SUSTAINABLE BUSINESS LAW? THE KEY ROLE OF CORPORATE GOVERNANCE AND FINANCE

BY
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Lawyers, law schools, and corporate entities have shown an increased interest in sustainable business strategies. This is reflected by the increase in sustainability practice groups, law school courses, and textbooks focusing on the relationship between sustainability and business law; lawyers moving into executive-level sustainability positions in the private sector; and the proliferation of corporate sustainability policies, as well as increased interest in mitigating climate risk and engaging in sustainable finance. But what exactly is sustainable business law, and what role do lawyers play in advancing sustainability in the corporate world? This Article argues that "sustainable business law" has emerged as a distinct area of law and serves as an introductory explanation to define and understand the growing subject matter at the intersection of sustainability, business, and the law, as well as explores the key role that corporate governance and finance play in achieving sustainability.

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I. INTRODUCTION

Lawyers, law schools, and corporate entities have shown an increased interest in sustainable business strategies. This is reflected by the increase in sustainability practice groups, law school courses,[1] and textbooks[2] focusing on the relationship between sustainability and business law; lawyers moving into executive-level sustainability positions in the private sector; and the proliferation of corporate sustainability policies, as well as increased interest in mitigating climate risk and engaging in sustainable finance. For example, of the Am Law 50 law

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[1] Such law school courses include the following: Sustainability Law and Business; Sustainable Capitalism and environmental, social, and governance; Sustainable Business and the Environment; Strategic Planning for Sustainability; Sustainability and Business; Green Business Law; Lawyers for a Sustainable Economy.

[2] *See, e.g.*, MICHAEL BLOWFIELD, BUSINESS AND SUSTAINABILITY (2013) (giving an overview on how business is impacting and being impacted by sustainability); SUSTAINABILITY & BUSINESS LAW (Judd F. Sneirson & Nancy E. Shurtz eds., 2017) (presenting materials on sustainability as it relates to various areas of business law).

firms, thirty-five have a practice group or a specialty focus on sustainable business; environmental, social, and governance (ESG); or corporate social responsibility (CSR).[3] Also, according to the U.S. News & World Report, of the fourteen law schools tied for the top ten in environmental law specialty programs, at least seven have a course or program on the subject of sustainable business.[4] Even the American Bar Association has adopted a resolution urging lawyers "to advise their clients of the risks and opportunities that climate change provides."[5] Now, the Biden Administration may also be forcing businesses to prepare for new ESG regulations[6] and has named the first-ever senior policy adviser for climate and ESG to the U.S. Securities and Exchange Commission (SEC), underscoring the elevation of ESG issues.[7] This Article serves as an introductory explanation to define and understand the growing subject matter at the intersection of sustainability, business, and the law, as well as explores the key role that corporate governance and finance play in achieving sustainability.

This Article argues that "sustainable business law" has emerged as a distinct area of law. Vandenbergh, in his now seminal article *Private Environmental Governance*, asserts that environmental law has "transformed from a positive law field deeply rooted in administrative law

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[3] The Am Law 50 firms found to have a practice or area of focus in sustainable business, ESG, or CSR include: Kirkland & Ellis; Latham & Watkins; Baker McKenzie; DLA Piper; Sidley Austin; Hogan Lovells; Morgan, Lewis & Bockius; White & Case; Norton Rose Fulbright; Gibson, Dunn & Crutcher; Ropes & Gray; Greenberg Traurig; Simpson Thacher & Bartlett; Paul, Weiss, Rifkind, Wharton & Garrison; Sullivan & Cromwell; Mayer Brown; Davis Polk & Wardwell; Cleary Gottlieb Steen & Hamilton; Quinn Emanuel Urquhart & Sullivan; Cooley; Paul Hastings; Goodwin Procter; Reed Smith; Covington & Burling; Akin Gump Strauss Hauer & Feld; Orrick, Herrington & Sutcliffe; Morrison & Foerster; Squire Patton Boggs; Winston & Strawn; Shearman & Sterling; Holland & Knight; Wilson Sonsini Goodrich & Rosati; Foley & Lardner; McGuireWoods; and Willkie Farr & Gallagher.

[4] Law schools with a course in sustainable business include: Lewis & Clark, Pace (Haub), University of California Berkeley, Georgetown, Vermont, and University of Oregon. *Environmental, Natural Resources, and Energy Law*, LEWIS & CLARK L. SCH., https://perma.cc/WZK2-N2C7 (last visited Sept. 20, 2021); *Environmental Law Program*, PACE UNIV., https://perma.cc/239E-WE7F (last visited Sept. 20, 2021); *Environmental Law Program*, BERKELEY L., https://perma.cc/9ZXC-3JVU (last visited Sept. 20, 2021); *Georgetown's Environmental Law & Policy Program*, GEO. L., https://perma.cc/29R8-K9ME (last visited Sept. 20, 2021); *Environmental Law Concentrations*, VT. L., https://perma.cc/D3XM-NFAX (last visited Sept. 20, 2021); *Environmental & Natural Resources Law (ENR)*, UNIV. OF OR., https://perma.cc/4YS7-GE9H (last visited Sept. 20, 2021). Stanford has a program titled "Lawyers for a Sustainable Economy." *Lawyers for a Sustainable Economy*, STAN. L. SCH., https://perma.cc/BQK6-5JCR (last visited Sept. 20, 2021).

[5] RESOLUTION 111, HOUSE OF DELEGATES (AM. BAR ASS'N 2019), https://perma.cc/5EJC-D9TT.

[6] Climate-Related Financial Risk, Exec. Order No. 14030, 86 Fed. Reg. 27,967, 27,967–69 (May 25, 2021); Emily Glazer, *Companies Brace Themselves for New ESG Regulations Under Biden*, WALL ST. J., https://perma.cc/4FFK-75G5 (last updated Jan. 18, 2021). *See infra* Part IV.B.

[7] Andrew Ramonas, *SEC's Lee Names Agency's First Senior Adviser for Climate, ESG*, BLOOMBERG LAW (Feb. 1, 2021), https://perma.cc/TZ58-HBJ6.

to one that is also heavily rooted in private law and private governance."[8] Vandenbergh defines private environmental governances as "actions taken by non-governmental entities that are designed to achieve traditionally governmental ends such as managing the exploitation of common pool resources, increasing the provision of public goods, reducing environmental externalities, or more justly distributing environmental amenities."[9] Meanwhile, Light, in *The Law of the Corporation as Environmental Law*, rejects any notion of "a division of labor between firms and markets on the one hand, and public environmental law and regulation on the other."[10] "In light of the significant impact that firms can have on the environment . . . the law governing the corporation throughout its life cycle—corporate law, securities regulation, antitrust law, and bankruptcy law—should be understood as a fundamental part of environmental law."[11] Read together, private environmental governance and corporate law choices impacting the environment combine to create "sustainable business law" as a distinct legal discipline, or, at minimum, a component of environmental law—as "the future of environmental law will depend not upon traditional federal command-and-control legislation or executive branch maneuvering, but instead upon activating environmentalism through expanded substantive areas and innovative regulatory techniques that fall outside the existing, traditional norms of environmental law and legal scholarship."[12]

Accepting the existence of sustainable business law (like other emerging fields, such as food law) is a realization and acknowledgment "that these barriers to traditional environmental regulation have and will continue to force an expansion in the boundaries of environmental law and legal scholarship, and in our approaches to environmental regulation."[13] Todd Aagaard writes: "If it is to succeed in protecting human health and the environment, the environmental law of this new century may need to evolve into something that looks quite different from

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8 Michael P. Vandenbergh, *Private Environmental Governance*, 99 CORNELL L. REV. 129, 129 (2013). *See* Sarah E. Light & Michael P. Vandenbergh, *Private Environmental Governance*, *in* ENVIRONMENTAL DECISION MAKING, ENCYCLOPEDIA OF ENVIRONMENTAL LAW 253, 254 (Lee Paddock et al. eds., 2016), https://perma.cc/L5PW-ULJL?type=image (explaining that private environmental governance is important to environmental law and policy).

9 Vandenbergh, *Private Environmental Governance, supra* note 8, at 146.

10 Sarah E. Light, *The Law of the Corporation as Environmental Law*, 71 STAN. L. REV. 137, 140 (2019).

11 *Id.*

12 Jason J. Czarnezki & Sarah Schindler, *President Trump, the New Chicago School and the Future of Environmental Law and Scholarship*, *in* PERSPECTIVES ON ENVIRONMENTAL LAW SCHOLARSHIP: ESSAYS ON PURPOSE, SHAPE AND DIRECTION 195, 197 (Ole W. Pedersen ed., 2018).

13 *Id.*; *see* Cayleigh S. Eckhardt, *Pace Environmental Law Review 2015 Symposium: Reconceptualizing the Future of Environmental Law*, 32 PACE ENV'T L. REV. 379, 380–81 (2015) (explaining that the future of environmental law requires a multidisciplinary approach).

the extant environmental law canon."[14] Sustainable business looks quite different and is a viable part of the next generation of environmental laws as it can be implemented in an antagonistic political climate, is amenable to integration with other non-environmental law, and can make inroads against the monumental peril of global climate change.[15]

In recognition of the existence and potential of sustainable business law, this Article focuses on proactive rather than reactive[16] sustainable business initiatives that seek to avoid and mitigate environmental and social risk.[17] In doing so, Part II defines terms that are currently used in sustainable business: CSR, the three pillars of sustainability (environmental, social, and economic welfare), ESG, and the triple bottom line (people, profit, and planet) (TBL). Part III explores the role of the lawyer in promoting sustainable business. Part IV argues that corporate governance and finance provide the foundation for lawyers to successfully meet their obligations in fostering sustainable business practices. Part V concludes by tying together these theoretical and practical claims—that sustainable business law is part of the future of the environmental law canon with initial implementation by lawyers developing sustainable corporate governance and finance mechanisms.

II. DEFINING SUSTAINABLE BUSINESS

The private sector is pursuing a number of goals in the sustainability space, including, but not limited to, the Sustainable Development Goals (SDG), a low carbon economy, decarbonization, diversity and inclusion, employee engagement, long-term value, and innovation.[18] The list goes on. In response to consumer demand, to avoid financial risks, and in anticipation of the benefits of a greener future economy, businesses are pursuing these goals to take a proactive approach to mitigate environmental and social risk. But what exactly is a "sustainable business"? Sustainable business can be defined both formally (i.e., definitionally), as this Part seeks to do, and functionally (e.g., what is the goal of business and what actions can be taken to be more sustainable), as discussed in Parts III and IV. The terms used below are complex and vary in meaning depending on geography, jurisdiction, and context, and,

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14 Todd S. Aagaard, *Environmental Law Outside the Canon*, 89 INDIANA L. J. 1239, 1297 (2014).

15 *Id.*

16 By reactive, we mean activities in response to environmental law or engaging in environmental compliance and litigation. Proactive approaches anticipate and avoid risk.

17 *See, e.g.*, Stavros Gadinis & Amelia Miazad, *Corporate Law and Social Risk*, 73 VAND. L. REV. 1401, 1401–02 (2020) (arguing that through sustainability initiatives, companies are looking primarily for safeguards against downside risks).

18 SDGs are a blueprint that involves seventeen interconnected goals to achieve a better and more sustainable future for all. *Sustainable Development Goals*, UNITED NATIONS, https://perma.cc/Q7NE-YSTP (last visited Sept. 16, 2021).

as such, this Part merely offers a useful, while imperfect, primer on the terms often used when discussing sustainability in the business context.[19]

The term "sustainability" has been a buzzword for the past thirty years, yet there is still no precise, authoritative definition of the term,[20] although, "sustainability" and "sustainable development" are said to rest upon the three pillars of environmental, economic, and social welfare.[21] This lack of a precise definition has led to sustainability becoming a "container term"[22] and susceptible to greenwashing.[23] Furthermore, sustainability is often used interchangeably with ESG, CSR, or TBL, all three of which add an aspect of economic *viability* to the term (as opposed to economic *welfare* or *equality*), in addition to environmental and social considerations.[24]

In 1987, the World Commission on Environment and Development (the Brundtland Commission) defined sustainable development as "meet[ing] the needs of the present without compromising the ability of future generations to meet their own needs."[25] This definition draws on intergenerational equity, balancing resources usage and supplies over time.[26] Business sustainability has its roots in this definition, but due to the definition's focus on resources, many think it only pertains to

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[19] *See* Gerlinde Berger-Walliser & Inara Scott, *Redefining Corporate Social Responsibility in an Era of Globalization and Regulatory Hardening*, 55 AM. BUS. L.J., 167, 171 (2018) ("Researchers have noted that a particular challenge of studying CSR is finding commonality among the variety of definitions and contexts in which CSR is used. As one comprehensive review of CSR literature noted, the differences in the way the term is defined and the metrics used to assess it, often go 'beyond semantics to deeper construct-level differences . . . from philanthropy to ethics to safety issues to more composite measures assessed by external rating agencies.'").

[20] The use of the term began in the late 1980s after the release of the Brundtland Report. Brundtland Comm'n, Report of the World Commission on Environment and Development: Our Common Future (1987), https://perma.cc/R7VT-CWMT.

[21] *See, e.g.*, U.S. ENV'T PROT. AGENCY, *Sustainability Primer*, https://perma.cc/5USG-L3G6 (explaining the three pillars of sustainability); European Commission, *Sustainable Development* https://perma.cc/ZX72-ZSTT (explaining that sustainable development means meeting the needs of the present whilst ensuring future generations can meet their needs).

[22] Edmund A. Spindle, *The History of Sustainability: The Origins and Effects of a Popular Concept*, *in* SUSTAINABILITY IN TOURISM: A MULTIDISCIPLINARY APPROACH 9, 9–10 (Ian Jenkins & Roland Schroder eds., 2013).

[23] Jason J. Czarnezki & Katherine Fiedler, *The Neoliberal Turn in Environmental Regulation*, 2016 UTAH L. REV. 1, 37–38 (2016); *see* Jason Czarnezki et al., *Creating Order Amidst Food Eco-Label Chaos*, 25 DUKE ENV'T L. & POL'Y F. 281, 282, 302, 311 (2015) (discussing the concept of greenwashing and how the proliferation of eco-labels has contributed to greenwashing concerns); Jason J. Czarnezki et al., *Greenwashing and Self-Declared Seafood Eco-Labels*, 28 TULANE ENV'T L.J. 37, 37–38 (2014) (exploring the relationship between greenwashing and the rise of self-declared eco-labels for seafood products).

[24] *See, e.g.*, *The Difference Between Sustainability and ESG Policies*, ALVA, https://perma.cc/T26S-WX8M (last visited Oct. 18, 2021).

[25] World Comm'n on Env't and Dev., Rep. of the World Commission on Environment and Development: Our Common Future, 25, U.N. Doc. A/42/427, Annex (1987).

[26] Tima Bansal & Mark DesJardine, *Don't Confuse Sustainability with CSR*, IVEY BUS. J. (2015), https://perma.cc/QR7G-RJV5.

environmental issues.[27] However, this is an incorrect interpretation, sustainability relates to time.[28] Thus, business sustainability shifts the business's focus to the future and can be described "as a business strategy that creates long-term stakeholder value by addressing social, economic, and environmental opportunities and risks material to a company."[29]

Although sustainability and CSR are often used synonymously, the two should not be confused. CSR is "[a] responsibility among firms to meet the needs of their stakeholders and a responsibility among stakeholders to hold firms to account for their actions."[30] CSR focuses on the process a firm uses and the actions it takes to respond to its stakeholders' collective set of needs.[31] Importantly, Berger-Walliser and Scott argue that CSR is seen through one of two lenses—the lens of shareholder primacy, or CSR as a voluntary effort above and beyond any legal requirements.[32] Thus, CSR focuses on the *actions* a firm chooses to take (or not to take) based on shareholder interests, as voluntary activities undertaken by firms in environmental or social areas, or as an explicit moral, ethical, or social duty.[33]

Due to the frequent criticism from both organizations and scholars that companies merely use CSR as a public relations tool[34] rather than actually address non-financial issues, ESG has emerged as a metrics-based approach intended to increase corporate accountability.[35] Data collected from this approach can be used by companies to improve performance management as well as for external reporting purposes. The external reports can be used by investors and other stakeholders seeking to hold the company responsible for its actions. What is the difference between CSR and ESG to a company in regards to its environmental and social efforts? For example, in the interests of CSR, a company might announce an environmental initiative reducing its carbon footprint and increasing positive social impact. ESG would measure progress toward

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27 *Id.*

28 *Id.*

29 Joshua Cramer-Montes, *Sustainability: A New Path to Corporate and NGO Collaborations*, STAN. SOC. INNOVATION REV. (Mar. 24, 2017), https://perma.cc/6Y2Q-W455.

30 DAVID CHANDLER, STRATEGIC CORPORATE SOCIAL RESPONSIBILITY: SUSTAINABLE VALUE CREATION, at xx (Laureen Gleason et al. eds., 5th ed. 2020).

31 *Id.* at 6.

32 Berger-Walliser & Scott, *supra* note 19.

33 *Id.* at 171–83.

34 *See, e.g.*, CHRISTIAN AID, BEHIND THE MASK: THE REAL FACE OF CORPORATE SOCIAL RESPONSIBILITY 1–2, https://perma.cc/5W6N-B8VP (stating that CSR is "merely a branch of PR"); Angelica Petersson & Jasmin Dzafic, *Greenwashing in CSR Reports: A Case Study of Two Entities* 2–3 (2016) (M.A. thesis, Jonkoping University), https://perma.cc/H9BH-9FLQ; Privanka Aggarwal & Aarti Kadyan, *Greenwashing: The Darker Side of CSR*, 4 INDIAN J. APPLIED RSCH. 61, 63 (2014); Federica Balluchi et al., *CSR and Greenwashing: A Matter of Perception in the Search for Legitimacy*, *in* ACCOUNTING, ACCOUNTABILITY, AND SOCIETY: TRENDS AND PERSPECTIVES IN REPORTING, MANAGEMENT AND GOVERNANCE FOR SUSTAINABILITY 151, 152–53 (Mara Del Baldo et al. eds., 2020).

35 *See ESG: Key Trends in 2020 and Expectations for 2021*, SKADDEN, ARPS, SLATE, MEAGHER, & FLOM LLP (Feb. 1, 2021), https://perma.cc/3YXC-SHZD (explaining that ESG metrics help companies maintain accountability particularly with investors).

those goals.[36] CSR is a form of self-regulation representing a company's efforts to positively impact consumers, employees, the environment, etc.; whereas ESG focuses on metrics—assessing the company's actions and providing a system to ensure accountability.[37]

A sustainable business strategy requires a plan to create long-term value by managing both the business' financial and non-financial capital. To do this, a company must first identify the metrics it wants to measure, such as key performance indicators (KPIs), and then, using the knowledge gained from the data, craft strategies aimed at long-term growth.[38] This type of strategy uses ESG metrics to collect and benchmark performance and also helps satisfy a company's CSR responsibility. For example, ESG goals might include "Energy Efficiency" and "Waste Reduction," which requires KPIs that measure total energy consumption, waste production, and percentage of waste recycled.[39]

TBL, a term that has recently gained in popularity for its alliterative mnemonic of "people, planet and profit," is an accounting practice that aims to measure the economic, environmental, and social performance of a company over time.[40] By defining the TBL as an accounting framework, TBL encompasses both CSR and ESG. Like ESG, it calls for measuring actions, but it also incorporates CSR because, by using the TBL, a company fulfills its self-imposed responsibility to act positively by considering people and the planet when making business decisions. But, again, note here the divergence between the three pillars of sustainability and the TBL—economic equity and welfare versus profit.

III. DEFINING THE ROLE OF THE LAWYER

The traditional role of the business lawyer is that of either general counsel (GC) within a company or as a corporate lawyer with a private firm.[41] The GC role was once limited to reactive roles, such as overseeing

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36 For example, Unilever publishes an annual Sustainable Living Report that shows their ESG goals and their progress toward those goals, both positive and negative. UNILEVER SUSTAINABLE LIVING PLAN: PROGRESS IN 2019 (2019), https://perma.cc/8X7N-QRL7.

37 *What's the Difference Between CSR and ESG?*, ALVA (Oct. 27, 2020), https://perma.cc/6NEX-LNVQ; Peter Chadwick, *Understanding the ESG/CSR Value Chain*, INT'L EXEC. DEV. PROGRAM (Mar. 22, 2013), https://perma.cc/8H2E-T55Q; *Why ESG Is Replacing CSR—and What This Means to Your Business*, NPOWER BUS. SOLUTIONS (Apr. 26, 2020), https://perma.cc/HS9T-5CFU.

38 *See, e.g.*, DEP'T OF ENV'T, FOOD & RURAL AFFS., ENVIRONMENTAL KEY PERFORMANCE INDICATORS: REPORTING GUIDELINES FOR UK BUSINESS 4, 10, 12, 24–25 (2011), https://perma.cc/BH4Z-3J86 (providing guidance that KPIs help companies "communicate the links between environmental and financial performance").

39 *Id.* at 21, 27, 49–50.

40 ANDREW W. SAVITZ & KARL WEBER, THE TRIPLE BOTTOM LINE: HOW TODAY'S BEST-RUN COMPANIES ARE ACHIEVING ECONOMIC, SOCIAL, AND ENVIRONMENTAL SUCCESS–AND HOW YOU CAN TOO xiii (2006).

41 The scope of this Article is limited to business lawyers; however, lawyers practicing in other spaces also play a significant role in driving sustainable business law by steering

outside counsel during litigation.[42] However, this has changed in recent years. Now GCs and corporate lawyers engaged in corporate sustainability practice are key members of corporate decision-making teams: taking on proactive roles in corporate compliance, developing and implementing ESG programs, addressing risk management and corporate reputation issues, monitoring political landscapes in the corporation's operational jurisdictions, and "work[ing] with internal and external auditors and accountants to ensure that the appropriate due diligence is conducted prior to securing ESG-based financial commitments—and to develop control systems and checks to ensure that compliance is maintained throughout the lifecycle of financed projects."[43]

John Dernbach, in his 2017 article *Sustainable Development in Law Practice: A Lens for Addressing All Legal Problems*, assessed what lawyers who incorporate sustainable development into their law practice actually do, and their work varies considerably.[44] Their portfolios include work in "environmental law, climate change and clean energy law, corporate law, land use and development law, sustainable infrastructure finance, and corporate social responsibility and human rights," with a diverse client base of "developers, banks, multinational corporations, start-up businesses, nongovernmental organizations, and federal, state, and local governments."[45] Of note, "[t]hese [sustainability] lawyers also perform a wide variety of types of legal work–not only counseling clients but also performing transactional work, litigating, advocating, and drafting."[46]

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the way business lawyers counsel their clients. For example, lawyers at nongovernmental organizations (NGOs) like the Environmental Defense Fund, World Wildlife Fund, Amazon Action Network, Greenpeace, the Carbon Disclosure Project, the Marine Stewardship Council, Ceres, and World Resources Institute, just to name a few, drive sustainable business through disclosure programs, developing certification schemes, designing naming and shaming campaigns, creating voluntary standards, and providing thought leadership and policy suggestions. *See, e.g.*, *Influencing Policy*, ENV'T DEF. FUND, https://perma.cc/JB9W-TYNJ (last visited Sept. 17, 2021). Government lawyers also have a large effect on sustainable business law. *See What Attorney Generals Do*, NAT'L ASS'N OF ATT'Y GEN., https://perma.cc/HAD2-VR3V (last visited Sept. 17, 2021). Government lawyers can guide antitrust policy, disclosure standards, fiduciary duty standards, and make enforcement decisions. *Id.* Exploring the role of NGO and government lawyers with respect to sustainable business law is a topic worthy of its own article.

[42] Elaine McArdle, *In the Driver's Seat: The Changing Role of the General Counsel*, HARV. L. TODAY (July 1, 2012), https://perma.cc/5ALZ-37F3.

[43] *See* ASS'N OF CORP. COUNSEL., ROLE OF THE GENERAL COUNSEL 7–8 (2009), https://perma.cc/YE6L-RF2Y (describing the wide variety of high-level roles and responsibilities held by the modern GC); Jillian C. Kirn & Bernadette M. Rappold, *Considering ESG? Three Ways Lawyers Can Help*, BLOOMBERG LAW (Jan. 27, 2021), https://perma.cc/T2LE-PCT7 (explaining the growing acceptance of ESG as an important measure of corporate success and having well-versed lawyers as critical to ensuring ESG measures are properly implemented).

[44] John C. Dernbach, *Sustainable Development in Law Practice: A Lens for Addressing All Legal Problems*, 95 DENVER L. REV. 123, 131–32 (2017).

[45] *Id.*

[46] *Id.* at 132.

A future project for scholars to expand upon Dernbach's work is to explore the organization and workload of corporate sustainability groups within law firms to confirm the current view that when it comes to corporate sustainability, lawyers are well-positioned and equipped to increase the focus on sustainability within their organization.[47] The United Nations (UN) Global Compact,[48] the basis on which firms advise businesses on corporate sustainability, suggests ten principles that companies should incorporate into their value systems.[49] The principles are derived from previous declarations and conventions, including the Universal Declaration of Human Rights,[50] the International Labour Organization's Declaration on Fundamental Principles and Rights at Work,[51] the Rio Declaration on Environment and Development,[52] and the UN Convention Against Corruption.[53] The Ten Principles touch on four areas of law that companies should strive to be responsible in: human rights, labor, environmental, and anti-corruption.

Since 2015, Linklaters LLP has worked with the UN Global Compact to create a guide for GCs on corporate sustainability, incorporating the Ten Principles.[54] The guide identifies five areas where GCs can work to embed sustainability into their organization's DNA (each having internal and external implications): corporate sustainability and business integrity, corporate sustainability and fiduciary duties, human rights and supply chain diligence, corporate sustainability and grievance

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47 U.N. GLOBAL COMPACT ET AL., GUIDE FOR GENERAL COUNSEL ON CORPORATE SUSTAINABILITY 6 (2019), https://perma.cc/ER2F-GUYN.

48 This organization "aim[s] to mobilize a global movement of sustainable companies and stakeholders." *Our Mission*, U.N. GLOBAL COMPACT, https://perma.cc/XXN6-9LQN (last visited Oct. 9, 2021).

49 *The Ten Principles of the UN Global Compact*, U.N. GLOBAL COMPACT, https://perma.cc/9YV4-U2NK (last visited Oct. 9, 2021).

50 *See* G.A. Res. 217 A (III), Universal Declaration of Human Rights. Arts. 1, 3, 28–30 (Dec. 10, 1948) (providing the basis for the proposition that businesses should support and respect the protection of internationally proclaimed human rights and ensure they are not complicit in human rights abuses).

51 *See* Int'l Lab. Or. [ILO], *ILO Declaration on Fundamental Principles and Rights at Work and Its Follow-Up*, at 7 (June 18, 1998) (providing the basis for the proposition that businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining, the elimination of all forms of forced and compulsory labor, the effective abolition of child labor, and the elimination of discrimination in respect of employment and occupation).

52 *See* U.N. Conference on Environment and Development, *Rio Declaration on Environment and Development*, ¶ 7–9 U.N. Doc. A/CONF.151/26/Rev.1 (Vol. I), annex I (Aug. 12, 1992) (providing the basis for the proposition that businesses should support a precautionary approach to environmental challenges, undertake initiatives to promote greater environmental responsibility, and encourage environmentally friendly technologies).

53 *See* G.A. Res. 58/4, ¶ 12, 21–22, United Nations Convention Against Corruption (Oct. 31, 2003) (providing the basis for the proposition that businesses should work against corruption in all its forms, including extortion and bribery).

54 U.N. GLOBAL COMPACT ET AL., *supra* note 47, at 2.

mechanisms, and challenges to corporate sustainability—managing a crisis.[55]

For business integrity, many organizations strive to do the right thing, not just what is required by law.[56] This has only been accelerated as more stakeholders demand that a corporation adopt CSR and sustainable business practices.[57] Corporate lawyers can work to create values-based compliance programs that move beyond legal compliance to embed business integrity into the organizational culture.[58] They can then work with those from the top to set the tone, create internal controls, measure performance, and create grievance mechanisms.[59] Lawyers are now in a good position to assist in creating grievance mechanisms because of their understanding of judicial processes and understanding that issues can escalate into legal risks quickly if not addressed appropriately.[60]

More stakeholders are demanding consideration of ESG issues, and more voluntary standards and purpose statements are arising that move away from the traditional norm of profit maximization toward a multistakeholder model.[61] Lawyers provide important advisory information to the board, monitor for incoming regulatory changes and industry-led initiatives, formulate ESG policies, and create ESG governance frameworks—though U.S. corporate boards may lack sufficient ESG expertise.[62]

Stakeholders are intensifying scrutiny on corporate supply chains, and issues such as poor working conditions and human rights violations expose organizations to reputational risk. Lawyers assist with mapping suppliers, analyzing operational jurisdictions for changes to hard and soft law relating to human rights and other sustainability issues, and assist with due diligence on those suppliers or jurisdictions that are deemed high risk.[63]

Lastly, for managing a crisis, lawyers play an important role in gathering relevant facts and evidence, identifying key issues, and

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55 *Id.* at 6.

56 *Id.* at 11.

57 *See id.* (describing increasing concerns over organizations' integrity and transparency on the part of investors, employees, clients, and consumers are driving corporations to take CSR more seriously).

58 *Id.* at 11–12.

59 *See generally id.* at 12–15 (describing the "tone from the top" method for fostering a corporate culture of integrity and responsibility, where senior business leaders drive messaging around company values, create policies and procedures that reflect those values, establish methods for assessing the effectiveness of the initiative, and implement whistle-bower and grievance mechanisms in the event of misconduct or unethical business practices).

60 *Id.* at 37–39.

61 *Id.* at 19.

62 TENSIE WHELAN, U.S. CORPORATE BOARDS SUFFER FROM INADEQUATE EXPERTISE IN FINANCIALLY MATERIAL ESG MATTERS 2, 3 (2021), https://perma.cc/ZE4U-YPU3.

63 U.N. GLOBAL COMPACT ET AL., *supra* note 47, at 29–34.

balancing the tone of the initial press releases.[64] Next, the GCs, in particular, play a key role in conducting an investigation and reporting to the board.[65] The GC should encourage transparency to help maintain and achieve goodwill by the organization adopting a culture of sustainability.[66]

Although corporate sustainability and risk management lawyers—whether as GCs or outside counsel—can be involved in almost every aspect of sustainability within a company (such as marketing, taxation, supply chain management, risk management, information management, and many others), they are most often involved with roles falling within the two categories of corporate governance and corporate finance. The following Part IV provides an overview of the lawyer's role within these two functions of the business as they relate to sustainability.

IV. ACHIEVING SUSTAINABILITY THROUGH CORPORATE GOVERNANCE AND FINANCE

Improved corporate governance mechanisms and more thoughtful consideration of corporate finance are the foundation for building sustainable businesses. The board of directors, and the lawyers advising them, have a fiduciary duty to consider social and environmental risks and benefits. This Part discusses topics, both internal and external to the company, that lawyers deal with in achieving sustainable corporate governance (Part IV.A.) and finance (Part IV.B), as well as the emerging demands now being placed upon lawyers to proactively consider and implement practices that account for and disclose social, welfare, and environmental harm (Part IV.C).

A. Corporate Governance and Sustainability

This Part focuses on corporate governance mechanisms that impact sustainability, such as ESG metrics, KPIs, climate risk management, accounting, and capital valuation. First, Part IV.A.1. discusses the board of directors' fiduciary duty to the business and lawyers advising on this duty, which provides the foundation for considering sustainability interests in corporate governance.[67]

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64 *Id.* at 43–44.

65 *Id.* at 44.

66 *Id.* at 45–46.

67 *See* Lisa Benjamin, *The Road to Paris Runs Through Delaware: Climate Litigation and Directors' Duties*, 2 UTAH L. REV. 313, 355–56 (2020) (identifying "duty of care" and "duty of loyalty" as legal standards directors need to meet under their fiduciary obligations to an organization).

1. Fiduciary Duty and Sustainability

While historically it was said that for-profit company directors must consider how to best achieve wealth maximization for shareholders,[68] directors have sufficient flexibility while fulfilling their fiduciary duties to incorporate social enterprise approaches (e.g., considering benefits to society and the environment in addition to profit)—approaches with a longer-term perspective that consider the opportunities and benefits from energy transitions and sustainability metrics.[69] In fact, the Business Roundtable has endorsed the view of "stakeholder capitalism," whereby companies should be led for the benefit of all stakeholders—customers, employees, suppliers, communities, and shareholders.[70] Signed by 181 Chief Executive Officers (CEOs), the Business Roundtable Statement on the Purpose of a Corporation reads in part:

> While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders. We commit to:
>
> - Delivering value to our customers. We will further the tradition of American companies leading the way in meeting or exceeding customer expectations.
>
> - Investing in our employees. This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect.

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68 *See, e.g.*, Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAGAZINE, Sept. 13, 1970, at 32, 33 (asserting that a corporate executive "has direct responsibility to his [shareholders] . . . to make as much money as possible").

69 *See, e.g.*, Benjamin, *supra* note 67, at 363, 368 ("[C]orporate law provides sufficient flexibility . . . to consider what is best for shareholders in the long term, and can incorporate social enterprise approaches that consider shareholder wealth maximization. . . . [A]ssessing climate risk is not only consistent with but is now a prerequisite to the maximization of wealth.").

70 *Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans'*, BUS. ROUNDTABLE (Aug. 19, 2019), https://perma.cc/M4FV-CC77; Geoff Colvin, *Revisiting the Business Roundtable's 'Stakeholder Capitalism', One Year Later*, FORTUNE (Aug. 19, 2020), https://perma.cc/2BXJ-LS56; *see generally* WORLD ECON. F., MEASURING STAKEHOLDER CAPITALISM: TOWARDS COMMON METRICS AND CONSISTENT REPORTING OF SUSTAINABLE VALUE CREATION 3 (2020), https://perma.cc/V44Q-XC54 ("[D]efining a core set of 'Stakeholder Capitalism Metrics' (SCM) and disclosures that can be used . . . [for] mainstream reporting on performance."). *See also* John C. Coffee, *The Future of Disclosure: ESG, Common Ownership, and Systematic Risk* ii, 40 (European Corp. Governance Inst., Working Paper No. 541/2020, 2021), https://perma.cc/5XWG-Q9RT (exploring "the desire of institutions for greater ESG disclosures" from a perspective that endorses avoiding "risks that could depress the entire economy" instead of "subordinating economic returns to social welfare").

- Dealing fairly and ethically with our suppliers. We are dedicated to serving as good partners to the other companies, large and small, that help us meet our missions.

- Supporting the communities in which we work. We respect the people in our communities and protect the environment by embracing sustainable practices across our businesses.

- Generating long-term value for shareholders, who provide the capital that allows companies to invest, grow and innovate. We are committed to transparency and effective engagement with shareholders.

> Each of our stakeholders is essential. We commit to deliver value to all of them, for the future success of our companies, our communities and our country.[71]

In conjunction with this forward-thinking view of the purpose of the company, to comply with their fiduciary duties under the law, directors must identify and assess climate risks and their financial implications.[72] The fiduciary duties of loyalty and prudence/care, protected by the business judgment rule, require the incorporation of ESG issues.[73] ESG issues are financially material, and policy and regulatory frameworks are changing to require ESG incorporation,[74] mandating the development of guidance for good climate and environmental governance.[75]

Fiduciary duties not only require company directors to manage sustainability performance, but also fiduciary investors that manage other peoples' money must consider ESG risks in investments and portfolio construction. Similar to the fiduciary duties of board members, the fiduciary duties of fiduciary investors do not prevent them from considering environmental and social factors, nor will portfolios suffer financially when investors engage in sustainable or responsible or social impact investing.[76] In fact, some businesses are becoming "benefit

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71 *Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans'*, *supra* note 70.

72 Benjamin, *supra* note 67, at 319, 363, 368.

73 Janet E. Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board's Decision to Engage in Social Entrepreneurship*, 29 CARDOZO L. REV. 623, 634 (2007).

74 *Fiduciary Duty in the 21st Century*, U.N. ENV'T PROGRAMME FINANCE INITIATIVE, https://perma.cc/4MFQ-6GYS (last visited Sept. 21, 2021); *see Fiduciary Duty*, PRINCIPLES FOR RESPONSIBLE INV., https://perma.cc/3R6D-UJBW (last visited Sept. 21, 2021) ("Fiduciary duty requires investors to incorporate all value drivers, including environmental, social, and governance (ESG) factors, in investment decision making.").

75 WORLD ECON. F., HOW TO SET UP EFFECTIVE CLIMATE GOVERNANCE ON CORPORATE BOARDS: GUIDING PRINCIPLES AND QUESTIONS 6 (2019), https://perma.cc/9YG7-5BDV.

76 Susan N. Gary, *Best Interests in the Long Term: Fiduciary Duties and ESG Integration*, 90 U. COLO. L. REV. 731, 796–98 (2019).

corporations" to consider social responsibility,[77] often certified by a third party.[78] The UN Environmental Programme Finance Initiative has gone as far as to say that "[i]nvestors who fail to incorporate ESG issues are failing their fiduciary duties and are increasingly likely to be subject to legal challenges."[79]

As discussed below, achieving sustainability through corporate governance requires 1) improved accounting mechanisms, 2) a better understanding of available capital, and 3) proper risk management in light of climate effects and environmental degradation. These three basic foundations link to suggested principles to set up effective climate governance on corporate boards, as they support ensuring the sustainability and climate knowledge base and continual learning within the board, oversight of executives, and improved organizational structure and reporting.[80]

To accurately manage the financial costs and benefits through the lens of sustainability, firms can engage in "true cost accounting," "life cycle costing," or "impact valuation"—similar practices that account for the economic, environmental, and social externalities generated by products and services.[81] A product's life cycle includes the extraction of raw materials used to make goods, production and manufacturing, packaging, distribution, use, and disposal.[82] Accounting is used in the public procurement context in the European Union (EU), which now permits—explicitly using the term "life-cycle costing" in the legislation—the consideration of environmental and social factors, as opposed to just lowest prices, when determining the cost of a good.[83] This accounting can be integrated into private procurement mechanisms.

An example of modern accounting techniques to quantitatively measure externalities is greenhouse gas emissions accounting, which measures:

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77 Miriam F. Weismann, *The Missing Metrics of Sustainability: Just How Beneficial Are Benefit Corporations?*, 42 DEL. J. CORP. L. 1, 10–11 (2017).

78 *See, e.g.*, *Certified B Corporation*, B LAB, https://perma.cc/YL98-CQ2U (last visited Oct. 9, 2021).

79 *Fiduciary Duty in the 21st Century*, *supra* note 74.

80 *See* WORLD ECON. F., HOW TO SET UP EFFECTIVE CLIMATE GOVERNANCE ON CORPORATE BOARDS: GUIDING PRINCIPLES AND QUESTIONS, *supra* note 75 (laying out eight guiding principles that corporate boards can use to guide the development of better climate governance).

81 *See, e.g.*, Katherine Fiedler et al., *Life Cycle Costing and Food Systems: Concepts, Trends, and Challenges of Impact Valuation*, 8 MICH. J. ENV'T & ADMIN. L. 1, 5 (2018) (explaining that quantifying all of the environmental, social and health costs of food systems through impact valuation can help lessen their impacts and create sustainability); STEVEN LORD, VALUING THE IMPACT OF FOOD: TOWARDS PRACTICAL AND COMPARABLE MONETARY VALUATION OF FOOD SYSTEM IMPACTS ii (2020), https://perma.cc/NG7F-WSVG (stating that economic valuation and true cost accounting methodologies better inform policy and economic decisions that support the growth of sustainable food systems).

82 Jason J. Czarnezki, Green Public Procurement: Legal Instruments for Promoting Environmental Interests in the United States and European Union 11 (Dec. 13, 2019) (LL.D. Dissertation, Uppsala University) (SSRN).

83 *Id.* at 132.

- Scope 1 emissions: direct emissions from owned or controlled sources;
- Scope 2 emissions: indirect emissions from the generation of purchased electricity, steam, heating and cooling consumed by the reporting company; and
- Scope 3 emissions: all other indirect emissions that occur in a company's value chain.[84]

But externalities are not the only costs and benefits that must be measured. Various types of capital can be considered to fall under corporate governance accounting methods because the board or management must choose to measure and manage this capital, set goals, and use the data to drive strategy (though Chief Financial Officers (CFOs) and internal finance teams actually do the measuring and reporting).[85] Capital assets include:

> - [N]atural capital: the limited stocks of physical and biological resources found on earth, and of the limited capacity of ecosystems to provide ecosystem services;
> - [P]roduced capital: all manufactured capital, such as buildings, factories, machinery, physical infrastructure (roads, water systems), as well as all financial capital and intellectual capital (technology, software, patents, brands, etc.);
> - [S]ocial capital: encompasses networks, including institutions, together with shared norms, values and understandings that facilitate cooperation within or among groups;
> - [H]uman capital: the knowledge, skills, competencies and attributes embodied in individuals that facilitate the creation of personal, social and economic well-being[; and]
>
> . . .
>
> - Financial capital: ownership of financial value (assets such as stocks, deposits, bonds, etc.) that can produce, of itself, value flows. Some financial assets derive financial value form association to other capitals (stocks represent financial value of produced capital, derivatives are linked to physical commodities, etc.). Quality of financial capital can include return rate and risk. Financial capital changes can result in changes in financial value and, through impact, changes in economic value.[86]

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[84] *Scope 1 and Scope 2 Inventory Guidance*, U.S. ENV'T PROT. AGENCY, https://perma.cc/Y4A6-BVTU (last visited Sept. 20, 2021); *Scope 3 Inventory Guidance*, U.S. ENV'T PROT. AGENCY, https://perma.cc/Q2W3-FVBP (last visited Sept. 20, 2021).

[85] Lynn S. Paine & Suraj Srinivasan, *A Guide to the Big Ideas and Debates in Corporate Governance*, HARV. BUS. REV. (Oct. 14, 2019), https://perma.cc/YG6R-6UQQ.

[86] LORD, *supra* note 81, at 9–11. *See also What is Social Capital? Definition and Meaning*, MKT. BUS. NEWS, https://perma.cc/SLG4-R28T (last visited Oct. 5, 2021) (explaining the definition of social capital); *What is Natural Capital?,* WORLD F. ON NAT. CAP., https://perma.cc/WXJ6-N2FA (last visited Oct. 5, 2021) (defining natural capital and

Directors and management must also engage in sustainability risk assessment and management. The impending threat of a worsening climate crisis provides a strong case for boards to embed sustainability in their risk management program.[87] Doing so offers a systemic approach to the management of ESG performance, allowing directors and management to embed sustainability-related priorities in their business models and value chains.[88]

Directors can use an iterative six-step approach to gain insight on integrating sustainability and stakeholder expectations into long-term strategy and governance.[89] The first step involves scanning various areas of the corporate strategy, such as value drivers, the internal and external environments, value propositions, profitability, and governance.[90] The second step suggests that directors view their value drivers (e.g., mission, vision, values, goals, and results) through an SDG lens.[91] With this view, directors should be able to identify potential risks, such as transition[92] and physical risks,[93] and opportunities, such as resource efficiency, renewable energy, low carbon innovation, new markets, product development, and resiliency.[94] To consider how these risks and opportunities may evolve, directors should use scenario analysis to understand potential implications under possible future states.[95]

After scanning the corporate strategy using an SDG lens and identifying risks and opportunities, directors can then develop a response design in areas such as risk capacity, mitigation strategy, change management, business continuity, capacity building, and partnership

ecosystem services); *Natural Capital Protocol*, CAPS. COALITION, https://perma.cc/LBR9-H4BJ (last visited Oct. 6, 2021) (explaining how natural capital can impact risk mitigation for businesses); BLOWFEILD, *supra* note 2, at 29 (illustrating the relationship between the different types of capital).

87 *See generally* TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES, FINAL REPORT: RECOMMENDATIONS OF THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES ii–iii (2017) [hereinafter TCFD RECOMMENDATIONS], https://perma.cc/4AAB-R5GS (explaining that the potential impacts of climate change will impact organizations in the short term because the widespread transition to a lower-carbon economy will affect most economic industries, and investments in activities that do not have long term viability because of worsening climate change will not provide long term returns).

88 DELOITTE, SUSTAINABILITY RISK MANAGEMENT: POWERING PERFORMANCE FOR RESPONSIBLE GROWTH 9 (2019), https://perma.cc/8LBZ-8A3W.

89 *Id.* at 12.

90 *Id.*

91 *Id.* at 13.

92 Risks associated with the transition to a low-carbon economy include policy and legal risks, technology risk, market risk, and reputation risk. TCFD RECOMMENDATIONS, *supra* note 87, at 5–6.

93 Physical risks resulting from climate change can be acute risks, which are event driven (e.g., hurricanes), or chronic risks, which are longer-term shifts in climate patterns (e.g., sustained higher temperatures). *Id.* at 6.

94 *Id.* at 6–7.

95 *Id.* at 25. "Scenario analysis is a process for identifying and assessing the potential implications of a range of plausible future states under conditions of uncertainty." *Id.*

mobilization.[96] Designs should seek outcomes that deliver four types of value: value creation, value protection, value for people, and value for money.[97] Lastly, directors should implement controls that assure achievement of the outcomes, such as measurement and reliable reporting.[98]

Directors of companies, as well as investment managers, have a fiduciary duty to manage the firm/portfolio in the best interests of their shareholders, clients, and perhaps all stakeholders. As sustainability risk becomes more evident every day, fiduciary duties require directors to embed sustainability priorities throughout their organization and manage ESG performance, and require investment managers to consider ESG factors in their investment decision-making.[99] Directors that fail to embed sustainability priorities risk being ousted by shareholders, as was seen at Exxon in 2021.[100] Lawyers have an obligation to advise their clients about this duty and can help decide the best ways to implement sustainability strategies. An important avenue for implementation is through an organization's corporate finance team.

B. Corporate Finance and Sustainability

Corporate finance is the function of the firm that deals with its capital structure, the purpose of which is to maximize the value of the business.[101] Three important activities govern corporate finance: investments and capital budgeting,[102] capital financing,[103] and dividends and return on capital.[104] The debt to equity ratio often determines how risky a company's capital financing is—while more debt potentially creates a larger risk for stakeholders, it is often a primary reason for a company's growth and success.[105]

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96 *Id.* at 13.

97 *Id.*

98 *Id.* at 12.

99 *Id.* at 3.

100 *See* Alastair Marsh & Saijel Kishan, *Engine No. 1's Exxon Win Provides Boost for ESG Advocates*, BLOOMBERG GREEN (May 27, 2021), https://perma.cc/7BNE-4LW4 (reporting on the successful effort led by Engine No. 1, a small hedge fund, to reject Exxon Mobil's management team and install new board members to diversify beyond oil).

101 *Corporate Finance Overview: An Overview of the Corporate Finance Industry*, CORP. FIN. INST., https://perma.cc/34J5-4MTZ (last visited Sept. 19, 2021).

102 Investing and capital budgeting is the process of "planning where to place the company's long-term assets in order to generate the highest risk-adjusted returns." *Id.*

103 Capital financing involves determining the optimal debt and equity mix to finance capital investments, which may involve selling company stock or issuing debt. *Id.*

104 Dividends and return on capital are the processes of determining whether to use retained earnings to fund a capital investment or to return excess capital to shareholders via dividends or share buybacks. *Id.*

105 *Id.*

Corporate finance decisions are made by senior management, primarily the CFO and CEO.[106] However, lawyers play a vital role in these decisions.[107] GCs act as one of the primary CEO counselors, and when aligned properly with the CFO, can be a crucial player in implementing a firm's core strategy.[108] Outside counsel, on the other hand, assists firms with a wide array of corporate finance matters, such as drafting disclosure documents, conducting transaction due diligence, and assisting with structuring the deal or offering.[109] However, the knowledge base required to appropriately manage risk and identify business opportunities is quickly expanding.

The evolution of corporate sustainability and the meteoric rise of ESG metrics in the investor community (which has only increased because of the COVID-19 pandemic)[110] has forced lawyers to reevaluate their role in managing a firm's risks, particularly in the corporate finance space.[111] Business lawyers can no longer be reactive to sustainability issues; rather, they must take a proactive role in integrating sustainability risks and opportunities into the business.[112]

As boards begin to manage sustainability risks as required by their fiduciary duty, they can look to their corporate finance teams—and the lawyers that work with them—to carry out initiatives that manage these risks. This Part explores the disclosure of sustainability information in mandatory reports required under securities laws, the rise of voluntary reporting, and the rapidly expanding field of sustainable finance.

1. Sustainability Disclosure in the U.S.

a. Mandatory Reporting

As the primary regulator of U.S. federal securities law, the SEC is tasked with "protect[ing] investors" and "maintain[ing] fair, orderly, and efficient markets."[113] To achieve this, the SEC requires public companies "to regularly disclose significant financial and other information so investors have the timely, accurate, and complete information they need to make confident and informed decisions about when or where to

106 Ben W. Heineman, Jr., *How the CFO and General Counsel Can Partner More Effectively*, HARV. BUS. REV. (July 25, 2016), https://perma.cc/82Z3-D4LA.

107 *Id.*

108 *Id.*

109 Jennifer B. Ezring, *The Life of a Corporate Finance Attorney*, CHAMBERS ASSOC., https://perma.cc/KE9Q-DGGM (last visited Oct. 9, 2021).

110 *Why COVID-19 Could Prove to be a Major Turning Point for ESG Investing*, J.P. MORGAN (July 1, 2020), https://perma.cc/2V3S-ZD3B.

111 Natasha Luther-Jones et al., *How General Counsel and Lawyers Must Help Deliver Sustainability and ESG Outcomes* (Dec. 3, 2020), https://perma.cc/JE9F-HYKP.

112 *Id.*

113 *About the SEC*, U.S. SEC. & EXCH. COMM'N, https://perma.cc/F44E-PS7E (last updated Nov. 22, 2016).

invest."[114] One way in which the SEC achieves this is by requiring public companies to submit annual Form 10-K reports, which require those companies to provide an overview of their business and financial condition, and to disclose material risks and information to investors.[115]

To determine materiality, courts use the reasonable investor standard: whether a reasonable investor would consider the disclosure important in making decisions;[116] the SEC adopted an almost identical definition.[117] When regulating materiality, the SEC uses some prescriptive and line-item disclosure requirements but also uses a principles-based approach, "which articulate[s] an objective and allow[s] companies to satisfy the objective by providing disclosure appropriately tailored to their facts and circumstances."[118] Despite the flexibility that the principles-based approach provides, it is not without its critics, especially when applied to climate change and ESG disclosure.[119]

Beginning in the late 1960s and early 1970s, the SEC began to address demands from investors for mandatory environmental and social disclosures but ultimately denied those demands because the SEC believed those types of disclosures would be of little use to investors and burdensome for issuers.[120] A subsequent SEC advisory committee endorsed those findings and recommended that the SEC only classify environmental and social disclosures as material "when it reflects significantly on the economic and financial performance of the Company."[121]

Between 2007 and 2009, investors filed various rulemaking petitions demanding the adequacy of climate change disclosures.[122] The SEC responded with interpretive guidance advising that some issues relating

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[114] *What We Do*, U.S. SEC. & EXCH. COMM'N, https://perma.cc/YD2J-6Z99 (last visited Oct. 9, 2021).

[115] *How to Read a 10-K/10-Q*, U.S. SEC. & EXCH. COMM'N, https://perma.cc/V426-BFQP (last visited Sept. 17, 2021).

[116] TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976).

[117] 17 C.F.R. §§ 230.405, 240.12b-2 (2020).

[118] William Hinman, Dir., Div. of Corp. Fin., U.S. Sec. Exch. Comm'n, The Regulation of Corporate Finance—A Principles-Based Approach (Nov. 18, 2020), https://perma.cc/43LJ-KRZW.

[119] LEE REINERS & CHARLIE WOWK, CLIMATE RISK DISCLOSURES & PRACTICES: HIGHLIGHTING THE NEED FOR A STANDARDIZED REGULATORY DISCLOSURE FRAMEWORK TO WEATHER THE IMPACTS OF CLIMATE CHANGE ON FINANCIAL MARKETS 27, https://perma.cc/NNM7-MT7A; Anthony Alden & Matthew Hosen, *Climate Change SEC Financial Disclosures: Will New Rules Come with a New President?* JDSUPRA (Dec. 18, 2020), https://perma.cc/D8HQ-3V72.

[120] Disclosure of Environmental and Other Socially Significant Matters, 40 Fed. Reg. 7013 (Feb. 18, 1975); Environmental and Social Disclosure, 40 Fed. Reg. 51,656 (Nov. 6, 1975) (codified at 17 C.F.R. pts. 239–40, 249). An "'issuer' means every person who issues or proposes to issue any security." 15 U.S.C § 77b(a)(4) (2018).

[121] Business and Financial Disclosure Required by Regulation S-K, 81 Fed. Reg. 23,916, 23,971 n.687 (Apr. 22, 2016) (codified at 17 C.F.R. pts. 210, 229–30, 232, 239–40, 249).

[122] California Public Employees' Retirement System et al., Petition for Interpretive Guidance on Climate Risk Disclosure before the United States Securities and Exchange Commission 2 (Sept. 18, 2007), https://perma.cc/6KMU-A2TT.

to climate change may have significant financial impacts and are thus material.[123] The SEC stated that four Items within Regulation S-K could trigger climate disclosures: Items 101 (Description of Business), 103 (Legal Proceedings), 303 (Management's discussion and analysis of financial condition and results of operations), and 503(c) (now 105).[124] The guidance provided four business factors that management should consider under these Items: 1) the impact of legislation and regulations; 2) international accords; 3) the indirect consequences of regulations on business trends; and 4) the physical impacts of climate change.[125] As guidance, however, this only clarified obligations under existing law rather than created prescriptive climate disclosure requirements.

By not creating prescriptive requirements and sticking with a principles-based approach, few new issuers began reporting on material climate change risks, and SEC enforcement was brief.[126] Petitioners were not satisfied with the progress and continued making demands for prescriptive regulations, and the SEC, in 2016, published a concept release that sought public comment on whether the SEC should consider sustainability-related line-item disclosures, as well as materiality standards for sustainability issues.[127]

The 2016 Concept release was never acted upon, even as the SEC worked on modernizing Regulation S-K. On November 9, 2020, amendments to Regulation S-K became effective.[128] Despite this rule being an opportune time to satisfy investor demands and improve sustainability disclosures, the final rule was passed with minimal ESG requirements.[129] The vote to approve this final rule was made along party lines, with the two Democratic dissenting Commissioners making statements that the rule was a lost opportunity to create a mandatory reporting framework for ESG issues.[130] Aside from the addition of human

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123 Commission Guidance Regarding Disclosure Related to Climate Change, 75 Fed. Reg. 6290, 6292–93 (Feb. 8, 2010) (codified at 17 C.F.R. pts. 211, 231, 241) [hereinafter 2010 Climate Guidance].

124 *Id.* at 6293–94. Item 503(c) is now empty and reserved. Risk Factors moved to Item 105 under the FAST Act in 2019. FAST Act Modernization and Simplification of Regulation S-K, 84 Fed. Reg. 12,674, 12,688–89 (Apr. 2, 2019) (codified at 17 C.F.R. pts. 229–30, 232, 239–40, 249, 270, 274–75).

125 2010 Climate Guidance, 75 Fed. Reg. at 6290–91.

126 JIM COBURN & JACKIE COOK, COOL RESPONSE: THE SEC & CORPORATE CLIMATE CHANGE REPORTING 11, 25 (2014), https://perma.cc/DX99-VNDN.

127 Business and Financial Disclosure Required by Regulation S-K, 81 Fed. Reg. 23,916, 23,926 (Apr. 22, 2016) (codified at 17 C.F.R. pts. 210, 229–30, 232, 239–40, 249).

128 Modernization of Regulation S-K Items 101, 103, and 105, 85 Fed. Reg. 63,726 (Oct. 8, 2020) (codified at 17 C.F.R. pts. 229, 239–40).

129 The rule added human capital disclosure requirements (the "S" of ESG), such as the disclosure of human capital resources and any measurements or objectives used to manage them. Colin P. Myers & Thomas A. Utzinger, *SEC Amends Regulation S-K Disclosure Rules with Minimal ESG Requirements*, AM. BAR ASS'N, SECTION OF ENV'T, ENERGY, & RES. (Dec. 15, 2020), https://perma.cc/9QY6-2K8B.

130 Caroline Crenshaw, Comm'r, U.S. Sec. Exch. Comm'n, Statement on the "Modernization" of Regulation S-K Items 101, 103, and 105, (Aug. 26, 2020), https://perma.cc

capital disclosure, there was little progress in addressing ESG issues (and even some backtracking) during the Trump administration.[131]

However, since the start of the Biden administration, the SEC has taken a flurry of actions to address ESG issues. On February 24, 2021, then Acting Chair Lee issued a public statement on the review of climate-related financial disclosure.[132] The review aims to assess "the extent to which public companies address the topics identified in the 2010 [Climate Guidance], assess compliance with disclosure obligations under the federal securities laws, engage with public companies on these issues, and absorb critical lessons on how the market is currently managing climate-related risks."[133] The SEC intends to use the insights gained "from this work to begin updating the 2010 [Climate Guidance] to take into account developments in the last decade."[134] On March 15, 2021, then Acting Chair Lee released a public statement welcoming public input on climate change disclosures.[135]

Other recent actions taken by the SEC with regard to ESG-related issues include the Division of Examinations' enhanced focus on climate-related risks in its 2021 exam priorities,[136] the creation of a Climate and ESG Task Force within the Division of Enforcement,[137] the issuance of an investor bulletin on ESG funds,[138] and the appointment of a Senior Policy Advisor for Climate and ESG.[139] All of these actions (and any future actions) are now included in new a link on the SEC's homepage titled "SEC Response to Climate and ESG Risks and Opportunities."[140]

With Democratic control of Congress and a Democratically controlled SEC, some mandatory form of ESG reporting might arise.[141] This could

/9Q26-R2N6; Allison Herren Lee, Comm'r, U.S. Sec. Exch. Comm'n, Regulation S-K and ESG Disclosure: An Unsustainable Silence (Aug. 26, 2020), https://perma.cc/9Q26-R2N6.

131 *See* Allison Herren Lee, Comm'r, U.S. Sec. Exch. Comm'n, Statement on the Amendments to Rule 14a-8 (Sept. 23, 2020), https://perma.cc/6LD9-N2PG (stating the amendment will dial back shareholder oversight of company management and undermine ESG initiatives).

132 Allison Herren Lee, Acting Chair, U.S. Sec. Exch. Comm'n, Statement on the Review of Climate-Related Disclosure (Feb. 24, 2021), https://perma.cc/RL9V-34B3.

133 *Id.*

134 *Id.*

135 Allison Herren Lee, Acting Chair, U.S. Sec. Exch. Comm'n, Public Input Welcomed on Climate Change Disclosures (Mar. 15, 2021), https://perma.cc/J4KV-RKQV.

136 Press Release, U.S. Sec. Exch. Comm'n, SEC Division of Examinations Announces 2021 Examination Priorities (Mar. 3, 2021), https://perma.cc/K2DG-47VR.

137 Press Release, U.S. Sec. Exch. Comm'n, SEC Announces Enforcement Task Force Focused on Climate and ESG Issues (Mar. 4, 2021), https://perma.cc/MSP5-H824.

138 *Environmental, Social and Governance (ESG) Funds—Investor Bulletin*, INVESTOR.GOV, U.S. SEC. & EXCH. COMM'N (Feb. 26, 2021), https://perma.cc/EZD9-G57C.

139 Press Release, U.S. Sec. Exch. Comm'n, Satyam Khanna Named Senior Policy Advisor for Climate and ESG (Feb. 1, 2021), https://perma.cc/MJZ9-PLFL.

140 *SEC Response to Climate and ESG Risk and Opportunity*, U.S. SEC. & EXCH. COMM'N, https://perma.cc/F6BH-8JRJ (last updated Oct. 26, 2021).

141 Commissioners Crenshaw and Lee, the two Democratic Commissioners, although both appointed by Trump, have made public statements supporting required ESG reporting. Jay Clayton, the Republican SEC Chairman, stepped down at the end of December 2020.

come in the form of new federal legislation or through various administrative mechanisms,[142] such as amending Regulation S-K or promulgating a new regulation.[143] SEC rulemaking would be less vulnerable to legal challenges if the securities laws were amended pursuant to new federal legislation, a possible scenario in the 117th Congress but one with a difficult path given the 50-50 Senate split with Vice President Harris as the tie-breaking vote.

There have been attempts to craft federal legislation regarding climate risk and ESG disclosure, but all have been unsuccessful so far. The climate risk disclosure bill, first introduced in the 115th Congress (Senator Elizabeth Warren's Climate Risk Disclosure Act of 2018),[144] ultimately died with the end of that legislative session.[145] The bill was reintroduced in the 116th Congress as the Climate Risk Disclosure Act of 2019[146] with some changes. A companion bill was also introduced in the House by Representative Sean Casten.[147] Both bills would direct the SEC to require issuers to disclose information regarding climate-related risks posed to the issuer and any strategies to mitigate those risks.[148]

Similarly, Representative Juan Vargas of California introduced the ESG Disclosure Simplification Act of 2019,[149] which would require issuers to disclose certain ESG metrics and explain how they are connected to their long-term business strategy. On April 15, 2021, Senator Warren and Representative Casten reintroduced the Climate Risk Disclosure Act in both the Senate[150] and House.[151] On February 18, 2021, Representative Vargas reintroduced the ESG Disclosure Simplification Act.[152] Other proposed legislation includes the Paris Climate Agreement Disclosure

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The Commission is currently split 2-2. President Biden has already nominated Gary Gensler, a Democrat, former CFTC Chair under Obama, and Wall Street critic, as Commission Chairman. This will create a 3-2 Democratic majority. Given Biden's environmental agenda and actions to become involved internationally again (e.g., rejoining the Paris Agreement), and Gensler's history of regulating new areas, this increases the likelihood of mandatory ESG reporting. Glazer, *supra* note 6; Crenshaw, *supra* note 130; Lee, *supra* note 130.

[142] *Investor Bulletin: An Introduction to the U.S. Securities and Exchange Commission - Rulemakings and Laws*, U.S. SEC. & EXCH. COMM'N (Aug. 20, 2015), https://perma.cc/B8VG-JR6Y.

[143] Colin Myers, *Financing Our Future's Health: Why the United States Must Establish Mandatory Climate-Related Financial Disclosure Requirements Aligned with the TCFD Recommendations*, 37 PACE ENV'T L. REV. 415, 439–51 (2020).

[144] Climate Risk Disclosure Act of 2018, S. 3481, 115th Cong. (2018).

[145] *S. 3481 (115th): Climate Risk Disclosure Act of 2018*, GOVTRACK, https://perma.cc/EED6-C688 (last visited Oct. 9, 2021).

[146] Climate Risk Disclosure Act of 2019, S. 2075, 116th Cong. (2019).

[147] Climate Risk Disclosure Act of 2019, H.R. 3623, 116th Cong. (2019).

[148] *Id.*; Climate Risk Disclosure Act of 2019, S. 2075, 116th Cong. (2019).

[149] ESG Disclosure Simplification Act of 2019, H.R. 4329, 116th Cong. (2019).

[150] Climate Risk Disclosure Act of 2021, S. 1217, 117th Cong. (2021).

[151] Climate Risk Disclosure Act of 2021, H.R. 2570, 117th Cong. (2021).

[152] ESG Disclosure Simplification Act, H.R. 1187, 117th Cong. (2021).

Act[153] and the Climate Leadership and Environmental Action for Our Nation's Future Act (CLEAN Future Act).[154]

The demand for ESG information continues to grow every year. In 2020, 91% of investors surveyed stated that ESG information played a pivotal role in their investment decision-making during the past year.[155] With this demand, and the criticism that there are too many and often unverified voluntary reporting standards,[156] we ought to expect some rendition of a mandatory ESG reporting framework will be created in the next few years, either demanded by the 117th Congress or solely put forth by the new Democratic SEC.[157] The newly appointed SEC Chair, Gary Gensler, has stated that climate disclosure rules are among his top priorities,[158] and has "asked SEC staff to develop a mandatory climate risk disclosure rule proposal for the Commission's consideration by the end of [2021]."[159]

Furthermore, President Biden issued an Executive Order in May 2021 aimed at addressing climate-related financial risk.[160] The Executive Order directs federal agencies to assess and mitigate climate change risks to individuals, businesses, the federal government, and the U.S. financial system.[161] This involves developing a whole-government approach to mitigate climate-related financial risk; encouraging financial regulators to assess climate-related financial risk; bolstering the resilience of life savings and pensions; modernizing federal lending, underwriting, and procurement; and reducing the risk of climate change to the federal budget.[162] Although this is a big first step to addressing the climate risk

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153 This bill would amend the Exchange Act to require disclosures related to the Paris Agreement, including whether the issuer has set targets in line with the goals of the Paris Agreement or if it plans to do so in the future, or if it has not and does not plan to, a statement as to why and whether it supports the Agreement's temperature goals. Paris Climate Agreement Disclosure Act, H.R. 1780, 117th Cong. (2021).

154 The CLEAN Future Act would amend the Exchange Act to require that the SEC promulgate rules requiring public companies to disclose information relating to, among other things, direct and indirect greenhouse gas emissions of the issuer and its affiliates, fossil fuel-related assets owned or managed by the issuer, and climate-related risk disclosures by industry or sector. CLEAN Future Act, H.R. 1512, 117th Cong. (2021).

155 Press Release, Ernst & Young LLP, ESG Disclosures Take Center Stage as Investors Raise Stakes to Assess Company Performance (July 23, 2020), https://perma.cc/W5SX-M76Y.

156 Allison Herren Lee, Comm'r, U.S. Sec. & Exch. Comm'n, "Modernizing" Regulation S-K: Ignoring the Elephant in the Room (Jan. 30, 2020), https://perma.cc/SMZ6-YGZ3.

157 *See* Glazer, *supra* note 6 (discussing forthcoming SEC action under the Biden administration); Deborah M. Meshulam et al., *SEC 2021 and Beyond: What to Expect*, DLA PIPER (Dec. 7, 2020), https://perma.cc/9TPS-CFUH.

158 Dean Seal, *Gensler Says Climate Disclosure Rules Among 'Top Priorities'*, LAW360 (May 13, 2021), https://perma.cc/E2WR-9K2Q.

159 Gary Gensler, Chair, U.S. Sec. Exch. Comm'n, Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar (July 28, 2021), https://perma.cc/3ZD3-L586.

160 Climate-Related Financial Risk, Exec. Order No. 14030, 86 Fed. Reg. 27,967 (May 25, 2021).

161 *Id.*

162 *Id.* at 27,969–70.

in the financial system, the word "encourag[ing]" reflects the limit of the White House's authority over independent financial regulators, such as the SEC and the Commodity Futures Trading Commission (CFTC).[163]

b. Other Types of Mandatory Sustainability-Related Disclosures

There are also various other types of sustainability-related disclosures required on both a federal and state level, such as the SEC Conflict Minerals Disclosure Rule.[164] This rule requires companies that file reports with the SEC under Exchange Act Section 13(a) or Section 15(d) to file a Form SD if they manufacture or contract to have manufactured products that contain conflict minerals (e.g., tin, tantalum, tungsten, gold) necessary to the functionality or production of those products.[165] A company must "(1) determine whether it manufactures or contracts to have manufactured products with 'necessary' conflict minerals; (2) conduct a reasonable country-of-origin inquiry (RCOI) concerning the origin of conflict minerals used[, if any, and file a Form SD]; and (3) exercise due diligence, if appropriate, to determine the source and chain of custody of conflict minerals used."[166]

The SEC CEO Pay Ratio Disclosure (Item 402(u) of Regulation S-K) rule was intended to inform shareholders when they are voting on "Say-on-Pay" and requires public companies to disclose the median of the annual total compensation of all its employees except the CEO, the annual total compensation of the CEO, and the ratio of those two amounts.[167] Another informational disclosure requirement, the California Transparency in Supply Chains Act, requires every retail seller or manufacturer doing business in California with annual worldwide gross receipts exceeding $100 million to disclose information regarding their efforts to eradicate human trafficking and slavery within their supply chains.[168]

c. Liability for Inadequate and Misleading Disclosures

When making SEC filings, lawyers must concern themselves with the quality of information disclosed. Inadequate or misleading disclosures can subject clients to various types of liability. Companies can be held

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[163] *Id.* at 27,969.

[164] 17 C.F.R. § 240.13p-1 (2020).

[165] *Id.*

[166] U.S. GOV'T ACCOUNTABILITY OFF., GAO-16-805, SEC CONFLICT MINERALS RULE: COMPANIES FACE CONTINUING CHALLENGES IN DETERMINING WHETHER THEIR CONFLICT MINERALS BENEFIT ARMED GROUPS 10 (2016), https://perma.cc/CV45-QKYE.

[167] 17 C.F.R. § 229.402(u) (2020); SEC. EXCH. COMM'N, OFF. OF INV. EDUC. AND ADVOC., INVESTOR BULLETIN: SAY-ON-PAY AND GOLDEN PARACHUTE VOTES 1 (Mar. 2011), https://perma.cc/8KN5-A364.

[168] Cal. Civ. Code § 1714.43 (2021).

liable for material misstatements under Section 10(b) of the Securities Exchange Act and SEC Rule 10b-5—the anti-fraud provisions of the federal securities laws.[169] These provisions cover fraudulent statements made to investors, regardless of when or where they are made.[170] Companies may also be held liable under Sections 11 and 12(a)(2) of the Securities Act for material misstatements made in registration statements and prospectuses.[171]

Companies may further be held liable for statements made outside of SEC filings, such as statement made in voluntary reports, earnings calls, and investor presentations.[172] For example, in a Section 10(b) action brought against BP after the Deepwater Horizon incident, the Southern District of Texas found that the plaintiffs had adequately plead materiality and falsity for various statements BP made in its sustainability reports, annual reviews and reports, and during analyst calls.[173] In another case, the Central District of California denied the defendants' motion to dismiss on a Rule 10b-5 claim because the defendants' boilerplate disclosures about environmental compliance were materially misleading.[174]

On top of liability with the SEC, plaintiffs continue to bring claims under other laws. Such laws include state consumer protection and anti-fraud laws,[175] books and records requests,[176] and lawsuits and investigations brought by state and municipal governments.[177] To date, most cases brought under Sections 11 and 12, and also under state laws,

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169 15 U.S.C § 78j(b) (2018); 17 C.F.R. § 240.10b-5 (1967).

170 *Id.*

171 15 U.S.C. § 77k(a) (2018).

172 *See infra* text accompanying note 258.

173 In re BP P.L.C. Sec. Litig., No. 4:12-cv-1256, 2013 WL 6383968, at *41 (S.D. Tex. Dec. 5, 2013).

174 Loritz v. Exide Tech., No. 2:13-cv-02607, 2015 WL 6790247, at *21 (C.D. CA. July 21, 2015).

175 *See, e.g.*, Beyond Pesticides v. Exxon Mobil Corp., No. 20-1815 (TJK), 2021 WL 1092167, at *1 (D.D.C. Mar. 22, 2021) (accusing Exxon of overstating its clean energy investments while renewables represent only a miniscule portion of its total investments); City of New York v. Exxon Mobil Corp., No. 451071/2021 (N.Y. Sup. Ct. filed Apr. 22, 2021) (claiming that Exxon violated the City's consumer protection laws by promoting products like gasoline as more environmentally friendly than they actually are and improperly inflating their climate leadership); Ruiz v. Darigold, Inc./Nw. Dairy Ass'n, No. C14-1283RSL, 2014 WL 5599989, at *3 (W.D. Wash. Nov. 3, 2014) (challenging statements made in the company's CSR report as misleading); Hodsdon v. Mars, Inc., 162 F. Supp. 3d 1016, 1022 (N.D. Cal. 2016) (alleging Mars had a duty to disclose that its chocolate likely contains cocoa beans picked by children and forced laborers).

176 *See, e.g.*, Louisiana Mun. Police Employees' Ret. Sys. v. Hershey Co., No. 7996-ML, 2013 WL 6120439, at *1 (Del. Ch. Nov. 8, 2013).

177 *See, e.g.*, California v. BP P.L.C., No. C 17-06011 WHA, 2018 U.S. Dist. LEXIS 32990, at *3–4 (N.D. Cal. Feb. 27, 2018); City of N.Y. v. BP P.L.C., 325 F. Supp. 3d 466, 468 (S.D.N.Y. 2018); King Cnty. v. BP P.L.C., No. C18-758-RSL, 2018 U.S. Dist. LEXIS 178873, at *2 (W.D. Wash. Oct. 17, 2018); Exxon Mobil Corp. v. Schneiderman, 316 F. Supp. 3d 679, 686 (S.D.N.Y. 2018).

have been unsuccessful.[178] However, this could change as more companies begin to disclose sustainability information, if companies are not diligent when crafting their disclosures.

2. Sustainability Disclosure Outside of the U.S.

Outside of the U.S., regulators are already taking significant action regarding mandatory sustainability disclosure—most significantly the EU and United Kingdom (UK). EU laws have the potential to affect U.S. companies (e.g., General Data Protection Regulation)[179] and can act as a guiding post for U.S. regulators (e.g., California Consumer Privacy Act).[180] With the Biden Administration's ambitious climate plan and the significant catch-up necessary to meet the Paris goals, the U.S. may look to EU sustainability disclosure laws as a baseline for U.S. regulation.

The first major overhaul to include sustainability-related information in the EU was the Non-Financial Reporting Directive (NFRD).[181] This directive, which came into force on December 5, 2014, amended the Accounting Directive[182] to require large companies, from 2018 onwards, to include a non-financial statement in their annual reports that discloses certain information on the way they operate and manage social and environmental challenges.[183] The law affects public companies with more than 500 employees and requires them to publish reports on the policies they implement in relation to environmental protection, human rights, social responsibility and treatment of employees, anti-corruption and bribery, and board diversity.[184]

The content of the statement should include at least a description of 1) the entities' business models; 2) a description of the policies pursued by the [group] in relation to the five matters above, as well as the due diligence processes used; 3) policy outcomes; 4) the main risks arising from the non-financial matters out of the entities' operations; and 5) non-

178 Connor Kuratek et al., *Legal Liability for ESG Disclosures*, HARV. L. SCH. F. CORP. GOV. (Aug. 3, 2020), https://perma.cc/RW84-WUND.

179 Regulation (EU) 2016/679 of the European Parliament and of the Council on 27 April 2016 on the Protection of Natural Persons with Regard to the Processing of Personal Data and on the Free Movement of Such Data, and Repealing Directive 95/46/EC (General Data Protection Regulation), O.J. (L 119); Sara H. Jodka, *What US-Based Companies Need to Know About the GDPR, and Why Now?*, DICKINSON WRIGHT (Mar. 2018), https://perma.cc/ZU72-EW78.

180 CA. Civ. Co. § 1798.100 (2020).

181 Directive 2014/95/EU, of the European Parliament and of the Council of 22 October 2014 Amending Directive 2013/34/EU as Regards Disclosure of Non-Financial and Diversity Information by Certain Large Undertakings and Groups, O.J. (L 330).

182 Directive 2013/34/EU, of the European Parliament and of the Council of 26 June 2013 on the Annual Financial Statements, Consolidated Financial Statements and Related Reports of Certain Types of Undertakings, Amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC, O.J. (L 182) [hereinafter NFRD].

183 Directive 2014/95/EU, *supra* note 181.

184 *Id.*

financial KPIs.[185] If entities do not have a policy on any of these non-financial matters, the statement must provide a clear and reasoned explanation for not doing so.[186] The NFRD provides significant flexibility for entities in choosing the framework used to disclose, allowing the use of international, union-based, or national frameworks.[187]

In June 2017, the European Commission (EC) published non-binding guidelines to assist entities with disclosing environmental and social information.[188] The EC drew on international, union-based, and national frameworks when preparing the guidelines, including all of the frameworks and standards mentioned in Part IV.B.4., the Voluntary Reporting section.[189] Then, in June 2019, the EC published supplemental guidance on reporting climate-related information.[190] The guidelines integrate the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) (discussed below in Part IV.B.4.).[191]

The EC has also put forth additional regulations that primarily concern investment managers (financial market participants) without ESG mandates.[192] The Sustainability-Related Disclosure Regulation (Disclosure Regulation), which takes effect on March 10, 2021, aims to enhance transparency about the integration of sustainability risks and impacts when making investment decisions and recommendations.[193] Managers are expected to 1) consider and document the relevance of ESG in their investment policies and procedures, 2) publish a disclosure on their website concerning sustainability risks in their investment decision-making process, 3) make pre-contractual disclosures on how sustainability risks are integrated into the investment decisions/advice, and 4) provide additional detailed disclosures if the investments are marketed as sustainable investments or promote specific ESG characteristics.[194]

In addition to these directives, regulations, and guidelines, the EC also crafted the Taxonomy Regulation, which entered into force on July

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185 *Id.* art. 1.

186 *Id.*

187 *Id.*

188 C/2017/4234, Communication from the Commission, Guidelines on Non-Financial Reporting, O.J. (C 215).

189 *Id.*

190 C/2019/4490, Communication from the Commission, Guidelines on Non-Financial reporting: Supplement on Reporting Climate-Related Information, O.J. (C 209) [hereinafter EU Climate Guidelines].

191 *Id.*

192 Anna Meleva-Otto & Joshua Wright, *New ESG Disclosure Obligation*, HARV. L. SCH. F. CORP. GOV. (Mar. 24, 2020), https://perma.cc/TEH8-YU9K.

193 Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on Sustainability-Related Disclosures in the Financial Sector, art. 1, O.J. (L 317).

194 *Id.*

12, 2020.[195] The Taxonomy Regulation is a framework intended to provide investors and companies with a common language concerning environmentally sustainable economic activities.[196] It sets forth six environmental objectives: climate change mitigation, climate change adaptation, the sustainable use and protection of marine resources, the transition to a circular economy, pollution prevention and control, and the protection and restoration of biodiversity and ecosystems.[197] An environmentally sustainable economic activity must contribute to one or more of these environmental objectives, not significantly harm any of the objectives, be carried out in compliance with listed minimal safeguards, and comply with technical screening criteria established by the EC.[198]

The Taxonomy Regulation creates mandatory reporting requirements for the companies covered under the Disclosure Regulation, as well as those covered under the NFRD.[199] For entities covered under the Disclosure Regulation that offer financial products that contribute to any of the environmental objectives, the entity must disclose details of the environmental objective(s) to which the underlying investment contributes and describe the extent to which the underlying investments are sustainable economic activities.[200] If the financial product does not have sustainable investment objectives, the entity must make a negative disclosure statement in pre-contractual and periodic reporting disclosures.[201] Companies covered under the NFRD must disclose whether, and the extent to which, their activities are environmentally sustainable; specifically, the proportion of their turnover, capital expenditures, and operating expenditures associated with sustainable economic activities as defined by the Taxonomy Regulation.[202]

The effectiveness of the Disclosure and Taxonomy Regulations is only as good as the information disclosed by companies. To strengthen the foundations for sustainable investments in the EU and to carry forth the European Green Deal, the EC committed to reviewing the NFRD in 2020.[203] The EC sought public feedback between February and June of 2020 on possible revisions to the NFRD.[204] The proposal for a Directive

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195 Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the Establishment of a Framework to Facilitate Sustainable Investment, and Amending Regulation (EU) 2019/2088, 2020 O.J. (L 198).

196 *European Commission, EU Taxonomy, Corporate Sustainability Reporting, Sustainability Preferences and Fiduciary Duties: Directing Finance Towards the European Green Deal*, at 1, COM (2021) 188 final (Apr. 21, 2021).

197 Regulation (EU) 2020/852, *supra* note 195, at 29.

198 *Id.* at 27.

199 *Id.* at 28–29.

200 *Id.* at 28.

201 *See id.* (The disclosure states: "[t]he investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities.").

202 *Id.* at 29.

203 *European Commission, The European Green Deal*, at 17, COM (2019) 640 final (Dec. 11, 2019).

204 *Corporate Sustainability Reporting: About This Initiative*, EUROPEAN COMM'N, https://perma.cc/TSD3-R8S3 (last visited Oct. 19, 2021).

was published on April 26, 2021, and public feedback was open until July 14, 2021; the feedback will be summarized by the EC and presented to the European Parliament and Council to feed the legislative debate.[205]

On April 21, 2021, the EC announced a comprehensive package of measures intended to improve the flow of money toward sustainable activities.[206] One measure is the EU Taxonomy Climate Delegated Act, which was formally adopted in June 2021.[207] The Delegated Act aims to support sustainable investment by making it clearer which economic activities most contribute toward the environmental objectives of the Taxonomy Regulation.[208] The second measure is a proposal for a CSR Directive (CSRD), which would amend the existing reporting requirements of the NFRD.[209] "[T]he [CSRD] will set common European reporting rules that will increase transparency, requiring companies to report sustainability information in a consistent and comparable manner."[210] The proposal requires audit (assurance) of reported information, introduces more detailed reporting requirements, and requires companies to report according to mandatory EU sustainability reporting standards.[211] The last measure would amend "delegated acts to better reflect sustainability preferences in insurance and investment advice and sustainability considerations in product governance and fiduciary duties."[212]

The UK has also taken steps to require sustainability-related disclosure, particularly climate-related disclosures. In December 2020, the Financial Conduct Authority (FCA) published a Policy Statement[213] and a final rule and guidance promoting better climate-related financial disclosures for UK premium-listed commercial companies.[214] The final rule[215] requires premium-listed companies to report against the

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[205] *Id.*; *see Comment on EU Policy and Law*, EUROPEAN COMM'N, https://perma.cc/Z5BD-3UJ3 (last visited Oct. 5, 2021) ("The Commission will consider [public input] when [formulat]ing policy and legislation.").

[206] *European Commission, EU Taxonomy, Corporate Sustainability Reporting, Sustainability Preferences and Fiduciary Duties: Directing Finance Towards the European Green Deal, supra* note 196, at 1.

[207] Financial Stability, et al., *Sustainable Finance Package*, EUROPEAN COMM'N, https://perma.cc/T5G3-EM2J (last visited Oct. 19, 2021).

[208] *European Commission, EU Taxonomy, Corporate Sustainability Reporting, Sustainability Preferences and Fiduciary Duties: Directing Finance Towards the European Green Deal, supra* note 196, at 1, 6–7.

[209] *Id.* at 1.

[210] *Id.*

[211] *Id.* at 9.

[212] *Id.* at 1.

[213] FIN. CONDUCT AUTH., PROPOSALS TO ENHANCE CLIMATE-RELATED DISCLOSURES BY LISTED ISSUERS AND CLARIFICATION OF EXISTING DISCLOSURE OBLIGATIONS, 2020, PS20/17 (UK), https://perma.cc/3KFX-DBW5 [hereinafter FCA Policy Statement].

[214] The FCA is also consulting on plans to require asset managers, life insurers, and FCA-regulated pension schemes to meet these climate-related disclosure rules. *Id.* at 4.

[215] Listing Rules (Disclosure of Climate-Related Financial Information) Instrument 2020, FCA 2020/75, annex B (Eng.), https://perma.cc/QU7A-F4J6 [hereinafter Listing Rules Instrument 2020].

recommendations and recommended disclosures of the Financial Stability Board's TCFD.[216] The new requirement, which applies to financial years beginning on January 1, 2021, affecting annual reports published in 2022, requires companies to state whether they have made disclosures consistent with the TCFD Recommendations in their annual financial report; directs companies that have not disclosed against a TCFD Recommendation to identify and explain why they have not done so, and set out steps they plan to take to do so in the future; and requires companies that disclose TCFD Recommendations outside of an annual report to explain why they do so and direct readers of the annual report to the relevant disclosure document.[217] The FCA also published guidance on ESG reporting in the Policy Statement.[218]

3. Stock Exchanges

Outside of regulatory agencies, stock exchanges are increasingly implementing ESG reporting requirements. As of September 2021, there are twenty-six stock exchanges where ESG reporting is a required listing rule according to the Sustainable Stock Exchanges Initiative.[219] Some notable inclusions include the Hong Kong Stock Exchange (HKEX), EURONEXT, and the National Stock Exchange of India.[220] HKEX, for example, requires issuers to publish an ESG report on an annual basis, the contents of which include both "mandatory disclosure" obligations and "comply or explain" provisions.[221]

In the U.S., Nasdaq also now has an ESG-related listing requirement. On August 6, 2021, the SEC approved Nasdaq's new listing rule regarding board diversity and disclosure.[222] The new listing rule adopts a comply or explain mandate for board diversity for most listed companies and requires companies listed on Nasdaq's U.S. exchange to publicly disclose consistent, transparent diversity statistics regarding the composition of their boards.[223] Nasdaq sets a recommended objective of at least two diverse directors on a company's board, and if the company does not meet that objective, it must explain the rationale for not doing so.[224]

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216 *See* discussion *infra* Part B.IV(a) for a discussion of the TCFD.

217 Listing Rules Instrument 2020, *supra* note 215, at 3–4, 8.

218 FCA Policy Statement, *supra* note 213, at App. 2.

219 *Stock Exchange Database*, SUSTAINABLE STOCK EXCHS. INITIATIVE, https://perma.cc/RRE8-ADQB (last visited Sept. 30, 2021) (filtered by "ESG reporting required as a listing rule").

220 *Id.*

221 HONG KONG STOCK EXCH., APPENDIX 27 ENVIRONMENTAL, SOCIAL AND GOVERNANCE REPORTING GUIDE 1, https://perma.cc/4GKE-HUPX.

222 The Nasdaq Stock Market LLC, Nasdaq's Board Diversity Rule: What Nasdaq-Listed Companies Should Know (Oct. 1, 2021), https://perma.cc/5RNZ-9JGJ.

223 *Id.*

224 *Id.*

4. Voluntary Reporting

Although the governmental response to investor demand for sustainability has been slow in many respects, private environmental governance has answered the call.[225] Over the years, a plethora of organizations have created voluntary reporting standards and frameworks; however, with so many organizations providing different standards and frameworks, voluntary reporting has not been without criticisms.[226] This Part will provide an overview of the main players in the voluntary reporting space, as well as how they differ and their potential role in the future as more regulators require mandatory reporting.[227]

a. Task Force on Climate-Related Financial Disclosures

The TCFD was formed in 2015 by the Financial Stability Board—an international body established by the G20.[228] The TCFD's goal is "to develop recommendations for more effective climate-related financial disclosures that could promote more informed investment, credit, and insurance underwriting decisions."[229] The organization released its Recommendations in 2017, establishing a disclosure framework that provides companies with better information to support informed capital allocation decisions.[230] The Recommendations are structured around four thematic areas and emphasize forward-looking scenario analysis:[231] Governance, Strategy, Risk Management, and Metrics and Targets.[232]

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[225] *See* Vandenbergh, *Private Environmental Governance, supra* note 8, at 161; Michael P. Vandenbergh, *Disclosure of Private Environmental Governance Risks* 3–4 (Vanderbilt U. L. Sch., Working Paper No. 21-01, 2021), https://perma.cc/9GZQ-U9LQ.

[226] The primary criticism is that, because organizations target different audiences and use different standards and frameworks, it is difficult for investors to compare information provided by different companies.

[227] *Cf.* Vandenbergh, *Disclosure of Private Environmental Governance Risks*, *supra* note 225, at 11–12 ("The Article identifies several viable steps that can be taken immediately to recognize and disclose PEG climate transition risks. The SEC under the new administration can update the 2010 Guidance to indicate explicitly that firms should assess and disclose the transition risks arising from PEG climate initiatives, as can the CFTC and the Federal Reserve. Public-private and private disclosure regimes, such as those developed by the TCFD and SASB, can clarify their disclosure language to note the importance of PEG initiatives more explicitly and can provide more detailed guidelines on how these risks should be assessed and disclosed. Over the longer term, the training of scholars, lawyers, accountants, business managers, and policymakers can better prepare the principal actors in the securities regulatory regime to recognize, assess, and disclose these risks.").

[228] *About*, TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES, https://perma.cc/T7AZ-QKY2 (last visited Oct. 9, 2021).

[229] *Id.*

[230] *Id.*

[231] DELOITTE, *supra* note 88, at 25.

[232] TCFD RECOMMENDATIONS, *supra* note 87, at 14.

This organization focuses specifically on the subject of climate and has a target audience of investors, lenders, and insurance underwriters. It also provides both a general and sector-specific scope, providing ease of use for companies and simplified comparison for investors. The TCFD recommends that companies disclose their climate-related financial information in the mainstream (annual) disclosure required by their regulator.[233]

The TCFD Recommendations have garnered much support from both international organizations and governments. The most recent status report states that there is support from "over 1,500 organizations globally, [with] over 1,340 companies with a market capitalization of $12.6 trillion and financial institutions responsible for assets of $150 trillion."[234] More important than the organizational support, the Recommendations have garnered governmental support. The 2020 Status Report states that over 110 governmental entities support the Recommendations, "including the governments of Belgium, Canada, Chile, France, Japan, New Zealand, Sweden, and the United Kingdom."[235] The Network for Greening the Financial System[236]—a group of central banks from around the world—also encourages companies to disclose in line with the TCFD Recommendations.[237]

Several government regulators have also moved toward requiring TCFD disclosures through legislation and regulation.

On June 17, 2019, the European Commission incorporated the TCFD Recommendations into its *Guidelines on Reporting Climate-Related Information*.[238] The guidelines are only meant to assist companies with reporting climate-related information under the Non-Financial Reporting Directive and are not themselves binding.[239]

On September 15, 2020, New Zealand's Ministry for the Environment announced that the government plans to require climate-related financial disclosures for some organizations, and that the standard would be developed in line with the TCFD Recommendations.[240] These disclosure requirements would apply to around 200 organizations in New Zealand, including all companies listed on the NZX and large financial institutions.[241]

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233 *Id.* at 33.

234 TASK FORCE ON CLIMATE-RELATED FIN. DISCLOSURES, 2020 STATUS REPORT 2 (2020), https://perma.cc/V3DY-EHUA [hereinafter 2020 STATUS REPORT].

235 *Id.*

236 *Origin and Purpose*, NETWORK FOR GREENING THE FIN. SYS., https://www.ngfs.net/en (last visited Oct. 21, 2021).

237 NETWORK FOR GREENING THE FIN. SYS., A CALL FOR ACTION: CLIMATE CHANGE AS A SOURCE OF FINANCIAL RISK 5 (2019), https://perma.cc/3KHK-VDLD.

238 EU Climate Guidelines, *supra* note 190, at 2.

239 NFRD, *supra* note 182, at 22.

240 *New Zealand Becomes First to Implement Mandatory TCFD Reporting*, CLIMATE DISCLOSURE STANDARDS BD. (Sept. 15, 2020), https://perma.cc/7UN2-RG8D.

241 *Mandatory Climate-Related Disclosures*, MINISTRY FOR THE ENV'T, https://perma.cc/ARW9-WABV (last updated Apr. 28, 2021).

On December 21, 2020, the UK's Financial Conduct Authority published a policy statement and final rule and guidance requiring companies to include a statement in their financial report on whether their disclosures are consistent with the TCFD Recommendations and to explain if they have not done so.[242]

These are just the regulators that have moved to require the TCFD disclosures. Others have started the process to require them, and many more are likely to follow.[243]

b. Sustainability Accounting Standards Board and the International Integrated Reporting Council

The Sustainability Accounting Standards Board (SASB) is a non-profit organization that sets standards for voluntary use by companies, specifically aiming to provide standards for publicly traded companies on U.S. exchanges.[244] SASB recommends use of their standards in SEC filings and uses the SEC's standard of materiality.[245] The standards are meant to facilitate the identification of financially material sustainability information that is industry specific, produce information that is decision-useful to investors; further, the standards are designed to be cost effective for companies to use and were developed using a market-informed and evidence-based approach.[246]

Since its inception in 2011, SASB has gained much momentum in the reporting community.[247] In 2020, 557 companies reported using SASB

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[242] FCA Policy Statement, *supra* note 213, at 3.

[243] *See, e.g.*, 2020 STATUS REPORT, *supra* note 234, at 3, n.11 (these "include the Australian Securities and Investment Commission, the Bank of England, the European Central Bank, the Hong Kong Monetary Authority, the Japanese Ministry of Economy, Trade and Industry, the Monetary Authority of Singapore, the National Treasury of South Africa"); N.Y. PUB. SERV. COMM'N, CASE 20-M-0499 – IN THE MATTER REGARDING THE NEED FOR REPORTING RISKS RELATED TO CLIMATE CHANGE 2 (2020) (the New York Public Service Commission); Jill Feblowitz, *Climate Risk Is Investment Risk – What Utilities Need to Know: An Introduction*, UTIL. ANALYTICS INST. (Dec. 8, 2020), https://perma.cc/47RP-BZHA (the California Public Utilities Commission); N.Y. DEP'T FIN. SERV., FOR PUBLIC COMMENT: PROPOSED GUIDANCE FOR NEW YORK DOMESTIC INSURERS ON MANAGING THE FINANCIAL RISKS FROM CLIMATE CHANGE 3 (2021), https://perma.cc/4BMJ-P6Q6 (the New York State Department of Financial Services); *Switzerland Promotes Transparency on Climate-Related Financial Disclosures*, SWITZERLAND FED. DEP'T FIN. (Jan. 12, 2021), https://perma.cc/RMB9-SX7N (the Switzerland Federal Council).

[244] SUSTAINABILITY ACCT. STANDARDS BD., SASB CONCEPTUAL FRAMEWORK 1 (2017), https://perma.cc/EK49-LYHQ.

[245] Letter from Jean Rogers, CEO & Founder, Sustainability Accounting Standards Bd., to Brent J. Fields, Sec'y, U.S. Sec. and Exch. Comm'n (July 1, 2016), https://perma.cc/782T-E73R; 17 C.F.R. §§ 230.405, 240.12b-2 (2020). *See TSC Indus., Inc.*, 426 U.S. 438, 449 (1976) (defining materiality as matters to which "there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote").

[246] *About Us*, VALUE REPORTING FOUND.: SASB STANDARDS, https://perma.cc/3G7K-8UV7 (last visited Oct. 21, 2021).

[247] SUSTAINABILITY ACCT. STANDARDS BD., 2019 ANNUAL REPORT: BUILDING RESILIENCE 10 (2019), https://perma.cc/5DMV-GZZZ.

standards,[248] a significant increase from 133 the year prior.[249] The SASB standards have also been endorsed by major players such as BlackRock[250] and State Street Global Advisors.[251]

"The International Integrated Reporting Council (IIRC) is a global coalition of regulators, investors, companies, standard setters, the accounting profession, academia and NGOs" that strives to promote communication about value creation.[252] The IIRC developed the International Integrated Reporting (<IR>) Framework to meet that goal.[253] The IIRC targets reporters on an international level and advocates for an integrated report. The purpose of an integrated report is to explain to investors "how an organization creates, preserves or erodes value over time."[254] The report is also intended to benefit all stakeholders.[255] The organization does not create standards but rather attempts to embed integrated thinking as a corporate reporting norm.[256]

On November 25, 2020, SASB and the IIRC announced their intention to merge as the Value Reporting Foundation.[257] The new organization believes that the <IR> Framework and the SASB Standards are complementary and that combining these organizations will answer the calls by investors for a simplified corporate reporting framework.[258] Upon announcement of the merger, Barry Melancon, Chair of the IIRC, stated the following:

> Integrated reporting describes all relevant value creation topics and the approach to integrating them in corporate thought and reporting. SASB provides the precise definitions of the data that should be reported for these topics in each industry. Organizations globally already use both to communicate effectively with investors about how sustainability issues are connected to long-term enterprise value, with these endeavors ultimately benefiting other key stakeholders. Under the Value Reporting Foundation, we will

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248 *Companies Reporting with SASB Standards*, VALUE REPORTING FOUND. SASB STANDARDS, https://perma.cc/J5J7-8RAX (last visited Oct. 21, 2021).

249 SUSTAINABILITY ACCT. STANDARDS BD., *supra* note 247.

250 *Larry Fink's 2020 Letter to CEOs: A Fundamental Reshaping of Finance*, BLACKROCK, https://perma.cc/4NXS-CCJ9 (last visited Oct. 21, 2021) [hereinafter Letter from Larry Fink].

251 Cyrus Taraporevala, *CEO's Letter on our 2020 Proxy Voting Agenda*, ST. STREET GLOB. ADVISORS (Jan. 28, 2020), https://perma.cc/PP7R-JD42.

252 INTEGRATED REPORTING, INTERNATIONAL <IR> FRAMEWORK 1 (2021), https://perma.cc/7J7U-SXCV.

253 *Id.*

254 *Id.* at 5.

255 *Id.*

256 *Id.*

257 Press Release, Sustainability Acct. Standards Bd., IIRC and SASB Announce Intent to Merge in Major Step Towards Simplifying the Corporate Reporting System (Nov. 25, 2020), https://perma.cc/Q3G3-4F84.

258 *Id.*

link the concepts between the <IR> Framework and SASB Standards even further.[259]

The two organizations also left open the possibility of joining with other entities in the future.[260]

c. Global Reporting Initiative

The Global Reporting Initiative (GRI) creates global sustainability standards using a multi-stakeholder process.[261] GRI differs from the two organizations previously mentioned because it targets all stakeholders, not just investors. GRI's standards differ from SASB's in that they focus on the economic, environmental, and social impacts of a company in relation to sustainable development.[262] On a global scale, GRI remains the common language of sustainability reporting. A 2020 report by KPMG found that two-thirds of N100[263] companies and three-quarters of G250[264] companies report using GRI standards.[265]

d. Carbon Disclosure Project and the Climate Disclosure Standards Board

The Carbon Disclosure Project (CDP) is a global system for companies and cities to measure and disclose an array of environmental data, including carbon emissions, water use, deforestation, and supply chain data.[266] The data is collected by companies and cities via questionnaire then published on CDP's website to help investors better understand and mitigate risks in their investment portfolios.[267]

The CDP has also teamed up with the Climate Disclosure Standards Board (CDSB) to provide a verified reporting system for climate disclosures.[268] The CDP collects the data, and the CDSB provides the

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259 *Id.*

260 *Id.*

261 *Our Mission and History*, GLOB. REPORTING INITIATIVE, https://perma.cc/SRD6-NX2C (last visited Oct. 21, 2021).

262 *SASB Standards & Other ESG Frameworks*, VALUE REPORTING FOUND.: SASB STANDARDS, https://perma.cc/AG47-YC7N (last visited Oct. 5, 2021).

263 "The N100 refers to a worldwide sample of 5,200 companies. It comprises the top 100 companies by revenue in each of the 52 countries and jurisdictions researched in th[e KPMG] study." KPMG, THE TIME HAS COME: THE KPMG SURVEY OF SUSTAINABILITY REPORTING 2020, at 4, 25 (2020), https://perma.cc/4LDR-USBM.

264 "The G250 refers to the world's 250 largest companies by revenue as defined in the Fortune 500 ranking of 2019." *Id.*

265 *Id.* at 25.

266 *About Us*, CDP, https://perma.cc/8GPF-VFZ6 (last visited Oct. 21, 2021).

267 *See What We Do*, CDP, https://perma.cc/B6RW-VE4V (last visited Oct. 5, 2021) (CDP runs a global environmental disclosure system, supporting thousands of companies, cities, and regions).

268 *CDP*, CLIMATE DISCLOSURE STANDARDS BD., https://perma.cc/F9BM-WTSW.

framework and guidance for companies to use to disclose the climate data in their mainstream report.[269]

e. The "Big Five" of Voluntary Reporting's Statement of Intent

In September 2020, in response to investor demand for a more uniform, comprehensive sustainability reporting system, the five major standard- and framework-setting institutions released a *Statement of Intent to Work Together Toward Comprehensive Corporate Reporting*.[270] The collaboration intends to provide 1) joint market guidance on how to use their respective standards and frameworks "in a complementary and additive way;" 2) "[a] joint vision of how these elements could complement financial generally accepted accounting principles (Financial GAPP) and serve as a natural starting point for progress towards a more coherent, comprehensive reporting system;" and 3) "[a] joint commitment to drive toward this goal, through an ongoing program[] of deeper collaboration . . . and a stated willingness to engage closely with other interested stakeholders."[271]

f. Stakeholder Capitalism Metrics

In September 2020, the World Economic Forum, in consultation with the Big Four accounting firms,[272] unveiled its own ESG reporting standards.[273] The initiative was spearheaded by the International Business Council, with the support of the World Economic Forum. The initiative sought "to identify a set of universal, material ESG metrics and recommend[] disclosures that could be reflected in the mainstream annual reports of companies on a consistent basis across industry sectors and countries."[274] The standards outline twenty-one core metrics, thirty-four expanded metrics, and, "organized under four pillars . . . aligned with the SDGs and principal ESG domains: Principles of Governance, Planet, People and Prosperity."[275] The IBC encourages its members to report on these metrics and disclosures.[276]

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269 *Id.*

270 CDP ET AL., STATEMENT OF INTENT TO WORK TOGETHER TOWARDS COMPREHENSIVE CORPORATE REPORTING 2, 6 (2020), https://perma.cc/E87E-CUF2.

271 *Id.* at 3.

272 Deloitte, PricewaterhouseCoopers (PwC), Ernst & Young (EY), and Klynveld Peat Marwick Goerdeler (KPMG).

273 WORLD ECON. F., MEASURING STAKEHOLDER CAPITALISM: TOWARDS COMMONS METRICS AND CONSISTENT REPORTING OF SUSTAINABLE VALUE CREATION 6 (2020), https://perma.cc/F6Z9-XC4M.

274 *Id.*

275 *Id.*

276 *Id.* at 44.

g. CFA Institute's ESG Disclosure Standards for Investment Products

The CFA Institute, the global association of investment professionals, has also developed voluntary, global industry standards to establish disclosure requirements for investment products with ESG-related features.[277] The standards aim to advance investment product transparency and comparability amidst the growing market for ESG-labeled investment products.[278] The target audience for these standards is institutional, private wealth, and retail investors.[279]

h. Other Developments

At the 2021 United Nations Climate Change Conference in November 2021, the International Financial Reporting Standards (IFRS) Foundation—a nonprofit accounting organization that oversees the International Accounting Standards Board, an independent accounting standard-setting body—announced the formation of a new International Sustainability Standards Board.[280] The CDSB and the Value Reporting Foundation (VRF) will consolidate into the new Board.[281] Additionally, a Technical Readiness Working Group published prototype climate and general disclosure requirements, with assistance and input from the CDSB, International Accounting Standards Board, TCFD, VRF, the World Economic Forum, and the International Oorganization of Securities Commissions.[282]

5. Sustainability in Financial Decision Making

Investor demand for increased and improved sustainability disclosure has also been driven by investor demand for sustainable investment offerings. Sustainable investing continues to account for a larger share of the capital markets each year. Since 1995, when U.S. sustainable investment was sized at $639 billion, the amount of sustainable investment has increased twenty-five fold to $16.6 trillion at the beginning of 2020.[283] The compound annual growth rate during this time was 14%, with the most significant increase in investments coming

[277] CFA INST., GLOBAL ESG DISCLOSURE STANDARDS FOR INVESTMENT PRODUCTS 1 (2021), https://perma.cc/QR6Y-QL4K.
[278] *Id.* at 9.
[279] *Id.*
[280] IFRS FOUND., IFRS FOUNDATION ANNOUNCES INTERNATIONAL SUSTAINABILITY STANDARDS BOARD, CONSOLIDATION WITH CDBS AND VRF, AND PUBLICATION OF PROTOTYPE DISCLOSURE REQUIREMENTS (Nov. 3, 2021), https://perma.cc/RWJ2-Q793.
[281] *Id.*
[282] *Id.*
[283] US SIF FOUND., REPORT ON US SUSTAINABLE AND IMPACT INVESTING TRENDS 2020, at 1 (2020), https://perma.cc/PW3N-MC7H.

since 2012, with climate change as a top issue among money managers and institutional investors.[284] In June 2020, net flows into sustainable funds reached "$20.9 billion, just shy of the annual record of $21.4 billion . . . in 2019."[285] The $21.4 billion in 2019 was four times the previous record.[286] Strikingly, 2021 may be the first year since the signing of the Paris Agreement that banks are financing more clean energy projects than fossil fuel projects.[287] In the five years since the signing of the Agreement, banks financed more than $3.6 trillion of fossil fuel projects, almost three times more than the total backing for clean energy projects.[288] So far in 2021, however, banks have committed $203 billion in financing to clean energy projects compared to $189 billion to fossil fuel business.[289]

This trend creates significant opportunities for companies to capture the demand and to pursue, or further, a sustainable business strategy.[290] However, for companies to benefit from this trend, they must be aware of the new ways their stock price and credit rating can be impacted.

The demand for sustainable investing—and the sustainability data required to make these decisions—has caused the proliferation of sustainable raters and data providers. The market for these providers is quite saturated right now, with at least thirty significant providers, all of whom use different rating scales and methodologies to determine ratings, and most lack global coverage.[291] Some of the main providers include Bloomberg ESG Data Service, Corporate Knights Global 100, Dow Jones Sustainability Index, Institutional Shareholder Services ESG, Morgan Stanley Capital International ESG Research, RepRisk, Sustainalytics, and Thomson Reuters ESG Research.[292]

It is important for companies to focus on their scores from these providers because 85% of investment practitioners consider ESG factors in their investment decisions.[293] Research shows that companies with

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284 *Id.* at 1, 5.

285 Jon Hale, *Sustainable Funds Continue to Rake in Assets During the Second Quarter*, MORNINGSTAR (July 30, 2020), https://perma.cc/U3SC-H4EH.

286 *Id.*

287 Tim Quinson & Mathieu Benhamou, *Banks Always Backed Fossil Fuel Projects Over Green Projects—Until This Year*, BLOOMBERG GREEN (May 19, 2021), https://perma.cc/ND77-LLRE.

288 *Id.*

289 *Id.*

290 *See* Letter from Larry Fink, *supra* note 250 (Noting that "[o]ver time, companies and countries that [fail to] respond to stakeholders and address sustainability" will face market skepticism and higher capital costs, while "[c]ompanies and countries that champion transparency and [stakeholder responsiveness] will attract investment[s]" and capital gains).

291 *ESG Ratings Are Not Perfect, But Can Be a Valuable Tool for Asset Managers*, KPMG (Oct. 6, 2020), https://perma.cc/EH2Z-7WTQ.

292 Betty Moy Huber & Michael Comstock, *ESG Reports and Ratings: What They Are, Why They Matter*, HARV. L. SCH. F. CORP. GOVERNANCE (July 27, 2017), https://perma.cc/SPM3-6W5R.

293 CFA INST., FUTURE OF SUSTAINABILITY IN INVESTMENT MANAGEMENT: FROM IDEAS TO REALITY 4, 34 (2020), https://perma.cc/U7QK-ZZQ2.

high ESG ratings are less exposed to systemic risks, making them a more attractive asset.[294] This evidence held true during the COVID-19 economic downturn, further amplifying the flow of money into sustainable funds.[295]

The attractiveness of these higher rated ESG companies allows them to "enjoy[] a sustainability premium."[296] In the Mergers & Acquisition market, executives say they are willing to pay a 10% premium for a company that has performed well on ESG issues compared to lower performers.[297] More importantly for companies, however, is ensuring they maintain high ESG ratings so as to be included in sustainable funds, where most new money is being invested.[298]

Sustainable funds use a variety of methods when determining what assets to include. Some of the more popular ones include negative screening,[299] positive screening,[300] best in class,[301] themed funds,[302] and integrated analysis.[303] Companies should strive to maintain high ESG ratings so they do not get screened out of, or increase their chances of being screened into, sustainable funds.

Some argue that strong ESG performance is a result of good management, which translates into better long-term performance.[304] This helps explain why higher rated ESG companies also tend to have higher market valuations.[305] Higher market valuations coincide with high stock prices, which can also benefit a company. High stock prices, and strong ESG performance, can help ward off shareholder proposals.[306] High stock

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294 GUIDO GIESE & LINDA-ELING LEE, WEIGHING THE EVIDENCE: ESG AND EQUITY RETURNS 3 (2019), https://perma.cc/X2ZX-282X.

295 BLACKROCK, SUSTAINABLE INVESTING: RESILIENCE AMID UNCERTAINTY 5–6 (2020), https://perma.cc/S2E5-UMRR; *see* Hale, *supra* note 285 (sustainable fund flows set record pace in 2020).

296 *Larry Fink's 2021 Letter to CEOs*, BLACKROCK, https://perma.cc/56JH-L7J2 (last visited Oct. 21, 2021).

297 *The ESG premium: New Perspectives on Value and Performance*, MCKINSEY SUSTAINABILITY (Feb. 12, 2020), https://perma.cc/F82R-CE8P.

298 Hale, *supra* note 285.

299 *See* SUSTAINABLE INVESTING: THE ART OF LONG-TERM PERFORMANCE 21 (Cary Krosinsky & Nick Robins eds., 2008) (negative screening results in "[a]voiding companies for [their] involvement in environmentally or socially damaging sectors or practices," such as fossil fuel production).

300 "Active inclusion of companies because of environmental or social benefits." *Id.*

301 Active inclusion of companies that either lead their sectors or outperform their peers in environmental or social performance, sometimes limited to material environmental and social criteria. *Id.*

302 "Active selection of companies on the basis of investment opportunities driven by sustainability factors, such as renewable energy." *Id.*

303 "Active inclusion of environmental and social factors within conventional fund management." *Id.*

304 Sara E. Murphy, *Amid Plunging Stock Prices, ESG Leaders are Holding Their Own*, GREENBIZ (Apr. 13, 2020), https://perma.cc/94LJ-6RLJ.

305 Svetlana Borovkova, *How do ESG Scores Relate to Financial Returns*, REFINITIV (Aug. 26, 2020), https://perma.cc/3LN9-G466.

306 Chris B. Murphy, *Why Do Companies Care About Their Stock Prices*, FORBES, https://perma.cc/4PML-AQ3T (last updated Aug. 23, 2021); Kai H.E. Liekefett et al., *Shareholder*

prices also allow companies to access lower costs of equity by issuing more shares if they choose to do so.[307]

Furthermore, because stock price is usually an indication of financial health, companies with a high and continually growing stock price often obtain lower costs of capital through debt financing.[308] The sustainability premium that high ESG rated companies enjoy on their stock price also spills over into their ability to obtain lower cost debt capital in the credit market.[309]

The credit market is where companies go to issue debt securities, such as bonds.[310] A bond works as an I.O.U. where an investor provides a company with a loan (the principal), and the company promises to pay interest coupons (the annual interest rate paid on the bond expressed as a percentage of the principal) usually annually or semiannually.[311] These coupon payments continue until the end of the loan (maturity date), at which point the company returns the principal.[312]

Important for determining the interest coupon is a company's credit rating. Credit ratings are provided by credit agencies, with almost the entire rating industry controlled by Fitch Ratings, Moody's Investor Services, and Standard and Poor (S&P) Global.[313] The ratings provided by these agencies are based on extensive due diligence of the borrower's creditworthiness.[314] These ratings indicate to a potential investor the riskiness of the investment; lower credit ratings suggest that a company has had trouble paying back loans in the past and that they may have trouble in the future.[315] Because of this risk, investors demand a higher interest rate and thus higher coupon payments.

Companies have put their sustainability premium to use by jumping on investor demand for sustainable debt. In 2020, there was a total sustainable debt issuance of $565.5 billion.[316] The types of debt instruments created to meet this demand include green loans,[317] green

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Activism and ESG: What Comes Next, and How to Prepare, REUTERS (June 6, 2021), https://perma.cc/Z2JA-FVZE.

307 Murphy, *supra* note 306.

308 *Id.*

309 Ashish Lodh, *ESG and the Cost of Capital*, MCSI (Feb. 25, 2020), https://perma.cc/CRF5-65GD.

310 Cory Mitchell, *Credit Market*, INVESTOPEDIA, https://perma.cc/SZ4E-EFM7 (last updated May 29, 2021).

311 Jason Fernando, *Bond*, INVESTOPEDIA, https://perma.cc/5TCS-TWVN (last updated Oct. 28, 2021).

312 *Id.*

313 Julia Kagan, *Credit Rating*, INVESTOPEDIA, https://perma.cc/6JUF-XUKF (last updated Aug. 22, 2021).

314 *See Updated Investor Bulletin: The ABCs of Credit Ratings*, U.S. SEC. EXCH. COMM'N (Oct. 12, 2017), https://perma.cc/9PB2-C7VR (a credit rating is an assessment of an entity's creditworthiness, i.e., the ability to pay financial obligations).

315 *Id.*

316 *Sustainable Debt Breaks Annual Record Despite Covid-19 Challenges*, BLOOMBERGNEF (Jan. 11, 2021), https://perma.cc/EPY8-CJCQ.

317 *See* LOAN MKT. ASS'N ET AL., GREEN LOAN PRINCIPLES: SUPPORTING ENVIRONMENTALLY SUSTAINABLE ECONOMIC ACTIVITY (2018), https://perma.cc/W5YW-

bonds,[318] sustainability bonds,[319] social bonds,[320] and sustainability-linked loans[321] and bonds.[322] The International Capital Markets Association and the Loan Market Association have created guidelines for issuing these types of debt instruments.[323] The bonds are use of proceeds bonds where the proceeds are to be applied to green or social projects.[324] In addition to the use of proceeds bonds, the sustainability-linked debt instruments create varying financial characteristics based on the achievement of sustainability or ESG goals.

One example of these instruments is JetBlue's sustainability-linked loan.[325] The loan was a revision to a revolving credit facility to "include[] a pricing mechanism related to the applicable margin and commitment fee linked to JetBlue's ESG score provided by Vigeo Eiris."[326] Another example is Volkswagen's green bond issuance in 2020, with the use of proceeds earmarked for electric vehicle development.[327] On the other side of the spectrum, companies ignoring sustainability-related issues face significant risks in the credit market. For example, oil companies are at risk of having their credit rating cut due to industry risk associated with climate change.[328] Other sectors must also tread carefully as credit agencies are increasingly scrutinizing environmental credit risk.[329]

JALQ ("[A]ny type of loan instrument made available exclusively to finance or re-finance, in whole or in part, new and/or existing eligible Green Projects.").

318 *See* INT'L CAP. MKT. ASS'N, GREEN BOND PRINCIPLES (2018), https://perma.cc/J2XQ-6KPU ("[A]ny type of bond instrument where the proceeds will exclusively applied to finance or re-finance, in part or in full, new and/or existing eligible Green Projects.").

319 *See* INT'L CAP. MKT. ASS'N, SUSTAINABILITY BOND GUIDELINES (2018), https://perma.cc/5EWG-6T5P ("[B]onds where the proceeds will be exclusively applied to finance or re-finance a combination of both Green and Social projects.").

320 *See* INT'L CAP. MKT. ASS'N, SOCIAL BOND PRINCIPLES: VOLUNTARY PROCESS GUIDELINES FOR ISSUING SOCIAL BONDS (2020), https://perma.cc/ZW9T-7G4N ("[A]ny type of bond instrument where the proceeds will be exclusively applied to finance or re-finance in part or in full new and/or existing eligible Social Projects.").

321 *See* LOAN MKT. ASS'N ET AL., SUSTAINABILITY LINKED LOAN PRINCIPLES (2019), https://perma.cc/D5DY-FZCK ("[A]ny types of loan instruments and/or contingent facilities (such as bonding lines, guarantee lines or letters of credit) which incentivi[z]e the borrower's achievement of ambitious, predetermined sustainability performance objectives.").

322 *See* INT'L CAP. MKT. ASS'N, SUSTAINABILITY-LINKED BOND PRINCIPLES: VOLUNTARY PROCESS GUIDELINES (2020), https://perma.cc/NMV7-MHJK ("[A]ny type of bond instrument for which the financial and/or structural characteristics can vary depending on whether the issuer achieves predefined Sustainability/ ESG objectives.").

323 Mathias Lund Larsen, *A Growing Toolbox of Sustainable Finance Instruments*, GREEN BELT AND ROAD INITIATIVE CTR. (Nov. 22, 2019), https://perma.cc/77GA-A4YJ.

324 *See supra* text accompanying notes 317–322 (discussing the use of bond proceeds for green projects, social projects, performance objectives, and sustainability/ESG objectives).

325 Chris Wack & Mark Mauer, *JetBlue Closes Sustainability-Linked Loan with BNP Paribas*, WALL ST. J. (Feb. 24, 2020), https://perma.cc/2PFX-389V.

326 *Id.*

327 *Volkswagen Successfully Places First Green Bonds with a Volume of € 2 Billion*, VOLKSWAGEN (Sept. 16, 2020), https://perma.cc/S3TZ-CVSV.

328 Javier Blas & Laura Hurst, *Exxon, Shell Face Rating Cuts on Greater Climate Risk, S&P Says*, BLOOMBERG FIN. (Jan. 26, 2021), https://perma.cc/ZT89-ZVQM.

329 *Moody's - Thirteen Sectors with $3.4 Trillion of Debt Face Heightened Environmental Credit Risk*, MOODY'S INVS. SERV. (Dec. 14, 2020), https://perma.cc/65SG-GQCR.

The demand for sustainability-related debt will only continue to rise as most issuances now are oversubscribed.[330] Companies seeking to further their sustainable business strategy will be further incentivized by the potential lower cost of debt for achieving certain ESG goals or pursuing sustainability-related projects that create long-term value.

Although the ESG market has been dominated by fixed income products, offerings in other asset classes and of other financial products has begun to rise. Some banks are starting to explore green equity where shares issued in the primary market receive a green label.[331] This type of asset is still in its early stages, with some complex issues still needing to be resolved.[332] The derivatives market has started creating ESG derivatives, where ESG-related pricing components are added to conventional hedging instruments, such as interest rate swaps, cross-currency swaps, and forwards.[333] An example is a positive or negative spread added to the fixed rate of an interest rate swap based on a company's ESG performance, which is scored by an ESG rating service.[334] There are also now exchange-traded, index-based derivatives (futures and options), such as the CME E-mini S&P 500 ESG Futures Index.[335] Real estate investors are also increasingly focused on ESG performance. Investors are focusing on properties' energy management (e.g., asking whether a property is Leadership in Energy and Environmental Design (LEED) certified), water management, management of tenant sustainability practices, and climate change adaptation factors, such as location within 100-year flood zones.[336] ESG has also quickly become a focus in cryptocurrency because of the rising concern over crypto's environmental effects caused by high energy usage tied to electrical grids run by fossil fuels.[337] Some crypto miners are working to sell "coins whose transactions are verified on the blockchain by computers powered only by renewable energy" and may command a 10% premium.[338] There is even a

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[330] Nathaniel Bullard, *The Sustainable Debt Market Has Become Unsustainable*, BLOOMBERG SPARKLINES (Oct. 22, 2020), https://perma.cc/VAH5-T6LX.

[331] Frances Schwartzkopff, *Goldman Joins Banks Exploring Green Equity as New ESG Asset*, BLOOMBERG GREEN (May 19, 2021), https://perma.cc/XN8L-Q7CD.

[332] *Id.*

[333] INT'L SWAPS & DERIVATIVES ASS'N, OVERVIEW OF ESG-RELATED DERIVATIVES PRODUCTS AND TRANSACTIONS 3 (2021), https://perma.cc/LQ2B-N9QH.

[334] *Id.*

[335] *Id.* at 8.

[336] JEM E. HUDSON, THE RISE OF ESG IN REAL ESTATE: WHY ESG MATTERS IN REAL ESTATE INVESTING AND HOW TO GET STARTED 7, 11 (2019), https://perma.cc/S3PV-L3BY.

[337] *See Bitcoin Energy Consumption Index*, DIGICONOMIST, https://perma.cc/R8H2-PXUV (last visited Oct. 5, 2021) (discussing Bitcoin's energy-intensive networks, such as the significant fossil fuel consumption from Bitcoin mining).

[338] Olga Kharif & Josh Saul, *Bitcoiners Waving Eco-Friendly Bona Fides Bet on Premium*, BLOOMBERG (May 22, 2021), https://perma.cc/MA6J-WS63; Tim Quinson, *Wall Street's ESG Gold Rush Has Conjured a 'Green Bitcoin'*, BLOOMBERG FIN. (May 26, 2021), https://perma.cc/Z3E6-XUXF.

proposed "ESG Crypto Mining ETF."[339] These new types of offerings will only increase as ESG complexities are worked through.

Risks and opportunities within commercial lending has also emerged as an area of concern for sustainable business lawyers. Through private environmental governance, banks have taken on a major role in the transition to a low-carbon economy.[340] Throughout history, banks have played an important societal role like facilitating financial programs during times of crisis, as was seen during the 2008 financial crisis and the coronavirus pandemic.[341] Banks also tend to focus on lending to promising industries, conducting extensive underwriter due diligence and loan lifecycle analysis to actively monitor borrowers.[342] These historical factors encourage banks to monitor for climate risks and opportunities, which then "motivate[s] environmentally responsible behavior on the part of corporate borrowers that need access to bank credit."[343]

Banks have taken various measures to reallocate capital toward climate friendly activities. Banks have started focusing on their own operational footprint, such as reducing their Scope 1, 2, and 3 emissions by changing lightbulbs to LEDs, purchasing renewable energy to power daily operations, and reducing or offsetting employee business travel.[344] For example, JP Morgan committed to becoming carbon neutral across its operations.[345] In 2020, it began sourcing all of its power from renewable energy.[346] More importantly, however, has been banks' commitments to reduce portfolio emissions and the partnerships they have undertaken to achieve that. For example, JP Morgan has committed to finance and facilitate more than $2.5 trillion to climate friendly projects by 2030 while restricting lending to fossil fuel projects.[347] Many banks have also joined various partnerships and networks and have adopted principles that advance the transition to a low-carbon economy, such as the Equator

339 U.S. Sec. & Exch. Comm'n, Alpha Architect ETF Trust, Registration Statement (Form N-1A) (Apr. 14, 2021), *available at* https://perma.cc/VE85-2DTJ.

340 Sara E. Light & Christina Parajon Skinner, *Banks and Climate Governance*, 121 COLUM. L. REV. 1895, 1895–96, 1900 (2021).

341 *Id.* at 1909–13.

342 *Id.* at 1915–18.

343 *Id.* at 1917.

344 *Id.* at 1928–29.

345 *Sustainability*, JPMORGAN CHASE & CO., https://perma.cc/2RN2-5LT3 (last visited Oct. 21, 2021).

346 *Id.*

347 *JPMorgan Chase Targets More Than $2.5 Trillion Over 10 Years to Advance Climate Action and Sustainable Development*, JPMORGAN CHASE & CO., https://perma.cc/D76M-NGVB (last visited Oct. 5, 2021).

Principles,[348] the Poseidon Principles,[349] the Principles for Responsible Investment,[350] the Principles for Responsible Banking,[351] and the Partnership for Carbon Accounting Professionals.[352]

Lastly, business lawyers must be aware of the growing risk posed by the universal owner concept as it relates to sustainability.[353] As the Big Three institutional investors (BlackRock, State Street, and Vanguard) continue to increase the proportion of the share of all outstanding shares on the market, they have an increased incentive to internalize externalities.[354] Because climate change is a systemic risk, these institutional investors benefit themselves, and the entire economy, by engaging in shareholder activism for climate change mitigation.[355] Although the activism is a cost the investor must bear and could potentially reduce the profitability of the target firm, it protects other portfolio companies from the risks of climate change.[356] Because these powerful institutional investors are engaging in increased shareholder activism, companies should work to avoid their crosshairs.

Companies, and the lawyers who represent them, must be aware of these trends to manage risks and capture potential opportunities. By failing to account for these trends and the demands from stakeholders, companies may miss out on potential premiums in the primary markets and risk being excluded from the growing offering of ESG products in secondary markets. Companies also risk being excluded from a bank's commercial lending client list. These risks, if materialized, could be detrimental to a company, but proper management of sustainability-

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348 "[A] risk management framework, adopted by financial institutions, for determining, assessing and managing environmental and social risk in projects and is primarily intended to provide a minimum standard for due diligence and monitoring to support responsible risk decision-making." *The Equator Principles*, EQUATOR PRINCIPLES, https://perma.cc/W5UF-KSF6 (last visited Oct. 5, 2021).

349 "[A] framework for integrating climate considerations into lending decisions to promote international shipping's decarbonization." *About*, POSEIDON PRINCIPLES, https://perma.cc/6YW2-TSZ9 (last visited Oct. 5, 2021).

350 A "voluntary and aspirational" set of investment principles that "offer a menu of possible actions for incorporating ESG issues" into investment practice. *What Are the Principles for Responsible Investment?*, PRINCIPLES FOR RESPONSIBLE INV., https://perma.cc/QMK7-ZR38 (last visited Oct. 5, 2021).

351 "[A] unique framework for ensuring that signatory banks' strategy and practice align with the vision society has set out for its future in the Sustainable Development Goals and the Paris Climate Agreement." *Principles for Responsible Banking*, UN ENV'T PROGRAMME FIN. INITIATIVE, https://perma.cc/M6Q7-K5ZK (last visited Oct. 5, 2021).

352 "An industry-led partnership to facilitate transparency and accountability of the financial industry to the Paris Agreement." *About*, PARTNERSHIP FOR CARBON ACCT. FIN., https://perma.cc/J8RA-MK96 (last visited Oct. 5, 2021).

353 *See* Madison Condon, *Externalities and the Common Owner*, 95 WASH. L. REV. 1, 3–4, 6–7, 9 (2020) (explaining how anti-competitive models such as universal ownership disincentivizes businesses from engaging in sustainable practices).

354 *Id.* at 10, 49.

355 *See id.* at 10–11, 17–18 (explaining how investors can exercise control over climate risk).

356 *Id.* at 43, 47.

related issues, especially if done proactively, assists the firm with long-term value creation.

C. The Future of Proactive Sustainability Management

The role of lawyers in the sustainability space is increasing, especially due to expected government action and increasing stakeholder pressures. As noted above, with incoming Democratic control of the presidency, Congress, and the SEC, mandatory ESG reporting may be required by new federal legislation or various administrative mechanisms. Thus, lawyers must stay abreast of developments in the disclosure landscape and can prepare for a mandatory disclosure framework in the U.S. by gaining knowledge about the various voluntary reporting frameworks and standards and the EU sustainable disclosure laws.

To proactively prepare for these rules, lawyers can help their clients take steps to enjoy the "early-mover" advantage while avoiding potential policy and legal, technology, market, and reputational risks. First, lawyers should seek to understand financially material ESG issues required to be disclosed under current laws in the industries they represent. A resource for understanding these issues is the SASB's Materiality Map, which identifies ESG issues within industries and provides accompanying accounting metrics that can be used to identify "issues that are likely to affect the financial condition or operating performance of companies within an industry."[357] Lawyers must also understand that disclosures made on sustainability topics, even outside of SEC filings, carry legal risks.[358]

Also, lawyers, in terms of advising their clients about material ESG issues, should be keenly aware of the power of private environmental governance. Vandenbergh argues that an overlooked consideration is the disclosure of risks posed by private environmental governance initiatives whereby non-governmental actors (including corporations, investors, advocacy groups, and other private sector actors) perform traditionally governmental functions.[359]

> PEG climate initiatives pose potentially material transition risks through a wide range of activities such as advocacy group pressure on firms to disclose or reduce emissions. These initiatives also include naming-and-shaming campaigns directed at managers, employees, or retail customers, and divestiture or investor engagement campaigns directed at institutional investment firms,

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357 *SASB Materiality Map*, SUSTAINABILITY ACCT. STANDARDS BD., https://perma.cc/73CP-BFEW (last visited Oct. 21, 2021).

358 Connor Kuratek et al., *Legal Liability for ESG Disclosures*, HARVARD L. SCH. F. CORP. GOVERNANCE (Aug. 3, 2020), https://perma.cc/YBU3-S2U7.

359 Vandenbergh, *Disclosure of Private Environmental Governance Risks*, *supra* note 225, at 6–7.

> lenders, and insurers. PEG climate transition risks also arise from the knock-on effects of this direct pressure, including adoption by corporations, investment firms and pension funds, lenders, and insurers of public climate commitments, annual disclosure of carbon emissions, and reporting on progress toward meeting climate goals. Perhaps most important, PEG climate transition risks also include the risks that arise from the transfer of this pressure to reduce carbon emissions to borrowers, equity issuers, suppliers, and utilities.[360]

Thus, Vandenbergh suggests the updating of guidance to include PEG initiatives as transition risks.

> The SEC under the new administration can update the 2010 Guidance to indicate explicitly that firms should assess and disclose the transition risks arising from PEG climate initiatives, as can the CFTC and the Federal Reserve. Public-private and private disclosure regimes, such as those developed by the TCFD and SASB, can clarify their disclosure language to note the importance of PEG initiatives more explicitly and can provide more detailed guidelines on how these risks should be assessed and disclosed. Over the longer term, the training of scholars, lawyers, accountants, business managers, and policymakers can better prepare the principal actors in the securities regulatory regime to recognize, assess, and disclose these risks.[361]

Lawyers can advise their clients to include a discussion about sustainability in the management discussion and analysis (MD&A) section of their annual report. This can prepare companies for the potential addition of a sustainability discussion and analysis (SD&A) section in their annual report, which Jill Fisch proposes.[362] An SD&A section would be modeled after the MD&A and compensation discussion and analysis sections of Regulation S-K.[363] Her proposal requires issuers to identify the three sustainability issues most significant to their operations and then discuss the potential impact of those sustainability issues on the issuer's economic performance, including "an explanation of the basis for [that] determination of significance."[364] This is analogous to the MD&A section because it requires issuers to identify "risks, trends, and opportunities that, in the opinion of the board of directors, are material to the issuers' business plan or operations."[365]

The SD&A would also require an issuer's directors or sustainability committee of the board, rather than CEO and CFO, to certify the accuracy

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360 *Id.* at 7.

361 *Id.* at 11–12.

362 Jill E. Fisch, *Making Sustainability Disclosure Sustainable*, 107 GEO. L. J. 923, 950–51 (2019).

363 *Id.* at 953.

364 *Id.* at 956.

365 *Id.*

of the disclosures made, similar to the requirements under the Sarbanes-Oxley Act.[366] This encourages boards to implement internal controls to collect the information necessary to make these disclosures and places upon the board an obligation to become knowledgeable and consider sustainability issues, a practice that is central to this Article's recommendation in Part IV.A. Advising clients to also focus on sustainability issues when crafting their MD&A can prepare the client for potential amendments or additions to U.S. disclosure laws. In the meantime, it will help the client better manage ESG performance, understand the needs of various stakeholders, and improve the company's risk management.

On the sustainable finance side, lawyers can take multiple steps to gain an early advantage from this market boom while avoiding downside risks. One step relating to credit markets is to advise clients against greenwashing and to ensure contracts for sustainability-related financial instruments. A common criticism of these new financial products is that they merely amount to greenwashing because if the issuer does not meet its targets, the penalties are not meaningful enough to matter.[367] Companies can also set easily achievable targets, or targets that they were already on track to reach without the project, to capture the lower cost of debt without expending more resources.[368] Lawyers should advise against these tactics to avoid the downside risk of reputational damage. If investors find out that the label of the bond is just a ploy to obtain lower costs of debt, the company could be treated unfavorably in the future. If customers find out that a company is touting its environmental actions but is not actually making significant changes to its operations, customers may boycott the company or take other negative actions.[369]

Another criticism is that, although the products, such as green bonds, can fund sustainable projects, that does not mean a firm is reducing its carbon emissions throughout its entire business. A recent study found companies that issue green bonds only show a minimal decrease in carbon intensity—the ratio of carbon emissions to revenue.[370] This is because the label of a green bond is applied to a standalone project, not the entire company. Similarly, with a Sustainability-Linked Bond, once a company reaches its target, it can apply the proceeds of the issuance to whatever it wants.[371]

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366 Sarbanes-Oxley Act of 2002, Pub. Law 107-204; Fisch, *supra* note 362, at 958.

367 David Caleb Mutua, *JPMorgan's ESG Debt Head Expects Sustainability-Linked Bond Boom*, BLOOMBERG GREEN (Feb. 4, 2021), https://perma.cc/LX7A-4QYH.

368 *Id.*

369 Menno D. T. de Jong, et al., *Different Shades of Greenwashing: Consumers' Reactions to Environmental Lies, Half-Lies, and Organizations Taking Credit for Following Legal Obligations*, 34 J. BUS. & TECH. COMMC'N 38, 40, 44 (2020).

370 Torsten Ehlers et al., *Green Bonds and Carbon Emissions: Exploring the Case for a Rating System at the Firm Level*, *in* BIS QUARTERLY REVIEW: INT'L BANKING AND FIN. MKT. DEVS. 31, 32, 37–38 (2020), https://perma.cc/2P4K-4KWS.

371 Richard Howard, *Sustainability Linked Bonds Part 2: Challenges and Opportunities*, GREEN FIN. GUIDE, https://perma.cc/B9M4-H653 (last visited Oct. 1, 2021).

When it comes to ESG within equity, lawyers must warn their clients of the growing power of the Big Three asset managers: BlackRock, Vanguard, and State Street. The power these entities are amassing through the passive index revolution, in conjunction with their commitments to sustainability, can spell trouble for companies that do not fully consider sustainability in their business model and monitor their sustainability ratings.[372] Christie argues that the Big Three may be assuming the role of "sustainable capitalists," taking the private environmental governance initiative of surrogate regulators, as governments are too slow to tackle the climate crisis.[373]

Companies that do not monitor their ESG ratings and account for sustainability in their business models face two major risks from a financial perspective. The first is the risk of the Big Three, at a minimum, lowering the proportion of a company's stock held in an index fund and, worst case, being excluded from funds entirely.[374] This could potentially lower a company's valuation if it is seen as an ESG laggard. The second risk comes from activist shareholders seeking to promote change within a company. This could take the form of name and shame campaigns or through shareholder voting and engagement.[375]

To account for the many future risks posed by sustainability, lawyers must play a crucial role for clients, taking a proactive role beyond what has traditionally been required of them. The most important step starts with lawyers advising their client, whether a business or investment firm, that its fiduciary duty includes sustainability issues. To satisfy this duty, executives of the firm must, at a minimum, become knowledgeable on, or ensure they have a committee dedicated to, sustainability issues. With this first step, the firm can implement sustainable risk management strategies and begin to measure ESG performance to more accurately identify risks and opportunities.

With this foundation based in corporate governance, lawyers must then assist in managing the financial issues associated with sustainability. This requires lawyers to monitor not only the regulatory landscape but also the private initiatives taking place in the market that could influence new laws, such as the TCFD and SASB. As investors increasingly demand sustainable offerings, they also demand improved disclosures. Lawyers must seek to truly understand material sustainable issues, as well as the vocabulary associated with them, to ensure that their clients do not create false or misleading disclosures. Lastly, when attempting to capture the demand for sustainable offerings, lawyers must

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372 *See generally* Anna Christie, *The Agency Costs of Sustainable Capitalism*, 55 U.C. DAVIS L. REV. 1, 8, 25 (2021) (explaining how modern investors are more likely to invest with companies that are perceived as sustainable); *see also* John C. Coffee, *The Future of Disclosure: ESG, Common Ownership, and Systematic Risk* 3–5 (Colum. Univ., Am. Academy Arts and Soc. Sci, and ECGI, Law Working Paper, No. 541/2020, 2021), https://perma.cc/S64J-KCH3 (explaining investors' increasing demand for ESG disclosures).

373 Christie, *supra* note 372, at 16–17.

374 *Id.* at 21–23.

375 *Id.* at 55.

advise against greenwashing and promote strong ESG targets to avoid the risk of reputational damage.

V. CONCLUSION

This Article laid out the key, sometimes confusing and contradictory, terms that are used to define sustainability in the business context, including CSR, the three pillars of sustainability (environmental, social, and economic welfare), ESG, and the TBL (people, profit and planet). This descriptive information is useful for lawyers, policymakers, investors, and business leaders alike to develop a shared vocabulary.

The role of lawyers in the sustainability space is expanding in the context of corporate governance and finance. Outside counsel and GCs must advise corporate boards of their fiduciary duty to evaluate sustainability benefits and risks, and formal legal (e.g., SEC disclosure and ESG regulation) and informal, non-governmental (e.g., private environmental governance) sustainability disclosure obligations mounting for businesses. Thus, sustainable business law is part of the future of the environmental law canon with initial implementation by lawyers developing sustainable corporate governance and finance mechanisms.

Future research will consider the structure of corporate governance as businesses adopt sustainability metrics, the scope of sustainability disclosure required by U.S. law and demanded by private actors, and the impact of new disclosure laws on companies in the EU. We must also empirically inquire: "What are lawyers in the sustainability space actually doing?" This means cataloging how sustainability, CSR, and risk management law firm practice areas are structured and evaluating what GCs are doing in their day-to-day work that impacts sustainability. How are lawyers involved in a company's sustainability planning?

As the future of environmental law will depend not upon traditional federal command-and-control legislation or executive branch maneuvering, what role will business lawyers play? Sustainable business law activates environmentalism as an expanded substantive area and innovative regulatory technique falling outside the existing, traditional norms of environmental law and legal scholarship. Sustainable business law, as a distinct field, incorporates environmental law, corporate law, and private environmental governance.