Some Do's and Don't's for Voluntary ESG Reporting and Disclosures

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Securities and Capital Markets

Increased attention has recently been given by both investors and the Securities and Exchange Commission (SEC) to promoting clear and comparable disclosures of environmental, social and governance (ESG) factors. On May 21, the SEC's Investor Advisory Committee (Committee) debated and endorsed recommendations of the Investor as Owner Subcommittee (Subcommittee) that the SEC begin in earnest an effort to update the public disclosure reporting framework for companies to include material, decision-useful ESG factors.

The path forward with respect to possible new principles-based SEC disclosure rules around ESG factors may be long and uncertain. Reactions by SEC commissioners to the recommendations are mixed. Pending any new rules, the Subcommittee highlighted that many investors regard certain ESG information in voluntary reports to be material to their voting and investment decisions. But investors complain of the lack of consistent, comparable information, as company voluntary disclosure practices vary widely and third-party data sources often muddle company voluntary disclosures. A Committee member who supported the Subcommittee's recommendations also noted that voluntary ESG reports expose companies to anti-fraud litigation risks for misleading disclosures.

Strong investor demand for voluntary ESG disclosures, coupled with the concomitant risk that courts could find such disclosures to be materially false or misleading, suggests that companies must take great care in formulating these kinds of disclosures. The recommendations below seek to assist companies in preparing voluntary ESG reports.

1 Craft company-tailored ESG disclosures that are significant to investors' investment and voting decisions

- Develop and highlight disclosures based on ESG factors and metrics that are clearly relevant to the company and its industry and meaningful for stakeholders
- Avoid defaulting to a check-the-box approach identified by some third-party frameworks
- Isolate and distinguish softer "greenwash" stories from material ESG disclosures

2 Encourage internal collaboration and apply "disclosure committee" rigor to ESG reports

- Establish a system of collaboration among the teams involved in gathering, drafting, reviewing and publishing ESG disclosures
- Break down organizational barriers to create teams capable of seeing the disclosure from all angles, allowing members throughout the company to bring their particular knowledge and areas of expertise to bear
- Outline and obtain group consensus around key themes and content organization of ESG reports prior to producing comprehensive drafts
- Consider obtaining disclosure committee approval of ESG disclosures before the disclosures are publicly disseminated

3 Bring a "securities lawyer's eye" to ESG disclosures

- Include forward-looking statement disclaimers and/or other hedging language to clarify that the standards or goals described in the ESG disclosures are not guarantees or promises, as well as the factors that could cause material deviations from these standards or goals
- Frame ESG goals in aspirational language, using words such as "seek," "expect" or "strive" and avoid making unqualified commitments, using words such as "shall" or "will"
- Challenge comparative and qualitative statements regarding ESG performance such as "best," "most," "largest" or "first" and assure that the company has adequate back-up for such statements
- Define in plain English any jargon or terms that lack well-understood definitions that are associated with ESG disclosures
- Cross check the company's SEC filings against ESG reports to avoid inconsistencies in facts or degrees of emphasis

4 Internally and externally verify the accuracy of ESG disclosures

- Consider implementing internal and external procedures to assess internal controls around ESG disclosure and measurement and to confirm the accuracy of ESG disclosures
- Consider hiring internal and external sustainability disclosure experts who can evaluate ESG disclosures for overstatements, misstatements or concrete statements that have the potential to become misleading or false through reasons beyond the company's control
- Properly cite and publish independent certifications of ESG data provided by third-party certifiers

5 Be transparent and consistent in methodology for developing and applying ESG metrics

- Consider following all or a part of one of the leading voluntary ESG frameworks, including those promulgated by the Sustainability Accounting Standards Board, the Global Reporting Initiative and the Task Force on and Climate-Related Financial Disclosures, or adopting Science Based Targets to facilitate investors' comparison of the company's ESG metrics with those of other companies
- Just as with non-GAAP financial measure disclosures, consider when including any ESG metric whether the related disclosure provides substantive detail on the usefulness and purpose for investors of such metric
- Clearly and adequately describe how each ESG metric is calculated and clearly track and update progress against stated ESG goals
- Ensure that, if an ESG metric has been presented before, the method of the inputs to the calculation of such metric has not changed since it was previously presented, and if so, revise the relevant metric for the comparable periods consistently and consider explaining why certain inputs to the calculation of such metric have changed
- Avoid misleading graphics such as skewed scales and disproportionate subsets in Venn Diagrams that give a misimpression of quantitative performance on ESG goals

6 Work with and monitor ESG data providers and ratings organizations to ensure that accurate information is disseminated

- Know and be discerning about the many ESG data providers and ratings organizations that use different information sources and standards to conduct their analyses
- Respond carefully and strategically to requests for information from leading ESG data providers and complete them fully and accurately, or risk receiving poor ESG ratings or scores
- Be vigilant about the ESG metrics that data providers publish and seek to correct any material errors that are made (we can attest to having seen such errors), so as not to confuse investors and to maintain clarity in the market regarding the company's true and complete ESG metrics

7 Tend to company sustainability or ESG websites to enhance investor access to pertinent information

- Make ESG information easy for investors to locate, such as by organizing the information on dedicated web pages with a logical taxonomy
- Update web pages regularly with pertinent information and cull outdated information using a standard similar to other investor information pages

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Capital Markets and Securities practice:

Kerry Burke	+1 202 662 5859	kburke@cov.com
Christopher DeCresce	+1 212 841 1017	cdecresce@cov.com
David Engvall	+1 202 662 5307	dengvall@cov.com
Andy Jack	+1 202 662 5232	ajack@cov.com
Brian Rosenzweig	+1 212 841 1108	brosenzweig@cov.com
David Martin	+1 202 662 5128	dmartin@cov.com
Matt Franker	+1 202 662 5895	mfranker@cov.com
Reid Hooper	+1 202 662 5984	rhooper@cov.com
Alex Barlow*	+1 202 662 5077	abarlow@cov.com

*Member of the Bar of New York. District of Columbia bar application pending; supervised by principals of the firm.