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SEC's Focus on Climate and Environmental, Social and Governance Issues

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While the U.S. Securities and Exchange (SEC) has not been very active in holding companies accountable for failing to report climate-related information, litigation under state provisions—and the growing urgency of climate-related risks—has shown the need for more active enforcement.

In recent years, states have pursued companies for allegedly making misleading financial disclosures in violation of state statutes. In 2015, for example, the New York Attorney General entered into a settlement with Peabody Energy Corporation involving misleading disclosures under New York-specific statutes. After subpoenaing internal records that showed the company had made internal market projections showing severe negative impacts from certain potential laws and regulations and had failed to disclose those projections to the public, the company agreed to enhance disclosures relating to climate change and greenhouse gas emissions in their annual reports. Failure to disclose information known internally about climate-related information and risks has also resulted in litigation. See, e.g., Ramirez v. Exxon Mobil Corp., 334 F. Supp. 3d 832, 859 (N.D. Tex. 2018) (allowing shareholders to proceed on claims against Exxon alleging that the company had made materially misleading statements regarding climate-related information in its disclosures); Complaint, Massachusetts v. ExxonMobil Corp., No. 19-3333 (Mass. Sup. Oct. 24, 2019) (alleging that ExxonMobil misled investors, as well as consumers, in violation of Massachusetts business regulation and consumer protection statutes).

The SEC has taken several steps recently that signal the new administration is making climate issues a priority. On March 3, 2021, the Commission announced its 2021 examination priorities for the Division of Examinations, which include an enhanced focus on climate-related and environmental, social, and governance (ESG) issues. The next day, the Commission also announced the creation of a Climate and ESG Task Force. Led by Kelly L. Gibson, the Acting Deputy Director of Enforcement, the Climate and ESG Task Force will initially focus on "any material gaps or misstatements in issuers' disclosure of climate risks under existing rules." The Climate and ESG Task Force will also develop initiatives to proactively identify ESG-related misconduct.

These announcements follow other recent steps taken by the Commission that demonstrate its focus on climate-related and ESG matters across the agency's divisions. The Commission appointed a Senior Policy Advisor for Climate and ESG, Satyam Khanna, to oversee and coordinate its climate and ESG initiatives. Prior to this announcement, the Acting Chair Allison Herren Lee directed the Division of Corporation Finance to update guidance on climate-related disclosures in public company filings. On March 15, 2021, the SEC requested public comments on climate-related disclosures. This request seeks input on the process for providing disclosures, the content of the disclosures, and the advantages and disadvantages of specific approaches.[1]

What are climate-related disclosures?

Section 13(a) of the Securities Exchange Act requires every issuer of a security registered pursuant to

Section 12 of the Act to file certain reports periodically with the SEC. 15 U.S.C. § 78m(a). In addition to expressly required information, companies must add "such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading." 17 C.F.R. § 230.408; see also 17 C.F.R. § 240.12b-20 (requiring companies to include in their Forms 10-Q additional material information as necessary to make them not misleading). In the 2010 Commission Guidance Regarding Disclosure Related to Climate Change, the SEC identified the specific areas within these disclosure requirements that provide for climate-related information. For example, companies must report certain costs associated with complying with environmental laws. They also must report information such as legal proceedings to which the company is a party, certain environmental litigation, and significant risk factors, an assessment that should take into account climate-related risks.

In addition to identifying where climate-related information should be included in existing disclosure requirements, the Commission's 2010 guidance provided some insight into how climate change may impact companies in a way that would require disclosure. As the Commission noted then—and especially pertinent now with the new federal administration—changes in the regulatory and legislative environment could have significant impacts on companies' financial decisions, operations, and assessment of risk. The physical effects of climate change may also alter companies' business and operations, by limiting availability and access to natural resources, damaging physical facilities or equipment, or even reducing consumer demand for specific products.

The 2010 guidance left many questions unanswered about what should be included in climate-related disclosures. The Commission seems poised to provide greater clarity on this subject in the future, as indicated in its request for public comments, and it has some useful models for guidance. For example, the Task Force on Climate-Related Financial Disclosures (TCFD) was established specifically to develop recommendations for more effective climate-related disclosures. The TCFD is an international partnership created by the Financial Stability Board, an international body established after a G20 Summit with a mandate to monitor and make recommendations about the global financial system. In 2017, the TCFD presented its final report with recommendations for helping businesses disclose climate-related financial information. These existing recommendations may serve as a template for the SEC.

Public comments thus far in response to the SEC's request for input into climate-related disclosure guidance have been varied. Some commenters urge the SEC to stay in its lane, arguing that the issue of climate change is unrelated to the Commission's mandate to protect investors. Others have welcomed the Commission's decision to focus on updating guidance now over a decade old, especially as significant regulatory and legislative changes are expected in the near future. Among the commenters was Patrick Morrisey, Attorney General for the State of West Virginia, who warned that the Commission's efforts to compel specific disclosures on climate-related and ESG issues may lead to First Amendment violations for compelling speech. In contrast, Keir D. Gumbs, Vice President, Deputy General Counsel and Deputy Corporate Secretary of Uber Technologies, Inc. welcomed the SEC's focus on climate-related matters. His comment urged the Commission to model disclosures after those created by the TCFD, as companies, like Uber, have already invested resources into complying with those frameworks.

What does this mean for whistleblowers?

In addition to announcing the Climate and ESG Task Force, the SEC's March 2021 press release stated that the Commission "will evaluate and pursue tips, referrals, and whistleblower complaints on ESG-related issues, and provide expertise and insight to teams working on ESG-related matters." SEC whistleblowers play a particularly significant role in this regard in that they can provide the SEC valuable information about the nuances of the specific industry and how the companies' misrepresentations harm investors. Indeed, providing specialized knowledge to the SEC as part of an enforcement action may contribute to one of several factors that may enhance a whistleblower's award. The regulations provide that the SEC may consider "[w]hether the whistleblower provided ongoing, extensive, and timely cooperation and assistance by, for example, helping to explain complex transactions, interpreting key evidence, or identifying new and productive lines of inquiry." 17 C.F.R. § 240.21F-6(a)(2)(i).

While some commenters may not welcome the Commission's focus on climate-related and ESG matters, this focus is unlikely to disappear any time soon. States and international bodies have recognized the connection between the impact of climate change on companies across many industries and its potential harm to investors. International partnerships, like the TCFD, are steps ahead of the SEC in making recommendations for global financial systems. Further, the new administration has announced new ambitious goals related to climate change, specifically cutting greenhouse gas pollution. Scientists have increasingly warned of the need to shift away from economies dependent on fossil fuels. The impact of recent climate events, like this past year's winter storms in Texas, will no doubt continue to impact companies and, in turn, their investors.

As climate change impacts communities across the globe, corporate entities are not insulated from its effects. Information about climate-related issues is material to investors. Whistleblowers with expertise in climate and ESG-related issues should be aware of the SEC's renewed focus on these important matters, as they may have specialized knowledge that would assist the SEC in protecting investors.

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[1] The SEC started accepting comments on March 15, 2021 and requested that comments be submitted within 90 days. For more information about submitting a comment, go to: https://www.sec.gov/rules/submitcomments.htm.