ESG and Climate Change Blind Spots: Turning the Corner on SEC Disclosure

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Introduction

Over the last decade, a fundamental shift has taken place amongst global and U.S. institutional investors and asset managers such as BlackRock, Vanguard, State Street, and Goldman Sachs.[1] Global assets under management with sustainability screens have risen 34% between 2016 and 2018 to $30.7 trillion in five major markets (the EU, United States, Canada, Japan, and Australia/New Zealand).[2] Just under 40% of this total ($12 trillion) is held by U.S. investors and asset managers, comprising 26% of money under professional management in the United States, with the dominant strategy being integration of environmental, social, and governance (ESG) data into fundamental value analysis for portfolio selection and management.[3] This shift has occurred because institutional investors have realized the financial value of ESG data integration. A recent Edelman Trust Barometer 2020 special report on institutional investors found that 98% of the top-100 institutional investors in the United States say they consider ESG data in the investment process and that 88% of them agree or strongly agree

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** C. Ben Dutton Professor of Law, Indiana University Maurer School of Law. We presented this Article at the Institute for Law and Economic Policy's Symposium on Governance Wars: Contesting Power and Purpose in the 21st Century Corporation on January 29, 2021. We are grateful to Marc Gross, the *Texas Law Review* editors, and our fellow symposium participants. The Article has also benefitted from helpful insights and comments by Sharon Nelles and Professor Jill Fisch, and from excellent research assistance by Emily McDaniels (IU-Maurer '22). Although we reference the SEC's continuing across-the-agency initiatives to prioritize climate and environmental, social, and governance (ESG) matters under the leadership of Interim Chair Allison Herren Lee, *see infra* note 18 and accompanying text, as this Article is going to press, we have not attempted to update it in any systematic way.

1. *See* Jon Hale, *Sustainable Funds U.S. Landscape Report: More Funds, More Flows, and Strong Performance in 2018*, MORNINGSTAR 4 (Feb. 2019), https://www.morningstar.com/content/dam/marketing/shared/pdfs/sustainability/Sustainable_Funds_Landscape_2018.pdf?utm_source=eloqua&utm_medium=email&utm_campaign=&utm_content=15987 [https://perma.cc/2N97-P5FS] (reporting that BlackRock and Vanguard have begun to provide mainstream ESG equity offerings).

2. GLOB. SUSTAINABLE INV. ALL., 2018 GLOBAL SUSTAINABLE INVESTMENT REVIEW 3 (2018), http://www.gsi-alliance.org/wp-content/uploads/2019/06/GSIR_Review2018F.pdf [https://perma.cc/E9AQ-4Z2W].

3. *Id.* at 4.

that "[c]ompanies that prioritize ESG initiatives represent better opportunities for long-term returns than companies that do not."[4]

Climate change (hereinafter "climate," understood to include the risks and opportunities for companies relating to climate change) is a particular focus of investors' requests for clearer, more consistently presented, and more comparable ESG disclosure. Larry Fink, the CEO of BlackRock, predicts a "fundamental reshaping of finance" as "climate change has become a defining factor in companies' long-term prospects" and "investors are increasingly . . . recognizing that climate risk is investment risk."[5] Here, there is an existing framework for disclosure, put together by the Task Force on Climate-Related Financial Disclosures (TCFD), which is a global consortium of investors, accountants, and company executives. Established by the Financial Stability Board in December 2015 and chaired by Michael Bloomberg with special assistance from former SEC Chair Mary Schapiro, the TCFD seeks disclosure of companies' governance, strategy, risk management, targets, and metrics for evaluating climate risks and opportunities.[6] Its 2020 Status Report states that the TCFD's framework has been endorsed by "over 1,500 organizations globally, including over 1,340 companies with a market capitalization of $12.6 trillion and financial institutions responsible for assets of $150 trillion."[7] The Status Report also highlights that "[o]ver 110 regulators and governmental entities from around the world support the TCFD" (a group that does not yet include the United States) and identifies a range of governmental actions being taken to implement general support for TCFD.[8] Those governmental actions include: the European Commission's (EC) June 2019 publication of *Guidelines on Reporting Climate-Related Information*, which integrates TCFD recommendations into the EC's Non-Financial Reporting Directive

4. EDELMAN, SPECIAL REPORT: INSTITUTIONAL INVESTORS, U.S. RESULTS 13, 15 (2020), https://www.edelman.com/sites/g/files/aatuss191/files/2020-11/Edelman%202020%20Institutional%20Investor%20Trust_FINAL.pdf [https://perma.cc/3ZFT-LR3D].

5. Larry Fink, *A Fundamental Reshaping of Finance*, BLACKROCK (2020), https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter [https://perma.cc/S9WE-3DHP]. BlackRock's assets under management as of September 2020 were $7.81 trillion. *BlackRock Reports Third Quarter 2020 Diluted EPS of $8.87, or $9.22 as Adjusted*, BLACKROCK 1 (Oct. 13, 2020), https://s24.q4cdn.com/856567660/files/doc_financials/2020/Q3/BLK-3Q20-Earnings-Release.pdf [https://perma.cc/M29A-P524].

6. *About*, TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES, https://www.fsb-tcfd.org/about/ [https://perma.cc/SUY5-DHUX]; *Task Force Members*, TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES, https://www.fsb-tcfd.org/members/ [https://perma.cc/Z7BR-EPXH].

7. FIN. STABILITY BD., TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES: TCFD 2020 STATUS REPORT 2 (2020), https://www.fsb.org/wp-content/uploads/P291020-1.pdf [https://perma.cc/AWP6-RM9W].

8. *Id.* at 2–3.

(NFRD);[9] consultations among financial supervisors, central banks, and government advisory committees in the EU, Australia, Canada, Colombia, Hong Kong, Japan, Malaysia, Mexico, New Zealand, Singapore, South Africa, and the U.K. aimed at promulgating mandatory TCFD disclosure requirements or issuing guidelines for firms' disclosures referencing TCFD standards;[10] and the April 2019 publication of *A Call for Action: Climate Change as a Source of Financial Risk* by the Network for Greening the Financial System (NGFS), which encouraged all companies issuing public debt or equity to disclose in line with the TCFD recommendations.[11] Notably—and a harbinger for changes to come—the U.S. Federal Reserve Bank recently joined the seventy-four other central banks and supervisors in the NGFS.[12]

And yet, as U.S. and worldwide investors are increasingly demonstrating the financial value of ESG information and as securities and bank regulators across the globe work towards mandatory climate disclosure, the SEC has been, to date, failing to act. We focus this paper on four areas in which the SEC has resisted reform or impeded shareholders' access to sought-after ESG information: (1) the SEC's refusal to act on rulemaking petitions calling for expanded ESG disclosure; (2) the SEC's grudging promulgation of rules concerning social disclosures as required by Congress in the Dodd–Frank Act of 2010; (3) the recent revisions to SEC Rule 14a-8 that make the submission of shareholder proposals more difficult, thereby thwarting investor efforts to raise ESG concerns; and (4) the SEC's commitment to moving away from line-item disclosure towards a more principles-based system.

After discussing the SEC's actions and inactions in these four areas, our paper turns to some of the reasons for the agency's ESG disclosure reticence, notwithstanding the clear trends indicating the importance of such information to investors. The SEC's regulatory agenda post-Dodd–Frank has been daunting, so it is understandable that addressing ESG disclosure issues was not an early priority in the wake of the Act. But we believe there is more to the lack of prioritization than capacity constraints.

First, there seems to be a blind spot in place that either mistakenly assumes issuers already operate under an affirmative disclosure obligation

9. EUROPEAN COMM'N, GUIDELINES ON REPORTING CLIMATE-RELATED INFORMATION 4 (2019), https://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf [https://perma.cc/5N5L-DMUV].

10. FINANCIAL STABILITY BD., *supra* note 7, at 72–73.

11. NETWORK FOR GREENING THE FIN. SYS., A CALL FOR ACTION: CLIMATE CHANGE AS A SOURCE OF FINANCIAL RISK 3 (2019), https://www.ngfs.net/sites/default/files/medias/documents/synthese_ngfs-2019_-_17042019_0.pdf [https://perma.cc/53GZ-D7WY].

12. Martin Arnold, *Fed Joins Central Bankers Backing Paris Climate Goals*, FIN. TIMES (Dec. 15, 2020), https://www.ft.com/content/008a12d2-7736-4db0-af9c-e063a0bcdd7a [https://perma.cc/UY3C-X3V2].

when ESG information is material or more generally resists the concept that much ESG information is material, decision-useful information using traditional definitions of "materiality." As then-Commissioner Robert Jackson lamented in December 2019, some of the SEC's reluctance toward the recognition of ESG information's materiality appears premised on "untested empirical assertion[s] about investor behavior based exclusively on . . . intuition" and the substitution of a "view from Washington about what is important for the collective views of investors around the world."[13] Given that investors managing trillions of dollars of invested capital have stated that ESG disclosure in the United States is currently insufficient,[14] the SEC's intuitions and views are difficult to square with the actual evidence.

The SEC's blind spot toward ESG significance, however, is also a symptom of a larger and more endemic blind spot. Specifically, many SEC officials adhere to an unduly narrow construction of the SEC's tripartite mission—to protect investors; maintain fair, orderly, and efficient capital markets; and facilitate capital formation—and they thereby regard disclosure to "effectuate social policy or political change" as "disclosure that does not fit within our core mission."[15] Yet, as one of us has long argued, in adopting the federal securities laws in the 1930s, Congress had a broader understanding of disclosure,[16] which included giving shareholders information on how America's public companies were being managed and

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13. Robert J. Jackson, Jr., Statement on Proposed Disclosure of Issuer Payments Related to Extraction of Natural Resources (Dec. 18, 2019), https://www.sec.gov/news/public-statement/statement-jackson-2019-12-18-resource-extraction [https://perma.cc/DEQ7-BQ8Z]. ESG disclosure resistance has roots dating back decades. *See* Roberta S. Karmel, *Disclosure Reform—The SEC Is Riding off in Two Directions at Once*, 71 BUS. LAW. 781, 790 (2016) (contending that "the forces buffeting the SEC today are part of a recurring pattern of reformers calling for deregulation and simplification of SEC disclosures while other reformers call for public companies to make more extensive disclosures—particularly those designed to change corporate conduct—and prevent past disclosure failures from reoccurring").

14. *See* Cynthia A. Williams & Jill E. Fisch, Petition for SEC Rulemaking on Environmental, Social, and Governance Information Disclosure (Oct. 1, 2018), https://www.sec.gov/rules/petitions/2018/petn4-730.pdf [https://perma.cc/YTA2-8L7L] (stating that investors representing approximately $5 trillion of invested capital supported the petition calling on the SEC to require comprehensive ESG disclosure). The petition was also supported in submitted comments by global investors within the International Corporate Governance Network, representing over $34 trillion. International Corporate Governance Network, Request for Rulemaking on Environmental, Social and Governance (ESG) Disclosure 1 (Mar. 21, 2019), https://www.sec.gov/comments/4-730/4730-5159355-183433.pdf [https://perma.cc/9NAX-GXSC].

15. *See, e.g.*, Mary Jo White, Chair, U.S. Sec. & Exch. Comm'n, The Importance of Independence at the 14th Annual A.A. Sommer, Jr. Corporate Securities and Financial Law Lecture, Fordham Law School (Oct. 3, 2013), https://www.sec.gov/news/speech/spch100113mjw [https://perma.cc/LB7K-BHTZ] (arguing for respect of the SEC's independence and expertise by "those who seek to effectuate social policy or political change through the SEC's powers of mandatory disclosure").

16. Cynthia A. Williams, *The Securities and Exchange Commission and Corporate Social Transparency*, 112 HARV. L. REV. 1197, 1237–38, 1245–46 (1999).

how companies and banks were exercising power—power that had profound effects on the American economy. Fundamentally, Congress sought mechanisms of corporate accountability, which we argue is precisely what it sought to achieve in the Dodd–Frank ESG provisions—and what today's investors are demanding through the shareholder proposal process and through ESG-rulemaking petitions. ESG disclosure would not be in service of pursuing any individual commissioner's "environmental and social vision for the world," as Commissioner Elad Roisman has suggested.[17] Rather, expanded ESG disclosure would be in service of informing shareholders' voting, engagement with management, and investing, all of which we argue is demonstrably within the core of the SEC's mission.

Today, in early 2021, the SEC is undertaking further analysis of investors' calls for expanded ESG disclosure, and the agency is acting more rapidly to prioritize climate and ESG disclosure than even our most optimistic predictions in early January would have suggested.[18] Some of the prior sources of resistance may thus become less relevant in that undertaking. But we hope this Article illuminates some of the more persistent misconceptions that could thwart effective SEC action as the process for expanded ESG disclosure continues to unfold.

17. Elad L. Roisman, Comm'r, U.S. Sec. & Exch. Comm'n, Keynote Speech at the Society for Corporate Governance National Conference (July 7, 2020), https://www.sec.gov/news/speech/roisman-keynote-society-corporate-governance-national-conference-2020 [https://perma.cc/4CBL-TR5C].

18. *See, e.g.*, Allison Herren Lee, *Public Input Welcomed on Climate Change Disclosures*, U.S. SEC. & EXCH. COMM'N (Mar. 15, 2021), https://www.sec.gov/news/public-statement/lee-climate-change-disclosures [https://perma.cc/WW2S-QNFE] (stating that "[i]n light of demand for climate change information and questions about whether current disclosures adequately inform investors, public input is requested from investors, registrants, and other market participants on climate change disclosure"); Allison Herren Lee, *Statement on the Review of Climate-Related Disclosure*, U.S. SEC. & EXCH. COMM'N (Feb. 24, 2021), https://www.sec.gov/news/public-statement/lee-statement-review-climate-related-disclosure [https://perma.cc/F6EC-6572] (directing the Division of Corporation Finance to evaluate its prior guidance on climate change, discussed at *infra* text accompanying notes 133–39, "on the path to developing a more comprehensive framework that produces consistent, comparable, and reliable climate-related disclosures"); Memorandum from David M. Silk, Sabastian V. Niles & Carmen X. W. Lu, Wachtell, Lipton, Rosen & Katz (Feb. 4, 2021), https://www.wlrk.com/webdocs/wlrknew/WLRKMemos/WLRK/WLRK.27354.21.pdf [https://perma.cc/U9WA-JG64] (discussing other likely SEC actions to require expanded disclosure of climate and ESG matters). *See also SEC Response to Climate and ESG Risks and Opportunities*, U.S. SEC. & EXCH. COMM'N (Mar. 25, 2021), https://www.sec.gov/sec-response-climate-and-esg-risks-and-opportunities [https://perma.cc/9GXA-ERKG] (hyperlinking to documents cataloging a host of SEC initiatives).

I. The SEC's Recent Resistance to ESG Reform

A. Petitions Seeking Expanded ESG Data from Issuers

In October 2018, we were among a group of SEC petitioners seeking a new rule requiring clearer, more consistent, and more easily comparable ESG information from issuers subject to the SEC's jurisdiction.[19] There were three underlying premises supporting that petition. First, much ESG data is relevant to the strategic risks and opportunities facing American companies, including longer term risks.[20] Second, many of America's largest asset managers and public pension funds have recognized the financial value of ESG information, have started to integrate it into their financial analyses, but have also stated that there are substantial problems with the quality of the information currently being produced pursuant to voluntary disclosure initiatives.[21] And third, in response to changing business norms and pressure from investors, 83% of America's largest 100 public companies are voluntarily producing reports containing such "sustainability information," but without the clarity to companies and assurance to investors that would come from using standardized reporting frameworks.[22]

Yet, 2018 was hardly the first time advocates or investors had petitioned the SEC for expanded ESG disclosure. Other notable petitions included: a request in 2009 by the Social Investment Forum (SIF) for a new, annual requirement for ESG disclosure, modeled on the framework of the Global Reporting Initiative (GRI);[23] a 2011 request by ten securities law scholars at leading law schools, in the wake of the U.S. Supreme Court's decision in *Citizens United v. Federal Election Commission*,[24] that urged new rules requiring public companies to "disclose to shareholders the use of corporate resources for political activities";[25] a 2016 request by the investment adviser

19. Williams & Fisch, *supra* note 14.

20. *Id.* at 1–2.

21. *Id.* at 6–8.

22. *Id.* at 9–12.

23. Social Investment Forum, Petition to the SEC for Rulemaking Concerning Mandatory Sustainability Reporting and Disclosure 2 (July 21, 2009), https://www.sec.gov/rules/petitions/2009/petn4-642.pdf [https://perma.cc/93FD-JGTA] (explaining that the "GRI was established to develop standardized indicators for reporting on ESG and continues to evolve these over time through a public and transparent standards-setting process"). The petition also asked the SEC to issue interpretive guidance "to clarify that companies are required to disclose short- and long-term sustainability risks in the Management Discussion and Analysis section of the 10-K (MD&A)." *Id.*

24. 558 U.S. 310 (2010).

25. Committee on Disclosure of Corporate Political Spending, Petition to the SEC to Require Disclosure of Use of Corporate Resources for Political Activities 1, 7 (Aug. 3, 2011), https://www.sec.gov/rules/petitions/2011/petn4-637.pdf [https://perma.cc/8RNV-BGJX] (arguing that for shareholder mechanisms to hold management accountable to work, "shareholders must have information about the company's political speech").

for the Pax Ellevate Global Women's Index Fund for a rule requiring public companies to disclose gender pay ratios on an annual basis;[26] and a 2017 request by the Human Capital Management Coalition, a group of institutional investors with $2.8 trillion in assets, for the adoption of new rules "requir[ing] issuers to disclose information about their human capital management policies, practices and performance."[27] The 2011 political spending disclosure petition is particularly noteworthy because it generated more than 1.2 million comments, the most in the agency's history.[28] Four years later, though, Congress responded and has each year since prohibited the SEC from using appropriated funds to adopt a disclosure rule in this area.[29]

A number of factors, apart from Congress's limited intervention, likely explain the SEC's failure to act on any of these rulemaking petitions.[30] First, many of the petitions overlapped in time with the Commission's Disclosure Effectiveness Initiative, which was based on congressional mandates in both the Jumpstart Our Business Startups (JOBS) Act of 2012[31] and the Fixing America's Surface Transportation (FAST) Act of 2015.[32] As Congress directed, this ongoing Initiative is seeking to modernize disclosure, both in

26. Pax Ellevate Management LLC, Petition to the SEC to Require Disclosure of Gender Pay Ratios 1 (Feb. 1, 2016), https://www.sec.gov/rules/petitions/2016/petn4-696.pdf [https://perma.cc/2YKW-4E8K] (contending that "pay equity is a useful and material indicator of well-managed, well-governed companies, and conversely, that companies exhibiting significant gender pay disparities may bear disproportionate risk, and that investors therefore may benefit from having such information").

27. Human Capital Management Coalition, Petition to the SEC to Require Disclosure of Human Capital Management Policies, Practices and Performance 1 (July 6, 2017), https://www.sec.gov/rules/petitions/2017/petn4-711.pdf [https://perma.cc/QHY8-CLKB] (pointing out the "broad consensus that human capital management is important to the bottom line, and a large body of empirical work has shown that skillful management of human capital is associated with better corporate performance, including better risk mitigation").

28. Lucian A. Bebchuk, Robert J. Jackson, Jr., James D. Nelson & Roberto Tallarita, *The Untenable Case for Keeping Investors in the Dark*, 10 HARV. BUS. L. REV. 1, 3 (2020).

29. *See id.* at 5 n.15 (quoting the Consolidated Appropriations Act of 2016, Pub. L. No. 114-113, § 707, 129 Stat. 2242, 3029–30 (2015) and citing parallel provisions in subsequent years).

30. Although it failed to answer the call for climate disclosure rulemaking, the SEC did issue guidance in 2010 to clarify existing disclosure obligations in response to petitions seeking such guidance. *See SEC Issues Ground-Breaking Guidance Requiring Corporate Disclosure of Material Climate Change Risks and Opportunities*, CERES (Jan. 27, 2010), https://www.ceres.org/news-center/press-releases/sec-issues-ground-breaking-guidance-requiring-corporate-disclosure [https://perma.cc/TR2G-BC5Q] (discussing its petitions from 2007, 2008, and 2009). Moreover, as part of its current Disclosure Effectiveness Initiative, the SEC has adopted one, quite limited, aspect of the Human Capital Management Coalition petition, *supra* note 27. We discuss both instances of such limited uptake of proposed ESG disclosure at *infra* text accompanying notes 133–39, 156.

31. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, § 108, 126 Stat. 306, 313 (2012) (requiring the SEC to undertake a review of its Regulation S-K with the goal of modernization).

32. Fixing America's Surface Transportation Act, Pub. L. No. 114-94, § 72002, 129 Stat. 1312, 1784–85 (2015) (ordering the SEC to eliminate redundant provisions of Regulation S-K and reduce the requirements of the regulation to ease the burden on emerging growth companies).

content and form of delivery; to better integrate qualitative and financial disclosure requirements; and to eliminate "redundant, overlapping, outdated, or superseded" disclosure.[33] But as we shall see, movement away from line-item disclosure toward principles-based disclosure has become a key feature of this Initiative, and the rulemaking urged in the petitions plainly runs counter to this momentum. The SEC's inaction can also be understood as an instance of "[p]aralysis by [a]nalysis"[34]—a consequence of extensive cost–benefit analysis requirements, imposed through judicial interpretation of the statutory command that SEC rulemaking "consider" the promotion of "efficiency, competition, and capital formation" in addition to the "protection of investors."[35] Relatedly, the SEC could have reasonably anticipated that its adoption of the petitioned rules would have prompted time-consuming litigation challenges by industry associations on cost–benefit grounds.[36] Apart from these factors, however, more fundamental resistance to imposing ESG disclosure requirements is evident.

B. Congressionally Mandated Social Disclosure

Although Congress has directed the SEC to enact very few social disclosure regulations, several mandates in the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 stand as notable exceptions. The Act contains three specialized corporate disclosure mandates, each targeting an aspect of a company's social or law compliance record: "conflict minerals" disclosure in instances in which tin, tantalum, tungsten, or gold (3TG) from the Democratic Republic of the Congo or neighboring countries were incorporated into listed companies' products;[37] extractive industry disclosure of payments to host countries or the U.S. government for rights to extract oil, natural gas, or minerals;[38] and mine operator disclosures relating

33. Mary Jo White, Chair, U.S. Sec. & Exch. Comm'n, The SEC in 2017 and the Path Ahead: Alan B. Levenson Keynote Address at the 44th Annual Securities Regulation Institute 6–7 (Jan. 23, 2017), https://www.law.northwestern.edu/academics/continuing-legal-education/sri/documents/SRI-Remarks-Mary-Jo-White-1-23-2017.pdf [https://perma.cc/W7DN-BUHM].

34. Thomas O. McGarity, *A Cost-Benefit State*, 50 ADMIN. L. REV. 7, 50 (1998) (observing that "exceedingly ambitious cost–benefit analysis" requirements often "drain scarce agency analytical resources and slow down the rulemaking process" and suggesting that such "paralysis may have been the ulterior goal").

35. *See* Donna M. Nagy, *The Costs of Mandatory Cost–Benefit Analysis in SEC Rulemaking*, 57 ARIZ. L. REV. 129, 133–34 (2015) (quoting Securities Act § 2(b) and Exchange Act § 3(f) and discussing cost–benefit analysis as a de facto requirement effectively imposed on SEC rulemaking through excessive judicial scrutiny by the D.C. Circuit).

36. *See id.* at 139–46 (recounting litigation challenges to the sufficiency of the SEC's cost–benefit analysis).

37. Dodd–Frank Wall Street Reform and Consumer Protection Act § 1502, 15 U.S.C. § 78m(p) (2018).

38. *Id.* § 78m(q).

to violations of the Federal Mine Safety and Health Act of 1977.[39] The conflict mineral and extractive industry payment provisions required the SEC to engage in rulemaking, and both SEC rules were challenged in litigation by the U.S. Chamber of Commerce and industry groups. But piled onto the litigation obstacles was the fact that many of the SEC's key decision makers viewed all three types of disclosures as falling outside of the SEC's "core mission."[40]

1. Conflict Minerals Disclosure.—The SEC's conflict minerals disclosure rule, adopted in 2012 as Rule 13p-1,[41] requires listed companies to engage in a due diligence process to determine if their supplies of the named 3TG minerals were from mines supporting armed rebels or the Congolese army.[42] Conflict in the Democratic Republic of the Congo had killed 5.4 million people between 1998 and 2007.[43] The disclosure was aimed at addressing this serious human rights set of problems by causing American companies to pay more attention to their sourcing of these commercially important minerals, with hopes that such attention would move resources away from rebel groups or the Congolese Army. The rule was upheld by the D.C. District Court[44] and affirmed by the D.C. Circuit with one exception.[45] That exception was a statement the rule required issuers to make: that minerals "have 'not been found to be DRC conflict free'" where a company's due diligence process could not exclude the possibility of conflict minerals

39. *Id.* § 78m-2.

40. *See* White, *supra* note 15 (stating that on occasion Congress has asked the SEC to issue rules outside of what she views as the SEC's "core mission" and suggesting that conflict minerals and mine safety disclosures "seem[ed] more directed at exerting societal pressure on companies to change behavior, rather than to disclose financial information that primarily informs investment decisions"); *see also* Jay Clayton, U.S. Sec. & Exch. Comm'n, Statement on Adoption of Resource Extraction Disclosure Rules (Dec. 16, 2020), https://www.sec.gov/news/public-statement/clayton-resource-extraction-2020-12-16 [https://perma.cc/CPJ7-LGXV] (describing resource extraction as a "non-investment oriented issue" and stating that the SEC should be "wary of using our effectiveness for purposes beyond our remit"). Many securities law commentators expressed similar sentiments. *See, e.g.*, Celia R. Taylor, *Drowning in Disclosure: The Overburdening of the Securities & Exchange Commission*, 8 VA. L. & BUS. REV. 85, 89–90, 94 (2014) (arguing that §§ 1502 and 1504 of Dodd–Frank have "little connection with the traditional mission of the SEC"); David M. Lynn, *The Dodd-Frank Act's Specialized Corporate Disclosure: Using the Securities Laws to Address Public Policy Issues*, 6 J. BUS. & TECH. L. 327, 327–30 (2011) (noting that §§ 1502, 1503, and 1504 of Dodd–Frank "were borne out of discrete public policy concerns" and represent a historic shift away from the SEC's mission).

41. 17 C.F.R. § 240.13p-1 (2020).

42. Conflict Minerals, Exchange Act Release No. 67,716, 77 Fed. Reg. 56,274, 56,320 (Sept. 12, 2012) (to be codified at 17 C.F.R. pts. 240 & 249b).

43. *Mortality in the Democratic Republic of Congo: An Ongoing Crisis*, INT'L RESCUE COMM. 16 (May 1, 2007), https://www.rescue.org/sites/default/files/document/661/2006-7congomortalitysurvey.pdf [https://perma.cc/AVW4-8DWN].

44. Nat'l Ass'n of Mfrs. v. SEC, 956 F. Supp. 2d 43, 46 (D.D.C. 2013).

45. Nat'l Ass'n of Mfrs. v. SEC, 748 F.3d 359, 373 (D.C. Cir. 2014).

in their supply chains.[46] The D.C. Circuit held that the requirement violated companies' First Amendment rights against compelled speech.[47] The D.C. Circuit further reviewed that aspect of its decision after an intervening opinion in another case possibly lowered the standard of constitutional review for compelled commercial speech,[48] but it ultimately reiterated its prior ruling that the required language was constitutionally infirm.[49]

The rest of the conflict minerals rule, including companies' due diligence requirements, has been in place since 2012, but in something of a state of suspended animation. That is, the D.C. District Court entered a final judgment in April 2017, which remanded the rule to the SEC for further rulemaking, if any, concerning disclosure.[50] Four days later, Acting SEC Chair Michael Piwowar asked the staff to study how best to proceed, and whether further rulemaking should ensue, but also stated that the SEC would not be enforcing the "extensive and costly requirements for due diligence" since their "primary function" was to enable companies to make disclosures found to be unconstitutional.[51] Piwowar's actions drew a rebuke from Commissioner Kara Stein, who found it "unprecedented for one commissioner, acting alone and without official notice and comment, to engage in de facto rulemaking."[52] Piwowar's actions, and the subsequent no-action position adopted by the Division of Corporation Finance, likewise drew stark criticism from members of Congress.[53] Yet, notwithstanding that

46. *Id.* (quoting 15 U.S.C. § 78m(p)(1)(A)(ii)).

47. *Id.*

48. Soon after its decision in *National Association of Manufacturers*, the full D.C. Circuit decided another disclosure case, rejecting a similar claim by companies (that requiring country-of-origin disclosure for meat products violated their First Amendment rights), and using a lower level of constitutional scrutiny ("*Zauderer* standard") than had been applied in the litigation challenging the conflict minerals disclosure. Am. Meat Inst. v. U.S. Dep't of Agric., 760 F.3d 18, 20 (D.C. Cir. 2014) (en banc).

49. Nat'l Ass'n of Mfrs. v. SEC, 800 F.3d 518, 530 (D.C. Cir. 2015).

50. Nat'l Ass'n of Mfrs. v. SEC, No. 1:13-CV-00635-KBJ, 2017 WL 3503370, at *1 (D.D.C. Apr. 3, 2017).

51. Michael S. Piwowar, Statement of Acting Chairman Piwowar on the Court of Appeals Decision on the Conflict Minerals Rule (Apr. 7, 2017), https://www.sec.gov/news/public-statement/piwowar-statement-court-decision-conflict-minerals-rule [https://perma.cc/3NUM-6VL7].

52. Sarah N. Lynch, *SEC Halts Some Enforcement of Conflict Minerals Rule Amid Review*, REUTERS (Apr. 7, 2017, 2:23 PM), https://www.reuters.com/article/us-usa-sec-conflictminerals-idUSKBN1792WX [https://perma.cc/GK82-NSNZ] (quoting Commissioner Stein).

53. *See* Letter from Cory Booker, Richard Durbin, Sherrod Brown, Christopher Coons, Patrick Leahy & Elizabeth Warren, U.S. Senators, to The Honorable Michael S. Piwowar, Acting Chairman, U.S. Sec. & Exch. Comm'n (Apr. 26, 2017) [hereinafter Senate Letter], https://www.scribd.com/document/346487033/04-26-17-Ltr-to-SEC-Acting-Chairman-Piwowar-Re-Suspension-of-1502-Conflict-Minerals-Rule [https://perma.cc/M2JC-BVNJ] (expressing "deep concern about [Piwowar's] recent instruction to halt enforcement of key parts of the Conflict Minerals rule"); Letter from Maxine Waters, U.S. Representative, Ranking Member of the Fin. Servs. Comm., & Rep. Gwen Moore, Ranking Member of the Subcomm. on Monetary Policy &

no-action position, many companies are continuing to engage in the due diligence and are reporting the specialized disclosure the 2012 Rule contemplated.[54]

2. Extractive Industry Disclosure.—Rule 13q-1's transparency requirements for the extractive industry[55] have had an equally turbulent history, involving three separate instances of rulemaking over the span of nearly a decade. In § 1504 of the Dodd–Frank Act, Congress directed the SEC to promulgate a rule requiring annual disclosure of companies' payments to foreign governments or the U.S. federal government for the rights to extract oil, natural gas, or minerals.[56] The primary goal of the legislation, explicitly modeled on a voluntary, multi-lateral initiative between countries, companies, investors, and other international organizations (the Extractive Industry Transparency Initiative (EITI)), was to "empower citizens of those resource-rich countries to hold their governments accountable for the wealth generated by those resources."[57] Thus, § 13(q) of the Exchange Act, like the conflict minerals disclosure mandate, sought broader corporate and government accountability through disclosure. Although the SEC's 2012 Rule closely tracked the statutory language, a D.C. District Court vacated it the following year for failing to include any exemptions for public disclosure where host countries prohibit it (such as Angola, Cameroon, China, and Qatar) and for interpreting the mandate to

Trade, to The Honorable Walter J. Clayton, Chairman, U.S. Sec. & Exch. Comm'n 1 (Aug. 29, 2017), https://financialservices.house.gov/uploadedfiles/08.2017_cmw_ltr_to_sec.pdf [https://perma.cc/FP47-7TAM] (expressing strong concern over the SEC's "non-enforcement position" regarding Rule 13p-1).

54. *See* Senate Letter, *supra* note 53, at 2 (observing that several companies, including Apple, Richline, and Tiffany & Co., "have embraced the law and its underlying objectives"). There is encouraging evidence that the conflict minerals disclosure is having a demonstrable, positive effect in the Congo. *See Progress and Challenges on Conflict Minerals: Facts on Dodd-Frank 1502*, ENOUGH PROJECT (June 2018), https://enoughproject.org/wp-content/uploads/Progress-and-challenges-June-2018.pdf [https://perma.cc/B2WF-T6X9] (reporting that Dodd–Frank § 1502 transparency has reduced the power of armed groups by significantly lowering the prices of minerals without traceable provenance and has encouraged the development of independent, third-party auditing using the Responsible Minerals Assurance Process, pursuant to which 78% of smelters and refiners have now been certified to be conflict minerals free).

55. 17 C.F.R. § 240.13q-1 (2020).

56. Dodd–Frank Wall Street Reform and Consumer Protection Act § 1504, 15 U.S.C. § 78m(q) (2018).

57. Disclosure of Payments by Resource Extraction Issuers, Exchange Act Release No. 67,717, 77 Fed. Reg. 56,365, 56,366 (Sept. 12, 2012) (to be codified at 17 C.F.R. pts. 240 & 249).

require public disclosure rather than considering disclosure only to the SEC.[58] The SEC did not appeal the judgment, choosing instead to rewrite its rule.[59]

The SEC issued the second version of Rule 13q-1 in 2016, but only after a federal district court ruled in favor of a claim by Oxfam America that the agency's extensive delay in rulemaking constituted action "unlawfully withheld" within the meaning of § 706(1) of the Administrative Procedure Act.[60] This version of the rule again required public disclosure by companies, given the congressional goals of improving transparency and reducing corruption, but with explicit exemptive authority being reserved to the SEC where individual circumstances required it, such as where foreign laws or specific contracts precluded disclosure.[61] Although the rule at the time of its adoption was supported by the U.S. Department of State and the U.S. Agency for International Development as a mechanism to advance "the United States' strong foreign policy interests in promoting transparency and combatting corruption globally,"[62] it was subsequently invalidated in February 2017,[63] pursuant to the Congressional Review Act (CRA), which allows Congress in joint resolutions signed by the President to nullify agency rules that were adopted toward the end of a prior term.[64] In the first weeks of the Trump administration, concerns were expressed for the competitive position of U.S. firms (even though EITI has broad international take-up and the EU and Canada have passed laws more stringent than EITI), the costs of compliance, and the effects on the U.S. economy.[65]

As the SEC points out in its December 2020 release accompanying the third "final rule" on extractive industry disclosure, the CRA joint resolution did not modify the Dodd–Frank mandate to promulgate a resource extraction payment disclosure rule.[66] In the 2020 rule, disclosure will still be public, subject to broad exemptive authority where countries' laws do not permit public disclosure, contractual provisions prohibit it, or the SEC agrees that

58. *See* Am. Petroleum Inst. v. SEC, 953 F. Supp. 2d 5, 11 (D.D.C. 2013) (concluding that the SEC had "misread [§ 13(q)] to mandate public disclosure of the reports, and its decision to deny any exemption was, given the limited explanation provided, arbitrary and capricious").

59. Yin Wilczek, *SEC Will Not Appeal Judgment Invalidating Its Resource Extraction Rule*, 45 SEC. REG. & L. REP. 1635, 1635 (2013).

60. Oxfam Am., Inc. v. SEC, 126 F. Supp. 3d 168, 172–73 (D. Mass. 2015) (stating that "even if the Court considers [Congress's initial] 270-day deadline to have reset from the date of the remand order—July 2, 2013—the SEC is now more than a year past a renewed 270-day deadline with no assurances as to when a final rule may be promulgated").

61. Disclosure of Payments by Resource Extraction Issuers, Exchange Act Release No. 78,167, 81 Fed. Reg. 49,360, 49,386, 49,391 (July 27, 2016) (to be codified at 17 C.F.R. pts. 240 & 249b).

62. *Id.* at 49,362.

63. H.R.J. Res. 41, 115th Cong. (2017).

64. 5 U.S.C. §§ 801–808 (2018).

65. Disclosure of Payments by Resource Extraction Issuers, Exchange Act Release No. 90,679, 86 Fed. Reg. 4662, 4664, 4703 (Jan. 15, 2021) (to be codified at 17 C.F.R. pts. 240 & 249b).

66. *Id.* at 4664.

individual circumstances brought to its attention require confidentiality.[67] The major change between 2016 and 2020 is in the definition of the reporting unit, the project, for which disclosure must be made. In 2016, disclosure was to be made based on individual contracts for extraction; by 2020, disclosure was to be made aggregating all payments of a specified type (licenses, dividends, community support, etc.) across geographical units, national or subnational.[68] This process of aggregation elicited a strong dissent from Commissioner Allison Lee.[69]

3. *Mine Safety Violations.*—Unlike the Dodd–Frank Act's mandates for conflict minerals and extractive industry disclosures, which obligated the SEC to adopt a rule requiring issuers to make the requisite disclosures, § 1503's mandate for mine operators to disclose safety violations was self-executing—the disclosure requirements were effective thirty days following Dodd–Frank's enactment.[70] Congress was responding to a West Virginia coal-mine explosion a few months prior, which had killed twenty-nine miners,[71] and to evidence that the company owning the mine had received more than one thousand notifications of health and safety law violations in the five years leading up to the explosion.[72] But the SEC adopted rules in 2011 to implement § 1503's detailed requirements. Specifically, the SEC revised Regulation S-K to include an Item 104, which requires issuers that are mine operators to disclose Mine Safety and Health Administration (MSHA) citations, orders, and notices in their quarterly and annual reports.[73] The SEC also added Item 1.04 to Form 8-K, which requires the filing of a current report upon the receipt of certain notices, citations, or orders of mine-safety violations or a pattern of such violations.[74]

As a self-executing congressional mandate, the mine-safety disclosure requirements did not trigger the litigation challenges that in part slowed the SEC's administration of Dodd–Frank's other specialized corporate disclosures. But like conflict minerals and resource extraction disclosure,

67. *Id.* at 4705.

68. *Id.* at 4666, 4668.

69. Allison Herren Lee, Statement on Rules Governing the Disclosure of Payments by Resource Extraction Issuers (Dec. 16, 2020), https://www.sec.gov/news/public-statement/lee-resource-extraction-2020-12-16 [https://perma.cc/C2HS-ZD42].

70. 15 U.S.C. § 78m-2(f) (2018).

71. Ian Urbina, *No Survivors Found After West Virginia Mine Disaster*, N.Y. TIMES (Apr. 9, 2010), https://www.nytimes.com/2010/04/10/us/10westvirginia.html [https://perma.cc/CWU6-VLQZ].

72. Tom Zeller, Jr., *Coal Mine's Safety Record Under Scrutiny*, N.Y. TIMES: GREEN (Apr. 6, 2010, 1:19 PM), https://green.blogs.nytimes.com/2010/04/06/coal-mines-safety-record-under-scrutiny/ [https://perma.cc/X44V-XG39].

73. 17 C.F.R. §§ 229.104, 229.601(b)(95) (2020).

74. Mine Safety Disclosure, Securities Act Release No. 9286, Exchange Act Release No. 66, 019, 76 Fed. Reg. 81,785 (Dec. 21, 2011) (to be codified at 17 C.F.R. pts. 229, 239, & 249).

mine safety disclosure was viewed by some SEC officials as a type of disclosure that "does not comport with our mission as we see it."[75] The sentiment is puzzling because issuers that are mine operators are required to disclose *violations* of federal health and safety laws, and the SEC has recognized that matters relating to law compliance can be regarded as material information notwithstanding a quantitatively small effect on a financial statement.[76]

C. Changes to Shareholder Proposals under Rule 14a-8

Rather than expand ESG disclosure, the SEC acted at the end of the Trump administration to narrow the ability of shareholders to put items on the agenda of the annual meeting. Indeed, shareholder proposals have historically been a mechanism for even small shareholders to raise corporate governance, social, or environmental concerns with companies and are often used to seek ESG and climate disclosure. Preserving the power of small shareholders to submit such proposals is also important because while some large shareholders (such as mutual funds) increasingly support ESG proposals, such institutional investors rarely submit proposals of their own.[77]

The Rule 14a-8 revisions, as adopted in September 2020, will make it more difficult for small shareholders to engage with companies using shareholder proposals. Specifically, they raise the dollar amounts of investments needed to be eligible to put a proposal on the agenda from $2,000 with a one-year holding period to $25,000 with a one-year holding period. They also raise the voting thresholds necessary to resubmit a proposal to the same company's shareholders from a 3% positive vote in the first year that a proposal is on the agenda to be eligible to resubmit, 6% in the second year, and 10% in the third year, to 5%, 15%, and 25%, respectively.[78] The revisions also prohibit shareholders from aggregating their holdings to meet the investment thresholds and modify the existing one-proposal limitation to apply to "each person" rather than "each shareholder" who submits a

75. *See* White, *supra* note 15 (questioning the use of federal securities law and the SEC's power of mandatory disclosure to achieve the goal of improved safety in mines).

76. SEC Staff Accounting Bulletin No. 99, 64 Fed. Reg. 45,150, 45,152 (Aug. 19, 1999); *see also* IBEW Loc. Union No. 58 Pension Tr. Fund & Annuity Fund v. Royal Bank of Scot. Grp., PLC, 783 F.3d 383, 390 (2d Cir. 2015) (citing SAB No. 99 and observing that "qualitative factors . . . can turn a quantitatively immaterial statement into a material misstatement").

77. *See* Lucian A. Bebchuk, Comment Letter on Proposed Revisions to Rule 14a-8, at 2 (Feb. 3, 2020), https://www.sec.gov/comments/s7-23-19/s72319-6744343-207928.pdf [https://perma.cc/N4RJ-MXZ8] (highlighting "evidence that significant institutional investors tend to avoid the submission of shareholder proposals though they regularly vote for certain types of shareholder proposals").

78. Procedural Requirements and Resubmission Thresholds Under Exchange Act Rule 14a-8, Exchange Act Release No. 89,964, 85 Fed. Reg. 70,240, 70,244, 70,256–57 (Nov. 4, 2020) (to be codified at 17 C.F.R. pt. 240). A shareholder owning $2,000 worth of shares could still submit a proposal so long as the shares had been held for at least three years. *Id.* at 70,244.

proposal (effectively barring a law firm from submitting a proposal on behalf of more than one client).[79]

These Rule 14a-8 changes occurred in the wake of data revealing that shareholders are increasingly signaling their support for resolutions raising ESG issues and seeking disclosure. An analysis of shareholder voting trends from 2000 to 2018 by ISS Analytics, the research arm of the major proxy advisor Institutional Shareholders' Services (ISS), concluded that "the most significant change in investors' voting behavior pertains to environmental and social issues, as these proposals are earning record levels of support in recent years."[80] Indeed, ESG proposals are increasingly "shifting . . . focus towards disclosure, risk assessment, and oversight" and are thus key indicators of management's approach to matters such as workforce diversity, climate change, or employee health and safety.[81] Moreover, while the median level of support has been increasing for environmental and social proposals, the number of shareholder proposals generally has been going down over the last decade. As Commissioner Allison Lee stated in dissenting from the final rule, "[a]n analysis of Russell 3000 companies reveals that, on average, only 13 percent of companies received a shareholder proposal in a particular year between 2004 and 2017. That translates to approximately one proposal every 7.7 years for the average company."[82] Part of the reason that the number of proposals has been going down is because many investor-led governance initiatives have been successful, such as promoting annual board elections and encouraging companies to adopt majority voting rules,[83] so those governance topics no longer inspire shareholder proposals.

That investors are increasingly voting for shareholder proposals or have successfully used shareholder proposals to encourage important governance changes at U.S. companies is not discussed in either the proposing or final release. As Commissioner Robert Jackson stated in dissenting from the proposing release, "rather than engage carefully with the evidence produced by [debates over shareholder proposals], today's proposal simply shields

79. *Id.* at 70,248, 70,254; *see also* Professor James D. Cox, Comment Letter on Behalf of Fourteen Corporate and Securities Law Professors on Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8, at 4 (Feb. 2, 2020), https://www.sec.gov/comments/s7-23-19/s72319-6744343-207928.pdf [https://perma.cc/N4RJ-MXZ8] (pointing out the "one-dimensional quality" of this limitation given that a law firm representing a corporate client "can request no-action relief to omit unrelated proposals" submitted by different proponents).

80. Kosmas Papadopoulos, *The Long View: U.S. Proxy Voting Trends on E&S Issues from 2000 to 2018*, HARV. L. SCH. F. CORP. GOVERNANCE (Jan. 31, 2019), https://corpgov.law.harvard.edu/2019/01/31/the-long-view-us-proxy-voting-trends-on-es-issues-from-2000-to-2018/ [https://perma.cc/2CGE-MT9M].

81. *Id.*

82. Allison Herren Lee, Statement on the Amendments to Rule 14a-8 (Sept. 23, 2020) (footnotes omitted), https://www.sec.gov/news/public-statement/lee-14a8-2020-09-23 [https://perma.cc/N876-H56X].

83. *Id.*

CEOs from accountability to investors."[84] Commissioner Jackson's staff conducted an empirical study, concluding that 40% of proxy-access proposals and over 50% of proposals to limit CEOs' sales of their companies' stock granted in compensation would have been excluded for three years had the new resubmission thresholds been in effect.[85] In both cases, the data he presented showed an alignment of the shareholder proposal with investors' financial interests.[86] The final rule adopted the resubmission thresholds, as proposed, with no discussion of that data or any other empirical evidence.

Commissioner Lee's dissent to the final rule found the same lack of policy analysis and paucity of evidence for making the changes to Rule 14a-8. Among unique letters, there were only sixteen comment letters in support of raising eligibility thresholds, most by issuers and their representatives, and "15 times as many letters" in opposition, including from individual investors, institutional investors, representatives of institutional investors, and the SEC's Investor Advisory Committee.[87] The Release for the final rule does not engage with these facts. Commissioner Lee also observed that:

> Shareholder proposals related to climate change continued to increase in number and in support last season, garnering an average of 31 percent support, with four such proposals passing. Shareholders are beginning to accomplish on climate change what they have accomplished on numerous other significant issues crucial to good governance and long-term value—focus management attention and drive valuable and needed change. The Commission should be encouraging this kind of engagement, not stifling it.[88]

The SEC took these actions in conjunction with changes to the regulation of proxy advisors, who often support ESG proposals,[89] and as the Department of Labor (DOL) enacted new rules to reduce the incentives for

84. Robert J. Jackson, Jr., Statement on Proposals to Restrict Shareholder Voting (Nov. 5, 2019), https://www.sec.gov/news/public-statement/statement-jackson-2019-11-05-open-meeting [https://perma.cc/Q62E-K6TW].

85. *Id.*

86. *Id.*

87. Lee, *supra* note 82, at n.5.

88. *Id.* (footnotes omitted) (citing *2020 Proxy Season Review: Part 1: Rule 14a-8 Shareholder Proposals*, SULLIVAN & CROMWELL LLP 10 (July 15, 2020), https://www.sullcrom.com/files/upload/SC-Publication-2020-Proxy-Season-Review-Part-1-Rule-14a-8.pdf [https://perma.cc/9Y82-JWY3] for data on shareholder proposal support); and Kosmas Papadopoulos, *The Long View: The Role of Shareholder Proposals in Shaping U.S. Corporate Governance (2000–2018)*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 6, 2019), https://corpgov.law.harvard.edu/2019/02/06/the-long-view-the-role-of-shareholder-proposals-in-shaping-u-s-corporate-governance-2000-2018/ [https://perma.cc/WK67-SX86]).

89. *See* Keith Johnson, Cynthia Williams & Ruth Aguilera, *Proxy Voting Reform: What Is on the Agenda, What Is Not on the Agenda, and Why It Matters for Asset Owners*, 99 B.U. L. REV. 1347, 1353–55 (2019) (discussing proxy advisors' support for ESG shareholder proposals).

pension fund trustees to use ESG data in constructing their portfolios.[90] Why the SEC majority would act to limit shareholder proposals at a time when leading business organizations are emphasizing companies' social and environmental responsibilities,[91] and votes in favor of environmental and social proposals are generally increasing, is perplexing. One possibility is suggested by Professor John Coffee, who has analyzed institutional investors' recent attention to the importance of ESG as a matter of investment strategy and has discussed the political pushback that attention is creating.[92] Shareholder proposals create opportunities for engagement with companies' management and give these shareholders some degree of leverage; both may be uncomfortable for some companies. One type of leverage is the agreement to withdraw a proposal when the company agrees to shareholders' requests.[93] Thirty-three climate proposals were withdrawn in 2018 when the company agreed to shareholders' requests, which are increasingly seeking disclosure consistent with TCFD, and six more were withdrawn when the company agreed to begin a dialogue on the underlying issues.[94] Yet, the SEC has not responded to limit hedge fund shareholder activists' leverage similarly, notwithstanding calls from leading law firms and academics for it to do so.[95] Accordingly, while a general resistance to certain types of shareholder activism undoubtedly explains part of the reason a divided Commission

90. *See* Lee, *supra* note 82 (recognizing that the SEC's amended Rule 14a-8 is consistent with the DOL's efforts to restrict ESG investment by retirement plans).

91. *See Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans'*, BUS. ROUNDTABLE (Aug. 19, 2019), https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans [https://perma.cc/BC5F-ETQQ] (emphasizing that the purpose of a corporation includes social and environmental responsibility).

92. *See* John C. Coffee, *The Future of Disclosure: ESG, Common Ownership, and Systematic Risk*, 34 n.81, 37–38 (European Corp. Governance Inst., Law Working Paper No. 541/2020, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3678197 [https://perma.cc/X9NB-BH8P] (discussing DOL efforts to limit ESG investing and voting as a political response to institutional investors' increasing understanding that ESG matters often are material from a whole-portfolio perspective).

93. *See, e.g.*, Sarah C. Haan, *Shareholder Proposal Settlements and the Private Ordering of Public Elections*, 126 YALE L.J. 262, 297 (2016) (observing that "[t]he Rule 14a-8 regime itself, which was not designed to facilitate social and environmental policy reforms, may actually channel social and environmental activism toward settlement").

94. Madison Condon, *Externalities and the Common Owner*, 95 WASH. L. REV. 1, 4 n.13 (2020).

95. *See, e.g.*, John C. Coffee, Jr., Robert J. Jackson, Jr., Joshua R. Mitts & Robert E. Bishop, *Activist Directors and Agency Costs: What Happens When an Activist Director Goes on the Board?*, 104 CORNELL L. REV. 381, 386–87 (2019) (demonstrating that "informed trading" increases when a director backed by an activist goes on the board of a public company, particularly when that activist director is an employee of the hedge fund); Martin Lipton, *Dealing with Activist Hedge Funds and Other Activist Investors*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jan. 20, 2020), https://corpgov.law.harvard.edu/2020/01/20/dealing-with-activist-hedge-funds-and-other-activist-investors-3/ [https://perma.cc/EKK7-M797] (stating that the SEC rules do not prevent hedge-fund activist attacks despite increasing criticism of hedge-fund activism).

diminished shareholders' Rule 14a-8 rights, ESG disclosure and the corporate accountability facilitated by shareholder proposals faced an additional headwind, which we discuss below.

D. The SEC's Disclosure Effectiveness Initiative and Its Shift from Line-Item Disclosure to a More Principles-Based System

We began this Article by summarizing some of the data showing institutional investors' increasing use of what ESG data are available in their engagement, voting, and portfolio construction. The SEC is well aware of these trends but squaring them with the momentum behind the SEC Disclosure Effectiveness Initiative and its shift from line-item disclosure to a more principles-based system is presenting stark challenges.

Even before changes brought about by the Biden presidency, the SEC had been taking small steps toward better understanding the increasing investor demands for ESG and climate disclosure. For example, at the start of 2020, then SEC Chair Jay Clayton spoke thoughtfully about the difficulties of developing an ESG or climate disclosure mandate without marginalizing the importance of that endeavor.[96] His statements indicated agency-wide efforts to understand the environmental and climate information investors currently use, how that information is used, and how issuers identify, assess, and manage environmental and climate risk in their businesses.[97] Chairman Clayton also referenced the SEC's participation in the International Organization of Securities Commissions' Sustainable Finance Network and its discussions with UK and EU regulators concerning climate disclosure.[98] Moreover, in May 2020, a subcommittee of the SEC's Investor Advisory Committee recommended that the SEC take up the issue of ESG disclosure,[99] and, in December 2020, the ESG subcommittee of the SEC's Asset Management Advisory Committee suggested in a discussion draft that the SEC should issue better guidance to issuers on providing decision-useful

96. Jay Clayton, Statement on 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), https://www.sec.gov/news/public-statement/clayton-mda-2020-01-30 [https://perma.cc/TA5B-WWRP].

97. *Id.*

98. *Id.*

99. Allison Bennington, Anne Sheehan & John Coates, *Recommendation from the Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee Relating to ESG Disclosure*, HARV. L. SCH. F. ON CORP. GOVERNANCE (May 28, 2020), https://corpgov.law.harvard.edu/2020/05/28/recommendation-from-the-investor-as-owner-subcommittee-of-the-sec-investor-advisory-committee-relating-to-esg-disclosure/ [https://perma.cc/YQ2L-R387].

ESG disclosure within a general materiality mandate.[100] Additional and faster paced efforts in this regard can be anticipated in the months to come.

The SEC's effort to broaden its understanding of ESG disclosure is also reflected in a small series of questions in its voluminous 2016 Concept Release on Business and Financial Disclosure Required by Regulation S-K Disclosures (Concept Release).[101] More specifically, in the Concept Release's staggering total of 340 questions, eight were directed at ESG.[102] Questions were asked about which sustainability issues are important to voting or investing, how rules could be crafted to "elicit meaningful disclosure" yet also be flexible, and how the SEC could avoid requiring the disclosure of immaterial information using prescriptive rules.[103] Others asked about free-standing sustainability reports; about voluntary, privately developed disclosure frameworks; and about the Commission's 2010 climate guidance and whether that guidance is sufficient to produce high-quality information.[104] And, there was a question about whether there are "sustainability or public policy issues for which line-item disclosure requirements would be consistent with the Commission's rulemaking authority and [its] mission to protect investors, maintain fair, orderly and efficient markets and facilitate capital formation."[105]

The SEC received over 26,500 comments in response to its 2016 Concept Release, making it one of only six major proposals by the SEC since 2008 to garner more than 25,000 comments.[106] And since the Release represented the SEC's first systematic examination of ESG disclosure since 1974, it is hardly surprising that there were hundreds of unique comment letters received from a wide range of market participants, including investors, advisors, organizations, issuers, and NGOs. An early analysis of the commentary found widespread support for expanded ESG disclosure among investors and their representatives (80% of the comments directed to sustainability supported expanded disclosure), versus concerns and criticisms

100. Asset Management Advisory Committee of the SEC, Discussion Draft, Potential Recommendations of ESG Subcommittee (Dec. 1, 2020), https://www.sec.gov/files/potential-recommendations-of-the-esg-subcommittee-12012020.pdf [https://perma.cc/A448-E8BJ].

101. 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, 23,972–73 (April 22, 2016) (to be codified in 17 C.F.R. pts. 210, 229, 230, 232, 239, 240, & 249).

102. *Id.* at 23,972–73.

103. *Id.* at 23,972.

104. *Id.* at 23,972–73.

105. *Id.* at 23,972.

106. TYLER GELLASCH, PUB. CITIZEN, TOWARDS A SUSTAINABLE ECONOMY: A REVIEW OF COMMENTS TO THE SEC'S DISCLOSURE EFFECTIVENESS CONCEPT RELEASE 8–9 (2016), https://www.citizen.org/wp-content/uploads/sustainableeconomyreport.pdf [https://perma.cc/VNT9-BGTH].

from issuers and their representatives (10% of the comments directed to sustainability voiced concern).[107]

But it does not appear that the Commission has systematically analyzed these comments.[108] Instead, we see evidence suggesting that its commitment to moving away from line-item disclosure towards a more principles-based system has been used as a generic reason to not engage with the issues of required ESG disclosure or better climate disclosure.

1. Revisions to S-K Items 101, 103, and 105.—The first substantial rule proposal based on the 2016 Concept Release suggested changes to Regulation S-K's items eliciting information about a company's business (Item 101), legal proceedings (Item 103), and risk factors (Item 105).[109] In general, the SEC proposed taking a more principles-based approach to the disclosure requirements in Items 101 and 105, while keeping line-item requirements (what it calls a "prescriptive approach") to Item 103.[110] Notably, the proposal sought input on five questions concerning companies' human capital management, to be promulgated as part of Item 101(c).[111] This aspect of the proposed rule was lauded by Commissioners Jackson and Lee in a statement in support of the proposed rule, but they also expressed two concerns.[112] First, in their view, the scope of the proposed shift to a principles-based approach risked producing inconsistent and incomparable disclosure.[113] Second, they expressed concern that the proposal did not include anything about climate risk. Stating that "research shows that we are long past the point of being unable to meaningfully measure a company's

107. *See* Virginia Harper Ho, *Disclosure Overload? Lessons for Risk Disclosure & ESG Reporting Reform from the Regulation S-K Concept Release*, 65 VILL. L. REV. 67, 115, 116 fig.2 (2020) (finding that there is a sharp divergence in how investors and issuers perceive expanded ESG disclosure); SUSTAINABILITY ACCOUNTING STANDARDS BD., THE STATE OF DISCLOSURE 2016: AN ANALYSIS OF THE EFFECTIVENESS OF SUSTAINABILITY DISCLOSURE IN SEC FILINGS 3–4 (2016), https://www.sasb.org/wp-content/uploads/2019/08/StateofDisclosure-Report-113016v2-1.pdf [https://perma.cc/F7K5-PD7Q] (finding that 80% of comments about sustainability called for improved sustainability-related disclosure and only 10% of comments opposed changes to sustainability disclosure).

108. *Cf.* Ho, *supra* note 107 (challenging key objections to ESG disclosure reform by the SEC based on a comprehensive analysis of nearly 300 unique public comments).

109. Modernization of Regulation S-K Items 101, 103, and 105, Securities Act Release No. 10,668, Exchange Act Release No. 86,614, 84 Fed. Reg. 44,358 (Aug. 23, 2019) (to be codified at 17 C.F.R. pts. 229, 239 & 240).

110. *Id.* at 44,360.

111. *Id.* at 44,371 (requesting comment on questions numbered twenty-one through twenty-five, which are focused on human capital management).

112. Robert J. Jackson, Jr. & Allison Herren Lee, Joint Statement on Proposed Changes to Regulation S-K (Aug. 27, 2019), https://www.sec.gov/news/public-statement/statement-jackson-lee-082719 [https://perma.cc/M7MP-RD96].

113. *Id.*

sustainability profile," they asked commenters to discuss climate disclosure in responding to the proposed rule.[114]

One year later the SEC published its final revisions to Items 101, 103, and 105.[115] As regards human capital, the final rule adopted some expanded disclosure.[116] It "will require, to the extent such disclosure is material to an understanding of the registrant's business taken as a whole, a description of a registrant's human capital resources, including any human capital measures or objectives that the registrant focuses on in managing the business."[117] The SEC did not include what "many commenters" had supported, a requirement for issuers to disclose how many full-time, part-time, and contingent workers they employed, and data on employee turnover, stating that "adopting these prescriptive elements . . . would be inconsistent with our objective to make Item 101(c) more principles-based."[118]

Commissioner Lee issued a sharp dissent to the final rule.[119] Noting the "overwhelming investor comment" advocating for specific, commonly-used metrics for tracking employment data as well as the COVID-19 pandemic and Black Lives Matter developments in the country in 2020, Commissioner Lee stated that "[t]his year's upheavals have driven home that ESG risks, like those associated with diversity and climate change, are strong predictors for resilience and for maximizing risk-adjusted returns."[120] Commissioner Lee then summarized the data showing that ESG matters generally, and climate risks specifically, have become fundamental to investors' analyses, with trillions of dollars of invested capital being managed by combining traditional financial metrics and such ESG data as are available.[121] Asserting that generalized materiality determinations will not provide the kind of consistent, comparable ESG or climate data that investors seek, she concluded with a statement that seems to invite public-interest litigation:

> As for comments, from reading the release, one might think we received two or three isolated letters on the subject [of the need for required disclosure of climate risk]. In fact, we received thousands. This, coupled with an unprecedented and massive campaign [by investors] to obtain voluntary climate-related disclosures from

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114. *Id.*

115. Modernization of Regulation S-K Items 101, 103, and 105, Securities Act Release No. 10,825, Exchange Act Release No. 89,670, 85 Fed. Reg. 63,726 (Oct. 8, 2020) (to be codified at 17 C.F.R. pts. 229, 239, & 240).

116. *Id.* at 63,739–40.

117. *Id.* at 63,739.

118. *Id.* at 63,740.

119. Allison Herren Lee, Statement on Regulation S-K and ESG Disclosures: An Unsustainable Silence (Aug. 26, 2020), https://www.sec.gov/news/public-statement/lee-regulation-s-k-2020-08-26 [https://perma.cc/4YTY-J2LN].

120. *Id.* (footnote omitted).

121. *Id.*

> companies, speaks volumes regarding the deficiencies under the existing guidance and principles-based regime.
>
> Nevertheless, today's rule is silent on the topic of climate risk. It does not even explain or justify the decision to exclude it from the rule.[122]

2. Revisions to S-K Item 303, Management Discussion and Analysis (MD&A).—A similar pattern emerges regarding proposed changes to Item 303 of Regulation S-K. MD&A is arguably the natural home for ESG and climate disclosure, since it specifically calls for analysis of "known trends or any known demands, commitments, events or uncertainties" that are reasonably likely to have a material impact on the company's liquidity, capital resources, results of operations, or off-balance sheet arrangements.[123] MD&A seeks management's views of its current financial results on a quarterly and annual basis, but also may require the disclosure of future-looking information according to the above standards.[124]

Yet, the SEC has jettisoned specific information from that which was required to be disclosed in MD&A,[125] and has refused to add climate disclosure to the mix. These policy choices were questioned by Commissioner Lee, in reaction to the proposed rule,[126] and she was joined in dissenting to the final rule by the newest Commissioner, Caroline Crenshaw.[127] While applauding some of the improvements in MD&A requirements that will eliminate duplicative disclosure, their dissent criticized deleting the requirement to provide a future contractual obligations table: while some of that information can be found in the financial statements, much of it is not available elsewhere, including data that provides "insight into supply chain and risk management."[128] They also observed that climate

122. *Id.*

123. 17 C.F.R. § 229.303(a)(1)–(4) (2020).

124. *See id.* § 229.303(a)–(b) (requiring MD&A for each fiscal year and interim period financial statement including future-looking disclosures of known trends or uncertainties).

125. *See* Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information, Securities Act Release No. 10,890, Exchange Act Release No. 90,459, 86 Fed. Reg. 2080, 2081 (Jan. 11, 2021) (to be codified at 17 C.F.R. pts. 210, 229, 230, 239, 240, & 249) (adopting amendments to registrant disclosure requirements to reduce duplicative disclosure requirements and focus on material information).

126. Allison Herren Lee, Statement on "Modernizing" Regulation S-K: Ignoring the Elephant in the Room (Jan. 30, 2020), https://www.sec.gov/news/public-statement/lee-mda-2020-01-30 [https://perma.cc/53Y4-JJ62].

127. Allison Herren Lee & Caroline A. Crenshaw, Joint Statement on Amendments to Regulation S-K: Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information (Nov. 19, 2020), https://www.sec.gov/news/public-statement/lee-crenshaw-statement-amendments-regulation-s-k [https://perma.cc/ZLM5-HRHY].

128. *Id.*

disclosure is again ignored, notwithstanding many comment letters indicating investors' needs for consistent, comparable information.[129]

The policy choices reflected in the SEC's recent S-K revisions appear to be grounded both in an unproven assumption that a principles-based system is generally superior to one based on specific line items and a mistaken assumption that if climate change or ESG information is material, issuers already are obliged to disclose that information. Both notions, which have been pervasive in the SEC's policymaking on disclosure, but particularly so post-2016, are explored in our analysis below.

II. Analysis

A. The SEC's Materiality Blind Spot

The first question we turn to is whether "materiality" as a general principle for disclosure can do the work needed for today's investors. Voluntary, market-led ESG and climate disclosure frameworks have developed quite substantially over the last two decades, showing both a market demand and innovative supply. Yet, reporting according to those multiple frameworks has not produced reliable, comparable information that is consistently presented.[130] Nor have general materiality principles produced high-quality information, even pursuant to those Items in Regulation S-K where climate or ESG risks would be highly relevant, such as Items 105 (risk factors) or 303 (MD&A).[131] Indeed, issuers legally can—and frequently do—keep silent about information, notwithstanding its materiality to shareholders and potential investors.[132]

Our conclusion that a general materiality mandate is not sufficient is best supported by examining climate disclosure. In 2010, the SEC issued guidance to companies to clarify their disclosure obligations on climate risks.[133] The guidance emphasized several materiality principles that counselled in favor of more specific climate disclosure. In so doing, the SEC

129. *Id.*

130. *See* Thomas Lee Hazen, *Social Issues in the Spotlight: The Increasing Need to Improve Publicly-Held Companies' CSR and ESG Disclosures*, 23 U. PA. J. BUS. L. 740, 749–51 (2021) (describing the "lack of standardization" in voluntary ESG disclosures and the resulting "confusing inconsistencies in ESG data" in such disclosures); Virginia Harper Ho, *Nonfinancial Risk Disclosure and the Costs of Private Ordering*, 55 AM. BUS. L.J. 407, 443–52 (2018) (discussing the costs imposed on markets by the current manner of disclosure that relies on private ordering and the inconsistent and unreliable ESG disclosure resulting therefrom).

131. *See* Lee, *supra* note 126 (asserting that a principles-based materiality standard does not provide "consistent, reliable, and comparable" climate disclosure).

132. *See infra* text accompanying notes 146–48 (explaining that not all material information is required to be disclosed under the current disclosure rules).

133. Commission Guidance Regarding Disclosure Related to Climate Change, Securities Act Release No. 9106, Exchange Act Release No. 61,469, 75 Fed. Reg. 6290 (Feb. 8, 2010) (to be codified at 17 C.F.R. pts. 211, 231 & 241).

reiterated its general approach to disclosure obligations, and that of the Supreme Court:

> In the articulation of the materiality standards, it was recognized that doubts as to materiality of information [can] be commonplace, but that, particularly in view of the prophylactic purpose of the securities laws and the fact that disclosure is within management's control, "it is appropriate that these doubts be resolved in favor of those the statute is designed to protect."[134]

The guidance also discussed the relevance of Regulation S-K's Items 101, 103, 303, and 503 to climate disclosure,[135] with the recognition that MD&A places particular emphasis on a company's materiality determinations.[136] In addition, it emphasized the SEC's 1989 Release on required forward-looking disclosure pursuant to MD&A,[137] and reiterated the Supreme Court's test for the materiality of forward-looking information.[138] It then canvassed a number of different factual scenarios in which these various materiality principles might require disclosure.[139] In other words, the 2010 climate guidance gave issuers a refresher course on materiality, with a thumb on the scale towards disclosure.

Yet, over ten years later the results show that materiality principles alone have not produced high-quality, decision-useful climate disclosure.[140] An analysis by the Sustainability Accounting Standards Board (SASB) of the climate disclosure in the 10-Ks of the ten largest companies by revenue in each industry category in the United States found that 27% of these

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134. *Id.* at 6293 (quoting TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 448 (1976)).

135. *Id.* at 6293–95; *see supra* notes 109, 123 and accompanying text (discussing S-K items).

136. Commission Guidance Regarding Disclosure Related to Climate Change, 75 Fed. Reg. at 6294.

137. *See id.* at 6295 (explaining that the 1989 Release set out a process of analysis which requires issuers to evaluate the potential financial effects of a trend, event, demand, commitment, or uncertainty coming to fruition if the issuer cannot rule out that eventuality (the coming to fruition)).

138. *Id.* at 6294 (citing Basic Inc. v. Levinson, 485 U.S. 224, 238 (1988)). In *Basic*, the Court held that the materiality of contingent or speculative information "will depend at any given time upon a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity." *Basic*, 485 U.S. at 238 (quoting SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 849 (2d Cir. 1968) (en banc)).

139. *See* Commission Guidance Regarding Disclosure Related to Climate Change, 75 Fed. Reg. at 6295–97 (providing examples of climate change-related issues that might require disclosure).

140. *See, e.g.*, ANDY GREEN & ANDREW SCHWARTZ, CTR. FOR AM. PROGRESS, CORPORATE LONG-TERMISM, TRANSPARENCY, AND THE PUBLIC INTEREST 7–8, 10 (2018), https://www.sec.gov/comments/s7-10-16/s71016-4566028-176216.pdf [https://perma.cc/3NVZ-S5DB] (highlighting "overwhelmingly clear" investor demand for high-quality, consistent ESG disclosures); SUSTAINABILITY ACCOUNTING STANDARDS BD., CLIMATE RISK TECHNICAL BULLETIN TB#001-10182016 85–86 (2016), https://www.sasb.org/wp-content/uploads/2019/08/Climate-Risk-Technical-Bulletin-web.pdf [https://perma.cc/92DF-L2MX] (finding current ESG disclosure practices inadequate because of widespread omission of ESG disclosures and pervasive use of boilerplate language by companies that do provide ESG disclosures).

companies do not identify any climate risks, and more than 40% have boilerplate disclosures on the topic.[141] SASB's analysis also shows that there are material financial risks from climate change for companies in seventy-two of seventy-nine industries, representing $27.5 trillion, or 93% of the U.S. equity market.[142] The potential for macroeconomic disruption from climate change is confirmed in analyses by the Board of Governors of the Federal Reserve System, in its November 2020 Financial Stability Report,[143] and by a subcommittee of the U.S. Commodity Futures Trading Commission in September of that year.[144] A materiality mandate alone, even with specific SEC guidance, is not producing decision-useful information for investors on how companies are managing the risks of climate change, or we would not see this gap between the economy-wide risks of climate change and the low-quality disclosure from the United States' largest companies.[145]

As a matter of law, that conclusion is not surprising. U.S. securities laws do not impose upon securities issuers a general duty to disclose all material information—that is, "[s]ilence, absent a duty to disclose, is not misleading."[146] Generally the duty to disclose arises from specific transactions, such as an issuer buying or selling its own securities, or from specific reporting requirements (such as line items in Regulation S-K) as well as the backstop provisions in Exchange Act Rule 12b-20 and Securities Act Rule 408, which require issuers to include in certain SEC filings any "further material information . . . as may be necessary to make the required statements, in the light of the circumstances under which they are made[,] not misleading."[147] But such backstops are not implicated if a topic is not related to specific disclosures in a report's line items, nor would a general duty to

141. SUSTAINABILITY ACCOUNTING STANDARDS BD., *supra* note 140, at 3, 85–86. Modelled on the Financial Accounting Standards Board, SASB worked with 2,800 participants from U.S. accounting firms, investors, and industry representations to develop a framework of targeted, industry-specific ESG disclosure. *Id.* at 3.

142. *Id.* at 2.

143. BD. OF GOVERNORS OF THE FED. RESERVE SYS., FINANCIAL STABILITY REPORT 58–59 (2020), https://www.federalreserve.gov/publications/files/financial-stability-report-20201109.pdf [https://perma.cc/RZU6-47D3] (stating that "Federal Reserve supervisors expect banks to have systems in place that appropriately identify, measure, control, and monitor all of their material risks, which for many banks are likely to extend to climate risks").

144. CLIMATE-RELATED MKT RISK SUBCOMM., MARKET RISK ADVISORY COMM., U.S. COMMODITY FUTURES TRADING COMM'N, MANAGING CLIMATE RISK IN THE U.S. FINANCIAL SYSTEM 11 (2020), https://www.cftc.gov/PressRoom/PressReleases/8234-20 [https://perma.cc/C3YJ-AU5A].

145. *See* Lee, *supra* note 126 (emphasizing that "the broad, principles-based 'materiality' standard has not produced sufficient disclosure to ensure that investors are getting the information they need—that is, disclosures that are consistent, reliable, and comparable").

146. Basic Inc. v. Levinson, 485 U.S. 224, 239 n.17 (1988); *see also* Gallagher v. Abbott Labs., 269 F.3d 806, 808 (7th Cir. 2001) (Easterbrook, J.) (stating that "firms are entitled to keep silent (about good news as well as bad news) unless positive law creates a duty to disclose").

147. 17 C.F.R. §§ 230.408(a), 240.12b-20 (2020).

avoid half-truths arise.[148] Presumably climate (versus ESG) disclosure is the best case scenario for materiality to suffice as regulatory guidance, given the 2010 Release and its clear direction, but that it is insufficient is, in fact, to be expected.[149]

The SEC's reluctance to require ESG and climate disclosure arises in part from its view that it would be too difficult to frame meaningful disclosure requirements in these areas.[150] Former SEC Chair Clayton has expressed concerns about the uncertainty of the risks that climate change poses to companies and has observed that the issue is one of forward-looking application of managerial expertise in a field that is "complex, uncertain, multi-national/jurisdictional and dynamic."[151] That statement is obviously true. But it is precisely these external uncertainties that caused the TCFD global climate disclosure initiative to focus on four areas that represent the core elements of how organizations operate: the firm's (1) governance, (2) strategy, (3) risk management of the issue, and (4) targets for reducing greenhouse-gas emissions, if any, and metrics by which reductions will be measured.[152] This information is, or should be, within the ambit of management, and is a responsibility for board oversight. The TCFD's disclosure categories do not ask issuers to make speculative determinations about how climate might affect their business at a far future date. Rather, they call upon issuers to discuss how the company is approaching the identification, quantification, and management of climate risks and opportunities today, and what strategic risks and opportunities the company perceives from the transition to a low-carbon economy.

The TCFD's disclosure categories also fit comfortably within what then Chair Clayton identified in January 2020 as the approach the SEC supports regarding climate disclosure:

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148. *See* Roeder v. Alpha Indus., Inc., 814 F.2d 22, 27 n.2 (1st Cir. 1987) (stating that "[i]f the SEC wanted all possibly material information to be in the annual reports, we suspect that the regulations would have been amended to require it"); Donald C. Langevoort, *Disasters and Disclosures: Securities Fraud Liability in the Shadow of a Corporate Catastrophe*, 107 GEO. L.J. 967, 990 (2019) (observing that while "Regulation S-K is extensive and dense, . . . what is striking about these line-item requirements is how much potentially material information is *not* subject to any disclosure obligation").

149. Hazen, *supra* note 130, at 18 (stating that "[t]he amorphous nature of materiality means that it is not sufficiently precise to simply rely on an across-the-board requirement that CSR and ESG disclosures must be made when they are material").

150. *See* Clayton, *supra* note 96 (stating that he believes "climate-related factors are substantially forward-looking and likely involve estimates and assumptions regarding . . . complex and uncertain matters").

151. *Id.*

152. TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES, RECOMMENDATIONS OF THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES iv–v (2017), https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-TCFD-Report-062817.pdf [https://perma.cc/NBV4-D2G7].

> [O]ur ongoing commitment [is] to ensure that our disclosure regime provides investors with a mix of information that facilitates well-informed capital allocation decisions. . . . [T]his commitment has been, and in my view should remain, disclosure-based and rooted in materiality, including providing investors with insight regarding the issuer's assessment of, and plans for addressing, material risks to its business and operations.[153]

Yet, investors do not have insights into how companies are assessing and addressing material climate risks to their business and operations today, at least not from companies' required filings. As stated by a subcommittee of the CFTC, "the [climate] information disclosed falls significantly short of what capital market actors need to adequately integrate climate risk into their decision-making," in part because issuers have construed materiality narrowly.[154] Adopting TCFD as the framework for required climate disclosure could help to solve that problem, so long as those qualitative disclosures do not devolve into boilerplate ones.

Sustainability (ESG) disclosure presents a different issue, but with the same conclusion: materiality as the mandate is not meeting investors' professed needs. There is a wide range of social or environmental issues that can present financial risks to companies, but which issues affect which companies is specific to different industries, geographic locations, company history, what the emerging risks and technologies are in that industry, the social context—whether the pressing social issue of the day is a global pandemic, or structural racism, or populist violence, or all three—and so forth.[155] The SEC was smart to take up human capital management as its first foray into potential ESG disclosure since 1974, given that people and their organization and deployment is a feature of every company. Yet, the complexity of the issue, and the fact that commenters could not agree on one definition of "human capital management," essentially gave the SEC a rationale for hitting the pause button. To be sure, the SEC did enact a new disclosure requirement related to the topic, requiring "a description of the registrant's human capital resources, including . . . any human capital measures or objectives that [the registrant] focuses on in managing the business."[156] But ironically, this requirement could well lead to boilerplate

153. Clayton, *supra* note 96.

154. U.S. COMMODITY FUTURES TRADING COMM'N, *supra* note 144, at 88, 94.

155. *See, e.g.*, Jill E. Fisch, *Making Sustainability Disclosure Sustainable*, 107 GEO. L.J. 923, 950–52 (2019) (arguing that the potential relationships between an issuer's sustainability practices, and the company's risk management, strategy, and longer-term economic vulnerability warrant incorporation of a "sustainability discussion and analysis" requirement into mandated disclosure).

156. Modernization of Regulation S-K Items 101, 103, and 105, Securities Act Release No. 10,825, Exchange Act Release No. 89,670, 85 Fed. Reg. 63,726, 63,737 (Oct. 8, 2020) (to be codified at 17 C.F.R. pts. 229, 239, & 240). *See also supra* text accompanying note 27 (discussing the Human Capital Management Coalition petition).

disclosures. No issuer is likely to say that its human-capital objective is to shift as many employees as possible to part-time or contingent work, for instance. At the same time, the SEC rejected comments calling for data to be disclosed that could have illuminated if, in fact, a company's objective is such a shift, or if the company's employee-turnover rate suggests a management problem or future financial risk.

The SEC could have—and should still consider—enacting new qualitative disclosure that could encompass the field, such as the "Sustainability Discussion and Analysis" (SD&A) proposed by Professor Jill Fisch.[157] That proposal would ask every public company to discuss the top-three sustainability issues facing the company, including a discussion of the potential impacts of each issue on the company and the basis for identifying each issue as one of the top three.[158]

The SEC also could have enacted—and should still consider enacting—new line-item disclosure of data sufficient to inform investors of at least some aspects of the strength, or fragility, of a company's relationship to its employees in any customer-facing field dependent upon large numbers of employees, such as food services or commercial retail operations. The SASB disclosure framework would work well to identify what line-item disclosure would be material, by industry. SASB has a small number of key line-item disclosure requirements, typically about seven, targeted to the specific sustainability risks in each of seventy-seven industries and sub-industries.[159] Employee data will be part of disclosure in many relevant industries.

If SASB requirements were enacted together with TCFD and a generic SD&A requirement, we might see what can be termed "targeted materiality." We use this term to encompass a combination of structured qualitative (TCFD and SD&A) and quantitative (SASB) disclosure, the latter of which is industry specific.[160] Early empirical results suggest that SASB disclosure does provide financially material information to investors.[161] The combination would provide both comparable, consistent data to use for

157. Fisch, *supra* note 155, at 956.

158. *Id.*

159. *See Download SASB Standards*, SUSTAINABILITY ACCOUNTING STANDARDS BD., https://www.sasb.org/standards-overview/download-current-standards/ [https://perma.cc/X36C-WC3C] (explaining that the SASB Standards "identify the subset of environmental, social, and governance issues most relevant to financial performance in each of 77 industries").

160. The SEC has published industry-specific guidelines for disclosure in some industries, for example mining and oil and gas. The SASB targeted disclosure takes the SEC guidelines idea one step further by defining specific data to be disclosed that varies by industry, rather than adapting generic requirements to the specific disclosure challenges of some industries as do SEC industry guidelines.

161. *See* Mozaffar Khan, George Serafeim & Aaron Yoon, *Corporate Sustainability: First Evidence on Materiality*, 91 ACCT. REV. 1697, 1716 (2016) (finding based upon SASB standards "that firms with strong ratings on material sustainability issues have better future performance than firms with inferior ratings on the same issues").

analysis within sub-industries, combined with generic information that could provide insights into how proactive management is concerning future sustainability risks. This proposal is similar to what the world's largest investor, BlackRock, is demanding from each of its thousands of portfolio companies, which is TCFD plus SASB disclosure.[162] The artificial intelligence and big-data tools are being developed to allow high-quality, accurate information to be fed into whichever reporting framework is chosen—TCFD, SASB, or GRI—based on extracting information from companies' enterprise software, such as SAP or Oracle—thus using information the company is already tracking.[163]

B. The Blind Spot Concerning the SEC's Mission

Assuming, as we do, that the SEC is both watching investors' increasing use of ESG and climate data and recognizing the rapid shift in investors' understanding that these issues are related to core financial concerns, we attribute many of the actions and inactions we discuss in Part I to an even more endemic blind spot concerning the breadth of the SEC's mission. Specifically, while there is no doubt that Congress created the SEC to protect investors; maintain fair, orderly, and efficient capital markets; and facilitate capital formation, key SEC decision makers have often adopted an unduly narrow construction of these three overlapping policy goals, particularly when sought-after disclosures are rooted in risks and opportunities created by social or environmental events or trends.

For the reasons discussed below, the SEC's well-recognized mission of "protecting investors" should be construed to include granting investors access to more easily comparable ESG and climate data, given the trillions of dollars of invested capital seeking to incorporate that data into their portfolio constructions, company engagements, and voting. The SEC's current tripartite understanding of its mission is also missing a fundamental piece of what Congress hoped to achieve in adopting the Securities Act of 1933 and the Securities Exchange Act of 1934.

1. Investor Protection.—Intriguing work is being done to explain the rapid and profound shift in investors' views about the importance of ESG and

162. Larry Fink, *Larry Fink's 2021 Letter to CEOs*, BLACKROCK (2021), https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter [https://perma.cc/ZF7R-MYMU].

163. *See* Billy Nauman, Patrick Temple-West & Andrew Edgecliffe-Johnson, *Can Business Step Up as Trust in Government Crumbles?*, FIN. TIMES (Jan. 13, 2021), https://www.ft.com/content/a5e2d769-1346-4224-8828-3a6c4836972e [https://perma.cc/569H-W25M] (describing a company that extracts sustainability data from information that is already being tracked by "integrating with a company's existing enterprise software," and another that "uses big data and artificial intelligence to provide information" on sustainability).

climate data. Professor John Coffee, for instance, attributes it to "fundamental economic logic" driven by the growth of the largest asset managers, such as BlackRock, State Street Global Investors, and Vanguard Group, who together own 20% of shares of the S&P 500 and vote 25% of shares.[164] These institutional investors are diversified, so under standard capital asset pricing model (CAPM) assumptions, systematic risk (beta) is the source of their investment returns.[165] Coffee argues that these investors see ESG data as providing insights into systematic risk, particularly climate, having shifted to a portfolio perspective on their investments and voting, rather than an individual-firm (alpha) perspective.[166] In other words, investment concentration is leading investors to finally perceive themselves as "universal owners," as Hawley and Williams (not this author) theorized they should twenty years ago: if investors own the whole market (world), it is the social, political, and economic health of the whole market (world) that matters.[167] Thus, we see investors collaborating to put pressure on companies to reduce their negative externalities (harmful behavior).[168]

Other scholars attribute increasing ESG stewardship and climate activism by large institutional investors, many of whom are passive investors, to a competition to attract millennial investors.[169] Millennials are due to inherit between $12 trillion and $30 trillion over the next decades, and "place a significant premium on social issues in their economic lives."[170]

164. Coffee, *supra* note 92, at 3, 5–6.

165. *See id.* at 11–12 (stating that, under CAPM standards, "the price of a financial asset will be determined by the asset's systematic risk compared to the risk of the market as a whole"). Coffee cites data compiled by Professor Madison Condon, *supra* note 94. Coffee, *supra* note 92, at 6 n.15. He also references her exploration of the implications of concentrated ownership, particularly her insight that such firms will care about portfolio-level, systematic risks like climate change. *Id.* at 14. Condon, in turn, credits the originators of the idea that large, passive, diversified institutional investors are "universal owners" whose returns will be derived from market-spanning issues, not firm-specific outcomes. *See* Condon, *supra* note 94, at 6 & n.22 (citing JAMES P. HAWLEY & ANDREW T. WILLIAMS, THE RISE OF FIDUCIARY CAPITALISM 3–5, 170–72 (2000)).

166. Coffee, *supra* note 92, at 14–15.

167. *See* HAWLEY & WILLIAMS, *supra* note 165, at 170 (arguing that "because [universal owners] own the economy as a whole, universal owners should care about the overall health of the economy, not just the economic health of individual firms").

168. For instance, Condon provides data showing that the same six shareholders control 24% of ExxonMobil and 26% of Chevron and observes that these shareholders have pressured both companies regarding emissions and climate change. Condon, *supra* note 94, at 10–11, 24 & n.116. Another example is Climate Action 100+'s consortium of 545 investors, with $52 trillion invested capital, directly engaging with the world's largest companies and asking them to cut emissions, improve governance, and improve climate financial disclosures. CLIMATE ACTION 100+, https://www.climateaction100.org/ (last visited May 29, 2021) [https://perma.cc/ZV8M-5NQV].

169. *E.g.*, Michal Barzuza, Quinn Curtis & David H. Webber, *Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance*, 93 S. CAL. L. REV. 1243, 1250 (2020).

170. *Id.* at 1244, 1249.

In addition, the data on the financial materiality of many sustainability issues, certainly including climate, is starting to show rather consistently that firms that manage sustainability issues well outperform on many financial measures.[171] As BlackRock, the world's largest investor with over $8.5 trillion assets under management, recently emphasized, "[o]ver the past few years, more and more of our clients have focused on the impact of sustainability on their portfolios. This shift has been driven by an increased understanding of how sustainability-related factors can affect economic growth, asset values, and financial markets as a whole."[172]

Providing investors who manage trillions of dollars of other peoples' money with the data they need to accurately price risk (for active investors) and vote their shares (for active and passive investors) is firmly within the SEC's investor-protection remit.

2. Broader Accountability Goals.—Yet, Congress had broader accountability goals in enacting the Securities Act and the Exchange Act, and even investor protection was not simply a financial construct going to the investment decision as to whether to buy or sell a particular security—voting rights mattered. Congress saw fundamental public purposes in having well-regulated financial markets, ascribing responsibility for the Great Depression to the Wall Street crash. Those purposes included empowering shareholders in their exercise of voting rights, improving the "morals" of company directors, and promoting the well-being of the economy. This conclusion is based on three pillars: the language of the statutes, the purposes set out in those statutes, and the legislative history. Because these points have been covered at length, this summary will be short.[173]

First, in several provisions in each statute, Congress delegated power to the Commission to develop rules concerning disclosure "as necessary or appropriate in the public interest or for the protection of investors."[174] This language indicates a distinct regulatory mission broader than mere investor protection, although one to be construed according to the purposes of the

171. *See* Cynthia A. Williams, *Corporate Social Responsibility and Corporate Governance*, *in* THE OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE 647–50 (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2018) (discussing empirical data); *see also* Williams & Fisch, *supra* note 14 (pointing to research that found improvements in ESG performance and sustainability standards lead to improvements in financial performance); Fisch, *supra* note 155, at 925–26 & n.9 (discussing the importance of sustainability assessments for the economic valuation of issuers).

172. *Sustainability as BlackRock's New Standard for Investing*, BLACKROCK (2020), https://www.blackrock.com/corporate/investor-relations/2020-blackrock-client-letter [https://perma.cc/9A8F-WSBD].

173. Williams, *supra* note 16.

174. *Id.* at 1235–37, 1236 n.202 (emphasis omitted) (quoting the Exchange Act § 14(a), 15 U.S.C. § 78n (1994)) (analyzing the text and statutory citations delegating power to the Commission to regulate "as necessary or appropriate in the public interest or for the protection of investors").

statutes. Second, as set out in § 2 of the Exchange Act, those purposes directly included affecting the conduct of directors, bankers, and underwriters, since those market participants' actions were perceived by Congress to have badly affected the economy as a whole.[175] Manipulation of stock prices, "overboarding," excessive speculation, the misallocation of capital, undisclosed conflicts of interest, and the managing of companies in directors' or banks' interests (as opposed to in investors' and the public's interests), were all behaviors targeted for disclosure.[176] Third, the legislative history is replete with references to changing the conduct, the morals, and the sense of public responsibility of the people running America's companies.[177]

It is in this context that we question some of the public positions taken by former and current SEC officials. One well-known example occurred in 2013, in a speech by then-SEC Chair Mary Jo White discussing the importance of the SEC's independence.[178] She maintained that Congress on occasion directs the SEC to issue rules "requiring disclosure that does not fit within our core mission" and referenced in particular the Dodd–Frank rulemaking mandates for mine safety and conflict minerals disclosures, which, to her, "seem[ed] more directed at exerting societal pressure on companies to change behavior, rather than to disclose financial information that primarily informs investment decisions."[179] Other SEC Commissioners have likewise surmised that certain ESG disclosure requirements would exceed the scope of the SEC's mission.[180] The argument appears to be that

175. Williams, *supra* note 16, at 1223–27. *See also* JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET 39–40 (2d ed. 1995) ("[A] primary enduring mission of the SEC has been to compel disclosure of data by firms involved in the securities markets, indirectly inducing these firms to avoid illegal or embarrassing activities.").

176. *See* Williams, *supra* note 16, at 1227–35 (discussing the legislative history of the Securities Act of 1933).

177. *Id.*

178. White, *supra* note 15.

179. *Id.*

180. *See, e.g.*, Hester M. Peirce, Comm'r, U.S. Sec. & Exch. Comm'n, Festivus, Fortnite, and Focus: Remarks Before the Council of Institutional Investors Spring Conference (Mar. 5, 2019), https://www.sec.gov/news/speech/speech-peirce-030519 [https://perma.cc/6PV2-BRH9] (discussing ESG disclosure and stating that "[w]hen the SEC is asked to concentrate on issues other than protecting investors, facilitating capital formation, and fostering fair, orderly, and efficient markets, our focus shifts away from our mission"); Elad L. Roisman, Comm'r, U.S. Sec. & Exch. Comm'n, Keynote Speech at the Society for Corporate Governance National Conference (July 7, 2020), https://www.sec.gov/news/speech/roisman-keynote-society-corporate-governance-national-conference-2020 [https://perma.cc/DNN2-26LW] (discussing ESG disclosure and contending that "the federal securities laws . . . have a relatively narrow scope"). In the final year of her term, Chair Mary Jo White more frequently began to reference investors' pressure for more sustainability disclosure and stated that the "issue has our attention," but she did not concede that further requirements were needed. Mary Jo White, Chair, U.S. Sec. & Exch. Comm'n, Keynote Address at the International Corporate Governance Network Annual Conference: Focusing the Lens of Disclosure to Set the Path Forward on Board Diversity, Non-GAAP, and Sustainability (June 27,

corporate "behaviors" with social or political implications are not properly subject to the "societal pressure" engendered by securities disclosure, even though the disclosure is directed to and could be used by investors. But this concept of what disclosure is meant to protect—the accuracy of securities prices—is only a part, but not the whole, of investor protection. Disclosure is also meant to inform shareholders' voting rights, and information about corporate behaviors could well be material to director-election decisions. There is also ample evidence that the exertion of "societal pressure on companies to change behavior" was precisely what the New Deal Congress sought in enacting the federal securities laws.

Former-Chair White's speech narrowly termed this pressure "societal," but today we also see such pressure—addressed to companies' social, environmental, and political behavior—being exerted directly by institutional investors and others through Rule 14a-8's shareholder proposal process. The failure to consider this pressure as a necessary and appropriate part of corporate governance was at least a factor prompting the recent changes to Rule 14a-8 that limit public-company investors' ability to hold corporate insiders accountable.[181]

Conclusion

Aligning the SEC's ESG and climate disclosure requirements with those of its global allies would protect its institutional legitimacy and harness the creativity and power of American companies to address pressing social and environmental issues—issues that are a substantial part of the market to which investors are exposed. As we look to the next administration, there are promising indications that the SEC is poised to undertake just such alignment.

2016), https://www.sec.gov/news/speech/chair-white-icgn-speech.html [https://perma.cc/BG2W-7CGV].

181. *See supra* text accompanying notes 78–79 (discussing the revisions to Rule 14a-8 that will make it more difficult for small shareholders to engage with companies through shareholder proposals).