harvard Law School hosted a roundtable in June 2017 that examined the legal issues and practices around U.S. public companies' sustainability disclosures.[1] This group included 29 leading scholars and practitioners from law schools, businesses, the nonprofit sector, law, and accounting. The group touched on a number of issues at the heart of U.S. public companies' disclosures, as discussed below.

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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.

§ 6:6 —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] Put 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 raises 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,

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

as a rule, thought to be material. Times have changed, and ESG information is now important to mainstream investors. At the Harvard legal roundtable, "one participant noted that in a 2015 survey of 1,325 CFA Institute members (portfolio managers and analysts), 73 percent said they use environmental, social and governance data in their investment analysis and decisions. . . . 'If 73 percent of sophisticated investors are using the information, we can almost stop right there when asking if this is material information.'"[2] It is commonly accepted that in many circumstances, ESG information is 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.

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[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, citing CFA Institute, "Environmental, Social and Governance (ESG) Survey" (June 2015).

§ 6:7 —The quarterly earnings call

One of the Harvard legal roundtable participants argued that ESG information is perhaps not as important as some maintain. He noted that financial analysts appeared not to be asking about sustainability disclosures on quarterly earnings calls. That commenter postulated that sustainability information is perhaps not altogether significant to investors, or at least to the analysts covering the earnings calls.[1] If true, then this would seem to point to a misalignment between the financial analysts covering the quarterly earnings calls and the broader investor community calling for greater disclosure of ESG factors, as indicated in the CFA survey.

One theory advanced during the Harvard legal roundtable 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 that in some cases 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 the quarterly calls. Furthermore, some of the roundtable participants questioned whether risks with a long time horizon of perhaps five or ten years should be considered material or, at least from a civil liability perspective, whether their omission would be actionable.[3] All of 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,

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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.

[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.

therefore, not necessarily relevant to decisions made today. Those views, however, have begun to change."[4] The 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 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 roundtable, "Disclosure of sustainability information may not be useful to investors and analysts until

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

they better understand it, but they cannot develop their understanding until the information is being widely disclosed."[7]

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

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[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.

[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.

§ 6:8 —Identifying the ESG information that is material to the particular company

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. A key to bridging this divide is for companies to evaluate and discuss the ESG information that is most important to their performance now and in the future. One SASB roundtable participant expressed a desire for "a methodology that pulls out the relevant pieces and uses those as guideposts."[1] 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."[2] Due to the bespoke nature of sustainability risks, the SASB emphasizes that the materiality determination must be made by each company 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. The 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 sus-

[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-esg-data/, at 17.

[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-esg-data/, at 18.

tainability impacts, and then enter into a dialogue with key stakeholders — which they define themselves — to answer the question 'What 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."[3] This definition of materiality differs from that applied under the U.S. securities laws, and this difference can lead to confusion and concern over 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."[4] 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

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[3] 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.

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

by our legal team to reserve that term (materiality) for financial filings."[5]

Inherent in the discussion of materiality is the idea that the information that is important to investors evolves over time. We are in a period of change. Investors' informational needs are changing, and 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.[6] According to the Harvard legal roundtable, "[t]his ability of the disclosure regime to evolve alongside the reasonable investor is crucial in today's market, where broad macroeconomic trends such as population growth, globalization, and technological innovation have contributed to environmental and social impacts such as climate change, resource scarcity, and rising economic inequality."[7]

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[5] 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 10.

[6] 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/.

[7] 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 8.

§ 6:9 —Who "owns" sustainability disclosures? Silos within companies

Some of the Harvard legal roundtable participants suggested that while companies commit significant resources to sustainability efforts, those resources 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. 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 re-

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

porting 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.

One potential cause for ships passing in the night over ESG within some companies is the lack of a common language 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."[4] Others cautioned, however, that "speaking the

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[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.

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

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."[5] 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.

//library.sasb.org/dead-cobras-faberge-eggs-unlocking-the-potential-of-esg-data/, at 1.

[5] 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.

§ 6:10 —Proliferation of 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

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

teams of employees to filling out surveys or responding to third parties about ESG matters.”[2]

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 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.”[3] The legal roundtable participants expressed concern that some companies are spending significant sums to provide sustainability information to stakeholders, but without running that information through the rigor of 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 impact their economic value.

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

[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, at 7.

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 to disclose."[4] 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."[5] 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."[6] It bears noting that 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

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

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

[6] 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.

how well a company is run. Such scores can also forecast potential risks or untapped opportunity."[7]

The participants in the SASB roundtable 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.'"[8]

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 Sustainable Accounting Standards Board (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

[7] 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-sustain ability-ratings.

[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 2.

sustainability and impact remains paramount to overcoming this challenge."[9]

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 nonfinancial disclosure."[10] 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: "Nonfinancial 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 when they include due diligence mechanisms to achieve not only greater disclosure but also performance improvements."[11]

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[9] 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.

[10] 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/.

[11] 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.

§ 6:11 —Imperfect fit between the information that investors want and the information they receive

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 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 information that investors want in order to properly incorporate companies' sustainability performance in their capital allocation decisions.[1] 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.[2]

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[1] 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.

[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, at 2.

The study participants indicated the factors that would enhance their confidence in and ability to make use of 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.[3] According to the WBCSD: "Investors want 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."[4]

The study participants also articulated the difficulty of incorporating non-financial information in their valuation models. The investors interviewed emphasized the importance of providing ESG metrics for comparability across companies and within companies across time. However, the metrics alone are of limited use without narrative discussions that explain how the data are relevant to companies' performance and outlook.[5]

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[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 (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 7.

The SASB roundtable participants expressed similar frustration, noting investors' "increasing appetite" for high-quality ESG information. While companies are providing huge amounts of information at significant expense, at the end of the day, the roundtable participants noted, "investors are overwhelmed by the amount of information" and left searching for needles in a haystack.[6] The corporate participants in the roundtable discussion expressed their own frustration with the proliferation of questionnaires, with one participant bemoaning the litany of questionnaires and surveys that "just doesn't end."[7] Recognizing the state of mutual dissatisfaction, participants arrived at the conclusion that there is a need for an ongoing dialogue between the investor and corporate communities to come to a better solution. Ultimately, a central theme that emerged is that "as relatively new practices, ESG reporting and integration are — and should be — works in progress."[8]

The SASB issued a report in 2017 that provides its assessment of the effectiveness of sustainability disclosures in SEC filings. The report bases its conclusions on the SASB's review and analysis of sustainability disclosures in hundreds of SEC filings across industries. Consistent with the other discussions

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[6] 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 3.

[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 3.

[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 12.

noted above, the SASB report finds 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 declares: "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 finds that most sustainability disclosures rarely include sustainability performance metrics and typically consist of boilerplate language "which is largely useless to investors."[10]

The Bank of America Merrill Lynch report finds a similar disconnect between U.S. companies' and investors' views of the importance of ESG factors to the investment process. The report results indicate that more than 25 percent of institutional investors reported using ESG factors in their investment process. Notwithstanding that significant investor interest in ESG, issu-

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[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.

ers estimated that less than five percent of their outstanding shares are managed by ESG-focused investors.[11]

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[11] 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.

§ 6:12 Current reporting framework in the United States

The sections that follow discuss the current reporting framework for ESG disclosure in the United States, including Regulation S-K disclosure items and 2010 Commission interpretive guidance related to climate change. Proposed modifications to the SEC reporting framework are also discussed below.

§ 6:13 —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 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 —

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[1] 17 CFR § 229.

[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.

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] The Commission issued guidance regarding disclosures related to climate change in 2010 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.

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[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).

§ 6:14 — —Item 101 of Regulation S-K: Description of business

Item 101(c)(1)(xii) requires "disclosure of material effects that compliance with Federal, State and local (environmental laws and regulations) may have upon the capital expenditures, earnings and competitive position of the registrant." Item 101 also requires disclosure of material anticipated capital expenditures for environmental controls for the current and following fiscal year and such longer period as the registrant deems material.[1] The laws or regulations that could materially impact a

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[1] 17 CFR § 229.101(c)(1)(xii).

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 United States had not ratified the Kyoto Protocol, it nonetheless could materially impact U.S. registrants with operations outside the United States that are subject to its standards.

§ 6:15 — —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 registrant or any of its subsidiaries is a party or to which their property is subject. The requirement excludes ordinary, routine litigation that is incidental to the registrant's or its subsidiaries' business. However, with regard to this exclusion of routine litigation, Instruction 5 to Item 103 includes a specific discussion of environmental litigation or other legal proceedings. The instruction provides that 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 $100,000. The Division of Corporation Finance's Office of Chief Counsel has 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.

§ 6:16 — —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 most significant factors that make an investment in the registrant or offering speculative or risky." The item

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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.

cautions against disclosures that present risks that "could apply generically to any registrant or any offering."

§ 6:17 — —Item 303 of Regulation S-K: Management's Discussion and Analysis of Financial Condition and Results of Operations (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 also are 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. They are:

- To provide a narrative explanation of a registrant's financial statements that enables investors to see the registrant through the eyes of management.
- To enhance the overall financial disclosure and provide the context within which financial information should be analyzed.
- To provide information about the quality of, and potential variability of, a registrant's earnings and cash flow,

[1] 17 CFR § 229.303.

> 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 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 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

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[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.

[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

not quantified any specific future time period that must be considered in evaluating the events that might have a material effect 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 it is unlikely to do so, then no disclosure is required. If the registrant cannot make the determination that the event is unlikely to occur, then it must assess whether it 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 out 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]

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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.

[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.

§ 6:18 — —Disclosure requirements for 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).

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[1] 17 CFR § 249.220f.

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

- 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]

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

§ 6:19 —2010 Interpretive Release

The 2010 Interpretive Release provides guidance as to some of the ways in which climate change risks and opportunities might require disclosure under the reporting provisions discussed above. The examples provided are illustrative and not necessarily exhaustive.

§ 6:20 — —Impact of legislation, regulation, and international accords

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.

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

§ 6:21 — —Indirect consequences of regulation or business trends

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

§ 6:22 — —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.

§ 6:23 —Proposed modifications to the SEC reporting framework

Following is a discussion of proposed modifications to the SEC reporting framework. The discussion includes a review of the Commission's 2016 concept release on business and financial disclosure required by Regulation S-K as well as amendments to Regulation S-K the Commission proposed in August 2019.

§ 6:24 — —Concept Release on business and financial disclosure required by Regulation S-K

On April 13, 2016, the Commission issued a concept release pursuant to the Commission's Disclosure Effectiveness Initiative (Concept Release).[1] The Concept Release sought public comment broadly on modernizing the disclosure requirements in Regulation S-K. It also specifically sought comment on the disclosure requirements related to ESG issues. The Commission provided that the disclosure regime as it relates to ESG issues is essentially the same as it was in 1975, when the Commission last considered environmental and social disclosure matters.[2]

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[1] Sec. Act Release No. 10064 (Apr. 13, 2016), available at https://www.sec.gov/rules/concept/2016/33-10064.pdf. Sec. Act Release No. 9106 (Feb. 8, 2010), at 16. The SEC's Spotlight on Disclosure Effectiveness website explains the Disclosure Effectiveness Initiative: "The Division of Corporation Finance is reviewing the disclosure requirements in Regulation S-K and Regulation S-X, which provides requirements for financial statements, and is considering ways to improve the disclosure regime for the benefit of both companies and investors. The goal is to comprehensively review the requirements and make recommendations on how to update them to facilitate timely, material disclosure by companies and shareholders' access to that information." See https://www.sec.gov/spotlight/disclosure-effectiveness.shtml.

[2] Sec. Act Release No. 10064 (Apr. 13, 2016), available at https://www.sec.gov/rules/concept/2016/33-10064.pdf, at 209, citing "Environmental and Social Disclosure," SEC Release No. 33-5627, 40 FR 51656 (Nov. 6, 1975). This release was the subject of litigation and a measure of handwringing by the SEC, which might account, at least in part, for the decades-long stasis on environmental disclosure requirements. See Natural Resources Defense Council v. SEC, 606 F.2d 1031 (D.C. Cir. 1979). The case addressed an NRDC petition that asked the SEC to adopt rules requiring disclosure of

However, the Commission observed that "the role of sustainability and public policy information in investors' voting and investment decisions may be evolving as some investors are increasingly engaging on certain ESG matters."[3]

The Concept Release solicited comments on a number of issues related to ESG disclosures. It queried whether line-item disclosure requirements for sustainability would be beneficial, or whether they might prompt disclosure of immaterial information. It invited comment on whether the Commission should draw on any of the existing standards that currently frame voluntary sustainability disclosures and, if so, which standard should be used. It requested input on whether sustainability disclosures should appear in the documents filed with the Commission or whether registrants should make sustainability disclosures in stand-alone reports or on websites. It also sought comment on the challenges that registrants would face — including costs incurred — in preparing and providing enhanced ESG information.

The Concept Release received a significant response from commenters. An analysis by the SASB notes that the comments were disproportionately focused on sustainability disclosures, given the space allotted to the issue in the Concept Release. Out of the Concept Release's 92 pages (as published in the *Federal Register*), only four pages were devoted to sustainability disclosures. Yet according to the SASB, "the large majority of comment letters on the Concept Release addressed sustainability

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environmental and equal opportunity practices. After seven years of proceedings, the SEC declined to adopt the proposed rules, leading to the NRDC's suit in which the SEC ultimately prevailed at on appeal.

[3] Sec. Act Release No. 10064 (Apr. 13, 2016), available at https://www.sec.gov/rules/concept/2016/33-10064.pdf, at 211.

issues."[4] Specifically, of the 276 non-form comment letters, two-thirds addressed sustainability disclosures, with most of the letters supporting improved sustainability-related disclosures.[5] One comment letter pointedly declared that "the sustainability topic is clearly on the table at this point, and the Commission will sooner or later have to — and should — address it."[6]

A resounding theme in the comments is that there is a need to improve the quality of ESG disclosures. As Keith Higgins, then the Director of the Division of Corporation Finance, has observed, "Many of the commenters found voluntary disclosures to be inconsistent, difficult to find, and often not comparable and lacking in context."[7]

The SASB analysis concludes that the leading issue among those who commented on sustainability factors is climate change, with 51 percent of the sustainability-focused comment

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[4] SASB, "Business and Financial Disclosure Required by Regulation S-K — the SEC's Concept Release and Its Implications," available at https://www.sasb.org/wp-content/uploads/2016/09/Reg-SK-Comment-Bulletin-091416.pdf.

[5] SASB, "Business and Financial Disclosure Required by Regulation S-K — the SEC's Concept Release and Its Implications," available at https://www.sasb.org/wp-content/uploads/2016/09/Reg-SK-Comment-Bulletin-091416.pdf, at 3.

[6] SASB, "Business and Financial Disclosure Required by Regulation S-K — the SEC's Concept Release and Its Implications," available at https://www.sasb.org/wp-content/uploads/2016/09/Reg-SK-Comment-Bulletin-091416.pdf, at 3, quoting Sullivan & Cromwell LLP, Business and Financial Disclosure Required by Regulation S-K — File No. S7-06-16. Comment letter to the Securities and Exchange Commission (Aug. 9, 2016).

[7] "The SEC and Improving Sustainability Reporting: SASB 2016 Symposium," Journal of Applied Corporate Finance, Vol. 29, No. 2 (Dec. 1, 2016), at 3.

letters calling for improved climate change disclosures.[8] Other issues raised include access to and stewardship of water, land tenure rights, lobbying and political spending, diversity, gender pay equity, human rights, human capital management, sustainable palm oil, forestry, and supply-chain management.[9] The top five topics discussed in the comment letters, in descending order, are: improved disclosure on climate change, improved disclosure of human rights and human capital issues, disclosure of political spending and lobbying, improved disclosure of diversity, and improved disclosure with regard to water.[10]

Many of the comment letters stressed the importance of adhering to materiality as the North Star in determining what information should be disclosed. For example, a letter submitted by the Federal Regulation of Securities Committee of the American Bar Association (ABA) Business Law Section provided that the Committee agrees with "the Commission's long-standing position that disclosure relating to environmental and other matters of similar concern should not be required of all registrants unless, under the particular facts and circumstances,

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[8] SASB, "Business and Financial Disclosure Required by Regulation S-K — the SEC's Concept Release and Its Implications," available at https://www.sasb.org/wp-content/uploads/2016/09/Reg-SK-Comment-Bulletin-091416.pdf.

[9] The SASB summary provided that the SASB itself has not determined that all of these issues likely encompass material information across all industries and therefore are not all included in the SASB disclosure framework. See SASB, "Business and Financial Disclosure Required by Regulation S-K — the SEC's Concept Release and Its Implications," available at https://www.sasb.org/wp-content/uploads/2016/09/Reg-SK-Comment-Bulletin-091416 .pdf.

[10] SASB, "Business and Financial Disclosure Required by Regulation S-K — the SEC's Concept Release and Its Implications," available at https://www.sasb.org/wp-content/uploads/2016/09/Reg-SK-Comment-Bulletin-091416.pdf, at 6.

such matters are important to the reasonable investor (i.e., material information)."[11] This materiality assessment is particularly significant in the context of ESG disclosures when the issues are varied and their impact is company-specific. According to the Committee, "ESG issues encompass a wide and diverse range of issues from climate change to sustainable business practices to human capital management. Even with a particular topic, such as the impacts of climate change, the issues will vary significantly from industry to industry and from registrant to registrant."[12]

The comment letters were divided as to whether the Commission should adopt line-item disclosure requirements related to sustainability, with 26 percent of the sustainability-focused comment letters supporting line-item disclosure requirements and 21 percent opposing such requirements.[13] The SASB itself opposed a line-item disclosure requirement. "Sustainability issues are not material for all companies, and when they are material, they manifest in unique ways and require industry-specific metrics. Requiring generally applicable line-item disclosures would result in additional corporate reporting burden and disclosure of a large volume of information that is immaterial to

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[11] Comment Letter submitted by the ABA Business Law Section, Federal Regulation of Securities Committee on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (Dec. 15, 2017).

[12] Comment Letter submitted by the ABA Business Law Section, Federal Regulation of Securities Committee on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (Dec. 15, 2017).

[13] SASB, "Business and Financial Disclosure Required by Regulation S-K — the SEC's Concept Release and Its Implications," available at https://www.sasb.org/wp-content/uploads/2016/09/Reg-SK-Comment-Bulletin-091416.pdf, at 6.

investors."[14] Rather, the SASB advocated for the adoption of a market standard for industry-wide sustainability information calibrated to the specific and evolving sustainability issues that are material within different industries. The ABA Committee letter, similarly, expressed concern over mandatory line-item disclosures: "Line-item requirements may result in a significant number of registrants being required to make immaterial disclosure that is costly to prepare and not necessarily helpful to investors."[15] A comment letter submitted by the Nasdaq Stock Market (Nasdaq) similarly expressed the stock exchange's preference for a principles-based disclosure system rather than rules-based, line-item disclosure requirements: "While rules-based disclosure may facilitate comparability of information provided by public companies, a forced template regime increases the cost and complexity of producing the reports. Nasdaq believes that principles-based disclosure grounded in materiality allows companies the degree of flexibility needed to provide investors with the proper amount and mix of information . . . (applying a materiality analysis) investors are assured that unnecessary detail does not obscure important disclosure, while at the same time, all material information is disclosed."[16]

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[14] Comment Letter submitted by the Sustainability Accounting Standards Board on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (July 1, 2016).

[15] Comment Letter submitted by the ABA Business Law Section, Federal Regulation of Securities Committee on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (Dec. 15, 2017), at 9.

[16] Comment Letter submitted by Nasdaq on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (Sept. 16, 2016).

The U.S. Chamber of Commerce articulated the concern, echoed by other commenters, that prescriptive disclosure requirements can force companies to disclose information that is immaterial and unhelpful to investors, and that can have the effect of obscuring material information that investors do need. "Information overload strikes a blow to the effectiveness of the disclosure regime that the SEC administers," the Chamber stated. "The essential problem is that investors become inundated with information that is not useful, making it difficult to identify important information about a business." Instead, "we must be vigilant in applying the test of materiality."[17]

PRI's comment letter, consistent with many others, embraced materiality as the appropriate standard for assessing what should be disclosed but took a different position with regard to prescriptive versus principles-based disclosure obligations. "The existing materiality standard used by the Commission is familiar to the investment community and ought to be maintained," PRI stated. "The Commission should continue to use a mix of principles-based and prescriptive or rules-based disclosures."[18] Like many others, the PRI comment letter expressed concern over generic disclosures that are costly to produce and unhelpful to investors: "The production and analysis of disclosures both have significant costs associated with them, particularly where the information produced has a low signal to

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[17] Comment Letter submitted by the U.S. Chamber of Commerce on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (July 20, 2016).

[18] Comment Letter submitted by Principles for Responsible Investment on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (July 19, 2016).

noise ratio, is immaterial to an assessment of the business or generic in nature."[19]

Rather than advocate for a pure principles-based disclosure framework as some commenters did, the PRI proposed that the Commission require inclusion of ESG data in the annual report with connection back to the company's core business. The ESG data would be subject to assurance, consistent with financial disclosures. Registrants would be required to report "using common performance metrics to allow for comparability, in particular, comparability by industry, portfolio and across time-series. The Commission should codify industry and sector specific KPIs for ESG factors within Regulation S-K."[20] This idea of tying disclosures to a common industry-specific framework echoes the SASB comment letter. While the SASB letter opposed line-item disclosure requirements, it advocated for industry-specific sustainability guidelines to help companies identify the material issues facing their businesses. The SASB asked the Commission to acknowledge its standards as an acceptable disclosure framework for use by companies preparing their SEC filings.[21]

Notwithstanding some commenters' call for more prescriptive disclosure requirements, the Commission and its staff appear to favor continued adherence to a principles-based ap-

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[19] Comment Letter submitted by Principles for Responsible Investment on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (July 19, 2016).

[20] Comment Letter submitted by Principles for Responsible Investment on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (July 19, 2016).

[21] Comment Letter submitted by the Sustainability Accounting Standards Board on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064; 34-77599; File No. S7-06-16 (July 1, 2016).

proach. William Hinman, the Director of the Division of Corporation Finance, made the case for a principles-based approach in a March 2019 speech: "The very breadth of (ESG) issues illustrates the importance of a flexible disclosure regime designed to elicit material, decision-useful information on a company-specific basis."[22] Hinman also indicated his view that the dynamic nature of ESG issues militates in favor of the SEC's waiting for the market to settle before it makes any significant modifications to the disclosure requirements: "We recognize that market participants have raised questions about the sufficiency of sustainability disclosures, and I think this is a complicated issue. . . . We hear differing views on whether disclosure requirements should be principles-based or prescriptive, and whether they should utilize a specific set of reporting standards to enhance comparability. So it appears to me that the market is still evaluating what, if any, additional disclosure on these topics would provide consistently material and useful information."[23] The GAO issued a report to Congress in February 2018 concluding that the SEC had taken appropriate steps to clarify its disclosure requirements with regard to climate-related risks.[24]

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[22] 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).

[23] 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).

[24] United States Government Accountability Office Report to Congressional Requesters, "Climate-Related Risks: SEC Has Taken Steps to Clarify Disclosure Requirements," GAO 18-188 (Feb. 2018), available at https://www.gao.gov/assets/700/690197.pdf.

§ 6:25 — —August 2019 proposed amendments to Items 101, 103 and 105 of Regulation S-K

On August 8, 2019, the Commission issued proposed rule amendments to update Items 101, 103 and 105 of Regulation S-K.[1] The release refers extensively to the 2016 Concept Release. It leaves some of the concerns expressed in comment letters unresolved while addressing certain others. The proposed rules do not address the comments that advocate for application of the SASB standards. They largely maintain the status quo with regard to environmental disclosures, while encouraging registrants to calibrate their disclosures based on their materiality assessments. The proposals would expand the disclosure requirements related to human capital in recognition of the importance of intangible assets to companies' value.

The release explains that the proposed amendments are designed to improve the readability of disclosure documents, reduce repetition of information, and discourage disclosure of information that is not material. The release proposes a more principles-based approach to disclosures in Items 101 (Description of Business) and 105 (Risk Factors) and a prescriptive approach to Item 103 (Legal Proceedings). The Commission explains that the proposed principles-based approach to Items 101 and 105 reflects its concern that the current disclosure requirements might not elicit disclosures that are material to all companies. The release does not propose amendments to Item 303 (MD&A).

The proposed amendments would retain many of the specific line item disclosure requirements in Item 101 with an overlay of materiality that would clarify that disclosure is not required of immaterial information. The release also makes clear that in-

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[1] Sec. Act Release No. 10668 (Aug. 8, 2019).

formation material to the business should be disclosed even if not specifically enumerated in Item 101.

The revised rules would retain the requirement in Item 101(c) to disclose the source and availability of raw materials in recognition that raw materials are fundamental to businesses that depend on them. However, businesses for which the availability of raw materials is not material would not be required to disclose information concerning raw materials.

The proposals would retain the current requirement in Item 101(c) of disclosure of the material effects of compliance with material environmental laws and would expand the item to include compliance with material government regulations generally. The proposal would retain the requirement for disclosure of material estimated capital expenditures for environmental control facilities.

The revised rules would not require disclosure of additional specific expenditures related to environmental compliance as proposed by some commenters on the 2016 Concept Release. "We believe that a more principles-based approach would permit a registrant to tailor its disclosure by focusing on the effects of environmental compliance that are material to its particular business."[2] Further, "Our proposed approach is consistent with the views of several commenters that supported the retention of Item 101(c)'s environmental compliance provisions while opposing its expansion."[3] Not all of the Commissioners were so enthusiastic about this approach. Commissioners Jackson and Lee expressed their concern "about the shift toward a principles-based approach to disclosure and the absence of the topic of climate risk." Further, "Our concern is that the proposal's

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[2] Sec. Act Release No. 10668 (Aug. 8, 2019), at 43.

[3] Sec. Act Release No. 10668 (Aug. 8, 2019).

principles-based approach will fail to give American investors the information they need about the companies they own."[4] Commissioners Jackson and Lee encouraged commenters to step forward to help to ensure that Regulation S-K encourages transparency and meaningful, comparable disclosures.

The proposed revisions to Item 103 would, among other things, retain the existing required disclosure of any proceeding under environmental laws to which a governmental authority is party. However, the carve-out in Instruction 5.C for matters as to which the registrant reasonably believes it will not be subject to sanctions of $100,000 or more would be modified and the threshold increased to $300,000 to reflect inflation.

The release proposes new human capital disclosures by expanding Item 101(c)(1)(xiii), which currently requires disclosure of the number of employees employed by the registrant. Many commenters in response to the 2016 Concept Release recommended expanding the existing requirement to help investors understand the risks of potential material labor and human rights violations.[5] The Commission emphasizes the significance of human capital as an important intangible asset.

> Today, intangible assets represent an essential resource for many companies. Because human capital may represent an important resource and driver of performance for certain companies, and as part of our efforts to modernize disclosure, we propose to amend Item 101(c) to refocus registrants' human capital resources disclosures. Specifically, we propose replacing the current requirement to

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[4] Joint Statement of Commissioners Robert J. Jackson, Jr. and Allison Herren Lee on Proposed Changes to Regulation S-K (Aug. 27, 2019), available at https://www.sec.gov/news/public-statement/statement-jackson-lee-082719.

[5] Sec. Act Release No. 10668 (Aug. 8, 2019), at 44-45.

> disclose the number of employees with a requirement to disclose a description of the registrant's human capital resources, including in such description any human capital measures or objectives that management focuses on in managing the business, to the extent such disclosures would be material to an understanding of the registrant's business.[6]

The proposed new disclosure provision would require "a description of the registrant's human capital resources, including in such description any human capital measures or objectives that management 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 attraction, development and retention of personnel)."[7] The release solicits comment as to, among other matters, whether the new disclosure requirement should include prescriptive disclosure provisions or remain principles-based, as proposed.

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[6] Sec. Act Release No. 10668 (Aug. 8, 2019), at 48. The Commission's focus on the growing value of intangible assets echoes the report of the Conference Board's Integrated Reporting Working Group, discussed below.

[7] Sec. Act Release No. 10668 (Aug. 8, 2019), at 110.

§ 6:26 Further proposals for reform

The drumbeat for enhanced disclosure requirements continues.[1] Some of the recent calls for further action include those described below.

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[1] See James R. Barrett, Paul A. Davies, and Kristina S. Wyatt, "U.S. House Financial Services Committee Holds Landmark Hearing on ESG Reporting," Latham & Watkins Environment, Land & Resources Blog (July

22, 2019), available at https://www.globalelr.com/2019/07/us-house-financial-services-committee-holds-landmark-hearing-on-esg-reporting/.

§ 6:27 —October 2018 rulemaking petition

In October 2018, a group of academics, investors, and others petitioned the SEC to build a framework that would require public companies to disclose ESG impacts related to their businesses.[1] The petition, which was signed by CalPERS, the New York State Comptroller, the PRI, various state treasurers, investors, academics, and others, asks the SEC to develop a cohesive ESG reporting framework. Specifically, the petition:

- Asks the Commission to conduct rulemaking to develop a comprehensive ESG disclosure framework.
- Discusses the materiality of ESG issues.
- Describes the existing calls for standardized ESG disclosure by large asset managers.
- Discusses the importance of standardized ESG disclosure for companies and the competitiveness of the U.S. capital markets.
- Notes the existing rulemaking petitions, shareholder proposals, and stakeholder engagement on a number of top-

[1] Cynthia A. Williams and Saul A. Fox, Petition for Rulemaking on Environmental, Social and Governance Disclosure (Oct. 1, 2018), available at https://www.sec.gov/rules/petitions/2018/petn4-730.pdf.

> ics under the umbrella of ESG, and suggests that "it is time for the SEC to bring coherence to this area."[2]

The petition cites a Harvard Kennedy School report that found that, as of 2015, 23 countries had enacted legislation within the prior 15 years requiring public companies to issue reports that include environmental and/or social information.[3] Further, seven stock exchanges require social and/or environmental disclosures as part of their listing requirements. The petition emphasizes that while 93 percent of the largest companies globally report on ESG factors, the quality and comparability of the data are not good and "the information . . . is of limited practical use."[4]

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[2] Cynthia A. Williams and Saul A. Fox, Petition for Rulemaking on Environmental, Social and Governance Disclosure (Oct. 1, 2018), available at https://www.sec.gov/rules/petitions/2018/petn4-730.pdf. (Introductory letter to rule proposal).

[3] Cynthia A. Williams and Saul A. Fox, Petition for Rulemaking on Environmental, Social and Governance Disclosure (Oct. 1, 2018), available at https://www.sec.gov/rules/petitions/2018/petn4-730.pdf., at p.5, citing Initiative for Responsible Investment, *Corporate Social Responsibility Disclosure Efforts by National Governments and Stock Exchanges* (Mar. 12, 2015), available at http://hausercenter.org/iri/wp-content/uploads/2011/08/CR-3-12-15.pdf.

[4] Cynthia A. Williams and Saul A. Fox, Petition for Rulemaking on Environmental, Social and Governance Disclosure (Oct. 1, 2018), available at https://www.sec.gov/rules/petitions/2018/petn4-730.pdf, citing Klaus Dingwerth & Margot Eichinger, *Tamed Transparency: How Information Disclosure Under the Global Reporting Initiative Fails to Empower,* 10:3 GLOBAL ENV. POL. 74, 88 (2010).

§ 6:28 —Climate Risk Disclosure Act (Senate Bill 2018)

In September 2018, Senator Elizabeth Warren introduced a bill proposing adoption of the Climate Risk Disclosure Act.[1] The bill, if enacted, would amend the Exchange Act to, among other things, require the evaluation and disclosure of the financial impact of physical and transition risks posed by climate change and a description of the established corporate governance structures in place to assess and manage climate-related risks. The Commission would be directed to adopt rules to provide guidance to allow for comparison within and across industries using standardized industry-specific metrics. The rules also would require disclosure of GHG emissions, fossil fuel assets owned, and an allocated price of carbon to apply to the issuer's climate-related disclosure statements.

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[1] Climate Risk Disclosure Act of 2018, S. 3481, 115th Congress (2017-2018).

§ 6:29 —Climate Risk Disclosure Act (House Bill 2019)

In July 2019, Representatives Sean Casten and Matt Cartwright introduced their own bill to propose adoption of the Climate Risk Disclosure Act.[1] This bill, similar to Senator Warren's bill, would amend the Exchange Act to require registrants to disclose information in their annual reports concerning physical and transition risks posed by climate change, as well as the registrants' mitigation efforts undertaken to reduce the impact of such risks. Registrants also would be required to discuss the corporate governance processes in place to assess and manage

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[1] Climate Risk Disclosure Act of 2019, H.R. 3623, 116th Congress (2018-2019).

their climate-related risks. The Commission would be directed to enact rules in specified industries that, among other things, set forth reporting standards for estimating and disclosing the direct and indirect GHG emissions and assign a social cost of carbon to such registrants' activities.

§ 6:30 —ESG Disclosure Simplification Act of 2019 (House Bill 2019)

In July 2019, Representative Juan Vargas introduced the ESG Disclosure Simplification Act of 2019, which would require the disclosure of ESG information and the formation of a Sustainable Finance Advisory Committee.[1] The proposed ESG disclosure requirements include annual proxy statement disclosure of the link between ESG metrics and the issuer's long-term business strategy, as well as the processes the issuer uses to determine the impact of ESG metrics on its business strategy. The bill would require the SEC to mandate disclosure of ESG factors in filings requiring audited financial statements. The bill also would establish the Sustainable Finance Advisory Committee to advise the Commission on sustainable finance and report on opportunities and challenges for investors associated with sustainable finance. The Committee would further provide policy recommendations to the SEC related to facilitating the flow of capital to ESG investments.

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[1] ESG Disclosure Simplification Act of 2019, H.R. 4329, 116th Congress (2018-2019). The bill was passed by the House Financial Services Subcommittee on September 20, 2019.

§ 6:31 —Corporate Human Rights Risk Assessment, Prevention, and Mitigation Act of 2019

This House bill would amend the Exchange Act to require registrants to disclose information about their human rights practices.[1] Registrants would be required to conduct an annual analysis to identify and rank by severity any human rights risks in their operations and supply chains. Registrants would be required to disclose in their annual reports information related to their human rights risks and impacts, and any mitigation efforts undertaken to reduce such risks and impacts.

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[1] Corporate Human Rights Risk Assessment, Prevention, and Mitigation Act of 2019 (Draft), H.R.__, 116th Congress (2018-2019).

§ 6:32 —California Law on Public Employees' Retirement Fund and Teachers' Retirement Fund: Investments: Climate-related financial risk

California enacted a law in September 2018 that requires the California Public Employees' Retirement System (CalPERS) and the California State Teachers' Retirement System (CalSTRS), two of the country's largest pension plans, to analyze and report on the material climate-related risks in their portfolios.[1] The law, which will be effective between 2020 and 2035, requires the boards of CalPERS and CalSTRS to report every three years on the climate-related financial risk of their public market portfolios and their exposure to long-term risks.

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[1] Public Employees' Retirement Fund and Teachers' Retirement Fund: Investments: Climate-related financial risk, S.B. 964 (Sept. 23, 2018).

§ 6:33 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 Institutional Shareholder Services Inc. (ISS) in June 2019.[1] Fifteen environmental and social proposals were filed more than 10 times each during the 2019 proxy season. Environmental proposals received record rates of support in 2019, with 48 percent of such proposals receiving support from more than 30 percent of votes cast.[2]

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 that may have appeared disconnected from investment management fundamentals. However, as ESG integration

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[1] Kosmas Papadopoulos, "Early Review of 2019 U.S. 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] 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.

> 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.[3]

ISS reports that companies appear more likely to engage with proponents of environmental and social shareholder proposals than they were several years ago. Many companies agreed to implement environmental and social proposals in 2019, leading to proponents' withdrawal of a record number of such proposals.[4] At the same time, the number of Fortune 100 companies voluntarily reporting on their sustainability commitments has increased from 29 percent in 2016 to 69 percent in 2019.[5] This increased shareholder focus on environmental and social issues and companies' corresponding responses reflects the growing agreement that environmental and social issues are mainstream business concerns. Indeed, the discussion of environmental and social issues does not end with the annual meet-

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[3] Kosmas Papadopoulos, "Early Review of 2019 U.S. 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.

[4] Kosmas Papadopoulos, "Early Review of 2019 U.S. 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.

[5] 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.

ing. 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."[6]

[6] 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-proxy-season-takeaways/.

§ 6:34 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."

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

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 financial 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. It also includes five supporting actions to facilitate achievement of the action areas' goals: analysis, development of road maps 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

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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.

decisions."[4] The statement urges issuers to assess the materiality of ESG factors to their businesses and, when material, to disclose 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] 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 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."[6]

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[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.

[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] 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-exchanges-responds-ioscos-sustainable-finance-network.

A month prior, in May 2019, Nasdaq published its ESG Reporting Guide 2.0.[7] Nasdaq does not have specific ESG listing standards but agrees with the SEC staff's 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."[8] The reporting guide summarizes some of the key voluntary reporting frameworks and offers a road map for disclosure of the different ESG factors.[9] The road map provides 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 is-

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[7] 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.

[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, quoting Ed Knight, Nasdaq EVP and General Counsel, Comment Letter to the SEC on Concept Release (Sept. 16, 2016).

[9] 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, non-discrimination, injury rates, global health and safety, child and forced labor, and human 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.

sued 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."[10]

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[10] 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.

§ 6:35 Disclosure frameworks outside of the United States

While the focus of this chapter is the disclosure framework within the United States under the U.S. securities laws, the broader disclosure landscape beyond the United States 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 in the 50 largest economies, the PRI identified nearly 300 policy drivers that encouraged investors to consider long-term indica-

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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.

tors of value, such as ESG factors. Nearly half of those 300 policy drivers were implemented between 2013 and 2016.[2]

"We found a strong correlation between responsible investment regulation and better ESG risk management by companies," the PRI reported. "This is encouraging, especially given how recent many of these policies are."[3] 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 the initiatives in the European Union and China to align sustainability and financial market objectives.[4]

More recently, the United Kingdom adopted a Green Finance Strategy.[5] This move follows closely on the heels of its enactment of legislation committing the UK to achieve net zero GHG emissions by 2050.[6] The Green Finance Strategy's objectives

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

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

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

[5] 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.

[6] UK Department for Business, Energy & Industrial Strategy and Chris Skidmore MP, "UK Becomes First Major Economy to Pass Net Zero Emis-

are "to align private sector financial flows with clean, environmentally sustainable and resilient growth, supported by Government action. To strengthen the competitiveness of the UK financial sector."[7] 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.

The European Union, similarly, has announced that it is "strongly supporting the transition to a low-carbon, more resource-efficient and sustainable economy" and says that "it has been at the forefront of efforts to build a financial system that

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sions 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.

[7] 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.

supports sustainable growth."[8] On March 21, 2019, the European Commission (EC) held its Second High Level Conference on Sustainable Finance, which focused on establishing frameworks to help finance sustainable growth, deploy private capital to sustainable investments, and create a global approach to sustainable finance.[9]

The EC formed a technical expert group (TEG) on sustainable finance to assist the EC in evaluating certain key issues around sustainable finance between July 2018 and the end of 2019. The TEG will make recommendations to the EC on (1) the development of an EU classification system, termed the EU taxonomy, to assess whether an economic activity is sustainable, (2) the development of a green bond standard, (3) methodologies for climate benchmarking, and (4) guidance on corporate disclosures of climate-related information.[10] The TEG published its report on climate-related disclosures in January 2019, and the EC published guidelines in June 2019 on corporate disclosure of climate-related information based on the TEG's work.[11] The guidelines provide guidance to the 6,000 EU-listed

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

[9] European Commission, "High-Level Conference: A Global Approach to Sustainable Finance" (Mar. 21, 2019), available at https://ec.europa.eu/info/events/finance-190321-sustainable-finance_en.

[10] European Commission, Financial Stability, Financial Services and Capital Markets Union "Technical Expert Group on Sustainable Finance (TEG)," https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en.

[11] European Commission press release, "Sustainable finance: Commission publishes guidelines to improve how firms report climate-related information and welcomes three new important reports on climate finance by leading experts" (June 18, 2019), available at http://europa.eu/rapid/press-release_IP-19-3034_en.htm?locale=en).

companies, insurance companies, and banks that are required to disclose non-financial information pursuant to the EU's Non-Financial Reporting Directive, which governs disclosures of non-financial information. The guidelines incorporate the recommendations of the TCFD (discussed below). Further, the EC announced its proposal to incorporate sustainability metrics in its own budgeting process: "To implement the Paris Agreement and the commitment to the United Nations Sustainable Development Goals, the Commission proposes to raise the level of ambition for climate mainstreaming across all EU programmes, with a target of at least 25% of EU expenditure contributing to climate objectives between 2017-2021."[12]

These examples in the EU and UK are not isolated. Indeed, regulators and markets around the world are focused on the impact of ESG factors on their growth and the strength of their capital markets.[13] Moreover, non-U.S. regulatory initiatives naturally can be expected to have a bearing on the regulatory approach taken in the United States and on multinational com-

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[12] European Commission press release, "Sustainable finance: Commission publishes guidelines to improve how firms report climate-related information and welcomes three new important reports on climate finance by leading experts" (June 18, 2019), available at http://europa.eu/rapid/press-release_IP-19-3034_en.htm?locale=en).

[13] See, for example, Jacqueline Poh and Mariko Ishikawa, "China Set to Lead ESG Disclosure to Lure Foreign Investments," Bloomberg (June 20, 2019), available at https://www.bloomberg.com/news/articles/2019-06-20/china-set-to-lead-esg-disclosures-to-lure-foreign-investments; Japan Exchange Group, "Publication of Japanese Translation of 'Model Guidance for Companies on Reporting on ESG Information'" (June 3, 2019), available at https://www.jpx.co.jp/english/corporate/news/news-releases/0060/20190603-01.html; Nathalie Borgeaud, "Article 173: Lessons Learned from 2018 Climate Risk Disclosures in France" (Apr. 30, 2019), available at http://427mt.com/2019/04/30/article-173-lessons-learned-from-2018-climate-risk-disclosures-in-france/.

panies that are faced with the challenge of meeting the expectations and standards of different regulatory systems.

§ 6:36 —Voluntary disclosure frameworks

Mandatory reporting regimes are emerging around the world, as discussed above. Against this backdrop, many "voluntary" disclosure frameworks have evolved in response to investors' desire for more ESG information. Some of the more prominent frameworks are outlined below.

§ 6:37 — —Global Reporting Initiative

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 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 also provides training, information, and support for issuers and other market participants and works to promote the broad implementation of the

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[1] See GRI website https://www.globalreporting.org/Information/about-gri/Pages/default.aspx.

[2] https://www.globalreporting.org/information/sustainability-reporting/Pages/gri-standards.aspx.

GRI Standards, which offer specific metrics and measurement criteria to guide reporting on a host of ESG factors.[3]

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[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 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.

§ 6:38 — —Task Force on Climate-Related Financial Disclosures

The Financial Stability Board (FSB) formed the Task Force on Climate-Related Financial Disclosures (TCFD) in order to develop a consistent framework for companies to voluntarily make climate-related financial disclosures for investors, lenders, and others.[1] The TCFD, as its name suggests, is focused specifically on climate-related disclosures, as compared with the GRI and SASB frameworks, which focus more broadly on ESG factors. The TCFD's framework is focused on 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

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[1] See https://www.fsb-tcfd.org/about/.

investors, lenders, and insurance underwriters in understanding 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 place emphasis on 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, the disclosures should describe the organization's governance with regard to climate-related risks and opportunities. Second, the disclosures should explain how climate-related risks and opportunities could impact the company's business, financial condition, and strategy. Third, the disclosures should explain how the organization identifies, assesses, and manages climate-

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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/wp-content/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf.

[3] TCFD: 2019 Status Report (June 2019), available at https://www.fsb-tcfd.org/publications/tcfd-2019-status-report/.

related risks, including through scenario analyses. Fourth, the disclosures 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 broadly fall 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 the 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.

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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/wp-content/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf, at 176.

§ 6:39 — —Sustainability Accounting Standards Board

The Sustainability Accounting Standards Board (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] Its approach

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[1] See https://www.sasb.org/.

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 sustainability 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 focus on the issues most salient to their businesses and cut through the noise and information overload 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 as to best practices for sustainability reporting.

§ 6:40 — —Climate Disclosure Standards Board

The Climate Disclosure Standards Board (CDSB) was founded in 2007 and comprises a consortium of NGOs and businesses that are focused on incorporating environmental effects in mainstream financial reporting. The CDSB focuses on driving decision-useful environmental information to market participants through mainstream reports.[1] While the SASB and the GRI focus on ESG factors broadly, the CDSB's focus is on the environmental impacts and the treatment of "natural capital" alongside financial capital. The CDSB explains that it is "committed to advancing and aligning the global mainstream corporate reporting model to equate natural capital with financial

[1] See https://www.cdsb.net/our-story.

capital."[2] 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."[3] 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.[4] 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 manner that makes the climate-related risks clear and understandable to investors.

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[2] See https://www.cdsb.net/our-story.

[3] See https://www.cdsb.net/our-story.

[4] 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.

§ 6:41 — —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 policy-makers.

[1] See https://www.cdp.net.

[2] See https://www.cdp.net.

§ 6:42 — —United Nations Sustainable Development Goals

In 2015, the United Nations' member nations unanimously adopted the 2030 Agenda for Sustainable Development. The 17 Sustainable Development Goals (SDGs)[1] and 169 specific tar-

[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 gets embedded within the 17 goals "are an urgent call for action

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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

Goal 17: Strengthen the means of implementation and revitalize the Global Partnership for Sustainable Development 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, and the goals flow down into states, cities, businesses, schools, and other organizations. As organizations map their activities to the UN Sustainable Development Goals, they are encouraged to identify the goals that are most relevant to their businesses and establish targets that are suitable for their own circumstances that will advance progress on the selected SDGs. Companies are not expected to map all 17 of the SDGs but rather identify which ones they can most directly impact. The SDGs are voluntary and leave companies with substantial freedom to define which goals they will disclose. The SDGs are significant because they provide a common framework within which companies, governments, and others can work toward solutions to the problems that the United Nations has identified as most critical for the future.

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[2] See https://sustainabledevelopment.un.org/?menu=1300.

§ 6:43 Integration of financial and non-financial information and the ongoing dialogue over where ESG disclosures should appear

Following is a discussion of "integrated reporting" including work in the ESG area by the International Integrated Reporting Council as well as an Integrated Reporting Working Group organized by the Conference Board. The discussion focuses on the integration of financial and non-financial information. Section 6:45 addresses the ongoing dialogue over where ESG disclosures should appear.

§ 6:44 —Integrated reporting

The International Integrated Reporting Council (IIRC) is a global coalition composed of investors, corporations, NGOs, regulators, accountants, and standards setters.[1] The IIRC'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" used by an organization 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

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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-FRAMEWORK-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-FRAMEWORK-2-1.pdf.

[3] 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-FRAMEWORK-2-1.pdf.

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 along with financial factors in financial reports rather than in separate reports.

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.[4] 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."[5] Investors increasingly take ESG factors into account 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. 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 with a collective $33 trillion in assets under management.

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[4] 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.

[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, at 3.

Eighty percent of the survey's respondents support integrated reporting.[6] 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.[7]

The Conference Board views integrated reporting as a mechanism by which 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."[8] The focus is not solely on a company's

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[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 25.

[7] 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.

[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 3.

reporting to 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."[9]

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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[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 3.

§ 6:45 —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, “At 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-esg-data/, 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-esg-data/, 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 contemplated by the SASB may go beyond that which 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://corpgov.law.harvard.edu/2019/06/05/sustainability-accounting-standards-and-sec-filings/.

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, they will harmonize the disclosure processes within the company to ensure consistency between the sustainability reports and financial reports. Further, good practice would have the sustainability reports subjected to similar oversight and rigor as that applied to financial disclosures. This should help ensure consistency in reporting, and lead to a deeper analysis and scrutiny within the companies of the ESG disclosures.

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[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.

§ 6:46 Reconciling the various 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 road map 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]

The WBCSD's ESG Disclosure Handbook provides further guidance for companies as they approach their ESG reporting processes.[3] The ESG Disclosure Handbook is designed to help companies navigate the disclosure process, giving consideration to 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

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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.

[3] See https://www.wbcsd.org/Programs/Redefining-Value/External-Disclosure/Purpose-driven-disclosure/Resources/ESG-Disclosure-Handbook.

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.[4]

The Corporate Reporting Dialogue also aims to rationalize the ESG reporting landscape.[5] Organized by the IIRC, the Corporate Reporting Dialogue's participants include the CDP, CDSB, GRI, International Organization for Standardization, SASB, International Financial Reporting Standards, and FASB. The Corporate Reporting Dialogue has made efforts to reconcile the different reporting regimes by providing comparisons and summaries of the principal reporting frameworks, including a "landscape map" that compares the member organizations' disclosure standards.[6] 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, which aims to map the key provisions of the CDP, CDSB, GRI, IIRC, SASB, and TCFD to find points of overlap that can be harmonized.[7] 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

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[4] Https://www.wbcsd.org/Programs/Redefining-Value/External-Disclosure/Purpose-driven-disclosure/Resources/ESG-Disclosure-Handbook.

[5] See https://corporatereportingdialogue.com/.

[6] See https://corporatereportingdialogue.com/landscape-map/.

[7] Https://corporatereportingdialogue.com/better-alignment-project/.

efforts to adopt the TCFD recommendations. The Corporate Reporting Dialogue announced a forthcoming publication in Q3 2019 to demonstrate the linkages of the TCFD recommendations with the CDP, CDSB, GRI, IIRC, and SASB standards.[8] Consistent with the objectives of the IIRC, the Better Alignment Project aims to facilitate integrated disclosure of financial and non-financial information.

The exchanges also recognize the need for ESG disclosure guidance to help companies navigate and reconcile the various ESG reporting standards. Half of the UN Sustainable Stock Exchanges have issued ESG reporting guidance.[9] In May 2019, Nasdaq issued its global ESG Reporting Guide.[10] The guide "will help companies understand the complex (and sometimes conflicting) world of ESG-related reporting. It provides a business-centric rationale for focusing on certain essential data points, integrating these data points into management operations, and potentially reporting them to the public."[11] Recognizing the dynamic landscape, Nasdaq acknowledged that its guide is "the beginning of a conversation rather than a final pronouncement."

In the spring of 2019, the SASB and the CDSB published a TCFD Implementation Guide designed to help companies apply the TCFD recommendations in harmony with the SASB and

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[8] *Id*. This website indicates that the report will be posted at https://corporatereportingdialogue.com/better-alignment-project/.

[9] ESG Reporting Guide: A Voluntary Support Program for Companies, available at https://business.nasdaq.com/esg-guide/.

[10] Nasdaq, "ESG Reporting Guide 2.0: A Support Resource for Companies" (May 2019), available at https://business.nasdaq.com/media/Nasdaq-ESG-Reporting-Guide-2019_tcm5044-70227.pdf.

[11] ESG Reporting Guide Questions and Answers, available at https://business.nasdaq.com/esg-guide/.

CDSB standards in order to improve companies' climate-related disclosures.[12] 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 road map to remedy this disclosure gap. It explains how the three frameworks complement each other. The TCFD principles provide thoughtful processes by which to craft decision-useful disclosures. The CDSB principles can "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. The SASB standards can 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 road map to ESG disclosures following the TCFD, CDSB, and SASB guidance. The steps outlined are to: (1) get executive and board-level support; (2) integrate climate change issues into key company governance with board-level oversight; (3) bring together key functions within the company — sustainability, governance, finance, and compliance; (4) evaluate the financial

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[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/. 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/.

impacts of climate risk; (5) apply scenario analyses to assess climate risks; (6) apply existing risk-management processes to climate risks; (7) get feedback from investors as to what information they find most important; (8) use existing tools to collect and report climate information, rather than reinvent the wheel; (9) use 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.[13]

The TCFD Implementation Guide provides some 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."[14] 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 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

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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 8-10.

[14] 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.

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."[15]

[15] 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.

§ 6:47 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 "rate the raters" survey of several thousand sustainability professionals by SustainAbility, the number of ESG ratings services has increased by more than 500 percent since 2010, with the number currently estimated at over 600.[2]

[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/rate-raters-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.

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 methodologies to derive their ratings, 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 providing a path to greater clarity and comparability, some have criticized the ratings as subjective.[3]

SustainAbility's 2019 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."[4] For their part, some companies expressed concern that the proliferation of ratings firms has accelerated the flow of information requests.[5] On the other hand, the survey found that close to two-thirds of the corporate respondents reported using ESG ratings to help them to inform their internal corporate decision-making: "In open-ended responses, sustainability experts most often mentioned using ratings for internal assessments and

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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-you-ask-1537199931.

[4] SustainAbility, "Rate the Raters 2019: Expert Views on ESG Ratings" (Feb. 2019), p.4, available at http://sustainability.com/our-work/reports/rate-raters-2019/.

[5] SustainAbility, "Rate the Raters 2018: Ratings Revisited" (Mar. 2018), available at http://sustainability.com/our-work/reports/rate-raters-2018-white-paper/.

strategy, to help inform what data to disclose, identify trends and support stakeholder engagement."[6]

Traditional credit rating agencies also are increasing their focus on ESG factors. The S&P Global Ratings announced the launch of its ESG Evaluation in April 2019[7] and published its first ESG Evaluation in June 2019.[8] It explains its rationale to help investors mange 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 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."[9]

In May 2019, Moody's Investors Service solicited feedback on a new carbon transition risk-assessment tool for rated com-

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[6] SustainAbility, "Rate the Raters 2019: Expert Views on ESG Ratings" (Feb. 2019), p.9, available at http://sustainability.com/our-work/reports/rate-raters-2019/.

[7] 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.

[8] "S&P Global Ratings Publishes Its First ESG Evaluation," MarketWatch (June 17, 2019), available at https://www.marketwatch.com/press-release/sp-global-ratings-publishes-its-first-esg-evaluation-2019-06-17.

[9] S&P Global, "ESG Evaluation: Sustainable Practices. Sustainable Returns," available at https://www.spglobal.com/en/capabilities/esg-evaluation.

panies.[10] 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.[11]

Fitch launched its ESG Relevance Scores in January 2019.[12] 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.[13] The

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[10] 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.

[11] 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.

[12] 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.

[13] 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.

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."[14]

PRI launched its ESG in Credit Risk and Ratings Initiative "to enhance the transparent and systematic integration of ESG factors in credit risk analysis."[15] 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 partic-

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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, quoting Andrew Steel, Fitch Ratings Global Head of Sustainable Finance.

[15] 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-credit-risk-and-ratings-part-1-the-state-of-play/78.article.

ipants."[16] Nonetheless, a recent 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."[17]

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[16] PRI, "Shifting Perceptions: ESG, Credit Risk and Ratings: Part 3 — From Disconnects to Action Areas" available at https://www.unpri.org/download?ac=5819.

[17] PRI, "Shifting Perceptions: ESG, Credit Risk and Ratings: Part 3 — From Disconnects to Action Areas" available at https://www.unpri.org/download?ac=5819.

§ 6:48 Some practical guidance

ESG reporting requirements and voluntary reporting regimes are propagating at a dizzying pace. The SEC appears to be patiently watching these developments. As William Hinman noted in his recent speech, "[t]he marketplace evolution of sustainability disclosures is ongoing."[1] The process 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, certain guidelines might be useful for companies to consider as they navigate their ESG disclosures.

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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).

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 the North Star in guiding 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 making their investment decisions 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 facilitate risk mitigation, contingency planning, leveraging new market opportunities, and ultimately more meaningful reporting on companies' ESG risks and opportunities.

Treat material ESG risks like financial information. In order to ensure information is accurate and presented in a manner that is complete and trustworthy, 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 the sustainability team within the company 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 the 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 the 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 Act 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 reports 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. It is safe to say that this landscape will continue to change over time.

§ 6:49 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 ESG disclosures by U.S. public companies have remained static. On the contrary, disclosures under the existing principles-based framework necessarily 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 too riddled with boilerplate. These concerns have led investor groups to call for more meaningful disclosure requirements to be issued from both 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 on the parts of both 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.