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JUMPSTARTING SUSTAINABILITY DISCLOSURE

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Abstract

Sustainability disclosures have been on the agenda of the Securities and Exchange Commission for almost fifty years. The issue has been intractable. Activists and investors have been urging the SEC to adopt mandatory sustainability disclosures. The business community has opposed new disclosure obligations on the grounds of immateriality, cost and litigation risk. The SEC has historically been skeptical that sustainability information is material to investors and has resisted issuing new rules.

In the meantime, public companies have responded to pressure from activists, investors and other stakeholders by voluntarily publishing sustainability reports according to standards established by private standard-setting organizations with expertise in sustainability matters. But according to investors and other observers, the disclosures included in such voluntary sustainability reports are not sufficiently accessible, comparable and reliable to provide the information investors need to make informed decisions. As a response to the inadequacies of the current private-ordering regime, academics and investors have proposed new mandatory disclosure frameworks that are meeting stiff resistance from the business community, and the SEC has entered into a polarized public debate on the issue.

However, there is a path out of the present stalemate. The SEC can jumpstart progress on this contentious issue by harnessing private ordering under the watchful eye of the regulator - requiring public companies to furnish to the SEC on Form 8-K the sustainability reports they are already producing. By requiring sustainability reports to be included in its publicly available EDGAR filing system, the SEC could improve the accessibility, comparability and reliability of sustainability disclosures without materially increasing costs or liability risks for reporting companies. By lowering costs for investors, issuers and itself, the SEC can fulfill its mission of protecting investors, promoting fair and efficient capital markets and facilitating capital formation.

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INTRODUCTION

Sustainability disclosures have been on the agenda of the Securities and Exchange Commission (the "SEC") for almost fifty years. The issue has been intractable. In the last decade, a rising chorus of activists, investors and academics have been prodding the SEC to adopt mandatory rules for sustainability disclosures with increasing assertiveness. Although more than 90% of the companies in the S&P 500 now voluntarily publish annual sustainability reports,[1] the business community and some politicians consistently oppose new mandatory SEC disclosure obligations on the bases of immateriality, cost and liability risk. The SEC has remained skeptical, over the course of multiple presidential administrations, that information on sustainability and social policy issues, typically referred to as environmental, social and governance, or ESG, issues, is material to investors, and has resisted issuing new prescriptive disclosure rules.[2] Instead, it continues to rely on principles-based rules focused on disclosure of "material" information and refers issuers and investors to its general requirements for disclosure of material information in business descriptions, risk factors and Management's Discussion & Analysis of Financial Condition and Results of Operations.[3]

[1] Governance & Accountability Inst., *Flash Report: 90% of the S&P 500 Companies Published Corporate Sustainability Reports in 2019* (July 16, 2020), *available at*: https://www.ga-institute.com/research-reports/flash-reports/2020-sp-500-flash-report.html.

[2] In its Regulation S-K Concept Release, the SEC explained that "[s]ustainability disclosure encompasses a range of topics, including climate change, resource scarcity, corporate social responsibility, and good corporate citizenship. These topics often are characterized broadly as environmental, social or governance ('ESG') concerns." 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, 23,9670 (proposed Apr. 22, 2016) [hereinafter, "Reg S-K Concept Release"]. The terms "sustainability disclosures" and "ESG disclosures" are used interchangeably throughout this article.

[3] Commission Guidance Regarding Disclosure Related to Climate Change, Securities Act Release No. 33-9106, Securities Exchange Act Release No. 34-61469, 75 Fed. Reg. 6290 (interpretation, Feb. 8, 2010) [hereinafter, "Climate Change Release"]. "Principles-based" rules articulate a disclosure objective, such as disclosure of "material" information, and look to management to exercise judgment in satisfying that objective. Prescriptive, or line-item disclosure rules mandate specific disclosures, sometimes using quantitative thresholds, to minimize uncertainty when certain kinds of information are presumed to be material. Cydney Posner, *SEC adopts amendments to modernize Reg S-K requirements for business, legal proceedings and risk factor disclosures (UPDATED)*, COOLEY PUBCO (August 31, 2020), *available at:* https://cooleypubco.com/2020/08/31/sec-amendments-

The materiality of sustainability disclosures is subject to ongoing debate, but there is a growing body of scholarly empirical evidence and statements from institutional investors suggesting that such disclosures are material to investment and voting decisions.[4] Experts are explaining with increasing specificity how climate change poses material risks and opportunities for companies in almost all industries.[5] In 2016, the SEC issued a concept release (the "Reg S-K Concept Release") asking for comments about whether it should mandate sustainability disclosures, among other changes to its Regulation S-K rules for corporate disclosures in annual reports and registration statements.[6] The SEC received over 10,100 responses to its request for views on mandating sustainability disclosures.[7] Among the responses, 10,070 expressed support for mandatory sustainability disclosures, while 43 commenters expressed opposition or ambiguous views.[8]

Although the SEC has been reluctant to mandate disclosure of sustainability metrics, public companies have responded to pressure from activists, investors and other stakeholders by voluntarily publishing sustainability reports according to standards established by private standard-setting organizations with expertise in sustainability matters.[9] But according

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[4] *See infra*, Section II.A.2.

[5] Sustainability Accounting Standards Board, *Climate Risk—Technical Bulletin,* SASB Library 2017 (noting that 72 of 79 industries, representing 93% of the market value of U.S. capital markets, are vulnerable to material financial impacts from climate change), *available at* https://library.sasb.org/climate-risk-technical-bulletin/.

[6] Reg S-K Concept Release, *supra* note 2.

[7] TYLER GELLASCH, AFL–CIO ET AL., TOWARDS A SUSTAINABLE ECONOMY: A REVIEW OF COMMENTS TO THE SEC'S DISCLOSURE EFFECTIVENESS CONCEPT RELEASE 10 (2016)[hereinafter, the "GELLASCH REPORT"].

[8] GELLASCH REPORT, *supra* note 7 at 21. Pursuant to a public interest campaign sponsored by Public Citizen, 9,859 individuals submitted copies of a prepared letter calling for enhanced disclosures on taxes, political spending and sustainability issues. The remaining submissions – more than 250 – were unique comments posted by a variety of individuals and organizations. *Id.* at 15. The total number of comments on the concept release, which also dealt with other possible amendments to Regulation S-K's disclosure requirements, was more than 26,500. *Id.* at 8-9. Only five of 161 other major rule-making proposals by the SEC since 2008 had received a similar number of comments as of September 2016. *Id*

[9] ESG reporting standards have been developed by numerous organizations, including the Global Reporting Initiative (GRI), the Greenhouse Gas Protocol (from the World Business Council for Sustainable Development and the World Resources Institute), the UN Global Compact, the Carbon Disclosure Project (now CDP), established in 2000, which scored companies on , the International Integrated Reporting Council (IIRC), the

to investors and other observers, the disclosures included in such voluntary sustainability reports are not sufficiently accessible, comparable, or reliable to provide the information investors need to make informed decisions.[10]

Proponents of mandatory, or prescriptive, disclosure requirements argue that regulatory mandates are necessary to force reluctant companies to disclose potentially negative or competitively sensitive information. They aver that when the SEC relies on principles-based rules requiring "material information" as opposed to prescriptive rules requiring explicit categories or items of information to be disclosed, registrants will exercise their discretion to conclude such is not material and need not be disclosed.[11] Without mandatory rules, the costs of acquiring, processing and verifying this material information will be too high and equity prices will not reflect their equilibrium values.[12]

Academics have responded to the perceived need for mandatory SEC disclosure rules with a variety of proposals, from the establishment of a

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Sustainability Accounting Standards Board (SASB) and the Embankment Project for Inclusive Capitalism.

[10] *See infra*, Sections II.B.1 and II.C.

[11] *See, e.g.,* Allison Herren Lee and Robert J. Jackson, Jr., Comm'rs, Sec. Exch. Comm'n, Joint Statement of Commissioners Robert J. Jackson, Jr. and Allison Herren Lee on Proposed Changes to Regulation S-K (Aug. 27, 2019)[hereinafter, "Jackson/Lee Joint Statement"], *available at* https://www.sec.gov/news/public-statement/statement-jackson-lee-082719. Both principles-based and prescriptive disclosure regimes have their strengths and weaknesses. As noted by securities law blogger, Cydney Posner:

> While principles-based rules are necessarily imprecise, may be difficult to apply and can result in a loss of comparability among reporting entities, they can help to eliminate irrelevant information by permitting tailored responses that focus on information that is material to the particular business and are more flexible and adaptable as circumstances change. Prescriptive standards can help promote comparability, consistency and completeness of disclosure, but they can sometimes be circumvented and may not address or capture all the important information.

Cydney Posner, *SEC adopts amendments to modernize Reg S-K requirements for business, legal proceedings and risk factor disclosures (UPDATED)*, COOLEY PUBCO (August 31, 2020), *available at:* https://cooleypubco.com/2020/08/31/sec-amendments-modernize-reg-s-k-business-legal-risks/.

[12] Ronald J. Gilson & Reinier H. Kraakman, *The Mechanics of Market Efficiency*, 70 VA. L. REV. 549, 565 (1984). Allianz Global Investors stated in a 2017 research report that companies could get lower costs of capital by reducing the investment risk premium required by sophisticated investors from companies that do not provide adequate sustainability information. Allianz Global Investors, *ESG matters, Part 2: Added value or a mere marketing tool? What does ESG mean for investments?* (June 2017).

Sustainability Discussion & Analysis section in Annual Reports on Form 10-K[13] to the adoption of a comply or explain regime akin to the rules adopted by several countries in the European Union.[14] In October 2018, a group of institutional investors representing more than $5 trillion in assets under management petitioned the SEC to issue mandatory rules for ESG disclosures.[15] In May 2020, the Investors' Advisory Committee of the SEC recommended to the Commission that they "update the reporting requirements of Issuers to include material, decision-useful, ESG factors."[16] The SEC has not acted on either proposal, and the Commission has entered into a polarized public debate about the need for mandatory sustainability disclosure rules.[17]

Thus, the sustainability disclosure debate has bogged down in a polarized all-or-nothing stalemate between the proponents of mandatory disclosure and supporters of the private-ordering status quo. But there is a path out of this quagmire. Comparability and reliability can be improved without resort to mandatory disclosure requirements if the disclosing parties are aware that their disclosures will be shared with market participants and reviewed by their regulator for comparison with similar disclosures made by other companies in their industry.[18]

Where the vast majority of companies are already voluntarily disclosing significant amounts of arguably material information to the public, but the disclosures are not easily accessible to the entire market or lack clarity, comparability and reliability, procedural as opposed to substantive regulation may be sufficient to address the needs of investors.[19] Particularly

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[13] Jill E. Fisch, *Making Sustainability Disclosure Sustainable*, 107 GEO. L. J. 923 (2018).

[14] Virginia Harper Ho, *"Comply or Explain" and the Future of Nonfinancial Reporting*, 21 LEWIS & CLARK L. REV. 317 (2017) (describing the "comply or explain" approach and advocating its adoption in the United States for sustainability reporting).

[15] Cynthia A. Williams & Jill E. Fisch, *Request for Rulemaking on Environmental, Social, and Governance (ESG) Disclosure*, U.S. SEC. & EXCH. COMM'N (Oct. 1, 2018), https://www.sec.gov/ rules/petitions/2018/petn4-730.pdf [hereinafter *Petition for Rulemaking*].

[16] INVESTOR-AS-OWNER SUBCOMM., SEC INVESTOR ADVISORY COMMITTEE, RECOMMENDATION FROM THE INVESTOR-AS-OWNER SUBCOMMITTEE OF THE SEC INVESTOR ADVISORY COMMITTEE RELATING TO ESG DISCLOSURE 7 (as of May 14, 2020), https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[17] *See infra*, Section III.D.

[18] *See infra*, Sections IV.B. and IV.C.

[19] For a discussion of the differences between procedural and substantive regulation, and the ability to cooperate with private actors to establish substantive requirements, *see*

where there is no consensus among information providers, information consumers, legislators and regulators about which factors or metrics are material and which are not, the precise measures of materiality are not yet established and expert private standard-setters are issuing standards that companies can follow voluntarily, progress can be made while lowering the costs of both production and consumption of the information by requiring the voluntary disclosures following private standards to be filed with the regulator.[20] I call this "private ordering under the watchful eye of the regulator."

Disclosure under the watchful eye of the regulator occurs when the regulator permits private ordering to determine the substantive content of disclosure to the market but requires the disclosures to be submitted to the regulator to promote broad dissemination of the information and regulatory oversight to ensure the content is not misleading. This approach promotes comparability and reliability without significantly increasing information production costs and liability risks for companies. As such, companies have less incentive to oppose such a regulatory approach and may even be enlisted to support such regulation to avoid stricter regulation, such as mandatory disclosure rules.

The SEC could jumpstart progress on the contentious issue of sustainability disclosures by requiring public companies to furnish the sustainability reports they are already producing to the SEC on Form 8-K.[21] The SEC previously used this approach successfully when it mandated that voluntary quarterly earnings reports be submitted to its EDGAR system. As is true for voluntary quarterly earnings releases, the market would determine the substance of the disclosure, but the accessibility, comparability and reliability of the information would be increased without

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Jody Freeman, *The Private Role in Public Governance,* 75 N.Y.U. L. REV.543 (2000).

[20] The field of sustainability disclosures is still sufficiently nascent that it is difficult for regulators to determine with precision precisely which measures should be disclosed by which companies. While the market is in the process of determining precisely which information is most material to investors in various contexts, securities regulators can reduce their own costs as well as costs to producers and consumers of information by permitting the market to establish, through the work of private standards setters and iterative engagements among such standard setters and representatives of information providers and information consumers, the most important disclosure metrics.

[21] One company, Vornado Realty, has taken this step voluntarily. *See* Tom Riesenberg and Alan Beller, SUSTAINABILITY ACCOUNTING STANDARDS BOARD, *Sustainability Accounting Standards and SEC Filings*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (June 5, 2019) (discussing varying liability frameworks depending on the location of disclosure), *available at*: https://corpgov.law.harvard.edu/2019/06/05/sustainability-accounting-standards-and-sec-filings/.

materially increasing costs or liability risks for companies. If, as was the case with quarterly earnings reports, the SEC subsequently becomes concerned that the metrics used in the sustainability reports are misleading, it can issue substantive regulations covering the contents of the reports.[22]

The SEC currently permits public companies to furnish, rather than filing, quarterly earnings releases and documents responsive to Regulation FD (Fair Disclosure) on Form 8-K.[23] Statements made in documents furnished under Form 8-K are subject to 10b-5 liability, as are all public statements made by companies registered with the SEC, including sustainability reports posted on public relations websites, but they are not subject to liability under Section 18 of the Securities Exchange Act of 1934.[24] More importantly, documents that are furnished, as opposed to filed, under Form 8-K are not incorporated by reference into registration statements filed under the Securities Act pursuant to the SEC's integrated disclosure and reporting system, so they are not subject to strict liability under Section 11 of the Securities Act of 1933. If the SEC were to follow a similar approach to sustainability disclosures, public companies could furnish their sustainability reports to the SEC without significant additional liability risk.[25]

Requiring sustainability reports to be furnished on Form 8-K will promote progress on investors' concerns without imposing significant additional costs on companies.[26] Companies would still be able to choose whether to produce sustainability reports, just as they can choose whether to issue earnings releases. They could also continue to report sustainability information in the manner they prefer, but centralized availability in the SEC's EDGAR system will encourage convergence as companies compare their filings with those of their competitors.[27] EDGAR "filing" under the watchful eye of the SEC will also increase the reliability of the information by shifting responsibility for disclosures from corporate social responsibility departments to general counsel and other executives who

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[22] In the case of quarterly earnings reports, the SEC became concerned about some of the Non-GAAP measures used by companies to report their earnings results and issued Regulation G to provide conditions for the use of such measures. *See* Conditions for Use of Non-GAAP Financial Measures, Securities Act Release No. 33-8176, Securities Exchange Act Release No. 34-47226, 68 Fed. Reg. 4819 (Jan. 30, 2003).

[23] *See infra* Sections III.B and III.C.

[24] *See infra*, Section III.A.

[25] *See infra*, Sections III.A. and IV.D.

[26] *See infra*, Section IV.D.

[27] *See infra*, Section IV.B.

typically review all filings with the SEC.[28] Jumpstarting sustainability reporting through Form 8-K filings will also allow private ordering to establish the most important sustainability disclosures for each industry rather than requiring the SEC to decide which sustainability disclosures should be mandatory before there is a consensus among the users of the information, saving administrative as well as corporate resources.

I. MANDATORY DISCLOSURE AND PRIVATE ORDERING UNDER THE WATCHFUL EYE OF THE REGULATOR

Full and fair disclosure is a hallmark of the U.S. securities laws.[29] One way to think about full and fair disclosure is to consider market efficiency - which disclosures in what manner are necessary to ensure that securities reach their equilibrium prices as quickly and costlessly as possible?[30] Gilson and Kraakman explain that the efficiency of equity market prices will depend in part on the cost to investors of acquiring, processing, and verifying information about the issuers.[31] This implies that disclosure regulations should reduce the collective cost to investors of performing these functions as much as possible as long as such reduction in investor costs does not impose such high costs on the originators of the information (issuers) that they are unwilling to participate in the market.

Scholars have argued that the SEC should promote market efficiency in its rule-making by focusing on fair access, transparency and standardization, while policing the integrity and reliability of the information disclosed.[32] Fair access to information in the market, meaning that all investors have access to the same information at the same time, has, in fact, been a consistent theme of SEC rule-making.[33]

Whether new mandatory disclosure rules promote market efficiency and

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[28] *See infra*, Section IV.C.

[29] Securities Act of 1933, Pub. L. No. 73-22, 48 Stat. 74, 15 USC § 78(b)(preamble).

[30] Onnig H. Dombalagian, *Regulating Information Flows in Capital Markets*, 68 S.M.U. L. REV. 727, 728 (2015).

[31] Gilson & Kraakman, *supra* note 12.

[32] Dombalagian, *supra*, note 30 at 728-29 (noting that chief among the objectives of information policy in capital markets are "promoting transparency, fair access, standardization, verification, and interpretive transformation, while policing information flows for integrity and reliability, with a view to economizing on the costs of information dissemination and use.").

[33] *See*, *e.g.*, Final Rule: Selective Disclosure and Insider Trading, SEC Rel. 33-7881, 34-43154, 65 Fed. Reg. 51715 (2000) [hereinafter, "Reg FD Adopting Release"].

fairness has been the subject of extended scholarly debate for decades.[34] Building on the signaling theories of Hart and Grossman, opponents of mandatory disclosure generally argue that mandatory disclosure rules are inefficient because they are costly and unnecessary since individual issuers have incentives to distinguish themselves from competitors by providing superior disclosure when they have a superior story to tell. Issuers are in the best position to determine optimal disclosure for themselves, trading off the costs and benefits of disclosure.[35] Proponents of mandatory disclosure respond that even assuming companies have incentives to provide optimal disclosure for themselves,[36] mandatory disclosure has other socio-economic value, including more accurate pricing of other firms in the market,[37] and more robust competition in the markets for finance and products.[38]

Private ordering through expert private standard-setters can lower both

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[34] For views supporting mandatory disclosure rules, *see, e.g.*, Colleen Honigsberg, Robert J. Jackson, Jr. & Yu-Ting Forester Wong, *Mandatory Disclosure and Individual Investors: Evidence from the JOBS Act*, 93 WASH. U. L. REV. 293 (2015); Allen Ferrell, *The Case for Mandatory Disclosure in Securities Regulation Around the World*, 2 BROOK. J. CORP. FIN. & COM. L. 81 (2007); Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice Is Not Investor Empowerment*, 85 VA. L. REV. 1335 (1999); Merritt B. Fox, *Securities Disclosure in a Globalizing Market: Who Should Regulate Whom,* 95 MICH. L. REV. 2498 (1997); John C. Coffee, Jr., *Market Failure and the Economic Case for a Mandatory Disclosure System*, 70 VA. L. REV. 717 (1984); Ronald J. Gilson & Reinier H. Kraakman, *The Mechanisms of Market Efficiency*, 70 VA. L. REV. 549 (1984). For views opposing mandatory disclosure, *see, e.g.,* Steven M. Davidoff & Claire A. Hill, *Limits of Disclosure*, 36 SEATTLE U. L. REV. 599 (2013); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L. J. 2359 (1998); Paul G. Mahoney, *Mandatory Disclosure as a Solution to Agency Problems*, 62 U. CHI. L. REV. 1047 (1995); Frank H. Easterbrook & Daniel R. Fischel, *Mandatory Disclosure and the Protection of Investors*, 70 VA. L. REV. 669 (1984); George J. Bentson, *Required Disclosure and the Stock Market: An Evaluation of the Securities Exchange Act of 1934,* 63 AM. ECON. REV. 132 (1973); George J. Stigler, *Public Regulation of the Securities Markets*, 37 J. BUS. 117 (1964).

[35] *See, e.g.,* Romano*, supra* note 34; Robert E. Verrecchia, *Discretionary Disclosure*, 5 J. ACCT. & ECON. 179 (1983). *Cf.* Sanford J. Grossman, *The Informational Role of Warranties and Private Disclosure About Product Quality*, 24 J. L. & ECON. 461 (1981); S.J. Grossman & O.D. Hart, *Disclosure laws and Takeover Bids*, 35 J. FIN. 323 (1980).

[36] This assumption might be questioned on the basis that the desire to withhold information for other reasons (e.g., fear of competition) may outweigh the desire to obtain the best price for the company's securities in the capital markets (i.e., the costs of disclosure may outweigh the benefits of higher share prices and lower costs of capital). *See, e.g.,* Ferrell, *supra* note 34 at 88-99.

[37] *See* Fox, *Securities Disclosure in a Globalizing Market*, *supra* note 34 at 2562-69; Merritt B. Fox et al., *Law, Share Price Accuracy and Economic Performance: The New Evidence*, 102 MICH. L. REV. 331 (2003).

[38] *See* Ferrell, *supra,* note 34.

the costs of establishing rules and compliance costs.[39] If regulators insist on issuing standards themselves or relying on highly regulated standard-setting bodies, such as exchanges or self-regulatory organizations, they may frustrate innovation in the development and dissemination of information.[40] This may be particularly true when unregulated private standard-setting bodies have developed significant expertise in the substance of the disclosures that are under consideration, as is the case for sustainability disclosures.[41] To the extent that regulators rely on privately generated standards, however, it is important that they ensure reasonable public access to such standards and the promulgators' processes for establishing and modifying their standards.[42]

Currently, investor access to the sustainability information of U.S. public companies depends almost entirely on private ordering.[43] In a private ordering disclosure regime, companies may resist disclosing otherwise material information to the market due to concerns about the costs of producing the information, the impact of disclosure (of competitively sensitive information, for example) on their operations and other disincentives.[44] Information may also be disclosed in ways that make it difficult for investors to access, process and verify, decreasing the efficiency and fairness of the market.[45] As explained in more detail in Section II.B.1. below, the private ordering of sustainability disclosure suffers from these problems. Corporate sustainability disclosures tend to lack clarity, comparability and reliability and they are typically disclosed in a manner that makes them more difficult to acquire, process and verify, such as sustainability reports included on corporate CSR websites, rather than in annual reports filed with the SEC and posted on corporate investor relations websites.

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[39] Steven L. Schwarcz, *Private Ordering*, 97 NW. U. L. REV. 319, 320-21 (2002).

[40] Dombalagian, *supra*, note 30 at 730.

[41] Virginia Harper Ho, *Nonfinancial Risk Disclosure and the Costs of Private Ordering*, 55 AM. BUS. L. J. 407, 432 (2018).

[42] Dombalagian, *supra*, note 30 at 731 (citing the Administrative Conference of the United States, Recommendation 2011-5, Incorporation by Reference at 2 (December 8, 2011)).

[43] Harper Ho, *supra* note 41, at 410 (noting that investors obtain sustainability information primarily through voluntary sustainability reports produced by companies under reporting frameworks developed by private standard-setting bodies).

[44] *See, e.g.,* John C. Coffee, Jr., *Market Failure and the Economic Case for a Mandatory Disclosure System*, 70 Va. L. Rev. 717, 723-37 (1984); Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice Is Not Investor Empowerment*, 85 Va. L. Rev. 1335, 1343-46 (1999).

[45] *See* Gilson & Kraakman, *supra* note 12.

Regulators are not left with a binary choice between mandatory disclosure rules and private ordering of disclosure, however. They may also choose to engage in collaborative processes in which regulators and private parties work together to harness private ordering for regulatory ends.[46] The SEC has occasionally taken this approach, permitting private ordering to determine the substance of disclosure, subject always to anti-fraud rules, while establishing procedural rules that promote accessibility, comparability and reliability of the voluntarily disclosed information.[47] By permitting private ordering of substantive disclosure while keeping a watchful eye on the content of the disclosure and retaining the right to require modifications to the substance where necessary in the public interest, as the SEC has done with respect to quarterly earnings guidance, the SEC can decrease the costs to investors of acquiring, processing and verifying such information through access, transparency and standardization while minimizing the cost to issuers of providing such information.[48] Thus, this approach to regulation can maximize the efficiency of the markets in situations where neither private ordering nor mandatory disclosure can promote peak efficiency due to excessive costs for either issuers (the producers of information) or investors (the consumers of information). The costs of production, processing and verifying corporate disclosures are likely to be particularly high when there is a lack of consensus about which measures are most material to investors, as is the case with sustainability disclosures.

II. THE SUSTAINABILITY DISCLOSURE DEBATE

A. Confounding Factors: Multiple Standards and Materiality Questions

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[46] *See, generally,* Cary Coglianese and Evan Mendelson, *Meta-Regulation and Self-Regulation*, in THE OXFORD HANDBOOK OF Regulation (Robert Baldwin, et al., eds.) 146 (2010); Chris Ansell and Alison Gash, *Collaborative Governance in Theory and Practice*, 18, J. OF PUB. ADMIN. RESEARCH & THEORY 543 (2007); Orly Lobel, *The Renew Deal: The Fall of Regulation and the Rise of Governance in Contemporary Legal Thought,* MINN. L. REV. 342 (2004); Cary Coglianese and David Lazer, *Management-Based Regulation: Prescribing Private Management to Achieve Public Goals*, 37 LAW & SOC. REV. 691 (2003); Jody Freeman, *The Private Role in Public Governance,* 75 N.Y.U. L. REV.543 (2000); Jody Freeman, *Collaborative Governance in the Administrative State*, 45 UCLA L. Rev. 1 (1997); Paul Mahoney, *The Exchange as Regulator*, 83 Va. L. Rev. 1453 (1997).

[47] *See* Section III, *infra*.

[48] For instance, after choosing to make quarterly earnings guidance voluntary instead of mandatory, the SEC subsequently issued rules for the use of Non-GAAP financial measures to ensure clarity, comparability and reliability in the use of such measures. *See* Regulation G, 17 C.F.R. §244, 68 Fed. Reg. 4832 (Jan. 30, 2003). For additional discussion of the SEC's action on earnings releases*, see* Section III.C., *infra.*

1. Multiplicity of Standards

Sustainability, or ESG, reporting standards have been established by a plethora of ESG information-gathering organizations to promote transparency and consistency in voluntary sustainability reports, but the variety of frameworks is itself a challenge to promoting comparability as different corporations use different frameworks.[49] The different reporting frameworks have different purposes and were established for different audiences, which creates confusion and raises questions about materiality when applied to SEC reporting. The early-movers in the space, such as CDP and GRI, were established to seek information from corporations about issues of interest to activists, consumers and other stakeholders other than investors, and seek information that was not initially of interest to investors other than social-purpose investors, such as volumes of greenhouse gas

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[49] Some of the most prominent ESG standard-setting organizations include:

- **CDP (previously the Carbon Disclosure Project)**(established in 2000), an international non-profit that sends annual questionnaires to companies and investors and scores organizations on environmental risks and opportunities related to climate change, water security, and deforestation.
- **Global Reporting Initiative (GRI)**(established in 1997), an international nonprofit that created the first international guidelines for sustainability reporting in 2000, under which companies determine independently which GRI standards to apply to their disclosures.
- **International Integrated Reporting Council (IIRC)**(established in 2010), an international nonprofit that has worked to develop an International Integrated Reporting Framework that elicits from companies material information strategy, governance, and performance in a concise and comparable format intended to be integrated with financial reporting prepared pursuant to GAAP or IFRS.
- **Sustainability Accounting Standards Board (SASB)**(established in 2011), a U.S. nonprofit that developed a voluntary ESG reporting framework in 2018 consisting of industry-specific sustainability accounting standards for 77 industries.
- **Task Force on Climate-related Financial Disclosures (TCFD)**(established 2015), a multi-national inter-governmental organization established by the Financial Stability Board to make recommendations to improve voluntary climate change disclosures, which released a framework in 2017 to help companies evaluate and disclose financial risks posed to their business by climate change.
- **United Nations Global Compact** (established in 2000), a non-binding U.N. agreement that encourages participating companies to adopt sustainable and socially responsible policies consistent with "Ten Principles" regarding human rights, labor, environment, and anticorruption, and to report on their implementation.

GOVERNMENT ACCOUNTABILITY OFFICE, PUBLIC COMPANIES: DISCLOSURE OF ENVIRONMENTAL, SOCIAL AND GOVERNANCE FACTORS AND OPTIONS TO ENHANCE THEM 6 (July 2020)[hereinafter, "GAO 2020 Report"], https://www.gao.gov/products/gao-20-530.

emissions and supply-chain sources. More recently established standard-setters, such as SASB and IIRC, seek information that is tailored to be material to the financial condition and results of operations of corporations on an industry-by-industry basis, such as emissions per kilowatt hour of electricity delivered by a company in the electric utility industry. Thus, there are a broad variety of ESG factors being measured by different organizations, some of which may be material to investors, and others of which may not be.

The variety of different ESG reporting frameworks means that there is no agreed set of ESG factors, with agreed standards for measuring them, that all companies can use as standards for disclosure, as there are for financial statements. As a result of the large number of organizations seeking ESG information for different purposes, companies are flooded with requests for similar information in slightly different formats from numerous organizations every year. Companies are inundated with requests for ESG information and those who disregard or do not fully complete questionnaires risk low ESG ratings which can have adverse impacts on their stock price and access to capital.[50] Keeping up with all of the requests is a significant cost and companies can be confused about which information they should be disclosing.

The ESG information-gathering organizations are aware of this challenge. In order to ameliorate the burden on companies, some standard-setters are beginning to cooperate, rather than competing with one other, to establish a standard set of measures, based on industry, pursuant to which all companies can make sustainability disclosure, or to explain how companies can respond to multiple ESG frameworks in an efficient manner.[51] SASB and the Climate Disclosures Standards Board, an ESG

[50] IAC 2020 at 4-5. The IAC also noted that without a single source of disclosure standards for ESG matters small and midcap companies are disadvantaged in the market for capital compared to larger issuers, who are better able to keep up with the duplicative disclosure demands from multiple ESG standard setters.

[51] In July 2020, GRI and SASB announced their intent to create materials to explain to issuers and investors how their respective reporting systems, which are designed to fulfill different purposes and are based on different approaches to materiality, can be used concurrently in one report. SASB, GRI, *Promoting Clarity and Compatibility in the Sustainability Landscape* (July 12, 2020), https://www.sasb.org/blog/promoting-clarity-and-compatibility-in-the-sustainability-landscape-gri-and-sasb-announce-collaboration/. The press release notes that SASB's industry-specific standards identify the subset of sustainability-related risks and opportunities most likely to affect a company's financial condition (e.g., its balance sheet), operating performance (e.g., its income statement) or risk profile (e.g., its market valuation and cost of capital), while the GRI Standards focus on the economic, environmental and social impacts of a company, and hence its contributions –

standard-setting body created to guide and harmonize the gathering of ESG information from corporations, issued a joint guide for implementation of the TCFD recommendations using the SASB standards in 2019.[52] In January 2020, the World Economic Forum's International Business Council promulgated a consultation draft of core and expanded ESG disclosures pulling together metrics from existing reporting standards to promote consistent reporting of sustainability matters.[53]

As ESG has become an increasingly popular investing theme, a large number of organizations have been established to process the information disclosed by corporations pursuant to the standards established by the information-gathering organizations, to create either ESG indexes, pursuant to which corporations are scored on their sustainability pursuant to ESG factors chosen by the indexer, or investment funds, pursuant to which corporations with appropriate ESG scores established by either the ESG indexers or the asset manager of the fund are included in the fund to satisfy the investor demand for ESG investment opportunities.

ESG indexes and funds are subject to criticism because at least some of the factors they use require subjective, rather than objective, judgments, and because "E", "S" and "G" factors for any given company may vary.[54] If some factors are "good" according to the chosen ESG standards, and other factors are "bad", according to the chosen ESG standards, there is a high level of subjectivity inherent in the weighting given to the different factors in establishing a final ESG score. The result of these multiple subjective judgments and use of different factors by different indexers and asset managers is that the same company may be both scored dramatically differently by different indexers and asset managers, and may be scored inconsistently by the same indexer or asset manager in different years.[55]

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positive or negative – towards sustainable development and provide both the framework and supporting standards for a wide range of sustainability topics, and are aligned with international instruments for responsible business behavior.

[52] CLIMATE DISCLOSURE STANDARDS BOARD AND SUSTAINABILITY ACCOUNTING STANDARDS BOARD, TCFD IMPLEMENTATION GUIDE: USING SASB STANDARDS AND THE CDSB FRAMEWORK TO ENHANCE CLIMATE-RELATED FINANCIAL DISCLOSURES IN MAINSTREAM REPORTING (2019).

[53] WORLD ECONOMIC FORUM, TOWARD COMMON METRICS AND CONSISTENT REPORTING OF SUSTAINABLE VALUE CREATION (January 2020). The consultation draft was prepared in collaboration with the big four accounting firms – Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers.

[54] *See, e.g.,* Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and social Conscience: The Law and Economics of ESG Investing by a Trustee*, 72 STAN. L. REV. 381, 430-36 (2020).

[55] State Street Global Advisors reviewed the ESG scores issued by 30 ESG index

Identification of relevant factors, assessing whether they are bad or good from an investor's perspective in the case of each firm and determining how much weight to give to each factor are all highly subjective and make empirical valuation of ESG investing strategies challenging and contextual. SEC Commissioner Hester Pierce has argued that many ESG factors cannot be reduced to a standardizable score.[56] As a result of these issues with ESG scoring, the value of ESG as an investment proposition has been questioned.

2. Materiality Questions

Information is material to investors if ''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".[57] More succinctly, a fact is material if there is a substantial likelihood that a reasonable investor would consider it important in deciding how to vote or whether to trade a security.[58] Thus materiality depends on the current information in the market and how any new or omitted information changes reasonable investors' perceptions of a company's value or management in connection with trading or voting their shares.[59]

At least in part due to the legacy of ESG information gathering by organizations interested in social policy issues, as opposed to investment returns, there is significant debate at the SEC and elsewhere about the

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providers and found significant discrepancies in how they scored companies, noting that different methodologies for sourcing, research and scoring ESG factors led to significant variation in the scores. Rakhi Kumar and Ali Weiner, STATE STREET GLOBAL ADVISORS, THE ESG DATA CHALLENGE (March 2019). SSGA noted that when investors use the ESG scores of a particular provider for investment decisions, they are effectively adopting the ESG investment philosophy of that data provider in terms of data acquisition, materiality, and aggregation and weighting of ESG data. The scores given by MSCI and Sustainalytics (now a division of Morningstar), two of the largest ESG scoring providers, for instance, correlated in only 53% of cases. *See also,* Schanzenbach & Sitkoff, *supra* note 54, at 430-433 (citing differing evaluations of Tesla by different ESG rating firms (stock index creators FTSE and MSCI) as evidence of the inconsistency and subjectivity of such ratings).

[56] Hester M. Peirce, Comm'r, SEC, Scarlet Letters: Remarks Before the American Enterprise Institute (June 18, 2019).

[57] *TSC Industries, Inc.* v. *Northway, Inc.,* 426 U.S. 438, 448–449 (1976). *See also Basic* v. *Levinson,* 485 U.S. 224, 231 (1988). In *Basic* v. *Levinson,* the U.S. Supreme Court ''expressly adopt[ed] the *TSC Industries* standard of materiality for the § 10(b) and Rule 10b–5 context.'' *Id.* at 232.

[58] *TSC Industries*, *supra* note 57 at 449, *Basic*, *supra* note 57 at 232.

[59] Petition for Rulemaking, *supra* note 15 at 6.

materiality of sustainability disclosures.[60] The multiplicity of ESG factors sought from companies, some of which are not designed with investors in mind, makes evaluating the materiality of ESG information more complex. The subjectivity of some of the factors makes them more controversial from a materiality perspective.[61] Fundamentally, some ESG factors may be material to investors, while others may not be, so when discussing the materiality of ESG factors, or sustainability disclosures, it is important to draw with precision, not with a broad brush.

Although some observers remain skeptical, there is an emerging consensus among investors and academics that sustainability information is material to investment decisions. An increasing number of investors are stating publicly that sustainability metrics are important factors in their investment analyses. They argue, for example, that investment portfolios that fully integrate sustainability metrics perform better than those that do not.[62] The head of ESG investing for the Harvard Management Company has opined that despite some mainstream skepticism, more than forty years of academic and empirical evidence suggests that ESG integration in the investment process can lead to better risk-adjusted returns and long-term value creation.[63] He also noted that most investment management executives believe the right ESG strategy can provide a positive impact on long-term investment performance.[64] Recent reports from Morningstar and

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[60] *See infra*, Section II.D.

[61] It is important, however, to make a distinction, in this regard, between ESG factors and ESG ratings. ESG factors are issues as to which a company is requested to make disclosure, and can be received by an investor as is, without the bias of any third parties. ESG ratings, on the other hand, involve the bias of the rater, so subjectivity is of greater concern, since the rater, or indexer, may have different biases than a particular investor, which the investor will not know unless the rater/indexer carefully discloses the bases for all of its judgments of different ESG factors.

[62] Integration is different from screening. An ESG integration strategy incorporates information about ESG factors in valuing companies or selects companies for inclusion in a portfolio based in part on high performance on ESG factors. A screening strategy excludes companies with low-ESG profiles, sometimes entire industries, from a portfolio. Integration is perceived as more successful than screening at producing higher risk-adjusted returns than market indices. *See, e.g.,* Schanzenbach & Sitkoff, *supra* note 54, at 439-441; Michael Cappucci, *The ESG Integration Paradox*, 30 J. OF APPLIED CORP. FIN. 22 (2018).

[63] Cappucci, *supra* note 62 (*citing* Robert G. Eccles and Mirtha D. Kastrapeli, *The Investing Enlightenment*, STATE STREET (2017)).

[64] *Id*. *See also* Emirhan Ilhan, et al., *Institutional Investors' Views and Preferences on Climate Risk Disclosure*, EUROPEAN CORPORATE GOVERNANCE INSTITUTE, WORKING PAPER NO. 661/2020 (Feb. 2020), https://ecgi.global/sites/default/files/working_papers/documents/ilhankreugersautnerstarksfinal.pdf ("51% of respondents believe that climate risk reporting is as important as

others seem to bear this out, showing that ESG funds are outperforming competitors and the market in recent years, including during the recent pandemic downturn, and such funds are attracting record inflows of investment dollars.[65]

Investors and other market observers describe a variety of reasons for the value of incorporating sustainability factors into investment decisions. Bank of America Merrill Lynch concluded in 2017 that sustainability factors are "strong indicators of future volatility, earnings risk, price declines and bankruptcies."[66] In May 2020, the Government Accountability Office reported that fourteen large institutional investors it interviewed agreed that corporate attention to ESG issues can have a positive effect on a company's long-term value and they seek ESG information to better understand the risks that could affect companies' long-term value.[67] BofA even suggested that sustainability factors could be more important that traditional measures of value.[68] A significant portion of investors who use ESG factors in investment decisions report that they believe positive ESG

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traditional financial reporting, and almost one-third considers it to be more important."); BLACKROCK, TOWARD A COMMON LANGUAGE FOR SUSTAINABLE INVESTMENT (Jan. 2020) ("Our investment conviction is that sustainability-integrated portfolios – composed of more sustainable building-block products – can provide better risk-adjusted returns to investors. With the impact of sustainability on investment returns increasing, we believe that sustainable investment will be a critical foundation for client portfolios going forward.").

[65] See, e.g., *Sustainable Funds Weather Downturns Better Than Peers*, MORNINGSTAR.COM (June 15, 2020), https://www.morningstar.com/articles/988114/sustainable-funds-weather-downturns-better-than-peers; *ESG Funds Setting a Record Pace for Launches in 2020*, MORNINGSTAR.COM (June 24, 2020), https://www.morningstar.com/articles/989209/esg-funds-setting-a-record-pace-for-launches-in-2020; *Majority of ESG Funds Outperform Wider Market over 10 Years*, FT.COM (June 30, 2020), https://www.ft.com/content/733ee6ff-446e-4f8b-86b2-19ef42da3824; Oliver Schutzmann, *ESG stocks prove their value during Covid-19 crisis*, IR Magazine (Apr. 3, 2020); UBS ASSET MANAGEMENT – GLOBAL, "HOW HAS COVID-19 IMPACTED ESG INVESTING?" (finding that "higher rated ESG funds fared better in the Covid-19 induced market downturn"), *available at*, https://www.ubs.com/global/en/asset-management/insights/panorama/mid-year/2020/covid-19-impacted-esg-investing.html.

[66] Bank of American Merrill Lynch, *Equity Strategy Focus Point—ESG Part II: A Deeper Dive* (June 15, 2017).

[67] GAO 2020 Report, *supra* note 49, at 9.

[68] *Id*. ("Prior to our work on ESG, we found scant evidence of fundamental measures reliably predicting earnings quality. If anything, high quality stocks based on measures like Return on Equity (ROE) or earnings stability tended to deteriorate in quality, and low quality stocks tended to improve just on the principle of mean reversion. But ESG appears to isolate non-fundamental attributes that have real earnings impact: these attributes have been a better signal of future earnings volatility than any other measure we have found.").

scores are a proxy for good management.[69] Goldman Sachs asserted in 2018 that "integrating ESG factors allows for greater insight into intangible factors such as culture, operational excellence and risk that can improve investment outcomes."[70]

Recent academic studies support the conclusions of institutional investors, showing that portfolios integrating sustainability metrics perform better than those that do not**.** One study found that ESG portfolios focused on several ESG criteria, including best-in-class firms identified by the data firm Sustainalytics, outperformed a variety of global indices with lower volatility and risk.[71] Other studies are showing better performance at the firm level as opposed to investment portfolios. A seminal study found that firms with good ratings on material ESG issues as measured according to SASB metrics outperformed firms with poor ratings.[72] In 2018, the Government Accountability Office conducted a review of academic research published in peer reviewed academic journals between 2012 and 2017 on the performance of investments incorporating ESG factors and found that the vast majority of the investment scenarios studied in the literature resulted in a neutral or positive relationship between the use of ESG information and financial returns.[73]

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[69] CFA INST., ENVIRONMENTAL, SOCIAL AND GOVERNANCE (ESG) SURVEY 11 (2017)(41% of investors applying ESG principles in 2017 consider ESG a proxy for management quality). A representative of State Street Global Advisors observed that, "[t]here is an explosion of data showing strong ESG performance equals better operating and stock performance." Ted Knuston, *ESG Metrics For Investors in Infancy, SEC Told*, FORBES (December 14, 2018, 10:55 a.m.)(quoting Jennifer Bender, Research Executive at State Street Global Advisors), https://www.forbes.com/sites/tedknutson/2018/12/14/esg-corporate-performance-metrics-in-infancy-sec-told/#1884977f5a8b.

[70] Goldman Sachs Equity Research, *GS Sustain ESG Series: A Revolution Rising-From Low Chatter to Loud Roar [Redacted]*, 23 April 2018.

[71] Tim Verheyden, Robert G. Eccles, and Andreas Feiner, *ESG for All? The Impact of ESG Screening on Return, Risk, and Diversification*, 28 J. OF APP. CORP. FIN. 47 (2016).

[72] Mozaffar Khan and George Serafeim, and Aaron S. Yoon, *Corporate Sustainability: First Evidence on Materiality*, 91 The Acct. Rev. 1697-1724 (2016)(finding that firms that score high on sustainability factors considered material under the SASB rubric outperform lower scoring firms on financial performance and stock returns); George Serafeim, *Public Sentiment and the Price of Corporate Sustainability*, 76 FINANCIAL ANALYSTS J. 26 (2020)(" An ESG factor long (short) on companies with superior (inferior) sustainability performance and negative (positive) ESG sentiment momentum delivered significant positive alpha.").

[73] GOVERNMENT ACCOUNTABILITY OFFICE, RETIREMENT PLAN INVESTING: CLEARER INFORMATION ON CONSIDERATION OF ENVIRONMENTAL, SOCIAL AND GOVERNANCE FACTORS WOULD BE HELPFUL 7-8 (May 2018). The GAO report also refers to a 2015 meta-analysis that reported aggregate evidence from more than 2,000 empirical studies, which similarly found that 90 percent of the studies reported finding a neutral, positive or mixed relationship between incorporation of ESG factors in investment decisions and

B. The Corporate Response: Voluntary, not Mandatory

In response to the rising interest in ESG information from customers, employees, investors and other stakeholders, corporations around the world, including in the United States, have begun disclosing increasing amounts of information about sustainability issues related to their operations. While corporations in the United States have voluntarily responded to the requests for information from ESG information-gathering organizations such as CDP, GRI and SASB, however, they have been adamantly opposed to the establishment of mandatory sustainability disclosures by the SEC.

1. Voluntary Sustainability Reports

Based on pressure from investors and other stakeholders, the number of corporations reporting sustainability information voluntarily has increased dramatically in recent years. In 1993, 12% of the top 100 companies in the OECD countries (excluding Japan) published an environmental or social report.[74] As of 2017, 83% of the top 100 companies in the Americas published a corporate responsibility report, as did 77% of top 100 companies in Europe and 78% in Asia.[75] Among the largest 250 companies globally, reporting rates were 93%.[76] The number of public companies in the United States issuing annual sustainability reports has increased dramatically in the last decade. From 2011 to 2019, the percentage of S&P 500 companies publishing voluntary reports on sustainability matters increased from 20% to 90%.[77] However, the current disclosure landscape is market-driven and fragmented.[78]

Most corporate sustainability reports focus on multi-stakeholder issues, rather than the factors of greatest interest to investors. The GRI's

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portfolio performance. Gunnar Friede, Timo Busch, and Alexander Bassen, *ESG and Financial Performance: Aggregated Evidence from More than 2000 Empirical Studies*, 5 J. SUSTAINABLE FIN. & INVEST. (2015).

[74] *See* Ans Kolk, *A Decade of Sustainability Reporting: Developments and Significance*, 3 INT'L J. ENVIR. & SUSTAINABLE DEVELOPMENT 51, 52 Figure 1 (2004).

[75] KPMG, THE KPMG SURVEY OF CR REPORTING 2017, at 11, available *at* https://home.kpmg.com/content/dam/kpmg/campaigns/csr/pdf/CSR_Reporting_2017.pdf. KPMG is the most comprehensive source of data on ESG reporting by corporations. Petition for Rulemaking, *supra* note 15 at 9.

[76] *Id.*

[77] Governance & Accountability Inst., *supra* note 1.

[78] David A. Katz and Laura A. McIntosh, Wachtell, Lipton, Rosen & Katz, *Sustainability in the Spotlight*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Jan. 27, 2020), https://corpgov.law.harvard.edu/2020/01/27/sustainability-in-the-spotlight/.

framework for voluntary ESG reporting has emerged as the leading reporting system: 75% of the Global 250 use GRI as the basis for their corporate responsibility reporting.[79] Relatively few firms have adopted the rigorous line-item disclosures of sustainability information recommended on an industry-by-industry basis by the Sustainability Accounting Standards Board. Among S&P 500 firms, 51% reported using the GRI framework, which focuses on issues and metrics of interest from a social policy perspective, while only 14% reported using the SASB framework, which focuses on issues and metrics having a material impact on financial results and only 5% reported according to the framework established by the TCFD.[80] Academic studies of reporting under the GRI framework have, however, found issues with the quality of the disclosure.[81]

Investors are also dissatisfied with the current quality of sustainability reports.[82] According to a survey of 542 institutional asset owners and investment consultants in the U.S., Canada, Europe and Asia conducted by RBC Global Asset Management, fewer than 7% of investors are satisfied with the ESG reporting currently available to them.[83] The Council of Institutional Investors has noted that disclosures of ESG Risks too often consist of boilerplate risk identification without adequate discussion of how the risks apply to the individual registrant.[84] In its final report, the TCFD concluded that, "[e]vidence suggests that the lack of consistent information hinders investors and others from considering climate-related issues in their asset valuation and allocation processes."[85]

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[79] KPMG 2017 CR Survey at 28.

[80] G&A 2020 Flash Report

[81] *See also*, Virginia Harper Ho, *Nonfinancial Risk Disclosure and the Costs of Private Ordering*, 55 AM. BUS. L.J. 407, 407 (2018)(arguing that sustainability disclosure under private ordering "is inadequate for investment analysis" and calling for an SEC-mandated disclosure requirement).

[82] *See, e.g.,* STATE STREET GLOBAL ADVISORS, THE ESG DATA CHALLENGE (Mar. 2019) ("Asset owners and their investment managers seek solutions to the challenges posed by a lack of consistent, comparable, and material information. Investors increasingly view material ESG factors as being critical drivers of a company's ability to generate sustainable long-term performance. In turn, ESG data has increasing importance for investors' ability to allocate capital most effectively.").

[83] Cydney Posner, *Heat's on for climate change disclosure rules*, COOLEY PUBCO (October 4, 2018), https://cooleypubco.com/2018/10/04/climate-change-disclosure-petition/.

[84] Ken Bertsch, Exec. Dir., Council of Institutional Investors, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 7 (July 8, 2016)[hereinafter, "CII Letter"], http://www.blackrock.com/corporate/en-fi/literature/whitepaper/viewpoint-exploring-esg-a-practitioners-perspective-june-2016.pdf), https://www.sec.gov/comments/s7-06-16/s70616-49.pdf..

[85] TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES, FINAL REPORT:

In July 2020, the Government Accountability Office released a report commissioned by Senator Mark Warner reviewing the current state of ESG disclosure practices among U.S. public companies.[86] The report notes that some investors are dissatisfied with the quality and consistency of disclosure and most investors interviewed by the GAO are concerned that gaps and inconsistencies in companies' disclosures limit their usefulness and comparability.[87] The GAO reports that investors were dissatisfied with both qualitative and quantitative ESG disclosures. With respect to quantitative disclosures,

> [i]nvestors cited examples of inconsistencies […] that limit comparability, including comparability among companies that disclose on the same ESG topics. Specifically, investors described challenges such as the variety of different metrics that companies used to report on the same topics, unclear calculations, or changing methods for calculating a metric.[88]

The GAO's own review of company disclosures corroborated the investor perspective, finding several cases where companies used different definitions or calculations for the same topics over time.[89]

RECOMMENDATIONS OF THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES 1 (June 2017).

[86] GAO 2020 Report, *supra* note 49. To prepare its report, the GAO analyzed the disclosures of 32 large and midsize public companies on 33 ESG topics, including climate change, resource management, personnel management and other matters, interviewed 14 institutional investors (seven asset management firms and seven public pension funds), 18 public companies, and 13 market observers (including ESG standard-setting organizations), and reviewed existing studies regarding ESG disclosures.

[87] GAO 2020 Report, *supra* note 49, at 2, 9 – 13, 33 (companies use different metrics to report on the same topics, or different time periods for calculations – different base years, for example, when calculating their reduction in greenhouse gas emissions, limiting comparability); *see also*, WORLD ECONOMIC FORUM, TOWARD COMMON METRICS AND CONSISTENT REPORTING OF SUSTAINABLE VALUE CREATION (JANUARY 2020).

[88] GAO 2020 Report, *supra* note 49, at 12. In a 2016 report reviewing disclosure of climate risks by the top ten firms by revenue in 72 industries (a total of 637 public companies), the SASB noted that while about 40% of disclosures relevant to climate change included boilerplate language regarding climate risks, fewer than 20% of disclosures included quantitative metrics, less than 20% were narrowly tailored to a particular company and 27% had no mention of climate risks at all. SUSTAINABILITY ACCOUNTING STANDARDS BOARD, CLIMATE RISK TECHNICAL BULLETIN, TECHNICAL BULLETIN #:TB001 – 10182016 85-87 (2016).

[89] David M. Silk, David B. Anders and Sebastian Niles, Wachtell, Lipton, Rosen & Katz, *GAO Report Highlights Dearth of ESG Disclosure*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (July 17, 2020),

As a result of their dissatisfaction with the disclosures currently produced through private-ordering of voluntary sustainability reports, investors are calling for a standardized ESG disclosure framework to facilitate the disclosure of decision-useful information.[90] In July 2017, 390 investors with more than $22 trillion in assets under management wrote to the leaders of the G20, calling on them to "evolve the financial frameworks required to improve the availability, reliability and comparability of climate-related information."[91]

2. Corporate Opposition to Mandatory Disclosure Rules

While large numbers of companies are preparing voluntary sustainability reports, corporate executives and their representatives have consistently resisted mandatory imposition of sustainability reporting obligations in the United States. The most frequent reasons raised by corporations for opposing mandatory sustainability disclosure rules are lack of materiality, cost of providing the information and liability risk.[92]

U.S. public companies, industry and trade associations and their legal counsel often argue that sustainability disclosures pander to special interests

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https://corpgov.law.harvard.edu/2020/07/17/gao-report-highlights-dearth-of-esg-disclosure/.

[90] David M. Silk, David B. Anders and Sebastian Niles, Wachtell, Lipton, Rosen & Katz, *GAO Report Highlights Dearth of ESG Disclosure*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (July 17, 2020), https://corpgov.law.harvard.edu/2020/07/17/gao-report-highlights-dearth-of-esg-disclosure/.

[91] https://www.ceres.org/news-center/press-releases/over-200-global-investors-urge-g7-stand-paris-agreement-and-drive-its.

[92] Tom Reisenberg and Elisse Walter, Sustainability Accounting Standards Board, *Sustainability and Liability Risk*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (February 19, 2018), https://corpgov.law.harvard.edu/2018/02/19/sustainability-and-liability-risk/. SASB reports that the three reasons corporate executives most frequently espouse for avoiding sustainability disclosures under the SASB framework are irrelevance to investors, cost of providing the information and legal liability risk. The AICPA has enumerated a number of other reasons that it is more convenient for companies to separate their SEC reporting and their sustainability reporting, including the ability to include information appealing to a variety of stakeholders, some of which may not be of interest to investors, in their sustainability reports. *See* Barry C. Melancon, President and CEO, American Institute of CPAs, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 3-4 (July 20, 2016)[hereinafter "AICPA Letter"], https://www.sec.gov/comments/s7-06-16/s70616-194.pdf.

and are not material to investment decisions.[93] In response to the Reg S-K Concept Release, the U.S. Chamber of Commerce argued that materiality is seen through the eyes of the *reasonable investor*, not "the needs of an investor that is not representative of investors more broadly or that is looking to advance some special interest."[94] The Business Roundtable, an association of the chief executive officers of U.S. companies representing almost one-fifth of the total value of the U.S. stock markets, echoed the comments of the Chamber, arguing that interest groups hope that disclosure rules will change business behavior.[95] The Attorneys General of 14 states suing the federal government to stop implementation of the Environmental Protection Agency's Clean Power Plan sent the SEC a letter in response to the Reg S-K Concept Release encouraging the regulator to "reject the

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[93] *See, e.g.,* Richard F. McMahon, Jr., V.P., Edison Electric Institute, and Patrick J. Migliaccio, Chairman, American Gas Association Accounting Advisory Council, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 7 (July 21, 2016) [hereinafter, "EEI-AGA Letter"](arguing that materiality is focused on understanding registrants' *financial* information and the existing disclosure framework is sufficiently robust to encompass any disclosures related to sustainability issues), https://www.sec.gov/comments/s7-06-16/s70616-241.pdf. *See also*, Brendan Williams, Exec. V. P., American Fuel & Petrochemical Manufacturers, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 5 (July 21, 2016), https://www.sec.gov/comments/s7-06-16/s70616-282.pdf.

[94] Tom Quaadman, Sr.V.P., Center for Capital Markets Competitiveness, U.S. Chamber of Commerce, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 4 (July 20, 2016) [hereinafter, "Chamber of Commerce Letter"], https://www.sec.gov/comments/s7-06-16/s70616-173.pdf. The Chamber elaborated by arguing that,

> Each of these approaches to ESG disclosure expands the scope of materiality under the federal securities laws, such as by considering disclosure from the viewpoint of a wide range of stakeholders other than the reasonable investor, by using disclosure to advance social or political goals outside the SEC's mission, or by developing specific disclosure metrics that go well beyond what the courts or the SEC has endorsed in assessing materiality.

Id. at 17. *See also*, John Hayes, Chair, Corporate Governance Committee, Business Roundtable, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 4-5 (July 20, 2016), [hereinafter, "Business Roundtable Letter"], https://www.sec.gov/comments/s7-06-16/s70616-208.pdf; *See also*, David S. Rosenthal, V.P. and Controller, Exxon Mobil Corporation, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 2 (August 9, 2016), https://www.sec.gov/comments/s7-06-16/s70616-355.pdf. Corporate representatives frequently refer to the SEC's conflict mineral rules, mandated by the Dodd-Frank act, as an example of disclosure requirements of interest to society but not investors. *See, e.g.,* Business Roundtable Letter, *supra*, at 5.

[95] Business Roundtable Letter, *supra* note 94, at 3 (noting that many interest groups have sought changes in the SEC's disclosure rules because the rules influence the behavior of the nation's businesses, citing Securities Act Release No. 5627 (October 14, 1975)).

invitation to allow itself to be used as a tool to promote [activist] special interests".[96]

Two corollaries of the irrelevance argument are the "information overload" argument and the agency competence argument. The information overload argument posits that too much information adversely affects the value of disclosure to investors by obscuring material information with mandatory disclosures that are not useful.[97] This argument appears to be based on the Supreme Court's statement in *TSC Industries v. Northway*, that "[m]anagement's fear of exposing itself to substantial liability may cause it simply to bury the shareholders in an avalanche of trivial information – a result that is hardly conducive to informed decision-making."[98] Proponents of this view note that the audience for sustainability information is much broader than the audience for SEC filings and sustainability reports include information about many matters of little or no interest to investors.[99]

Opponents of mandatory sustainability disclosures also assert that sustainability disclosures are beyond the SEC's mandate as an organization dedicated to investor protection, fair markets and capital formation. They argue that given its history as a capital markets regulator the SEC is not

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[96] Scott Pruitt, et al., (July 21, 2016), https://www.sec.gov/comments/s7-06-16/s70616-289.pdf. The letter, signed by Scott Pruitt, then Attorney General of Oklahoma, was also signed by the AGs of Alabama, Arizona, Arkansas, Florida, Georgia, Michigan, Montana, Nebraska, Nevada, South Carolina, Texas, Utah and West Virginia, all of whom were members of the Republican Party. Among other things, the letter states:

> Rather, the push for new mandatory [climate change] disclosures is transparently a part of a no-holds-barred approach to destroy any person, institution, or company linked with greenhouse gas emission-in this instance, by attempting to politicize the U.S. securities laws. In hopes that such disclosures might confuse investors into believing that they are taking serious financial risk by investing in companies that might impact or be impacted by climate change, activists seek to promote divestment from these politically-disfavored companies and, "[a]lthough the impact of divestment on share prices may be relatively small, the reputational damage can have serious financial consequences."

Id. at 2 (*quoting* THE GUARDIAN, *A beginner's guide to fossil fuel divestment*, (https://www.theguardian.com/environment/2015/jun/23/a-beginners-guide-to-fossil-fueldivestment).

[97] Chamber of Commerce Letter, *supra* note 94 at 3.

[98] *See id.*, *supra* note 94 at 4 (*quoting TSC Industries v. Northway*, *supra* note 57 at 448-49); Business Roundtable Letter, *supra* note 94, at 2 (same).

[99] *See, e.g.,* EEI-AGA Letter, *supra* note 93 at 9 (arguing that sustainability reports include information of interest to stakeholders, but not investors, such as a company's policies, its practices and how they have changed over time, detailed information relevant to development or modification of public policy initiatives, and how an entity's activities impact a local community).

well-placed to resolve difficult political or social issues such as supply chain management, climate change, labor relations, the political process and foreign affairs, and that responding to calls for disclosure in these areas would threaten the agency's reputation.[100] The U.S. Chamber of Commerce stated that,

> The objective of many calling for new public company ESG disclosures is primarily to obtain some social impact or achieve a political goal. These goals, if met, would in many cases contribute to an environment that makes it more difficult for businesses to innovate, compete and grow.[101]

Given the burgeoning empirical and testimonial evidence from investors and academics that sustainability information is material to investment decisions of all investors, not just a niche of ethically oriented sustainable or impact investors,[102] arguments that sustainability disclosure is immaterial and mandating it would constitute pandering to special interests are unpersuasive, but they retain rhetorical power among legislators and regulators.[103] However, these are not the only arguments opponents of mandatory sustainability disclosure make: they are also concerned about cost and liability risk.

Several the companies and business associations responding to the Reg S-K Concept Release argued that mandating sustainability disclosures would impose significant additional costs on public companies. Some of them argued that requiring sustainability reports in SEC filings would add additional cost in an area already resource-constrained and busy responding to many other sustainability disclosure initiatives, such as GRI.[104] The SEC acknowledged in the concept release that mandating sustainability disclosures could impose significant additional costs on registrants.[105] The issue of costs has also been acknowledged by corporate counsel and

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[100] Chamber of Commerce Letter, *supra* note 94 at 19. *See also* Michael Labriola, Wilson Sonsini Goodrich & Rosati, 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/s70616-256.pdf.

[101] Chamber of Commerce Letter, *supra* note 94 at 18.

[102] *See supra* Section II.A.2.

[103] *See infra*, remarks of SEC Commissioners.

[104] EEI-AGA Letter, *supra* note 93 at 9. *See also*, Exxon Mobil Letter, *supra* note 94 at 1; Christina Crooks, Dir., Tax Policy, National Association of Manufacturers, 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/s70616-201.pdf.

[105] Reg S-K Concept Release, *supra* note 2 at 23972 n. 697 and accompanying text.

investors as a significant impediment to corporate acceptance of sustainability reporting obligations.[106]

Companies are also concerned about liability for sustainability disclosures.[107] There has been an increase in shareholder derivative suits and regulator lawsuits in recent years alleging fraud in connection with misstatements in or omission of sustainability disclosures.[108] Courts are less likely to dismiss cases alleging misrepresentations or omissions in sustainability disclosures if they occur, or should have occurred, in formal securities filings.[109] Thus, the prospect of incorporating sustainability disclosures into annual reports and other SEC filings is daunting. One reason for the vagueness of many sustainability disclosures may be a desire to avoid liability. Companies can escape liability, particularly for disclosures outside SEC filings, if they use aspirational language, often referred to as "puffery", rather than sharing facts.[110]

The Sustainability Accounting Standards Board has been told by issuers

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[106] SUSTAINABLE ACCOUNTING STANDARDS BOARD, HARVARD LAW SCHOOL, LEGAL ROUNDTABLE ON EMERGING ISSUES RELATED TO SUSTAINABILITY DISCLOSURE 17 (November 2017)[hereinafter, "SASB Legal Roundtable"].

[107] *See, e.g.,* Davis Polk & Wardwell, L.L.P., Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K (July 22, 2016), https://www.sec.gov/comments/s7-06-16/s70616-313.pdf ("registrants generally limit their voluntary forward-looking disclosure to earnings press releases, quarterly calls or other investor presentations that are 'furnished' with the Commission under Form 8-K rather than in 'filed' period or current reports in response to the heightened litigation risk associated with [filed] documents"); Martin Lipton, David M. Silk, and David B. Andrews, Wachtell, Lipton, Rosen & Katz, *ESG Disclosures and Litigation Concerns* HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (April 7, 2020), *available at*: https://corpgov.law.harvard.edu/2020/04/07/esg-disclosures-and-litigation-concerns/; Connor Kuratek (March & McLennan Companies, Inc.) and Joseph A. Hall and Betty M. Huber (Davis, Polk & Wardwell LLP), *Legal Liability for ESG Disclosures*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (August 3, 2020), *available at*: https://corpgov.law.harvard.edu/2020/08/03/legal-liability-for-esg-disclosures/.

[108] Lisa Benjamin, *The Road to Paris Runs through Delaware: Climate Litigation and Directors' Duties,* 2020 Utah L. Rev. 313 (2020); Caitlin M. Ajax & Diane Straus, *Corporate Sustainability Disclosures in American Case Law: Purposeful or Mere "Puffery"?*, 45 ECOLOGY L. Q. 703 (2019)(finding that whether disclosures are affirmative statements of fact or aspirational promises is most outcome determinative in disclosure fraud litigation regarding sustainability disclosures). *See also,* Sara K. Orr and Bart J. Kempf, *Voluntary Sustainability Disclosure and Emerging Litigation*, AMERICAN BAR ASSOCIATION, SECTION OF ENVIRONMENT, ENERGY AND RESOURCES, CLIMATE CHANGE, SUSTAINABLE DEVELOPMENT AND ECOSYSTEMS COMMITTEE NEWSLETTER, Vol. 19, No. 1 (November 2015).

[109] Ajax and Straus, *supra* note 108, at 706.

[110] *Id. See also*, SASB Legal Roundtable, *supra* note 106 at 12.

that one of the main stumbling blocks to the use of its sustainability metrics in disclosures is the potential liability risk, particularly if the standards were to be used to make disclosures in filings with the SEC.[111] Because of the liability risks, companies have been advised by their lawyers not to disclose any more than what is required by law, in order to mitigate litigation risk.[112] The risk of strict liability under Section 11 of the Securities Act, in particular, is a good reason to keep sustainability disclosures out of documents incorporated by reference in registration statements, such as Annual Reports on Form 10-K.[113] The risk of additional sources of liability lead companies to resist mandatory sustainability disclosures, particularly disclosure of line-item sustainability metrics.

C. Investor Calls for Mandatory Disclosure

As noted above, institutional investors have been publicly embracing the value of incorporating ESG considerations in investment analyses in recent years.[114] The investor interest in sustainability disclosure may be traced in part to the U.N. Principles for Responsible Investment, launched by U.N. Secretary-General Kofi Annan and a group of the world's largest institutional investors in 2006 to promote principles for a sustainable global financial system.[115] Signatories of the principles agree to incorporate ESG issues into investment analysis and decision-making processes and to seek appropriate disclosure on ESG issues by the entities in which they invest, among other things.[116] Presently, the PRI has more than 2900 investor and asset manager signatories, holding more than $100 trillion in assets under management, representing the majority of the world's professionally managed investments.[117] Another important impetus for investor interest in

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[111] *Id.* at 1, 7, 10, 12, 15.

[112] Thomas Reisenberg, *Top 10 Sustainability Developments of 2018*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (March 7, 2019). *See also*, SOCIETY FOR CORPORATE GOVERNANCE AND GIBSON, DUNN & CRUTCHER LLP, LEGAL RISKS AND ESG DISCLOSURES: WHAT CORPORATE SECRETARIES SHOULD KNOW (June 2018).

[113] SASB Legal Roundtable, *supra* note 106 at 15.

[114] *See* Sections II.A.2 and II.B.1. Investors typically refer to the value of understanding both the risks and opportunities presented by climate change and how proper management of risks and opportunities lead to better long-term corporate performance.

[115] PRINCIPLES FOR RESPONSIBLE INVESTMENT, ABOUT THE PRI, HTTPS://WWW.UNPRI.ORG/PRI/ABOUT-THE-PRI (last visited on August 27, 2020).

[116] *Id.*

[117] *Id. See also*, Principles for Responsible Inv., Signatory Directory Updated 8.23.2020 (2020); *PRI-11 year growth of AO, all signatories (Asset Owners, Investment Managers and service providers) and respective AUM,* Excel sheet available for download at PRINCIPLES FOR RESPONSIBLE INVESTMENT, ABOUT THE PRI, http://www.unpri.org/about.

sustainability measures is the stewardship regulations of national governments. Nine countries have enacted policies requiring public pension funds to disclose the extent to which they have considered social and environmental information in their investment decisions.[118]

Regardless of the impetus, investor interest in sustainability issues has become increasingly widespread in recent years.[119] As interest in incorporating ESG factors into investment strategies has increased, investors have become increasingly vocal about their dissatisfaction with accessibility, comparability and reliability (or consistency and quality) of the voluntary sustainability reports produced by listed companies, and have begun demanding that the SEC establish mandatory prescriptive rules for ESG disclosures.[120] One of the problems is the plethora of ESG reporting

[118] The countries are Australia, Belgium, Canada, France, Germany, Italy, Japan, Sweden and the United Kingdom. *See* Initiative for Responsible Investment, *Corporate Social Responsibility Disclosure Efforts by National Governments and Stock Exchanges* (March 12, 2015), *available at* http://hausercenter.org/iri/wp-content/uploads/2011/08/CR-3-12-15.pdf

[119] The CFA Institute surveyed its global membership of analysts and portfolio managers in 2019 and found that 51% of the 549 global respondents stated that they consider environmental and social issues in their investment analyses and decisions, primarily to manage investment risk. MOHINI SINGH, CFA INSTITUTE, THE CASE FOR QUARTERLY AND ENVIRONMENTAL, SOCIAL AND GOVERNANCE REPORTING 41 (2019), https://www.cfainstitute.org/en/research/survey-reports/financial-reporting-quarterly-and-esg-2019. In May 2017, the CFA Institute performed a similar member survey with 1,588 responses in which 73% of respondents (53% of whom were U.S.-based) said they take ESG issues into account in their investment analysis and decisions, the same result as a 2015 survey. CFA INSTITUTE, GLOBAL PERCEPTIONS OF ENVIRONMENTAL, SOCIAL AND GOVERNANCE ISSUES IN INVESTING (2017), https://www.cfainstitute.org/en/research/survey-reports/esg-survey-2017.

[120] The CFA Institute reports that 52% of respondents thought sustainability disclosures should be mandatory, while 63% felt securities regulators should develop ESG standards or support an independent standards setter. Singh, supra note 119. Eccles and Kastrapeli report that in response to various surveys, investment managers have identified the lack of standards for measuring ESG performance, the lack of ESG performance data reported by companies, the cost of accessing and analyzing ESG information, and the lack of comparability among firms and over time as some of the biggest barriers to full integration of ESG factors in portfolio construction. Eccles and Kastrapeli, *supra* note 63. *See also* Amir Amel-Zadeh and George Serafeim, *Why and How Investors Use ESG Information: Evidence from a Global Survey*, 74 FIN. ANALYSTS J. 87 (2018). In its 2018 Investment Stewardship Annual Report, Vanguard stated that companies should provide "consistent, comparable and decision-useful disclosure on sustainability risks"; VANGUARD, 2018 ANNUAL REPORT ON INVESTMENT STEWARDSHIP 23 (2018); Sarah Bernow, Jonathan Godsall, Bryce Klempner and Charlotte Merten, *More than values: The value-based sustainability reporting that investors want*, MCKINSEY & COMPANY 6 (July 2019); Cydney Posner, *Investors want more standardized sustainability disclosures*, COOLEY PUBCO (August 19, 2019) (noting that "[i]nvestors and executives identified the

standards.[121] Investors would like to see a single standardized source of ESG reporting standards, and argue that the only way to get a single standard is for the SEC to impose one.[122]

When the SEC asked for comments regarding the value of sustainability disclosures in its 2016 Reg S-K Concept Release, a number of major public and private pension funds and other asset managers issued comment letters to the SEC noting that they use sustainability information to make investment decisions and need more information than the SEC currently requires.[123] The Council of Institutional Investors, a U.S. association representing public, corporate and union pension funds and other asset owners with combined assets exceeding $3 trillion, and asset management firms with more than $20 trillion in assets under management, noted that ESG risks have assumed greater importance in recent years from the perspective of mainstream investors. [124] State Street Global Advisors, one of the largest U.S. asset managers, with over $2.3 trillion in assets under management, also wrote a comment letter noting the importance of sustainability measures to long-term investors such as index funds and urging the SEC to introduce standardized reporting of key performance indicators on sustainability matters by industry.[125]

In January 2020, BlackRock CEO Larry Fink issued a letter to CEOs warning that failure to produce sustainability disclosures conforming to SASB and TCFD standards could lead BlackRock to vote against management in director elections.[126] BlackRock had previously announced,

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inconsistency, incomparability and lack of alignment of standards as the most significant challenge of sustainability reporting".), https://cooleypubco.com/2019/08/19/investors-standardized-sustainability-disclosures/

[121] *See supra* Section II.A.1.

[122] Posner, *supra* note 120 (noting that in the McKinsey 75% of investors wanted only one standard, 82% of investors though companies should be legally required to issue sustainability reports, and 66% of corporate executives endorsed mandatory reports).

[123] GELLASCH REPORT, *supra* note 7 at 18, *citing* letters from the NYS Comptroller and CalSTRS, for example.

[124] CII Letter, *supra* note 84, at 7 (*citing* BLACKROCK VIEWPOINT, *Exploring ESG: A Practitioner's Perspective*).

[125] Rahki Kumar, Mang. Dir. and Head, Corporate Governance, and Christopher McKnett, Mang. Dir. and Head of ESG, State Street Global Advisors, Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K (July 20, 2016), https://www.sec.gov/comments/s7-06-16/s70616-160.pdf.

[126] Larry Fink, *A Fundamental Reshaping of Finance,* BLACKROCK.COM (January 14, 2020), https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter. The CEO of State Street Global Advisors, another of the "Big Three" asset managers, also called on companies to provide disclosures in line with SASB requirements. Cyrus Taraporevala, *CEOs Letter on our 2020 Proxy Voting Agenda*, STATE STREET GLOBAL

in August 2018, that its fund managers would be required to consider ESG factors when they invest.[127] Skeptics of investor interest in ESG disclosures have pointed out that institutional investors have not always supported shareholder proposals requiring such disclosures in the past. That seems to be changing as significant institutional investors increasingly support such proposals.[128]

In the absence of significant improvement in the quality of the voluntary sustainability reports prepared by corporations, academics have proposed structures for a mandatory disclosure regime and investors have filed rulemaking petitions with the SEC seeking mandatory sustainability disclosures. Proponents of these mandatory disclosure regimes argue that the comparability and reliability problems of the current voluntary sustainability disclosure regime cannot be effectively addressed through private ordering.[129]

Jill Fisch has proposed that the SEC institute mandatory sustainability disclosure in the form of a Sustainability Discussion & Analysis, or SD&A,

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ADVISORS|INSIGHTS (Jan. 28, 2020)(stating that "[w]e believe that addressing material ESG issues is good business practice and essential to a company's long-term financial performance—a matter of value, not values."), *available at*: https://www.ssga.com/us/en/individual/etfs/insights/informing-better-decisions-with-esg. Vanguard has also encouraged companies to use standardized frameworks for sustainability reporting and recognized the value of the SASB and TCFD frameworks. VANGUARD, INVESTMENT STEWARDSHIP 2019 ANNUAL REPORT 23 (2019). In March 2020, Morrow Sodali released a report noting that 81% of the respondents to its survey of institutional investors believed that issuers should use the SASB framework to report on sustainability factors and 77% believed issuers should use the TCFD framework to disclose climate-related financial information. MORROW SODALI, INSTITUTIONAL INVESTOR SURVEY 2020 4 (2020).

[127] Reisenberg, *supra* note 112. Lawyers from the Wachtell, Lipton, Rosen & Katz law firm have opined that Fink's letter should provide the SASB standards with momentum towards becoming the consensus industry-specific disclosure regime. David A. Katz and Laura A. McIntosh, Wachtell, Lipton, Rosen & Katz, *Sustainability in the Spotlight*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Jan. 27, 2020), https://corpgov.law.harvard.edu/2020/01/27/sustainability-in-the-spotlight/. BlackRock has also issued guidance on its approach, as a shareholder, to engagement with issuers on climate change matters, *see* BLACKROCK, COMMENTARY: BLACKROCK INVESTMENT STEWARDSHIP'S APPROACH TO ENGAGEMENT ON CLIMATE RISK (January 2020), and its expectations that issuers will report sustainability matters pursuant to the TCFD recommendations and SASB standards, which it perceives as complementary. *See* BLACKROCK, COMMENTARY: BLACKROCK INVESTMENT STEWARDSHIP'S APPROACH TO ENGAGEMENT ON THE TCFD AND THE SASB ALIGNED REPORTING (January 2020).

[128] *See* Hannah Orowitz and Brigid Rosati, *An Early Look at the 2020 Proxy Season*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (June 10, 2020).

[129] *See, e.g.,* Harper Ho, *Nonfinancial Risk Disclosure*, *supra* note 41 at 412.

similar to the Management Discussion & Analysis, or MD&A, currently required in annual reports on Form 10-K and the Compensation Discussion & Analysis currently required in annual reports or proxy statements.[130] Virginia Harper Ho has proposed a comply or explain regime for sustainability reporting, similar to the regimes adopted in several countries in the European Union and elsewhere, pursuant to which companies must disclose enumerated sustainability metrics or explain why they have not disclosed them.[131] In October 2018, institutional investors representing more than $5 trillion in assets under management petitioned the SEC to issue mandatory rules for ESG disclosure.[132]

In May 2020, the SEC's Investor Advisory Committee, a body of investor representatives and other market experts established under the Dodd-Frank Act to advise the SEC on issues of concern to the investor community in the United States, called upon the SEC to establish ESG disclosure requirements for public companies.[133] The committee acknowledged that many companies are voluntarily disclosing some kinds of ESG information, but noted, "despite a great deal of information being in the mix, there is a lack of consistent, comparable, material information in the marketplace and everyone is frustrated – Issuers, investors and regulators."[134]

D. SEC Reluctance to Mandate Disclosures

[130] Fisch, *supra* note 13.

[131] Harper Ho, *supra* note 14.

[132] Cynthia A. Williams & Jill E. Fisch, *Request for Rulemaking on Environmental, Social, and Governance (ESG) Disclosure*, U.S. SEC. & EXCH. COMM'N (Oct. 1, 2018), https://www.sec.gov/rules/petitions/2018/petn4-730.pdf. In 2019, a subcommittee of the House Financial Services Committee considered five bills directing the SEC to require disclosures of various ESG issues, including climate change risk, corporate taxes paid, human resources management, political contributions. *Building a Sustainable and Competitive Economy: An Examination of Proposals to Improve Environmental, Social and Governance Disclosures*, *Before the Subcomm. on Investor Protection, Entrepreneurship and Capital Markets, H. Comm. On Financial Services*, 116th Cong. (2019); Betty Moy Huber, *U.S. House Financial Services Committee Hearing on ESG Disclosure*, DAVIS POLK: BRIEFING: GOVERNANCE (July 11, 2019), https://www.briefinggovernance.com/2019/07/u-s-house-financial-services-committee-hearing-on-esg-disclosure/.

[133] INVESTOR-AS-OWNER SUBCOMM., SEC INVESTOR ADVISORY COMMITTEE, RECOMMENDATION FROM THE INVESTOR-AS-OWNER SUBCOMMITTEE OF THE SEC INVESTOR ADVISORY COMMITTEE RELATING TO ESG DISCLOSURE (as of May 14, 2020), https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

[134] *Id.* at 5.

The SEC has historically been skeptical about mandating sustainability disclosures,[135] refusing to issue prescriptive rules for sustainability disclosure through multiple rule-making petitions over the course of fifty years.[136] The SEC has taken the view that sustainability disclosures are not generally material or useful to investors,[137] and when they are material, they are already covered by existing rules requiring disclosure of business descriptions, risk factors, and forward-looking trends in MD&A. In the 1970s, following the passage of the Environmental Protection Act, the SEC issued an interpretive release stating that registrants should consider disclosing in their SEC filings the financial impact of compliance with environmental laws, to the extent the impact was material.[138] Subsequently, the SEC successfully fended off litigation to compel it to require extensive environmental disclosures and issued limited requirements for disclosure of costs related to compliance with environmental laws, environmental litigation and related matters.[139]

In the late 2000s, the SEC faced renewed calls from climate activists and some institutional investors for interpretive guidance on disclosures related to climate change and global warming. The SEC responded with a 2010 interpretive release providing guidance on how disclosure related to climate change can and should be included in response to existing disclosure requirements related to MD&A, risk factors and material trends.[140] The SEC's position in the release was, from an intellectual and policy perspective, consistent with its position in the 1970s – sustainability issues may be material to some companies in certain facts and circumstances, but sustainability information in general is, by its nature, more of a social policy issue than an investor information and protection issue, unless it has a direct impact on the financial condition and results of operations of registrants, and therefore not an appropriate subject for extensive mandatory disclosure treatment.[141] Market observers have noted that the SEC "has gone "to great effort" to give companies what they want,

[135] Fisch, *supra* note 13 at 934 (*citing* Cynthia A. Williams, *The Securities and Exchange Commission and Corporate Social Transparency*, 112 HARV. L. REV. 1197, 1247-63 (1999)).

[136] Fisch. *supra* note 13 at 934 – 941.

[137] *Id*.

[138] Securities Act Release No. 33-5170, 36 Fed. Reg. 13989 (July 19, 1971).

[139] *See* Nat. Res. Def. Council, Inc. v. SEC, 606 F.2d 1031, 1049, 1056-57 (D.C. Cir. 1979). *See also*, Securities Act Release No. 33-6130, 44 Fed. Reg. 56924 (Sept. 27, 1979), Securities Act Release No. 33-6315, 46 Fed. Reg. 25638 (May 4, 1981), Securities Act Release No. 33-6383, 47 Fed. Reg. 11380 (March 3, 1982).

[140] Climate Change Release, *supra* note 3.

[141] *Id*. at 6295 – 6297.

which is a principles-based disclosure framework in lieu of promulgating prescriptive line-item requirements.[142]

In its 2016 Reg S-K Concept Release, focused on improving and streamlining corporate disclosure requirements, the SEC asked for views on whether it should require disclosure of sustainability matters.[143] The SEC noted that it had determined in the past that disclosure relating to environmental and other matters of social concern should only be required to the extent they are material under particular facts and circumstances or subject to a specific congressional mandate.[144] The SEC sought guidance on which, if any, sustainability disclosures are important to an understanding of a registrant's business and financial condition.[145] The SEC also noted its conclusion in 1975 that it would require disclosure relating to social and environmental performance of public companies "only if such information … is important to the reasonable investor – material information."[146] While it acknowledged that the "role of sustainability and public policy information in investors' voting and investment decisions may be evolving as some investors are increasingly engaged in ESG matters," the SEC did not propose any new sustainability requirements or offer further interpretive guidance suggesting a need for more such disclosures.[147]

Since 2016, activists, investors and members of Congress have become increasingly strident in their calls for SEC rule-making on ESG disclosures.[148] As pressure has mounted, the Commission has finally broken into a polarized public debate on the matter in the last twelve months. Allison Herren Lee and Caroline Crenshaw, the Democrats on the Commission, have argued strenuously in favor of establishing new mandatory disclosure standards, while Hester Pierce and Elad Roisman, the Republican commissioners, have argued equally forcefully for maintaining the current principles-based regime requiring only disclosure of material business issues, litigation, trends and risks relating to climate and other ESG

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[142] SASB Legal Roundtable, *supra* note 106 at 10. The problem with this, from the investor perspective is that many companies interpret principles-based rules focused on materiality in a narrow manner that results in inadequate disclosures and SEC comments and enforcement of such principles-based rules have been lacking. *Id.*

[143] Reg S-K Concept Release, *supra* note 2 at 23969 – 23973.

[144] Reg S-K Concept Release, *supra* note 2 at 23970 n.663 and accompanying text (*citing* Environmental and Social Disclosure, Securities Act Release No. 33-5627, 40 Fed. Reg. 51656 (Nov. 6, 1975).

[145] *Id.*

[146] *Id.* at 23971 n. 687 and accompanying text.

[147] Reg S-K Concept Release, *supra* note 2 at 23972

[148] *See supra*, Section II.C.

matters, as laid out in its 2010 guidance. Jay Clayton, the Chair of the Commission, who is a political independent appointed by President Trump, and William Hinman, the Director of the Corporation Finance Division of the SEC, both of whom had long careers representing issuers and underwriters as corporate lawyers before joining the SEC, have taken a wait-and-see approach, arguing that the complexity and dynamism of the market's expectations for sustainability disclosures make it inappropriate for the SEC to take a position at this time, and the principles-based materiality standard is appropriately tailored to the conditions of each company, which vary significantly.

Democratic Commissioners have made the following arguments in support of mandating prescriptive sustainability disclosures:

- A broad variety of market participants – asset managers, investors, issuers, credit rating agencies, analysts and index providers are using ESG as a significant driver of decision-making, capital allocation, pricing and value assessments, incorporating ESG factors into traditional analyses focused on maximizing risk-adjusted returns on investments, and have been clear that such information is material to their investment decisions. [149]

- The risks posed by climate change are real and quantifiable, not academic – companies know how climate change is impacting their businesses and their investors should too.[150]

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[149] Allison Herren Lee, Comm'r, Sec. Exch. Comm'n, Regulation S-K and ESG Disclosures: An Unsustainable Silence (Aug. 26, 2020)[hereinafter, "Lee August 2020 Statement"], *available at* https://www.sec.gov/news/public-statement/lee-regulation-s-k-2020-08-26; Allison Herren Lee, Comm'r, Sec. Exch. Comm'n, "Modernizing" Regulation S-K: Ignoring the Elephant in the Room (Jan. 30, 2020)[hereinafter, "Lee January 2020 II Statement"], *available at* https://www.sec.gov/news/public-statement/lee-mda-2020-01-30; Allison Herren Lee, Comm'r, Sec. Exch. Comm'n, Statement at Inaugural Meeting of the Asset Management Advisory Committee (Jan. 14, 2020), *available at* https://www.sec.gov/news/public-statement/statement-lee-asset-management-advisory-committee-2020-01-14; Jackson/Lee Joint Statement, *supra* note 11.

[150] Caroline Crenshaw, Comm'r, Sec. Exch. Comm'n, Statement on the "Modernization" of Regulation S-K Items 101, 103 and 105 (Aug. 26, 2020) (citing financial losses of corporations from disasters such as the California fires and 2017 hurricanes and noting that 90% of North American CFOs surveyed by Deloitte said their company had taken at least one action in response to climate change) [hereinafter, "Crenshaw August 2020 Statement"], *available at* https://www.sec.gov/news/public-statement/crenshaw-statement-modernization-regulation-s-k.; Lee January 2020 II Statement, *supra* note 149; Jackson/Lee Joint Statement, *supra* note 11.

- Vague principles-based requirements, such as obligations to disclose "material" information, fail to get investors the information they need about companies' ESG factors.[151]

- Disclosure requirements should facilitate efficient comparison of the long-term sustainability of issuers, and voluntary disclosures lacking consistency and comparability increase research costs to investors and capital costs to issuers.[152]

- Investors are demanding that regulators provide rules to promote more consistent, comparable and reliable disclosures.[153]

- Without a mandatory standardized disclosure framework, not all issuers will disclose, and disclosure will continue to vary greatly by issuer, making comparability more difficult.[154]

- Companies are inundated with competing voluntary reporting requests, creating costs that could be mitigated through a

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[151] Crenshaw August 2020 Statement, *supra* note 150; Commissioner Lee and former Commissioner Robert J. Jackson, Jr., expressed concern that principles-based disclosure gives company executives discretion over what they tell investors. Jackson/Lee Joint Statement, *supra* note 11 (noting that "while a principles-based regime necessarily defers to *management* regarding the relative importance of information, the materiality standard is defined from the perspective of *investors*, whose views should have heavy weight in determining whether and how specified metrics can be material. *Basic, Inc. v. Levinson*, 485 U.S. 224, 244 (1988) (plurality op.) (defining materiality from the perspective of a "reasonable investor" (citing *TSC Industries, Inc. v. Northway, Inc*. 426 U.S. 438 (1976))."). Commissioner Lee has noted that the materiality standard is inadequate in part because the SEC has not been sufficiently enforcing it, noting that the Commission has made only minimal comments on climate disclosure, or the lack thereof, in registrant's Annual Reports on Form 10-K and other filings in the years following its 2010 climate disclosure guidance. Lee January 2020 II Statement, *supra* note 149; *see also,* Lee August 2020 Statement, *supra* note 149, at fn. 26 ("Reliance on principles-based disclosure rules alone can only work when regulators have the requisite resources, information, expertise, skepticism and independence from industry." *Citing* Cristie Ford, *Principles-based Securities Regulation in the Wake of the Financial Crisis*, 55 MCGILL L. J. 1 (2010).

[152] Crenshaw August 2020 Statement, *supra* note 150; Jackson/Lee Joint Statement, *supra* note 11 (noting that inconsistent and incomparable information make investment analysis, and therefore capital, more expensive, and that the Commission and the Staff have given great weight to the importance of comparability in the past); Lee August 2020 Statement, *supra* note 149.

[153] Lee January 2020 II Statement, *supra* note 149.

[154] Jackson/Lee Joint Statement, *supra* note 11; Lee January 2020 II Statement, *supra* note 149.

uniform government standard.[155]

- There are significant questions about the reliability of the current voluntary reports, which generally are not third-party verified and may leave investors with inadequate remedies for inaccurate and incomplete disclosures.[156]

- To the extent that ESG issues are too uncertain and variable across companies, the Commission should undertake to establish detailed, clear and standardized set of disclosure requirements to allow investors to more easily assess the long-term sustainability of companies.[157]

- American companies will be at a disadvantage if the SEC fails to act while regulators in other countries (notably the European Union, Hong Kong and the United Kingdom) move forward with mandatory prescriptive disclosure regimes.[158]

The two Republican SEC Commissioners have expressed strong aversion to mandatory prescriptive sustainability disclosure rules. Commissioner Peirce expressed reservations about the IAC's recommendations on ESG disclosures, noting that "ambiguity has made the ESG debate a difficult one" and stating that a new SEC disclosure framework for ESG information is unnecessary since "our existing securities disclosure framework is very good at handling all types of material information."[159] She concluded that:

> If this committee is able to focus our attention on discrete pieces of information for which disclosure mandates are necessary, perhaps a substantive discussion could follow. A more general call to develop a new ESG reporting regime – without a clear explanation of why the past fifty years of discussion on the topic has not crystallized into a universally applicable set of material ESG items, but now is the magic moment – may not be as helpful. Otherwise, let's keep using our tired and true disclosure framework, which is rooted in materiality and is flexible enough to

[155] Lee January 2020 II Statement, *supra* note 149.
[156] *Id*.
[157] Crenshaw August 2020 Statement *supra* note 150.
[158] Lee January 2020 II Statement, *supra* note 149; Lee August 2020 Statement, *supra* note 149.
[159] Hester Peirce, Comm'r, Sec. Exch. Comm'n, Remarks at Meeting of the SEC Investor Advisory Committee (May 21, 2020), https://www.sec.gov/news/public-statement/peirce-statement-investor-advisory-committee-meeting-052120.

accommodate a wide range of issuer, each with its unique and ever-evolving set of risks.[160]

The Republican Commissioners have made the following additional arguments in favor of maintaining the status quo reliance on principles-based materiality disclosure requirements:

- Governance should not be lumped together with environmental and social issues, since the former relates directly to optimal operation and shareholder value, and the latter tend to be more stakeholder focused. [161]

- Issues raised by ESG factors are subjective and evolving based on current events, making prescriptive disclosure rules difficult.[162]

- Many parties calling for more disclosure hope to change corporate behavior rather than obtaining better investment returns.[163] A related argument is that the SEC should "stay in its lane", not regulating environmental and social policy issues

[160] *Id.* At a meeting of the SEC's Investor Advisory Committee in December 2018, Commissioner Peirce referred to ESG as "Enabling Shareholder Graft". Peirce argued that ESG matters require companies to spend money on matters that do not benefit shareholders. Cydney Posner, *Clayton Q&A and ESG at the SEC's Investor Advisory Committee meeting*, COOLEY PUBCO (December 17, 2018), https://cooleypubco.com/2018/12/17/esg-at-investor-advisory-committee-meeting/. In June 2019, she delivered a lengthy speech to the American Enterprise Institute deriding ESG as "scarlet letters". Hester Peirce, Comm'r, Sec. Exch. Comm'n, Scarlett Letters: Remarks before the American Enterprise Institute (June 18, 2019), https://www.sec.gov/news/speech/speech-peirce-061819.

[161] Elad Roisman, Comm'r, Sec. Exch. Comm'n, Keynote Speech at the Society for Corporate Governance National Conference (July 7, 2020) (suggesting that environmental and social factors focus on issues such as how a company is "doing its part" to combat climate change or address global and political matters)[hereinafter, "Roisman Statement"], *available at* https://www.sec.gov/news/speech/roisman-keynote-society-corporate-governance-national-conference-2020.

[162] Roisman Statement, *supra* note 161 (noting any list of required disclosures prepared ten years ago would look very different from a list compiled today).

[163] Roisman also noted, as skeptics of sustainability disclosure often do, that "this type of mandated disclosure is often fraught with subjectivity and agendas that are unrelated to 'investor welfare'", and "there has been a desire from some quarters to conflate greater societal debates about environmental regulation and social policies with public company disclosure requirements". Noting that these areas involve different policy-makers and different goals, Roisman argued that only by acknowledging this broader context of the sustainability disclosure debate can we have a more objective and productive policy discussion. Roisman Statement, *supra* note 161.

through disclosure mandates, but focusing only on the SEC's mandates to protect investors and facilitate capital formation.[164]

- The principles-based materiality standard of disclosure is appropriate in these circumstances because while individual ESG issues or factors may be material to a company, different companies will have different issues and broadly applicable prescriptive standards will create a "sea of inapplicable information" that obscures material information.[165]

- Liability risk is a concern, since U.S. public companies face greater litigation risk than companies listed in other countries.[166]

- If information about sustainability issues is not disclosed under the current "materiality" disclosure regime, that means the information is not material in the judgement of management.

SEC Chairman Jay Clayton has sided with the Republican Commissioners in resisting the call for mandatory sustainability disclosures. Both Chairman Clayton and Division of Corporation Finance Director William Hinman have expressed caution about mandating new prescriptive disclosures. Director Hinman has expressed the view that principles-based disclosure, such as the SEC's current system requiring disclosure of "material" risks and trends, is well suited for complex, uncertain and rapidly evolving issues such as sustainability because it is a flexible regime "designed to elicit material, decision-useful information on a company-specific basis."[167] He argued that rather than the SEC issuing prescriptive

[164] The SEC's tripartite mission is to "protect investors, maintain fair, orderly and efficient markets, and facilitate capital formation." *See* U.S. Securities and Exchange Commission, WHAT WE DO, *available at*, https://www.sec.gov/Article/whatwedo.html. Commissioner Peirce lauds the materiality standard for disclosure on the basis that it "focuses on whether the information an issue is broadly useful to investors in the context of seeking a return on their investment" and not on "what is important to non-investors or to a select group of investors motivated by objectives unrelated or only tangentially connected to their investment's profitability". Hester Peirce, Comm'r, Sec. Exch. Comm'n, Statement on Proposed Amendments to Modernize and Enhance Financial Disclosures (January 30, 2020)[hereinafter, "Peirce January 2020 Statement"], *available at* https://www.sec.gov/news/public-statement/peirce-mda-2020-01-30.

[165] Roisman Statement, *supra* note 161; Peirce January 2020 Statement, *supra* note 164.

[166] Roisman Statement, *supra* note 161; Peirce January 2020 Statement, *supra* note 164.

[167] William Hinman, Dir., Div. of Corp. Fin., U.S. Sec. & Exch. Comm'n, Applying a Principles-Based Approach to Disclosing Complex, Uncertain and Evolving Risks:

disclosure prematurely it is better to allow the market to sort out which kinds of sustainability disclosures would be most decision-useful.[168] He also expressed concern that imposing additional disclosure costs on companies that do not deliver information benefits for the market justifying such costs could unnecessarily diminish the attractiveness of public markets as a source of capital.[169]

Chairman Clayton has addressed the merits of mandatory sustainability disclosures in several statements during his term. His views, some of which echo those of Director Hinman or the Republican Commissioners, can be summarized as follows:

- Sustainability issues are complex, uncertain, multi-national/jurisdictional and dynamic. [170]

Remarks at the 18th Annual Institute on Securities Regulation in Europe (March 15, 2019); Betty M. Huber and Megan Cronin, BRIEFING: GOVERNANCE, THE SEC ON ESG DISCLOSURE – LATEST DEVELOPMENTS, DAVIS, POLK & WARDWELL, LLP (March 19, 2019), https://www.briefinggovernance.com/2019/03/the-sec-on-esg-disclosure-latest-developments/. Director Hinman has high expectations for principles based disclosure. He noted that MD&A disclosures should allow investors "to understand how management is positioning the company in the face of uncertainties" and risk factor disclosure should provide investors with "decision-useful" information that is company-specific rather than burying the reader in "generic boilerplate or a laundry list of risks that might apply to any company". Cydney Posner, *Corp Fin director Discusses Brexit and sustainability disclosure*, COOLEY PUBCO (March 15, 2019), *available at*: https://cooleypubco.com/2019/03/15/hinman-discusses-brexit-and-sustainability-disclosure/. Noting that an important objective of the U.S. disclosure regime is to help investors see the company through the eyes of management, Director Hinman encouraged companies to provide disclosures on emerging issues, such as sustainability, that allow investors to understand how management plans to mitigate material risks and how their decisions regarding such risks could be material to their business.

[168] Hinman, *supra* note 167 ("So it appears to me that the market is still evaluating what, if any, additional disclosure on these topics would provide consistently material and useful information. The marketplace evolution of sustainability disclosures is ongoing – companies certainly provide more sustainability information than they did ten years ago – and allowing this evolution to continue should provide market participants with a continued opportunity to sort out the types of information they find useful. Had we leapt into action and issued prescriptive sustainability disclosure requirements when people first began calling for them, I believe we would have stymied that evolution and stifled efforts to develop useful disclosure frameworks. Substituting regulatory prescriptions for market-driven solutions, especially while those solutions are evolving, in my view, is something we need to manage with utmost care."). *See also*, Huber and Cronin, *supra* note 167.

[169] Hinman, *supra* note 167.

[170] *See* Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Public Statement, Proposed Amendments to Modernize and Enhance Financial Disclosures; Other Ongoing Disclosure Modernization Initiatives; Impact of the Coronavirus; Environmental and Climate-Related Disclosure (Jan. 30, 2020)[hereinafter "Clayton January 2020

- For both issuers and investors, capital allocation decisions based on, or materially influenced by, climate-related factors are substantially forward-looking and involve estimates and assumptions regarding complex and uncertain matters that are both issuer- and industry-specific, as well as regional, national and multi-national in nature.[171] The U.S. disclosure-based regulatory regime focuses primarily on verifiable and largely historic issuer-specific information. Forward-looking disclosure requirements are limited and generally afforded safe-harbor protection.[172]

- Issuers and investors should focus on the information that is material to each company's particular facts and circumstances.[173] The principles-based rules focused on material information are designed for this purpose and encourage disclosure of metrics the company and its management use in managing the company's business.[174]

- When crafting and implementing disclosure mandates and guidance, the members of the SEC should not be substituting their own operational and capital allocation judgments for those of issuers and investors. Standard setters should take care to stay within the bounds of their regulatory mandate.[175]

- The U.S. regulatory regime has a different public and private

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Statement"], *available at*: https://www.sec.gov/news/public-statement/clayton-mda-2020-01-30.

[171] *Id.*

[172] *Id.*

[173] Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Remarks to the SEC Investor Advisory Committee (Dec. 13, 2018)[hereinafter, "Clayton 2018 Statement"], *available at*: https://www.sec.gov/news/public-statement/clayton-remarks-investor-advisory-committee-meeting-121318. Clayton also emphasized that investment advisors have a fiduciary duty to their clients and cannot put their own interests ahead of the interests of their clients, echoing the Department of Labor's 2018 ESG guidance to ERISA plan fiduciaries.

[174] Cydney Posner, *SEC adopts amendments to modernize Reg S-K requirements for business, legal proceedings and risk factor disclosures (UPDATED)*, COOLEY PUBCO (August 31, 2020), *available at:* https://cooleypubco.com/2020/08/31/sec-amendments-modernize-reg-s-k-business-legal-risks/. At the August 2020 meeting adopting amendments to the SEC's disclosure rules for business, legal proceedings and risk factors, Clayton noted that the principles-based, flexible disclosure regime has worked well in connection with corporate disclosures on the impact of COVID-19. *Id.*

[175] Clayton January 2020 Statement, *supra* note 170.

liability and enforcement regime than other countries and that may affect disclosure requirements.[176]

- ESG factors can have value, in some cases, in much the same way that appropriate non-GAAP information and key performance indicators can have value to investors.[177]

- It is important not to burden companies with the costs of producing disclosure that is not material to investors.[178]

- Investor analysis of ESG issues appears to vary widely, "in some cases incorporating objectives other than investment performance over a particular time frame or frames."[179]

- "E", "S" and "G" disclosures are different categories of information from a disclosure regulatory perspective, and lumping them together, particularly in the context of a single rating, diminishes their usefulness. [180]

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[176] *Id.*

[177] Clayton 2018 Statement, *supra* note 173.

[178] Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Remarks at the Economic Club of New York (July 12, 2017)("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."), *available at*:), https://www.sec.gov/news/speech/remarks-economic-club-new-york.

[179] Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Public Statement, Remarks at Meeting of the Investor Advisory Committee (November 7, 2019)[hereinafter "Clayton 2019 Statement"], https://www.sec.gov/news/public-statement/clayton-remarks-investor-advisory-committee-110719. Chairman Clayton has repeatedly expressed an interest in learning from investors using sustainability disclosures to make investment decisions how and to what extent they use ESG data, whether it is a change in investment approach or an enhancement of their traditional approach, whether they use such data to improve investment performance over a particular term or to address other objectives or policies, and how their clients understand the asset manager's use of the data. *See Id.*; Clayton January 2020 Statement, *supra* note 170.

[180] Clayton 2019 Statement, *supra* note 179. *See also,* Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Public Statement, Remarks at Meeting of the Investor Advisory Committee (May 21, 2020)(stating, "I believe E, S and G are quite different baskets of disclosure matters and that lumping them together diminishes the usefulness, including investor understanding, of such disclosures"), https://www.sec.gov/news/public-statement/clayton-statement-investor-advisory-committee-meeting-052120; Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Remarks at Meeting of the Asset Management Advisory Committee (May 27, 2020)(stating, "while I believe that in many cases one or more "E" issues, "S" issues, or "G" issues are material to an investment decision, I have not seen circumstances where combining an analysis of E, S and G together, across a broad

- In many areas, mandating "E," "S" and "G" disclosures runs the risks of sacrificing what may be the more relevant, company-specific disclosure for the potential for greater comparability across companies."[181]

III. Private Ordering under the Eye of the SEC

While mandatory sustainability disclosure requirements might ultimately be necessary to accurately and efficiently capture the financial risks and opportunities posed by climate change, it is not necessary for the SEC to mandate specific sustainability disclosures in order to improve the accessibility, comparability and reliability of the disclosures currently being reported by companies on a voluntary basis. The SEC could promote progress in these areas by requiring the companies that voluntarily prepare sustainability reports pursuant to standards established by third parties such as SASB and GRI to furnish such reports to the SEC on Form 8-K. Recognizing the importance of its online archive of corporate reports, the Electronic Data Gathering, Analysis, and Retrieval system, or EDGAR, as a central source of information for participants in the U.S. capital markets, the SEC has previously used Form 8-K to promote the accessibility and reliability of material information voluntarily distributed into the market by U.S. public companies in other contexts by requiring such information to be furnished to the SEC on Form 8-K. Section III.A. below provides background on Form 8-K. Sections III.B. and III.C. describe how the SEC applied Form 8-K reporting requirements to selective disclosure and earnings releases, respectively.

A. Form 8-K

Form 8-K was established by the SEC in 1936 as a means to promote current disclosure of extraordinary corporate events occurring in the interim between mandated periodic reports.[182] The SEC has increased the number of events reportable on Form 8-K over the years as its views on material

range of companies, for example with a "rating" or "score," particularly a single rating or score, would facilitate meaningful investment analysis that was not significantly over-inclusive and imprecise"), https://www.sec.gov/news/public-statement/clayton-amac-opening-2020-05-27.

[181] Clayton 2019 Statement, *supra* note 179.

[182] Additional Form 8-K Disclosure Requirements, Securities Act Release No. 33-8106, Securities Exchange Act Release No. 34-46084, 67 Fed. Reg. 42914 (June 25, 2002)(*citing* Securities Exchange Act Release No. 34-925 (Nov. 11, 1936).

corporate events have changed.[183] Public companies are required to file current reports on Form 8-K following the occurrence of various corporate events,[184] such as entry into a material definitive agreement,[185] a significant acquisition or disposition of assets,[186] incurrence of material debt obligations,[187] unregistered sales of equity securities,[188] elections and departures of directors and appointment and changes in compensation arrangements of officers,[189] amendments of articles and by-laws[190] and results of shareholder votes.[191] Material misstatements or omissions included in a Form 8-K and any accompanying exhibits filed with the SEC are subject to liability under Section 18 of the Securities Exchange Act of 1934.[192] Also, because information filed with the SEC through current reports on Form 8-K is required to be incorporated by reference into prospectuses included in Registration Statements on Form S-3,[193] the statements therein are subject to strict liability under Section 11 of the Securities Act of 1933.[194]

In two cases, the SEC has permitted companies to furnish information on Form 8-K rather than filing the information. Information included in a Form 8-K and accompanying exhibits *furnished*, as opposed to *filed* with the SEC is not subject to liability under Section 18 of the Exchange Act.[195] Information furnished on Form 8-K is not incorporated by reference into Securities Act registration statements unless a registrant intentionally and explicitly incorporates the relevant 8-K into its registration statements, so registrants generally are not subject to strict liability under Section 11 of the Securities Act for the information included therein.[196] The SEC has applied

[183] See, e.g., *id* (describing history of amendment of Form 8-K and proposing further amendments).
[184] 17 C.F.R. § 240.13a–11.
[185] Current Report (Form 8-K), 17 C.F.R. § 249.308, Item 1.01
[186] *Id*., Item 2.01
[187] *Id.*, Item 2.03
[188] *Id.*, Item 3.02
[189] *Id.*, Item 5.02
[190] *Id*., Item 5.03
[191] *Id*., Item 5.07
[192] 15 U.S.C. 78r.
[193] Form S-3, Registration Statement Under the Securities Act of 1933, Item 12(a)(1), 17 C.F.R. 239.13.
[194] 15 U.S.C. 77k.
[195] Current Report (Form 8-K), 17 C.F.R. § 249.308, General Instructions, B.2.; Frequently Asked Questions About Form 8-K, MORRISON & FOERSTER LLP 8 (2017).
[196] Current Report (Form 8-K), 17 C.F.R. § 249.308, General Instructions, B.2. *See also*, Conditions for Use of Non-GAAP Financial Measures, Securities Act Release No. 33-8176, Exchange Act Release 34-47226, 68 Fed. Reg. 4820, 4826 (January 30, 2003)[hereinafter, "Earnings Release Adopting Release"].

this treatment to quarterly and annual earnings releases issued publicly prior to the filing of quarterly reports on Form 10-Q and annual reports on Form 10-K, and to statements filed for purposes of compliance with Regulation FD.[197]

The SEC has used exemption from the filing requirements and related liability regimes to encourage companies to make material non-public information available to the SEC and the public markets by uploading the information in the SEC's easily accessible EDGAR database for corporate filings.

Although documents furnished to the SEC on Form 8-K are not subject to liability under Section 18 of the Exchange Act, they remain subject to liability under the general fraud rules for statements made by a company to the public, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.[198] These provisions contain a general prohibition on making material misstatements and omissions of fact in connection with the purchase or sale of securities. However, these general anti-fraud provisions apply to all public statements made by public companies, so statements included in sustainability reports made public by companies are already subject to liability under these general anti-fraud rules, and they would not be subject to any new liability if they are furnished to the SEC on Form 8-K.[199]

Numerous SEC releases have taken the position that the anti-fraud rules apply to statements on company websites and other electronic media to the same extent they apply to other company statements.[200] For instance, in its

[197] Current Report (Form 8-K), 17 C.F.R. § 249.308, Items 2.02, 7.01.

[198] Rule 10b–5, 17 CFR 240.10b–5, makes it unlawful to ''make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, *in the light of the circumstances under which they were made,* not misleading'' (emphasis added).

[199] *See, e.g., In re BP P.L.C. Sec. Litig.*, 922 F. Supp. 2d 600 (S.D. Tex. 2013) (sustainability report was a potential basis for securities fraud claim); SOC'Y FOR CORP. GOVERNANCE, GIBSON, DUNN & CRUTCHER LLP, LEGAL RISKS AND ESG DISCLOSURES: WHAT CORPORATE SECRETARIES SHOULD KNOW (June 2018), https://www.gibsondunn.com/legal-risks-and-esg-disclosures-what-corporate-secretaries-should-know/.

[200] *Use of Electronic Media for Delivery Purposes,* Release No. 33–7233, 60 Fed. Reg. 53458 (Oct. 6, 1995)(''1995 Electronics Release'') at n. 11 (''The liability provisions of the federal securities laws apply equally to electronic and paper-based media. For instance, the antifraud provisions of the federal securities laws as set forth in Section 10(b) of the Exchange Act [15 U.S.C. 78j(b)] and Rule 10b–5 [17 CFR 240.10b–5] thereunder would apply to any information delivered electronically, as it does to information delivered in paper.''); *Use of Electronic Media by Broker-Dealers,* Release No. 33–7288, 61 Fed. Reg.

release on use of company websites for communicating with investors and the public, the SEC opined that,

> The antifraud provisions of the federal securities laws apply to company statements made on the Internet in the same way they would apply to any other statement made by, or attributable to, a company.[201]

The SEC explained in another release that companies "are responsible for the accuracy of their statements that reasonably can be expected to reach investors or the securities markets regardless of the medium through which the statements are made, including the Internet."[202]

B. Regulation FD

The first instance in which the SEC permitted material information to be furnished, rather than filed, with the SEC on Form 8-K was in connection with the promulgation of Regulation FD. Pursuant to Regulation FD, companies registered with the SEC are required to make public disclosure of any material non-public information disclosed to enumerated parties.[203] Whenever a public company, or a person acting on its behalf, discloses material non-public information to enumerated persons, the company must

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24643 (May 9, 1996)(''1996 Electronics Release''), at Section I, n. 4 (''The substantive requirements and liability provisions of the federal securities laws apply equally to electronic and paper-based media. For example, the antifraud provisions of the Exchange Act and Rule 10b–5 thereunder * * * apply to information delivered and communications transmitted electronically, to the same extent as they apply to information delivered in paper form.''); *Use of Electronic Media,* Release No. 33– 7856 (Apr. 28, 2000) [65 FR 25843] (''2000 Electronics Release''), at Section II.B. (''It is important for companies * * * to keep in mind that the federal securities laws apply in the same manner to the content of their Web sites as to any other statements made by or attributable to them.''). *See also* Robert Prentice *et al.*, *Corporate Web Site Disclosure and Rule 10b-5: An Empirical Evaluation,* 36 Am. Bus. L.J. 531, at 542 (   )(noting that the Commission's antifraud legal regime under Section 10(b) and Rule 10b–5 applies to all manner of electronic disclosure); Howard M. Friedman, *Securities Regulation in Cyberspace* § 10.01 (3rd ed. Supp. 2006).

[201] Commission Guidance on the Use of Company Websites, SEC Rel. 34-58288, 73 Fed. Reg. 45862, 45869 (August 7, 2008).

[202] 2000 Electronics Release, *supra* note 200, at Section II.B.1.

[203] Regulation FD, 17 CFR § 243.100. The enumerated parties include any person outside the registrant who: (1) is or is associated with a broker or a dealer; (2) is or is associated with an investment advisor or investment manager; (3) is or is affiliated with an investment company (including private investment companies under 3(c)(1) or 3(c)(7) of the Investment Company Act); or (4) holds any of the issuer's securities (e.g., shareholders and bond holders), under circumstances in which it is reasonably foreseeable that the person will purchase or sell the issuer's securities on the basis of the information. *Id.*

disclose the information to the public.[204] The public disclosure must be made through a Current Report on Form 8-K unless the registrant disseminates the information through another method (or combination of methods) reasonably designed to effect broad, non-exclusionary distribution of the information to the public.[205]

Regulation FD is an example of promoting broader public disclosure of corporate information without regulating the substance of disclosure – Regulation FD does not mandate any particular disclosures, it just requires public companies to share with the SEC and the general public any material non-public information it has shared with other participants in the capital markets. Regulation FD was intended to eliminate selective disclosure and promote full and fair disclosure of information by issuers.[206]

Information is "nonpublic" if it has not been disseminated in a manner making it available to investors generally[207] For information to have been made public,

> it must be disseminated in a manner calculated to reach the securities marketplace in general through recognized channels of distribution, and public investors must be afforded a reasonable waiting period to react to the information.[208]

While most companies post their sustainability reports on their corporate websites, such posting only satisfies Reg FD requirements if the relevant corporate website is a "recognized channel of distribution" of information relevant to investors.

In 2008, the SEC issued guidance stating that posting on a corporate website is an effective means for disseminating information to the public only if the website is a *recognized channel of distribution* and posting on the website makes the information generally available to the securities

[204] Frequently Asked Questions About Regulation FD, MORRISON & FOERSTER LLP 1 (2017).
[205] Regulation FD, 17 CFR § 243.101(e).
[206] Frequently Asked Questions About Regulation FD, MORRISON & FOERSTER LLP 1 (2017).
[207] Reg FD Adopting Release, *supra* note 33, citing Texas Gulf Sulphur, 401 F.2d 833, 854 (2d Cir. 1968), cert. denied, 394 U.S. 976 (1969); In re Investors Management Co., 44 S.E.C. 633, 643 (1971).
[208] Commission Guidance on the Use of Company Websites, SEC Rel. 34-58288, 73 Fed. Reg. 45862, 45867 (August 7, 2008), citing *In re Faberge*, Inc., 45 S.E.C. 249, 255 (1973).

marketplace.[209] Whether a company's website is a recognized channel of distribution depends on whether the company has taken steps to alert the market to its website and its disclosure practices and the use by investors and the market of the website.[210] The SEC has taken the view that if the information is important, companies should consider taking additional steps to alert the market that important information is being posted, such as filing or furnishing the information to the SEC or issuing a press release prior to the posting.[211] Posting on a company website in a location and format that is readily accessible to the general public would not generally be "selective" disclosure for purposes of Regulation FD.[212]

Since it was enacted in 2000, Regulation FD has fundamentally changed the way public companies communicate with the market through conference

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[209] Commission Guidance on the Use of Company Websites, SEC Rel. 34-58288, 73 Fed. Reg. 45862, 45867 (August 7, 2008).

[210] *Id.* Whether website posting is sufficient to disseminate information in manner making it generally available depends on several factors:

(1) Whether and how companies let investors and the markets know that the company has a website and they should look at the website for information – does the company include information about its website address and the fact it posts information to the website in its periodic reports?

(2) Whether the company has made investors and the markets aware that it will post important information on its website and whether it has a pattern or practice of posting such information on its website.

(3) Whether the company's website is designed to lead investors and the market efficiently to information about the company, including information specifically addressed to investors.

(4) Whether the information is prominently disclosed and routinely used for such disclosures, and whether the information is presented in a format readily accessible to the general public.

(5) The extent to which information posted on the website is regularly picked up by the market and readily available media or the extent to which the company has advised newswires or the media about such information and the size and market following of the company. Companies with less of a market following may need to take more affirmative steps to ensure investors and others know information is or has been posted to the company's website.

(6) The steps the company takes to make the information and website accessible by using other distribution channels such as press releases to make the market aware of its availability. *Id.*

[211] Given the emerging consensus that sustainability information is often material to investors, the SEC should arguably take enforcement action under Regulation FD against companies that have not established the part of their website on which they post sustainability reports as a "recognized channel of distribution" of information to investors, unless they include such information in their periodic reports to the SEC or furnish their reports on Form 8-K.

[212] *Id.* at 45868.

calls and investor meetings.[213] Regulation FD is generally perceived as having successfully decreased selective disclosure to analysts and other market participants and increased the amount of information available to the market more generally.[214] Following the promulgation of Regulation FD, the number of companies issuing earnings guidance through press releases increased significantly.[215] While there was some concern at the time it was introduced that Regulation FD would decrease the amount of information released to the market by public companies, empirical studies in the accounting literature have concluded that the feared decline in information production did not transpire.[216]

For present purposes, there are two important lessons from Regulation FD. First, it is an example of the successful migration of information from private settings onto the SEC's centralized public information clearinghouse, EDGAR, with the result that more participants have access to information they might not otherwise be able to access in a cost-effective manner.

Second, if the information included in sustainability reports is material to investors, as discussed in Section I.D. above, public companies should arguably be furnishing their sustainability reports to the SEC on Form 8-K already to satisfy their obligations under Regulation FD unless they are distributing their reports through a recognized channel of distribution in a manner calculated to reach the securities market in general.[217] Posting the sustainability report on the corporate website might not satisfy this standard if the website on which the corporation posts the report has not been identified by the company as a means of sharing information with investors and the public markets.[218] One might argue that posting the report on a corporate social responsibility website is not sufficient if the company also has an investor relations website, since information for investors would normally be expected to be on the investor relations website.

C. Earnings Releases

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[213] Frequently Asked Questions About Regulation FD, MORRISON & FOERSTER LLP 1 (2017).

[214] CITE

[215] CITE

[216] Jill Fisch, *Regulation FD: An Alternative Approach to Addressing Information Asymmetry*, *in* RESEARCH HANDBOOK ON INSIDER TRADING (Stephen Bainbridge ed., 2013).

[217] *See supra* notes 209-210 and accompanying text.

[218] *See supra*, note 212 and accompanying text.

The SEC also used the furnishing of information on Form 8-K to promote equal access to corporate earnings information historically distributed by companies through newswires and other services that not all investors had access to. Section 409 of the Sarbanes-Oxley Act[219] directed the SEC to establish new rules for the disclosure of material changes in the financial condition or operations of public companies.[220] The SEC responded to this direction in part by adding earnings releases to the list of corporate events required to be filed on Form 8-K.[221]

When it originally proposed Form 8-K filing of selected financial information from earnings announcements in 1998, the SEC expressed concern that not all investors subscribe to the publications that carry press release information and not all publications report on every company's release or include all the information in the releases.[222] This raised concern that not all investors received information regarding a company's financial results at the same time.[223] The SEC also noted that the presentation of financial information in earnings press releases varied from company to company, in some cases because companies want to focus on the positive aspects of the information.[224] In early 2002, the SEC dropped this proposal without comment when it proposed other new additions to Form 8-K.[225]

Shortly after dropping the proposal to require filing of selected financial information on Form 8-K, however, the SEC proposed filing of the entire earnings release on Form 8-K in its release proposing limitations on the use of Non-GAAP information in such releases and other SEC filings.[226] The primary impetus for the proposal was to bring earnings disclosures within

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[219] Pub. L. No. 107–204, 116 Stat. 745 (2002).

[220] Section 409 of the Sarbanes-Oxley Act added a new Section 13(l) to the Securities Exchange Act of 1934. Section 13(l) obligates public companies to disclose "on a rapid and current basis such additional information concerning material changes in the financial condition or operations of the issuer . . . as the Commission determines, by rule, is necessary or useful for the protection of investors and in the public interest." 15 U.S.C. 78m(l).

[221] Conditions for Use of Non-GAAP Financial Measures, Securities Act Release No. 33-8145, Securities Exchange Act Release No. 34-46788, 67 Fed. Reg. 68790 (proposed Nov. 13, 2002)[hereinafter, "Earnings Release 8-K Proposing Release"].

[222] The Regulation of Securities Offerings, Securities Act Rel. No. 33-7606A, Exchange Act Release No. 34-40632A, 63 Fed. Reg. 67174, 67241 (proposed Dec. 4, 1998)[hereinafter, "Aircraft Carrier Release"].

[223] *Id*.

[224] *Id*.

[225] Earnings Release 8-K Proposing Release, *supra* note 221.

[226] *Id.*

the current reporting system.[227] Consistent with its original concerns about earnings announcements, the SEC also noted that by including earnings announcements in the formal disclosure system, the proposal would make the earnings information available to investors on a widespread basis.[228] The SEC originally proposed that earnings releases reported on Form 8-K would be considered filed, rather than furnished, for liability purposes, unlike information furnished pursuant to Regulation FD.[229] In the adopted form of the rule, however, the SEC permitted earnings reports to be furnished, rather than filed, on Form 8-K due to concerns expressed by the American Bar Association and others that filing would have a detrimental effect on the level and quality of information provided to investors.[230] The commentators expressed the concern that enhanced liability would discourage issuers from distributing earnings releases in the first place.[231]

IV. BENEFITS OF FORM 8-K SUSTAINABILITY REPORTING

Requiring firms to furnish their sustainability reports to the SEC on Form 8-K is an alternative to the all-or-nothing alternatives of adopting new mandatory line item sustainability reporting in annual reports on Form 10-K and maintaining the private-ordering status quo. It would address, at least in part, the concerns of both investors and issuers. To begin with, it would address the issue of equal and ready accessibility of the information. As discussed in Sections IV.B. and C. below, it will also promote two objectives of investors calling for SEC action on sustainability disclosure: improved comparability and increased reliability. As noted in Section IV.D., this approach will also achieve the benefits of accessibility, comparability and reliability without imposing significant additional costs or litigation risks on public companies, eliminating two of the concerns often raised by the business community. Finally, as discussed in Section IV.E., this approach to regulation will allow the SEC to rely on private ordering to establish the most material sustainability measures in various industries before designing and implementing any mandatory disclosure regime should it become unequivocally necessary to establish one.

A. Addressing Accessibility

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[227] *Id*. at 68792.
[228] *Id.* at 68798.
[229] *Id.* at 68796.
[230] *See* Earnings Release Adopting Release, *supra* note 196 at 4826, note 64 and accompanying text.
[231] *Id.*

Disclosure of sustainability metrics in sustainability reports is already affecting the value of firms in the market,[232] but the disclosure is not incorporated in the SEC's formal reporting system. Investors do not have access to a one-stop shop for sustainability disclosures since companies disclose sustainability information because most companies publish the information on their websites and do not file them with the SEC.[233] This has an adverse effect on the ability of investors and the SEC to monitor the drivers of market value, and can be expected to increase the cost to investors of establishing accurate market prices for the securities of companies issuing such reports. It may also put some investors (smaller firms that don't have resources to chase the information on the website of every issuer) at a disadvantage because the information is not readily available at a central source. As noted in Section III.C. above, the SEC established its rule that voluntary earnings releases must be furnished on Form 8-K, and uploaded to the SEC's EDGAR system, in part to ensure broad public access to the preliminary earnings and forecast information typically included in such releases. Requiring companies to furnish their sustainability reports on Form 8-K, as the SEC did with earnings releases, will make the information more readily available to all investors.

B. Promoting Comparability

As noted in Section II.B.1 above, investors have expressed dissatisfaction with the consistency of sustainability information reporting from period-to-period and the comparability of sustainability reporting among companies in the same industry. Requiring sustainability reports to be furnished to the SEC on Form 8-K should mitigate both concerns as the reports become available in a central database subject to SEC scrutiny. As explained below, empirical evidence has shown that issuer's voluntary earnings reports became more comparable after the SEC required them to be uploaded to the SEC's EDGAR system.

One of the reasons the SEC decided to require earnings reports to be furnished on Form 8-K was its concern that earnings releases varied considerably in availability and presentation, sometimes "because the company wants to focus on the positive aspects of the financial

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[232] *See* Section II.A.2., *supra*.

[233] Holly J. Gregory, Heather Palmer, and Leonard Wood, Sidley Austin LLP, *Emerging ESG Disclosure Trends Highlighted in GAO Report*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (August 15, 2020), https://corpgov.law.harvard.edu/2020/08/15/emerging-esg-disclosure-trends-highlighted-in-gao-report/#2.

information".[234] The SEC believed that requiring companies to file selected financial information quarterly on Form 8-K would "ensure uniform and even disclosure by public companies" of the information typically included in quarterly earnings releases.[235]

Companies tend to look to the disclosures of their peers and competitors, particularly leaders in their industry, in drafting disclosures filed with the SEC.[236] This means that the comparability of disclosures among public companies in the same industry increases over time. These tendencies have been studied at length in the academic accounting literature and have been elucidated in a variety of contexts. It seems that disclosure on the SEC's EDGAR database focuses firms and investors on what competitors are disclosing.

Ronald Dye and Sri Sridhar proposed a theory to explain this phenomenon in their paper *Industry-Wide Disclosure Dynamics* in 1995.[237] Observing that voluntary disclosures by some firms seem to provoke other firms to make related disclosures, they attribute the interactions among corporate disclosures to the influence that one firm's disclosure has on the market's perception that other firms in the same industry have received firm-specific, value-relevant information that those firms have not yet disclosed.[238] They showed that as long as there is a positive correlation among firms' receipt of information about themselves (as with the advent of

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[234] Aircraft Carrier Release, *supra* note 222 at 67241 note 528 and accompanying text.

[235] *Id.* at 67241.

[236] Based on my experience as a practitioner, I would say this is at least in part due to the advisory and drafting habits of their in-house and outside securities counsel, who look to SEC comments and the disclosures of peer firms while preparing or advising on disclosures, particularly as it pertains to drafting risk factors. The tendency of third-party professional service providers to promote consistent disclosures among issuers has been documented in the case of independent auditors. *See* Kenneth L. Bills, Ryan Cating, Chenxi Lin and Timothy Seidel, *The Spillover Effect of SEC Comment Letters through Audit Firms: Evidence from Subjective Accounting Areas* (March 2019)(finding that when auditors' clients receive comment letters related to topics such as accounting estimates and goodwill, there is an increased likelihood that other clients will record changes in accounting estimates and impairment charges, and that these effects are stronger than the effect of such comment letters across the industry broadly (without influence of auditors on their clients)), https://ssrn.com/abstract=3349191. One asset manager recently opined that issuers aren't sharing more sustainability information with the market because their competitors aren't disclosing it and the SEC doesn't require it. Cydney Posner, *SEC debate on climate disclosure regulation gets heated*, COOLEY PUBCO (Feb. 6, 2020), *available at*: https://cooleypubco.com/2020/02/06/sec-debate-climate-disclosure-regulation/.

[237] Ronald A. Dye and Sri S. Sridhar, *Industry-Wide Disclosure Dynamics*, 33 J. Accounting Research 157 (1995).

[238] *Id.* at 167-68.

an industry-specific event that causes new aspects of firms' business models to become value relevant, as might occur with new legislation or new social trends), investors' re-assessments of the firms upon disclosure of the information by one firm increases the probability that other firms will disclose their information subsequently.[239] Dye and Sridhar argue their theory explains herding behavior in firms' disclosures.[240] Under the Dye and Sridhar model, one might expect that the social trend towards more investment in ESG funds and scrutiny of ESG issues might encourage companies to review the ESG disclosures of their competitors and consider amending their own disclosures.

Since the Dye and Sridhar paper, a variety of empirical studies have documented examples of herding behavior in disclosures. Several studies have looked at herd behavior in earnings announcements following the SEC's requirement that earnings releases be furnished on Form 8-K. One study found that peer's disclosure choices appear to affect other firms' earnings management decisions.[241] Controlling for industry and firm characteristics, firms are more likely to begin managing earnings after the public announcement of a restatement by another firm in their industry or geographic region.[242] In another study of herding behavior in earnings release disclosures the authors found that when an industry leader underperforms analysts' expectations, followers report lower discretionary accruals, have fewer income-decreasing special items, and are less likely to meet analysts' expectations. In contrast, when leaders report good news, followers report higher discretionary accruals and are more likely to meet expectations.[243] To explain this result, the authors postulate that managers

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[239] *Id.* at 158.

[240] *Id.* at 168.

[241] Simi Kedia, et al., *Evidence on Contagion in Earnings Management*, 90 The Accounting Review 2337 (2015).

[242] *Id*.

[243] Brian Bratten, et al. *Earnings Management: Do Firms Play "Follow the Leader"?* 33 CONTEMPORARY ACCOUNTING RESEARCH 616 (Summer 2016). Industry leaders were defined as firms in the top quartile of market capitalization in their industry. *See also*, Nerissa C. Brown, Lawrence A. Gordon and Russell R. Wermers, *Herd Behavior in Voluntary Disclosure Decisions: An Examination of Capital Expenditure Forecasts* (March 2006)(finding that managers are more likely to disclose capital expenditure plans when prior peer forecasts signal a decrease in capital spending and when prior peer forecasts are more precise, implying herding behavior), https://ssrn.com/abstract=649823; Rosemond Desir, *How Do Managers of Non-Announcing Firms Respond to Intra-Industry Information Transfers?*, 39 J. OF BUS. FIN. & ACC. 1180 (2012) (finding that managers in more-concentrated industries are more likely to disclose good news following a rival's good news, while managers in less-concentrated industries are more likely to disclose good news following a rival's bad news); David A. Reppenhagen, *Contagion of accounting*

of later reporting firms believe the earnings news of prior reporting industry leaders will affect the market's performance expectations for their firms, so the industry leaders' reports affect the discretionary reporting decisions of the later reporting firms.

Similar herd behavior phenomena have been observed with respect to risk factor disclosures. A study by Karen Nelson and Adam Pritchard found that risk factor disclosures of firms with low litigation risk converged with the higher quality disclosures of firms with high litigation risk following the implementation of the SEC's mandatory risk factor disclosure rule.[244] After the SEC mandated risk factor disclosure in 2005, firms with lower quality risk factors improved their disclosure by increasing the amount of disclosures, revising the disclosures more extensively each year and using more readable language, leading to more similar disclosures between firms with high and low litigation risks.[245] Thus, subsequent to the SEC mandate, the low-risk firms converged towards high-risk firms in terms of how meaningful their risk factor disclosures were to investors.[246] When there was little net benefit to additional disclosure, firms did not provide meaningful disclosure until compelled to do so.[247]

Disclosure under the watchful eye of the SEC has also been found significant. Studies appear to show that issuers pay attention to the

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methods: evidence from stock option expensing, 15 REV. ACCOUNT. STUD. 629 (2010)(finding that later reporting firms adopt the stock option expense accounting methods of earlier reporting firms since the prior adoptions are informative and change the net benefits of adopting the accounting method). Cf. Ling Tuo, Ji Yu and Yu Zhang, *How do industry peers influence individual firms' voluntary disclosure strategies?,* 54 REV. OF QUANT. FIN. & ACCOUNT. 911 (2020)(documenting peer firm influence in frequency and disclosure horizon of management earnings forecast disclosures, finding no industry leader effects, and attributing the influence more to signaling theory and litigation risk than to herding theory and free rider theory).

[244] Karen K. Nelson and A. C. Pritchard, *Carrot or Stick? The Shift from Voluntary to Mandatory Disclosure of Risk Factors*, 13 J. Emp. Leg. Stud. 266 (2016).

[245] *Id.* at 267. Increases in industry-wide risk factor disclosures may be more significant than increases in firm-specific risk factor disclosures. Todd Kravet and Volkan Muslu, *Textual risk disclosures and investors' risk perceptions* 18 Rev. Account. Stud. 1088, 1090, 1110 (2013)(finding stronger relations between risk disclosures and market perceptions for industry-level disclosures than for firm-specific disclosures).

[246] *Id.* at 268.

[247] *Id.* Firms may be reluctant to provide additional risk disclosure in low liability environments because increased risk disclosures lead to stock return volatility, higher trading volumes and dispersion of forecast revisions. *See* Kravet and Muslu, *supra* note 245 (finding that annual changes in risk disclosures are significantly and positively associated with changes in daily stock return volatility, relative volatility of negative daily returns, trading volume, and volatility of forecast revisions).

comments that the SEC makes on the disclosures of their industry peers so they can amend their own disclosures accordingly. Accounting studies have shown that firms react not only to comment letters from the SEC on their own disclosures but also to comment letters on the disclosures of peer firms. One study found that firms tend to edit their disclosures to reflect comments the SEC has made on the filings of industry leaders, in particular.[248] Another study showed that SEC comment letters generally lead to improved disclosure, a decrease in information asymmetry and a reduction in litigation risk.[249]

Most importantly for purposes of assessing the value of a rule requiring sustainability reports to be furnished to the SEC on Form 8-K, studies have found that firms tend to copy one another's disclosures with respect to matters on which there is little or no SEC guidance. Firms exhibit increases in quantity and detail of disclosure over time when they initially lag the disclosures of industry peers with respect to new issues for which there is no existing authoritative guidance from the SEC.[250] One study provides a theory to explain the improvement of voluntary disclosures over time: firms may compete for capital by increasing their voluntary disclosures in instances in which industry peers are receiving more institutional capital.[251]

While mandatory sustainability disclosures pursuant to guidelines enunciated by the SEC would be a strong way to improve the comparability

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[248] Stephen V. Brown, et al., *The Spillover Effect of SEC Comment Letters on Qualitative Corporate Disclosure: Evidence from the Risk Factor Disclosure*, 35 CONT. ACCT. RES. 622 (Summer 2018)(finding that firms not receiving SEC comment letters modify their subsequent disclosure more if the SEC has commented on the risk factor disclosures of (1) the industry leader, (2) a close rival, or (3) numerous industry peers); *see also*, Bills, et al., *supra* note 236.

[249] Zahn Bozanic, et al., *SEC comment letters and firm disclosure*, 36 J. Account. & Pub. Policy 337 (2017). *See also* Miguel Duro, et al., *The effect of enforcement transparency: Evidence from SEC comment-letter reviews*, 24 REV. ACCT. STUD. 780 (2019) (finding that the effect of regulatory oversight was enhanced by the public disclosure of SEC comment letters on registrant filings).

[250] Karen M. Hennes and Kristy M. Schenck, *The Development of Reporting Norms without Explicit Guidance: An Example from Accounting for Gift Cards*, 28 ACCOUNTING HORIZONS 561 (2014)(finding that evolution of reporting norms for gift card breakage demonstrates that the SEC, peers, and auditors all have roles in quickly shaping U.S. reporting norms in the absence of formal disclosure requirements).

[251] Yupeng Lin, et al. *Institutional Ownership, Peer Pressure, and Voluntary Disclosures*, 93 THE ACCOUNTING REVIEW 283 (July 2018)(finding that increase in institutional ownership and resultant improvement in the information environment of the top Russell 2000 index firms create pressures on their industry peers to increase voluntary disclosures to improve their own informational environments and compete for capital).

of sustainability disclosures relatively quickly,[252] the foregoing studies suggest that requiring companies to submit their existing voluntary sustainability reports to the SEC's EDGAR system, where they will be subject to easier scrutiny by the investing public, corporate competitors and the watchful eye of the SEC, would still lead to improvements in the comparability of reports over time through disclosure herding behavior among peers. The calls from BlackRock, State Street Global Advisors, and the International Business Council of the World Economic Forum for listed companies to begin reporting sustainability metrics according to the SASB framework in January 2020[253] should create momentum towards the use of such standards for reporting[254] which can be accelerated through herding behavior generated by posting of the reports on the SECs EDGAR system.

C. *Increasing Reliability*

One of the causes of the inadequate reliability of the information included in sustainability reports today is that the reports are neither prepared nor reviewed by the finance and legal functions at many firms. They are primarily prepared by public relations or corporate social responsibility professionals who have not been trained in how to prepare disclosures for investors. Most large companies now have a separate sustainability team to work on ESG communications and reporting.[255] The

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[252] Fisch, *supra* note 13, at 961-962. Increased mandatory disclosure through the SEC's Form 8-K requirements have also been shown to promote the efficiency of price formation. Jeff L. McMullin, et al., *Increased mandated disclosure frequency and price formation: evidence from the 8-K expansion regulation*, 24 REV. ACCOUNT. STUD. 1 (2019)(finding that regulations increasing the frequency of mandated disclosures of material events on Form 8-K increased the speed of price formation and firms with the largest increases in disclosure exhibited the greatest improvements in price formation efficiency).

[253] *See supra* notes 53 and 126.

[254] David M. Silk, Sabastian V. Niles and Carmen X. W. Lu, Wachtell, Lipton Rosen & Katz, *Acccelerating ESG Disclosure – World Economic Forum Task Force*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Feb. 10, 2020), *available at*: https://corpgov.law.harvard.edu/2020/02/10/accelerating-esg-disclosure-world-economic-forum-task -force.

[255] Andrew Holt, *Most large firms have ESG communications team, reveals new report,* IR MAGAZINE (June 13, 2019), https://www.irmagazine.com/esg/most-large-firms-have-esg-communications-team-reveals-new-report. *See also*, SASB Legal Roundtable, *supra* note 106 at 6 (noting that sustainability departments exist in silos, separate from finance, accounting, risk management, investor relations, compliance, and other departments or functions potentially relevant to rigorous sustainability disclosure); Paul A. Davies, Paul M. Dudek and Kristina S. Wyatt, *Environmental, Social and Governance Matters: The Rapidly Evolving ESG Reporting Landscape – Part 1*, 41 SEC. AND FED. CORP. L. REP. 113, 121 (July 2019).

environment for production of sustainability reports has been described as "loosely-controlled".[256] The American Institute of CPAs ("AICPA") has noted that the finance and sustainability functions in most U.S. companies have limited interaction and are not fully aligned.[257] Furthermore, the sustainability reports are subject to disjointed processing and limited internal controls, which significantly increases the risk of reporting imprecise or inaccurate information.[258]

Disclosures filed by U.S. public companies with the SEC are required to be subject to disclosure controls and procedures described in their annual reports on Form 10-K.[259] Thus, companies are more likely to have the disclosure included in their sustainability reports reviewed by divisions in the organization responsible for disclosure controls and procedures, such as the general counsel, chief accounting officer and chief financial officer, if the reports are furnished to the SEC on Form 8-K. Among other things, this process typically requires certifications from persons preparing the information that it is accurate in all material respects in order to support certifications of the CEO and CFO are required to provide pursuant to the SEC's rules.[260] The rigor of the disclosure controls and procedures process should improve the reliability of the disclosure.

In response to the SEC's 2002 proposal to accelerate deadlines for annual and quarterly reports, the American Bar Association's Subcommittee on Disclosure and Continuous Reporting of The Committee on Federal Regulation of Securities, Section of Business Law proposed alternatively that the SEC should require companies to file their earnings reports on Form 8-K. The ABA subcommittee noted that such a requirement would enhance the attention and level of care companies bring to those disclosures because companies would be aware that the disclosures will become part of the formal reporting system.[261] They also acknowledged that bringing the earnings release disclosures into the formal disclosure system would make

[256] CITE

[257] AICPA Letter, *supra* note 92 at 3. The AICPA goes on to note that a 2013 KPMG Survey of Corporate Responsibility Reporting revealed that 25% percent of the 100 largest companies in 41 countries that prepared a corporate responsibility report, made some form of restatement in 2013, with 21% of restatements due to errors or omissions. *Id.*

[258] *Id.* at 4.

[259] Regulation S-K, Item 307, 17 C.F.R. §229.307.

[260] 17 C.F.R. §240.13a-14, §240.15d-14.

[261] Comments of Stanley Keller, Chair, Comm. On Fed. Reg. of Securities, American Bar Association, et al., Letter to Mr. Jonathan G. Katz, dated June 4, 2002, at 4, https://www.sec.gov/rules/proposed/s70802/skeller1.htm

them available electronically on a widespread basis.[262]

It is possible that directors may also take more interest in sustainability reports if they are furnished to the SEC, even if they are not incorporated by reference into documents on which directors have liability, such as registration statements. If it is an issue being reviewed by the general counsel, it is more likely to be subject to board review as well, since the general counsel is often a direct report to the board. If the sustainability report is in front of the board, it is more likely to become part of the broader discussion of risks faced by the company as part of the board's review of corporate risks.

Fears that sustainability disclosure will decline if reports are required to be furnished to the SEC because companies will be more cautious about disclosures in such an environment are probably overblown. At the time Regulation FD was introduced, the business community and other commentators warned that fears of liability and other concerns would cause companies to disclose less information to the market.[263] In fact, public corporate disclosure expanded as a result of the rule, with almost five times the number of companies publicly releasing earnings guidance and four times the number of earnings webcasts.[264] The first formal empirical study concluded that there was no evidence that Regulation FD impaired the quality or quantity of investors' information and noted "a marked increase in firm's voluntary disclosure frequency."[265] There is some disagreement among later studies in the accounting and financial literature, with some finding increases or at least no reduction in disclosure, [266] and others finding

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[262] *Id.*

[263] Reg FD Adopting Release, *supra* note 33, at 51718, 51726. Scott Russell, *Regulation Fair Disclosure: The Death of the Efficient Capital markets Hypothesis and the Birth of Herd Behavior*, 82 B.U. L. Rev. 527, 545 (2002)(summarizing concerns about a chilling effect on disclosures); Peter Talosig III, *Regulation FD – Fairly Disruptive? An Increase in Capital Market Inefficiency*, 9 Fordham J. Corp. & Fin. L. 637 (2004).

[264] Fisch*, supra* note 216 at notes 32 and 35 and accompanying text.

[265] *Id.* at notes 41 and 42 and accompanying text, *citing* Frank Heflin, K.R. Subramanyam & Yuan Zhang, *Regulation FD and the Financial Information Environment: Early Evidence*, 78 ACCT'G REV. 1 (2003).

[266] Brian J. Bushee, Michael J. Jung & Gregory S. Miller, *Do Investors Benefit from Selective Access to Management?*, 2 J. Fin. Rep. 31 (2017)(summarizing literature finding that Regulation FD expanded real-time access to firms' disclosures); Adam S. Koch, Craig E. Lefanowicz, and John R. Robinson, *Regulation FD: A Review and Synthesis of the Academic Literature*, 27 Acct. Horizons 619 (2013)(same); Praveen Sinha & Christopher Gadarowski, *The Efficacy of Regulation FD* , 45 FIN . REV. 331 (May 2010) (describing mixed results of studies of disclosure quality and quantity post Regulation FD); Anchada Charoenrook & Craig M. Lewis, Information, Selective Disclosure, and Analyst Behavior,

some reduction in disclosure as a result of the new rule.[267]

While a mandatory disclosure system requiring sustainability disclosures to be included in annual reports, for which the disclosures must actually be certified by executive officers and on which the directors have personal liability when disclosures are incorporated into registration statements, would undoubtedly improve the reliability of the sustainability disclosures,[268] the SEC's experience with disclosures under Form 8-K, described above, suggest that requiring voluntary sustainability reports to be furnished on Form 8-K will still produce more reliable information over time as firms ensure the reports are reviewed by corporate divisions responsible for review of corporate information reported to the SEC.

D. Minimal Additional Cost and Liability Risk

As noted above, cost and liability risk are two of the factors leading corporations to oppose mandatory sustainability disclosures in SEC filings.[269] Requiring companies to furnish their sustainability reports to the SEC would improve the accessibility, comparability and reliability of the information in those reports without imposing significant additional costs or liability risks on corporations. While there would certainly be some increased costs for review of additional corporate information by the compliance and securities regulatory teams, and possible additional auditing costs if firms chose to have the reports audited or reviewed, these costs could be managed by each corporation since the content of the reports would remain at their discretion.

The vast majority of large companies are already producing sustainability reports. Those companies are already incurring the internal procedures costs to collect and evaluate the information necessary to produce the reports, so they should not have to incur significant additional costs as a result of the Form 8-K requirement. The SEC estimated that the additional cost of furnishing earnings releases on Form 8-K would be

Information, Selective Disclosure, and Analyst Behavior, 38 FIN. MANG. 39 (2009) (describing studies finding increased issuer disclosures of earnings guidance)

[267] Edward R. Lawrence, Gordon Karels, Arun Prakash & Siddharth Shankar, Effect of regulation FD on disclosures of information by firms, 21 APPLIED FIN . ECON . 979 (2011)(finding a reduction in disclosures, particularly among smaller firms); Koch, et al., *supra* note 266 (finding a chilling effect on overall information in the market for small or high-technology firms).

[268] *See* Fisch, *supra* note 13 at 962. *See also*, Nelson and Pritchard, *supra* note 244.

[269] *See supra* Section I.B.

minimal.[270] It is possible that the costs of producing sustainability reports could increase in the future if companies begin recording, collecting and reporting more quantitative sustainability metrics in their sustainability reports, but any such increased costs would be entirely voluntary, a matter of the business judgments of individual managers responding to market pressures to provide additional information. If, as anticipated by Section IV.B. above, laggard companies feel pressured to follow the lead of competitors that provide more fulsome disclosure, that again may increase their costs, but would still be voluntary and presumably rewarded with lower costs of capital. That is precisely how opponents of mandatory disclosure would expect private ordering to operate.[271]

As discussed above in Section IV.C., furnishing sustainability reports on Form 8-K may be expected to improve the reliability of the information included therein by subjecting the reports to review by the general counsels and directors of the furnishing companies. Adding sustainability reports to the agendas of general counsels and boards of directors will impose some additional administrative burdens on those bodies that cannot be ignored, but given that the liability risks associated with sustainability reports already exist (and would not change with this proposal), those are arguably costs that corporations should already be incurring from a liability management perspective.

As noted above,[272] information furnished to the SEC on Form 8-K is subject to no more liability than any other information shared by a public company with the markets through any other medium, whether press releases, websites or glossy reports. Thus, furnishing the reports on Form 8-K would not subject reporting companies to any greater liability than they already face by preparing and distributing sustainability reports to the public. In fact, as noted in Section III.B., requiring the reports to be furnished to the SEC could lower the liability risk arising from such reports by subjecting them to the same internal review processes currently utilized for annual reports, proxy statements and other documents filed with the SEC.

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[270] Earnings Release Adopting Release, *supra* note 196 at XXX.

[271] *See*, *e.g.*, Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L. J. 2359 (1998); George J. Bentson, *Required Disclosure and the Stock Market: An Evaluation of the Securities Exchange Act of 1934,* 63 AM. ECON. REV. 132 (1973); George J. Stigler, *public Regulation of the Securities Markets*, 37 J. BUS. 117 (1964).

[272] *See supra* Section III.A.

E. Harnessing Private Ordering Under the Watchful Eye of the Regulator

As noted above, Chairman Clayton and Director Hinman of the SEC are reluctant to impose new mandatory sustainability disclosure requirements on public companies in the U.S. [273] Director Hinman argued it is premature to establish new mandatory rules while the market is still parsing which sustainability metrics are material to investment and voting decisions.[274] One of the benefits of the Form 8-K approach to sustainability disclosure is that it allows companies to continue their dialogue with investors and other stakeholders about which metrics are most important. Furnishing sustainability reports on Form 8-K, rather than requiring specific line-item disclosures today, will permit private ordering to establish the most important sustainability disclosures for each industry. The NASDAQ has stated its view that market-based forces will result in more optimal sustainability related disclosure by public companies than that driven by an SEC mandate.[275]

Companies are already engaging with third-party sustainability standard-setters and investors to determine which measures are most material to particular companies and industries. The AICPA and other commentators have noted that material sustainability issues vary by industry and are evolving over time.[276] The Form 8-K approach will leave companies free to determine, in dialogue with investors and other stakeholders, which sustainability metrics are most material to their investors as needs and expectations evolve over time. This is what companies have been lobbying for and the SEC has endorsed.[277] The SEC has taken and continues to take the approach with respect to earnings releases. SEC permits companies to structure earnings releases in the manner most valuable to their investors and requires them to be furnished rather than filed. When the SEC became concerned about the nature of some of the disclosures in earnings releases – non-GAAP measures – its was able to structure rules that provide guidance on appropriate disclosure without mandating the items companies should include in their earnings releases. Private ordering has worked well in determining the information that should be included in such releases.

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[273] *See supra* Section I.C.

[274] Hinman, *supra* note 167.

[275] Edward S. Knight, Exec. V. P., General Counsel and Chief Regulatory Officer, Nasdaq, Inc., Comment Letter on Concept Release regarding Business and Financial Disclosure Required by Regulation S-K 4 (September 16, 2016), https://www.sec.gov/comments/s7-06-16/s70616-368.pdf.

[276] AICPA Letter, *supra* note 92 at 2.

[277] *See supra* Sections I.B. and I.C.

In addition to minimizing the costs of compliance among corporations, the Form 8-K approach would allow the SEC to save administrative resources by collecting further data before proposing rules for mandatory sustainability disclosures. Encouraging companies to furnish their reports to the SEC will permit private ordering to determine which disclosures are most material before the SEC takes a position on mandatory disclosures, saving administrative as well as corporate resources.

CONCLUSION

There is a growing consensus among investors and academics that sustainability metrics are material to investors seeking long-term growth. Based on this consensus, there has been a renewed push among activists and investors for the SEC to mandate disclosure of various sustainability metrics in the periodic filings of public companies. Corporate interests and the SEC, however, are no more amenable to mandatory sustainability disclosure obligations now than they have been in previous discussions of the issue over the past fifty years.

While integrated reporting may ultimately be necessary to have a fulsome understanding of the factors affecting corporate financial performance and market value, the time for integrated reporting has not yet arrived. The 2020 GAO report notes that regulatory and private-ordering approaches to improving sustainability disclosures involved trade-offs. While new regulatory requirements would improve comparability across companies, a private-ordering approach provides flexibility and limits the potential costs.[278] The SEC can promote incremental progress towards better sustainability reporting and more accountability for such reporting among corporate executives and boards, however, by adopting the proposal described herein: requiring companies that publicly distribute sustainability reports to furnish such reports to the SEC on Form 8-K.

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[278] GAO 2020 Report, *supra* note 49, at 38.