SEC & ESG: Climate Disclosures on the Horizon

By: Caitlin McCarthy Sarpal

I. Introduction

Climate change has the potential to cause enormous economic damage to this country; just one storm, Hurricane Sandy, inflicted nearly $30 billion in expenses on its own.[1] This issue is not lost on investors, who increasingly ask companies for information about climate-related risks.[2] Additionally, investors are asking the federal government to require companies to disclose this information.[3] Since the U.S. Securities and Exchange Commission's ("SEC") formation in 1934, one of its most vital tasks has been overseeing required disclosures of financially material information from companies.[4] As climate change continues to significantly impact companies and their operations, a strong need for mandatory climate disclosure rules has emerged.[5] This paper explores the SEC's pending proposed rule amendments on enhanced disclosures of companies' climate-related risks and opportunities with a focus on the historical and recent background that set the stage for potential climate risk disclosures and increased environmental, social, and governance ("ESG") considerations.

II. A Deregulatory Past and a Forward-Thinking Future

The SEC's mission is aimed at "protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation."[6] This mission is furthered by: (1) requiring companies

---

[1] Jim Coburn & Jackie Cook, COOL RESPONSE: THE SEC & CORPORATE CLIMATE CHANGE REPORTING 4 (Ceres 2014), https://www.ceres.org/sites/default/files/reports/2017-03/Ceres_SECguidance-append_020414_web.pdf.
[2] *See* Gary Gensler, Chairman, U.S. Sec. & Exch. Comm'n, Principles for Responsible Investment, Remarks at the Climate and Global Financial Markets Webinar (July 28, 2021), https://www.sec.gov/news/speech/gensler-pri-2021-07-28.
[3] *Id.*
[4] *Id.*
[5] *Id.*; Catherine M. Clarkin, et al., *The Rise of Standardized ESG Disclosure Frameworks in the United States*, HARV. L. SCH. F. CORP. GOVERNANCE (June 22, 2020), https://corpgov.law.harvard.edu/2020/06/22/the-rise-of-standardized-esg-disclosure-frameworks-in-the-united-states/#4.
[6] *What We Do*, U.S. SEC. & EXCH. COMM'N, https://www.sec.gov/about/what-we-do (last visited Jan. 4, 2022).

that sell securities to the public to remain honest regarding the risks associated with investing in those securities; and (2) ensuring fair treatment of investors by "brokers, dealers, and exchanges."[7] As the U.S. reckons with the current climate emergency,[8] federal agencies not traditionally thought of as being "environmentally-focused" are incorporating ESG factors into their core agency work.[9]

Following the publication of President Biden's Executive Order ("EO") 14030, Climate-Related Financial Risk, the current administration created a framework to prioritize "a whole-of-government effort" wherein all federal agencies are to incorporate climate resiliency into their work.[10] Publicly-traded securities play a fairly significant role in the specific goals of the EO, including the section outlining how SEC "staff [are] developing recommendations to the Commission for a mandatory disclosure rule for public issuers that is intended to bring greater clarity to investors about the material risks and opportunities that climate change poses to their investments."[11] The new rule is likely to be unveiled in 2022.

This EO and whole-of-government approach marks a stark charge from the deregulatory period under former President Trump for environmental governance.[12] Trump campaigned and led his presidency on a deregulatory agenda that saw the attempted and actual dismantling of key environmental regulations and initiatives, including for example, consequential changes to the foundational National Environmental Policy Act.[13]

---

[7] *Role of the SEC,* SEC, https://www.investor.gov/introduction-investing/investing-basics/role-sec (last visited Jan. 13, 2022).
[8] JOHN C. DERNBACH, LEGAL PATHWAYS TO DEEP DECARBONIZATION IN THE UNITED STATES 2 (Michael B. Gerrard & John C. Dernbach, eds., 2019).
[9] Exec. Order No. 14030, 86 Fed. Reg. 27,967 (May 20, 2021).
[10] WHITE HOUSE, A ROADMAP TO BUILD A CLIMATE-RESILIENT ECONOMY 21 (2021), https://www.whitehouse.gov/wp-content/uploads/2021/10/Climate-Finance-Report.pdf.
[11] *Id.* at 23.
[12] Nadja Popovich, et al., *The Trump Administration Rolled Back More Than 100 Environmental Rules. Here's the Full List*, N.Y. TIMES (Jan. 20, 2021), https://www.nytimes.com/interactive/2020/climate/trump-environment-rollbacks-list.html.
[13] Update to the Regulations Implementing the Procedural Provisions of the National Environmental Policy Act, 85 Fed. Reg. 43,304 (July 16, 2020); s*ee also* Robert L. Glicksman & Alejandro E. Camacho, *The Trump Card: Tarnishing Planning, Democracy, and the Environment*, 50 ELR 10281 (2020).

It came as no surprise, then, when Trump withdrew the U.S. from the Paris Agreement, stifling vital U.S. climate action.[14] Yet many American companies did not celebrate this action, instead reacting with dismay.[15] In this climate action void, hundreds of Fortune 500 and smaller corporations stepped up their private environmental governance efforts, pursuing their own emissions reduction targets in accordance with the Paris Agreement.[16] Ultimately, Trump's deregulatory agenda had the opposite effect as intended: it set the stage for a new era of environmental, social, and governance focus, including today's pending climate disclosure rule for publicly-traded companies.

III. Potential ESG Frameworks

While the SEC's proposed rule amendments are a landmark for U.S. ESG developments, they are not unprecedented on a global scale, and thus SEC staff can—in addition to their own research, the responses from the public comment periods, common industry practices, government directives, task force findings, and more—look to the international community for best practices in the development and implementation of the rule amendments. The European Union has long implemented stringent rules regarding climate disclosures and, in April 2020, these rules were strengthened to be in accord with the Paris Agreement.[17] Relatedly, every United Nations Climate Change Conference has included emission reductions and transparency as key goals. At the recent 26th session of the Conference of the Parties to the United Nations Climate Change Conference (COP26), the International Financial Reporting Standards Foundation announced the creation of

---

[14] Popovich et al., *supra* note 12.

[15] Courtney Lindwall, *Corporate Leaders to Trump: Withdrawing From the Paris Agreement Makes Bad Business Sense*, NRDC (Nov. 26, 2019), https://www.nrdc.org/onearth/corporate-leaders-trump-withdrawing-paris-agreement-makes-bad-business-sense.

[16] *See* CDP, *Business and the Paris Agreement*, 1, https://cdn.cdp.net/cdp-production/cms/reports/documents/000/000/826/original/corporate-support-global-agreement-on-climate-change.pdf?1471969971.

[17] Parliament and Council Regulation 2019/2089, 2019 O.J. (L. 317) 17.

the International Sustainability Standards Board, with the goal to "develop—in the public interest—a comprehensive global baseline of high-quality sustainability disclosure standards to meet investors' information needs . . . ."[18] Many of the publicly-traded companies who would need to adhere to the SEC's new rule amendments are multinational corporations who already comply with similar disclosure schemes around the world.

IV. Companies, Investors, SEC, & the General Public

Many companies appear willing to embrace the SEC's rule amendments, or at least will appreciate clarity around climate-disclosures, an area of increasing pressure from investors and the public that currently lacks a clear set of requirements or reporting rules.[19] Presently, the Value Reporting Foundation ("VRF") (formerly the Sustainability Accounting Standards Board and the International Integrated Reporting Council, which merged together in June 2021),[20] the Task Force on Climate-Related Financial Disclosures ("TCFD"),[21] and the Global Reporting Initiative ("GRI") provide the most widely accepted frameworks for voluntarily ESG disclosure standards, but these frameworks are not federally-mandated.[22]

Since its formation following the Great Depression, one of the most vital tasks of the SEC has been overseeing required disclosures of financially material information from companies.[23] As investors increasingly ask for information about climate-related risks and as climate change continues to significantly impact companies, there is a strong need for mandatory climate

---

[18] Press Release, Int'l Fin. Rep. Standards Found., IFRS Found. Announces Int'l Sustainability Standards Board, Consol. with CDSB and VRF, and Publ'n of Prototype Disclosure Requirements (Nov. 3, 2021), https://www.ifrs.org/news-and-events/news/2021/11/ifrs-foundation-announces-issb-consolidation-with-cdsb-vrf-publication-of-prototypes/.
[19] Clarkin, *supra* note 5.
[20] Sehrish Siddiqui, *ESG Organizations: The Journey Toward Consolidation and Collaboration Continues*, JD SUPRA (June 25, 2021), https://www.jdsupra.com/legalnews/esg-organizations-the-journey-toward-1711055/.
[21] Clarkin et al., *supra* note 5.
[22] GRI, *Setting the Agenda for the Future,* GRI, https://www.globalreporting.org/ (last visited Jan. 4, 2022).
[23] Gensler, *supra* note 2.

disclosure rules.[24] The development of these rule amendments is widely accepted by companies themselves, investors, and other stakeholders.[25]

While President Biden's whole-government approach has likely accelerated the development of the rule amendments from the federal government, the SEC has been increasingly prioritizing climate disclosures over the last several years. Notably, in 2010, the SEC issued "interpretive guidance on disclosure requirements as they apply to business or legal developments relating to the issue of climate change."[26] While not binding, the 2010 guidance was published with the aim of outlining how the SEC's existing disclosure requirements apply to climate change matters arising for companies.[27] The SEC noted that the guidance "[was] intended to assist companies in satisfying their disclosure obligations under the federal securities laws and regulations."[28] However at that point (and still today), there were no direct climate disclosure requirements.

Rather, this guidance clarified how companies could include indirect or related climate information in their reports. Examples of climate impacts covered by the 2010 guidance included: (1) capital expenditures to reduce emissions; (2) expenses related to purchasing allowances where companies under a potential cap and trade program did not meet their reduction targets; (3) climate impacts on companies' changing costs and/or prices for goods or services; and (4) significant physical effects of climate change on companies—for example, effects on the "personnel, physical assets, supply chain[s] and distribution chain[s]."[29] Further laying the groundwork for the

---

[24] *Id.*; Clarkin et al., *supra* note 5.
[25] Gensler, *supra* note 2.
[26] Press Release, U.S. Sec. & Exch. Comm'n, SEC Issues Interpretive Guidance on Disclosure Related to Bus. or Legal Dev.'s Regarding Climate Change (Jan. 27, 2010), https://www.sec.gov/news/press/2010/2010-15.htm.
[27] U.S. SEC. & EXCH. COMM'N, COMMISSION GUIDANCE REGARDING DISCLOSURE RELATED TO CLIMATE CHANGE, 1, 3 (2010), https://www.sec.gov/rules/interp/2010/33-9106.pdf.
[28] *Id.* at 3.
[29] *Id.* at 5–7.

upcoming rule amendments, the 2010 guidance notes that "some information relating to greenhouse gas emissions and climate change is [required to be] disclosed in SEC filings, [and] much more information is publicly available outside of public company disclosure documents filed with the SEC as a result of voluntary disclosure initiatives or other regulatory requirements."[30]

In 2016, the SEC sought public comments for a concept release about potentially modernizing the disclosure requirements in Regulation S-K, specifically to ensure that the disclosure requirements were useful for investors and registrants.[31] Of the comments received regarding disclosure effectiveness, a substantial number of them focused on climate change, corporate social responsibility ("CSR"), ESG, and related topics, with calls for the SEC to require sustainability disclosures.[32] There was concern outlined in the public comments that the current practice of voluntary corporate sustainability reporting, which lacked a uniform or mandated system, was ineffective, inconsistent, and incomplete, and thus not serving the needs of investors.[33] This issue has only grown over the years with increasing awareness and concern over "greenwashing" and a lack of transparency surrounding corporate actions or inactions related to climate change.[34] Later proposed rulemaking on modernizing the S-K regulations continued this call for sustainability or ESG disclosures, but nothing concrete was enacted in this regard.[35]

In May 2020, the SEC Investor Advisory Committee noted that they had, for nearly five decades, "periodically contemplated whether ESG disclosures are material and should be incorporated into its integrated disclosure regime for SEC registered Issuers."[36] In the same report,

[30] *Id.* at 8.
[31] Business and Financial Disclosure Required by Regulation S-K, 81 Fed. Reg. 23,915 (July 21, 2016).
[32] *Id.* at 23,970.
[33] *Id.* at 23,971.
[34] Magali A. Delmas & Vanessa Cuerel Burbano, *The Drivers of Greenwashing*, 54 CAL. MGMT. REV. 64 (2011).
[35] U.S. SEC. & EXCH. COMM'N, MODERNIZATION OF REGULATION S-K ITEMS 101, 103, AND 105, at 1 (2010), https://www.sec.gov/rules/proposed/2019/33-10668.pdf.
[36] INV.-AS-OWNER SUBCOMM. OF THE SEC INV. ADVISORY COMM., *Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure*, 1 (2020),

they concluded by providing their recommendation that the SEC update reporting requirements to include ESG considerations:

> We recognize that any new reporting regime is difficult and comes with related litigation risk. But well-constructed, principles-based reporting that enables each Issuer, regardless of industry or business line, to set out its risks, strategies and opportunities in relation to material ESG factors should be no different than current disclosure of business risk, strategy and opportunity. ESG matters are part and parcel of the business of every Issuer and are unique to every Issuer.[37]

The SEC continued to explore these public comments and recommendations, and in February 2021, then-Acting Chair Allison Herren Lee issued a "Statement on the Review of Climate-Related Disclosure" in which she directed the Division of Corporation Finance to more staunchly focus on potential climate disclosure requirements.[38] Quickly following this statement was the founding of a new task force in this area the Climate and ESG Task Force in the Division of Enforcement.[39] Shortly thereafter, another public comment period opened up on this topic, perhaps the most robust to date, with the goal of providing information to the SEC that could guide their evaluation of potential climate disclosure rules.[40]

---

https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[37] *Id.* at 9–10.

[38] Public Statement from Acting Chair Allison Herren Lee, Statement on the Review of Climate-Related Disclosure U.S. Sec. & Exch. Comm'n, (Feb. 24, 2021), https://www.sec.gov/news/public-statement/lee-statement-review-climate-related-disclosure.

[39] Press Release, U.S. Sec. & Exch. Comm'n, SEC Announces Enforcement Task Force Focused on Climate and ESG Issues (March 4, 2021), https://www.sec.gov/news/press-release/2021-42.

[40] Public Statement from Acting Chair Allison Herren Lee, , Public Input Welcomed on Climate Change Disclosures, U.S. Sec. & Exch. Comm'n (March 15, 2021), https://www.sec.gov/news/public-statement/lee-climate-change-disclosures.

V. On the ESG Horizon: Timeline and Potential Components of the Climate Disclosures

In May 2021, President Biden issued EO 14030 with the primary goal of "advanc[ing] consistent, clear, intelligible, comparable, and accurate disclosure of climate-related financial risk."[41] In July, SEC Chairman Gary Gensler reiterated his interest in bringing a climate disclosure rule to fruition and noted that he had tasked SEC employees with "develop[ing] a mandatory climate risk disclosure rule proposal for the Commission's consideration by the end of the year."[42]

While 2021 has concluded without publication of the proposed rule amendments, the historical background and more recent activity in this area indicates they are likely on the horizon. The rule amendments have the opportunity to usher in a new era of ESG through the SEC, but this is dependent on a fairly far-reaching outcome of the pending rule amendments. A mandatory climate risk disclosure rule could meet President Biden's goals, the needs of investors, and benefit the public at large. Presently, it is unknown what exactly could be in the rule amendments, but it is likely to be more robust than the 2010 guidance and hopefully include mandatory, instead of merely suggested, requirements. The disclosures could be modeled after international standards or the widely accepted VRF, TCFD, or GRI frameworks.

Chairman Gensler has noted that the new disclosures will promote consistency and comparability, which would further understanding among both investors and the general public as to companies' climate risks and actions.[43] Additionally, he has indicated that the disclosures are likely to be mandatory, a structure that would prove most useful and constitute a marked difference from the voluntary nature of disclosures and guidance to date.[44] The disclosures are also likely to

---

41 Exec. Order No. 14030, 86 Fed. Reg. 27967 (May 20, 2021).
42 Gensler, *supra* note 2.
43 *Id.*
44 Gensler, *supra* note 2.

be integrated into Form 10-K, amongst "other information that investors use to make their investment decisions."[45] For instance, the SEC employees focused on developing the climate disclosure rule amendments are considering a variety of qualitative measurements and criteria—including "how the company's leadership manages climate-related risks and opportunities and how these factors feed into the company's strategy"—as well as quantitative measurements and criteria, which "could include metrics related to greenhouse gas emissions, financial impacts of climate change, and progress towards climate-related goals."[46] Although, there may be issues of greenwashing and the challenges of assessing sustainability claims, especially as incorporated into climate disclosure reporting, Chairman Gensler's "decision-useful" approach to the disclosures, that requires a baseline level of substantial detail, may mitigate these concerns by providing investors with tangible and useful information from the reports.[47]

Without knowing precisely what the rule amendments will entail, it is challenging to postulate on their potential effects, but it is clear that fulfilling Chairman Gensler's proposed aims and increased transparency of corporations' climate risks can positively serve the needs of investors and the general public. With a significant lead time, companies can foresee changes to their reporting and begin a more proactive approach in assessing their own climate risk, and potentially also assess their opportunities for reducing such risk, promoting sustainability, reducing or eliminating greenwashing, and going beyond basic compliance.

---

[45] *Id.*
[46] *Id.*
[47] *Id.*

VI. Conclusion

With a pressing climate emergency, there has never been a more apt time for a whole-government approach to climate resiliency, and this extends to capital markets and American companies. Having the SEC, a vital federal government agency, require climate disclosures would further propel ESG into mainstream operations for companies and center ESG on the national stage. This could lead to a considerable decrease in greenwashing and further transparency for investors and the general public, which in turn can lead to increased accountability for companies on their climate actions. As climate change worsens conditions across the globe, it is time to see climate disclosures as a vital and mandatory component of financial disclosures for public companies, instead of an after-thought or voluntary disclosure. With a federally-created framework, such disclosures can be useful across industries for investors and the public and further environmental governance. After approximately fifty years of exploring ESG, the pending publication of the proposed rule amendments indicates a new chapter of environmental governance. With specific reporting standards and increased transparency, the disclosure of companies' climate-related risks can lead to increased sustainability and environmental action during a pressing time of the climate crisis.[48]

---

[48] DERNBACH, supra note 8.