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Forewarned is forearmed: shareholders to benefit from new SEC climate disclosure rules

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On March 21, 2022, in a long anticipated and historic move, the Securities & Exchange Commission proposed new disclosure rules that would require public companies to include climate-related disclosures in their registration statements and periodic reports, such as Forms 10-K and 20-F. Should the proposed rules take effect, public companies that register with the SEC will be specifically required to disclose detailed information about climate-related risks that could have a material impact on their business, as well as the companies' internal policies and procedures that address their preparedness for climate-related risks.

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Registrants would also need to issue disclosures about the greenhouse gas emissions from their direct and indirect business operations. By increasing transparency around corporate disclosures of climate information, the SEC has given shareholders an important tool to inform their investment decision-making and to hold corporations accountable for the impacts of their carbon emissions.

The SEC's new climate disclosure rules are the most comprehensive requirements the agency has ever imposed on climate-related disclosures. In the 534-page proposed rule, the SEC laid out a new set of requirements, including disclosure of: climate-related risks; climate-related effects on strategy, business model, and outlook; board and management oversight of climate-related issues; processes for identifying, assessing, and managing climate risks; plans for transition; financial statement metrics related to climate; greenhouse gas emissions; and climate targets and goals. The requirements go beyond mere disclosure, mandating that companies develop new procedures and policies to govern corporate climate operations and targets.

SEC Chairperson, Gary Gensler, in his statement supporting the proposed rules, stated that the rules are "guided by the concept of materiality." He added that disclosures concerning registrants' greenhouse gas emissions are material, explaining that emissions "are increasingly being used as a quantitative metric to assess a company's exposure to — and the potential financial effects of — climate related transition risks." Gensler further affirmed that the SEC's proposed rules, once enacted, would require disclosure of targets and commitments made by a company, as well as its plan to achieve those targets.

Environmental groups and shareholder rights activists have reacted positively to the SEC's proposed rules. Todd Phillips, director of financial regulatory and corporate governance at the Center for American Progress, was quoted in a March 21 article in The New York Times saying that the proposed rules give investors "access to important information they need to make informed investing decisions." ("The S.E.C. moves closer to enacting a sweeping climate disclosure rule.")

Danielle Fugere, the president of As You Sow, a shareholder representative organization promoting environmental and social corporate responsibility, wrote in *Sierra*, the magazine of the Sierra Club, that the SEC's rules "represent an important step forward in terms of using market mechanisms to spur progress on climate action." ("What Do the New SEC Rules Mean for Action on Climate Change?" March 24, 2022.)

The SEC's proposal is not without its critics, however. SEC Commissioner, Hester M. Peirce, said in a March 21 public statement published on the SEC's website that the proposed rules "undermine the existing regulatory framework that for many decades has undergirded consistent, comparable, and reliable company disclosures" and noted multiple perceived deficiencies in the proposed rules.

The U.S. Chamber of Commerce also raised concerns with the SEC's proposal, stating in a March 21 press release on its website that it "will limit companies' ability to provide information that shareholders and stakeholders find meaningful while at the same time requiring that companies provide information in securities filings that are not material to investors." Nevertheless, the Chamber stated that it was "committed to working constructively with the SEC to develop clear and workable rules for climate disclosures."

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These critics fail to meaningfully address the recent findings on the significant impact climate change will have on the environment and the global economy. By adding new climate-related disclosure requirements for public companies, the SEC is increasing transparency for investors at a time when climate risks are increasingly relevant. The United Nations' Intergovernmental Panel on Climate Change released a report on April 4, 2022, stating that, even if carbon emissions fall by 43% by 2030, the world is likely to surpass the 1.5-degree Celsius goal set by the Paris Agreement.

In a report released last year, economists at the Swiss Re Institute, the research arm of one of the world's largest insurance companies, projected that the world stands to lose approximately 10% of its total economic value from climate change if temperature increases remain on their current trajectory. The SEC's new rules, if approved, would help investors understand how the companies they have invested in are dealing with the impacts of climate change and the actions taken to mitigate climate change.

Increased transparency not only helps inform shareholders, but it further arms them with the information they need to punish fraud and govern their investments. Shareholder activism around environmental issues is already increasing. Last year, ExxonMobil and Chevron, two of the United States' largest fossil fuel corporations, faced shareholder rebellions over their failures to take action on climate risks.

A hedge fund, invested in Exxon, successfully replaced two Exxon board members with its own candidates in its effort to promote "greener" business strategies from the oil giant. At Chevron, a majority of shareholders voted 61% in favor of an activist proposal to require the company to cut its carbon emissions. Shareholder activism will only increase as companies provide investors with more information about their climate-related operations and targets. Exxon and Chevron are likely just the beginning.

Investors and regulators continue to use the securities laws to hold public companies accountable for climate-related securities fraud. The Climate Change Litigation Database for U.S. Climate Change Litigation, a project conducted in collaboration with Columbia Law School's Sabin Center for Climate Change Law, identified 24 cases in the past 10 years involving securities laws and climate change. As companies are required to disclose more information about how they are managing climate risks and emissions, investors may discover that the truth of how a company is actually handling climate issues contradicts what it has told investors. The SEC's new rules will further empower investors to hold companies to account.

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The SEC's climate-change disclosure rules are not yet final, and any final rules adopted by the SEC will likely be challenged in court. While the specifics of the SEC's proposed rules may be adjusted in response to public comments and legal challenges, the general goal of enhancing corporate disclosure around climate-related business operations will remain. Increased transparency begets increased accountability and, if the rules become final, shareholders will become better equipped to ensure the companies they invest in are prepared for a future further impacted by carbon emissions and climate change.

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