THE UNIVERSITY OF KANSAS
School of Law

Gary Gensler, Chair
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

June 12, 2021

RE: Request for Public Input – Comments on Climate Change Disclosures

Dear Chair Gensler:

I am writing to support the Commission's efforts to improve how climate-related information is disclosed to investors. My comments here draw on more comprehensive recommendations presented in an article entitled *Modernizing ESG Disclosure*, which is forthcoming in the Illinois Law Review and is available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3845145.

The Article responds to many of the questions raised in the March 15 request for comment, as summarized below.

Question 1: How . . . to provide more consistent, comparable, and reliable information for investors while also providing greater clarity to registrants as to what is expected of them? Where and how should such disclosures be provided? Should any such disclosures be included in annual reports, other periodic filings, or otherwise be furnished?

- Part II of the Article addresses these questions. It recommends a multi-dimensional, tiered approach in order to promote comparability of ESG information within and across industry sectors. It also proposes how to better align Regulation S-K with emerging global ESG reporting standards
- For climate-related disclosure, the Commission should seek to integrate the disclosure framework developed by the Financial Stability Board's Task Force on Climate-related Financial Disclosure (TCFD) into the existing framework for periodic reporting. Part II of the Article suggests how this may done with reference to Regulation S-K.
- While the TCFD framework recommends disclosure of some information that may not be material for some firms, it may be material to diversified investors at the portfolio level; it could also shed light on corporate externalities that contribute to climate change. Therefore, requiring such disclosures may be justified in order to protect investors and promote market efficiency and stability, as this Article explains.
- This Article recommends that climate-related disclosures generally be included in annual reports, and that they be subject to appropriate disclosure controls and procedures.

Question 2: What information related to climate risks can be quantified and measured? How are markets currently using quantified information? Are there specific metrics on which all registrants should report (such as, for example, scopes 1, 2, and 3 greenhouse gas emissions, and greenhouse gas reduction goals)? What quantified and measured information or metrics should be disclosed because it may be material to an investment or voting decision? Should disclosures be tiered or scaled based on the size and/or type of registrant)? If so, how? Should disclosures be phased in over time? If so, how? How are markets evaluating and pricing externalities of contributions to climate change? Do climate change related impacts affect the cost of capital, and if so, how and in what ways? How have registrants or investors analyzed risks and costs associated with climate change? What are registrants doing internally to evaluate or project climate scenarios, and what information from or about such internal evaluations should be disclosed to investors to inform investment and voting decisions? How does the absence or presence of robust carbon markets impact firms' analysis of the risks and costs associated with climate change?

- This Article recommends that Scope 1 greenhouse gas (GHG) emissions reporting and disclosure of the parameters used in conducting scenario analysis should be required, but only on a comply-or-explain basis.
- This Article supports the recommendations of the Commodity Futures Trading Commission, which has urged regulators to establish a common "menu" of scenarios that can promote comparability of reported results but which has also encouraged tailored analysis.[1]
- This Article encourages the Commission to phase in disclosure requirements for smaller reporting companies (SRCs) and emerging growth companies (EGCs) over a three-year period, but not to exempt them from climate-related reporting. This approach advances the goals of improving ESG transparency from those companies whose climate- and ESG disclosures are less robust than for larger firms. As the Commission has previously noted, "the benefits of disclosure may be greater for smaller registrants because information symmetries between investors and managers of smaller companies are typically higher than for larger, more seasoned companies with a large following."[2]

Question 3: What are the advantages and disadvantages of permitting investors, registrants, and other industry participants to develop disclosure standards mutually agreed by them? Should those standards satisfy minimum disclosure requirements established by the Commission? How should such a system work? What minimum disclosure requirements should the Commission establish if it were to allow industry-led disclosure standards? What level of granularity should be used to define industries (e.g., two-digit SIC, four-digit SIC, etc.)?

- Part I of this Article outlines the deficiencies of the current voluntary reporting system, which include under-reporting of risk-related information, including with respect to climate risk, and fragmentation of voluntary reporting standards. As the Commission has already recognized, there is now an urgent need for

[1] CFTC, MANAGING CLIMATE RISK IN THE U.S. FINANCIAL SYSTEM 73-77, 82, 88 (2020), *available at* https://www.cftc.gov/

[2] Business and Financial Disclosure Required by Regulation S-K: Concept Release, 81 Fed. Reg. 23,916 (Apr. 22, 2016), at 23,897.

"consistent, comparable, and reliable" information on climate change and its impacts on registrants, investors, and the capital markets that can only be achieved through mandatory disclosure. Harmonization with international standards will also be impossible if the Commission continues to look to private ordering as a source of reporting standards.

- I have emphasized the high costs of this approach for investors, investors, the Commission, and reporting companies themselves in prior work.[3]

Question 4: What are the advantages and disadvantages of establishing different climate change reporting standards for different industries, such as the financial sector, oil and gas, transportation, etc.? How should any such industry-focused standards be developed and implemented?

- Establishing different reporting standards for different industries improves comparability and is likely to be more informative for investors. For this reason, this Article advocates a "tiered" approach, with core disclosures that should be made by all registrants and additional disclosures that would apply on an industry-specific basis.
- Industry-specific climate-related disclosure rules could be readily introduced by requiring companies to disclose climate-related risk based on the SASB standards, with reference to SASB's *Climate Risk Technical Bulletin* (2021 ed.).[4] This technical bulletin is aligned with the TCFD framework.

Question 5: What are the advantages and disadvantages of rules that incorporate or draw on existing frameworks, such as, for example, those developed by the Task Force on Climate-Related Financial Disclosures (TCFD), the Sustainability Accounting Standards Board (SASB), and the Climate Disclosure Standards Board (CDSB)? Are there any specific frameworks that the Commission should consider? If so, which frameworks and why?

- The Commission can more quickly and efficiently adopt climate-related disclosure reform, and at lower cost to registrants if it endorses or implements existing frameworks, namely the TCFD framework and the SASB standards.
- The SASB and CDSB standards are TCFD-aligned, and as this Article explains, these frameworks are already widely endorsed by other governments, by institutional investors, and by companies themselves.
- The Commission has previously leveraged private standards and frameworks because of these regulatory efficiencies and because of the costs savings to registrants who have already voluntarily adopted leading frameworks.
- Given the urgency of climate change and the rapid pace of adoption of the TCFD framework globally, it is difficult to conceive of any reason why the Commission would not endorse and build upon the TCFD framework. The Article outlines which of the TCFD recommended disclosures could be implemented directly within Regulation S-K and which would require new rulemaking; it also

[3] Virginia Harper Ho, *Nonfinancial Disclosure & The Costs of Private Ordering,* 55 AM. BUS. L. J. 407 (2018).

[4] https://www.sasb.org/knowledge-hub/climate-risk-technical-bulletin/.

recommends that certain TCFD recommendations be adopted prescriptively, while others be adopted on a comply-or-explain basis.

Question 7: What is the best approach for requiring climate-related disclosures? For example, should any such disclosures be incorporated into existing rules such as Regulation S-K or Regulation S-X, or should a new regulation devoted entirely to climate risks, opportunities, and impacts be promulgated? Should any such disclosures be filed with or furnished to the Commission?

- These questions are central to this Article. *See* Part II.
- In general, this article recommends that the Commission adopt core mandatory disclosures that apply to all registrants and supplement them with more flexible, principles-based approaches (including comply-or-explain) approaches for sector-specific information or where materiality is likely to vary widely across issuers.

Question 8: How, if at all, should registrants disclose their internal governance and oversight of climate-related issues? For example, what are the advantages and disadvantages of requiring disclosure concerning the connection between executive or employee compensation and climate change risks and impacts?

- This Article recommends a narrative discussion of the board's oversight of climate-related financial risk, in alignment with the TCFD.

Question 9: What are the advantages and disadvantages of developing a single set of global standards applicable to companies around the world, including registrants under the Commission's rules, versus multiple standard setters and standards? If there were to be a single standard setter and set of standards, which one should it be? What are the advantages and disadvantages of establishing a minimum global set of standards as a baseline that individual jurisdictions could build on versus a comprehensive set of standards? If there are multiple standard setters, how can standards be aligned to enhance comparability and reliability? What should be the interaction between any global standard and Commission requirements? If the Commission were to endorse or incorporate a global standard, what are the advantages and disadvantages of having mandatory compliance?

- This Article urges the Commission to align its disclosure framework with the TCFD framework, as it is already widely adopted by reporting companies and supported by investors.
- In general, this Article supports harmonization with a global baseline standard that the SEC and other jurisdictions can build on; any such standard will almost certainly incorporate the TCFD recommendations.

Question 10: How should disclosures under any such standards be enforced or assessed? For example, what are the advantages and disadvantages of making disclosures subject to audit or another form of assurance? If there is an audit or assurance process or requirement, what organization(s) should perform such tasks? What relationship should the Commission or other existing bodies have to such tasks? What assurance framework should the Commission consider requiring or permitting?

- The Commission should ultimately move toward a goal of requiring assurance for climate-related disclosure. However, this Article recommends that at present, the

Commission should adopt a comply-or-explain approach to assurance, given that assurance is not yet standard practice for voluntary sustainability reporting, much less for information reported in public filings. Under such a rule, companies would be required to disclose whether climate-related disclosures were audited or assured, to what extent, and by what organization.

Question 12: What are the advantages and disadvantages of a "comply or explain" framework for climate change that would permit registrants to either comply with, or if they do not comply, explain why they have not complied with the disclosure rules? How should this work? Should "comply or explain" apply to all climate change disclosures or just select ones, and why?

- Comply or explain approaches should not apply to all climate change disclosures because they do not sufficiently promote comparability.
- However, a comply-or-explain approach offers greater comparability than a rule that is subject to a materiality qualifier and explanations for any deviation may be more informative for investors. Comply-or-explain disclosure is best suited for disclosures
- Table 3 of this Article proposes specific climate-related disclosures and identifies which should be mandated under prescriptive rules and which should be adopted on a comply-or-explain basis.
- In general, this Article recommends a mixed approach (see Table 3 of the Article) that relies more heavily on prescriptive rules in the interest of improving comparability.
- I have previously addressed the advantages and disadvantages of a "comply or explain" framework in prior work and advocated its use.[5]

Question 13: How should the Commission craft rules that elicit meaningful discussion of the registrant's views on its climate-related risks and opportunities? What are the advantages and disadvantages of requiring disclosed metrics to be accompanied with a sustainability disclosure and analysis section similar to the current Management's Discussion and Analysis of Financial Condition and Results of Operations?

- These questions are discussed in Part II of this Article, which makes specific recommendations regarding how best to elicit such disclosure. It also explains where Regulation S-K should already elicit information covered by the TCFD recommendations and where new rules or amendments are needed.
- As explained in Part II(A) of this Article, a stand-alone sustainability disclosure and analysis section does not promote sufficient comparability and specificity. Even if used in conjunction with disclosed metrics, it may be duplicative of narrative discussion of climate-related trends or uncertainties that should already be discussed in the MD&A.

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[5] Virginia Harper Ho, *"Comply or Explain' and the Future of Nonfinancial Reporting,* 21 LEWIS & CLARK L. REV. 317 (2017).

Question 15: In addition to climate-related disclosure, the staff is evaluating a range of disclosure issues under the heading of environmental, social, and governance, or ESG, matters. Should climate-related requirements be one component of a broader ESG disclosure framework? How should the Commission craft climate-related disclosure requirements that would complement a broader ESG disclosure standard? How do climate-related disclosure issues relate to the broader spectrum of ESG disclosure issues?

- This Article urges the Commission to consider ESG disclosure reforms with respect to (i) climate-related financial and systemic risk; (ii) corporate governance; and (iii) human capital.
- However, because of the urgency of climate change and the need for harmonization with global standards, this Article supports a "climate-first" approach.

I hope that the recommendations and supporting research presented in this Article will aid the Commission in moving quickly to implement new climate-related disclosure rules building on the TCFD framework.

Sincerely,

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