By Electronic Mail

The Honorable Gary Gensler
Chair, U.S. Securities and Exchange Commission
100 F St., NE
Washington, D.C. 20549-0609

Re: Public Input on Climate Change Disclosures

Dear Chair Gensler:

I appreciate the opportunity to submit the attached Article, Making Sustainability Disclosure Sustainable, 107 Georgetown L.J. 923 (2019) in response to the March 15, 2021, request for public comments on whether the current disclosure rules and regulations of the U.S. Securities and Exchange Commission (the “Commission”) appropriately address climate change.

The Article makes the case for Commission-mandated sustainability disclosure and offers a modest proposal for incorporating such disclosure into an issuer’s securities filings. The Article seeks to provide a mechanism for moving forward on integrating sustainability disclosure with financial reporting, a first step that could be taken without the need to resolve complex issues regarding the optimal scope of sustainability disclosure. The passage of time since the publication of the Article has, in my view, strengthened the case that sustainability disclosure is relevant to investing and voting decisions by an increasing percentage of investors.

The Article highlights the advantages of mandatory disclosure over the existing voluntary disclosure regime. As the Article argues, mandatory disclosure will increase the reliability and comparability of disclosures. Regulation will also serve a role in managing investor expectations and relieving issuers of the burden of responding to a multiplicity of disclosure requests by shareholders, third-party standard setters and stakeholder groups.

The Article also stresses the importance of both issuer and board accountability for sustainability disclosures. Because of the compliance issues associated with securities filings, the Commission’s disclosure regime serves an information-forcing role, increasing both the level of information that management provides to the board in connection with required disclosures and the board’s attention to
those issues. As issuers face growing operational challenges, regulatory attention and even liability in connection with their actions on climate and other ESG matters, the board’s ongoing engagement in evaluating the impact of these challenges on the issuer’s business plan and determining the extent to which that plan requires modification is critical.

Finally, as the Article explains, disclosure is only effective with accountability. Mandated disclosure will have the important effect of subjecting sustainability disclosures to the Commission’s oversight and enforcement. Although false statements and greenwashing in voluntary sustainability reports can potentially subject issuers to private antifraud litigation—as well they should, given their potential impact on the market—the inclusion of such disclosures in securities filings will clarify that liability exposure. Moreover, the prospect that a Commission mandate would subject issuers to extensive litigation for their ESG disclosures is unlikely. As the Article observes, only investors have the power to bring antifraud litigation, and investors would have to establish both loss causation and damages, making the prospect of private litigation unlikely except in the most extreme cases. The Commission could further reduce the scope of litigation through the adoption of a safe harbor akin to the safe harbor for forward-looking statements.

I welcome the opportunity to discuss these comments with the Commission or the Commission’s Staff. Thank you for your consideration.

Respectfully,

Jill E. Fisch

cc: Hon. Hester Peirce, Commissioner, U.S. Securities and Exchange Commission
Hon. Elad Roisman, Commissioner, U.S. Securities and Exchange Commission
Hon. Allison Lee, Commissioner, U.S. Securities and Exchange Commission
Hon. Caroline Crenshaw, Commissioner, U.S. Securities and Exchange Commission

1 The certification requirements adopted pursuant to the Sarbanes-Oxley Act serve a similar information-forcing function. See, e.g., 17 C.F.R. §§ 240.13a-14, 240.15d-14 (implementing certification requirement for annual and quarterly reports).
2 15 U.S.C. § 78u-5, 15 U.S.C. § 77z-2 (adopting safe harbors from private litigation for forward-looking statements that are not knowingly false and are accompanied by meaningful cautionary statements).
Sustainability is receiving increasing attention from issuers, investors, and regulators. The desire to understand issuer sustainability practices and their relationship to economic performance has resulted in a proliferation of sustainability disclosure regimes and standards. The range of approaches to disclosure, however, limits the comparability and reliability of the information disclosed. The Securities and Exchange Commission (SEC)’s longstanding policy that sustainability is not properly part of financial disclosure has contributed to the current regime. Although the SEC has solicited comment on whether to reverse this policy and require expanded sustainability disclosures in issuers’ periodic financial reporting, and investors have communicated broad-based support for such expanded disclosures, the SEC to date still has not required general sustainability disclosure.

This Article argues that claims about the relationship between issuer sustainability practices and risk management, business plans, and economic vulnerability warrant incorporating sustainability information into SEC-mandated financial reporting. Perhaps even more important, in light of the growing pressure for issuers to adopt sustainable business practices and the responsiveness of many issuers to this pressure, is the need for issuers, investors, and regulators to obtain the information necessary to evaluate claims about the economic impact of sustainability initiatives.

Drawing upon the existing narrative disclosure frameworks in SEC-mandated reporting requirements, this Article offers an innovative proposal for sustainability disclosure—a sustainability discussion and analysis, or “SD&A,” section of the annual report. This Article identifies the critical components necessary to make mandated sustainability disclosure both practical and cost-effective and offers a workable first step for integrating sustainability disclosure into issuer financial reporting.
INTRODUCTION

In January 2018, Larry Fink, CEO of BlackRock, made headlines when he called upon corporations to pay greater attention to sustainability and societal impact in his annual letter to CEOs. As Fink explained, “[A] company’s ability to manage environmental, social, and governance matters demonstrates the leadership and good governance that is so essential to sustainable growth, which is

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why we are increasingly integrating these issues into our investment process.”  

Fink’s letter was a high-profile example of a leading institutional investor expressing concern about corporate sustainability, but it was not an isolated occurrence. Investor focus on sustainability is accelerating. Even Martin Lipton has acknowledged that “sustainability has become a major, mainstream governance topic.” The debate over sustainability is leading investors, executives, and directors to rethink how corporations engage in long-term value creation.

The extent to which corporations should incorporate sustainability objectives into their operational decisionmaking is highly contested, as is the relationship between societal impact and economic value. Indeed, the Department of Labor subsequently issued new guidelines for retirement plans cautioning that “[f]iduciaries must not too readily treat ESG factors as economically relevant to the particular investment choices at issue when making a decision.” At the same time, however, issuers are modifying their operations in response both to investor demands and to the claim that sustainable business practices lead to improved economic performance. Being able to assess an issuer’s sustainability related activities are material to the financial success of a company over time.”

6. See UNRUH ET AL., supra note 4, at 7 (reporting survey results indicating that “more than 80% of investor respondents indicate that good sustainability performance increases a company’s potential for long term value creation”).
7. See, e.g., Robert G. Eccles, Ioannis Ioannou & George Serafeim, The Impact of Corporate Sustainability on Organizational Processes and Performance, 60 MGMT. SCI. 2835, 2836 (2014) (describing study finding that companies which voluntarily adopted sustainability policies by 1993 outperformed their counterparts over the long term).
9. See, e.g., KPMG, ESG, STRATEGY, AND THE LONG VIEW: A FRAMEWORK FOR BOARD OVERSIGHT 7 (2017), https://assets.kpmg.com/content/dam/kpmg/lu/pdf/2017/esgstrategyframeworkforboardoversight.pdf (“Some of the largest U.S. corporations are publicly emphasizing the strategic importance of ESG to their businesses . . . .”); The UN Global Compact Accenture Strategy CEO Study,
practices is critical to evaluating the effect of sustainability practices on economic value. For investors and capital markets to consider the societal impact of a firm’s operations—and to determine the consequences of that impact—they must have access to adequate sustainability disclosure.

Therein lies the problem. Although the focus on increasing sustainability disclosure is accelerating both in the United States and globally, investors continue to report dissatisfaction with existing disclosures. Recognizing this dissatisfaction, the SEC has raised the question of whether it should require increased sustainability disclosure as part of its “Disclosure Effectiveness Initiative.” The SEC received thousands of responses urging it to do so. Investors continue to request the SEC to “initiate rulemaking to develop mandatory rules for public companies to disclose high-quality, comparable, decision-useful environmental, social, and governance information.”

One reason for concern with current disclosure practices is that most existing sustainability reporting is voluntary, which means that individual issuers choose

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which information to disclose. The resulting lack of standardization means that issuer disclosures vary substantially, which impedes comparability.\textsuperscript{15} A second concern is that sustainability reporting is typically characterized as “non-financial” reporting\textsuperscript{16} and is distinct in location, format, and rigor from other investor-oriented information. Finally, sustainability reporting varies widely in quality, and its accuracy is rarely audited or monitored, reducing its effectiveness as a tool for improving accountability.\textsuperscript{17}

These limitations impede the ability of investors and researchers to evaluate the sustainability practices of issuers and to analyze the relationship between sustainable practices and economic performance. Investors are demanding greater sustainability, and issuers are responding to these demands, without reliable evidence of sustainability’s economic impact. One possible solution is to continue the reliance on private ordering but seek common standards to facilitate comparability.\textsuperscript{18} A variety of standard setters are assisting in the process by developing and publishing sustainability metrics, ratings, and guidelines.\textsuperscript{19} This variety is itself a problem, in that it increases search costs for investors and makes it challenging to compare information from different providers.\textsuperscript{20} The quality of third-party information is diminished because most standard setters rely on information voluntarily supplied by issuers, either directly to the standard setter or through

\begin{itemize}


\item\textsuperscript{17} See Patrick Odier, \textit{Why Lack of Data is the Biggest Hazard in ‘Green Investing,’} FIN. TIMES (Mar. 6, 2017), https://www.ft.com/content/be8e5db2 0249 11e7 aa5b 6bbf07f5c8e12 [https://perma.cc/5NB5 U55D] (“[D]ata on the real world impact that companies exert is poor, incomplete, non-standardised, or inaccessible.”).

\item\textsuperscript{18} For example, the Sustainability Accounting Standards Board (SASB) has been engaged in a multi year project, in conjunction with issuers and investors, to develop common standards for disclosure of material sustainability information. See \textit{generally Standards Overview}, SASB, https://www.sasb.org/standards overview/ [https://perma.cc/BEP2 E5R7] (last visited Feb. 13, 2019) (describing the development of the SASB’s sustainability standards).


\item\textsuperscript{20} See, e.g., Charles E. Merrill, \textit{The SEC Revisits Sustainability: Will Sustainability Reporting Become Mandatory for Publicly Traded U.S. Corporations?}, LEXOLOGY (Oct. 7, 2016), https://www.lexology.com/library/detail.aspx?g=8148a821 b3d0 4e23 b7de 55b06f9ed7da [https://perma.cc/UZA4 YFRU] (“[T]he current patchwork of ESG reporting methods does not make such information readily accessible.”).\end{itemize}
public disclosures. In addition, to the extent that standard setters use proprietary methodologies or information that is not publicly available, the significance of their ratings is not transparent and is difficult to evaluate.

Another option is mandatory sustainability disclosure. Several jurisdictions have imposed or are considering imposing mandatory disclosure requirements related to specific sustainability issues. One example of the move toward mandatory sustainability disclosure is the 2014 European Union (EU) Directive on the Disclosure of Non-Financial and Diversity Information, which required certain issuers to begin providing specific sustainability disclosures in 2018.

Commentators in the United States have repeatedly called upon the SEC to do more to formalize sustainability disclosure. The incorporation of sustainability reporting into the disclosure requirements of the federal securities laws faces obvious political obstacles, particularly under a presidential administration that publicly embraces a deregulatory approach. Apart from the political obstacles, however, there are concerns about the practicability of developing a workable structure for mandatory disclosure. Sustainability disclosures must be specific enough to provide investors and capital markets with meaningful and readily

21. See infra notes 114-17 and accompanying text.


Because the Directive is implemented at the country level, different countries have adopted varying criteria with respect to its application. For example, the Danish regulation redefines “large company” to include, inter alia, companies with an average of 250 employees. Innovative Implementation of EU Directive on Non Financial Reporting, GRI (Feb. 7, 2018), https://www.globalreporting.org/information/news and press center/Pages/EU Directive on Non Financial Reporting.aspx [https://perma.cc/QQ72 U539]. In contrast, the Greek legislation imposes a duty to report on companies of all sizes. Id.

23. See, e.g., Heather Slavkin Corzo, Dir., Office of Inv., AFL CIO, Comment Letter on Concept Release Regarding Business and Financial Disclosure Required by Regulation S K (July 21, 2016), https://www.sec.gov/comments/s7 06 16/s70616 305.pdf (“[G]iven the clear and growing demand from investors for environmental, social and governance (‘ESG’) information, the Commission must begin requiring ESG related line item disclosures as well as a process to incorporate emerging ESG metrics into disclosure in the future.”); Che Odom, Investors Want Sustainability Disclosures in SEC Overhaul, BLOOMBERG (July 21, 2016), https://www.bna.com/investors sustainability disclosures n73014445099/ [https://perma.cc/RAB2 LTH7] (“Investor advocates are making a strong push for the SEC to require annual, uniform sustainability reporting from public companies as part of the overhaul of the agency’s disclosure regime.”).

comparable information. At the same time, relevant sustainability issues vary substantially by issuer and industry, making a detailed line-item approach less feasible.\textsuperscript{25} The alternative, a principles-based approach, complicates policing the accuracy of issuer disclosures and risks producing low-quality or boilerplate disclosures.\textsuperscript{26}

This Article proposes a solution—mandating a “Sustainability Discussion and Analysis” (SD&A) as part of an issuer’s annual report to shareholders.\textsuperscript{27} The SD&A would be modeled after existing Management Discussion and Analysis (MD&A) and Compensation Discussion and Analysis (CD&A) and would reflect a similar principles-based approach to those provisions, requiring issuers to address those sustainability issues most important to their operations.\textsuperscript{28}

This Article proposes that the SD&A require an issuer to disclose, at a minimum, the three sustainability issues that are most significant for the firm’s operations, to explain the basis for that selection, and to explain the impact of those issues on firm performance. The SD&A would centralize sustainability disclosures within an issuer’s securities filings. As with the MD&A and CD&A requirements, implementing the SD&A would require that the SEC issue guidance by identifying sustainability issues that are likely to be material to investors and articulating the principles that issuers should apply in preparing their SD&As.\textsuperscript{29}

\textsuperscript{25} This problem is not insurmountable. Some sustainability issues are arguably common to all firms. See Douglas Hoffner, Interim Chief Exec. Officer, Cal. Pub. Emps.’ Ret. Sys., Comment Letter on Concept Release on Business and Financial Disclosure Required by Regulation S K (July 21, 2016), https://www.sec.gov/comments/s7 06 16/s70616 267.pdf (citing gender diversity and the impact of climate change as examples). The SASB has responded to this variation by developing seventy nine industry specific standards. See Standards Overview, supra note 18.

\textsuperscript{26} See generally Cristie L. Ford, New Governance, Compliance, and Principles Based Securities Regulation, 45 A M. B US. L.J. 1, 67 (2008) (explaining the difference between a principles based approach and a rules based approach and observing that a principles based approach entails greater flexibility but at the cost of increased uncertainty).

\textsuperscript{27} The formal requirement would be reflected by including the SD&A as part of Regulation S K. The SEC adopted the regulation in 1980 to centralize the disclosure requirements of the Securities Act of 1933 (which apply to public offerings) and the Securities Exchange Act of 1934 (which impose periodic reporting requirements on public companies). See John C. Coffee, Jr., Re Engineering Corporate Disclosure: The Coming Debate Over Company Registration, 52 W ASH. & L EE L. R EV. 1143, 1145 (1995) (describing the widespread criticism of the “pointless duplication” in disclosure rules prior to Regulation S K). The disclosures required by Regulation S K apply to various securities filings, including registration statements and annual reports, See 1 Cristopher Greer et al., FEDERAL SECURITIES ACT OF 1933 § 7.03, LEXIS (database updated 2018) (“The nonfinancial substantive disclosure provisions of Form S 1 rely entirely on the provisions of Regulation S K and include essentially the same information about the registrant as that required to be reported in an annual report to the Commission filed on Exchange Act Form 10 K.” (footnote omitted)).

\textsuperscript{28} See, e.g., Business and Financial Disclosure Required by Regulation S K, Securities Act Release No. 10,064, Exchange Act Release No. 77,599, 81 Fed. Reg. 23,916, 23,925 (proposed Apr. 22, 2016) (“Many of our rules require disclosure when information is material to investors. These rules rely on a registrant’s management to evaluate the significance of information in the context of the registrant’s overall business and financial circumstances and determine whether disclosure is necessary. The requirements are often referred to as ‘principles based’ because they articulate a disclosure objective and look to management to exercise judgment in satisfying that objective.” (footnotes omitted)).

\textsuperscript{29} See generally id. at 23,924 26 (summarizing the rules’ disclosure requirements regarding material information).
The SD&A would place responsibility for drafting such disclosures on the personnel who prepare the issuer’s financial reporting. It would subject sustainability disclosure to the same regulatory framework that applies to other securities disclosures, including SEC oversight through its review of issuer securities filings and, when applicable, liability exposure for fraudulent misrepresentations.

To ensure the board’s involvement in overseeing both the development of issuers’ sustainability practices and the disclosure of those practices, this proposal would require directors to certify the accuracy of the disclosures contained in the SD&A. This would establish a framework for effective director oversight and bring accountability to the disclosure regime. The SD&A would thereby address the key investor concern that boards consider sustainability practices with a material impact on, or posing material risks to, the firm’s operations and incorporate those considerations into their strategic planning.30

Incorporating sustainability disclosure into annual financial reporting would reflect the increasing economic importance of sustainability considerations and the growing concern they pose for investors and capital markets. It would be an important first step toward improving the uniformity, reliability, and comparability of sustainability disclosure and would provide important data to allow the capital markets to evaluate the impact of sustainable business practices.

This Article proceeds as follows. Part I sets the groundwork by describing existing sustainability disclosure practices. Part II identifies the limitations of existing practices and advocates for integrating mandatory sustainability disclosure into financial reporting. Part III proposes a new approach to sustainability disclosure: the SD&A. Part IV identifies advantages and potential limitations of the proposal.

I. BACKGROUND AND EXISTING SUSTAINABILITY DISCLOSURE PRACTICES

This Part provides a brief background of corporate sustainability disclosure. It begins with an overview of the scope and rationale for sustainability disclosure. It then outlines the history of the SEC’s regulation of sustainability disclosure as well as sources of mandatory sustainability reporting requirements beyond the federal securities laws. Finally, it identifies existing approaches to voluntary disclosure and the institutional players that contribute to the voluntary regime.

A. THE CONCEPT OF SUSTAINABILITY DISCLOSURE

Currently, there is no consensus on a precise definition of “sustainability.” Use of the term is often traced to a 1987 United Nations (UN) report defining sustainability as “[actions that] . . . meet the needs and aspirations of the present without

30. See, e.g., Dan Konigsburg et al., Why Sustainability Is a Board Level Risk, WALL ST. J. (July 6, 2018, 12:01 AM), https://deloitte.wsj.com/cfo/2018/07/06/why sustainability is a board level risk/ [https://perma.cc/8ZCM DSKD] (explaining how sustainability disclosure provides investors with insight as to how the issuer is incorporating sustainability its risk policies and strategy).
compromising the ability to meet those of the future."31 The UN formalized the principles in this report in its UN Global Compact, the “most prominent . . . [o]f the hundreds of international institutional and policy initiatives around corporate social and environmental responsibility and sustainability.”32 The idea behind corporate sustainability is decisionmaking that incorporates social, political, and ethical concerns in addition to traditional financial performance.33 As J. Robert Brown explained in his comment letter to the SEC: “Sustainability involves matters that can impact the long-term success of the company and the economy.”34 Martin Lipton notes that sustainability “encompasses a wide range of issues, such as climate change and other environmental risks, systemic financial stability, labor standards, and consumer and product safety.”35 Experts also use a variety of terms to describe corporate sustainability and sustainability reporting. Among these are “CSR” (Corporate Social Responsibility),36 “ESG” (Environmental, Social, and Governance),37 “triple bottom line,”38 and “societal impact.”39 Some
also describe sustainability disclosure as “non-financial” reporting.40

Demand for corporate sustainability disclosure has traditionally come from special-interest investors, such as religious organizations and ethical investment funds, and non-investor special interests.41 More recently, however, interest in sustainability disclosure has spread to mainstream investors. Goldman Sachs, describing this trend as the “ESG Revolution,” compiled data showing a rise in the ESG focus of traditional investor-directed communications, such as “earnings transcripts, social media and asset manager initiatives.”42 Support for ESG disclosure has extended to a growing percentage of the investor community.43 For example, at the 2017 annual meeting, Exxon shareholders voted on a shareholder proposal requesting the company to report “the impact on its business of compliance with global climate change guidelines.”44 The proposal received more than sixty-two percent of the votes cast, a tally that included the support of BlackRock and Vanguard.45 A similar proposal at Occidental Petroleum passed earlier in 2017.46

Traditional investors’ growing interest in sustainability disclosure is based on a variety of rationales. Many see sustainability information as facilitating their ability to evaluate a firm’s operational plan from a longer term perspective.47
Investors also use sustainability disclosures to evaluate business risk and have suggested that sustainability disclosure provides insights into a board’s level of engagement and oversight, enabling them to determine the extent to which the board is aware of and managing factors that affect the viability of the company’s strategy over the intermediate and long term.

These analyses identify a potential relationship between sustainability and economic performance. Although the evidence regarding this is mixed, several studies support the claim that sustainability factors are related to operating performance and share price. A recent Bank of America Merrill Lynch study found that positive ESG factors are associated with higher earnings quality and lower risk of bankruptcy. The report claims that ESG attributes are “a better signal of future earnings volatility than any other measure we have found.”

Similarly, an academic paper surveying the empirical ESG literature reports that the vast majority of empirical studies document correlations between sustainability practices and economic performance. Notably, these studies are in tension with the Department of Labor’s recent suggestion that ESG factors are typically collateral to economic considerations.

To the extent there is a relationship between sustainability and performance, sustainability disclosure would seem to fit within the traditional objectives of the federal securities laws. However, the history of sustainability disclosure within the mandatory disclosure regime in the United States has been fragmented. For the most part, as detailed further in the pages that follow, the SEC has taken the view that sustainability disclosure is ordinarily not material, and that mandatory disclosures

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48. See, e.g., Jonas Kron, Senior Vice President, Trillium Asset Mgmt., No Action Letter on The Middleby Corporation Exchange Act Rule 14a 8 (Mar. 23, 2018), https://www.sec.gov/divisions/corpfin/cf noaction/14a 8/2018/trilliumassetetal032318 14a8.pdf (arguing in support of shareholder proposal requesting company to provide a sustainability report that ESG reporting “allows companies to better integrate and capture value from existing sustainability efforts, identify gaps and opportunities in policies and practices, strengthen risk management programs, stimulate innovation, enhance company wide communications, and recruit and retain employees”).


51. Id. at 1.


53. See Canary, supra note 8 (referring to “otherwise collateral ESG issues” but acknowledging that such issues may sometimes “involve business risks or opportunities that are properly treated as economic considerations themselves”).
Disclosure should be limited to information that is useful to investors. The SEC’s approach has had the result of creating a norm that sustainability disclosure is not a component of financial reporting—a norm that this Article seeks to change.

B. THE HISTORY OF SUSTAINABILITY DISCLOSURE UNDER THE FEDERAL SECURITIES LAWS

Efforts by various social and political groups to use the securities laws to obtain greater corporate sustainability disclosure began in the 1960s, partly in response to concerns about the rise of corporate power and its related societal implications. In 1971, the Natural Resources Defense Council (NRDC) and the Project on Corporate Responsibility filed a rulemaking petition asking the SEC to require public companies to make civil rights and environmental disclosures. The SEC refused to adopt the requested rule changes, reasoning that expanded social disclosures were not required under the existing materiality standard. After protracted litigation challenging this decision, the District of Columbia Court of Appeals dismissed the complaint, holding that the SEC’s decision not to require specific disclosures and to require disclosure only of information that was reasonably likely to be material to investors was entitled to substantial deference.

The SEC’s position—that its disclosure requirements should be limited to information that is economically material to investors—was articulated in a 1977


55. See, e.g., id. at 1246 (“Efforts to use the federal securities laws to promote expanded social disclosure began during the late 1960s, growing out of the anti war and environmental movements.”); see also Rob Gray, The Social Accounting Project and Accounting Organizations and Society: Privileging Engagement, Imaginings, New Accountings and Pragmatism over Critique?, 27 Acct., Orgs. & Soc’y 687, 690 (2002) (explaining that, in the mid to late 1960s, interest in social accounting grew “contemporaneously, with an apparent growth in anxiety about corporate ethics, corporate power, social responsibility and ecological degradation”).


report of the Advisory Committee on Corporate Disclosure, led by then-former SEC Commissioner A. A. Sommer, Jr. (the Sommer Report).59 The Sommer Report introduced the disclosure framework that has subsequently been implemented through Regulation S–K.60 As Commissioner Sommer later explained, the Committee concluded that the SEC “should not try to use its powers to compel disclosure concerning, for instance, social or environmental matters, hiring practices, and the like, unless it could be shown that such matters were material to investors.”61

The SEC has adhered to the approach reflected in the Sommer Report. With limited exceptions, described below, the SEC has not required issuers to disclose specific categories of sustainability information. Instead, the SEC has taken the position that such information needs to be disclosed only to the extent it relates to an existing disclosure requirement or is necessary to prevent a required disclosure from being misleading.62 The benchmark is whether the information is material to investors.63 The SEC’s usual position is that, in the context of disclosure requirements, the materiality standard64 should be understood in terms of the information’s economic or financial impact.65 As the then-Director of the SEC’s Division of Corporate Finance explained, “In assessing materiality, the SEC staff takes the view that the reasonable investor generally focuses on matters that have affected, or will affect, a company’s profitability and financial outlook.”66

In articulating this standard, the SEC has relied on the definition of materiality first announced in the context of proxy fraud in TSC Industries, Inc. v. Northway,
In *TSC*, the Supreme Court defined information as material “if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote,” meaning that there is “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 made available.”

The scope of this definition is itself unclear because even in the context of investment decisions, investors might reasonably be interested in information that is nonfinancial or only tangentially related to the issuer’s financial performance.

Recognizing that the question of what information is material to investors is an evolving one, on several occasions the SEC modified its approach to require more comprehensive disclosure with respect to specific sustainability issues. One example is the SEC’s shift toward broadening the required disclosure about executive compensation. After years of taking a restrictive approach in which the SEC regularly went so far as to allow corporations to exclude shareholder proposals seeking to address executive pay, the SEC changed its position and imposed extensive mandatory disclosure requirements. The SEC subsequently modified and expanded these disclosure requirements. Notably, even accepting the view that the size and structure of executive compensation is economically material to investors, some elements of the required disclosure are arguably a stretch, such as the rule that issuers must disclose all executive perquisites valued at $10,000 or more. Nonetheless, the importance of this disclosure is reflected in the SEC’s recent enforcement action against Dow Chemical for failing to disclose executive perks adequately.

68. Id. The Court subsequently concluded that the TSC definition of materiality was applicable in transactional contexts as well. See Basic Inc. v. Levinson, 485 U.S. 224, 232 (1988) (“We now expressly adopt the TSC Industries standard of materiality for the § 10(b) and Rule 10b-5 context.”).
69. By way of example, some investors screen their investments according to social or ethical criteria. Michael S. Knoll, *Ethical Screening in Modern Financial Markets: The Conflicting Claims Underlying Socially Responsible Investment*, 57 BUS. LAW. 681, 684 89 (2002) (explaining that some investors screen their investments according to social or ethical criteria).
The SEC’s position has similarly shifted with respect to climate change disclosure. In 2007, twenty-two institutional investors petitioned the SEC asking it to issue guidance on climate change disclosure. The petition asserted that “the risks and opportunities many corporations face in connection with climate change fall squarely within the category of material information that is required to be analyzed and disclosed in many corporate filings.” Petitioners argued that, as a result, climate change fell within the existing disclosure requirements of Regulation S–K, but that existing disclosures were both inadequate and inconsistent. In 2010, almost three years later, the SEC issued the requested guidance in an interpretive release. The SEC advised issuers that they were required to disclose material information about their exposure to risks resulting from climate change, explaining that this requirement was based in several existing provisions of Regulation S–K, including the MD&A, the required disclosure of legal proceedings, and the section on risk factors. Issuer disclosure of climate change-related information increased following the interpretive release, although criticism of the disclosure’s quality continues, and the SEC’s enforcement has been limited.

Climate change disclosure remains limited due in large part to the vagueness of the disclosure obligation and issuers’ ability to determine, in their judgment, that a given issue is not material enough to warrant disclosure. Exxon’s 2017 10-K provides an example of these limitations. Item 3—“Legal Proceedings”—briefly describes three enforcement actions by the federal Environmental Protection Agency (EPA), North Dakota, and the U.S. Treasury Department.

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77. Id.
78. Id. at 13, 45.
80. Id. at 6293 97. Because the standard focused on materiality, the guidance left the materiality determination, and thus the decision whether to disclose, largely in the hands of the issuer’s management.
81. A Ceres 2018 report stated that fifty one percent of companies disclosed climate change information in their annual financial filings in 2017, as opposed to only forty two percent in 2014. KRISTEN LANG ET AL., CERES, TURNING POINT: CORPORATE PROGRESS ON THE CERES ROADMAP FOR SUSTAINABILITY 11 (2018), https://www.ceres.org/node/2275 [https://perma.cc/L95Q WWGM]. The report cautioned, however, that most of this reporting consisted of “boilerplate language [that failed] to provide investors decision useful information.” Id.; see also Nina Hart, Note, Moving at a Glacial Pace: What Can State Attorneys General Do About SEC Inattention to Nondisclosure of Financially Material Risks Arising from Climate Change?, 40 COLUM. J. ENVTL. L. 99, 114 (2015) (“[C]ompanies are treating climate change risks with brevity and superficiality.”).
83. See ExxonMobil Corp., Annual Report (Form 10 K) (Feb. 28, 2018) (disclosing climate change related risks of Exxon’s business operations).
84. Id. at 26.
Later, in the notes to the financial statements, Exxon states that “a variety of claims have been made against ExxonMobil and certain of its consolidated subsidiaries in a number of pending lawsuits.”\textsuperscript{85} The 10–K does not provide details about the lawsuits, yet it concludes that “[b]ased on a consideration of all relevant facts and circumstances, the Corporation does not believe the ultimate outcome of any currently pending lawsuit against ExxonMobil will have a material adverse effect upon the Corporation’s operations, financial condition, or financial statements taken as a whole.”\textsuperscript{86} Notably absent from the 10–K is any discussion of the high-profile litigation against Exxon by several states that allege its fossil fuel use poses “grave risks” to the planet.\textsuperscript{87} The SEC recently closed a related investigation of the manner in which Exxon disclosed the potential impact of climate change on the value of its assets without imposing a penalty.\textsuperscript{88}

The SEC has also adopted rules mandating disclosure with respect to specific sustainability issues. In response to a worldwide focus on board diversity,\textsuperscript{89} the SEC issued a rule in 2009 requiring issuers to disclose “whether, and if so how, the nominating committee (or board) considers diversity in identifying nominees” for the board of directors.\textsuperscript{90} Former SEC Commissioner Mary Jo White observed that this rule has had limited effect, with companies “generally vague” board diversity disclosures “chang[ing] little” since its adoption.\textsuperscript{91}

The Dodd–Frank Act required the SEC to adopt disclosure requirements with respect to two sustainability issues: conflict minerals and resource extraction.\textsuperscript{92}

\textsuperscript{85.} Id. at 86.

\textsuperscript{86.} Id.


\textsuperscript{90.} Proxy Disclosure Enhancements, Securities Act Release No. 9089, Exchange Act Release No. 61,175, Investment Company Act Release No. 29,092, 74 Fed. Reg. 68,334, 68,364 (Dec. 23, 2009). The Rule goes on to provide that, “[i]f the nominating committee . . . has a policy with regard to the consideration of diversity in identifying director nominees, [disclosure of] how this policy is implemented” is required. Id. at 68,343 44.

\textsuperscript{91.} Mary Jo White, Chair, U.S. Sec. & Exch. Comm’n, Keynote Address at the International Corporate Governance Network Annual Conference: Focusing the Lens of Disclosure to Set the Path Forward on Board Diversity, Non GAAP, and Sustainability (June 27, 2016), https://www.sec.gov/news/speech/white icgn speech.html [https://perma.cc/C5C8-M59H].

The SEC adopted rules in accordance with this mandate, although a subsequent Congress effectively eliminated both rules. Importantly, at the time of Dodd–Frank’s enactment, the SEC objected to the mandates, claiming that the required disclosures fell outside its core mission and were apparently “geared more toward influencing social policy than informing investors.” Indeed, with the limited exceptions described above, the SEC has adhered to the position reflected in the Sommer Report that, as a general matter, sustainability disclosure is not economically material and therefore need not be integrated into financial reporting.

Commentators have called upon the SEC to do more to formalize sustainability disclosure. As part of its Disclosure Effectiveness Initiative, the SEC issued a Concept Release in April 2016. The 341-page release listed various potential reforms to the disclosure system and invited comment on the extent to which SEC rules should mandate sustainability disclosure. Specifically, the release requested comment on the importance of sustainability disclosure for shareholder


96. See Petition for Rulemaking, supra note 14, at 1 2 (explaining how response to SEC’s 2016 Concept Release reflected “an enormous pent up demand by disclosure recipients for more and better disclosure” (quoting GELLASCH, supra note 13, at 10)).


99. Id. at 23,970.
investment and voting decisions. In response, the SEC received tens of thousands of comments on sustainability disclosure, with a substantial number of investors requesting that the SEC “require annual, uniform sustainability reporting from public companies as part of the overhaul of the agency’s disclosure regime.” To date, however, the SEC has not acted on that request.

Investors have attempted to remedy these shortcomings by seeking disclosures on a company-specific basis. One mechanism for doing so is the SEC’s shareholder proposal rule, Rule 14a-8. For many years, shareholders have used Rule 14a-8 with mixed success to introduce proposals addressed to social policy concerns. Such attempts have raised controversy among critics who contend that these proposals are often brought by special interest groups with limited economic stakes and in fact advance views tangential or even contrary to most shareholders’ economic interests.

Two developments have given shareholder proposals a more meaningful role in sustainability disclosure. First, proponents have modified their proposals to concentrate on seeking sustainability disclosure and oversight rather than attempting to cause the company to adopt specific sustainability policies. Second, the proposals are receiving growing support from shareholders in general and from large, mainstream institutional investors in particular.

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100. See id. (“[W]e seek feedback on which, if any, sustainability and public policy disclosures are important to an understanding of a registrant’s business and financial condition and whether there are other considerations that make these disclosures important to investment and voting decisions.”).

101. See, e.g., GELLASCH, supra note 13, at 10 (“As of August 16, 2016, the SEC had received 26,512 comments in response to its Concept Release.”).

102. Odom, supra note 23.

103. 17 C.F.R. § 240.14a-8 (2018). The shareholder proposal rule enables shareholders who meet various ownership and procedural requirements to introduce a proposal on which shareholders can vote at the issuer’s annual meeting and to have that proposal included in the issuer’s proxy statement. Id. The rule provides several bases upon which the issuer can seek to exclude the proposal. Id. For more on this rule, see Fisch, supra note 70, at 1146–47.


105. Classic examples include the shareholder proposal in Lovenheim v. Iroquois Brands, Ltd., 618 F. Supp. 554 (D.D.C. 1985), asking Iroquois to stop force feeding the geese used to make pate de foie gras and the proposal in Philip Morris Cos., 1990 SEC No Act. LEXIS 335 (Feb. 13, 1990), seeking to stop Philip Morris from conducting business in tobacco or tobacco products.

106. See, e.g., Devon Energy Corp., 2014 SEC No Act LEXIS 271 (Mar. 19, 2014) (rejecting issuer’s attempt to exclude shareholder proposal requesting “that the company prepare a report on the company’s goals and plans to address global concerns regarding the contribution of fossil fuel use to climate change, including analysis of long and short term financial and operational risks to the company” and finding that the proposal “does not seek to micromanage the company to such a degree that exclusion of the proposal would be appropriate”).

107. See, e.g., Thomas Singer, Environmental and Social Proposals in the 2017 Proxy Season, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Oct. 26, 2017), https://corpgov.law.harvard.edu/2017/10/26/environmental and social proposals in the 2017 proxy season/ [https://perma.cc/WB8E 5CUK] (“Large institutional investors, such as BlackRock and Vanguard, are beginning to exert pressure on companies by supporting E&S proposals that call for greater disclosure of issues they deem material to shareholder value.”).
A recent Conference Board report observed that almost half of the shareholder proposals brought to a vote during the 2017 proxy season concerned ESG issues and that, although most received limited support, the number of proposals supported by a majority of votes cast continues to increase.\footnote{See id. (describing the Conference Board report findings).} For example, during the 2017 proxy season, a majority of shareholders at three leading companies—Occidental Petroleum, PPL, and Exxon Mobil—approved shareholder proposals requesting greater disclosure on the potential effects of climate change.\footnote{See Cydney Posner, Are Shareholder Proposals on Climate Change Becoming a Thing?, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (June 21, 2017), https://corpgov.law.harvard.edu/2017/06/21/are shareholder proposals on climate change becoming a thing/ [https://perma.cc/JAV2 KEV6].} Among the shareholders voting in favor of the proposals were institutional heavyweights BlackRock and Vanguard,\footnote{See id.; Steven Mufson, Financial Firms Lead Shareholder Rebellion Against ExxonMobil Climate Change Policies, WASH. POST (May 31, 2017), https://www.washingtonpost.com/news/energy-environment/wp/2017/05/31/exxonmobil is trying to fend off a shareholder rebellion over climate change/?utm term=.9579fd3049f6 [https://perma.cc/XVA6 PDDL] (“BlackRock and Vanguard are the biggest shareholders in ExxonMobil, owning 13 percent . . . .”); cf. Jan Fichtner et al., Hidden Power of the Big Three? Passive Index Funds, Re Concentration of Corporate Ownership, and New Financial Risk, 19 BUS. & POL. 298 (2017) (describing BlackRock, Vanguard, and State Street as the “Big Three” of the passive fund industry).} both of which hold substantial stakes in most large public companies.\footnote{See, e.g., Rachel Evans et al., BlackRock and Vanguard Are Less Than a Decade Away From Managing $20 Trillion, BLOOMBERG (Dec. 4, 2017, 2:00 AM), https://www.bloomberg.com/news/features/2017 12 04/blackrock and vanguard s 20 trillion future is closer than you think [https://perma.cc/WT9U RPBQ] (quoting Vanguard founder Jack Bogle as stating that BlackRock, State Street, and Vanguard collectively own about twenty percent of the “biggest U.S. companies”).} The New York City Common Retirement Fund, a cosponsor of the Exxon proposal, described the proposal as economically motivated, explaining that “[c]limate change is one of the greatest long-term risks we face in our portfolio and has direct impact on the core business of ExxonMobil.”\footnote{Mufson, supra note 110.} To the extent that shareholders continue to support proposals for increased sustainability disclosure, issuers will face pressure to provide greater disclosure even in the absence of regulation.\footnote{See, e.g., Ed Crooks, ExxonMobil Bows to Shareholder Pressure on Climate Reporting, FIN. TIMES (Dec. 11, 2017), https://www.ft.com/content/8bd1f73a dedef 11e7 a8a4 0a1e63a52f9c [https://perma.cc/W9U2 RPBQ] (reporting Exxon’s announcement that, in response to investor demands, it would “start publishing reports on the possible impact of climate policies on its business”).}

C. SUSTAINABILITY DISCLOSURE REQUIREMENTS BEYOND THE FEDERAL SECURITIES LAWS

Federal securities laws are not the only source of sustainability disclosure requirements, some of which can be found in other areas such as federal
environmental law,114 employment law,115 and consumer law,116 and in the laws of some states.117 At best, however, these disclosure requirements operate in a piecemeal manner and do not provide a complete picture of the sustainability issues with a potentially material impact on issuer operations. Mandatory sustainability disclosure is more common in jurisdictions outside the United States.118 Since 2006, a four-institution partnership has led a project collecting and reporting data on required sustainability reporting across the


117. For example, the California Transparency in Supply Chains Act of 2010 requires any retailer that does business in the state and has annual worldwide gross receipts exceeding $100 million to make specific disclosures on its website about the efforts it makes to “eradicate slavery and human trafficking from [its] direct supply chain.” KAMALA D. HARRIS, ATT’Y GEN., CAL. DEP’T OF JUSTICE, THE CALIFORNIA TRANSPARENCY IN SUPPLY CHAINS ACT: A RESOURCE GUIDE, at i (2015), https://oag.ca.gov/sites/all/files/agweb/pdfs/sb657/resource guide.pdf. The Act requires disclosures on five areas: verification, audits, certification, internal accountability, and training and even companies that take no actions relating to a given category must disclose that fact. Id. at 4. The statute provides no private right of action and is enforceable exclusively by the California Attorney General. Id.

Plaintiffs’ lawyers have also been using class actions based on state consumer protection statutes or claims of false advertising in an effort to create broader sustainability disclosure obligations. In Barber v. Nestlé USA, Inc., plaintiffs sought to impose an obligation on Nestlé to disclose that its cat food likely contained some seafood that was “produced by forced labor.” 154 F. Supp. 3d 954, 957 (C.D. Cal. 2015). In Hodsdon v. Mars, Inc., 162 F. Supp. 3d 1016 (N.D. Cal. 2016), plaintiff sought to force Mars to disclose on its chocolate bars that they contained cocoa beans likely picked under conditions of child or slave labor. In Hall v. SeaWorld Entm’t, Inc., No. 3:15 CV 660 CAB RBB, 2015 WL 9659911 (S.D. Cal. Dec. 23, 2015), plaintiffs sought to require SeaWorld to disclose facts concerning the health and welfare of the killer whales it held in captivity. To date, such lawsuits have been largely unsuccessful. See, e.g., Andrew G. Barna, Note, The Early Eight and the Future of Consumer Legal Activism to Fight Modern Day Slavery in Corporate Supply Chains, 59 WM. & MARY L. REV. 1449, 1454 (2018) (reporting that trial courts dismissed each of the initial eight consumer activist suits in California, although, at the time of the article’s publication, appeals were still pending in several). In SeaWorld, for example, the court dismissed the case, reasoning that applying plaintiffs’ theory would expose companies to limitless liability. 2015 WL 9659911, at *7.


Although a comprehensive examination of foreign jurisdictions’ requirements is beyond the scope of this Article, it is worth noting some of the more interesting approaches to CSR, such as that in India. In 2013, India adopted a requirement that firms develop a board centered CSR policy and “spend at least two percent of their profits on CSR activities.” Afra Afsharipour, Corporate Social Responsibility and the Corporate Board: Assessing the Indian Experiment, in GLOBALISATION OF CORPORATE SOCIAL RESPONSIBILITY AND ITS IMPACT ON CORPORATE GOVERNANCE 95, 96 (Jean J. du Plessis et al. eds., 2018).
Its 2016 report details evidence of a trend toward mandatory disclosure. It also analyzes mandatory and voluntary disclosures across seventy-one countries. According to the report, many of the reporting requirements are found in areas such as environmental law rather than investor-oriented regulation, but stock exchanges and financial regulators are the source of almost one-third of the requirements, many of which take the form of an obligation to comply or explain.

The EU’s 2014 directive mandating sustainability disclosure is perhaps the most notable development in this regard. It required large companies across the EU to publish information on their policies with respect to environmental protection, social responsibility, human rights, anti-corruption, and board diversity, starting in 2018. The directive expressly terms this information part of a company’s “non-financial statement” and does not appear to contemplate the integration of these disclosures with issuers’ financial reporting.

In June 2017, the EU published guidelines to assist companies in complying with the directive. Although not mandatory, the guidelines clarify that the directive’s focus differs importantly from U.S. federal securities disclosure, in that the EU directive is explicitly stakeholder, rather than shareholder, oriented. By December 2017, all EU member states had implemented the directive through national legislation, although the form of that legislation varies...
“according to local conditions.” The EU directive is an important step that reflects an emerging global trend toward mandatory reporting, but it has also faced criticism from those who argue that its approach is likely to have limited efficacy in improving disclosure quality.

D. VOLUNTARY SUSTAINABILITY DISCLOSURE

In the absence of a uniform and universal mandatory regime, market forces continue to fuel the growth of voluntary sustainability disclosure. Most sustainability information is disclosed not in issuer financial or securities filings, but in standalone sustainability reports. The Governance & Accountability Institute reported that, in 2016, eighty-two percent of S&P 500 companies published sustainability or corporate responsibility reports. These reports vary in their length and the range of topics covered. It is increasingly common for sustainability reports to exceed one hundred pages in length, and some issuers produce multiple sustainability reports, each on different topics. For example, in 2017, Apple produced both an environmental responsibility report and a supplier responsibility report, and provided additional descriptions of its inclusion and diversity initiatives on its website.

The dominance of voluntary disclosure and the varied sources of that disclosure have contributed to the growth of global standard setters seeking to promulgate disclosure standards or guidelines, or rate issuers on the quality of their disclosure or sustainability practices. The number of standard setters, data repositories, and ratings organizations is huge and continues to grow. Although a description of all the important and relevant institutions and standards is beyond
the scope of this Article, the following discussion highlights a few of the most prominent examples.

One way that private organizations contribute to the quality and usability of sustainability disclosure is by promulgating disclosure standards. The Global Reporting Initiative (GRI), an international organization founded twenty years ago as a U.S. non-profit, is one of the best-known private standard-setting organizations. Companies around the world use the GRI’s standards for sustainability reporting in whole or in part. In its 2017 worldwide survey of companies that report sustainability information, KMPG found that seventy-three percent used the GRI standards. The GRI also maintains a free searchable database of more than 46,000 individual issuer sustainability reports.

Another well-known standard-setting organization is the Sustainability Accounting Standards Board (SASB). In contrast to the GRI, the SASB’s focus has been to develop disclosure standards that are incorporated into SEC filings rather than separate sustainability reports. To this end, the SASB has developed industry-specific disclosure standards for seventy-seven industries. The SASB’s position is that its standards either are or should be incorporated into issuer financial reporting under the current legal requirements. According to the SASB, its “standards focus on known trends and uncertainties that are reasonably likely to affect the financial condition or operating performance of a company and therefore would warrant disclosure under Regulation S–K.”

The volume of sustainability information disclosed in accordance with these and other standards complicates the task of evaluating a particular issuer’s sustainability practices. A number of organizations offer sustainability rankings or

137. For a list and brief description of key institutions, see id. app.1 at 23 24.

In 2010, the GRI and the UN Global Compact signed an accord in which the GRI agreed to integrate the UN Global Compact’s reporting framework into its sustainability reporting guidelines. United Nations Global Compact, GRI, https://www.globalreporting.org/information/about gri/alliances and synergies/Pages/United Nations Global Compact.aspx (last visited Feb. 13, 2019).

139. KMPG, supra note 138, at 29.
142. *Id.*
143. *Id.*
144. *Id.*
145. See, e.g., Rate the Raters: Understanding the Universe of Corporate Sustainability Rankings, SUSTAINABILITY, http://sustainability.com/rate the raters/ (last visited Feb. 13, 2019) (“There are a dizzying number and variety of external ratings, rankings, indices and awards that seek to measure corporate sustainability performance.”).
ratings to assist in this endeavor. One of the best-known indices is the Dow Jones Sustainability Index (DJSI). Notably, the DJSI is based not on public disclosures but on information collected directly by invitation from 3,400 worldwide issuers through a questionnaire called the Corporate Sustainability Assessment. The data are based on “approximately 80-120 questions on financially relevant economic, environmental and social factors that are relevant to the companies’ success, but that are under-researched in conventional financial analysis.” The DJSI rates top companies annually and is billed as the “gold star for corporate sustainability.”

Another rating organization, the CDP (formerly the Carbon Disclosure Project), publishes a variety of research based on voluntary environmental disclosures it obtains directly from issuers. According to the CDP, “[r]eporting companies now represent over 50% of global market capitalization.” The CDP scores companies based on their transparency and environmentalism, again using the information they supply.

Another rating organization run by Newsweek publishes annual sustainability rankings of large issuers, the Newsweek Green Rankings. Newsweek’s methodology is designed to be replicable by third parties, and it discloses its precise underlying metrics. In addition, unlike the DJSI and the CDP, Newsweek’s rankings are based on publicly available data.

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147. For a general description of this comprehensive index, see About Us, ROBECOSAM, https://www.sustainability indices.com/about us [https://perma.cc/2BFG YLKO] (last visited Oct. 25, 2018).


149. Id.

150. Id.


153. Id.


155. Id.

156. Id.
II. LIMITATIONS OF EXISTING SUSTAINABILITY DISCLOSURE

The structure of the existing voluntary disclosure framework is problematic for several reasons. This Part highlights some of the key problems with this regime to demonstrate why, despite the growth in the volume of sustainability disclosure, private ordering has not been successful in producing sustainability disclosures that meet investors’ needs. As Trillium Asset Management explained in a comment letter to the SEC: “While voluntary reporting frameworks are better than nothing at providing ESG information at participating companies they do not provide the consistency, accuracy and completeness that is inherent in securities filings.”

Under the current regime, sustainability disclosures are fragmented, of inconsistent quality, and often unreliable. As explained in this Part, issuers are incentivized to focus on the positive aspects of their business practices and to omit unfavorable information. This problem is compounded by a lack of standardization that makes it difficult for investors to compare information across issuers, in addition to the limited regulatory oversight of sustainability disclosure. These issues stem, in part, from the voluntary nature of the current regime. Because disclosure is voluntary, issuers can choose which issues to address and which reporting metrics to apply. As a result, issuers overwhelmingly disclose only information about the areas in which their business practices are highly sustainable.

See, e.g., VINTAGE & MERGERMARKET, A QUESTION OF QUALITY: HOW TO IMPROVE SEC DISCLOSURE 11 (2016), https://www.acuris.com/assets/Vintage Group Newsletter 3 2016 Final LR.pdf (“Many companies now produce separate sustainability or corporate social responsibility reports . . . . But sometimes they are selective and basically say, ‘Here are all the nice things we did last year’—community activities, reducing their carbon footprint, and various other things. They don’t necessarily focus on the issues that really matter in the context of their industry.”).


159. See, e.g., Klaus Dingwerth & Margot Eichinger, Tamed Transparency: How Information Disclosure Under the Global Reporting Initiative Fails to Empower, 10 GLOBAL ENVTL. POL. 74, 88 (2010) (explaining that information in disclosures is “unbalanced” and “of limited practical use”).

160. See, e.g., Markus J. Milne & Rob Gray, Whither Ecology? The Triple Bottom Line, the Global Reporting Initiative, and Corporate Sustainability Reporting, 118 J. BUS. ETHICS 13, 17 (2013) (describing the poor quality and incompleteness of many triple bottom line reports, most of which “cover few stakeholders” and “cherry pick elements of news and generally ignore the major social issues that arise from corporate activity.”).

161. See, e.g., VINTAGE & MERGERMARKET, A QUESTION OF QUALITY: HOW TO IMPROVE SEC DISCLOSURE 11 (2016), https://www.acuris.com/assets/Vintage Group Newsletter 3 2016 Final LR.pdf (“Many companies now produce separate sustainability or corporate social responsibility reports . . . . But sometimes they are selective and basically say, ‘Here are all the nice things we did last year’—community activities, reducing their carbon footprint, and various other things. They don’t necessarily focus on the issues that really matter in the context of their industry.”).

162. For example, in Volkswagen’s sustainability reports, the company concentrated heavily on its efforts to reduce CO2 emissions and included little discussion of its emissions of NOx, later found to be the main pollutant released by Volkswagen’s cars as a result of its emissions testing modifications. See, e.g., Akmaral Zhakypova, Dissecting Corporate Sustainability Reporting: VW Emissions Scandal Case 22 (2016) (unpublished manuscript), https://nature.berkeley.edu/classes/es196/projects/2016final/
reports poor tools for assessing the extent to which sustainability issues represent material business risks.

The practice of emphasizing positive and omitting negative information to make an issuer’s business practices appear to be more sustainable than they actually are is known as “greenwashing.”163 Perhaps the most prominent recent example of greenwashing was Volkswagen, which was long praised as a global leader in corporate social responsibility, based largely on its self-disclosed sustainable practices.164 In 2015, Volkswagen was named the world’s most sustainable car company by the Dow Jones Sustainability Index.165 Just one week later, U.S. regulators publicly announced the emissions scandal.166

Voluntary disclosure also tends to be vague, general, or boilerplate, rather than providing investors with the specific information that would enable comparison of companies’ sustainability practices.167 The corporate desire for generic disclosure is rational—to the extent issuers disclose specifics, investors can more readily identify outliers and pressure a change in their policies.
Even when voluntary disclosure is relatively balanced and comprehensive, it has other limitations. The absence of standardized disclosure requirements may lead issuers to disclose such a high quantity of information that it results in information overload. Critics have argued that existing securities disclosure requirements are so excessive as to flood the markets with so much information that investors cannot use the information intelligently, but voluntary sustainability disclosures are, in many cases, far more extensive than mandatory financial disclosures.

Because no centralized regulator or authority is responsible for establishing disclosure standards, even within a single jurisdiction, sustainability disclosure is fragmented rather than standardized. Issuers can choose which metrics or standards to use for their disclosures and which among those standards to report on. The absence of standardization impedes the market’s ability to compare issuer sustainability practices, even among similar companies. According to one study, nearly eighty percent of investors were dissatisfied with the “comparability of sustainability reporting between companies in the same industry.” In another, only eight percent of investors polled believed that “existing ESG disclosures allow for comparison across companies/peers.”

Although third-party ratings and rankings attempt to address the comparability issue, they suffer from some of the same defects, including limitations in coverage, differences in the information used, and heavy reliance on issuer-supplied information. In addition, rating agencies do not produce consistent results, presumably due in part to methodological differences. An analysis comparing “three of the most well-known and [publicly] available CSR rankings published in 2015: Newsweek, Forbes, and CSR Magazine Global” found that only twelve

170. See supra notes 132–35 and accompany text (describing length of voluntary sustainability reports).
173. SUBRAMANIAN ET AL., supra note 50, at 6.
174. Because third party ratings appear to be independent, they can be highly influential, making their unreliability and inconsistency particularly problematic. The influence of credit rating agencies prior to the 2008 financial crisis offers a warning. See, e.g., Frank Partnoy, What’s (Still) Wrong with Credit Ratings?, 92 WASH. L. REV. 1407, 1410, 1412 (2017) (discussing the contribution of credit ratings to the financial crisis).
175. As noted, see supra notes 164–66 and accompanying text. Volkswagen successfully concealed car emissions not just from regulators and consumers but also the DJSI, which named Volkswagen the world’s most sustainable car company in 2015, just before news of the emissions scandal broke.
percent of companies appeared on all three lists. A *Wall Street Journal* study noted similar disagreement among the “four leading ESG ratings providers,” finding they came to completely different conclusions “about what makes a company a ‘sustainable’ investment.” As another *Wall Street Journal* explained, despite these inconsistencies, ESG ratings “are used as though they were some sort of objective truth,” although “[i]n reality they are no more than a series of judgments by the scoring companies about what matters.”

Finally, sustainability reporting is not reliable. As noted, such reporting mostly occurs in standalone reports that are not integrated with the issuer’s securities filings. These reports are often prepared by public relations or marketing personnel and, as a result, contain disclosures that do not meet the standards applied to securities filings. Furthermore, they are not routinely prepared or reviewed by disclosure lawyers, reviewed or certified by the CEO or board of directors, or subject to the oversight of third-party auditors. Finally, unlike securities filings, sustainability reports are not filed with and reviewed by the SEC. Although, in theory, sustainability reports are public disclosures, it is unclear whether greenwashing or other false disclosures in these reports would subject the issuer to liability for federal securities fraud. As a result, issuers may take less care in the preparation of their sustainability disclosures.

These limitations in the existing framework are behind investors’ demands for an SEC rule that mandates sustainability reporting. Investors that value sustainability considerations as relevant to economic performance, as well as those that wish to explore the question of their relevance, need quality information. Significantly, sustainability information is important for an evaluation of issues such as board oversight, risk management, and business practices, regardless of the extent to which investors believe an issuer should focus on sustainability in business decisions. Moreover, if sustainability disclosures relate to issues such as financial performance and risk management, those disclosures should be


180. This Article does not take a position on the normative question of the extent to which corporate decisionmaking should reflect sustainability considerations or, if so, which sustainability issues it should address.
integrated into investor-oriented disclosure documents rather than provided in separate reports as in current practice. Integration would have the added benefit of increasing interfirm comparability and reducing wasteful and duplicative search costs. Critically, SEC action is necessary because investors are allocating capital and businesses are basing operational decisions on sustainability information that is unreliable. As a result, the economic value of sustainability practices cannot be assessed effectively.

However, the challenge in adopting a disclosure mandate for sustainability within the existing securities disclosure framework is in the implementation. As noted, commentators have called for sustainability reporting to address a wide range of issues,181 but the applicability of any specific issue varies by issuer and industry.182 In addition, sustainability is a moving target, meaning that the issues that arguably warrant disclosure and their importance continue to evolve. Because of these characteristics, designing a line-item series of disclosures to address sustainability is likely unworkable, and a principles-based approach appears more appropriate.

The SEC’s materiality standard is arguably a principles-based requirement in that, to the extent sustainability issues are material to the existing mandated disclosure items—such as an issuer’s business plan, financial operations, risk factors, or litigation risk—disclosure of those issues is required. This approach, however, does little to encourage either affirmative disclosures or issuer attention to determining whether sustainability issues are economically significant. In other words, an additional value to an affirmative disclosure requirement is its ability to focus board and management attention on acquiring information and exercising oversight.

This benefit can be analogized to that provided by the CEO and CFO certification requirement established by the Sarbanes–Oxley Act of 2002 (SOX).183 Section 302 of SOX requires the CEOs and CFOs of public companies personally to certify that the reports filed by their companies with the SEC are both accurate and complete.184 Among the statute’s requirements are that the certifying officers establish, maintain, and evaluate the effectiveness of the company’s internal controls.185 False certifications subject officers to potential liability in an SEC enforcement action, as well as to criminal liability.186 SOX also contains a

181. See Brown, supra note 34 (describing various calls for expanded sustainability disclosure).
184. SOX § 302(a).
185. Id.
186. SOX § 906, 18 U.S.C. § 1350 (2012), imposes criminal liability. See also Erin Massey Everitt, Sarbanes Oxley’s Officer Certification Requirements Has Increased Accountability Equaled Increased Liability?, 6 DEPAUL BUS. & COM. L.J. 225, 244 45 (2008) (discussing criminal and enforcement liability). Notably, the provision does not contain a private right of action. Id. at 235 36.
A provision requiring executives to forfeit incentive compensation and bonuses if their companies must restate their financial statements due to fraud or accounting errors.\textsuperscript{187}

Enforcing the SOX certification requirement presents a challenge. Some commentators have characterized the SEC’s limited enforcement efforts as “worrisome and problematic,”\textsuperscript{188} or have criticized the failure of the provisions themselves to impose liability on private plaintiffs.\textsuperscript{189} On the other hand, there is widespread evidence of the certification requirement’s effectiveness in encouraging corporate executives to be more engaged in their company’s financial reporting and more proactive in seeking out the information necessary to engage in better oversight.\textsuperscript{190} In the next Part, this Article offers a proposal for sustainability disclosure designed to encourage greater information flow and board oversight akin to the rationale behind SOX section 302. In the following Part, the Article addresses enforcement of the proposal.

### III. SD&A: A Proposed Approach for Mandated Sustainability Disclosure

This Article proposes that the SEC implement a new disclosure requirement of sustainability discussion and analysis as part of Regulation S–K, thereby requiring issuers to include SD&A reporting as part of their annual reports.\textsuperscript{191} The SD&A requirement is modeled on the existing MD&A and CD&A reporting requirements, which are described in this first section of this Part. In the second section, this Part then describes the details of the SD&A proposal, including several modifications to the MD&A and CD&A models that both address the specialized issues implicit in sustainability disclosure and enhance the effectiveness of the requirement.\textsuperscript{192}

\begin{itemize}
\item[187.] SOX § 304(a), 15 U.S.C. § 7243(a).
\item[189.] Everitt, supra note 186, at 235 36.
\item[190.] See id. at 245 (“The officer certification requirements of the Sarbanes Oxley Act have proven quite effective at prompting executives of publicly traded companies to become more engaged in the financial reporting process.”).
\item[191.] This Article’s proposal for issuers to include a narrative discussion of sustainability issues in the annual report is highly workable. Indeed, Salesforce voluntarily introduced a discussion of environmental, social, and governance information in its 2018 Annual Report, Salesforce, Annual Report 64–65 (Form 10-K) (Feb. 28, 2018), https://s1.q4cdn.com/454432842/files/doc_financials/2018/Salesforce FY18 Annual Report.pdf.
\item[192.] To the extent that the SEC determines that the SD&A requirement will impose significant new oversight costs on issuers, it may decide to implement the requirement on a delayed or tiered basis for smaller issuers or emerging growth companies. This approach would resemble that taken by the JOBS Act, which exempts emerging growth companies from some of Dodd Frank’s disclosure requirements with respect to executive compensation as well as the non-binding shareholder vote on such compensation. See, e.g., Amy Coleman, Note, A Plague of Locusts: The JOBS Act as Foe More than Friend, 16 DUQ. BUS. L.J. 43, 61 (2013) (“[The JOBS Act] negates the separate shareholder vote for executive compensation and the disclose of executive compensation for median employee income requirement set by Dodd Frank.”).\
\end{itemize}
A. MD&A AND CD&A: THE MODELS FOR AN SD&A REQUIREMENT

The SD&A requirement is modeled on two existing narrative disclosure frameworks: Management Discussion and Analysis (MD&A) and Compensation Discussion and Analysis (CD&A). The MD&A disclosure requirement—contained in Item 303 of Regulation S–K and SEC Interpretive Release Number 6835—was adopted specifically to supplement the line-item disclosures with more flexible and company-specific disclosures.193 As the SEC explained,

The Commission has long recognized the need for a narrative explanation of the financial statements, because a numerical presentation and brief accompanying footnotes alone may be insufficient for an investor to judge the quality of earnings and the likelihood that past performance is indicative of future performance. MD&A is intended to give the investor an opportunity to look at the company through the eyes of management by providing both a short and long-term analysis of the business of the company. The Item asks management to discuss the dynamics of the business and to analyze the financials.194

Importantly, Item 303 creates an affirmative and nonspecific duty to disclose material information when management knows of a trend, demand, commitment, or uncertainty.195 In adopting Item 303, the SEC explicitly disclaimed the application of the court-adopted definition of materiality.196 Instead, in its 1989 Release, the SEC issued the following guidance: “A disclosure duty exists where a trend, demand, commitment, event or uncertainty is both presently known to management and reasonably likely to have material effects on the registrant’s financial condition or results of operation.”197

The SEC went on to explain that that, when management knows of a trend, demand, commitment, event, or uncertainty, it must “make two assessments”:

(1) Is the known trend, demand, commitment, event or uncertainty likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required.

(2) If management cannot make that determination, it must evaluate objectively the consequences of the known trend, demand, commitment, event


196. See id. at 22,430 n.27 (“The probability/magnitude test for materiality approved by the Supreme Court in Basic, Inc. v. Levinson, 108 S. Ct. 978 (1988), is inapposite to Item 303 disclosure.”).

197. Id. at 22,429.
or uncertainty, on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the registrant’s financial condition or results of operations is not reasonably likely to occur.\footnote{198}

The importance of MD&A disclosure continues to grow. As explained in one article, “[T]he MD&A is fast becoming the primary disclosure vehicle for management to relate its unique insider’s critique of the registrant’s financial performance and operations to help predict future performance.”\footnote{199} Another explains that “[t]oday, the MD&A is widely considered to be the primary form of narrative disclosure that is reviewed, together with financial statements, for investment decision making.”\footnote{200} On the other hand, the vague and flexible standard makes the requirement difficult for issuers to comply with.\footnote{201} In one high-profile case, the SEC brought an enforcement action against Caterpillar for failing to disclose, in its MD&A, the importance of its Brazilian subsidiary to the firm’s financial results and the likely impact of political changes in Brazil on future results.\footnote{202} Caterpillar has been characterized a “message case” indicating that the SEC intends to require improved disclosure.\footnote{203}

The CD&A is a more recent disclosure requirement, modeled on the MD&A. The SEC adopted the CD&A requirement in 2006 as part of its executive compensation disclosure reforms.\footnote{204} Issuers are required to provide the CD&A as part


201. See Rick E. Hansen, Climate Change Disclosure by SEC Registrants: Revisiting the SEC’s 2010 Interpretive Release, 6 BROOK. J. CORP. FIN. & COM. L. 487, 495 (2012) (“[C]rafting an MD&A that is responsive to the SEC’s rules is arguably among the most difficult aspects of preparing a quarterly or annual report and has prompted the SEC to issue MD&A specific guidance on several occasions.”).


of their executive compensation disclosure in the proxy statement. The CD&A is intended "to provide to investors material information that is necessary to an understanding of the [company’s] compensation policies and decisions," focusing on "the most important factors relevant to analysis of those policies and decisions." Specifically, the CD&A is intended to be principles-based and to avoid boilerplate. Item 402, the SEC rule that governs executive compensation disclosure, sets out the requirements for the CD&A in two ways. First, Item 402(b)(1) lists a variety of "mandatory principles-based topics" that issuers must address. The rule identifies a variety of components of the required CD&A disclosure, including the objectives of the compensation program and how each element of compensation is determined. Item 402(b)(2) then acknowledges that "the material information to be disclosed under Compensation Discussion and Analysis will vary depending upon the facts and circumstances," and lists fifteen "examples" of "material information" that may be included in the CD&A.

Both the MD&A and CD&A disclosures are primarily principles-based. As such, they offer flexibility that both permits tailoring the disclosures to the issuer’s particular circumstances and allows the disclosures to evolve in response to changes in issuer and market conditions. As the SEC staff explained with respect to its MD&A requirement: "[T]he flexible nature of this requirement has resulted in disclosures that keep pace with the evolving nature of business trends without the need to continuously amend the text of the rule." The flexibility of the existing MD&A and CD&A disclosures is a primary reason to use them as the model for an SD&A requirement. At the same time, these disclosures suffer from several disadvantages relative to line-item disclosure requirements. First, because they are premised on a materiality determination by management, the disclosures offer management substantial discretion that is

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205. See 17 C.F.R. § 240.14a 101, Item 8(b) (2018) (setting forth the required disclosure of the compensation of directors and executive officers). The details of the CD&A requirement are included in id. § 229.402(b)(1), which is cross referenced in Regulation 14A.

206. Id. § 229.402, Instructions to Item 402(b), ¶ 1.

207. See id. (noting that the CD&A “should focus on the material principles underlying the registrant’s executive compensation policies and decisions and the most important factors relevant to analysis of those policies and decisions” and “shall avoid boilerplate language”).


209. Id. § 229.402(b)(1)(2018).

210. Id. § 229.402(b)(2).

211. Id.

212. Id.


often exercised in favor of failing to disclose. Even well-meaning insiders may evaluate the materiality standard differently. Second, the disclosures are not as readily comparable as quantitative disclosure requirements. The SEC itself has criticized existing MD&A disclosure as “less detailed” than desired and in need of “greater analysis” and “additional explanation.”215 One SEC official offered the view that “in too many MD&As . . . . [t]here is too much elevator music, and not enough really useful analysis.”216 As a result, it is worth considering whether, in adopting the MD&A model for sustainability disclosure, that model can be refined to enhance its effectiveness.

B. THE SD&A PROPOSAL

The SD&A requirement proposed by this Article would require issuers to include a discussion of sustainability in their annual financial reporting. Issuers would be required, in their SD&A, to identify and explain the three sustainability issues most significant to their operations.217 The required disclosure would include a discussion of the potential impact of those sustainability issues on the issuer’s economic performance,218 as well as an explanation of the basis for the issuer’s determination of significance.219 Analogous to the MD&A, the SD&A disclosure would be premised on known risks, trends, and opportunities, in that the requirement would be framed in terms of known or reasonably knowable sustainability issues. This would include risks, trends, and opportunities that, in the opinion of the board of directors, are material to the issuers’ business plan or operations.


217. Although this requirement may seem arbitrary, including three sustainability issues is a cost effective way of capturing the most significant risks without making the disclosure requirement unduly burdensome. Anecdotal evidence suggests that it also reflects existing practice. For example, at a September 2018 public program, NYU Law’s Investors and ESG Conference, a high level public company executive identified three primary subjects in discussing his corporation’s approach to sustainability.

218. This proposal focuses on sustainability that is “internal” in the sense that it is focused on the issuer’s operational practices and not on an issuer’s engagement efforts aimed at general societal improvements such as volunteerism or donating to charity. Some commentators have distinguished between internal and external CSR, although the use of these terms varies. See, e.g., Olga Hawn & Ioannis Ioannou, Mind the Gap: The Interplay Between External and Internal Actions in the Case of Corporate Social Responsibility, 37 STRATEGIC MGMT. J. 2569 (2016) (empirically analyzing issuer engagement in internal and external CSR as well as the gap between external and internal actions).

219. Robert Eccles and Tim Youmans have proposed that boards voluntarily issue a sustainability statement in their annual reports through what they term a “Statement of Significant Audiences and Materiality.” Robert G. Eccles & Tim Youmans, Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality 6 (Harvard Bus. Sch., Working Paper No. 16 023, 2015), https://www.hbs.edu/faculty/Publication%20Files/16 023 /f9dce5d cbac 4840 8d5f 32b21e6f644e. pdf. Like the SD&A, the Eccles and Youmans statement would increase board involvement in and oversight of sustainability issues, but their proposal differs from the one developed in this Article in several key aspects, including perhaps most importantly its focus on stakeholder significance. See id. at 1, 6.
The requirement that issuers identify and discuss the three most significant sustainability issues responds to the range of challenges that have been brought against mandated sustainability disclosure.\textsuperscript{220} By requiring the SD&A to focus on the specific issues that are most important to a particular issuer’s operations, the proposal addresses the difficulty in articulating a precise definition of materiality or determining an appropriate materiality standard. Although the SD&A does not provide a comprehensive level of disclosure, it is a workable starting point that enables boards and investors to identify and evaluate those practices most likely to have a substantial economic impact. In addition, as discussed further in the pages that follow, a requirement that issuers disclose the three most material issues reduces the potentially burdensome impact associated with a more ambitious disclosure requirement, while providing more objectivity than the generic but un-cabinined materiality standard currently reflected in the SEC’s approach to MD&A disclosure. Thus, the proposal is arguably superior to a standard that would require disclosure of all material sustainability issues or condition disclosure requirements in terms of a minimum dollar threshold of anticipated economic impact.\textsuperscript{221}

The proposal contemplates that the SEC’s adopting release would provide additional guidance with respect to the nature and scope of sustainability issues, similar to the guidance it provided for CD&A. Specifically, the guidance would identify the range of topics that have been identified within the framework of sustainability, such as “climate change, resource scarcity, corporate social responsibility, and good corporate citizenship,”\textsuperscript{222} but would note that the identification of material sustainability issues is industry- and issuer-specific. The release would also note that the materiality of specific sustainability issues can evolve over time and is a product of a variety of considerations, including the relevance of the issue to earnings quality and volatility, reputational and regulatory risk, and the quality of board oversight and internal controls.

The SD&A proposal would modify the guidelines of Item 303 to place responsibility for the determination of what sustainability issues require disclosure in...
the hands of the board of directors, rather than management.223 This is consistent with one of the main reasons proffered by investors for requiring sustainability disclosure: that such disclosure provides them with valuable insight into the board’s familiarity with and oversight of critical issues such as risk management. In addition, the SEC recently highlighted the expertise of the board in evaluating the significance of particular issues to the company’s business.224 The board or a sustainability committee of the board225 would also be required to sign the SD&A.226 Like the CEO and CFO certification requirements of Sarbanes–Oxley, the certification requirement would encourage issuers to develop systems for collecting and communicating the information necessary for the board to meet this obligation.227

The rationale for requiring both board responsibility and certification is to ensure that the process of preparing the SD&A enhances the board’s role in understanding and overseeing the issuer’s sustainability practices. From an investor’s perspective, the key issues are whether the directors are aware of the sustainability issues that may materially affect the issuer’s operations and whether they have incorporated those issues into their strategic planning and oversight. Placing specific responsibility on directors enables investors to ensure that the board is performing this role and to hold the board accountable for doing so.

Finally, as detailed later, this Article contemplates that the SD&A requirement would be enforced through a combination of public and private enforcement. The SEC staff would review and comment on issuers’ SD&A disclosures as part of its review of securities filings and would have the authority to bring enforcement

223. This board centered approach follows that of India, which, through legislation, placed primary responsibility for development and oversight of an issuer’s CSR policy in the board of directors. See Afscharipour, supra note 118, at 101 04 (discussing India’s approach). This Article’s focus on the board’s role is limited to disclosure oversight, with the expectation that such oversight would broaden the information available to the board for purposes of risk management and strategic planning.

224. See, e.g., Staff Legal Bulletin No. 14I (CF), U.S. SEC. & EXCH. COMM’N (Nov. 1, 2017), https://www.sec.gov/interps/legal/cfslb14i.htm [https://perma.cc/RZL5 TUA2] (observing that, in the context of determining the application of the ordinary business exemption to shareholder proposals, “[a] board acting in this capacity and with the knowledge of the company’s business and the implications for a particular proposal on that company’s business is well situated to analyze, determine and explain whether a particular issue is sufficiently significant”).

225. See, e.g., Jayne W. Barnard, At the Intersection of Corporate Governance and Environmental Sustainability, 2 WM. & MARY BUS. L. REV. 207, 207 (2011) (articulating “several advantages to having a board level sustainability committee”).

226. This requirement was part of Jeffrey Gordon’s proposal for CD&A but was not adopted. See Gordon, supra note 204, at 695 (“This CD&A should . . . be signed by the members of the committee (or the independent directors, as the case may be).”).

227. See, e.g., Robert Charles Clark, Corporate Governance Changes in the Wake of the Sarbanes Oxley Act: A Morality Tale for Policymakers Too, 22 GA. ST. U. L. REV. 251, 266 (2005) (“[A] fair number of public company CEOs have already expressed the view that the process of getting ready for section 404 attestation has helped them improve their management information systems;”; see also Robert A. Prentice & David B. Spence, Sarbanes Oxley as Quack Corporate Governance: How Wise is the Received Wisdom?, 95 GEO. L.J. 1843, 1898 1907 (2007) (discussing the impact of Sarbanes Oxley’s certification requirements).
actions against issuers and individual directors for failure to comply. In addition, fraudulent misrepresentations and omissions in an issuer’s SD&A would be actionable under Rule 10b-5, and shareholders could, in appropriate cases, pursue private litigation.

IV. ADVANTAGES AND LIMITATIONS OF SD&A

This Part identifies the key advantages of the SD&A proposal as well as the principal potential objections. Importantly, SD&A is a modest starting point for sustainability disclosure, and the proposal advanced in this Article is intended as a first step that will enable issuers, investors, and regulators to assess the utility of sustainability disclosure and provide data to evaluate claims of the relationship of sustainability to economic value. This Article does not make the claim that the SD&A will provide investors and the markets with comprehensive sustainability information or that it will or should displace existing voluntary disclosure regimes. Rather, for the reasons set out in the sections that follow, integrating sustainability disclosure into traditional financial reporting provides several advantages.

A. THE SD&A PROPOSAL IS A WORKABLE FIRST STEP

A key advantage to the SD&A proposal is its workability. One of the challenges in formulating a mandatory sustainability disclosure requirement is that the topic of sustainability is vast and open-ended. Private organizations such as GRI and SASB have identified dozens of disclosure items, and current sustainability reports commonly exceed one hundred pages in length. The cost of developing and complying with comparable mandatory disclosure requirements would place a heavy burden on issuers. As a result, issuers might reasonably question the extent to which specific disclosure issues were relevant to their operations. And the utility of such extensive disclosures for investors—for whom the overall volume of mandatory disclosure is already overwhelming—is questionable.

Increasing the number of issues addressed, requiring issuers to provide hard sustainability data, and formulating line-item disclosure requirements would

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228. The mandatory nature of the SD&A requirement is critical for enhancing comparability and incentivizing the board to take its responsibility seriously. Cf. Eccles & Youmans, supra note 219, at 8 (proposing to mobilize investors to “ask company boards to issue The Statement”). For the reasons previously detailed, this Article takes the view that boards will be unwilling to provide meaningful sustainability information in the financial statements unless required to do so.


231. Cf. Jay Clayton, Chairman, U.S. Sec. & Exch. Comm’n, Remarks at the Economic Club of New York (July 12, 2017), https://www.sec.gov/news/speech/remarks economic club new york [https://perma.cc/T2EW YDPZ] (“There are circumstances in which the Commission’s reporting rules may require publicly traded companies to make disclosures that are burdensome to generate, but may not be material to the total mix of information available to investors.”).

232. See, e.g., id.; Paredes, supra note 169 (explaining how increasing the quantity of required disclosures reduces their value to investors).
potentially increase the informational content of sustainability disclosure. That increase would come, however, at a substantial cost both to issuers preparing the information and to investors relying on it. Instead, the SD&A proposal offers a balance between informational value and workability. In particular, the requirement that issuers determine which sustainability issues are most important and explain the basis for their determination might reduce the propensity of issuers to engage in duplicative or boilerplate disclosure that is likely to be uninformative.\footnote{But see Inv’r Responsibility Res. Ctr. Inst., The Corporate Risk Factor Disclosure Landscape 3 (2016), https://www.weinberg.udel.edu/IIRCiResearchDocuments/2016/01/FINAL EY Risk Disclosure Study.pdf (criticizing the narrative format of the risk factor disclosure requirement as “tend[ing] to represent a listing of generic risks, with little to help investors distinguish between the relative importance of each risk to the company”).}

In addition, a more comprehensive disclosure requirement would embroil issuers and regulators in difficult determinations of the appropriate scope of disclosure. It would force regulators to assess which sustainability issues warrant line-item disclosure requirements and to evaluate contested claims about the economic materiality of the required information. At the same time, it would exacerbate the risk of information overload by requiring issuers to provide extensive boilerplate disclosures rather than identifying the specific issues on which investors should focus.

The SD&A requirement creates an explicit, although limited, affirmative reporting obligation rather than simply leaving sustainability issues within the ambiguous materiality assessment applicable to an issuer’s overall MD&A and risk-factor disclosure. As the previous discussion demonstrates, it is a mistake to attempt to load sustainability disclosure into these general disclosure frameworks, and the SEC’s decision to do so has had the effect of unduly limiting both issuer consideration and disclosure of sustainability issues. At the same time, the mandate would have the practical effect of requiring issuers to examine and evaluate the impact of a broader range of sustainability issues than those covered by the three most significant mandated disclosures, because this evaluation would be necessary to determine which issues to disclose. Accordingly, the proposal’s effect on information reporting and board oversight would be substantially greater than requiring the company to consider just three disclosure items.

The SEC’s adoption of an SD&A requirement would reverse its prior position that distinguished sustainability issues from financial performance and encourage a norm in which issuers and their boards view sustainability considerations as part of their operational strategy. It would also encourage the evaluation of sustainability factors from a financial perspective.

Finally, a sustainability disclosure requirement is a way of managing expectations. Although a wide range of sustainability issues may be relevant to investors, formalizing the type and quantity of such disclosure that is required enhances predictability and investor confidence. Moreover, there is evidence that qualitative disclosure can provide substantial value to the market. For example, a recent
empirical study of the effect of the SEC’s 2005 mandate that firms include a “risk factor” section in their annual reports found that, contrary to the assertions of critics, “managers provide useful risk factor disclosures and investors incorporate this information into market values.”

B. SD&A REPORTING WILL PROMOTE COMPARABILITY

In addition, the SD&A proposal will promote the comparability of sustainability disclosure. Concededly, a disclosure obligation that admits to issuer-specific variation offers less comparability than a set of one-size-fits-all disclosure requirements. Because each issuer’s board determines the most significant sustainability issues independently, there is likely to be substantial variation among the issues addressed. As a result, the market may learn little by comparing, for instance, Volkswagen’s discussion of emissions with PepsiCo’s discussion of water conservation. At the same time, including sustainability disclosures within an issuer’s securities filings and subjecting those disclosures to SEC staff review and comment is likely to have a significant effect on comparability. The SEC staff currently reviews more than half of issuer 10–Ks filed each year. The SEC’s comments focus on not just the hard numbers in the 10–K but also the narrative components—the MD&A, CD&A, and the staff review subjects these disclosures to meaningful scrutiny.

In addition, although only a small percentage of those 10–Ks receive staff comment letters, a variety of industry participants review the letters and report to issuers on trends in SEC policies and concerns with respect to 10–K disclosure. These reports and the SEC reviews themselves lead to revisions and refinements of the narrative disclosures in the MD&A and CD&A. This review process is likely to generate common disclosure policies among issuers, particularly for those in the same or related industries. In particular, because the SEC staff

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236. Cf. id. at 6 7 (reporting that in 2016 and 2017, comments on the MD&A represented forty three percent of comments overall).
have access to all issuers’ disclosures, they will be able to identify situations in
which an issuer has not addressed a subject apparently important to its peer firms
or within its industry. The staff comment letters themselves will generate infor-
mation about an issuer’s evaluation of sustainability issues and the risks they
present. And issuers will learn from and be able to emulate the disclosures made
by their peers.

C. SD&A WILL IMPROVE SUSTAINABILITY DISCLOSURE RELIABILITY

Finally, SD&A will improve the reliability of sustainability disclosure over the
current system. Here is arguably where this Article’s proposal has the most to
offer. First, it is important to recognize the substantial methodological impact of
integrating sustainability disclosure into traditional securities reporting. Under
this proposal, sustainability disclosures will be prepared by disclosure attorneys
rather than marketing personnel and subjected to the same verification require-
ments as traditional financial disclosures.240

Furthermore, the SD&A proposal will lead to the board of directors being ac-
countable for sustainability disclosures in a way in that they are not in the current
system. The board’s role in overseeing and certifying the sustainability disclo-
sures will require that they set up reporting systems to receive information about
the issues addressed in the SD&A and their impact on operations. This reporting
process will both improve the reliability of the disclosures and provide the board
with a greater role in overseeing and understanding the issuer’s sustainability
practices. In addition, it will enable the board to incorporate sustainability consid-
erations into its analysis of strategic issues and operational risk management. By
contrast, in the current system, the degree of board oversight of sustainability
issues is unclear, and there is no direct link between the board or even high-level
executives and the choice of issues addressed in an issuer’s sustainability reports.

Even if some firms make high-quality sustainability disclosures under the vol-
untary system, a mandatory system is likely to improve the quality of sustainabil-
ity disclosure more broadly. In an analogous examination of the shift from
voluntary to mandatory disclosure of risk factors, Nelson and Pritchard found
that, although those firms facing significant litigation risk made substantial dis-
closures under a voluntary regime, mandatory disclosure improved the quality of
disclosure for other firms.241

The value of mandatory disclosure in ensuring quality disclosure depends crit-
ically on its enforcement; the risk of liability for noncompliance is what gives
teeth to the statutory disclosure provisions. Accordingly, if the goal of the SD&A

240. For a discussion of the preparation of traditional securities filings, see supra notes 235 39 and
accompanying text.

241. See generally Karen K. Nelson & A.C. Pritchard, Carrot or Stick? The Shift from Voluntary to
Mandatory Disclosure of Risk Factors, 13 J. EMPIRICAL LEGAL STUD. 266, 287 95 (2016) (empirically
analyzing the effect of mandated disclosure of risk factors).
is to improve the reliability of sustainability disclosures, it is necessary to give attention not just to the disclosure requirement itself but to the way it is enforced. The disclosure requirements of Regulation S–K do not themselves “create[] an independent private right of action.” Thus, an issuer’s failure to disclose a known trend in violation of Item 303 can only be enforced by the SEC. On the other hand, the federal courts have universally recognized a private right of action for federal securities fraud under Rule 10b-5. Accordingly, to the extent that an issuer makes an affirmatively false disclosure, that conduct is arguably actionable through private litigation. Courts have typically held both that Regulation S–K creates an affirmative obligation to disclose and that failure to comply with that requirement can provide the basis for a private securities fraud suit.

As a result, inclusion of SD&A within securities filings would subject issuers’ sustainability disclosures to SEC oversight and enforcement and clarify that fraudulent misrepresentations and omissions are actionable as securities fraud. Notably, the structure of the SD&A proposal increases the likely reliability of the disclosure by making the issuer’s affirmative disclosure requirement explicit. Issuers cannot greenwash their SD&As to avoid addressing issues likely to cause the market concern because, to the extent those issues are potentially among the three most significant, an issuer’s decision to omit them would constitute not just an omission but a fraudulent misrepresentation—a representation that the omitted issue is not among the three most significant.

243. Cf. id.
244. See, e.g., Jill E. Fisch, Cause for Concern: Causation and Federal Securities Fraud, 94 IOWA L. REV. 811, 815 (2009) (“The federal courts have recognized an implied private right of action under section 10(b) of the Securities Exchange Act and SEC Rule 10b-5, and have used federal common law to define the contours of the cause of action.” (footnotes omitted)).
245. See, e.g., Ind. Pub. Ret. Sys. v. SAIC, Inc., 818 F.3d 85, 94 n.7 (2d Cir. 2016) (“Item 303 imposes an ‘affirmative duty to disclose . . . [that] can serve as the basis for a securities fraud claim under Section 10(b).’” (quoting Stratte McClure v. Morgan Stanley, 776 F.3d 94, 101 (2d Cir. 2015) (alteration in original))).
246. There is ongoing debate about the extent to which all material omissions under Item 303 are actionable as securities fraud, centered on the question of whether the materiality standard for Item 303 is lower than that under Basic Inc. v. Levinson, see, e.g., Oran, 226 F.3d at 288 (“[A] violation of SK 303’s reporting requirements does not automatically give rise to a material omission under Rule 10b-5.”); see also Matthew C. Turk & Karen E. Woody, Leidos and the Roberts Court’s Improvident Securities Law Docket, 70 STAN. L. REV. ONLINE 89, 92 (2017), https://review.law.stanford.edu/wp-content/uploads/sites/3/2017/11/70 Stan. L. Rev. Online 89 Turk and Woody.pdf (“A consequence of the slightly lower materiality threshold for Item 303 is that it reduces the range of claims that private investors may bring based on firms’ incomplete disclosure of required MD&A information.”).
247. The Supreme Court was positioned to address this question when it granted certiorari in Leidos last year. Leidos, Inc. v. Ind. Pub. Ret. Sys., 137 S. Ct. 1395 (2017), but that case was settled before oral argument, Turk & Woody, supra, at 89.
248. The SD&A requirement is therefore more constraining than the risk factor disclosure requirement. Cf. Edward A. Morse, Vasant Raval & John R. Wingender, Jr., SEC Cybersecurity Guidelines: Insights into the Utility of Risk Factor Disclosures for Investors, 73 BUS. L. W. 20 21 (2017 2018) (finding that most issuers failed to disclose cybersecurity risks after the SEC’s release of new guidelines and that the market apparently viewed disclosing such risk as a negative signal).
This Article contemplates that implementation and enforcement of the SD&A would take place primarily through SEC oversight and, when appropriate, enforcement action. As described, because of the review process, the SEC staff would be well-positioned to identify critical weaknesses in an issuer’s MD&A—by allowing the staff to ask Exxon, for example, why it has failed to address climate change in its SD&A considering disclosures by peer firms like Occidental Petroleum and BP.

There are advantages to relying on the SEC to undertake most SD&A enforcement. First, the SEC may have greater expertise, enabling it to choose more accurately the cases in which enforcement is most consistent with the purposes of federal regulation. Second, public enforcement may be more efficient. Third, public enforcement is unlikely to be affected by the incentives that have the potential to produce abusive and excessive litigation, such as the high fees that plaintiffs’ attorneys can recover. Thus, for example, private litigants have rarely targeted individual defendants because of their lack of “deep pockets”; but the prospect of SEC enforcement is likely to focus corporate directors’ attention on ensuring the accuracy of their sustainability disclosures. Finally, the government can often send a message by bringing a limited number of high-profile cases, such as the SEC’s enforcement action against Caterpillar.

There are problems, however, with limiting enforcement to the SEC. A variety of courts, including the U.S. Supreme Court, commentators, and the SEC itself, have acknowledged the valuable role that private efforts play in supplementing

248. See, e.g., James J. Park, *Rules, Principles, and the Competition to Enforce the Securities Laws*, 100 CALIF. L. REV. 115, 124 (2012) (describing the argument that public enforcement may be premised on “the idea that the SEC is a better securities enforcer than private parties because of its expertise with respect to the securities laws”); see also Joseph A. Grundfest, *Disimplying Private Rights of Action Under the Federal Securities Laws: The Commission’s Authority*, 107 HARV. L. REV. 961, 1023–24 (1994) (suggesting, in light of these considerations, that the SEC eliminate private litigation as a means to enforce Rule 10b-5).


251. See Bradley Bondi, *A Brief History of SEC Enforcement Actions Against Directors*, LAW360 (Oct. 16, 2015, 1:59 PM), https://www.law360.com/articles/714967/a-brief-history-of-sec-enforcement-actions-against-directors-https://perma.cc/HG8577JD (“Though rare, enforcement actions against directors are a key component of the SEC’s targeting of misconduct by ‘gatekeepers’ . . .”). A relatively small number of SEC actions involving individual directors can be effective in increasing directors’ attention to their oversight responsibilities. See, e.g., SEC *Sharpens Focus on Disclosure of Executive Perks*, SHEPPARD MULLIN: CORP. & SEC. LAW BLOG (June 22, 2005), https://www.corporatesecuritieslawblog.com/2005/06/sec sharpens focus on disclosure of executive perks/ https://perma.cc/R2YZ PY3U (advising that one message from SEC’s enforcement actions against Tyson Foods and GE is that members of compensation committees face “personal liability for inaccurate or incomplete [compensation] disclosure[s]”).

public enforcement.\textsuperscript{253} The government may have limited resources available to address wrongdoing. In addition, SEC enforcement efforts are vulnerable to both political pressures and shifting administrative priorities.\textsuperscript{254} The risk of underenforcement is illustrated by the SEC’s limited track record with respect to MD&A disclosure; it has brought less than one hundred enforcement cases alleging violations since Regulation S–K’s adoption.\textsuperscript{255}

Accordingly, private enforcement is likely to serve as a valuable supplement to public enforcement. Although concerns have been raised about the potential for excessive or burdensome securities fraud litigation,\textsuperscript{256} that risk is likely to be especially limited under the SD&A proposal. There are three reasons for this. First, the SD&A requirement is explicit and limited—issuers are only required to disclose the three most significant sustainability issues. As a result, the requirement does not open the door to efforts to characterize additional sustainability issues as fraudulent omissions. Second, to succeed in a securities fraud lawsuit, private litigants must establish loss causation and damages, meaning that they must show that the issuer’s misrepresentation or omission had an economic impact on the value of their shares.\textsuperscript{257} As interpreted by the courts, the loss causation requirement requires affirmative proof that the fraud impacted stock price.\textsuperscript{258} Thus, only the most economically significant of sustainability disclosure-related failures could trigger private litigation.\textsuperscript{259} Third, to bring a securities fraud suit, a

\textsuperscript{253} See, e.g., Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 313 (2007) (“[P]rivate actions . . . are an essential supplement to criminal prosecutions and civil enforcement actions brought, respectively, by the Department of Justice and the Securities and Exchange Commission (SEC).”); James D. Cox et al., SEC Enforcement Heuristics: An Empirical Inquiry, 53 DUKE L.J. 737, 738 (2003) (“Since the inception of the federal securities laws, the government’s broad enforcement authority has been complemented by private causes of action.”); see also A.C. Pritchard, The SEC at 70: Time for Retirement?, 80 NOTRE DAME L. REV. 1073, 1085 (2005) (“With a few minor exceptions . . . the SEC has sided with the plaintiffs’ bar in the courts.”).

\textsuperscript{254} See Harvey L. Pitt & Karen L. Shapiro, Securities Regulation by Enforcement: A Look Ahead at the Next Decade, 7 YALE J. REG. 149, 279 (1990) (“[A]ny projection of future SEC enforcement trends is highly dependent upon the accuracy of prognostications about the prevailing political climate.”).

These concerns can be mitigated if public enforcement by multiple regulators is possible. See, e.g., John C. Coffee, Jr. & Hillary A. Sale, Redesigning the SEC: Does the Treasury Have a Better Idea?, 95 VA. L. REV. 707, 763 (2009) (“[S]tate Attorneys General have played an aggressive role in prosecuting securities fraud and have pushed the SEC to be more vigorous in its own enforcement efforts.”).

\textsuperscript{255} Leidos Amicus Brief, supra note 214, at 26–27.

\textsuperscript{256} This risk is potentially heightened with respect to sustainability disclosure due to uncertainty about issues such as the definition of sustainability, the determination of economic materiality, and the difficulty for even a well intentioned issuer in evaluating the economic impact of a known risk or trend. See, e.g., Langevoort, supra note 179, at 970–71 (discussing the difficulty of determining the extent of the duty to disclose disaster related risks).


\textsuperscript{258} See id. at 915 (terming this “‘ex post’ price distortion”).

\textsuperscript{259} Because the relative significance of sustainability issues can change over time, it may be worthwhile for the SEC to consider a safe harbor providing that, under appropriate circumstances, an issuer’s identification of a new sustainability issue does not subject it to liability for previously failing to discuss that issue. See, e.g., BARBARA NOVICK ET AL., BLACKROCK, EXPLORING ESG: A PRACTITIONER’S PERSPECTIVE 9 (2016), https://www.blackrock.com/corporate/literature/whitepaper/viewpoint exploring
private litigant must be a purchaser or seller of the securities.\textsuperscript{260} As a result, private litigation could not be used by environmental groups or other non-shareholder stakeholders to promote noneconomic objectives.

**CONCLUSION**

Despite the growing quantity of corporate sustainability disclosures, the existing disclosure system is fragmented, unreliable, and incomplete. In light of the worldwide debate over sustainability practices and investor claims regarding the necessity of quality sustainability disclosures for an adequate evaluation of issuer operations, it is necessary for the SEC to reverse its position that sustainability disclosure is not properly included within financial reporting. This Article proposes that the SEC adopt a principles-based disclosure approach through a narrative sustainability disclosure and analysis reporting requirement. It argues that the SD&A is a cost-justified approach that is well-suited to improve the availability of corporate sustainability information for investors, and that SD&A quality can be enhanced by a liability and enforcement structure with direct incentives for board involvement and oversight.

It is too early to determine the extent to which sustainable business practices impact economic performance, or the degree to which boards that engage with sustainability can exercise better risk management and monitoring. SD&A disclosure represents a valuable first step that would enable investors and researchers to weigh those questions with minimal burden on corporate issuers.

\textsuperscript{260} Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 735\textsuperscript{36} (1975).