



COMMONWEALTH
Climate and Law Initiative

Commonwealth Climate and Law Initiative
c/o MinterEllison

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U.S. Securities and Exchange Commission
100 F St., NE Washington
D.C. 20549-0609

June 13, 2021

Dear U.S. Securities and Exchange Commission,

Re: Commonwealth Climate and Law Initiative response to SEC Request for Comment on Climate Disclosure

The Commonwealth Climate and Law Initiative (CCLI) welcomes the opportunity to provide a submission to the U.S. Securities and Exchange Commission (SEC) in response to the SEC's 15 March 2021 request for comment on climate disclosure.

Should you wish for any of our global experts to be available to discuss, we will endeavour to make the necessary arrangements.

1. Introduction

Climate change poses serious risks to the U.S. real economy, in three main categories: physical risk, transitional risk (arising from the transition to a low-carbon economy), and liability risks (arising from potential litigation). Due to their wide-ranging nature, climate change risks lead to systemic risks to the U.S. business and financial markets; as a result, investor demands for disclosures on climate change and other ESG information are increasing, with large asset managers and other financial institutions now calling for such disclosures. The U.S. Government has shown strong leadership on the systemic risks posed by climate change, most recently with the Executive Order on Climate-Related Financial Risk issued on 20 May 2021. The SEC should now take steps to ensure that companies' climate risks are disclosed in a manner that is useful to investors, and that supports efficiency, competitiveness, and capital market formation in the U.S. capital markets.

While current regulations oblige companies to disclose climate change risks when these comprise material information in connection with disclosures required under law, current disclosures may not clearly reflect the risks posed by climate change to a company's business. Investors have expressed concerns about the usefulness, comparability, and consistent presentation of disclosures being made in SEC filings.

Improving guidance on required climate change disclosures or adopting a mandatory set of rules for these (as has been done in a number of other jurisdictions) would aid clarity, comparability of information, and ensure that investors are aware of the risks they take when investing their money or voting their shares.

About the CCLI

The CCLI is a legal research and stakeholder engagement initiative founded by Oxford University Smith School of Enterprise and the Environment, ClientEarth, and Accounting for Sustainability (A4S). The CCLI examines the legal basis for directors and trustees to manage and report on climate change-related risk and climate mitigation. Our research is at the forefront of the intersection of climate and biodiversity risks under existing company and securities laws.

Founded to focus on four Commonwealth countries – Australia, Canada, South Africa, and the United Kingdom – the CCLI has expanded its remit to the United States, Singapore, India, Hong Kong, Japan, and Malaysia. The CCLI leverages the inter-disciplinary and cross-jurisdictional perspectives provided by its global experts from academia and the legal, accountancy, business, and scientific communities. Our publications include:

- Janis Sarra, *Audit Committees and Effective Climate Governance. A Guide for Boards of Directors* (December 2020)
- Sarah Barker, Ellie Mulholland, and Temitope Onifade, *The emergence of foreseeable biodiversity-related liability risks for financial institutions: A gathering storm?* (August 2020)
- Alexia Staker, Alice Garton, Sarah Barker, *Concerns misplaced: will compliance with the TCFD recommendations really expose companies and directors to liability risk?* (September 2017)

2. Climate Risk in the US

There is an overwhelming scientific consensus that human activities, such as fossil fuel combustion for transportation, manufacturing, and energy production, land clearing, and modern agricultural practices, contribute significant volumes of greenhouse gases into the atmosphere. This has, in turn, caused observed warming over and above natural variability. According to the UN Intergovernmental Panel on Climate Change (IPCC), emissions-intensive human activities have already caused approximately 1°C (1.8°F) of global warming above average pre-industrial temperatures.¹

These changes create risks to physical infrastructure, human health, ecosystems, water supply, and resource security, with financial consequences for productivity, supply chain integrity, and the costs and availability of finance and insurance.

A. Physical Risks

Climate change leads to more frequent, and more extreme, weather-related events, such as heat waves, rainfall variability and extreme precipitation events, fires, drought, coastal inundation and inland floods, as well as gradual onset changes, such as rising sea levels due to thermal expansion of the oceans and glacial melt, ocean acidification, and sustained higher temperatures. These impacts give rise to commercial issues and have financial implications. These issues include business disruption such as plant and infrastructure outages, upstream changes in the availability and price of key inputs, downstream distribution interruption, population dislocation, reduced workforce productivity, changes in the cost or availability of insurance, energy price volatility, increases in adaptation capex, and increased risk of customer default. Exposures to physical risks compound and multiply between impacts and across supply and distribution chains.

¹ IPCC, IPCC Special Report: Global Warming of 1.5°C (Summary For Policymakers) (2018).

The impacts of a changing climate already are having profound financial effects on the U.S. economy. In 2020, unprecedented West Coast wildfires linked to climate change² caused billions of dollars of damage to homes, businesses and supply chains.³ There were 11 “severe storm” events made more intense by climate change,⁴ each causing over a billion dollars of damage.⁵ Sea level rise is accelerating,⁶ posing a threat to a large proportion of the population and economic activity in the U.S., especially along the Atlantic coast.⁷ A recent report by McKinsey set forth the financial risks of rising sea levels and more severe storms to the public and private stakeholders in the Florida residential real estate markets, including homeowners, private insurance carriers, municipal governments, through to reinsurance carriers and bank balance sheets.⁸

As this warming continues, the acute and gradual onset changes will increase, in turn increasing the physical risks generally. The specific physical risks associated with climate change vary according to location, circumstance and future warming pathway. The risks for natural and human systems at a macro level, and financial risks to business assets and operations at a micro level, depend on the magnitude and rate of warming, geographic location, level of development and vulnerability, and implementation of adequate adaptation activities.⁹

On current rates, the global average temperature is expected to reach +1.5°C (2.7°F) around 2040, although this could occur as early as 2024.¹⁰ The physical risks of a “1.5°C world” are higher than today, and in turn, a “2°C world” higher still. On a “business as usual” emissions trajectory, scientists warn of warming in excess of 4°C (7.2°F) by 2100.¹¹ The physical risks will be extreme, and insurers have described a “4°C world” as “uninsurable.”¹²

B. Economic Transition Risks

Research by diverse analysts, from the IPCC to McKinsey, shows that rapid economic transition scenarios which limit the most catastrophic climate impacts require deep emissions reductions across industry, transport, power, buildings, and agriculture.¹³ This essential economic transition creates financial risks from:

² Stanford Earth, *The science behind the West Coast fires* (Sept. 29, 2020); Susanne Rust and Tony Barboza, *How climate change is fuelling record-breaking California wildfires, heat and smog*, Los Angeles Times (13 September 2020).

³ Earth Observatory, *Historic Fires Devastate the Pacific Coast*, NASA (Sept 9, 2020) <<https://earthobservatory.nasa.gov/images/147277/historic-fires-devastate-the-us-pacific-coast>>.

⁴ Chelsea Harvey, *E&E News on Climate: Climate change may cause more storms to rapidly intensify*, Scientific American (9 October 2020).

⁵ National Center for Environmental Information, ‘Billion-Dollar Weather and Climate Disasters: Events,’ National Oceanic and Atmospheric Administration (NOAA) <<https://www.ncdc.noaa.gov/billions/events/US/2020>>.

⁶ R. W.V Horton et al., *Sea Level Rise*, in Climate Science Special Report: Fourth National Climate Assessment, Vol I, D.J. Wuebbles, D.J., D.W. et al. (eds) (US Global Change Research Program, 2017) 333-363.

⁷ Environment Protection Agency, *Climate Change Indicators in The United States* (2016) 34-5.

⁸ McKinsey Global Institute, *Climate Risk and Response: Physical Hazards and Socioeconomic Impacts* (2020), 20.

⁹ IPCC, *supra* note 1 [A.3].

¹⁰ IPCC, *Global Warming of 1.5°C*, FAQ [1.2] 80-81. The uncertainty in the range is due to the difficulty of accounting for solar and volcanic activity over the historical period until 2000, and the estimation of the annual growth in temperature (IPCC, *Global Warming of 1.5°C*, Technical Summary, at 31).

¹¹ IPCC, *Climate Change 2014 Synthesis Report, Summary for Policy Makers*, 10.

¹² James Fearnough, *Climate change on track to make the world ‘uninsurable’*, The Australian Financial Review (Nov. 15, 2018).

¹³ McKinsey & Co, *Climate Math: What A 1.5-Degree Pathway Would Take* (April 2020).

- policy or regulatory responses that attempt to either constrain emissions-intensive activities (e.g. carbon pricing mechanisms), or to promote adaptation to climate impacts;
- technology trends, such as advances in renewable energy generation, electric vehicles, battery storage, energy efficiency and carbon capture, storage and use;
- market forces via impacts on supply and demand dynamics in financial markets and the real economy; and
- reputational, strategic or competitiveness risks associated with evolving stakeholder perceptions and expectations.

These transition risks lead to compliance risks to companies, with the likely introduction of new regulatory requirements such as carbon pricing, methane pollution limits, or climate risk disclosure. They also fall within the broader suite of business risks affecting balance sheet values through changes in revenue or costs. These economic transition risks can transmit between financial actors as systemic risks to the financial sector. For example, a report by Ceres found that over half of syndicated lending of major U.S. banks is exposed to systematic economic transition risks because their clients across a wide range of sectors are inadequately prepared for the net zero transition in line with the Paris Agreement. In turn, banks' leverage and connectivity could lead to balance-sheet contagion or "fire sales" of financial assets similar to those which occurred in the financial crisis.¹⁴

i. Policy and regulatory responses

The global community agreed to the required economic transition in the 2015 Paris Agreement, which sets out two primary goals:

- to limit the "increase in the global average temperature to well below 2°C [3.6°F] above pre-industrial levels" and to pursue "efforts to limit the temperature increase to 1.5°C [2.7°F] above pre-industrial levels", to be achieved through countries' nationally determined contributions (NDCs); and
- to achieve net zero global emissions in the second half of the century.¹⁵

Limiting global warming to 1.5°C (2.7°F) is still technically feasible, but requires "rapid, far-reaching and unprecedented" changes in all aspects of society and the economy, according to the IPCC.¹⁶ To date, global pledges are not sufficient to meet these goals. Under its current NDC, the U.S. committed to reduce its emissions by 26-28% below 2005 levels by 2025, and 50-52% below 2005 levels by 2030.¹⁷

President Biden has moved quickly to emphasize climate change as part of both U.S. foreign and domestic policy. His climate change Executive Order on 27 January 2021 established a process to embed climate change in every executive agency of the federal government, including establishing an inter-agency coordinating process and appointing both a foreign and domestic policy lead in newly-established positions within the White House.¹⁸ Secretary

¹⁴ Ceres, *Financing A Net-Zero Economy: Measuring and Addressing Climate Risks for Banks* (October 2020).

¹⁵ Paris Agreement to the United Nations Framework Convention on Climate Change, Dec. 12, 2015, T.I.A.S. No. 16-1104.

¹⁶ IPCC, *supra* note 1.

¹⁷ United States NDC (2021)
<<https://www4.unfccc.int/sites/ndcstaging/PublishedDocuments/United%20States%20of%20America%20First/United%20States%20NDC%20April%2021%202021%20Final.pdf>>.

¹⁸ The White House, Executive Order on Tackling the Climate Crisis at Home and Abroad, (27 January 2021), <<https://www.whitehouse.gov/briefing-room/presidential-actions/2021/01/27/executive-order-on-tackling-the-climate-crisis-at-home-and-abroad>>. Former Obama Administration Secretary of State John Kerry has been appointed as Special Presidential Envoy for Climate with a foreign-policy remit, and former Administrator

of the Treasury Janet Yellen has stated that climate change will be a priority, creating a hub within the Treasury that will focus on financial system related risk posed by climate change, and tax policy incentives to effect change.¹⁹

These actions are consistent with conclusions by the Federal Reserve Bank Board of Governors, which for the first time identified climate change as a risk to the American financial system in its Financial Stability Report of November 2020:²⁰

“[C]limate change, which increases the likelihood of dislocations and disruptions in the economy, is likely to increase financial shocks and financial system vulnerabilities that could further amplify these shocks. ... Federal Reserve supervisors expect banks to have systems in place that appropriately identify, measure, control, and monitor all of their material risks, which for many banks are likely to extend to climate risks.”

Demonstrating commitment to this approach, President Biden has recently signed an Executive Order on Climate-Related Financial Risk, which requires the National Climate Advisor, Gina McCarthy, to create a comprehensive government-wide climate-risk strategy to identify and disclose climate-related financial risk to government programs, assets, and liabilities, and sets out a policy of “advanc[ing] consistent, clear, intelligible, comparable, and accurate disclosure of climate-related financial risk”.²¹

Various governments in Europe and Asia have flagged their preparedness to use trade mechanisms to “incentivize” progress on emissions reduction by laggard countries.²² Once a potential target for these trade mechanisms, the U.S. may join these countries as the Biden Administration has expressed support for such a “carbon adjustment fee”.²³ Carbon pricing now covers over 20% of the world's emissions.²⁴ The report of the Climate-Related Market Risk Subcommittee of the Commodity Futures Trading Commission (CFTC) calls for the introduction of a carbon price consistent with the Paris Agreement.²⁵

Developments in climate policy and sustainable finance in other major jurisdictions have far-reaching consequences for global markets, including the US.²⁶ An increasing number of net zero carbon or net zero emissions targets are being introduced or actively considered by

(head) of the Environmental Protection Agency in the Obama administration, Gina McCarthy, has been appointed as the National Climate Advisor to the President.

¹⁹ Reuters, Yellen says would appoint senior climate official at Treasury (20 January 2021), <<https://www.reuters.com/article/us-usa-biden-yellen-climate-idUSKBN29O2B3>>.

²⁰ United States Federal Reserve Bank Board of Governors, Financial Stability Report 59 (2020).

²¹ The White House, Executive Order on Climate-Related Financial Risk, (20 May 2021), <<https://www.whitehouse.gov/briefing-room/presidential-actions/2021/05/20/executive-order-on-climate-related-financial-risk/>>.

²² Mehreen Khan and Gideon Rachman, *Davos 2020: Ursula von der Leyen warns China to price carbon or face tax*, Financial Times (22 January 2020).

²³ Biden for President, *The Biden Plan to Ensure the Future is “made in All of America” By All of America’s Workers* <<https://joebiden.com/made-in-america%20/>>.

²⁴ World Bank, *Carbon Pricing Dashboard* <<https://carbonpricingdashboard.worldbank.org/>>.

²⁵ Market Risk Advisory Committee of the US Commodity Futures Trading Commission, Managing Climate Risk in the US Financial System, Report Of The Climate-Related Market Risk Subcommittee (2020), Recommendation 1. While the average carbon price is only \$2 per tonne of CO₂e, estimates of a “Paris-aligned” carbon price that would be likely to limit warming to “well below 2°C” range from \$40 to \$100 per tonne of CO₂e and increasing over time: at 5.

²⁶ For example, the EU continues to progress key components of its Sustainable Finance Action Plan, including new sustainability-related disclosure requirements, which will impact US financial institutions that participate in European financial markets and increase disclosure expectations from European investors of their US investee companies: European Commission, Action Plan: Financing Sustainable Growth (2018), <<https://ec.europa.eu/transparency/regdoc/rep/1/2018/EN/COM-2018-97-F1-EN-MAIN-PART-1.PDF>>; see also <https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance_en>; see especially the Taxonomy and Sustainable Finance Disclosure Regulation.

governments at national and sub-national levels: as of the end of 2020, 127 countries, responsible for almost two-thirds of global emissions are considering or have adopted net zero targets, including the UK, EU, Canada, Japan, South Korea and China.²⁷ In the US, there are subnational net zero targets in 23 states (including California and New York), as well as in the District of Columbia.²⁸ In a recent report, the International Energy Agency set out a pathway to attaining net zero by 2050, which includes an immediate cessation of developing new oil, gas and coal fields, no further sale of automobiles using internal combustion engines after 2035, and the transition of over 90% of heavy industry to low-emission processes by 2050.²⁹

There is growing consensus among institutional investors that climate change affects their calculations of investment risks and returns. Analysis by investment consultant Mercer suggests that any investor holding a business-as-usual, diversified equity portfolio that is not sustainability-themed, and with significant oil, gas, and coal holdings, risks “undue loss” or, indeed, catastrophic loss in some asset classes, starting to eventuate over the next decade.³⁰ The UN-supported investor network the PRI has warned its members to prepare for near-term portfolio disruption based on the PRI’s forecast that governments will strongly accelerate climate policies within the next five years.³¹

ii. **Technology trends**

Renewable energy technologies are increasingly economically competitive with fossil fuel generation.³² In the U.S., coal power plants are rapidly being retired, while renewable energy outpaced coal-fired power generation for the first time ever in 2019.³³ While primarily driven by declining costs of renewable energy generation and battery storage, renewable energy technologies are increasingly supported in economic policy, particularly for Covid-19 recovery plans. President Biden has set out a \$2 trillion economic recovery plan focused on clean energy investments and the creation of green jobs as part of his “Plan for Clean Energy and Environmental Justice”.³⁴ In the automotive sector, California has committed to phasing out the sale of new internal combustion engine vehicles by 2035. It joins a growing number of national and sub-national governments, and automotive manufacturers, setting targets to phase out such sales in passenger and light-duty vehicles – from the UK to Japan, from General Motors to Volvo.³⁵ A recent Carnegie Mellon University study concluded that electric vehicles may reach price parity with cars with internal combustion engines in the U.S. on or before 2025.³⁶

iii. **Market forces**

²⁷ Climate Action Tracker, *Temperatures* <<https://climateactiontracker.org/global/temperatures/>>.

²⁸ Gernot Wagner, *Don’t discount states*, Bloomberg Green (Nov 20, 2020).

²⁹ International Energy Agency, *Net Zero by 2050: A Roadmap for the Global Energy Sector* (18 April 2021).

³⁰ Mercer, *Investing in a Time of Climate Change — The Sequel* (2019).

³¹ PRI, *What is the Inevitable Policy Response: Policy Forecasts* <<https://www.unpri.org/inevitable-policy-response/the-inevitable-policy-response-policy-forecasts/4849.article>>.

³² Carbon Tracker, *The Trillion Dollar Energy Windfall: Analyst Note* (5 September 2019); Globally, more than 50% of new build renewables undercut the cheapest existing coal-fired power plants: International Renewable Energy Agency, *Renewable Power Generation Costs in 2019* (June 2020).

³³ Energy & Climate Intelligence Unit, *The Sum of its Parts* (22 October 2020) 8.

³⁴ Climate Action Tracker, *USA* <<https://climateactiontracker.org/countries/usa/current-policy-projections/>>.

³⁵ Sandra Wappelhorst and Hongyang Cui, *Growing momentum: Global overview of government targets for phasing out sales of new internal combustion engine vehicles*, The International Council on Clean Transportation (Nov. 11, 2020, 14:01).

³⁶ Venkat Viswanathan, Alexander Bills and Shashank Sripad, *The road to electric vehicles with lower sticker prices than gas cars – battery costs explained*, The Conversation (27 July 2020).

Changing supply and demand dynamics in the economic transition can lead to “stranded assets”. These assets cannot be profitably exploited, or used for the full expected period of time during which a physical asset such as a coal-fired power plant was expected to be utilised, which negatively affects current valuations of these assets. These risks are particularly acute in industries with high emissions intensities or long-lived physical plant and infrastructure. Stranded asset risks have been the subject of significant recent investor concern in the energy and resources sectors, in particular coal, oil, gas, and conventional electric utilities. Yet stranded asset risks cut across many sectors of the economy, including automotive and airline industries, as well as financial market participants who have debt or equity exposures to companies in those sectors or their assets, such as banks, insurance companies, asset owners and asset managers.³⁷ The past year has seen a spate of asset revaluations by carbon majors with \$80 billion in write downs across the industry.³⁸

C. Litigation Risks

Litigation risks arise from private or regulatory legal actions relating to the physical or economic transition risks associated with climate change. Such claims may arise in a number of circumstances, including: a failure to mitigate (i.e., reduce) emissions; a failure to adapt to the foreseeable impacts associated with climate change; a failure to disclose the risks associated with climate change where an obligation exists to do so (e.g., under corporate reporting and securities laws); and a failure to comply with climate-specific regulatory obligations such as emissions intensity standards.³⁹

Climate litigation against companies and their directors is on the rise, with 1,200 climate cases filed by regulators, bondholders, shareholders and municipalities across the U.S. as of late 2020.⁴⁰ Carbon majors have faced a surge in climate lawsuits in recent years,⁴¹ on the basis of state law violations, including public and private nuisance, trespass, product liability and consumer protection.⁴²

³⁷ Climate Analytics, *Global and Regional Coal Phase-Out Requirements of the Paris Agreement: Insights From the IPCC Special Report on 1.5°C* (2019)

<https://climateanalytics.org/media/report_coal_phase_out_2019.pdf>; Carbon Tracker, 2 Degrees Of Separation: Transition Risk For Oil And Gas in a Low Carbon World (Sept. 13, 2019); Ben Caldecott et al., Stranded Assets And Thermal Coal: An Analysis Of Environment-Related Risk Exposure (January 2016).

³⁸ Ron Bousso, *Oil majors wipe \$80 billion off books as epidemic, energy transition bite*, Reuters (2 December 2020). This trend is partly attributable to the Covid-19 pandemic but assumptions around increasing carbon prices and constrained demand in the energy transition were also key factors for Shell's up to \$22 billion impairment and BP's up \$17.5 billion reduction. Both companies said these accounting decisions were a response to not only the recession, but also to global efforts to tackle climate change. By contrast, ExxonMobil's record \$17-20 billion write down in the fourth-quarter of 2020 was based on pre-pandemic forward price assumptions and made no reference to climate change. ExxonMobil, *ExxonMobil to prioritize capital investments on high-value assets* (30 November 2020).

³⁹ Bank of England Prudential Regulation Authority, *The Impact Of Climate Change on the UK Insurance Sector* (2015).

⁴⁰ UNEP and Sabin Center for Climate Change Law, *Global Climate Litigation Report: 2020 Status Review* (2020).

⁴¹ Climate Case Chart, *US Climate Change Litigation – Common Law Claims* <<http://climatecasechart.com/case-category/common-law-claims/>>.

⁴² Lisa Benjamin, *The Road to Paris Runs Through Delaware: Climate Litigation and Directors' Duties*, Utah L. Rev. (2020) 25-32; Karen Savage, *Climate Suits Grew in 2020, Could Clear Huge Hurdle in 2021*, Climate Docket (Dec. 30, 2020); David Hasemyer, *Fossil Fuels on Trial: Where the Major Climate Change Lawsuits Stand Today*, Inside Climate News (17 January 2020); David Hasemyer, *Five States Having Filed Climate Change Lawsuits, Seeking Damages from Big Oil and Gas*, Inside Climate News (15 September 2020).

3. The Demand for New Climate Change Disclosures

As the SEC has noted, at present, disclosures relating to climate change (and potentially wider ESG issues) will be required when such issues are material information in connection with required statements, such as those made under Regulation S-K and Regulation S-X.⁴³ The SEC has published guidance on which required statements may necessitate disclosure of material climate change information to prevent such statements from being misleading, in line with the requirements of Securities Act Rule 408 and Exchange Act Rule 12b-20.⁴⁴ As Commissioner Allison Herren Lee has recently emphasised, current regulations do not require a company to disclose climate change information solely because the information is material to its business – there must be a duty to disclose the information separate from its materiality.⁴⁵ Such a duty may arise based on statements which the company has made that would be misleading without further disclosure, but there is no absolute duty of disclosure based on the materiality of information within the company.⁴⁶ Thus, as the physical, technological, regulatory, and litigation risks discussed above accelerate, investors are increasingly calling for clearer, more consistent, and more easily comparable disclosure by companies with which to evaluate the risks and future prospects of companies in their portfolios. The disclosure is also necessary to inform shareholders' voting, giving insight into how proactive the board is being in addressing climate change risks in its strategy, and oversight of legal and business risk: thus, how well is the board fulfilling its fiduciary duties?

This section examines: the adoption of mandatory climate change risk disclosures by other regulators and investor reception of these disclosures; the demand for climate change and other ESG disclosures by investors; and the potential issues of disclosures currently made under the existing voluntary and mandatory frameworks. It then addresses the possibility of increased liability for companies and directors as a result of increased climate change disclosures.

Question 5

Question 9

A. Adoption of Climate Change Disclosure Standards by other Regulators

Globally, there is increasing recognition that climate-related risks are relevant to international accounting standards and to financial disclosures, and this is leading to increased adoption of both voluntary and mandatory standards for companies to disclose climate change-related information.⁴⁷

⁴³ Securities and Exchange Commission, Securities Act Release No. 34-9106 (Commission Guidance Regarding Disclosure Related to Climate Change) (8 February 2010). Registrants may also be required by the SEC guidance pertaining to MD&A disclosure to discuss material trends, events, or uncertainties arising from either climate risk or other ESG factors.

⁴⁴ Securities Act Rule 408 and Exchange Act Rule 12b-20 requires the disclosure of “such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading.”

⁴⁵ SEC Commissioner Allison Herren Lee, Living in a Material World: Myths and Misconceptions about “Materiality” (24 May 2021).

⁴⁶ See *Basic v. Levinson*, 485 U.S. 224, xxx fn. 17 (1988) (“Silence, absent a duty to disclose, is not misleading.”)

⁴⁷ SEC Commissioner Allison Herren Lee, Playing the Long Game: The Intersection of Climate Change Risk and Financial Regulation, Keynote Address at PLI’s 52nd Annual Institute on Securities Regulation (5 November 2020); AASB and AUASB, Climate-Related and Other Emerging Risks Disclosures: Assessing Financial Statement Materiality Using AASB Practice Statement 2 (April 2019); Nick Anderson, IFRS Standards and climate-related disclosures (28 November 2019); IFRS, Educational material: The effects of climate-related matters on financial statements prepared applying IFRS Standards (20 November 2020). The

The International Financial Reporting Standards (IFRS) Foundation has confirmed that the IFRS already require disclosure of climate-related risks in financial accounting and disclosure.⁴⁸ It is conducting a consultation on its potential role in developing sustainability reporting standards, responding to investor demand and global consolidation efforts to align sustainability standards being developed amongst private standard setters.⁴⁹

The Basel Committee on Banking Supervision, which sets the global standards for capital adequacy, has recognized that climate change potentially impacts the safety and soundness of individual financial institutions and has broader financial stability implications for the banking system.⁵⁰ It has announced plans to make recommendations as to how climate risks should be factored into the prudential capital framework in 2021.⁵¹

Economic transition risks include shifts in stakeholder perceptions, including the approaches of central banks, prudential, and securities regulators.⁵² First mover jurisdictions such as the UK are mandating climate-risk disclosures in line with the Task Force on Climate-Related Financial Disclosure (TCFD) recommendations by 2025 at the latest.⁵³ Established by the Financial Stability Board in December 2015 and chaired by Michael Bloomberg with special assistance from former SEC Chair Mary Schapiro, the TCFD seeks disclosure of companies' governance, strategy, risk management, targets, and metrics for evaluating climate risks and opportunities.⁵⁴ The TCFD's 2020 Status Report states that its framework has been endorsed by "over 1,500 organizations globally, including over 1,340 companies with a market capitalization of \$12.6 trillion and financial institutions responsible for assets of \$150 trillion."⁵⁵

Investor responses to the introduction of the TCFD framework have been positive, but TCFD disclosures are viewed as a baseline, with additional disclosures required. For example, the UK Financial Reporting Council (FRC), a government body which regulates auditors, accountants and actuaries, and which is responsible for UK's Corporate Governance and Stewardship Codes, held discussions with over 20 investors and investor groups and reported that investors supported the TCFD, but expected to see additional disclosures

IFRS Foundation is currently consulting on a proposal to establish a Sustainability Standards Board, to sit alongside the International Accounting Standards Board, which would be tasked with developing international standards for sustainability reporting. If established, it is proposed that climate-related reporting standards would be first to be developed: IFRS, Consultation Paper on Sustainability Reporting (Sept. 2020).

⁴⁸ IFRS, Consultation Paper on Sustainability Reporting (Sept. 2020).

⁴⁹ *Id.*

⁵⁰ Basel Committee on Banking Supervision, 'The Basel Committee's initiatives on climate-related financial risks' (Oct. 14, 2020), <<https://www.bis.org/speeches/sp201014.htm>>.

⁵¹ *Id.*

⁵² See, e.g., U.S. Federal Reserve Board Governor Lael Brainard, Why Climate Change Matters for Monetary Policy and Financial Stability, Address at 'The Economics of Climate Change' Conference, California (Nov. 8, 2019) <<https://www.federalreserve.gov/newsevents/speech/brainard20191108a.htm>>. See also Market Risk Advisory Committee of the US Commodity Futures Trading Commission, *supra* note 24, at vi: "The United States already participates in the Basel Committee on Banking Supervision's climate task force, the International Organization of Securities Commissions (IOSCO) sustainable finance network, and relevant committees within the Financial Stability Board (FSB) to study climate-related financial risks." The U.S. National Association of Insurance Commissioners, the California Department of Insurance, the New York Department of Financial Services, and the Washington State Office of the Insurance Commissioner are members of the international Sustainable Insurance Forum (SIF), a global network of 31 insurance supervisors and regulators.

⁵³ HM Treasury, UK Joint Regulator and Government TCFD Taskforce: Interim Report and Roadmap (Nov. 9, 2020).

⁵⁴ See TCFD <<https://www.fsb-tcfd.org/>>.

⁵⁵ TCFD, 2020 Status Report (2020).

regarding the financial implications of climate change.⁵⁶ Similarly, during 2020, the UK Financial Conduct Authority (which regulates the UK financial markets) (FCA), held a consultation on the introduction of a new rule obliging certain companies to disclose information in line with the TCFD. The FCA received responses from listed companies, investors, and asset managers; the respondents almost unanimously agreed that reporting in line with TCFD should be introduced, initially on a “comply or explain” basis before being made fully mandatory.⁵⁷ Notably, the majority of respondents stated that governance and risk management disclosures required by the TCFD should be made regardless of the outcome of a materiality assessment.⁵⁸

As requirements to disclose climate change risks become mandatory in other jurisdictions, large multinationals may find themselves bound by multiple disclosure requirements. The NYSE lists 156 European-incorporated companies, worth a total of \$4.4 trillion;⁵⁹ it would benefit these companies and international investors if consistent, or at least comparable, disclosure requirements regarding climate change risk were adopted between the SEC and overseas regulators. Equally, U.S. companies which are listed on UK and European exchanges will in some cases already be required to disclose in accordance with the TCFD recommendations, and this number is likely to rise as these disclosures become mandatory for an increasing number of companies in these jurisdictions.

Question 1

Question 2

B. Investor Demand for Climate Change Disclosures

There is growing consensus among institutional investors that climate change affects their calculations of investment risks and returns, and demand for disclosures on climate change and other ESG issues is increasing as a result.

Investors are leading calls for climate change and ESG disclosures. The Climate Action 100+ is a global coalition of investors with \$52 trillion in assets under management (AUM) committed to driving corporate action on climate change.⁶⁰ One of its members, BlackRock, has stated that it expects companies to disclose climate risks in accordance with the TCFD and SASB (Sustainability Accounting Standards Board) frameworks, and has announced it will divest its active funds from companies that derive more than 25% of revenues from thermal coal production.⁶¹ BlackRock’s CEO, Larry Fink, stated in his 2021 letter to the CEOs of its investee companies that there is no company whose business model will not be profoundly affected by the transition to net zero emissions, and that net zero demands a

⁵⁶ Financial Reporting Council, *FRC Climate Thematic Investors – What do investors want to see?* (November 2020).

⁵⁷ Financial Conduct Authority, Policy Statement PS20/17: Proposals to enhance climate-related disclosures by listed issuers and clarification of existing disclosure obligations (December 2020).

⁵⁸ *Id.*, 22.

⁵⁹ NYSE. International Listings | International Companies at NYSE. (2021).
<<https://www.nyse.com/listings/international-listings#>>.

⁶⁰ Climate Action 100+ <<http://www.climateaction100.org/>> (as of January 2021).

⁶¹ BlackRock CEO Larry Fink’s Letter to CEOs, A Fundamental Reshaping of Finance (14 January 2020); Blackrock, Our Approach to Sustainability: Blackrock Investment Stewardship (July 2020). Similarly, California State Teachers’ Retirement System (CalSTRS) divested from U.S. thermal coal companies in 2016 and from non-U.S. thermal coal companies in 2017: <<https://www.calstrs.com/news-release/calstrs-takes-action-divest-all-non-us-thermal-coal-holdings>>.

transformation of the entire economy.⁶² As a result, in 2021, BlackRock is asking investee companies to disclose a plan for how their business model will be compatible with a net zero economy, and how this plan is incorporated into the company's long-term strategy and reviewed by the board of directors.⁶³

Cross-sectoral analysis also indicates a high appetite for climate change disclosures. The U.S. Government Accountability Office (GAO) interviewed a number of large and mid-sized institutional investors and pension funds to determine how and why investors sought ESG disclosures.⁶⁴ The majority of these entities agreed that ESG issues (including climate change) can have a substantial effect on a company's long-term financial performance, and that they engage directly with companies in which they hold investments in order to request additional ESG disclosures.⁶⁵ In preparation for the 2021 proxy season, Ernst & Young held discussions with more than 60 institutional investors representing over US\$38 trillion AUM, over half of which stated that climate risk was among the biggest threats facing companies over the next three to five years.⁶⁶

Mainstream investors are increasingly voting in favour of shareholder resolutions that seek increased information on companies' exposure and contribution to climate change, and their strategies for mitigation, adaptation or reaching net zero. Analysis by Ceres has shown that the number of shareholder resolutions has increased approximately fourfold between 2009 and 2018.⁶⁷ So far during the 2021 proxy season, at least 136 climate-related shareholder resolutions have been filed, at least 54 of which were withdrawn following engagement and agreement with the relevant company (indicating that the company had agreed to provide sufficient information to the investors).⁶⁸ Among those proceeding to vote were resolutions proposing that:

- ConocoPhillips and Chevron set and report on emission reduction targets covering the greenhouse gas emissions of the company's operations as well as their energy products (Scope 1, 2 and 3) (with 59.3% and 60.7% of the vote, respectively);⁶⁹
- Chevron report on the implications of the International Energy Agency's October 2020 Net Zero 2050 scenario (failed with 47.8% of the vote);⁷⁰

⁶² Larry Fink, BlackRock letter to CEOs (January 2021) <<https://www.blackrock.com/us/individual/2021-larry-fink-ceo-letter>>.

⁶³ *Id.*

⁶⁴ U.S. Government Accountability Office. *Public Companies: Disclosure of Environmental, Social, and Governance Factors and Options to Enhance Them* (2 July 2020).

⁶⁵ *Id.* 18.

⁶⁶ EY Center for Board Matters, *2021 proxy season preview: What investors expect from the 2021 proxy season* (January 2021) 3.

⁶⁷ Ceres, *The Role of Investors in Supporting Better Corporate ESG Performance* (February 2019).

⁶⁸ Ceres, *Investors seek greater climate action in 2021 Proxy Season* (2 April 2021), <<https://www.ceres.org/news-center/press-releases/investors-seek-greater-climate-action-2021-proxy-season>>

⁶⁹ ConocoPhillips. Form 8-K (filed 13 May 2021). EDGAR. Securities and Exchange Commission, 2021, <https://www.sec.gov/ix?doc=/Archives/edgar/data/1163165/000110465921065508/tm2116180d1_8k.htm>; Chevron Corporation. Form 8-K (filed 28 May 2021). EDGAR. Securities and Exchange Commission, 2021, <<https://www.sec.gov/Archives/edgar/data/0000093410/000009341021000020/cvx-20210526.htm>>.

⁷⁰ Chevron Corporation. Form 8-K (filed 28 May 2021). EDGAR. Securities and Exchange Commission, 2021, <<https://www.sec.gov/Archives/edgar/data/0000093410/000009341021000020/cvx-20210526.htm>>.

- Phillips 66 set and report on GHG reductions targets as well as the alignment of its lobbying activities with the objectives of the Paris Agreement (passed with 80.28% of the vote);⁷¹
- General Electric evaluate and disclose if and how the company has met the criteria of the 'Net Zero Indicator' produced by the Climate Action 100+ (passed with 97.97% of the vote);⁷²
- Exxon Mobil evaluate and report on the alignment of its lobbying activities with the objectives of the Paris Agreement, on the basis that "corporate lobbying that is inconsistent with the goals of the Paris Agreement presents regulatory, reputational and legal risks to investors" (passed with 63.8 % of the vote).⁷³

Shareholder resolutions have also targeted financial institutions – including large investors such as BlackRock, CalPERS and CalSTRS.⁷⁴ Proxy advisors such as ISS and Glass Lewis are also increasingly recommending voting in favour of requiring companies to disclose information on climate change risks.⁷⁵ Similarly, shareholder resolutions at each of Bank of America, CitiBank, Goldman Sachs, JP Morgan Chase and Wells Fargo proposing that each entity issue a report on reducing GHG emissions associated with its financing activities were withdrawn after each entity adopted a goal of attaining net zero emissions by 2050.⁷⁶ The 2021 proxy season has also seen the emergence of "Say on Climate" resolutions, asking that corporate transition plans be submitted to an advisory vote by shareholders. A "Say on Climate" has already been agreed to by corporate heavyweights from Unilever, to Moody's, Shell, Rio Tinto, and Glencore.⁷⁷

Question 1

Question 2

Question 5

C. Limits of Current Climate Change Disclosures

The number of companies which report on climate change and other ESG matters is increasing. Between 2017 and 2020, the percentage of Fortune 100 companies voluntarily reporting on environmental sustainability commitments increased from 37% to 77%.⁷⁸

⁷¹ Phillips 66. Form 8-K (filed 12 May 2021) EDGAR, Security and Exchange Commission, 2021, > Alex: can you replace with 8_K? My computer is acting up.

⁷² General Electric Company. Form 8-K (filed 4 May 2021). EDGAR. Securities and Exchange Commission, 2021 <<https://www.sec.gov/ix?doc=/Archives/edgar/data/40545/000004054521000030/ge-20210504.htm>>

⁷³ Exxon Mobil Corporation. Form 8_K (filed 2 June 2021). EDGAR, Security and Exchange Commission, 2021, <<https://ir.exxonmobil.com/static-files/6e0b2aef-43eb-4a52-bd34-92b283783b6c>>.

⁷⁴ In May 2020, JP Morgan Chase faced a resolution for greater disclosure on the climate impacts of its lending activities, which was only narrowly defeated on receiving 48.6% of the votes: Rachel Koning Beals, JP Morgan Chase shareholders defeat call for greater climate-change disclosure at world's largest oil funder, Market Watch (20 May 2020).

⁷⁵ Glass Lewis. *Guidelines: An Overview of the Glass Lewis approach to Proxy Advice: Environmental, Social & Governance ("ESG") Initiatives* (February 2021). < <https://www.glasslewis.com/wp-content/uploads/2020/11/ESG-Initiatives-Voting-Guidelines-GL.pdf?hsCtaTracking=c5fe11ce-e51d-449a-91fe-c00bfb8e16d0%7C80513084-8049-48f0-85bb-0e6864e24a9f>>.

ISS, *United States Proxy Voting Guidelines Benchmark Policy Recommendations*. (February 2021). <<https://www.issgovernance.com/file/policy/latest/americas/US-Voting-Guidelines.pdf>>

⁷⁶ Eamon Barrett, *Wells Fargo is the last of the Big Six banks to issue a net-zero climate pledge. Now comes the hard part*. Fortune. (2021) <<https://fortune.com/2021/03/09/wells-fargo-climate-carbon-neutral-net-zero/#:~:text=On%20Monday%2C%20Wells%20Fargo%20became,zero%20carbon%20emissions%20by%202050.>>.

⁷⁷ Say on Climate, *Supporters – Voluntary Adoption* <<https://www.sayonclimate.org/supporters/>>.

⁷⁸ EY Center for Board Matters, *Four ESG highlights from the 2020 proxy season* (July 2020) 4.

Another study has found that up to 60% of Russell 3000 firms mention climate change to some extent in their Form 10-K filings, an increase from 44% in 2010.⁷⁹

As well as reporting material climate change risks, a number of companies have adopted climate change disclosures under voluntary frameworks, including the TCFD, SASB and Climate Disclosure Project (CDP) frameworks. The number of companies disclosing under these frameworks is significant: over 700 U.S. companies produced TCFD disclosures in 2019,⁸⁰ over 500 SASB reports have been issued by U.S. companies since 2017,⁸¹ and over 9,000 companies globally have reported on climate change, water, and forestry issues through CDP.⁸²

However, there are a number of issues which continue to affect the disclosure of climate change- and other ESG-related disclosures:

- i. There is scope for improvement in the quality and consistency of climate change-related disclosures; and
- ii. Despite the wide-ranging risks created or exacerbated by climate change (as discussed in Section 2 above), the extent to which climate change is deemed to be a 'material' factor is not consistent across or even within industries.

i. *Quality and consistency of climate change-related disclosures*

Although the number of climate change-related disclosures has increased over the past decade, the utility of these disclosures to investors remains limited. Investors bemoan a lack of consistency and quality in climate change-related and other ESG disclosures, while at the same time, companies report being subject to varying requests for ESG information.⁸³ As Christopher Ailman, the CEO of CalSTRs, summarises the issue:⁸⁴

"It is an ongoing, constant topic. I'm devoting a lot of my time and attention because we're getting really inconsistent reporting. People are measuring in different metrics. They're not following a common template. And companies will tell you they're getting survey fatigue. They get so many ESG surveys. And so what we're really trying to do is promulgate more consistent standards, certainly the TCFD — Task Force on Climate-Related Financial Disclosures — standards for corporate disclosure. We're big proponents of SASB — Sustainability Accounting Standards Board — in terms of sustainability disclosures, and those aren't just U.S.-based frameworks."

Investors have described challenges with understanding and interpreting both quantitative and narrative disclosures due to inconsistencies in how data is presented and information gaps.⁸⁵ Comparing disclosures between companies is difficult as companies may report similar disclosures in different sections of their annual filings;⁸⁶ for example, in 2019, 30% of

⁷⁹ Parker Bolstad, Sadie Frank, Eric Gesick, and David G. Victor, *Flying blind: What do investors really know about climate change risks in the U.S. equity and municipal debt markets?*. Brookings (16 September 2020).

⁸⁰ TCFD, 2020 Status Report (2020).

⁸¹ SASB, Companies Reporting with SASB Standards. (17 January 2021). <<https://www.sasb.org/company-use/sasb-reporters/>>.

⁸² CDP. What we do (2021). <<https://www.cdp.net/en/info/about-us/what-we-do>>.

⁸³ PricewaterhouseCoopers, Mind the gap: the continued divide between investors and corporates on ESG (June 2020).

⁸⁴ Loretta Clodfelter, IREI, A conversation with CalSTRS' Christopher Ailman on ESG (19 June 2019).

⁸⁵ Government Accountability Office. *Public Companies: Disclosure of Environmental, Social, and Governance Factors and Options to Enhance Them* (2 July 2020) 12.

⁸⁶ Government Accountability Office. *Climate-Related Risks: SEC has taken steps to clarify disclosure requirements* (February 2018).

Russell 3000 companies discussed climate change as a risk in their 10-K statement, but only 3% of companies discussed climate change risk in the MD&A section.⁸⁷

The quality of the disclosures is often characterised by a lack of quantitative data and the use of boilerplate language.⁸⁸ U.S. companies could report significantly more useful climate data; in 2020, KPMG tested the disclosures of G250 companies against a set of 'best practice' standards based on TCFD and other frameworks. KPMG found that, for example, only 23% of U.S. companies included scenario analysis of climate-related risks in their reporting; and only 29% included a section on climate-related risk in their annual financial report and/or published a stand-alone climate risk report.⁸⁹

The effect of these inconsistencies is to limit investors' ability to utilise ESG data effectively. BlackRock has noted that "the lack of accepted data-reporting standards means investors cannot readily compare or combine insights across providers. This limits the ability to fully harness the potential of ESG information."⁹⁰ This is in line with the experience of financial institutions more broadly; in a survey on the usefulness of forward-looking metrics by the TCFD, half of financial institutions surveyed said that the disclosures would be useful with improved standardisation, and a majority stated that they found existing disclosures challenging to use.⁹¹

In addition to investor demands for consistency, some companies have explained that they have received requests for different information from different investors, which may indicate that investors are not aligned on what information they consider to be important.⁹² While it is perfectly plausible that investors will interpret data differently, there needs to be a common set of quantitative data presented, based on measurements using defined standards, comparable to financial reporting.

ii. *Uncertainty as to materiality of climate change risks*

Under the existing disclosure regime, companies must disclose information if they are under a specific duty to disclose that information or if that information is material and failing to disclose it would lead to statements made by the company being misleading.⁹³

Although there is currently no specific duty to disclose climate change risks in themselves, outside of the SEC's 2010 climate guidance, there is little question that these risks are material for U.S. companies. According to a 2019 survey, two thirds of companies consider climate change-related risks to be an issue for their business.⁹⁴ Climate change risk meets

⁸⁷ Rozin, L., *ESG Risks Trickle into Financial Filings*. Arlington, VA.: National Association of Corporate Directors. (21 October 2019) <<https://blog.nacdonline.org/posts/esg-risks-trickle-into-financial-filings>>.

⁸⁸ Government Accountability Office. *Climate-Related Risks: SEC has taken steps to clarify disclosure requirements* (February 2018).

⁸⁹ KPMG, *Towards net zero: How the world's largest companies report on climate risk and net zero transition* (November 2020).

⁹⁰ BlackRock Investment Institute, *Sustainability: The future of investing* (February 2019).

⁹¹ TCFD, *Forward-Looking Financial Metrics Consultation: Summary of responses* (March 2021), <<https://assets.bbhub.io/company/sites/60/2021/03/Summary-of-Forward-Looking-Financial-Metrics-Consultation.pdf>>

⁹² Government Accountability Office. *Public Companies: Disclosure of Environmental, Social, and Governance Factors and Options to Enhance Them* (2 July 2020).

⁹³ SEC Commissioner Allison Herren Lee, *Living in a Material World: Myths and Misconceptions about "Materiality"* (24 May 2021).

⁹⁴ Richard Mahony and Diane Gargiulo, Gargiulo Partners, *The State of Climate Risk Disclosure: A Survey of US Companies* (24 October 2019).

the threshold of materiality from an investor perspective,⁹⁵ as demonstrated by the increased demand for climate change information and the effect of climate change disclosures on stock price. A 2020 study concluded that companies which disclosed climate change-related risks had a lower cost of equity than those which did not – meaning that investors required a lower return on their investment to encourage investment in the company, implying that they saw the companies as less risky.⁹⁶ This effect was significantly greater when the company operated in a sector which investors perceived to be particularly exposed to climate change risks.⁹⁷ Similarly, a study on the adoption of the voluntary SASB sustainability disclosures found a strong correlation between SASB disclosures and stock price informativeness (i.e. the degree to which a company's stock price accurately reflects private and public information about that company in the market), which suggests that these disclosures contain financially-relevant, firm-specific information which inform investors' considerations of future earnings.⁹⁸ Research has also shown that a majority of investors using ESG disclosures (including disclosures relating to climate change) do so because they believe it is financially material to investment performance.⁹⁹

The SEC's 2010 guidance on climate change disclosures gives examples of required statements in respect of which material climate change information may need to be disclosed. These include MD&A disclosures, the purpose of which is to enable investors to see the registrant through the eyes of management, and which should include known trends, events, demands, commitments and uncertainties that are reasonably likely to have a material effect on financial condition or operating performance;¹⁰⁰ and risk factors which make an investment speculative or risky.¹⁰¹ In light of the severity and scope of climate change risks on the U.S. economy,¹⁰² a reasonable investor might well expect climate change information to be included in a company's disclosures in order to enable them to understand the risks reasonably likely to have a material effect on the company.¹⁰³

However, it appears that climate change-related information is not being disclosed in SEC filings despite its likely materiality. Comparative analyses between materials disclosed by companies in their SEC filings and voluntarily disclosed elsewhere show that a substantial amount of information relating to climate change may be disclosed without being included in

⁹⁵ Information is "material" if "there is a substantial likelihood that a reasonable investor would consider it important in deciding how to vote or make an investment decision." *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976).

⁹⁶ Ella Mae Matsumura, Rachna Prakash, Sandra C. Vera-Muñoz, *Climate-Risk Materiality and Firm Risk* (10 August 2020).

⁹⁷ *Id.*

⁹⁸ Grewal J., Hauptmann C., and Serafeim G. "Material Sustainability Information and Stock Price Informativeness". *Journal of Business Ethics* (29 January 2020).

⁹⁹ Amir Amel-Zadeh & George Serafeim, *Why and How Investors Use ESG Information: Evidence From a Global Survey*, 74 Fin. Analysts J. 87 (2018). Government Accountability Office. *Public Companies: Disclosure of Environmental, Social, and Governance Factors and Options to Enhance Them* (2 July 2020).

¹⁰⁰ Regulation S-K, Item 303.

¹⁰¹ Regulation S-K, Item 504.

¹⁰² See Section 2 above.

¹⁰³ Hana Vizcarra, *The Reasonable Investor and Climate-Related Information: Changing Expectations for Financial Disclosures*, *Environmental Law Reporter*, 50 ELR 10106 (2020).

SEC filings.¹⁰⁴ This discrepancy has also been noted by the SEC itself in comment letters sent to companies.¹⁰⁵

There have been high profile cases in which companies have failed to meet their legal obligations to disclose climate change risks. The SEC 2010 guidance on climate change notes three instances in which, following investigations by the New York Attorney General's office (NYAG), a company was obliged to enhance their disclosures relating to climate change and greenhouse gas emissions in their annual reports filed with the SEC.¹⁰⁶ Since the publication of this guidance, at least one further high-profile instance of this has occurred with the investigation of Peabody Energy Corporation (Peabody), in which the NYAG found that Peabody had failed to include disclosures in its SEC filings on the impacts of possible future energy scenarios on its business.¹⁰⁷

One possible reason for the uncertainty regarding the materiality of climate change risks may be the timescales on which materiality is considered under U.S. law. As the Climate-Related Market Risk Subcommittee of the U.S. Commodity Futures Trading Commission suggests:¹⁰⁸

“Disclosure in SEC filings has been inadequate, in part, because materiality under U.S. law is often interpreted as limiting required disclosure to short- and medium-term risks, and firms may have assumed that climate risks are relevant only over longer time horizons. However, different firms and industries may have different time horizons over which climate risks are deemed material, taking into account factors like the economic life of assets, the percentage of valuation that can be attributed to future growth, the nature of climate-related risk exposure, and corporate strategy.”

The scope and significance of climate change risks and the requests by investors for climate change and other ESG disclosures indicates that climate change disclosures should, in many cases, fall within the existing scope of materiality. Increased guidance for regulated companies on the disclosure of climate change risks, which should take the form of a mandated set of standards, would be welcomed by investors and would assist companies in fulfilling their existing disclosure obligations.

Investors are increasingly demanding increased disclosures on climate change risks. However, there is a significant amount of uncertainty regarding when such risks may be material for the purpose of disclosure. As a result, most climate change disclosures are made voluntarily, but with differences in the quality and consistency of disclosures, and a lack of material information. Materials reviewed in preparing this Comment suggest that useful disclosures should, at least:

- Be included in a standardised part of a filing, such as MD&A disclosures or as part of non-financial reporting;

¹⁰⁴ Ceres, *Cool Response: The SEC and Corporate Climate Change Reporting* (February 2014); Benjamin Hulac, *Inside the mirage of good climate info at the SEC*, E&E News (11 August 2016), <<https://www.eenews.net/stories/1060041464>> [Accessed 21 May 2021].

¹⁰⁵ See, e.g. Letter from Christopher O. Champion, Vice President, Chief Accounting Officer and Controller, Anadarko Petroleum Corporation to Mr. H. Roger Schwall, SEC, dated 30 September 2016.

¹⁰⁶ Securities and Exchange Commission, Securities Act Release No. 34-9106 (Commission Guidance Regarding Disclosure Related to Climate Change) (February 8, 2010).

¹⁰⁷ *In re Peabody Energy Corp.* 15-242 (2015).

¹⁰⁸ Climate-Related Market Risk Subcommittee, Market Risk Advisory Committee of the U.S. Commodity Futures Trading Commission, *Managing Climate Risk in the U.S. Financial System* (9 September 2020).

- Contain relevant quantitative data (such as direct, indirect and value chain GHG emissions, reductions in GHG emissions, and potential financial impact of climate change risks) and qualitative information (such as identified climate related risks and how they are managed and who is responsible, and how these risks may crystallise under different climate scenarios), in a way which is comparable and comprehensive;
- Use reputable and verifiable information and sources in support; and
- Avoid 'boilerplate' language.

D. Little or no exposure to increased litigation risk

Companies, and in particular directors, may be concerned that increased disclosures on ESG issues may lead to increased litigation risk.¹⁰⁹ This concern is likely overstated.

While companies may potentially face claims for failing to disclose material risks – indeed, there is outstanding litigation regarding allegedly inadequate disclosures by ExxonMobil regarding the impact of climate change on the company's business¹¹⁰ – compliance with climate change guidance and/or mandatory standards will not necessarily increase liability exposure. Compliance with existing law will translate into good practice on climate change related disclosures.

Under U.S. law, directors and companies may be liable for misstatements or omissions of a material fact where they have an intention to deceive or recklessness about the capacity of a statement to deceive investors. However, various protections arise under the “safe harbor” provisions of Rule 175 of the Code of Federal Regulations, and section 21E of the Securities Exchange Act of 1934, which each protect issuers from liability for forward-looking statements (including projections of revenues, incomes, earnings per share, management plans and objectives and statements of future economic performance within the management discussion and analysis) under specified conditions: under Rule 175, provided that these statements are made on a reasonable basis and disclosed in good faith; or under section 21E, if the statements are identified as forward-looking statements, and accompanied by meaningful cautionary statements.¹¹¹ The courts provide additional protections, and will assess whether a forward-looking statement is misleading in light of other cautionary statements in the document in which it is made (the “bespeaks caution doctrine”).¹¹² Directors and companies may also proffer opinions on material matters which may subsequently turn out to be incorrect without fear of liability, provided that the opinion is given with a reasonable basis in the facts in the company's possession on the subject of the opinion, and is honestly believed by the speakers.¹¹³

Therefore, directors and companies are unlikely to face liability exposure where their disclosures accurately represent a robust, good-faith process of assessment that applies the best evidence reasonably available at the relevant time, and where those disclosures are appropriately caveated or qualified, and do not merely “cherry-pick” optimistic scenarios.¹¹⁴

¹⁰⁹ See Simon Clarke, Nihar Lovell and Sousan Gorji, Herbert Smith Freehills LLP, “Climate-related disclosures: the new frontier?” *Butterworths Journal of International Banking and Financial Law* (October 2020) 615-619.

¹¹⁰ *Ramirez v. Exxon Mobil Corp.*, 334 F.Supp. 3d 832 (N.D. Tex. 2018).

¹¹¹ 17 CFR § 230.175 - Liability for certain statements by issuers.

¹¹² *Kaufman v. Trump's Castle Funding*, 7 F.3d 357 (3d Cir. 1993).

¹¹³ *Omnicare v. Laborers Dist. Council Constr. Indus. Pension Fund*, 135 S. Ct. 1318 (2015).

¹¹⁴ Alexia Staker, Alice Garton, Sarah Barker, *Concerns misplaced: will compliance with the TCFD recommendations really expose companies and directors to liability risk?* (September 2017).

Indeed, encouraging climate change risk disclosures and setting standards for these disclosures may decrease companies' and directors' exposure to liability, as it becomes clear to companies how they need to report on these risks, and it becomes clear to investors that the relevant risks are being transparently reported.¹¹⁵

Question 15

4. Other ESG disclosures

Along with climate change risks, investor demand for other ESG disclosures is growing.¹¹⁶ ESG information desired by investors is broad, covering many aspects of environmental, social and governance issues.¹¹⁷ While recognising the importance of these issues in social and financial terms, this comment will focus on the requirement for disclosures relating to biodiversity and related environmental risks.

Similar to climate change, biodiversity loss poses significant risks to the commercial and financial world. The Organisation for Economic Co-operation and Development (OECD) has identified ecological risks (associated with resource dependency, scarcity and quality), liability risks,¹¹⁸ regulatory risks, reputational risks, market risks (caused by changes in consumer preferences or supply-chain requirements by purchasers), and financial risks from biodiversity loss.¹¹⁹ The UN PRI has identified biodiversity risk as a systemic risk which has the potential to affect investment value in the short, medium and long term.¹²⁰ The World Economic Forum (WEF)'s 2020 Global Risks Perception Survey identified biodiversity loss related risk as one of the top three risks facing the global economy in terms of both likelihood and impact.¹²¹

As well as posing significant risks in its own right, biodiversity loss is inextricably linked with climate change risks. Taking steps to mitigate climate change will help to prevent biodiversity loss, and *vice versa*, actions to prevent biodiversity loss will assist in mitigating climate

¹¹⁵ Robin Hamaker-Taylor, Richard Bater, Nadine Coudel, *Voluntary Climate Disclosures Can Reduce Litigation Risk*, Acclimatise News (13 June 2019) <<http://www.acclimatise.uk.com/2019/06/13/voluntary-climate-disclosures-can-reduce-litigation-risk/>>; Thomas Bourveau; Yun Lo; and Rencheng Wang. *Shareholder litigation and corporate disclosure: Evidence from derivative lawsuits*. *Journal of Accounting Research*. 56, (3), 797-842. Research Collection School Of Accountancy (2018) <https://ink.library.smu.edu.sg/soa_research/1713>.

¹¹⁶ Government Accountability Office. *Public Companies: Disclosure of Environmental, Social, and Governance Factors and Options to Enhance Them* (2 July 2020).

¹¹⁷ *Id.*; Amel-Zadeh, Amir, and George Serafeim. "Why and How Investors Use ESG Information: Evidence from a Global Survey." *Financial Analysts Journal*. 74.3 (2018), 87-103.

¹¹⁸ Liability risks relating to biodiversity are varied, and should be considered under three categories: (a) the nature and breadth of potential liability exposures (causes of action); (b) the transmission mechanisms within and between the real economy and the financial sector; and (c) legal and market dynamics in the jurisdiction. Financial institutions should prepare for these risks and price their investments accordingly. See Sarah Barker, Ellie Mulholland, and Temitope Onifade, *The emergence of foreseeable biodiversity-related liability risks for financial institutions: A gathering storm?* (August 2020) <<https://ccli.ouce.ox.ac.uk/wp-content/uploads/2020/09/CCLI-Biodiversity-liability-risks-report-vFINAL.pdf>>.

¹¹⁹ OECD, *Biodiversity: Finance and the Economic and Business Case for Action*, report prepared for the G7 Environment Ministers' Meeting, 5-6 May 2019, 37-38. See also Girvan et al., *Biodiversity Risk - Integrating Business and Biodiversity in the Tertiary Sector* (2018) <<https://data.jncc.gov.uk/data/7cac352f-1b21-420e-9e0a-c0860f4da556/JNCC-Report-620-FINAL-WEB.pdf>> [Accessed on 21 May 2021].

¹²⁰ UN PRI, *Investor Action on Biodiversity: Discussion Paper* (1 September 2020) <<https://www.unpri.org/download?ac=11357>>.

¹²¹ World Economic Forum. *The Global Risks Report 2020* (15 January 2020) <http://www3.weforum.org/docs/WEF_Global_Risk_Report_2020.pdf>.

change.¹²² Conversely, failure to take action on either biodiversity or climate change is likely to give rise to increased risks and losses caused by the other; the two issues are therefore likely to 'feedback' with each other to give rise to compound risks.¹²³

Large asset managers, including CalPERS, BMO Asset Management, and Allianz Global Investors strongly consider biodiversity in their investment strategies.¹²⁴ However, as with climate change and other ESG information, investors cite a lack of consistent high-quality information and data as a barrier to suitable investment. A Credit Suisse study found that 55% of investors surveyed believe that biodiversity is a major issue which needs to be addressed in the next few years, but that 70% of investors found a lack of data availability and metrics to be a major barrier to investing.¹²⁵ Similarly, a UN PRI study reports that:¹²⁶

"[i]nvestors interviewed for this report cited a lack of access to appropriate asset and company-level data to assess company performance and evaluate fund or investment impact. Data is often not fit for purpose. Biodiversity is location specific and varies according to the actual asset at that location. Therefore, it can be challenging to aggregate biodiversity data at an enterprise level."

As with climate change, voluntary reporting standards on biodiversity have been developed by third party organisations, including SASB and the Global Reporting Initiative (GRI). However, the UN PRI has noted that although investors are already using the SASB materiality map to identify sectors for which biodiversity may be financially material, there is scope for development in the standards set by SASB and other organisations.¹²⁷ The Taskforce for Nature-related Financial Disclosures (TNFD), comprising 74 financial institutions, regulators, corporates and others representing over \$8 trillion AUM, is developing a set of standards for biodiversity, which may assist in aligning corporate approaches to this issue.

The SEC should consider broadening the scope of any increased guidance or mandatory disclosure rules to include other ESG factors such as biodiversity. There is clear investor appetite for clear, accurate and informative disclosures on these issues.

¹²² See Conference Of The Parties To The Convention On Biological Diversity, Key Messages from the Workshop on "Biodiversity And Climate Change: Integrated Science For Coherent Policy" Paris (18 October 2018) <<https://www.cbd.int/doc/c/c429/2df7/dc8cc589bbf1f5b58f8a1d63/cop-14-inf-22-en.pdf>>.

¹²³ *Id.*

¹²⁴ Leaders Arena, *Biodiversity Reporting Study 2021* (February 2021).

¹²⁵ Credit Suisse, *Unearthing investor action on biodiversity* (January 2021), 42.

¹²⁶ UN PRI, *Investor Action on Biodiversity: Discussion Paper* (1 September 2020) <<https://www.unpri.org/download?ac=11357>>.

¹²⁷ *Id.* at 16-17, 29.

Conclusion

We commend the SEC for engaging in this important regulatory process. We welcome the opportunity to discuss these comments with the Commission or the Commission's Staff.

Your sincerely



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