

## A Corporate Finance and Securities Legal Update

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### **New Guidance Issued by Securities and Exchange Commission for Climate Change Disclosures by Public Companies**

On February 2, 2010, the Securities and Exchange Commission (“SEC”) published an interpretive release to provide guidance to public companies on the SEC’s existing disclosure requirements relating to climate change. Those requirements apply to registration statements and periodic reports filed under the Securities Act of 1933 and the Securities Exchange Act of 1934.

This is the first time the Commission has addressed climate change disclosures. The interpretive release does not create new legal requirements or modify existing requirements. Instead, the guidance is intended to provide clarity about the requisite disclosures for public companies regarding the impacts of climate change on their businesses. The guidance is meant to foster consistency in the treatment public companies give to their disclosures related to climate change.

#### **Existing SEC Disclosure Rules and Regulations**

The SEC has identified the following disclosure rules and regulations as the source of existing disclosure obligation related to climate change:

- ***Business Description.*** Item 101 of Regulation S-K under the Securities Act requires disclosure of the material effects that compliance with environmental laws may have on capital expenditures, earnings or the competitive position of a company.
- ***Legal Proceedings.*** Item 103 of Regulation S-K requires a company to describe any material pending legal proceedings to which it or any of its subsidiaries is a party. This would include any environmental enforcement actions and orders material to the company.
- ***Management’s Discussion and Analysis (“MD&A”).*** Item 303 of Regulation S-K requires a company to disclose known trends, events, obligations or uncertainties that will, or are reasonably likely to, materially affect the company’s liquidity, capital resources or operations. Companies are also required to disclose any other information the company believes is necessary to an understanding of its financial conditions, changes in financial condition and results of operations.

- **Risk Factors.** Item 503(c) of Regulation S-K requires a public company to provide a discussion of “the most significant factors that make the offering speculative or risky.” A company should clearly state the risk and indicate how the particular risk specifically affects the company and avoid generic risk factor disclosures that could apply to any company.

The interpretive release also notes that Securities Act Rule 408 and Exchange Act Rule 12b-20 require disclosure of all material information, in addition to the information expressly required by SEC regulations, as may be necessary to make a company’s existing disclosures not materially false or misleading.

### **Climate Change Related Disclosures**

The interpretive guidance highlights four specific topics as examples of where climate change may trigger disclosure requirements under the existing rules and regulations summarized above.

- **Impact of Legislation and Regulation:** A company should consider whether existing laws and regulations regarding climate change have a material effect on the company and evaluate the potential impact of pending legislation and regulation related to climate change. These developments may trigger disclosure obligations under Items 101, 103, 503(c) and 303 of Regulation S-K.

In the case of risk factor disclosures (Item 503(c)), companies should consider specific exposure they face as a result of climate change laws and avoid generic risk factor disclosures that could apply to any company. In addition, a company should not limit its disclosure analysis regarding proposed legislation or regulation only to the adverse consequences of those regulations. Rather, companies should also evaluate whether there are any new opportunities afforded to the company by changes in the law or in the company’s business practices that would warrant disclosure under the circumstances. The SEC notes that companies will need to regularly assess their potential disclosure obligations related to climate change since climate change regulation is a rapidly developing area. In addition, disclosures should be attuned to the risks that are particular to the company’s industry. For example, a company in the energy sector may face significantly different risks compared to a company in the transportation sector.

- **Impact of International Accords:** A company should consider and disclose any material risks or effects of international accords and treaties relating to climate change on the company’s business. The need for this disclosure should be assessed by reference to the MD&A disclosure requirements under Item 303 of Regulation S-K (e.g., disclosure of any known trends, events, obligations or uncertainties that will or are reasonably likely to materially impact the company’s liquidity, capital resources or operations).
- **Indirect Consequences of Regulation or Business Trends:** A company should consider, and disclose where material, any indirect consequences of regulation or business trends relating to climate change. Those consequences may occur as a result of legal, technological, political or scientific developments that may create demand for new products or services or decrease demand for existing products or services. For example, a technological innovation

that enables a competitor to produce products that emit lower greenhouse gases could result in an increase in demand for that competitor's products and a corresponding decrease in demand for a company's products. These business trends or risks may trigger disclosure as risk factors under Item 503(c) or as a trend or uncertainty that may have a material favorable or unfavorable impact on the company's business under Item 503.

- **Physical Impacts of Climate Change:** Companies should evaluate the physical impacts of climate change on their businesses. Floods, hurricanes, sea levels, arability of farmland and water availability and quality all have the potential to affect a company's operations and results. Accordingly, companies whose businesses may be vulnerable to severe weather or climate-related events should consider and disclose the material risks of, or consequences from, such events as risk factors under Item 503(c).

### **Further Guidance is Being Considered**

The SEC intends to monitor the impact of this interpretive release as part of the SEC's ongoing disclosure review program. As part of the SEC's evaluation of whether further guidance or rulemaking related to climate change disclosure is necessary, the SEC intends to: (i) review its experience with the disclosure review program, (ii) hold a public roundtable on climate change disclosure in Spring 2010 and consider the information it gains through the roundtable, and (iii) consider any recommendations made by the SEC's Investor Advisory Committee (formed in June 2009 to advise the SEC on matters of concern to investors in the securities markets) which has been considering climate change disclosure issues.

The text of the interpretive release is available at <http://www.sec.gov/rules/interp.shtml>.

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