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MAKING SUSTAINABILITY DISCLOSURE SUSTAINABLE

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Abstract

Sustainability is receiving increasing attention from issuers, investors and regulators. The desire to understand issuer sustainability practices and their relationship to economic performance has resulted in a proliferation of sustainability disclosure regimes and standards. The range of approaches to disclosure, however, limit the comparability and reliability of the information disclosed. The Securities & Exchange Commission (SEC) has solicited comment on whether to require expanded sustainability disclosures in issuer's periodic financial reporting, and investors have communicated broad-based support for such expanded disclosures, but, to date, the SEC has not required general sustainability disclosure.

This Article argues that claims about the relationship between issuer sustainability practices and risk management, business plan and economic vulnerability, as well as the need for investors and regulators to evaluate those claims, warrant incorporating sustainability information into SEC-mandated financial reporting. Drawing upon the existing narrative disclosure frameworks in SEC-mandated reporting requirements, the Article offers an innovative proposal sustainability disclosure -- a sustainability discussion and analysis or SD&A section of

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the annual report. The Article identifies critical components necessary to make mandated sustainability disclosure both practical and effective and offers a workable first step for integrating sustainability disclosure into issuer financial reporting.

Introduction

In January 2018, Larry Fink, CEO of Blackrock, made headlines when he called upon corporations to pay greater attention to sustainability and societal impact in his annual letter to CEOs.[1] As Fink explained, "a company's ability to manage environmental, social, and governance matters demonstrates the leadership and good governance that is so essential to sustainable growth, which is why we are increasingly integrating these issues into our investment process."[2] One reporter termed the letter "a watershed moment on Wall Street."[3]

Fink's letter was a high-profile example of a major institutional investor expressing its concerns about corporate sustainability, but it was not an isolated occurrence. Investor focus on sustainability is accelerating.[4] Indeed, even Martin Lipton has acknowledged that "sustainability has become a major, mainstream governance topic."[5] The

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[1] See, e.g., Sarah Krouse, BlackRock CEO to Companies: Pay Attention To 'Societal Impact', Wall St. J., Jan. 16, 2018, https://www.wsj.com/articles/blackrock-ceo-to-companies-pay-attention-to-societal-impact-1516120840 (reporting Fink's letter); Andrew Ross Sorkin, BlackRock's Message: Contribute to Society, or Risk Losing Our Support, N.Y. Times Dealbook, Jan. 15, 2018, https://www.nytimes.com/2018/01/15/business/dealbook/blackrock-laurence-fink-letter.html (same).

[2] Larry Fink's Annual Letter to CEOs, A Sense of Purpose, BlackRock website, https://www.blackrock.com/corporate/en-no/investor-relations/larry-fink-ceo-letter

[3] Sorkin, supra note __.

[4] See, e.g., Gregory Unruh, et al., Investing For a Sustainable Future, 2016, at 3, http://marketing.mitsmr.com/offers/SU2016/57480-MITSMR-BCG-Sustainability2016.pdf?utm_source=WhatCounts%2c+Publicaster+Edition&utm_medium=email&utm_campaign=surpt16&utm_content=Download+the+Report+(PDF)&cid=1 ("a growing number of investors are paying attention to ESG performance, as evidence mounts that sustainability-related activities are material to the financial success of a company over time").

[5] Martin Lipton, Spotlight on Boards, Wachtell Lipton Memo, June 1, 2018.

debate over sustainability is leading investors, executives and directors to rethink how corporations engage in long term value creation.[6]

The extent to which corporations should incorporate sustainability objectives into their operational decision-making is highly contested, as is the relationship between societal impact and economic value.[7] Indeed, the Department of Labor subsequently issued new guidelines for retirement plans cautioning that "Fiduciaries must not too readily treat ESG factors as economically relevant to the particular investment choices at issue when making a decision."[8] Critical to evaluating the effect of sustainability practices on economic value, however, is being able to assess and evaluate an issuer's sustainability practices. For investors and capital markets to consider the societal impact of a firm's operations, they must have access to adequate sustainability disclosure.

Therein lies the problem. Although the focus on increasing sustainability disclosure is accelerating both in the United States and globally,[9] investors continue to report dissatisfaction with existing disclosures.[10] Recognizing this dissatisfaction, the SEC has raised the question of whether it should require increased sustainability disclosure as

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[6] See Unruh, et al., supra note __ at 7 (reporting survey results indicating that "more than 80% of investor respondents indicate that good sustainability performance increases a company's potential for long-term value creation.").

[7] See, e.g., Robert G. Eccles, Ioannis Ioannou & George Serafeim, The Impact of Corporate Sustainability on Organizational Processes and Performance, 60 Mgmt. Sci. Rev. 2835 (2014) (describing study finding that companies which voluntarily adopted sustainability policies by 1993 outperformed their counterparts over the long term).

[8] U.S. Dept. of Labor Field Assistance Bulletin No. 2018-01, Apr. 23, 2018, https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2018-01.

[9] Thousands of companies around the world, including 95 percent of the Global Fortune 250, voluntarily report on their environmental, societal, and economic impacts. Adam Sulkowski & Sandra Waddock, Beyond Sustainability Reporting: Integrated Reporting is Practiced, Required and More Would be Better, 10 U. St. Thomas L.J. 1060, 1061 (2013).

[10] For example, a 2014 PWC survey reported that over 89% of investors are dissatisfied with existing sustainability disclosures. PWC, Sustainability goes mainstream: Insights into investor views, May 2014, at 18, https://www.pwc.com/us/en/pwc-investor-resource-institute/publications/assets/pwc-sustainability-goes-mainstream-investor-views.pdf. Michael Bloomberg, who chairs the Sustainability Accounting Standards Board stated in 2015 that "[F]or the most part, the sustainability information that is disclosed by corporations today is not useful for investors or other decision-makers. . . ." Bloomberg, *Impact Report Update 2015* 2, (2015), *available at* http://www.bbhub.io/sustainability/sites/6/2016/04/16_0404_Impact_report.pdf.

part of its "Disclosure Effectiveness Initiative."[11] The SEC received thousands of responses urging the SEC to do so.[12] Investors continue to request the SEC to "initiate rulemaking to develop mandatory rules for public companies for disclosure of high quality environmental, social, and governance information."[13]

One reason for concern with current disclosure practices is most existing sustainability reporting is voluntary which means that individual issuers choose which information to disclose. The resulting lack of standardization means that issuer disclosures vary substantially, impeding comparability.[14] A second concern is that sustainability reporting is

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[11] See, e.g., Rick A. Fleming, Investor Advocate, Moving Forward with the Commission's Disclosure Effectiveness Initiative, Nov. 19, 2016, https://www.sec.gov/news/speech/moving-forward-with-the-disclosure-effectiveness-initiative.html (describing the initiative as partially a response to legislation ordering the SEC to revise Regulation S-K but explaining that the initiative is "broader in its objectives and scope"). The SEC issued a staff report on the effectiveness of the disclosure requirements in Regulation S-K in December 2013. Report on Review of Disclosure Requirements in Regulation S-K, Dec. 2013, https://www.sec.gov/news/studies/2013/reg-sk-disclosure-requirements-review.pdf. In April 2016, the In April 2016, the SEC issued Concept Release on Disclosure Effectiveness which, in part, invited comment on the extent to which SEC rules should mandate sustainability disclosure. Concept Release, Business and Financial Disclosure Required by Regulation S-K, Sec, Act Rel. No. 33-10064, Apr. 13, 2016, https://www.sec.gov/rules/concept/2016/33-10064.pdf ("Concept Release on Disclosure Effectiveness").

[12] See, e.g., Tyler Gellasch, *Joint Report: Towards a Sustainable Economy: A review of Comments to the SEC's Disclosure Effectiveness Concept Release*, 14 (Sept. 2016), *available at:* https://static1.squarespace.com/static/583f3fca725e25fcd45aa446/t/5866d3c0725e25a97292ae03/1483133890503/Sustainable-Economy-report-final.pdf (summarizing responses to SEC's concept release)

[13] See Draft Petition for Rulemaking from Cynthia Williams to Brent J. Fields Secretary, SEC, dated March 2, 2018 (on file with author).

[14] By way of example, both General Motors and Ford provide different information on exactly the same topic -- their developments with respect to electric vehicles. General Motors describes the number of electric vehicles that it intends to bring to market by 2023 and the number of miles driven by drivers of GM electric vehicles. General Motors 2017 Sustainability Report, 2017 Highlights, https://www.gmsustainability.com/aspire/highlights.html. Ford reports on the number of hybrid and fully-electric vehicles that it intends to bring to market by 2022, the size of its investment in electric vehicles, and the progress of several specific global partnerships on electrified vehicles. Ford Sustainability Report 2017/2018, https://corporate.ford.com/microsites/sustainability-report-2017-18/driving-change/electrification.html.

typically characterized as "nonfinancial reporting,"[15] and is distinct in location, format and, in many cases, rigor, from other investor-oriented information. Finally, sustainability reporting varies widely in quality and its accuracy is rarely audited or monitored, reducing its effectiveness as a tool for improving accountability.[16]

These limitations impede the ability of investors and researchers to evaluate rigorously the sustainability practices of issuers and to analyze effectively the relationship between sustainable practices and economic performance. One possible solution is to continue the reliance on private ordering but to seek common standards that facilitate comparability.[17] A variety of standard-setters are assisting in the process by developing and publishing sustainability metrics, ratings and guidelines.[18] This variety is, in itself, a problem, in that it both increases search costs for investors and makes it difficult to compare information from different providers.[19] The quality of third party information is diminished by the fact that most standard-setters rely on information voluntarily supplied by issuers, either through public disclosures or directly to the standard setter. In addition, to the extent that standard setters use proprietary methodologies or information that is not publicly available, the significance of their ratings is not transparent and is difficult to evaluate.

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[15] See Nasdaq ESG Reporting Guide, A Support Program for Nasdaq Issuers Focus Area: Nordic & Baltic Markets, Mar. 23, 2017, at 10, http://business.nasdaq.com/media/ESG-Reporting-Guide_tcm5044-41395.pdf

[16] See Patrick Odier, Why lack of data is the biggest hazard in 'green investing,' Fin. Times, Mar. 6, 2017, https://www.ft.com/content/be8e5db2-0249-11e7-aa5b-6bb07f5c8e12 (observing that "data on the real-world impact that companies exert is poor, incomplete, non-standardised, or inaccessible").

[17] For example, the Sustainability Accounting Standards Board (SASB) has been engaged in a multi-year project, in conjunction with issuers and investors, to develop common standards for disclosure of material sustainability information. See About the SASB, https://www.sasb.org/about-the-sasb/.

[18] Elisse Walter, The Future of Sustainability Disclosure: What Remains Unchanged in an Environment of Regulatory Uncertainty?, Harv., Law School Forum on Corp. Gov. & Fin. Reg., Dec. 7, 2016, https://corpgov.law.harvard.edu/2016/12/07/the-future-of-sustainability-disclosure-what-remains-unchanged-in-an-environment-of-regulatory-uncertainty/

[19] See, e.g., Charles Merrill, The SEC Revisits Sustainability: Will Sustainability Reporting Become Mandatory for Publicly-Traded U.S. Corporations?, Lexology, Oct. 7, 2016, https://www.lexology.com/library/detail.aspx?g=8148a821-b3d0-4e23-b7de-55b06f9ed7da ("the current patchwork of ESG reporting methods does not make such information readily accessible").

Another option is mandatory sustainability disclosure. A number of jurisdictions have imposed or are considering the imposition of mandatory disclosure requirements related to specific sustainability issues. One example of the move toward mandatory sustainability disclosure is the 2014 EU Directive on the Disclosure on Non-Financial and Diversity Information, which will require certain issuers to begin providing specified sustainability disclosures in 2018.[20]

In the United States, commentators have repeatedly called upon the SEC to do more to formalize sustainability disclosure.[21] Incorporating mandatory sustainability reporting into the disclosure requirements of the federal securities laws faces obvious political obstacles, particularly under an administration that embraces a deregulatory approach.[22] Apart from the political obstacles, however, there are concerns about the practicability

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[20] DIRECTIVE 2014/95/EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 22 October 2014, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0095. The Directive requires non-financial reporting by 1) large companies, 2) "public-interest" entities, and 3) companies with more than 500 employees per year, on average. See CSR Europe & GRI, Member State Implementation of Directive 2014/95/EU, 2017, at 8, https://www.globalreporting.org/resourcelibrary/NFRpublication%20online_version.pdf (explaining these criteria). Because the Directive is implemented at the country level, different countries have adopted somewhat different criteria with respect to its application. For example, the Danish Regulation redefines large company to include, inter alia, companies with an average of 250 employees. GRI, Innovative implementation of EU Directive on Non-Financial Reporting, Feb. 7, 2018, https://www.globalreporting.org/information/news-and-press-center/Pages/EU-Directive-on-Non-Financial-Reporting.aspx. Similarly, the Greek legislation imposes a duty to report on small and medium-size companies, as well as large companies. Id.

[21] See, e.g., Letter from AFL-CIO, July 21, 2016, available at https://www.sec.gov/comments/s7-06-1 6/s706 l 6-305.pdf. ("given the clear and growing demand from investors for environmental, social and governance . . . information, the Commission must begin requiring ESG related line-item disclosures as well as a process to incorporate emerging ESG metrics into disclosure in the future."); Che Odom, Investors Want Sustainability Disclosures in SEC Overhaul, Bloomberg Law, July 21, 2016, https://www.bna.com/investors-sustainability-disclosures-n73014445099/ (reporting that investors want "the SEC to require annual, uniform sustainability reporting from public companies as part of the overhaul of the agency's disclosure regime").

[22] The Trump administration and the Republican Congress have announced their intention to reduce or repeal existing disclosure requirements such as resource extraction and conflict minerals. See Financial Choice Act, H.R. 10, 115th Cong. (Discussion Draft 2017), https://financialservices.house.gov/uploadedfiles/choice_2.0_discussion_draft.pdf [https://perma.cc/UE8M-B5GR]

of developing a workable structure for mandatory disclosure requirements. As commentators have observed, sustainability disclosures must be specific enough to provide investors and the capital markets with meaningful and readily comparable information. At the same time, relevant sustainability issues vary substantially among issuers and industries, making a detailed line item approach difficult.[23] The alternative, a principles-based approach, complicates policing the accuracy of issuer disclosures and risks producing low quality or boilerplate disclosures.

This Article proposes a solution – mandating a required sustainability discussion and analysis or SD&A as part of an issuer's annual report to shareholders.[24] The SD&A, which would be modeled after existing Management Discussion and Analysis (MD&A) and Compensation Discussion and Analysis (CD&A) and, like them, included in the annual report to investors, would reflect a principles-based approach requiring issuers to address the sustainability issues most important to their operations.[25] This Article proposes that the SD&A require an issuer to disclose, at a minimum, the three sustainability issues that are most significant for the firm's operations, to explain the basis for its selection and to explain the impact of those issues on firm performance.

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[23] This problem is not insurmountable. Some sustainability issues are common to all firms. See, e.g., Letter from CALPRS, July 21, 2016, available at https:/1www.sec.gov/cornments/s7-06-16/s706 l 6-267 .pdf ("there are some issues that are common to all firms, for example, gender, diversity and the impact of climate change."). In addition, the Sustainability Accounting Standards Board (SASB) has developed a proposed solution to industry variation by creating accounting standards for 79 industries in 11 sectors. See SASB website, https://www.sasb.org/.

[24] The formal requirement would be reflected by including the SD&A as part of Regulation S-K. The SEC adopted Regulation S-K in 1980 to centralize the disclosure requirements of the Securities Act of 1933 (which apply to public offerings) and the Securities Exchange Act of 1934 (which impose periodic reporting requirements on public companies). See John C. Coffee, Jr., Re-Engineering Corporate Disclosure: The Coming Debate over Company Registration, 52 Wash. & Lee L. Rev. 1143, 1145 (1995) (describing the widespread criticism of the "pointless duplication" in disclosure rules prior to Reg S-K). The disclosures required by Regulation S-K thus apply in the context of various securities filings including registration statements and annual reports.

[25] See, e.g., Concept Release on Disclosure Effectiveness, supra note __, 81 Fed. Reg. 23,916, 23,925 (defining requirements as "'principles-based' because they articulate a disclosure objective and look to management to exercise judgment in satisfying that objective.").

The SD&A would centralize sustainability disclosures within an issuer's securities filings. As is currently the case with the MD&A and CD&A requirements, the proposal would require the SEC to issue guidance identifying sustainability issues that are likely to be material to investors and articulating the principles that issuers should apply in preparing their SD&As. The SD&A proposal would place responsibility for drafting such disclosures on the personnel who prepare the issuer's financial reporting, and subject sustainability disclosure to the same regulatory framework that applies to other securities disclosures including SEC oversight through its review of issuer securities filings, and, when applicable, liability exposure for fraudulent misrepresentations.

To ensure the board's involvement in overseeing both the development of an issuer's sustainability practices and the disclosure of those practices, the proposal would require directors to certify the accuracy of the disclosures contained in the SD&A. This requirement would establish a framework for effective director oversight that would bring accountability to the disclosure regime, thereby addressing a key investor concern – that boards consider sustainability practices that have a material impact on or pose material risks to the firm's operations and incorporate those considerations into their strategic planning.

Incorporating sustainability disclosure into annual financial reporting would reflect the reality that sustainability considerations are growing in economic importance and thus of concern to investors and the capital markets. It would be an important first step toward increasing the uniformity, reliability and comparability of sustainability disclosure. And it would provide important data to allow the capital markets to evaluate the economic importance of sustainable business practices.

The Article proceeds as follows. Part I sets the groundwork by describing existing sustainability disclosure practices. Part II identifies the limitations of existing practices, making the case for mandatory sustainability disclosure integrated with financial reporting. Part III introduces this Article's proposed approach to sustainability disclosure – the SD&A. Part IV identifies advantages and potential limitations of the proposal.

I. Background and Existing Sustainability Disclosure Practices

This section provides a brief background of corporate sustainability disclosure. It starts with an overview of the scope and rationale for sustainability disclosure. It then outlines the history of SEC regulation of sustainability disclosure and sources of mandatory sustainability reporting requirements beyond the federal securities laws. Finally, it identifies existing approaches to voluntary disclosure and the institutional players that contribute to the voluntary regime.

A. The Concept of Sustainability Disclosure

Although it is useful to start any discussion of sustainability disclosure by defining the term sustainability, there is no consensus on a precise definition. Use of the term is often traced to a 1987 United Nations report that defined sustainability as "[actions that]...meet the needs and aspirations of the present without compromising the ability to meet those of the future."[26] The principles in this report were formalized in the UN Global Compact, the "most prominent . . . the hundreds of international institutional and policy initiatives around corporate social and environmental responsibility and sustainability.[27] The idea behind corporate sustainability is decisions that incorporate social, political and ethical concerns in addition to traditional financial performance.[28] As J. Robert Brown explained in his comment letter to the SEC: "Sustainability involves matters that can impact the long-term success of the company and the economy."[29] Martin Lipton notes that sustainability "encompasses

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[26] U.N. World Comm'n on Env't. & Dev., Our Common Future, U.N. Doc. A/42/427 (1987), available at http://www.un-documents.net/our-common-future.pdf., at 4. See, e.g., Sarah Widder, Institutionalizing Sustainability: Implementation of Executive Order 13,514 and its Impact on the Environmental, Economic and Social Performance of Pacific Northwest National Laboratory, 27 ND J. L. Ethics & Pub Pol'y 229, 230 (2013) (extolling the "simplicity and breadth of this definition").

[27] See Thomas Clarke, The Widening Scope of Directors' Duties: The Increasing Impact of Corporate Social and Environmental Responsibility, 39 Seattle U. L. Rev. 531, 551 (2016).

[28] See Concept Release on Disclosure Effectiveness, supra note __, at 207 (discussing various sustainability considerations).

[29] Comment Letter of J. Robert Brown dated Oct. 3, 2016 at 1 n3, https://www.sec.gov/comments/s7-06-16/s70616-374.pdf. Brown goes on to explain that these matters "relate to corporate governance, international tax strategies, climate change, political spending, derivatives exposures, investments in human capital, and other areas of demonstrated interest for investors and the public." Id. The precise topics that arguably fall within the scope of sustainability continue to evolve. See, e.g., Scott

a wide range of issues, such as climate change and other environmental risks, systemic financial stability, labor standards, and consumer and product safety."[30]

Commentators use a variety of terms to describe corporate sustainability and sustainability reporting including CSR (corporate social responsibility),[31] ESG (environmental, social and governance),[32] triple bottom line,[33] and societal impact. Some commentators use the term nonfinancial reporting to describe sustainability disclosure.[34]

Traditionally the demand for corporate sustainability disclosure has come from special interest investors such as religious organizations and ethical investment funds as well as non-investor special interests.[35] More recently, however, interest in sustainability disclosure has spread to the mainstream investor. Goldman Sachs has described this interest as the "ESG Revolution" and compiled data showing a rise of ESG focus in

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J. Shackelford & Scott Russell, Operationalizing Cybersecurity Due Diligence: A Transatlantic Case Study, 67 S.C. L. Rev. 609, 626 (2016) (advocating "a wide view of risk management to encompass all of the dimensions of sustainability--economic, environmental, social, and, potentially, [cyber-] security.")

[30] Lipton, supra note __.

[31] See, e.g., John M. Conley & Cynthia A. Williams, Engage, Embed, and Embellish: Theory Versus Practice in the Corporate Social Responsibility Movement, 31 Iowa J. Corp. L. 1 (2005) (describing the CSR movement).

[32] The Nasdaq explains that the term sustainability is more commonly used by issuers, while investors commonly use the term ESG. See Nasdaq ESG Guide, supra note __ at 10. ("while this document primarily uses the term "ESG" because it is commonly used among investors, the term "sustainability" is used interchangeably as it is more common among companies.")

[33] John Elkington, Cannibals with Forks: The Triple Bottom Line of 21st Century Business (1997).

[34] Letter from Calvert Investments, July 21, 2016, available at https://www.sec.gov/comments/s7-06-l 6/s706 l 6-245.pdf ("Investors increasingly consider non-financial factors when assessing companies' long-term performance."). This term is somewhat misleading in light of the claimed relevance of sustainability information to economic performance. See, e.g. Nasdaq ESG Guide, supra note __ at 10 ("The very term non-financial is a controversial point of reference, because many believe that ESG information is no less relevant or useful to an investor in assessing the financial prospects and operational performance of a company than information channeled through traditional accounting practices.").

[35] See, e.g., Commissioner Michael S. Piwowar, Dissenting Statement at Open Meeting on Resource Extraction, Dec. 11, 2015, https://www.sec.gov/news/statement/piwowar-dissenting-statement-at-open-meeting-resource-extraction.html (describing Congressional mandate of disclosure of resource extraction payments as responding to the demands of non-shareholder special interest groups).

traditional investor-directed communications such as "earnings transcripts, social media and asset manager initiatives." Support for ESG disclosure has extended to a growing percentage of the investor community.[36] For example, Exxon shareholders voted on a shareholder proposal at the 2017 annual meeting requesting that the company report on "the impact on its business of compliance with global climate change guidelines."[37] The proposal received more than 62 percent of the votes cast, a tally that included the support of Blackrock and Vanguard.[38] A similar proposal passed at Occidental Petroleum earlier in 2017.[39]

The growing interest by traditional investors in sustainability disclosure is based on a variety of rationales. Many investors believe that that sustainability information allows them to evaluate the firm's operational plan from a long-term financial perspective.[40] Investors use sustainability disclosures to understand a firm's long-term business risk.[41] Investors also argue that sustainability disclosure provides insights into the board's level of engagement and oversight, enabling them to determine the extent to which the board is aware of and managing factors that affect the viability of the company's strategy over the intermediate and long term.

These analyses identify a potential relationship between sustainability and economic performance. Although the evidence on this

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[36] Goldman Sachs, A Revolution Rising - From Low Chatter to Loud Roar, Apr. 23, 2018, https://www.goldmansachs.com/insights/pages/esg-revolution-rising.html

[37] Exxon shareholders approve measure on climate-change report, CNBC, May 31, 2017, http://www.cnbc.com/2017/05/31/exxon-steps-up-efforts-to-sway-shareholders-on-climate-report-vote.html.

[38] Id.

[39] Rob Kozlowski, Occidental Petroleum shareholders pass climate change disclosure proposal, Pensions & Investments, May 12, 2017, http://www.pionline.com/article/20170512/ONLINE/170519941/occidental-petroleum-shareholders-pass-climate-change-disclosure-proposal.

[40] See, e.g., Letter from Sanford J. Lewis to SEC Div. of Corp. Fin. re Shareholder Proposal to Goldman Sachs, dated Jan. 19, 2017, 2017 SEC No-Act. LEXIS 47, *30 (explaining that investors use sustainability disclosures to evaluate "long-term value creation and systemic risk.")

[41] See, e.g., Letter from Trillium Asset Mgmt to SEC Div. of Corp. Fin. dated Jan. 11, 2018, 2018 SEC No-Act. LEXIS 198, *26 (arguing in support of shareholder proposal requesting company to provide a sustainability report that ESG reporting "allows companies to better integrate and capture value from existing sustainability efforts, identify gaps and opportunities in policies and practices, strengthen risk management programs, stimulate innovation, enhance company-wide communications, and recruit and retain employees").

point is mixed, several studies support the claim that sustainability factors are related to operating performance and share price. Notably, these studies are in some tension with the Department of Labor's recent suggestion that ESG factors are typically collateral to economic considerations.[42] A recent Merrill Lynch study, for example, reports that ESG factors are associated with higher earnings quality and lower risk of bankruptcy.[43] Notably, the report claims that ESG attributes "have been a better signal of future earnings volatility than any other measure we have found."[44] Similarly, an academic paper surveys the empirical literature and reports that the vast majority of empirical studies document correlations between sustainability practices and economic performance.[45]

To the extent there is a relationship between sustainability and performance, sustainability disclosure would seem to fit within the traditional objectives of the federal securities laws. The history of sustainability disclosure within the mandatory disclosure regime in the U.S. has been fragmented, however. For the most part, as detailed further below, the SEC has taken the view that sustainability disclosure is not generally material and that mandatory disclosure should be limited to information that is useful to investors.[46]

B. The History of Sustainability Disclosure under the Federal Securities Laws

Efforts by various social and political groups to use the securities laws to obtain greater sustainability disclosure from corporations started in the 1960s and were, in part a response to concerns about the growth of

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[42] See U.S. Dept. of Labor Field Assistance Bulletin No. 2018-01, supra note __ (referring to "otherwise collateral ESG issues" but acknowledging that such issues may sometimes "involve business risks or opportunities that are properly treated as economic considerations themselves").
[43] Savita Subramanian, Bank of American Merrill Lynch, *Equity Strategy Focus Point—ESG Part II: A Deeper Dive* (June 15, 2017), https://www.bofaml.com/en-us/content/esg-socially-responsible-investing-strategies.html.
[44] Id. at 1.
[45] Gordon L. Clark, Andreas Feiner & Michael Viehs, From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance (2015), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2508281
[46] See Cynthia A. Williams, The Securities and Exchange Commission and Corporate Social Transparency, 112 Harv. L. Rev. 1197, 1247 (1999) (describing and challenging SEC's position that sustainability disclosure is not generally economically material).

corporate power and the societal implications of that growth.[47] In 1971, the Natural Resources Defense Council (NRDC) and the Project on Corporate Responsibility filed a rulemaking petition asking the SEC to require public companies to mandate civil rights and environmental disclosure.[48] The SEC largely refused to adopt the requested rule changes to the extent that the information did not have to be disclosed under the existing materiality standard, although it did modify its requirements with respect to environmental disclosure.[49] After protracted litigation challenging this decision, the DC Court of Appeals dismissed the complaint, holding that the that the SEC's decision not to require specific disclosures and to require disclosure only of information that was reasonably likely to be material to investors[50] was entitled to substantial deference.[51]

The SEC's reasoning that its disclosure requirements should be limited to information that is economically material to investors was articulated in the 1977 report issued by the Advisory Committee on Corporate Disclosure led by former Commissioner A. A. Sommer, Jr. (the

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[47] Id. See also Rob Gray, The Social Accounting Project and Accounting Organizations and Society: Privileging Engagement, Imaginings, New Accountings and Pragmatism over Critique?, 27 Acct., Orgs. & Soc'y 687, 690 (2002), (explaining that interest in social accounting grew, in the mid to late 1960s, "contemporaneously, with an apparent growth in anxiety about corporate ethics, corporate power, social responsibility and ecological degradation").

[48] See Natural Resources Defense Council, Inc. v. SEC (NRDC I), 389 F. Supp. 689, 693-94 (D.D.C. 1974) (describing the petition).

[49] Williams, supra note __ at 1249. The SEC issued an interpretive release stating Disclosures Pertaining to Matters Involving the Environment and Civil Rights, Exchange Act Release No. 5170, 1971 SEC LEXIS 20 (July 19, 1971) calling attention to issuers' obligations to disclose "matters pertaining to the environment" and "certain civil rights matters", where material, such as when the existing requirements regarding disclosure of legal proceedings applied. In 1973, the SEC codified the requirement that material legal proceedings relating to environmental matters be disclosed. See Notice of Adoption of Amendments to Registration and Report Forms to Require Disclosure with Respect to Compliance with Environmental Requirements and Other Matters, Exchange Act Release No. 5386, 1973 SEC LEXIS 2992 (Apr. 20, 1973). This requirement was subsequently incorporated into Regulation S-K. See Adoption of Integrated Disclosure System, Exchange Act Release No. 6383, 1982 WL 90370 (Mar. 3, 1982).

[50] Natural Resources Defense Council, Inc. v. SEC, 606 F.2d 1031, 1049 (D.D.C. 1979) ("recogniz[ing] that environmental concerns to some extent run counter to the SEC's primary mandate of financial protection of investors").

[51] Id.

Sommer Report).[52] The Sommer Report provided the disclosure framework that has been implemented through Regulation S-K.[53] As Commissioner Sommer explained, the Committee concluded that the SEC "should not try to use its powers to compel disclosure concerning, for instance, social or environmental matters, hiring practices, and the like, unless it could be shown that such matters were material to investors."[54]

The SEC has adhered to the approach reflected in the Sommer report in formulating its requirements concerning sustainability disclosure. With limited exceptions, described below, the SEC has refrained from adopting requirements that issuers disclose specific categories of sustainability information. Instead, the SEC has taken the position that sustainability issues may have to be disclosed to the extent to which they relate to an existing disclosure requirement or are necessary to prevent the information disclosed in response to that requirement from being misleading. The benchmark for determining whether disclosure is required is whether the information is material to investors. The SEC has generally taken the position that the materiality standard in the context of the disclosure requirements[55] should be evaluated in terms of the economic or financial impact of the information.[56] As the then-Director of the SEC Division of Corporate Finance explained, "In assessing materiality, the SEC staff takes the view that the reasonable investor

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[52] Report of the Advisory Committee on Corporate Disclosure to the Securities and Exchange Commission, Cmte. Print 95-29, House Cmte. On Interstate and Foreign Commerce, 95th Cong., 1st. Sess (Nov. 3, 1977) available at http://opc-ad-ils/InmagicGenie/DocumentFolder/report%20of%20the%20advisory%20committee%20on%20corporate%20disclosure%20to%20the%20sec%2011011977.pdf.

[53] See Concept Release on Disclosure Effectiveness, supra note __, at 12. The Sommer Report has served as an ongoing guide to the SEC in its evaluation of the appropriate scope and structure of the mandatory disclosure system. See id.

[54] A.A. Sommer Jr., The U.S. Securities and Exchange Commission Disclosure Study, 1 J. Comp. Corp. L.& Sec.Reg.145, 149 (1978).

[55] A related question is the relationship between the concept of materiality in the context of disclosure and the scope of issuer liability for securities fraud. See, e.g., Stratte-McClure v. Morgan Stanley, 776 F.3d 94, 100-104 (2d Cir. 2015).

[56] According to the SEC, a minority of the Advisory Committee that prepared the Sommer Report believed, for example, "that disclosure of social and environmental information is material to an investment decision regardless of its economic impact on the financial performance of the company", in part because that information might reflect on the quality of management. See Concept Release on Disclosure Effectiveness, supra note __ n. 687.

generally focuses on matters that have affected, or will affect, a company's profitability and financial outlook."[57]

In articulating this standard, the SEC has relied on the definition of materiality that was first articulated in the context of proxy fraud in *TSC Industries, Inc. v. Northway, Inc*.[58] The *TSC* Court defined information as material "if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote," meaning that there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[59] The scope of this definition is, itself, unclear in that, even in the context of making an investment decision, investors might reasonably be interested in nonfinancial information or information that is only tangentially related to the issuer's financial performance.[60]

On several occasions, the SEC has recognized that the question of what information is material to investors is an evolving one and modified its approach in order to require more comprehensive disclosure with respect to a specific sustainability issue. One example is the SEC's shift to increasing the required disclosure about executive compensation. After years of taking a restrictive approach, to the point that the SEC regularly allowed corporations to exclude shareholder proposals seeking to address executive pay,[61] the SEC changed its position and imposed extensive mandatory disclosure requirements.[62] The SEC has subsequently modified and expanded the disclosure requirements with respect to

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[57] Memorandum from David B.H. Martin, Director, Division of Corporation Finance, SEC, to Laura Unger, Acting Chair, SEC (May 8, 2001), 2001 SEC No-Act. LEXIS 579, *15.

[58] 426 U.S. 438, 449 (1976).

[59] The Court subsequently concluded that the TSC definition of materiality was applicable in the transactional context as well. See Basic Inc. v. Levinson, 485 U.S. 224 (1988).

[60] An example is investors that screen their investments according to social or ethical criteria. See, e.g., Michael S. Knoll, Ethical Screening in Modern Financial Markets: The Conflicting Claims Underlying Socially Responsible Investment, 57 Bus. Law. 681, 684 (2002).

[61] Jill E. Fisch, From Legitimacy to Logic: Reconstructing Proxy Regulation, 46 Vand. L. Rev. 1129, 1158-59 (1993) (describing SEC policy of permitting exclusion of such proposals as relating to ordinary business operations).

[62] See Executive Compensation Disclosure, Securities Act Release No. 33-6962, 52 SEC Doc. 1961 (Oct. 16, 1992) (imposing extensive disclosure requirements for executive compensation).

executive compensation on several occasions.[63] Notably, even accepting the view that the size and structure of executive compensation is material to investors,[64] some elements of the required disclosure would seem to be a stretch, such as the requirement that issuers disclose all executive perquisites valued at $10,000 or more.[65] The importance of this disclosure is reflected in the SEC's recent enforcement action against Dow Chemical for failing to disclose executive perks adequately.[66]

A second example is climate change disclosure. In 2007, twenty-two institutional investors submitted a petition to the SEC seeking guidance on climate change disclosure.[67] The petition specifically argued that "the risks and opportunities many corporations face in connection with climate change fall squarely within the category of material information that is required to be analyzed and disclosed in many corporate filings."[68] Petitioners argued that, as a result, climate change fell within the existing disclosure requirements of Regulation S-K,[69] but that existing disclosures were inadequate and inconsistent.[70]

Although the SEC took three years to respond to the petition, in 2010, it issued the requested guidance.[71] The SEC's interpretive release advised issuers that they were required to disclose material information about their exposure to risks resulting from climate change, and explained that this requirement was based in several existing provisions of

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[63] See, e.g., Kenneth Rosen, "Who killed Katie Couric?" and other Tales from the World of Executive Compensation Reform, 76 Fordham L. Rev. 2907, 2912 (2008) (describing the SEC's 2006 "significant changes to the existing system of disclosure related to executive and director compensation").

[64] See generally Lucian Bebchuk & Jesse Fried, Pay without Performance: The Unfulfilled Promise of Executive Compensation (2004) (arguing about the importance of the size and structure of executive compensation packages); but see Bevis Longstreth, A Real World Critique of Pay without Performance, 30 Iowa J. Corp. L. 767, 770-71 (2005) (questioning the materiality of executive compensation to investors).

[65] 17 C.F.R. § 229.402 (2011).

[66] See In the Matter of the Dow Chemical Co., Sec. Exch. Act Rel. No. 83581 (July 2, 2018), https://www.sec.gov/litigation/admin/2018/34-83581.pdf (imposing a cease and desist order and a monetary penalty of $1,750,000 against Dow Chemical).

[67] Petition for Interpretive Guidance on Climate Risk Disclosure, No. 4-547, 2 (Sept. 18, 2007), available at http://www.sec.gov/rules/petitions/2007/petn4-547.pdf

[68] Id. at 1.

[69] Id. at 13

[70] Id. at 45.

[71] SEC, Commission Guidance Regarding Disclosures Related to Climate Change, Sec. Act Rel. No. 9106 (Feb. 8, 2010).

Regulation S-K, including the MD&A, the required disclosure of legal proceedings, and the section on risk factors.[72] Following issuance of the release, issuer disclosure of information relating to climate change has increased, although commentators continue to criticize the quality of the disclosure.[73] In addition, the SEC enforcement has been limited.[74]

Climate change disclosure remains limited, in large part, because of the vagueness of the disclosure obligation and the ability of issuers to determine, in their judgment, that issues are not material enough to warrant disclosure. An example of these limitations is reflected in Exxon's 2017 10-K.[75] Item 3 of the 10-K, legal proceedings, contains a brief description of three enforcement actions by the Environmental Protection Agency, the State of North Dakota, and the U.S Dept. of the Treasury.[76] In the notes to the financial statements, Exxon goes on to state that "A variety of claims have been made against ExxonMobil and certain of its consolidated subsidiaries in a number of pending lawsuits."[77] Without providing details of those lawsuits, Exxon concludes that "Based on a consideration of all relevant facts and circumstances, the Corporation does not believe the ultimate outcome of any currently pending lawsuit against ExxonMobil will have a material adverse effect upon the Corporation's operations, financial condition, or financial statements taken as a whole."[78] Notably absent from the 10-K is any discussion of the high profile litigation that

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[72] Because the standard focused on materiality, the guidance left the determination whether information was material and therefore the decision whether to disclose largely in the hands of the issuer's management.
[73] A 2018 Ceres report stated that 51% of companies disclosed climate change information in their annual financial filings in 2017 as opposed to only 42% in 2014. Ceres, TURNING POINT: Corporate Progress on The Ceres Roadmap for Sustainability, Feb. 28, 2018, at 11, https://www.ceres.org/node/2275 The report cautioned, however, that most of this reporting consisted of "boilerplate language [that failed] to provide investors decision-useful information." Id. See also Nina Hart, Note, Moving at a Glacial Pace: What Can State Attorneys General Do About SEC Inattention to Nondisclosure of Financially Material Risks Arising from Climate Change?, 40 Colum. J. Envtl. L. 99, 114 (2015) (explaining that "companies are treating climate change risks with brevity and superficiality").
[74] Robert Repetto, It's Time the SEC Enforced its Climate Disclosure Rules, IISD, Mar. 23, 2016, https://www.iisd.org/blog/it-s-time-sec-enforced-its-climate-disclosure-rules
[75] EXXON MOBIL CORPORATION 2017 Form 10-K dated Feb. 28, 2018, avail. at https://www.sec.gov/Archives/edgar/data/34088/000003408818000015/xom10k2017.htm
[76] Id. at 26.
[77] Id. at 86.
[78] Id.

several states have filed against the issuer alleging that Exxon's use of fossil fuels poses "grave risks" to the planet.[79] The SEC recently closed a related investigation about the manner in which Exxon disclosed the potential impact on the value of its assets without penalizing Exxon.[80]

The SEC has also adopted rules mandating disclosure with respect to specific sustainability issues. In response to a worldwide focus on board diversity,[81] the SEC issued a rule in 2009 requiring issuers to disclose "whether, and if so how, a nominating committee considers diversity in identifying nominees for [the board of directors]."[82] Former SEC Commissioner Mary Jo White observed that the SEC's disclosure requirement on board diversity has had limited effect, explaining that "Companies' disclosures on board diversity in reporting under our current requirements have generally been vague and have changed little since the rule was adopted."[83]

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[79] See, e.g., Bob Van Voris, Exxon Sues the Suers in Fierce Climate-Change Case, Bloomberg Businessweek, Feb. 13, 2018, https://www.bloomberg.com/news/articles/2018-02-13/exxon-sues-the-suers-in-fierce-bid-to-defeat-climate-lawsuits (describing claims by New York City and eight California cities); Ephrat Livni, Big Oil says government climate change lawsuits are a "conspiracy", Quartz, Jan. 12, 2018, https://qz.com/1177685/exxonmobile-says-government-climate-change-lawsuits-are-a-conspiracy-against-the-company/ (describing the allegations and Exxon's filing alleging that the climate change lawsuits are a "conspiracy").

[80] Dave Michaels & Bradley Olson, SEC Drops Probe of Exxon's Climate-Change Disclosures, Wall St. J. Aug. 3, 2018, https://www.wsj.com/articles/sec-drops-probe-of-exxons-climate-change-disclosures-1533317730?mod=djemalertNEWS.

[81] This focus resulting in many countries' adopting required gender quota for corporate boards. See, e.g., Aaron A. Dhir, Challenging Boardroom Homogeneity: Corporate Law, Governance, and Diversity 3 (2015) (discussing gender quota laws in Norway, Sweden and Finland); Darren Rosenblum & Daria Roithmayr, More than a Woman: Insights into Corporate Governance After the French Sex Quota, 48 Ind. L. Rev. 889 (2015) (analyzing impact of board diversity quota law in France).

[82] Proxy Disclosure Enhancements, Securities Act Release No. 33-9089, 74 Fed. Reg. 68,334 (proposed Dec. 16, 2009) (to be codified at C.F.R. pts. 229 et al.). The rule goes on to require that, if the nominating committee "has a policy with regard to the consideration of diversity in identifying director nominees, disclosure would be required of how this policy is implemented."

[83] Chair Mary Jo White, Keynote Address, 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, 2016, https://www.sec.gov/news/speech/chair-white-icgn-speech.html

The Dodd-Frank Act[84] required the SEC to adopt disclosure requirements with respect to two sustainability issues – conflict minerals and resource extraction[85] –and the SEC adopted rules in accordance with this mandate,[86] although a subsequent Congress effectively eliminated both rules.[87] Notably, at the time Dodd-Frank was enacted, the SEC objected to the mandates, claiming that the required disclosures fell outside the agency's core mission and were addressed to social policy rather than informing investors.[88]

Commentators have called upon the SEC to do more to formalize sustainability disclosure.[89] The issue has been on the SEC's rulemaking

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[84] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010)

[85] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376, § 1502 (2010) (codified as amended in scattered sections of 12, 15, 22, and 26 U.S.C.); § 1504 ("Disclosure of Payments by Resource Extraction Issuers"). See also 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, 331, 339 (2011) (describing and criticizing the attempts of the SEC to achieve public policy objectives through information disclosure).

[86] See Conflict Minerals, Securities Exchange Act of 1934, Release No. 34-67716, 2012 WL 3611799 (Aug. 22, 2012) and Disclosure of Payments by Resource Extraction Issuers Final Rule, Exchange Act Release No. 34-67717 (Aug. 22, 2012), available at http://www.sec.gov/rules/final/2012/34-67717.pdf.

[87] In February 2017, Congress eliminated the resource extraction rule by voting to disapprove the rule under the Congressional Review Act. See Nick Graber, et al., Congress Rolls Back SEC Resource Extraction Payments Rule, Cleary M&A and Corporate Governance Watch, Feb. 6, 2017, https://www.clearymawatch.com/2017/02/congress-rolls-back-sec-resource-extraction-payments-rule/ (reporting on the action and explaining that a rule disapproved by Congress under the CRA "is treated as though it had never taken effect."). Later in 2017 Congress suspended funding to enforce the conflict minerals rule. See Marc Butler, Conflict Minerals Reporting Requirements Continue to Face Uncertain Future, Intelligize, Oct. 12, 2017, https://www.intelligize.com/conflict-mineral-reporting-requirements-continue-face-uncertain-future/ (reporting on congressional action and citing SEC Chair Jay Clayton's public statement supporting reduction of the disclosure requirements).

[88] See, e.g., Aruna Viswanatham, SEC chair chastises Congress over new disclosure rules, Reuters, Oct. 3, 2013, https://www.reuters.com/article/us-sec-disclosures/sec-chair-chastises-congress-over-new-disclosure-rules-idUSBRE99215Q20131003 (reporting comments by then-SEC Chair Mary Jo White).

[89] Letter from AFL-CIO, *supra* note __ ("given the clear and growing demand from investors for environmental, social and governance . . . information, the Commission must begin requiring ESG related line-item disclosures as well as a process to incorporate emerging ESG metrics into disclosure in the future.").

agenda for the past several years. In April 2016, as part of its Disclosure Effectiveness Initiative,[90] the Securities & Exchange Commission (SEC) issued a Concept Release on Disclosure Effectiveness.[91] The 341-page release identified a variety of potential reforms to the disclosure system. As part of the release, the SEC invited comment on the extent to which SEC rules should mandate sustainability disclosure. The release specifically asked for comment on the importance of sustainability disclosure to shareholder investment and voting decisions.[92] The SEC received tens of thousands of comments specifically addressed to the issue of sustainability disclosure.[93] A substantial number of investors requested "the SEC to require annual, uniform sustainability reporting from public companies as part of the overhaul of the agency's disclosure regime."[94] To date, however, the SEC has not acted on that request.

Investors have attempted to obtain more extensive disclosure as well as to require an issuer to address particular topics of concern on a company-specific basis. One mechanism for doing so is through the SEC's shareholder proposal rule, rule 14a-8.[95] Shareholders have used

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[90] The JOBS Act required the SEC to conduct "a review of Regulation S-K to determine how such requirements can be updated to modernize and simplify the registration process." SEC Staff, Report on Review of Disclosure Requirements in Regulation S-K, Dec. 2013, https://www.sec.gov/news/studies/2013/reg-sk-disclosure-requirements-review.pdf, at 1. In response, the SEC staff issued a report in December 2013 that recommended a "comprehensive" review of disclosure requirements for all public companies. Id. at 114. The SEC created a Disclosure Effectiveness Initiative to undertake this comprehensive review. Robert Herz, Disclosure effectiveness gains traction and momentum, Compliance Week, Oct. 12, 2016, https://www.complianceweek.com/blogs/robert-herz/disclosure-effectiveness-gains-traction-and-momentum#.WnugnsJy63g

[91] See Concept Release on Disclosure Effectiveness, supra note **Error! Bookmark not defined.**.

[92] See id. at 204 ("we seek feedback on which, if any, sustainability and public policy disclosures are important to an understanding of a registrant's business and financial condition and whether there are other considerations that make these disclosures important to investment and voting decisions").

[93] See, e.g., Gellasch, supra note _ at 10 (reporting that, as of August 2016, the SEC had received 26,512 comments in response to the Concept Release).

[94] Odom, supra note __.

[95] 17 C.F.R. § 240.14a-8 (2018). The shareholder proposal rule enables shareholders who meet various ownership and procedural requirements to introduce a proposal on which shareholders can vote at an issuer's annual meeting and to have that proposal included in the issuer's proxy statement. The rule contains a variety of bases upon

rule 14a-8 to introduce proposals addressed to social policy concerns for many years, and these proposals have met with mixed success.[96] They have also been controversial, with critics arguing that the proposals were often brought by special interest groups with limited economic stakes and advanced views that were tangential to or even contrary to the economic interests of shareholders generally.[97]

Two developments have caused shareholder proposals to play a more meaningful role in sustainability disclosure. First, proponents have modified the form of their proposals to concentrate on seeking disclosure and oversight of sustainability considerations rather than attempting to cause the company to adopt specific sustainability policies. Second, the proposals are receiving increasing support from shareholders generally and from large mainstream institutional investors in particular.[98] A recent conference board report observes that almost half the shareholder proposals brought to a vote during the 2017 proxy season concerned ESG issues and that, although most receive limited support, the number of proposals that received the support of a majority of the votes cast continues to increase.[99]

A recent example is shareholder proposals requesting increased disclosure about the potential effects of climate change. During the 2017 proxy season, a majority of shareholders at three major companies -- Occidental Petroleum, PPL and ExxonMobil -- approved these

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which the issuer can seek to have the proposal excluded. See generally Fisch, supra note __, 46 Vand. L. Rev. at 1146-47 (explaining the shareholder proposal rule).

[96] See generally Scott Hirst, Social Responsibility Resolutions. __ J. Corp. L. __ (forthcoming 2017), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2773367

[97] Classic examples were the shareholder proposal in Lovenheim v. Iroquois Brands, Ltd., 618 F. Supp. 554 (D.D.C. 1985), asking Iroquois to stop force feeding the geese that were used to make pate de foie gras, and the proposal in Philip Morris Companies, SEC No-Action Letter, Feb. 13, 1990, 1990 SEC No-Act. LEXIS 335, seeking to have Philip Morris stop conducting any business in tobacco or tobacco products.

[98] See, e.g. Thomas Singer, Environmental and Social Proposals in the 2017 Proxy Season, Harv. L. Sch. Forum on Corp. Gov. & Fin. Reg., Oct. 26, 2017, https://corpgov.law.harvard.edu/2017/10/26/environmental-and-social-proposals-in-the-2017-proxy-season/ (reporting that "Large institutional investors, such as BlackRock and Vanguard, are beginning to exert pressure on companies by supporting E&S proposals that call for greater disclosure of issues they deem material to shareholder value").

[99] Id.

shareholder proposals.[100] Among the shareholders voting in favor of the proposal were institutional heavyweights BlackRock and Vanguard, both of which hold substantial stakes in most large public companies.[101] The New York City Common Retirement Fund, which co-sponsored the proposal at Exxon, explained that the proposal was motivated by economic interests. "Climate change is one of the greatest long-term risks we face in our portfolio and has direct impact on the core business of ExxonMobil."[102] To the extent shareholders continue to support proposals advocating increased sustainability disclosure, issuers will face pressure to provide greater disclosure even in the absence of regulation.[103]

C. Sustainability Disclosure Requirements Beyond the Federal Securities Laws

Federal securities laws are not the only source of sustainability disclosure requirements; some mandatory sustainability disclosure requirements can be found in other areas of the law such as environmental

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[100] Cydney Posner, Are Shareholder Proposals on Climate Change Becoming a Thing?, Harv. L. School Forum on Corp. Gov. & Fin. Reg., June 21, 2017, https://corpgov.law.harvard.edu/2017/06/21/are-shareholder-proposals-on-climate-change-becoming-a-thing/.

[101] Id. See Jan Fichtner, Eelke M. Heemskerk & Javier Garcia-Bernardo, Hidden power of the Big Three? Passive index funds, re-concentration of corporate ownership, and new financial risk. 19 Bus. & Pol. 298 (2017) (terming BlackRock, Vanguard and State Street the "big three" and explaining that they dominate the passive fund industry); Steven Mufson, Financial firms lead shareholder rebellion against ExxonMobil climate change policies, Wash. Post, May 31, 2017, https://www.washingtonpost.com/news/energy-environment/wp/2017/05/31/exxonmobil-is-trying-to-fend-off-a-shareholder-rebellion-over-climate-change/?utm_term=.9579fd3049f6 (reporting that BlackRock and Vanguard owned 13% of ExxonMobil).

[102] Id.

[103] See, e.g. Ed Crooks, ExxonMobil bows to shareholder pressure on climate reporting, Fin. Times, Dec. 11, 2017, https://www.ft.com/content/8bd1f73a-dedf-11e7-a8a4-0a1e63a52f9c (reporting Exxon's announcement that, in response to investor demands, it will "start publishing reports on the possible impact of climate policies on its business").

law,[104] employment law[105] and consumer law.[106] In addition, some states impose additional sustainability disclosure requirements.[107] At best, however, these disclosure requirements operate in a piecemeal manner and do not present a complete picture of the sustainability issues that potentially have a material impact on an issuer's operations.

Outside the United States, mandatory sustainability disclosures are more common. A number of jurisdictions have mandated disclosure requirements.[108] Although a comprehensive examination of those

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[104] See, e.g., David W. Case, Corporate Environmental Reporting as Information Regulation: A Law and Economics Perspective, 76 U. Colo. L. Rev. 379, 384 (2005) (describing required environmental disclosure).

[105] See, e.g., Cynthia Estlund, Just the Facts: The Case for Workplace Transparency, 63 Stan. L. Rev. 351, 356 (2011) (discussing use of disclosure requirements in employment law and advocating for expanding such requirements).

[106] See, e.g., Jonathan H. Adler, Compelled Commercial Speech and the Consumer "Right to Know," 58 Ariz. L. Rev. 421, 424 (2016) (describing expanding universe of disclosure requirements based on a "consumer right to know,")

[107] For example, the California Transparency in Supply Chains Act of 2010 requires any retailer that does business in the state and has annual worldwide gross receipts exceeding $100 million to make specific disclosures on its website about efforts it makes to "eradicate slavery and human trafficking from its direct supply chain." https://oag.ca.gov/sites/all/files/agweb/pdfs/sb657/resource-guide.pdf at i. The Act requires disclosure on five topics – verification, audits, certification, internal accountability and training. Id. at 4. Even companies that take no actions relating to these categories must disclose that fact. Id. The statute provides no private right of action and is enforceable exclusively by the California Attorney General. Id. Plaintiffs' lawyers have also been using class action to attempt to create broader sustainability disclosure obligations based on state consumer protection statutes or claims of false advertising. For example, in Nestle, plaintiffs sought to impose an obligation on Nestle to disclose that some of the seafood used in its cat food was likely "produced by forced labor." Barber v. Nestlé USA, Inc., 154 F. Supp. 3d 954, 957 (C.D. Cal. 2015). In Hodsdon v. Mars, Inc., 162 F. Supp. 3d 1016 (N.D. Cal. 2016), plaintiff sought to impose an obligation on Mars to disclose on its chocolate bars that they contained cocoa beans that were likely picked under conditions of child or slave labor. In Hall v. SeaWorld Entm't, Inc., 2015 U.S. Dist. LEXIS 174294 (S.D. Cal. 2015), plaintiffs sought to impose an affirmative obligation on Sea World to disclose facts concerning the health and welfare of the killer whales that it held in captivity. To date, these lawsuits have largely been unsuccessful. For example, the court in Sea World reasoned that to apply plaintiffs' theory would expose companies to limitless liability. Id. at *26.

[108] See, e.g., Galit A. Sarfaty, Regulating Through Numbers: A Case Study of Corporate Sustainability Reporting, 53 Va. J. Int'l L. 575, 598 (2013) (describing mandatory disclosure requirements in a variety of European countries); Initiative for Responsible Investment, Corporate Social Responsibility Disclosure Efforts by

requirements is beyond the scope of this Article,[109] four project partners have been collecting and reporting data on global sustainability reporting requirements since 2006. In their 2016 report, they provide evidence of a trend toward mandatory disclosure requirements as well as a detailed analysis of mandatory and voluntary requirements in 71 countries.[110] Although the report explains that many of the reporting requirements are based in area such as environmental law rather than investor-oriented entities, stock exchanges and financial regulators are the source of almost a third of the reporting instruments.[111] Notably, many reporting requirements imposed by financial markets or regulators take the form of an obligation to comply or explain.[112]

National Governments and Stock Exchanges (March 12, 2015), available at http://hausercenter.org/iri/wp-content/uploads/2011/08/CR-3-12-15.pdf (reporting that 23 countries have adopted legislation requiring public companies to disclose environmental or social information).

[109] India's approach to CSR is one of the most interesting. In 2013, India adopted a requirement that its firms develop a board-centered CSR policy and spend at least two percent of their profits on CSR activities. Afra Afsharipour, Corporate Social Responsibility and the Corporate Board: Assessing the Indian Experiment, in Globalisation of Corporate Social Responsibility and its Impact on Corporate Governance, at 96 (Springer 2018) (providing a detailed description and analysis of the Indian approach).

[110] U.N. Environment Programme et al., Carrots and Sticks - Global trends in sustainability reporting regulation and policy 9 (2016), https://www.globalreporting.org/resourcelibrary/Carrots%20and%20Sticks-2016.pdf (summarizing growth in sustainability reporting instruments and observing that "Mandatory instruments dominate").

[111] Id. at 14. The stock exchange reporting requirements are particularly prevalent in emerging markets. Id. at 15. See also Initiative for Responsible Investment, Corporate Social Responsibility Disclosure Efforts by National Governments and Stock Exchanges (March 12, 2015), available at http://hausercenter.org/iri/wp-content/uploads/2011/08/CR-3-12-15.pdf (reporting that seven stock exchanges, including the London Stock Exchange, require social or environmental disclosure as part of their listing requirements); KPMG, Business Responsibility Reporting, July 2017, https://assets.kpmg.com/content/dam/kpmg/in/pdf/2017/07/Business-Responsibility-Reporting.pdf (reporting on implementation of SEBI's requirement that the top 100 listed companies in India include reporting on sustainability as part of their annual financial reports).

[112] Id. at 13. See also Jerry K C Koh & Victoria Leong, The Rise of the Sustainability Reporting Megatrend: A Corporate Governance Perspective18-3 BLI 233, Sept. 2017 (describing Singapore Stock Exchange's 2016 amendment to its listing manual to require issuers to produce sustainability reports on a 'comply or explain' basis); Virginia Harper Ho, "Comply or Explain" and the Future of Nonfinancial Reporting, 21 Lewis

The EU's adoption of a directive mandating sustainability disclosure is perhaps the most notable development in this regard. In 2014, the European Union adopted Directive 2014/95/EU[113] which requires large companies across the European Union, starting in 2018, to publish information on their policies with respect to environmental protection, social responsibility, human rights, anti-corruption and board diversity.[114] The information is expressly termed a "non-financial statement," and the Directive does not appear to contemplate that the disclose will be integrated with an issuer's financial reporting.[115]

In June 2017, the EU published its guidelines to assist companies in complying with the directive.[116] The guidelines are not mandatory, but they make it clear that the focus of the directive differs importantly from federal securities disclosure in that it is explicitly stakeholder oriented rather than shareholder oriented.[117] By December 2017, all of the EU member states had implemented the directive through national legislation, although the form of that legislation varies "according to local conditions."[118] Although the EU directive is an important step and "reflects an emerging global trend toward mandatory reporting,"[119]

& Clark L. Rev. 317 (2017) (describing comply or explain approach and advocating its adoption in the United States for sustainability reporting).

[113] DIRECTIVE 2014/95/EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 22 October 2014, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0095

[114] European Commission, Non-financial reporting, https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en#how-to-report

[115] DIRECTIVE 2014/95/EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 22 October 2014, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0095

[116] COMMUNICATION FROM THE COMMISSION, Guidelines on non-financial reporting (methodology for reporting non-financial information) (2017/C 215/01), http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52017XC0705(01)

[117] See id. ("Companies are expected to consider the information needs of all relevant stakeholders").

[118] Global Reporting Initiative, Innovative implementation of EU Directive on Non-Financial Reporting, Feb. 7, 2018, https://www.globalreporting.org/information/news-and-press-center/Pages/EU-Directive-on-Non-Financial-Reporting.aspx.

[119] Constance Z. Wagner, Evolving Norms of Corporate Social Responsibility: Lessons Learned from the European Union Directive On Non-Financial Reporting. Transactions, 19 Tenn. J. Bus. L. 619 (2018).

some commentators have argued that its approach is likely to have limited effectiveness in improving disclosure quality.[120]

D. Voluntary Sustainability Disclosure

In the absence of a uniform and universal mandatory regime, market forces are continuing to fuel the growth of voluntary sustainability disclosure.[121] Most sustainability information is not disclosed in issuer financial or securities filings but in stand-alone sustainability reports. The Governance & Accountability Institute reported that, in 2016, 82% of S&P 500 companies published a sustainability or corporate responsibility report.[122] These reports take a variety of forms, cover a range of different topics and vary in length. It is increasingly common for sustainability reports to exceed a hundred pages in length, and some issuers produce multiple sustainability reports addressing different topics. For example, in 2017 Apple produced both an environmental responsibility report and[123] a supplier responsibility report,[124] as well as providing additional website describing its initiatives regarding inclusion and diversity.[125]

The dominance of voluntary disclosure and the variety of sources of that disclosure have contributed to the growth of global standard setters that seek to promulgate disclosure standards or guidelines or to rate issuers on the quality of their disclosure or sustainability practices. The number of standard setters, data repositories and ratings organizations is huge and continues to grow, [126] and a description of all the important and relevant

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[120] Id.
[121] Walter, supra note __.
[122] Governance and Accountability Institute, Flash Report: 82% of the S&P 500 Companies Published Corporate Sustainability Reports in 2016, May 31, 2017, https://3blmedia.com/News/Flash-Report-82-SP-500-Companies-Published-Corporate-Sustainability-Reports-2016
[123] Apple, Environmental Responsibility Report, 2017 Progress Report, Covering Fiscal Year 2016, https://images.apple.com/environment/pdf/Apple_Environmental_Responsibility_Report_2017.pdf
[124] Apple, Supplier Responsibility, 2017 Progress Report, https://images.apple.com/supplier-responsibility/pdf/Apple-Progress-Report-2017.pdf
[125] Apple, Inclusion and Diversity, https://www.apple.com/diversity/
[126] See, e.g., KMPG et al., Carrots Sticks Global trends in sustainability reporting regulation and policy, 2016 edition, at 10, https://www.globalreporting.org/resourcelibrary/Carrots%20and%20Sticks-2016.pdf

institutions and standards is beyond the scope of this article.[127] The following discussion highlights a few of most prominent examples for illustrative purposes.

One way in which private organizations contribute to the quality and usability of sustainability disclosure is by promulgating disclosure standards. The Global Reporting Initiative (GRI), an international organization that was founded 20 years ago as a U.S. non-profit, is one of the best known private standard-setting organizations. The GRI's standards for sustainability reporting are used, in whole or in part, by companies around the world.[128] According to a 2017 KMPG survey, 73% of companies worldwide that report sustainability information use the GRI standards.[129] The GRI also maintains a free searchable database of more than 46,000 individual issuer sustainability reports.[130]

Another well-known standard-setting organization is the Sustainability Accounting Standards Board (SASB).[131] In contrast to the GRI, SASB's focus has been to develop disclosure standards that are incorporated into SEC filings rather than separate sustainability reports. Toward that end, SASB has developed provisional industry-specific disclosure standards for 79 industries. SASB takes the position that its standards either are or should be incorporated into issuer financial reporting under the current legal requirements. According to SASB, "The standards focus on known trends and uncertainties that are reasonably likely to affect the financial condition or operating performance of a

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(reporting that 2016 research identified 383 sustainability reporting instruments in 64 countries).

[127] For a listing and brief description of many key institutions see KMPG et al., supra note __ appendix 1.

[128] Global Strategic Alliances, GRI Standards, https://www.globalreporting.org/standards. In 2010, the GRI and the UN Global Compact signed an accord in which the GRI agreed to integrate the UN Global Compact's reporting framework into its sustainability reporting guidelines. GRI, United Nations Global Compact, https://www.globalreporting.org/information/about-gri/alliances-and-synergies/Pages/United-Nations-Global-Compact.aspx

[129] KMPG, The Road Ahead, The KPMG Survey of Corporate Responsibility Reporting 2017, https://assets.kpmg.com/content/dam/kpmg/xx/pdf/2017/10/kpmg-survey-of-corporate-responsibility-reporting-2017.pdf

[130] GRI, Sustainability Disclosure Database, http://database.globalreporting.org/

[131] About the SASB, SASB website, https://www.sasb.org/about-the-sasb/

company and therefore would be considered material under Regulation S-K."[132]

The volume of sustainability information disclosed in accordance with these and other standards complicates the task of evaluating a particular issuer's sustainability practices. To assist in this endeavor, a number of organizations offer sustainability rankings or ratings.[133] One of the best-known indices is the Dow Jones Sustainability Index.[134] Notably, the DJSI is not based on public disclosures, instead, RobecoSam collects the information used in the index directly from 3400 invited issuers worldwide using a proprietary questionnaire, called the Corporate Sustainability Assessment.[135] The data is based on "industry-specific questions focusing on economic, environmental and social factors that are relevant to the companies' success, but that are under-researched in conventional financial analysis."[136] The ratings of top companies are released annually, and the DJSI is billed as the "gold star for corporate sustainability."[137]

Another rating organization, the CDP (formerly the Carbon Disclosure Project), obtains voluntary disclosure on environmental issues directly from issuers, which it then uses to produce a variety of research.[138] According to the CDP, "Reporting companies now represent 56% of global market capitalization."[139] The CDP also scores companies on their

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[132] Id.

[133] See, e.g., SustainAbility, Rate the Raters, Understanding the universe of corporate sustainability rankings, http://sustainability.com/rate-the-raters/ ("There are a dizzying number and variety of external ratings, rankings, indices and awards that seek to measure corporate sustainability performance.") The Global Initiative for Sustainability Ratings, for example, includes 143 ratings, rankings and indexes in its database. See Global Initiative for Sustainability Ratings, GISR Ratings Directory, http://ratesustainability.org/hub/index.php/search?filter=index

[134] Robecosam, About Us, http://www.sustainability-indices.com/

[135] Robecosam, The Corporate Sustainability Assessment at a glance, http://www.robecosam.com/en/sustainability-insights/about-sustainability/corporate-sustainability-assessment/index.jsp

[136] Id.

[137] Top Companies Listed on Dow Jones Sustainability Index, Security Newswire, Sept. 18, 2017, https://www.securitymagazine.com/articles/88327-top-companies-listed-on-dow-jones-sustainability-index

[138] CDP, About Us, https://www.cdp.net/en/info/about-us

[139] CDP, the A List, https://www.cdp.net/en/scores-2017

transparency and environmental action, based on the information they supply.[140]

A third rating organization, run by Newsweek, publishes its own annual sustainability ranking of large issuers, the Newsweek Green Rankings. The Newsweek methodology is designed to be replicable by a third party. Newsweek discloses the precise metrics it uses, and, unlike the DJSI and the CDP, its rankings are based on publicly-available data.[141]

II. Limitations of Existing Sustainability Disclosure

The structure of the existing voluntary disclosure framework is problematic for several reasons.[142] This section highlights some of the key problems with the existing regime, thereby demonstrating why, despite the growth in the volume of sustainability disclosure, private ordering has not been successful in producing sustainability disclosures that meet investors' needs. As Trillium Asset Management explained to the SEC, "While voluntary reporting frameworks are better than nothing at providing ESG information at participating companies they do not provide the consistency, accuracy and completeness that is inherent in securities filings."[143]

Existing sustainability disclosures are fragmented, of inconsistent quality, and, in many cases, unreliable.[144] As this section will explain, issuers have incentives to focus on the positive aspects of their business practices and to omit unfavorable information. A lack of standardization makes it difficult for investors to compare information across issuers. And regulatory oversight of sustainability disclosure is extremely limited.

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[140] Id.

[141] Carlos Barria, Newsweek Green Rankings 2017 Methodology, Newsweek, Dec. 7, 2017, http://www.newsweek.com/newsweek-green-rankings-2017-methodology-739761

[142] See generally Virginia E. Harper Ho, Nonfinancial Risk Disclosure & the Costs of Private Ordering, __ Am. Bus. L. J. __ (forthcoming 2018), https://ssrn.com/abstract=3108363 (arguing that "the current state of sustainability disclosure" as implemented through private ordering "is ineffective for financial analysis" and calling for an SEC-mandated disclosure requirement).

[143] Letter from Trillium Asset Management, July 21, 2016, available at https://www.sec.gov/comments/s7-06-l6ts706 l 6-276.pdf

[144] See, e.g., Klaus Dingwerth & Margot Eichinger, Tamed Transparency: How Information Disclosure under the Global Reporting Initiative fails to Empower, 10:3 GLOBAL ENV. POL. 74, 88 (2010) (explaining that the information is "of limited practical use and "unbalanced.").

The problems stem, in part from the voluntary nature of the current regime. Because disclosure is voluntary, issuers can choose which issues to address as well as choosing the applicable reporting metrics.[145] As a result, issuers overwhelmingly disclose information about the areas in which their business practices are highly sustainable.[146] In many cases issuers simply omit discussion of the issues on which their practices fall short and choose not include reporting metrics that would flag shortcomings.[147] This makes their reports a poor tool for accurately assessing the extent to which sustainability issues represent material business risks.

The practice of emphasizing positive information and omitting negative information to make an issuer's business practices appear to more sustainable than they actually are is known as greenwashing.[148] Perhaps the most prominent recent example of greenwashing was Volkswagen which was praised for years as a "global leader in "corporate social responsibility," based largely on its self-disclosed sustainable business

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[145] See, e.g., Markus J. Milne, Amanda Ball & Rob Gray, Wither Ecology? The Triple Bottom Line, the Global Reporting Initiative, and the Institutionalization of Corporate Sustainability Reporting,188 (1) J. BUS. ETHICS 1 (2013) (reporting that "the quality—and especially the completeness—of many triple bottom line reports are not high" and that issuers "cherry pick elements of news, and generally ignore the major social issues that arise from corporate activity").

[146] See, e.g., Acuris, A question of quality: How to improve SEC disclosure, Dec. 21, 2016 at 11, https://www.acuris.com/question-quality-how-improve-sec-disclosure ("But sometimes they are selective and basically say, "Here are all the nice things we did last year" – community activities, reducing their carbon footprint, and various other things. They don't necessarily focus on the issues that really matter in the context of their industry.")

[147] For example, Volkswagen's sustainability reports concentrated heavily on its efforts to reduce CO2 emissions and included little discussion of NOx emissions. NOx was the main pollutant that Volkswagen cars released as a result of the emissions testing modifications. See, e.g. Akmaral Zhakypova, Dissecting Corporate Sustainability Reporting: VW Emissions Scandal case, unpublished manuscript dated Spring 2016 at 22, avail. at https://nature.berkeley.edu/classes/es196/projects/2016final/ZhakypovaA_2016.pdf (reporting on relative discussion of CO2 and NOx in Volkswagens 2013 and 2014 sustainability reports).

[148] See, e.g., Bryant Cannon, Student Article, A Plea for Efficiency: The Voluntary Environmental Obligations of International Corporations and the Benefits of Information Standardization, 19 N.Y.U. Envtl. L.J. 454, 478 (2012) (explaining that "corporate greenwashing allows those companies that falsely, yet effectively, portray an image of environmental responsibility to obtain undeserved benefits").

practices. In 2015, Volkswagen was named the world's most sustainable car company by the Dow Jones Sustainability Index.[149] Just one week later, U.S. regulators publicly announced the emissions scandal.[150]

Voluntary disclosure also tends to be vague, general or boilerplate rather than providing investors with the type of specific information that enables them to compare the sustainability practices of different companies. The corporate desire for generic disclosure is rational – to the extent that issuers disclose specifies, investors can more readily identify outliers and pressure them to change their policies.

Even when voluntary disclosure is relatively balanced and comprehensive, it has other limitations. The absence of standardized disclosure requirements may lead issuers to disclose such a high quantity of information that it results in information overload.[151] Critics have argued that existing securities disclosure requirements are excessive and flooding the markets with so much information that investors cannot use the information intelligently,[152] but voluntary sustainability disclosures are, in many cases, far more extensive than mandated financial disclosures.

Because no centralized regulator or authority is responsible for establishing disclosure standards, even within a single jurisdiction, sustainability disclosure is fragmented rather than standardized. Issuers

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[149] See Volkswagen U.S. Media Site, Volkswagen is world's most sustainable automotive group, Sept. 11, 2015, https://media.vw.com/en-us/releases/566 (announcing that "The Volkswagen Group has again been listed as the most sustainable automaker in the world's leading sustainability ranking"). See also Erika Fry, VW fooled everyone. Was it the only one?, Fortune, Oct. 26, 2015, http://fortune.com/2015/10/26/emissions-testing-software-cheat-volkswagen-scandal/ ("In early September the Dow Jones Sustainability Index (DJSI) crowned Volkswagen (vlkay, -0.58%) the world's most sustainable car company").

[150] U.S. Environmental Protection Agency, Notice of Violation, Sept. 18, 2015, https://www.epa.gov/sites/production/files/2015-10/documents/vw-nov-caa-09-18-15.pdf. Volkswagen subsequently agreed to a $15.3 billion settlement with U.S. regulators. See Margaret Cronin Fisk, Kartikay Mehrotra, Alan Katz & Jeff Plungis Bloomberg, Volkswagen Agrees to $15 Billion Diesel-Cheating Settlement June 28, 2016, https://www.bloomberg.com/news/articles/2016-06-28/volkswagen-to-pay-14-7-billion-to-settle-u-s-emissions-claims

[151] One commentator describes this practice, in the context of sustainability disclosures to consumers, as "information flooding" and warns that it enables issuers to bury bad facts as well as omitting them. Karen Bradshaw Schulz, Information Flooding, 48 Ind. L. Rev. 755, 756 (2015).

[152] Troy A. Paredes, Blinded by the Light: Information Overload and its Consequences for Securities Regulation, 81 Wash. U. L.Q. 417, 417, 443 (2003).

can choose which metrics or standards to use for their disclosures and can choose among those standards which issues to report on. The absence of standardization impedes the market's ability to compare issuer sustainability practices, even among similar companies.[153] As one study reports, 80% of investors are dissatisfied with the "comparability of sustainability reporting between companies in the same industry."[154] Another study reports that only 8% of investors polled believe that "existing ESG disclosures allow for comparison across companies/peers."[155]

Although third party ratings and rankings attempt to address the comparability issue, they suffer from some of the same defects,[156] including limitations in coverage, differences in the information used, and heavy reliance on issuer-supplied information.[157] In addition, the rating agencies do not appear to produce consistent results, presumably due in part to their differences in methodology. For example, one study compared the DJSI, the CDP ratings and the Newsweek Green rankings in 2015 and found that only 12% of companies appeared on all three lists.[158] "A [Wall Street] Journal analysis of four leading ESG ratings providers found that

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[153] Comparability of disclosures is a critical attribute for investors to use those disclosures effectively. Cf. Letter from Amy C. McGarrity, CIO, Colorado PERA to Jay Clayton & Russell G. Golden dated Mar. 16, 2018 (expressing concern over lack of comparability among non-GAAP measures of financial performance and calling for the SEC to undertake a project to provide greater standardization).

[154] Verdantix, The Future of Sustainability Disclosures – 2015, White paper dated Sept. 14, 2015, http://research.verdantix.com/index.cfm/papers/Products.Details/product_id/827/the-future-of-sus%ADtainability-disclosures/-19.

[155] Subramanian, supra note __ at 6.

[156] Because third party ratings appear to be independent, they can be highly influential, making their lack of reliability or inconsistency particularly problematic. The influence of credit rating agencies prior to the 2008 financial crisis offers a warning. See, e.g., Frank Partnoy, What's Still Wrong with Credit Ratings?, 92 Wash. L. Rev. 1407 (2017) (discussing the contribution of credit ratings to the financial crisis).

[157] As noted above, Volkswagen successfully concealed the emissions generated by its cars, not just from regulators and consumers, but also from the DJSI, which named Volkswagen the world's most sustainable car company in 2015. See note __ supra and accompanying text.

[158] Beixin (Betsy) Lin, et al., Are Sustainability Rankings Consistent Across Ratings Agencies?, CPA Journal, July 2017, https://www.cpajournal.com/2017/07/19/sustainability-rankings-consistent-across-ratings-agencies/.

they come to completely different conclusions about what makes a company a 'sustainable' investment."[159]

Finally, sustainability reporting is not reliable. As noted above, most sustainability reporting occurs in stand-alone sustainability reports rather than being integrated with an issuer's securities filings. These reports are often prepared by public relations or marketing personnel. As a result, the disclosures contained in those reports do not meet the standards applied to securities filings. They are not routinely prepared or reviewed by disclosure lawyers, they are typically not reviewed or certified by the CEO or the board of directors, and they are not subject to the oversight of third-party auditors. Finally, unlike securities filings, sustainability reports are not filed with and reviewed by the SEC. Although in theory sustainability reports are public disclosures, it is unclear whether greenwashing or other false disclosures in sustainability reports would subject an issuer to liability for federal securities fraud.[160] As a result, issuers may take less care in preparing sustainability disclosures.

These limitations in the existing framework for sustainability disclosure are behind the investor demands for an SEC rule that mandates sustainability reporting. To the extent that investors care about sustainability issues, to the extent that they believe sustainability considerations are relevant to economic performance, or to the extent to which they wish to explore the question, they need quality information. Significantly, this information is important for an evaluation of issues such as board oversight, risk management and business practices regardless of the extent to which an investor believes that issuers should

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[159] Jon Sindreu & Sarah Kent, Why It's So Hard to Be an 'Ethical' Investor, Wall St. J. Sept. 1, 2018, https://www.wsj.com/articles/why-its-so-hard-to-be-an-ethical-investor-1535799601?mod=?mod=itp&mod=djemITP_h.

[160] See Cadesby B. Cooper, Rule 10b-5 at the Intersection of Greenwash and Green Investment: The Problem of Economic Loss, 42 Bus. Coll. Env. Affairs L. Rev. 405, 408 (2015) (exploring this question and observing that the answer depends, in part, on the extent to which the misrepresentation "involve information[s] bearing on the future expected cash flows of the company."). See also Donald Langevoort, Disasters & Disclosures (in this issue) (questioning whether compliance with voluntary disclosure standards can create an affirmative duty to disclose, thereby subjecting an issuer that fails to do so to antifraud liability).

focus on sustainability considerations in business decision-making.[161] Moreover, if sustainability disclosures relate to issues such as financial performance and risk management, those disclosures should properly be integrated into investor-oriented disclosure documents rather than being provided, as is currently the practice, into separate reports. Integration would have the additional benefit of increasing comparability between firms and reducing wasteful and duplicative search costs.

The challenge in adopting a disclosure mandate for sustainability within the existing securities disclosure framework is the implementation, however. As noted above, commentators have called for sustainability reporting to address a wide range of issues. The applicability of any particular issues varies by issuer and industry. In addition, sustainability is a moving target. Both the issues that arguably warrant disclosure and their importance to particular issues continue to evolve. Because of these characteristics, designing a line-item series of disclosures to address sustainability issues is likely unworkable, and a principles-based approach appear to be more appropriate.

Arguably, the SEC's materiality standard is, to a degree, a principles-based disclosure requirement in that, to the extent that sustainability issues are material to the existing mandated disclosure items such as an issuer's business plan, financial operations, risk factors or litigation risk, disclosure of those issues is required. This approach, however, does little to encourage either affirmative disclosures or issuer attention to determining whether sustainability issues are economically significant. In other words, an additional value to an affirmative disclosure requirement is its ability to focus board and management attention on acquiring information and exercising oversight.

This benefit can be analogized to that provided by the CEO and CFO certification requirement established by the Sarbanes-Oxley Act of 2002 (SOX).[162] Section 302 of SOX requires the CEO and CFO of public companies personally to certify that the reports their companies file with the SEC are both accurate and complete. The statute provides, among its requirements, that the certifying officers establish and maintain internal controls and evaluate the effectiveness of those internal

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[161] This article does not take a position on the normative question about the extent to which corporation decisions should incorporate sustainability considerations or, if so, which sustainability issues should be addressed.
[162] Exchange Act Rules 13a-15 and 15d-15

controls.[163] False certifications subject officers to potential liability in an SEC enforcement action as well as criminal liability.[164] SOX also establishes, among the sanctions, a provision providing for executives to forfeit incentive compensation and bonuses if their companies are required to restate their financial statements due to fraud or accounting mistakes.[165]

The challenge of course with the Sarbanes-Oxley certification requirement has been enforcement. Some commentators have challenged the SEC's enforcement efforts as "worrisome and problematic"[166] or criticized the failure of the provisions to impose liability to private plaintiffs.[167] On the other hand, there is widespread evidence that the certification requirement has been effective in encouraging corporate executives to be more engaged in their company's financial reporting and more proactive in seeking out the information necessary to engage in effective oversight.[168] In the next Part, this article will offer a proposal for sustainability disclosure designed to encourage greater information flow and board oversight akin to the rationale behind SOX section 302. In the following Part, the article will address enforcement of the proposal.

III. SD&A – a Proposed Approach for Mandated Sustainability Disclosure

This Article proposes that the SEC implement a new disclosure requirement of sustainability discussion and analysis as part of Regulation S-K, thereby requiring issuers to include SD&A reporting as

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[163] Sarbanes-Oxley Act of 2002 § 302, 15 U.S.C. § 7241 (2006). An executive who falsely certifies can be held personally liable.

[164] SOX section 906, 18 U.S.C. § 1350, imposes criminal liability. See Erin Massey Everitt, Sarbanes-Oxley's Officer Certification Requirements - Has Increased Accountability Equaled Increased Liability?, 6 DePaul Bus. & Comm. L.J. 225, 245 (2008) (discussing criminal liability and enforcement liability). Notably, the provision does not contain a private right of action.

[165] SOX section 304, 15 U.S.C. § 7243.

[166] Allison List, Note, The Lax Enforcement of Section 304 of Sarbanes-Oxley: Why is the SEC Ignoring Its Greatest Asset in the Fight Against Corporate Misconduct?, 70 Ohio St. L.J. 195, 218 (2009).

[167] Everitt, supra note __.

[168] The officer certification requirements of the Sarbanes-Oxley Act have proven quite effective at prompting executives of publicly traded companies to become more engaged in the financial reporting process. See, e.g., id. at 245.

part of their annual reports.[169] The SD&A requirement is modeled on the existing MD&A and CD&A reporting requirements, which are described in this first part of this section. The section then describes, in the second part, the details of the SD&A proposal, including several modifications to the MD&A and CD&A models that both address the specialized issues implicit in sustainability disclosure and enhance the effectiveness of the requirement.[170]

A. MD&A and CD&A – the Models for an SD&A Requirement

The SD&A requirement is modeled on two existing narrative disclosure frameworks – management discussion and analysis (MD&A) and compensation discussion and analysis (CD&A). The MD&A disclosure requirement is contained in Item 303 of Regulation S-K and SEC Interpretive Release No. 6835[171] and was specifically adopted to supplement the line item disclosures with disclosure that was more flexible and company-specific.[172] As the SEC explained,

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[169] This Article's proposal for issuers to include a narrative discussion of sustainability issues in the annual report is highly workable. Indeed, Salesforce voluntarily introduced a discussion of environmental, social and governance information in its 2018 Annual Report. See Salesforce 2018 Annual Report at 64, https://s1.q4cdn.com/454432842/files/doc_financials/2018/Salesforce-FY18-Annual-Report.pdf.

[170] To the extent that the SEC determines that SD&A requirement will impose significant new oversight costs on issuers, it may determine to implement the requirement on a delayed or tiered basis for smaller issuers or emerging growth companies. This approach would resemble that taken by the JOBS Act, which exempts emerging growth companies from some of Dodd-Frank's disclosure requirements with respect to executive compensation as well as the non-binding shareholder vote on such compensation. See, e.g., Amy Coleman, A Plague of Locusts: The JOBS Act as Foe More than Friend, 16 Duq. Bus. 44, 61 (2013) (reporting that the JOBS Act "negates the separate shareholder vote for executive compensation and the disclosure of executive compensation for median employee income requirement set by Dodd-Frank.").

[171] Securities Act Release No. 6835 (May 18, 1989), Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, 54 FR 22427.

[172] Id. at 22,436. See id. at *3-4 (summarizing the background of the MD&A disclosure requirement).

> The Commission has long recognized the need for a narrative explanation of the financial statements, because a numerical presentation and brief accompanying footnotes alone may be insufficient for an investor to judge the quality of earnings and the likelihood that past performance is indicative of future performance. MD&A is intended to give the investor an opportunity to look at the company through the eyes of management by providing both a short and long-term analysis of the business of the company. The Item asks management to discuss the dynamics of the business and to analyze the financials.[173]

Importantly, Item 303 creates an affirmative and non-specific duty to disclose material information when management knows of a trend, demand, commitment or uncertainty. In adopting Item 303, the SEC explicitly disclaimed the application of the court-adopted definition of materiality.[174] Instead, in its 1989 Release, the SEC issued the following guidance: "A disclosure duty exists where a trend, demand, commitment, event or uncertainty is both presently known to management and reasonably likely to have material effects on the registrant's financial condition or results of operation."[175]

The SEC went on to explain that that, when management knows of a trend, demand, commitment, event or uncertainty, it must "make two assessments:

> (1) Is the known trend, demand, commitment, event or uncertainty likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required.
>
> (2) If management cannot make that determination, it must evaluate objectively the consequences of the known trend,

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[173] Securities Act Release No. 6711 (April 17, 1987), Concept Release on Management's Discussion and Analysis of Financial Condition and Results of Operations, 52 FR 13715, at 13717.

[174] See Securities Act Release No. 6835, at 22,430 n.27. (explaining that the "probability/magnitude test for materiality approved by the Supreme Court in Basic, Inc. v. Levinson. . . is inapposite to Item 303 disclosure.")

[175] Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, Sec. Act Rel. No. 6835, 1989 SEC LEXIS 1011, *13 (May 18, 1989).

> demand, commitment, event or uncertainty, on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the registrant's financial condition or results of operations is not reasonably likely to occur."[176]

The importance of MD&A disclosure continues to grow. As one commentator observes "the MD&A is fast becoming the primary disclosure vehicle for management to relate its unique insider's critique of the registrant's financial performance and operations to help predict future performance."[177] Another explains that "Today, the MD&A is widely considered to be the primary form of narrative disclosure that is reviewed, together with financial statements, for investment decision making."[178] On the other hand, the vague and flexible standard makes the requirement difficult for issuers to comply with.[179] In one high profile case, the SEC brought an enforcement action against Caterpillar for failing to disclose, in its MD&A, the importance of its Brazilian subsidiary to the firm's financial results and the likely impact of political changes in Brazil on future results.[180] Caterpillar has been characterized

[176] See id. at *19. Former SEC Commissioner Edward H. Fleischman, stated that the standard "reasonably likely" "suggests a likelihood of about forty percent." Mark S. Croft, MD&A: The Tightrope of Disclosure, 45 S.C. L. Rev. 477, 485 (1994), citing Edward H. Fleischman, The Intersection of Business Needs and Disclosure Requirements: MD&A, Address before the Eleventh Annual Southern Securities Institute (Mar. 1, 1991).

[177] John W. Bagby, Paula C. Murray, & Eric T. Andrews, Show Green was my Balance Sheet? Corporate Liability and Environmental Disclosure, 14 Va. Envtl. L.J. 225, 299 (1995).

[178] Henry C. Hu, Keynote Address: Disclosure Universes and Modes of Information: Banks, Innovation, and Divergent Regulatory Quests, 31 Yale J. on Reg. 565, 594 (2014).

[179] See Rick E. Hansen, Climate Change Disclosure by SEC Registrants: Revisiting the SEC's 2010 Interpretive Release, 6 Brook. J. Corp. Fin. & Com. L. 487, 495 (2012) (observing that "crafting an MD&A that is responsive to the SEC's rules is arguably among the most difficult aspects of preparing a quarterly or annual report and has prompted the SEC to issue MD&A-specific guidance on several occasions.").

[180] Exchange Act Release No. 30,532 (In re. Caterpillar Inc.) [1992 Transfer Binder] 7 Fed. Sec. L. Rep. (CCH) P 73,830 (March 31, 1992), 1992 SEC LEXIS 786. Notably, the SEC's enforcement action was based on section 13(a) of the Exchange Act, not the antifraud provision. See id. at *18.

a “message case” indicating that the SEC intends to require improved disclosure.[181]

A more recent disclosure requirement, modeled on the MD&A is the compensation disclosure and analysis (CD&A). The SEC adopted the CD&A requirement in 2006 as part of its executive compensation disclosure reforms.[182] Issuers are required to provide the CD&A as part of their executive compensation disclosure in the proxy statement.[183]

The CD&A is intended "to provide to investors material information that is necessary to an understanding of the [company's] compensation policies and decisions,"[184] focusing on "the most important factors relevant to analysis of those policies and decisions."[185] Specifically, the CD&A is intended to be principles-based and to avoid boilerplate. [186] Item 402, the SEC rule that governs executive compensation disclosure sets out the requirements for the CD&A in two ways. First, item 402(b)(1) sets out a variety of “mandatory principles-

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[181] See Suzanne J. Romajas, Note, The Duty to Disclose Forward-Looking Information: A Look at the Future of MD&A, 61 Fordham L. Rev. 245, 258 (1993) (explaining that Caterpillar has been termed a "message case" intended to communicate that the SEC requires "improved disclosures" of known trends and uncertainties.)

[182] Executive Compensation and Related Person Disclosure, Securities Act Release No. 33-8732A, Exchange Act Release No. 34-54302A, 71 Fed. Reg. 53,158 (proposed Aug. 29, 2006). Jeffrey Gordon, a Columbia law professor, argued in a 2005 law review article that “the SEC should require proxy disclosure of a ‘Compensation Discussion and Analysis’ statement (CD&A) signed by the members of the compensation committee.” Jeffrey Gordon, Symposium on Bebchuck & Fried's Pay without Performance: Executive Compensation: If There's A Problem, What's the Remedy? The Case for "Compensation Discussion and Analysis", 30 Iowa J. Corp. L. 675, 677 (2005).

[183] See Schedule 14A, 17 C.F.R. § 240.14a-101, Item 8 (2014) (setting forth the requirements for the Compensation of Directors and Executive Officers (CD&A) portion).

[184] 17 C.F.R. § 229.402(b), Instruction 1 (2014).

[185] 17 C.F.R. § 229.402(b), Instruction 3 (2014).

[186] See 17 C.F.R. § 229.402, Instructions to Item 402(b). ("The Compensation Discussion and Analysis should focus on the material principles underlying the registrant's executive compensation policies and decisions and the most important factors relevant to analysis of those policies and decisions. The Compensation Discussion and Analysis shall reflect the individual circumstances of the registrant and shall avoid boilerplate language and repetition of the more detailed information set forth in the tables and narrative disclosures that follow.").

based topics" that issuers must address.[187] The rule identifies a variety of components of the required CD&A disclosure including the objectives of the compensation program and how each element of compensation is determined.[188] Item 402(b)(2) then acknowledges that "the material information to be disclosed under Compensation Discussion and Analysis will vary depending upon the facts and circumstances"[189] and lists fifteen "examples" of "material information" that may be included in the CD&A.

Both the MD&A and CD&A disclosures are primarily principles-based. As such, they offer flexibility that both allows the disclosures to be tailored to the circumstances of a particular issuer and allows the disclosures to evolve in responses to changes in issuer and market conditions. As the SEC staff explained with respect to its MD&A requirement: "the flexible nature of this requirement has resulted in disclosures that keep pace with the evolving nature of business trends without the need to continuously amend the text of the rule."[190]

The flexibility of the existing MD&A and CD&A disclosures is a reason to use them as the model for an SD&A requirement. At the same time, these disclosures suffer from several disadvantages relative to line-item disclosure requirements.[191] First, because they are premised on a materiality determination by management, they offer management substantial discretion, discretion that is often exercised in favor of failing to disclose. Even well-meaning insiders may evaluate the materiality standard differently. Second, they do not permit the same easy comparability as quantitative disclosure requirements. The SEC itself has criticized existing MD&A disclosure as "less detailed" than desired

[187] Stephen M. Salley, Note: "Fixing" Executive Compensation: Will Congress, Shareholder Activism, or the New SEC Disclosure Rules Change the Way Business is Done in American Boardrooms?, 70 Ohio St. L.J. 757, 787-788 (2009).
[188] 17 C.F.R. § 229.402(b) (1)
[189] 17 C.F.R. § 229.402(b) (2)
[190] Commission Guidance Regarding Disclosure Related to Climate Change, supra note __.
[191] See generally J. Robert Brown, James D. Cox, Joan MacLeod Heminway & Lyman Johnson, Brief of Professors at Law and Business Schools as Amicus Curiae in Support of Respondents, Leidos, Inc., fka SAIC, Inc., Petitioners, v. Indiana Public Retirement System, Indiana State Teachers' Retirement Fund, and Indiana Public Employees' Retirement Fund, Respondents, No. 16-581 (S. Ct. Sept. 7, 2017), https://ssrn.com/abstract=3034103 (detailing the shortcomings of the MD&A requirement in providing meaningful information).

and in need of "greater analysis" and "additional explanations. . . ."[192] One SEC official offered the view that "in too many MD&As . . . There is too much elevator music, and not enough really useful analysis."[193] As a result, it is worth considering whether, in adopting the MD&A model for sustainability disclosure, that model can be refined to enhance its effectiveness.

B. The SD&A Proposal

The SD&A requirement proposed by this Article would require issuers to include a discussion of sustainability issues in their annual financial reporting as follows. Issuers would be required, in their SD&A, to identify and explain the three sustainability issues most significant to their operations. The required disclosure would include a discussion of the potential impact of those sustainability issues as well as an explanation of the basis for the issuer's determination of significance.[194] Analogous to the MD&A, the SD&A disclosure would be premised on known trends, risks and opportunities in that the requirement would be framed in terms of known or reasonably knowable sustainability issues, including risks, trends, and opportunities that, in the opinion of the board of directors, are material to the issuers' business plan or operations.

The requirement that issuers identify and discuss the three most significant sustainability issues responds to the range of challenges that have been brought against mandated sustainability disclosure. By

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[192] See Business and Financial Disclosure Required by Regulation S-K, Exchange Act Release No. 77,599, 81 Fed. Reg. 23915, * 49 (April 22, 2016)

[193] Remarks of Alan Beller at The Roundtable on The Integration of the 1933 and 1934 Acts, transcript at 126 (Mar. 21, 2002), avail. at http://3197d6d14b5f19f2f440-5e13d29c4c016cf96cbbfd197c579b45.r81.cf1.rackcdn.com/collection/programs/int1933_1934Transcript.pdf.

[194] Robert Eccles and Tim Youmans have a proposal for boards voluntarily to issue a sustainability statement in their annual reports that they term a "statement of significant audiences and materiality." Like the SD&A, the Eccles and Youmans statement would increase board involvement in and oversight of sustainability issues, but their proposal differs from the one developed in this Article in several key aspects, including perhaps most importantly the fact that it focuses on stakeholder significance. See Robert Eccles and Tim Youmans, Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality (2015), https://www.hbs.edu/faculty/Publication%20Files/16-023_f29dce5d-cbac-4840-8d5f-32b21e6f644e.pdf.

requiring the SD&A to focus on the specific issues that are most important to a particular issuer's operations, the proposal addresses the difficulty in articulating a precise definition of materiality or determining an appropriate materiality standard. Although the SD&A does not provide a comprehensive level of disclosure, it is a workable starting point that enables boards and investors to identify and evaluate those practices most likely to have a substantial economic impact. In addition, as discussed further below, a requirement that issuers disclose the three most material issues reduces the potentially burdensome impact associated with a more ambitious disclosure requirement, while providing a more objective standard than the generic but un-cabined materiality standard currently reflected in the SEC's approach to MD&A disclosure. Thus, the proposal is arguably superior to a standard that would require disclosure of all material sustainability issues or condition disclosure requirements in terms of a minimum dollar threshold of anticipated economic impact.[195]

The proposal contemplates that the SEC's adopting release would provide additional guidance with respect to the nature and scope of sustainability issues, similar to the guidance provided by the SEC for CD&A. Specifically, the guidance would identify the range of topics that have been identified within the framework of sustainability such as "climate change, resource scarcity, corporate social responsibility, and good corporate citizenship"[196] but would note that the identification of material sustainability issues is industry- and issuer-specific. The release would also note that the materiality of specific sustainability issues can evolve over time and is a product of a variety of considerations including the relevance of the issue to earnings quality and volatility, reputational and regulatory risk, and the quality of board oversight and internal controls.

The SD&A proposal would modify the guidelines of Item 303 to place responsibility for the determination of what sustainability issues

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[195] Such an alternative approach could provide, for example, that trends or risks that the board estimates are reasonably likely to affect revenues by more than $1 million annually are presumptively material. This guidance would be roughly analogous to Item 404's disclosure requirement for related party transactions, which requires disclosure of all such transactions in which the amount involved exceeds $120,000. See 17 CFR 229.404. Given the difficulty of ascertaining the impact of ESG considerations, this Article takes the position that such an approach is less workable.

[196] SEC Concept Release, supra note __ at 206.

require disclosure in the hands of the board of directors, rather than management.[197] This would be consistent with one of the main reasons proffered by investors for requiring sustainability disclosure – that such disclosure provides them with valuable insight into the board's familiarity with and oversight of critical issues such as risk management. In addition, the SEC recently highlighted the expertise of the board in evaluating the significance of particular issues to the company's business.[198] The board or a sustainability committee of the board[199] would also be required to sign the SD&A.[200] Like the CEO and CFO certification requirements in Sarbanes-Oxley, the certification requirement would encourage issuers to develop systems for collecting and communicating the information necessary for the board to meet this obligation.[201]

The rationale for requiring both board responsibility and certification is to ensure that the process of preparing the SD&A enhances the board's role in understanding and overseeing the issuer's

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[197] This board-centered approach follows that of India, which, through legislation, placed primary responsibility for development and oversight of an issuer's CSR policy in the board of directors. See Afsharipour, supra note __ at 101-104. The focus of the board's role in this Article's proposal is limited to disclosure oversight, with the expectation that such oversight will broaden the information available to the board for purposes of risk management and strategic planning.

[198] See, e.g., Shareholder Proposals, SEC Staff Legal Bulletin 14I (Nov. 1, 2017), https://www.sec.gov/interps/legal/cfslb14i.htm (observing that, in the context of determining the application of the ordinary business exemption to shareholder proposals, "A board acting in this capacity and with the knowledge of the company's business and the implications for a particular proposal on that company's business is well situated to analyze, determine and explain whether a particular issue is sufficiently significant. . . . ").

[199] See, e.g., Jayne Barnard, At the Intersection of Corporate Governance and Environmental Sustainability, 2 Wm. & Mary Bus. L. Rev. 207 (2011) (articulating several advantages of a board-level sustainability committee).

[200] This requirement was part of Jeff Gordon's proposal for CD&A, it but was not adopted. See Gordon, supra note __ at 695 (proposing that the CD&A "be signed by the members of the committee (or the independent directors, as the case may be").

[201] See, e.g., Robert Charles Clark, Corporate Governance Changes in the Wake of the Sarbanes-Oxley Act: A Morality Tale for Policymakers Too, 22 GA. ST. U. L. REV. 251, 266 (2005) ("a fair number of public company CEOs have already expressed the view that the process of getting ready for section 404 attestation has helped them improve their management information systems."). See also Robert A. Prentice & David B. Spence, Sarbanes-Oxley as Quack Corporate Governance: How Wise is the Received Wisdom?, 95 Geo. L.J. 1843, 1898-1907 (2007) (discussing impact of Sarbanes-Oxley's certification requirements).

sustainability practices. From an investor's perspective, the key issues are whether the directors are aware of the sustainability issues that may materially affect the issuer's operations and whether they have incorporated those issues into their strategic planning and oversight. Placing specific responsibility on directors enables investors to ensure that the board is performing this role and to hold the board accountable for doing so.

Finally, as detailed below, this Article contemplates that the SD&A requirement would be enforced through a combination of public and private enforcement. The SEC staff would review and comment on issuers' SD&A disclosures as part of its review of securities filings and would have the authority to bring enforcement actions against issuers and individual directors to failure to comply.[202] In addition, fraudulent misrepresentations and omissions in an issuer's SD&A would be actionable under Rule 10b-5, and shareholders could, in appropriate cases, pursue private litigation.

IV. Advantages and Limitations of SD&A

This section identifies the key advantages of the SD&A proposal as well as the principal possible objections. Importantly, it should be noted that SD&A is a modest starting point for sustainability disclosure, and the proposal advanced in this Article is in the nature of a first step that will enable issuers, investors and regulators to evaluate the utility of sustainability disclosure as well as providing data to evaluate claims of the relationship of sustainability to economic value. This Article does not make the claim that the SD&A will provide investors and the markets with comprehensive sustainability information, nor that it will or should displace existing voluntary disclosure regimes. Rather, for the reasons set out below, integrating sustainability disclosure into traditional financial reporting provides a number of advantages.

A. The SD&A Proposal is a Workable First Step

[202] The mandatory nature of the SD&A requirement is critical both in enhancing comparability and providing an incentive for the board to take its responsibility seriously. Cf. Eccles & Youman, supra note __ (proposing to mobilize investor to "as company boards to issue The Statement"). For the reasons detailed above, this Article takes the view that boards will be unwilling to provide meaningful sustainability information in the financial statements unless required to do so.

A key advantage to the SD&A proposal is its workability. One of the challenges in formulating a mandatory sustainability disclosure requirement is that the topic of sustainability is vast and open-ended. Private organizations such as GRI and SASB have identified dozens of disclosure items, and current sustainability reports commonly exceed 100 pages in length. The cost of developing and complying with comparable mandatory disclosure requirements would place a heavy burden on issuers.[203] Issuers might reasonably question the extent to which specific disclosure issues were relevant to their operations. And the utility of such extensive disclosures for investors, for whom the overall volume of mandatory disclosure is already overwhelming, is questionable.[204]

Increasing the number of issues addressed, requiring issuers to provide hard data on sustainability issues and formulating line item disclosure requirements are ways potentially to increase the information content of sustainability disclosure. That increase comes, however, at a substantial cost both to issuers in preparing the information and to investors in using it. Instead, the SD&A proposal offers a balance between information value and workability. In particular, the requirement that issuer determine which sustainability issues are most important and explain the basis for their determination is likely to reduce the propensity of issuers to engage in duplicative or boilerplate disclosure that is likely to be uninformative.[205]

In addition, a more comprehensive disclosure requirement would embroil issuers and regulators in difficult determinations of the appropriate scope of disclosure. It would force regulators to answer

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[203] Cf. SEC Chairman Jay Clayton, Remarks at the Economic Club of New York, July 12, 2017, https://www.sec.gov/news/speech/remarks-economic-club-new-york ("There are circumstances in which the Commission's reporting rules may require publicly traded companies to make disclosures that are burdensome to generate, but may not be material to the total mix of information available to investors.").

[204] See, e.g., Paredes, supra note __ (explaining how increasing quantity of required disclosure reduces its value to investors).

[205] Compare Investor Responsibility Research Center Institute (IRRC), The Corporate Risk Factor Disclosure Landscape, Jan. 2016, https://irrcinstitute.org/wp-content/uploads/2016/01/FINAL-EY-Risk-Disclosure-Study.pdf (criticizing required narrative format of risk factor disclosure requirement as "tend[ing] to represent a listing of generic risks, with little to help investors distinguish between the relative importance of each risk to the company.").

difficult questions about which sustainability issues warrant disclosure in order to create line item disclosure requirements, and to evaluate contested claims about the economic materiality of the required information. At the same time, it would exacerbate the risk of information overload by issuers to provide extensive boilerplate disclosures rather than identifying the particular issues on which investors should focus.

The SD&A requirement also, although limited, creates an explicit component of sustainability disclosure rather than simply leaving sustainability issues within the ambiguous materiality assessment applicable to an issuer's overall MD&A and risk factor disclosure. As the discussion above demonstrates, it is a mistake to attempt to load sustainability disclosure into these general disclosure frameworks, and the SEC's decision to do so has had the effect of unduly limiting both issuer consideration and disclosure of sustainability issues. At the same time, the mandate will have the practical effect of requiring issuers to examine and evaluate the impact of a far broader range of sustainability issues than the three most significant, of which disclosure is mandated, because this evaluation will be necessary to make the determination about which issues to disclose. Accordingly, the proposal's effect on information reporting and board oversight will be substantially greater than requiring the company to consider just three disclosure items.

Finally, a sustainability disclosure requirement is a way of managing expectations. Although a wide range of sustainability issues may be relevant to investors, formalizing the type and quantity of such disclosure that is required provides predictability and increases investor confidence. Moreover, there is evidence that qualitative disclosure can provide substantial value to the market. For example, John Campbell et al. empirically the effect of the SEC's 2005 mandate that firms include a "risk factor" section in their annual reports and found that, contrary to the assertions of critics, "managers provide useful risk factor disclosures and investor incorporate this information into market values."[206]

B. SD&A Reporting Will Promote Comparability

[206] John Campbell, et al., The Information Content of Mandatory Risk Factor Disclosures in Corporate Filings, 19 Rev. Acct'ing Stud. 396 (2014).

In addition, the SD&A proposal will promote the comparability of sustainability disclosure. Concededly, a disclosure obligation that admits to issuer-specific variation offers less comparability than a set of one-size-fits-all disclosure requirements. Because each issuer's board determines the most significant sustainability issues independently, there is likely to be substantial variation among the issues addressed. As a result, the market may learn very little by comparing Volkswagen's discussion of emissions with Pepsico's discussion of water conservation. At the same time, including sustainability disclosures within an issuer's securities filings and subjecting those disclosures to SEC staff review and comment is likely to have a significant effect on comparability. The SEC staff currently reviews more than half of issuer 10-K's filed every year.[207] The SEC's comments focus not just on the hard numbers in the 10-K, but also on the narrative components – the MD&A and the CD&A, and the scrutiny to which the staff subjects these disclosures is real.[208]

In addition, although only a small percentage of those 10-K's receive staff comment letters, a variety of industry participants review those letters and report to issuers on trends in SEC policies and concerns with respect to 10-K disclosure.[209] These reports, as well as the SEC reviews themselves, lead to revisions and refinements of the narrative disclosures in the MD&A and CD&A.[210]

[207] Ernst & Young, SEC Reporting Update 2017 trends in SEC comment letters, Sept. 25, 2017, http://www.ey.com/publication/vwluassetsdld/secreportingupdate_05444-171us_25september2017/$file/secreportingupdate_05444-171us_25september2017.pdf?OpenElement, at 5.

[208] See id at 7 (reporting that, in 2016 & 2017, comments on the MD&A represented 43% of total comments).

[209] See, e.g., id. (describing trends in SEC comment letters); Deloitte, SEC Comment Letters — Including Industry Insights: What "Edgar" Told Us, Oct. 2015, https://www2.deloitte.com/content/dam/Deloitte/us/Documents/audit/us-aers-sec-comment-letters-including-industry-insights-what-edgar-told-us-102015.pdf (reporting the top ten topics discussed in SEC comment letters).

[210] See Elizabeth A. Ising, et al., Executive Compensation Disclosure Handbook: A Practical Guide to the SEC's Executive Compensation Disclosure Rules, October 2016, at 12, https://www.gibsondunn.com/wp-content/uploads/documents/publications/Ising-Mueller-Hanvey-Executive-Compensation-Disclosure-Handbook-Donnelley-Financial-Solutions-Oct-2016.pdf ("companies are increasingly seeing their peers make favorable changes to their disclosures and, regardless of prior say-on-pay votes, those that see this may be inclined to take a fresh look at their own CD&A simply to avoid falling behind.").

This review process is likely to generate common disclosure policies among issuers, particularly those in the same or related industries.[211] In particular, because the SEC staff have access to other issuer's disclosures, it will be able to identify situations in which an issuer has not addressed an issue that appears to be important to its peer firms or within its industry. The staff comment letters themselves will generate information about an issuer's evaluation of sustainability issues and the risks that they present. And issuers will themselves learn from and emulate the disclosures made by their peers.

C. SD&A Will Increase the Reliability of Sustainability Disclosures

Finally, SD&A will improve the reliability of sustainability disclosure over the current system. Here is arguably where this Article's proposal has the most to offer. First, it is important to recognize the substantial methodological impact of integrating sustainability disclosure into traditional securities reporting. Under this proposal, sustainability disclosures will be prepared by disclosure attorneys rather than marketing personnel and subjected to the same verification requirements as traditional financial disclosures.

Furthermore, the SD&A proposal will lead to the Board of Directors being accountable for sustainability disclosures in a way in that they are not in the current system. Because of the board's role in overseeing and certifying the sustainability disclosures, boards will have to set up information reporting systems through which they regularly receive information about the issues addressed in the SD&A and their impact on operations. This reporting process will both improve the reliability of the disclosures and provide the board with a greater role in overseeing and understanding the issuer's sustainability practices. In addition, it will enable the board to incorporate sustainability considerations into its analysis of strategic issues and operational risk management. By contrast, in the current system, the degree of board oversight over sustainability issues is unclear. In addition, there is no direct link between the board or even high-level executives and the choice of issues addressed in an issuer's sustainability reports.

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[211] Stephen V. Brown, Xiaoli (Shaolee) Tian & Jenny Wu Tucker, The Spillover Effect of SEC Comment Letters on Qualitative Corporate Disclosure: Evidence from the Risk Factor Disclosure, __ Contemp. Accounting Res. __ (2018).

Even if the quality of sustainability disclosures made some firms is high under a voluntary system, a mandatory disclosure requirement is likely to improve the quality of sustainability disclosure more broadly. In an analogous examination of the shift from voluntary to mandatory disclosure of risk factors, Adam Prichard and Karen Nelson found that, although those firms facing significant litigation risk made substantial disclosures under a voluntary regime, mandatory disclosure improved the quality of disclosure for other firms.[212]

The value of a mandatory disclosure requirement in ensuring quality disclosure depends critically on its enforcement. In other words, the risk of liability for noncompliance is what gives teeth to the statutory disclosure provisions. Accordingly, if the goal of the SD&A is to improve the reliability of sustainability disclosures, it is necessary to give attention not just to the disclosure requirement itself but to the manner in which it is enforced.

The disclosure requirements of Regulation S-K do not, themselves, create an independent private right of action.[213] Thus an issuer's failure to disclose a known trend in violation of Item 303, can only be enforced by the SEC.[214] On the other hand, the federal courts have universally recognized a private right of action for federal securities fraud under rule 10b-5. Accordingly, to the extent that an issuer makes an affirmatively false disclosure, that conduct is arguably actionable through private litigation. Courts have generally held both that Regulation S-K creates an affirmative obligation to disclose and that failure to comply with that disclosure requirement can serve as the basis for a private securities fraud suit.[215]

As a result, inclusion of SD&A within securities filings would both subject issuers' sustainability disclosures to SEC oversight and enforcement and also make it clear that fraudulent misrepresentations and omissions are actionable as securities fraud. Notably, the structure of the SD&A proposal increases the likely reliability of the disclosure by

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[212] Carrot or Stick? The Shift from Voluntary to Mandatory Disclosure of Risk Factors
[213] Oran v. Stafford, 226 F.3d 275, 287 (3d Cir. 2000)
[214] Id.
[215] See, e.g., Ind. Pub. Ret. Sys. v. SAIC, Inc., 818 F.3d 85, 94 n.7, 98 (2d Cir. 2016), quoting Stratte-McClure v. Morgan Stanley, 776 F.3d 94, 103-04 (2d Cir. 2015) (explaining that "Item 303 imposes an 'affirmative duty to disclose. . . . [that] *can* serve as the basis for a securities fraud claim under Section 10(b).'").

making the issuer's affirmative disclosure requirement explicit.[216] Issuers cannot greenwash their SD&A to avoid addressing issues that are likely to cause the market concern[217] because, to the extent that those issues are potentially most significant, an issuer's decision to omit them would constitute securities not just an omission but a fraudulent misrepresentation – to wit, a representation that the omitted issue is not among the three most significant.

This article contemplates that implementation and enforcement of SD&A would take place primarily through SEC oversight and, when appropriate, enforcement actions. As noted above, because of the review process, the SEC staff will be well-positioned to identify critical weaknesses in an issuer's MD&A – allowing the staff to ask Exxon, for example, why it has not addressed climate change in its SD&A in light of the disclosures by Occidental Petroleum and BP.

There are advantages to relying on the SEC to undertake most SD&A enforcement. First, the SEC may have greater expertise, enabling it to choose more accurately the cases in which enforcement is most consistent with the purposes of federal regulation.[218] Second, public

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[216] There is ongoing debate about the extent to which all material omissions under Item 303 are actionable as securities fraud. The issue involves the question of whether the materiality standard for Item 303 is lower than that under Basic Inc. v. Levinson. See, e.g., See Oran v. Stafford, 226 F.3d at 288 ("a violation of SK-303's reporting requirement does not automatically give rise to a material omission under Rule 10b-5"). See also Matthew C. Turk & Karen E. Woody, Leidos and the Roberts Court's Improvident Securities Law Docket, SLR Online, Nov. 2017, https://www.stanfordlawreview.org/online/leidos-and-the-roberts-courts-improvident-securities-law-docket/ ("A consequence of the slightly lower materiality threshold for Item 303 is that it reduces the range of claims that private investors may bring based on firms' incomplete disclosure of required MD&A information"), The Supreme Court was positioned to address this question when it granted certiorari in Leidos last year, Ind. Pub. Ret. Sys. v. SAIC, Inc., 818 F.3d 85, 94 n.7 (2d Cir. 2016), cert. granted sub nom. Leidos, Inc. v. Ind. Pub. Ret. Sys., 137 S. Ct. 1395 (2017). but the Leidos case was settled prior to oral argument. Turk & Woody, supra.

[217] The SD&A requirement is therefore more constraining than the risk factor disclosure requirement. Cf. Edward A. Morse, Vasant Raval, & John R. Wingender, SEC Cybersecurity Guidelines: Insights into the Utility of Risk Factor Disclosures for Investors (December 29, 2015). Available at SSRN: https://ssrn.com/abstract=2711439 or http://dx.doi.org/10.2139/ssrn.2711439 (finding that most issuers failed to disclose cybersecurity risk after the SEC's release of new guidelines and that market appeared to view disclosure of such risk as a negative signal).

[218] See, e.g., James J. Park, Rules, Principles, and the Competition to Enforce the Securities Laws, 100 Calif. L. Rev. 115, 124 (2012) (observing that public enforcement

enforcement may be more efficient.[219] Third, public enforcement is unlikely to be affected by the incentives that have the potential to produce abusive and excessive litigation such as the high fees that plaintiffs' attorneys can recover. Thus, for example, private litigants have rarely targeted individual defendants because of their lack of "deep pockets," but the prospect of SEC enforcement is likely to focus the attention of corporate directors on ensuring that their sustainability disclosure is accurate.[220] Finally, the government can often send a message by bringing a limited number of high profile cases. The SEC's enforcement action in Caterpillar is an example.[221]

There are problems, however, with limiting enforcement to the SEC. A variety of courts and commentators, including the U.S. Supreme Court and the SEC itself have acknowledged the valuable role that private enforcement plays in supplementing public enforcement efforts.[222] The government may have limited resources available to

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may be premised on "the idea that the SEC is a better securities enforcer than private parties because of its expertise with respect to the securities laws."). See also Joseph A. Grundfest, Disimplying Private Rights of Action Under the Federal Securities Laws: The Commission's Authority, 107 Harv. L. Rev. 961 (1994) (suggesting, in light of these considerations, that the SEC eliminate private litigation to enforce rule 10b-5).

[219] William W. Bratton & Michael L. Wachter, The Political Economy of Fraud on the Market, 160 U. Pa. L. Rev. 69, 118 (2011) (advocating "stepped-up SEC enforcement capability as a cost-effective substitute" for private litigation).

[220] "Though rare, enforcement actions against directors are a key component of the SEC's targeting of misconduct by 'gatekeepers." Bradley Bondi, A Brief History Of SEC Enforcement Actions Against Directors, Law360.com, Oct. 16, 2015, https://www.law360.com/articles/714967/a-brief-history-of-sec-enforcement-actions-against-directors. A relatively small number of SEC actions that involve individual directors can be very effective in increasing directors' attention to their oversight responsibilities. See, e.g., Sheppard Mullin, SEC Sharpens Focus on Disclosure of Executive Perks, June 22, 2005, https://www.corporatesecuritieslawblog.com/2005/06/sec-sharpens-focus-on-disclosure-of-executive-perks/ (advising that one message from SEC's enforcement actions against Tyson Foods and GE is that members of compensation committees face "personal liability for inaccurate or incomplete [compensation] disclosures").

[221] In re Caterpillar, Inc., Exchange Act Release No. 30,532, 7 Fed. Sec. L. Rep. (CCH), 73,830 (Mar. 31, 1992).

[222] See, e.g., Tellabs, Inc. v. Makor Issues & Rts., Ltd., 551 U.S. 308, 313 (2007) (noting that private actions are an "essential supplement to criminal prosecutions and civil enforcement actions brought, respectively, by the Department of Justice and the Securities and Exchange Commission"); James D. Cox et al., SEC Enforcement Heuristics: An Empirical Inquiry, 53 Duke L.J. 737, 738 (2003) (observing that "Since the inception of the federal securities laws, the government's broad enforcement

address wrongdoing. In addition, the SEC enforcement efforts are vulnerable both to political pressures and shifting administrative priorities.[223] The risk of under-enforcement is illustrated by the SEC's limited track record with respect to MD&A disclosure; it has brought fewer than 100 enforcement cases alleging MD&A violations since the adoption of Regulation S-K.[224]

Accordingly, private enforcement is likely to serve as a valuable supplement to public enforcement. Although commentators have raised concerns about the potential for excessive or burdensome securities fraud litigation,[225] that risk is likely to be especially limited under the SD&A proposal for three reasons. First, the SD&A requirement is explicit – issuers are only required to disclose the three most significant sustainability issues. As a result, the requirement does not open the door to efforts to characterize additional sustainability issues as fraudulent omissions. Second, to succeed in a securities fraud lawsuit, private litigants must establish loss causation and damages, meaning that they must show that the issuer's misrepresentation or omission had an economic impact on the value of their shares. The loss causation requirement, at least in the way it has been interpreted by the courts, requires affirmative proof that the fraud impacted stock price. Thus only the most economically important sustainability disclosure failures will

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authority has been complemented by private causes of action."); A.C. Pritchard, The SEC at 70: Time for Retirement?, 80 Notre Dame L. Rev. 1073, 1085 (2005) (noting that "With a few minor exceptions … the SEC has sided with the plaintiffs' bar in the courts.").

[223] See Pitt & Shapiro, supra note __ at 279 (observing that "any projection of future SEC enforcement trends is highly dependent upon the accuracy of prognostications about the prevailing political climate"). These concerns can be mitigated if public enforcement by multiple regulators is possible. See, e.g., John C. Coffee, Jr. & Hillary A. Sale, Redesigning the SEC: Does the Treasury Have a Better Idea?, 95 Va. L. Rev. 707, 763 (2009) (explaining that "state Attorneys General have played an aggressive role in prosecuting securities fraud and have pushed the SEC to be more vigorous in its own enforcement efforts.").

[224] Leidos Amicus Brief, supra note __ at 26.

[225] This risk is potentially heightened with respect to sustainability disclosure because of uncertainty about issues such as the definition of sustainability, the determination of economic materiality, and the difficulty for even a well-intentioned issuer in evaluating the economic impact of a known risk or trend. See, e.g., Donald Langevoort, Disasters & Disclosures (in this issue) (discussing the difficulty in determining the extent of a duty to disclose disaster-related risks).

potentially trigger private litigation.[226] Third, to bring a securities fraud suit, a private litigant must be a purchaser or seller of the securities. As a result, private litigation cannot be used by environmental groups or other non-shareholder stakeholders to promote non-economic objectives.

Conclusion

Despite the growing quantity of corporate sustainability disclosures, the existing disclosure system is fragmented, unreliable and incomplete. In light of the growing worldwide debate over sustainability practices and investor claims that quality sustainability disclosures are necessary for them to evaluate issuer operations adequately, it is necessary for the SEC to replace the existing framework with an integrated disclosure structure. This article has proposed a principles-based disclosure approach through a narrative sustainability disclosure and analysis reporting requirement. The article argues that the SD&A is well suited to improving the information about corporate sustainability issues available to investors and that SD&A quality can be enhanced by a liability and enforcement structure that creates direct incentives for board involvement and oversight.

It is too early to determine the extent to which sustainability business practices impact economic performance or the degree to which boards that engage with sustainability practices can exercise better risk management and monitoring. SD&A disclosure represents a valuable first step that will enable investors and researchers to evaluate those questions while imposing a minimal burden on corporate issuers.

[226] Because the relative significance of sustainability issues can change over time, it may be worthwhile for the SEC to consider a safe harbor providing that, under appropriate circumstances, an issuer's identification of a new sustainability issue does not subject it to liability for previously failing to discuss that issue. See, e.g., Barbara Novick, et al., EXPLORING ESG: A Practitioner's Perspective, BlackRock Viewpoint, June 2016, at 9, https://www.blackrock.com/corporate/literature/whitepaper/viewpoint-exploring-esg-a-practitioners-perspective-june-2016.pdf (proposing "safe harbor provisions that ensure that companies which initiate ESG factor reporting do not face retrospective litigation").