The Essential ESG Toolkit

Bloomberg Law

Introduction

Environmental, social, and governance (ESG) issues have become increasingly important factors impacting a company's performance. These factors allow investors and consumers the ability to spot potential risks and opportunities. Many jurisdictions, including the European Union and some U.S. states, have adopted legal standards or requirements concerning ESG-related reporting.

As the ESG landscape evolves, general counsel, chief legal officers, and corporate boards must closely monitor the latest developments to ensure they're aligning their corporate purpose with their business strategy, as well as identifying and mitigating potential risks.

In this toolkit, you'll find professional perspectives, overviews, resources, and analysis covering the key ESG issues that are top of mind for corporate counsel, including proposed U.S. and international climate reporting rules, tips for incorporating ESG concerns into M&A deal processes, guidance around managing reputational risk, and more.

This collection offers just a glimpse of the many resources available to Bloomberg Law subscribers. Not a subscriber? **Learn how** Bloomberg Law can help you tackle the complexities of ESG and other essential legal issues and developments.

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Climate Risk Compliance & SEC Enforcement

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The Securities and Exchange Commission has demonstrated that enforcement and regulation of disclosures relating to environmental, social, and governance (ESG) and climate risks are priorities. On March 21, 2022, the SEC proposed rule amendments requiring public companies (issuers) to include certain climate-related information in their public disclosure filings (the issuer rule).

On May 25, 2022 the SEC published a new proposed rule requiring certain investment advisers and investment companies to make ESG disclosures (the investor rule). The SEC also recently settled charges against BNY Mellon Investment Management (BNYM) relating to the investment adviser's ESG disclosures, and charged Vale, SA, a Brazilian mining company, for allegedly making false and misleading claims regarding the safety of a Brazilian dam prior to its collapse.

Although many questions remain as to the final form of the proposed rules, and whether, if adopted, they'll be upheld in the courts, this appears to be the beginning of a new wave of enforcement, and the actions against BNYM and Vale show that the policing of ESG-related disclosures and curbing "greenwashing" are already high priorities of the SEC.

Proposed Rules

The issuer rule would require domestic and foreign issuers to include in their registration statements and periodic reports information relating to climate-related risks, including business impacts and risk management processes, as well as information relating to greenhouse gas (GHG) emissions and climate-related metrics, planning and goals, among other information.

The investor rule would establish disclosure requirements for funds and advisers that market themselves as having an ESG focus. Those funds and advisers would be required to provide more specific disclosures in fund prospectuses, annual reports, and adviser brochures based on the ESG strategies they pursue. For example, funds focusing on the consideration of environmental factors generally would be required to disclose the greenhouse gas emissions associated with their portfolio investments.

The issuer rule was open for public comments through June 17, 2022. The investor rule is open for public comments through August 16, 2022—a deadline that could be extended. After the respective comment periods end, the SEC will consider whether to make further amendments and adopt the proposed rules.

It appears that the SEC is endeavoring to finalize and adopt the issuer rule, or some version of it, before the end of 2022. However, even if the issuer rule and the investor rule are adopted in current form, there will undoubtably be legal challenges that create further uncertainty as to whether and how much of the proposed rules will survive judicial review.

Litigation Certain

Despite the SEC's reference to widespread support for the climate disclosures it has recommended, and significant momentum favoring adoption of the proposed rules in some quarters, the proposed rules will face strong litigation headwinds. Two sources provide an illustrative roadmap for the opposition—first, the dissenting statements of Commissioner Hester Pierce, who opposed the proposed rules, and second, the comments submitted in response to the March 2021 call for comments on proposed climate disclosures by then-Acting Chair Allison Herren Lee.

Two overriding issues predominate: a statutory objection, on the grounds that the Commission is exceeding its limited statutory authority in proposing amendments to Regulations S-K and S-X, and a constitutional objection, on the grounds that the compelled speech required by the proposed amendments violates the First Amendment of the US Constitution.

Statutory Challenge

Objectors to the proposed rules have already argued that the proposed mandatory climate disclosures are neither "necessary" nor "appropriate" to ensure investor protection and fairness in the securities markets, and therefore exceeds the SEC's rule-making authority pursuant to Section 13(a) of the Exchange Act, **15 U.S.C.**

§ 78m(a), which states that the Commission may adopt rules and regulations "as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security …"

For example, in a letter on behalf of himself and 15 other state attorneys general submitted in June 2021, West Virginia Attorney General Patrick Morrisey noted that "the governing statutes make clear that legitimate mandatory disclosures are those required to protect investors from inflated prices and fraud," which letter argues that climate-change disclosures—such as those required by the proposed rules—would not meet that standard.

This argument derives some support from the fact that there is no explicit statute authorizing the proposed rules (although the argument may be stronger with respect to the issuer rule because the Commission does arguably have more regulatory authority under the statutes regulating investment companies and advisers to justify the investor rule).

Indeed, in her comments on the Issuer Rule, Pierce pointed to the Supreme Court's prior statement in *Util. Air Regulatory Grp. v. EPA*, **573 U.S. 302**, 324 (2014)—ironically, an environmental regulation case involving the Environmental Protection Agency (EPA)—with some force: "When an agency claims to discover in a long-extant statute an unheralded power to regulate 'a significant portion of the American economy,'" Pierce quoted, "we typically greet its announcement with a measure of skepticism. We expect Congress to speak clearly if it wishes to assign to an agency decisions of vast 'economic and political significance.'"

Given the Supreme Court's current makeup, the limits of the SEC's statutory authority to promulgate the proposed rules will certainly be tested in court. Indeed, some justices have expressed concern for separation of powers particularly in the context of agency rule-making without clear statutory authorization. See *Nat'l Fed'n of Indep. Bus. v. Dep't of Labor, Occupational Safety & Health Admin.*, **142 S. Ct. 661**, 667 (2022) (Per Curium) (Gorsuch, J., Thomas, J., and Alito, J., concurring); *Gundy v. United States*, **139 S. Ct. 2116**, 2141 (2019) (Gorsuch, J., dissenting).

The Supreme Court may be asked again to apply the "major questions doctrine," which provides that regulatory initiatives with significant economic or societal impacts must be explicitly articulated by Congress. If the "major questions doctrine" supported the court's intervention in the national vaccine mandate, the SEC's climate and ESG disclosure mandates (with less immediately at stake than a national pandemic) may have a similar fate.

Indeed, the Supreme Court's recent decision in *West Virginia v. EPA*, casts further doubt on the proposed rules surviving a challenge based on the application of the major questions doctrine. The Supreme Court applied the major questions doctrine and concluded that the EPA exceeded its authority under the Clean Air Act by establishing emission caps in the Clean Power Plan that would have required a shift in electrical generation from coal to cleaner sources such as natural gas, wind and solar. The Court pointed to the fact that the Clean Power Plan represented a departure from 50 years of regulation under the Clean Air Act and would have implemented a system that Congress has repeatedly refused to adopt. The decision lends further support for the argument that the SEC is similarly discovering a newfound power to regulate issues relating to climate change and emissions, which issues were not traditionally regulated by the SEC in the new manner proposed, under long-standing statutory authority.

Constitutional Challenge

Opponents of the Proposed Rules have also raised First Amendment concerns arising from the compulsion of statements by issuers and advisers, pointing to courts overturning prior regulation by the SEC that would compel speech in violation of the First Amendment. The SEC previously sought to require that issuers using certain minerals from the Democratic Republic of the Congo (DRC) (i.e., gold, tantalum, tin, and tungsten) file a statement that the minerals were not "DRC conflict free" both on their websites and in filings with the SEC.

That particular compelled statement—despite the explicit statutory authorization from the Dodd-Frank Act, which does not exist for the proposed rules—was deemed to be unconstitutional. *Nat'l Ass'n of Manufacturers v. S.E.C.*, **800 F.3d 518**, 553 (D.C. Cir. 2015). The court concluded that, even assuming the government had a sufficient interest in requiring companies to make the compelled statement (i.e., to lessen the humanitarian crisis in the DRC), the SEC failed to carry its burden of proving that the compelled statement was effective in achieving that objective.

Furthermore, the court concluded that even if the government interest were sufficient, and even if the chosen means to achieve the objective was effective, the statement was still not "purely factual and uncontroversial."

Given that the proposed rules would require disclosures and attestations regarding GHG emissions and climate change risks and impacts, among other topics—without express statutory authorization such as that found in the Dodd-Frank Act for the "DRC conflict free" regulation which was nonetheless ruled unconstitutional—there are questions as to whether the proposed rules will survive judicial review. Ultimately, a court will decide whether the government's interest in the proposed rules is of sufficient weight, whether the required disclosures are tailored to achieve that purpose, and whether the resulting statements compelled are "purely factual and uncontroversial."

Regulatory Framework

Companies must also grapple with the shifting regulatory framework on climate impacts, in particular with respect to GHG emissions. Although the issuer rule only requires disclosures by public companies and the investor rule only requires disclosures in certain situations, they will nonetheless impact private companies. The issuer Rule will reach vendors, suppliers and even customers of larger public companies, as those issuers seek more information regarding upstream and downstream GHG emissions resulting from their business operations. The investor rule might also reach private companies to the extent they have ESG-focused funds as investors or are part of an investment adviser's ESG-related strategy.

Under the issuer rule, issuers would be required to disclose quantitative information about their own direct GHG emissions (Scope 1), namely those directly generated by the company's facilities and vehicles; and indirect GHG emissions (Scope 2), namely those generated to create the electricity/energy consumed by the company in its operations. Certain issuers would also be required to disclose quantitative information about indirect emissions from upstream and downstream activities in the issuer's value chain (Scope 3) if either material, or the issuer has set a GHG emission target that includes Scope 3 emissions.

That would have wide-ranging implications as any issuers required to make disclosures regarding Scope 3 emissions would seek information regarding the GHG emissions and operations of the participants in their value chain in order to assess the materiality of their Scope 3 emissions. This materiality assessment would require issuers to attempt to collect or estimate GHG emissions information from third parties, regardless of whether those third parties are publicly traded and/or obligated to make GHG disclosures themselves.

Many issuers are already making GHG emissions disclosures to other regulatory agencies, and will have to carefully consider the consistency of reporting under different and evolving standards. For example, many companies with significant emissions sources are already required to report on GHG emissions to the EPA and/or state regulatory agencies. Although the SEC notes that its proposed reporting requirements would be consistent with the EPA's 2009 Mandatory Reporting of Greenhouse Gases Rule (**40 C.F.R.Part 98**), issuers will likely not be able to rely on the same reporting.

That is because the EPA rule generally requires facility-specific reporting, but the issuer rule requires organizational reporting. Additionally, any reporting required to be made to state agencies may not be consistent with the GHG Protocol methodology that the issuer rule would adopt.

As a result, companies may need to collect more emissions-related data than already compiled for the EPA and state agencies in order to comply with SEC reporting requirements. Further muddying the water is the Supreme Court's decision in *West Virginia v. EPA* limiting the EPA's regulation of GHG emissions, and raising questions as to any federal regulations relating to climate change and GHG emissions absent clear Congressional authority. The SEC's issuer rule would also extend to more companies than are already reporting GHG emissions to the EPA. In either instance, this means higher costs for companies both to collect the data needed for reporting and to compile that data into unique reports for each overlapping reporting requirement.

In particular, energy companies will face unique challenges as they also disclose information relating to GHG emissions to the Federal Energy Regulatory Commission (FERC). But the FERC's GHG policy is in transition. In February 2022, the FERC approved an **Updated Policy Statement on Certification of New Interstate Natural Gas Facilities** and the **Interim Policy Statement** (GHG Policy), which would have significantly changed the manner in which FERC quantified GHG emissions.

Notably, the GHG policy stated that the FERC will follow the Council on Environmental Quality (CEQ) regulations to quantify GHG emissions. But those regulations are also in flux, as CEQ rescinded its 2019 draft guidance on the consideration of GHG emissions in February 2021, and is now reviewing, for revision and update, its 2016 final guidance. However, on March 24, 2022, the FERC issued an order making the Updated Policy Statement and GHG Policy draft policies and inviting comments and reply comments over the next 60 days. The final form of the FERC's new policies (and the CEQ regulations) remains unclear, and, as with the SEC's Proposed Rules and the EPA's regulations, there will likely be legal challenges.

For international companies, there are also global climate disclosure standards to consider. There is an ongoing effort to consolidate global reporting standards, as the International Financial Reporting Standards (IFRS) Foundation formed a new International Sustainability Standards Board (ISSB) that will develop a comprehensive global baseline for sustainability disclosure standards.

The ISSB developed prototype disclosure requirements from the joint efforts of a number of organizations, including the Task Force on Climate-Related Financial Disclosures (TCFD)—whose "four pillar" disclosure framework heavily influenced the SEC's proposed rules—and with the support of the International Organization of Securities Commissions (IOSCO) regulators.

The standards being developed by the ISSB—to be known as the IFRS Sustainability Disclosure Standards—are intended to be compatible with the IFRS Accounting Standards used in most jurisdictions other than the US. While the SEC is certainly aware of the ISSB standards and may take such standards into consideration in the future, it appears that the SEC intends to develop its own standards rather than adopt any international standard. Again, this means that companies may have to collect additional data or quantify and report it differently for the SEC than for international securities commissions.

What Companies Can Do Now

Although the timing and eventual fate of the proposed rules are uncertain, we expect both regulators and investors to continue to focus on and advocate for increased disclosures on ESG and climate-related risks. SEC chair Gary Gensler recently emphasized that climate disclosures are already happening and his belief that the proposed rules are consistent with the SEC's central mission to protect investors, maintain fair, orderly, and efficient markets and facilitate capital formation.

The adopted version of the proposed rules may be delayed or scaled down in the future, whether in response to comments or legal challenges, or the Supreme Court's decision in *West Virginia v. EPA*, but it appears some version of the proposed rules are likely to be enacted eventually. Given the uncertainty posed by the evolving standards for climate disclosures and legal challenges to regulations on climate change, ensuring consistency and compliance across all reporting and disclosures of climate change issues, especially GHG emissions, will require careful scrutiny and coordination between a company's legal, reporting, risk management and corporate communications groups.

For example, the sample comment letter provided by the SEC in September 2021 indicated that the SEC might ask for an explanation if a company provides more climate-related disclosures in an ESG report or CSR report than in its SEC filing.

Regardless of the outcome of the proposed rules, it is clear that with the SEC's launch of an ESG enforcement task force in March 2021 and the recent actions against BNYM and Vale, companies should expect a continued focus on regulation and enforcement actions relating to ESG disclosures. With that in mind, companies should consider the following steps to plan for a future of enhanced regulation on ESG and climate change impacts:

- determine whether sufficient resources are dedicated to monitoring and evaluating climate-related risks.
- determine whether sufficient management and board expertise exists to assess climate-related risks.
- take steps to ensure collection and evaluation of appropriate data, including GHG emissions data, for purposes of monitoring and evaluating climate-related risks, as well as for reporting Scope 1 and 2 emissions (and, where relevant, Scope 3 emissions).
- determine whether financial and audit teams have sufficient expertise to provide guidance and management of the changing financial statement presentations that would be required under the proposed rules.

- review internal controls and processes to ensure consistency and coordination of reporting across regulatory filings, corporate social responsibility (CSR) reports and company statements on climate related-risks and GHG emissions.
- determine whether appropriate policies, procedures, and controls are in place to monitor and evaluate performance against sustainability or ESG plans and targets, both qualitatively and quantitatively.
- if GHG emissions are already tracked, determine what additional data is necessary to comply with the SEC's disclosure requirements and what additional processes are needed to track GHG emissions.
- for larger companies that may be required to make disclosures regarding Scope 3 emissions, consider whether and how to collect emissions data from private companies both upstream and downstream in the value chain and engage with key suppliers, vendors, and customers regarding that process.
- for private companies in the value chain of large public companies, consider what processes are needed to track emissions to provide the data that large public companies will seek for Scope 3 emissions.
- for private companies, consider whether your investors are going to be subject to the investor rule and thus require heightened disclosures from you.
- carefully vet all public statements regarding climate risk to avoid material misstatements or material omissions that could elicit either government enforcement action or private securities litigation.

FINANCIAL ACCOUNTING:

Bigger ESG Changes Loom After Climate Reporting Rules: Explained

by Amanda Iacone, Reporter and Michael Kapoor, Freelance Correspondent, Bloomberg News
April 26, 2022

Corporate reporting proposals released by both the U.S. securities regulator and the International Sustainability Standards Board in March would give investors more reliable details about the air pollution that companies emit and what steps they are taking to avoid risks that a warming planet poses to their operations.

But efforts to shed more light on greenhouse gas emissions are likely the beginning of a sweeping shift in corporate reporting requirements globally. On the international front, the ISSB and the European Commission are considering a wide range of disclosures – from clean water to biodiversity to human rights.

Those measures would go far beyond climate disclosures. Here's a look at international efforts to force companies to report in detail about their impact on the world.

What has the ISSB proposed?

The ISSB was launched in November to develop formal reporting standards spanning the full range of environmental, social and governance issues. In March it issued drafts for the first two of these standards covering climate and general sustainability reporting.

Over the next year the board plans to consult over which areas to tackle next, aiming to create a baseline set of ESG reporting requirements similar to international financial accounting standards used by most large countries. The standards will be aimed specifically at investors, many of whom have said sustainability issues are central to gauging a company's long-term viability.

The standards would mean investors not only get more information, but also could compare companies' disclosures about such issues as gender, diversity, and corporate governance. Sustainability would be reported in the management commentary section of companies' annual report.

Who would have to follow ISSB reporting standards?

A wide range of countries look likely to adhere to the international sustainability rules. But none have formally adopted the standards, which haven't been written yet. Most big markets—including the U.S., China, and the E.U.—supported the ISSB's launch, and a global group of stock market regulators has said it will probably recommend that its members follow the ISSB rules.

But individual countries still would have to adopt the standards as part of their national requirements, much like the financial accounting rules set by the board's sister body: the International Accounting Standards Board, whose accounting rules are required by 140 countries worldwide.

Most large companies globally already publish a sustainability report, but they use a plethora of voluntary frameworks. Companies and investors have been calling for a single set of international standards to cut through an alphabet soup of competing standards and provide more consistent and comparable figures.

How does this fit in with the EU proposal?

The European Union wants to go much further than the ISSB. Legislation likely to be adopted this year would require companies to report on the damage they are doing to society, as well the various ESG related threats they face from an investor's viewpoint.

Nearly 50,000 companies that employ more than 250 people—both private and public—would have to follow its rules. Under the draft legislation, companies would have to meet the EU's broad reporting requirements as soon as fiscal year 2023.

What has the U.S. proposed, and is it separate from the ISSB?

Yes, the U.S. proposal is separate from the ISSB plans. The U.S.—among several countries to propose specific climate requirements—would compel publicly traded companies to give investors more details about the sources of their greenhouse gas pollution and describe what risks a warming planet could pose to their business and financial results, under draft rules the Securities and Exchange Commission released in March. If adopted, the largest U.S. filers could begin applying the rules in their 2023 annual reports

Although mandatory climate reporting is a top policy goal for the Biden administration's environmental agenda, legal and political challenges could derail the requirements, which are coming from a regulator, not lawmakers.

The U.S. proposal holds the door open to using global standards, asking if the SEC should accept climate reporting based on international sustainability standards. The SEC is also working on separate rules that would expand what companies should say about their employees and the diversity of their boards.

So what happens now?

The big question is over what individual countries will require, and when. The EU has said that it wants its broader reporting mandate to serve as a template for other markets in setting ESG requirements.

Because the ISSB is run by the same entity that has set international accounting rules for many years, its ESG reporting standards could be required by many of the countries that already follow global accounting standards. Some countries may opt to mirror the EU's wider approach, forcing companies to admit to the damage they do to the world as well as the threats they face from it.

The ISSB and EU approaches are designed to be complementary, and their specific climate requirements would pair with the SEC's draft rules. Still U.S. companies should pay attention to both the new standardsetter and the EU policy agenda as subsidiaries operating in Europe and beyond could have to comply with both sets of reporting frameworks.

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Hospitals Confront Their Climate Achilles Heel: Supply Chains

By **Shira Stein**
Reporter, Bloomberg Law
June 7, 2022

The health-care industry accounts for 8.5% of the United States' greenhouse gas emissions, almost as much as agriculture. So the Biden administration is pushing hospital systems to do more to combat climate change: The US Department of Health and Human Services has asked hospitals, health suppliers, drug companies and others in the industry to pledge to reduce their GHG emissions to net zero by 2050, inventory their supply chain emissions and develop a climate resilience plan for their facilities.

Some hospitals have already taken carbon-cutting steps like installing on-site solar power, purchasing renewable energy, and improving energy efficiency in their buildings. But the vast majority of emissions in the sector – 80% – come from the medical supply chain. These are difficult for hospitals to address because they're not under their direct control.

Health-care leaders are now looking for ways to cut these Scope 3 emissions, knowing that otherwise, attempts to decarbonize the sector will fall short.

"The supply chain is absolutely critical to this success," HHS Assistant Secretary for Health Rachel Levine said. "Without dealing with the supply chain, we won't be successful and that's a challenge, but we're going to work on it."

Chemicals, pharmaceuticals, medical devices and food are among the largest contributors to hospitals' supply-chain emissions, said Jodi Sherman, a professor at the Yale School of Medicine and director of the Yale Program on Healthcare Environmental Sustainability. Addressing the unsustainable supply chain has become even more critical after hospitals experienced shortages during the Covid-19 pandemic. Nurses and doctors had to reuse masks and gowns using protocols that hadn't been fully tested for safety. Finding ways to use those items more efficiently could help with both emissions and future disruptions, including those stemming from climate-related weather events.

Deciding what products to use in the operating room can be "a little bit harder" than where to get a hospital's energy from because it involves more decision-makers, according to Lovisa Gustafsson, vice president of controlling health-care costs at the Commonwealth Fund, which promotes improvement and equity in health care. "You never want to dvo anything that's going to sacrifice quality of care or access to care, or anything like that. But there definitely are questions there in terms of how things could be done in a better way," she said.

There has been a perception in the sector that green initiatives are costly, but "you're choosing to eliminate waste, and waste is usually associated

A worker pulls a cart of medical products at a Dealmed-Park Surgical supply f acility in Lakewood, New Jersey, on March 11, 2020.

Photographer: Victor J. Blue/ Bloomberg

with cost," said Matthew Meyer, co-chair of the University of Virginia health sustainability committee and a professor of anesthesiology. A 2019 study found that the cost of waste to the US health-care system is $760 billion to $935 billion annually.

To curtail their Scope 3 emissions, health systems are considering putting pressure on their suppliers to move toward more sustainable practices. They are also trying to stem the consumption of single-use items inside their walls.

Hospitals have a major card to play when it comes to getting their suppliers to address their climate footprint—massive purchasing power. They typically get medical supplies from distributors like McKesson Corp. and AmerisourceBergen Corp., and often partner with other hospitals to use their collective purchasing power to negotiate discounts. If one large hospital system or one of these groups pushes their suppliers on addressing emissions, that could affect a supplier's bottom line, and "these companies will start to take notice," Meyer said.

AmerisourceBergen, one of the largest medical supply distributors in the US, signed the HHS pledge and plans to reduce its Scope 1 and 2 emissions by 50% in 2032, a spokesperson said. The company says it is cutting carbon through more efficient energy usage in buildings and transportation and by expanding its renewable energy portfolio.

At least two major hospital systems — Kaiser Permanente and Providence Health and Services — are already working with suppliers on strategies to tamp down on emissions, the systems said. Health Care Without Harm, an advocacy organization focused on addressing climate change in health care, has been consulting with its members to put together questions that health systems can ask suppliers, such as whether they are monitoring their emissions or have an action plan to reduce them, said Antonia Herzog, associate director of climate policy and advocacy.

If the whole health-care system is demanding this, "vendors are going to have the option to either be public about this information and work to make their product the most sustainable … or they're going to risk losing the contract," Meyer said.

Researchers and hospitals are looking to the UK's National Health Service as a model. It has a plan to decarbonize by 2045 and has reduced its emissions by 26% from 1990 to 2020. The NHS requires its larger suppliers to report their greenhouse gas emissions through a standardized framework, benchmark them and manage them with a goal of getting to net zero, Sherman said, and it plans to work with smaller suppliers to try to reach the same goal.

Hospitals can also control how much waste they produce. Many items used daily are designed to be discarded after a single use, which is both expensive and bad for the environment.

Non-reusable items like syringes and IV tubing don't account for most of the waste. Things like blood pressure cuffs, pulse oximetry probes, bed linens and even expensive devices such as laparoscopic instruments are often designed for disposal when they could be sterilized and used again. The manufacture of replacements for these discarded items generates more emissions.

Sherman calls this an "unscrutinized, out of control, largely non-evidence-based trend," which has left the US vulnerable to supply-chain interruptions both from health emergencies like Covid-19 and climaterelated extreme weather. The federal government could require companies seeking Food and Drug Administration approval to design their products for reuse and to include that in their applications, she added.

Hospitals also routinely throw away billions of dollars worth of drugs each year because the vials are large and regulations prohibit them from being split between patients. "In the operating room, I have a vial that is 99 times more than I need. And I have to throw it away," said Sherman. Potential solutions modeled on the NHS include hospitals buying right-sized packages and only stocking the amount of a drug they need, to avoid having expired stock that has to be tossed out.

Seema Wadhwa, executive director of environmental stewardship at Kaiser, said the system recently worked with its supplier for disinfecting wipes to cut waste. Normally the wipes come in a hard-case canister that has residual chemicals considered hazardous. The supplier now provides the wipes in containers like those that hold diaper wipes. They can be transported more easily, create less waste and don't have the dangerous chemicals.

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ANALYSIS:

Tips for Powering Up ESG Diligence and Reps in M&A

By **Emily Rouleau**
April 29, 2022

As important as environmental, social, and governance issues have become in the corporate world, I wondered whether the standard M&A deal process was keeping up. Researching Bloomberg Law's Transactional Precedents, that does not appear to have happened yet. At a minimum, the standard environmental- and governance-related representations and warranties buyers customarily use in M&A agreements come up short on ESG details.

To get the proverbial "jump on it" and, possibly more importantly, to align acquisitions with ESG commitments of buyers, target companies, and investors, I recommend that buyers and their counsel take action to address ESG issues more fully, during both the due diligence and the drafting stages of the M&A deal timeline.

Specifically, buyers should (1) ensure that ESG is covered thoroughly during the due diligence process, both in terms of commitments the target company has made and expectations the buyer and investors have, and (2) consider including a fulsome ESG representation and warranty in the agreement itself. Without doing so, buyers expose themselves to the same potential liabilities and reputational harm that they would for any other problems that were superficially investigated during due diligence or inadequately addressed in a merger or purchase agreement.

Investigate ESG Issues During Due Diligence

Standard buyer due diligence requests often ask for information on a target company's (1) environmental compliance, such as asking the company to identify whether it uses hazardous materials and to describe whether it has been the subject of any environmental investigations, audits, or penalties; (2) social issues, such as asking the company to provide employee handbooks, employment policies, and lists of all employees and contractors; and (3) governance issues, such as asking the company to identify its officers and board members and to provide the resolutions or minutes from their appointments. But these requests do not go far enough.

ESG is now more complex, and its elements are less tangible, than these more conventional requests. How does a buyer ensure that a target company is making meaningful ESG decisions? Buyers should boost their diligence requests—either initially or through supplemental diligence—to drill down deeper into the ESG landscape. Here are some questions worth asking:

Environmental

1. What are the levels of the company's greenhouse gas emissions?
2. How does the company measure its carbon footprint?
3. What steps has the company taken to be more sustainable?
4. Has the company set any goals for greenhouse gas emissions and/or sustainability efforts? If so, what goals? What are the deadlines for the company to achieve these goals?
5. Has the company issued any public statements or published marketing materials related to the above referenced goals? If so, please provide a copy of all materials.
6. Have any of the company's goals been achieved?
7. Has the company failed to achieve any goals? If so, what were the reasons for failing to reach those goals? How has the company changed its processes in response to same?
8. What processes are in place to ensure the company achieves the goals by the deadlines?
9. Who is responsible for overseeing the company's environmental and sustainability goals? Is there a committee?

Social

1. Has the company conducted customer satisfaction surveys or studies? If so, please provide a copy of same.

2. How often does the company measure customer satisfaction? What does the company do with the results? Please provide copies of all related policies and procedures.
3. Does the company study and measure employee satisfaction and retention? If so, how does the company measure employee satisfaction and retention? Please provide copies of all related documentation.
4. Does the company have processes in place to vet suppliers and vendors? How does the company ensure that suppliers and vendors do not participate in human rights violations? Please provide copies of all policies.
5. How does the company approach sexual harassment and #MeToo issues? Is there a written policy? Has the company received any complaints, claims, allegations, or other HR reports?
6. Has the company set any goals related to company culture, diversity, equity, and inclusion, or other social issues? If so, what goals? What are the deadlines for the company to achieve these goals?
7. Has the company issued any public statements or published marketing materials related to the abovereferenced goals? If so, please provide a copy of all materials.
8. Has the company achieved any of the above-referenced goals?
9. Has the company failed to achieve any goals? If so, what were the reasons for failing to reach those goals? How has the company changed its processes in response to same?
10. What processes are in place to ensure the company achieves its stated goals by the assigned deadlines?
11. Who is responsible for overseeing the company's social goals? Is there a committee?

Governance

1. Does the company have a DEI advisory committee? If so, how is it structured? Who is part of the committee?
2. Does the company have cybersecurity, data privacy, and breach notification policies? If so, please provide copies of same.
3. If there is a cyber incident or data breach, what are the company's response procedures? Who is involved in the response? Please provide copies of relevant documents.
4. Does the company have an ESG-related committee or team? If so, how is it structured? Who is part of the committee or team?
5. How do the company's board and executive officers view and approach ESG issues?
6. What managers, officers, directors, and/or executives are involved in ESG initiatives?
7. Does the company have incentives for executives that are related to ESG issues? If so, how are the incentives structured, monitored, and awarded?

Yes, the due diligence process is expensive, efficiency is of the utmost importance, and delving into ESG may increase some fees at the start. But the extra analysis of a target company's ESG may save the buyer in the long run by identifying risks or liabilities that can then be negotiated, properly allocated, fully disclosed, and sufficiently addressed in the resulting merger or purchase agreement.

Include Comprehensive Reps, Warranties in the Agreement

As M&A lawyers know, buyers use a target's representations and warranties to address and disclose potential risks or liabilities—such as pending claims or litigation, assignment or change-of-control obligations, and existing debt or loans—likely identified during due diligence. The same logic can and should be applied to ESG issues. Like conventional due diligence, standard reps and warranties—such as those stating a target company has had no environmental violations and is properly authorized to enter into the transaction—fail to address the full scope of today's ESG priorities.

As I mentioned earlier, I conducted a search of Transactional Precedents, and was surprised to see so few publicly available M&A agreements with ESG-dedicated provisions—or even with references to ESG at all. The Transactional Precedents Search pulls agreements from EDGAR, so I thought that there might be more such agreements here than are typically seen in private companies' M&A activities.

That being said, my search for M&A deals with agreements that included references to "ESG" (or combinations of "environmental," "social," and "governance") yielded just 55 agreements as of April 27. Broadening the searches to add specific components of ESG among the search terms—such as "climate change," "sustainability," "human trafficking," or "DEI" or its components—still yielded fewer than 200 agreements in each search, out of thousands of precedent agreements available on the database since 1996.

Many of the agreements that referenced "climate change" did so in the definitions of environmental laws for that particular agreement or in the definitions of "material adverse effect," rather than in actual ESGrelated statements. Agreements that referenced "human rights" most often did so in the form of general representations that a party abided by applicable laws, including those related to human rights.

In contrast to the generic references to climate change and human rights, the agreements that referenced "human trafficking" did so in dedicated reps and warranties related to slavery and human trafficking. In three agreements governed by Delaware law, the target company represented that it complied with all human trafficking and slavery laws. In each of the three agreements, the target company also represented to compliance with human trafficking laws and its supply chain.

Specifically, two agreements represented that the target company complied with the California Transparency in Supply Chains Act, and the third agreement represented that the target company maintained a system of internal controls "reasonably designed to ensure compliance with Human Trafficking and Slavery Laws, including with respect to its supply chain."

Other agreements from the searches conducted did contain references to ESG or had other ESG-related provisions. The agreements did not always include references to ESG in the reps and warranties themselves; some discussed ESG only in closing covenants.

For example, a business combination agreement included post-closing covenants requiring the company to use a set amount of funds for activities that include the analysis of risks and opportunities associated with potential M&A transactions, which includes the review of environmental, social, and governance risks.

A merger agreement represented that the target company did not have contracts for services performed, related to, or the product of ESG indices.

Another merger agreement included covenants that the surviving corporation "may continue its work plan on diversity, equity, inclusion, and justice for no less than one (1) year following the Closing Date."

This same agreement then included covenants for the parent company stating that, among other things, "[w]ithin one (1) year of the Closing Date, [the parent company] shall: ... create an impact committee that focuses on climate change, social impact, diversity, and community relations."

And an asset purchase agreement included a financing covenant that the sellers would use reasonable best efforts to provide responses to ESG questionnaires.

Overall, ESG is a topic addressed in some precedent agreements, but these agreements are sparse when it comes to ESG reps and warranties. Furthermore, the agreements reveal no consistent approach to addressing ESG matters (except for the dedicated reps related to human trafficking and modern slavery).

Considering that regulators and individual companies are paying closer attention to the reputational impacts ESG issues can have, I imagine that buyers' general lack of explicit coverage of novel ESG issues in M&A agreements will change, and that buyers and their counsel will need to include comprehensive ESG reps and warranties as part of their normal M&A practice.

Therefore, depending on the results of the due diligence process, it is important for buyers to consider including comprehensive ESG reps and warranties in purchase or merger agreements.

For example, buyers should:

1. Consider adding additional representations addressing sustainability, greenhouse gas emissions, or other climate-change related issues to existing environmental law reps and warranties.
2. State in a rep that the target company will continue toward achieving sustainability goals (if the target company has set such goals) in the normal course of business until and/or after the closing, depending on the structure of the transaction.
3. Add corresponding details to existing governance reps and warranties.

4. Create subsections that address the management approach to ESG, the target company's committees, and how management incentivizes work towards ESG goals.
5. Add a rep regarding the social aspect of ESG, so that the target company represents and warrants how it handles diversity, equity, and inclusion as well as overall workplace culture and #MeToo concerns.
6. Remember that ESG-related reps and warranties could include disclosures of any liabilities, complaints, or risks, so include references to disclosure schedules as applicable.

By fleshing out ESG issues and including additional ESG-specific reps and warranties in the purchase or merger agreement, buyers can better protect themselves and increase the possibility that they would have claims for breaches of the reps and warranties if ESG issues arise post-closing. And, if buyers believe a target company has risks or pending liabilities related to ESG, adding these provisions can ensure that the target company discloses those risks and liabilities. Buyers would also be able to negotiate the inclusion of indemnification language to address such issues in the merger or purchase agreement.

Overall, the information gleaned through detailed due diligence of the target company's ESG issues will best inform a buyer of any liabilities and risks—or, conversely, any reputational benefits a buyer may gain from a target company's ESG successes. Regardless, buyers will benefit from fulsome ESG due diligence and from the resulting merger or purchase agreements that more fully address ESG issues and more accurately reflect the value and risks buyers assume at closing.

Bloomberg Law subscribers can find related content on our Practical Guidance: ***ESG Risk Management and ESG Practice pages, as well as our M&A Deal Analytics resources.***

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Energy-Sector Shareholders Have Begun to Act Globally

By Abigail Gampher
April 19, 2022

Public investor activists have waged very few campaigns against energy-sector corporations so far this year. But there are indications that stakeholders are looking beyond traditional objectives and pushing for change on issues such as the energy industry's environmental and social responsibilities and its involvement with global conflicts like the war in Ukraine.

Only six investor activism campaigns in the energy sector have been publicly announced in 2022. That is well off the pace of recent years: Energy companies were faced with 48 campaigns in 2019, 40 in 2020, and 39 in 2021.

In terms of what activists are asking for, 2022 so far has been similarly quiet. The first quarter included only eight investor activist objectives within the energy sector, falling within four different categorizations: four board actions, one cost change and realization action, one corporate reorganization action, and two other.

Despite the low level of recent activity, we still should expect investor activists to go beyond traditional corporate campaign types that target management and the board as the year progresses.

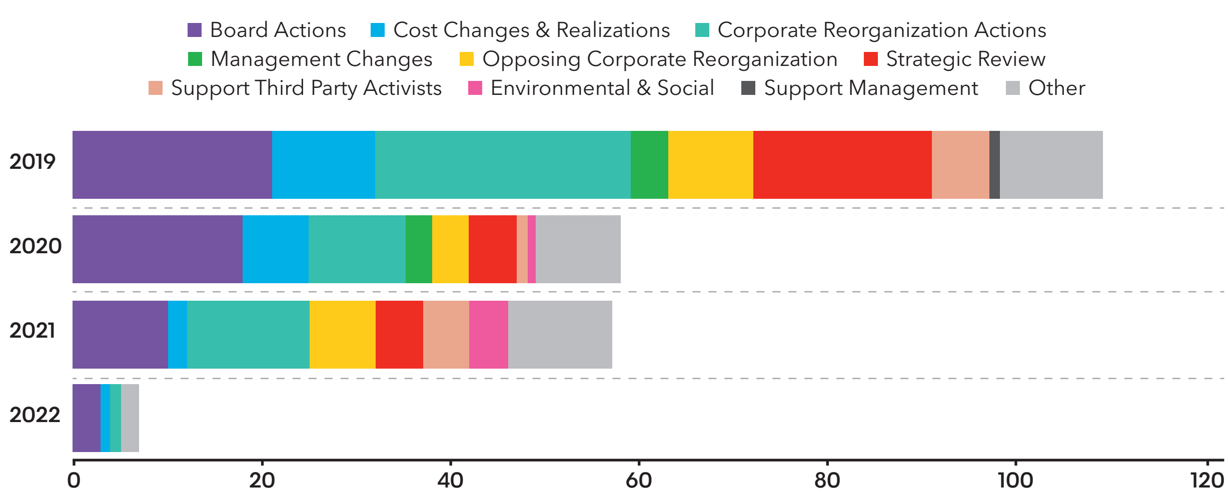
In the past two years, environmentally and socially focused activist campaigns have targeted the energy sector's ESG-related policies, and that trend could continue into 2022.

A look at recent patterns in energy-sector shareholder proposals suggests that greater stakeholder scrutiny in this area may be coming in the next quarter, ahead of annual shareholder meetings. In each of the past four years, the number of proposals filed by energy company shareholders in the "environmental and social" category has increased from Q1 to Q2.

A Shift in Stakeholder Objectives

Beyond environmental and social issues, where we can expect energy-sector stakeholders to make the most high-profile shift is even further outside of traditional areas, and into the realm of global affairs.

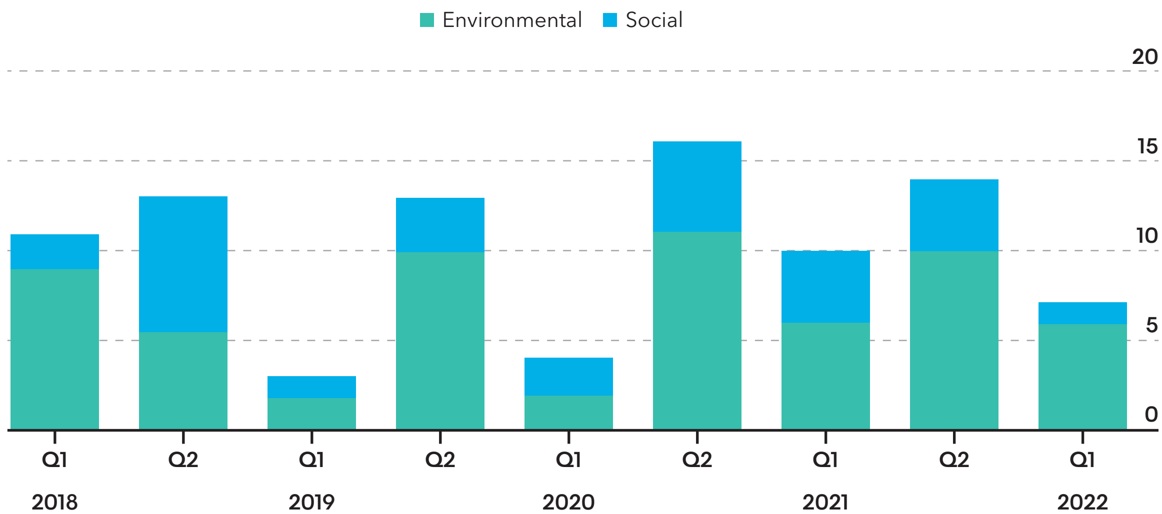
2022 Investor Activist Campaigns in Energy Sector Off to Slow Start
Number of objectives addressed by campaigns against energy companies



Source: Bloomberg as of April 15, 2022. Investor activism campaign objectives are sorted by campaign start date. For campaigns with multiple objectives, each objective is included in the data. Stake-only activism campaigns were excluded from the data.

Is a Boost in Environmental/Social Shareholder Proposals Ahead?

Q1-to-Q2 changes in shareholder proposals filed against energy companies



Source: Bloomberg as of April 15, 2022. Data filtered by energy sector and environmental and social proposal category

Activist Clearway Capital's campaign, launched on March 11, aims for TotalEnergies SE to exit Russian operations. The Clearway Capital campaign is the first public campaign to specifically target a company's country-specific operations in response to an international conflict since Bloomberg started tracking all public investor activism in 2017. While TotalEnergies announced that it will not divest its Russian assets, Clearway indicated that it is poised to submit a shareholder proposal if Total does not meet its demands ahead of the company's May 25 annual general meeting.

Shareholder proposals may be reflecting a similar shift into global affairs. Chevron Corp. received a shareholder proposal April 7th to report on business with conflict-complicit governments, based on the company's involvement in Myanmar. Chevron's Board urged shareholders to vote against the proposal, which remains pending. The proposal, for Chevron to create and enforce a general conflict policy in response to operations in a particular country, may spur shareholders to go beyond the isolated requests of investor activists and seek lasting conflict policies for energy companies.

As energy sector stakeholders prepare for annual meetings, we should expect them to urge new ways for companies to shape their environmental and social policies and limit operations involving armed conflict.

Bloomberg Law subscribers can find related content on our ***ESG Practice page, as well as our Practical Guidance: Shareholders page*****.**

PRACTICAL GUIDANCE:

ESG, Professional Perspective – Legal Counsel's Role in Enforcing Net-Zero Plans

Contributed by **Amit Garg**, smartContract CLM &
Nancy Nelson, ABiz Corporation May 2022

Net-zero transitions are high on the corporate agenda with increasing pressure on businesses to acknowledge their responsibilities to the environment. Those who don't have a robust environment, social, and governance (ESG) strategy are finding it increasingly difficult to find partners in this business environment.

The concept of net-zero transition plans requires emissions of an organization to be reduced as much as possible and the remaining emissions to be captured from the atmosphere to achieve a net balance.

The challenge for companies is to find sufficient land, time, and resources to produce the carbon credits—let's say, through increased planting—needed to satisfy the demand for offsets.

To avert this carbon crunch, there is a need to innovate and find different ways to both reduce emissions and capture carbon from the atmosphere. This is what makes it difficult for companies to follow through on their targets and enforce their action plans.

Why Legal?

Net-zero is not required by law, but in-house lawyers are still expected to play a key leadership role. So how does legal expertise support the transition?

In-house lawyers are the conscience of their companies, and are uniquely placed to influence the executive board and spearhead strategic change. Therefore, a subject like net-zero, defined by social conscience, needs the in-house lawyer's influence as well as skills to carry out the practical aspects of embedding policy.

Legal professionals touch so many parts of an organization that they are among the few that have the ability to connect the dots and ensure their business follows a consistent approach. ESG, Professional Perspective - Legal Counsel's Role in Enforcing Net-Zero Plans They have the power to measure and enforce the steps required to achieve the ambitious netzero targets of organizations.

Take contracts for example—these are bespoke documents with obligations and specific terms that can break down the humongous puzzle of achieving net-zero into enforceable pieces, such as Corporate Social Responsibility (CSR) policy clauses or mandatory green reporting by suppliers and other stakeholders.

When you put requirements into a contract, it is reviewed by multiple parties and priced in. The next step is to ensure effective post-execution management of contracts so those obligations are not overlooked. Legal can take the lead to ensure these terms and obligations cascade to operations, suppliers, customers, and other stakeholders.

Another important aspect of the role of legal counsel in the transition to net-zero is being able to present opportunities to better align the in-house legal team to the wider commercial strategy and future-proof the organization.

A case in point is aligning progress on climate change and other ethical issues like inequality to the commercial strategy. The legal function's role becomes much more holistic in this context. Businesses need help from their legal teams to put in place requisite risk management systems, practices, and procedures. The role is to provide foresight about unwanted risk by ensuring that current net-zero and other ESG strategies are aligned with the direction of the current, evolving, and future regulations in a way that benefits society and shareholders.

Playing the Part

In-house lawyers should start by helping to develop the right net-zero path for their company and consider their part in achieving the relevant targets. They need to be able to react incredibly quickly with a refreshed vocabulary around climate-related threats to business and put changing business priorities in their immediate focus.

"Playing the part" for legal counsel may—and often will—vary from organization to organization based on a range of factors including jurisdiction, regulation, industry, and more. But here are some points that can guide legal departments to tailor their framework to align to the organization's net-zero transition plan.

Steer Clear of 'Greenwashing'

Undoubtedly, it is important to seek opportunities to promote the good work that the company is doing to increase the company's trustworthiness and foster a positive overall public opinion of its efforts. But it is all the more important to beware of the "say-do" gap as it increasingly has the potential to inflict reputational, commercial, or financial damage to companies.

There have been many reports of regulatory and shareholder blowback on companies that fail to take serious action to achieve their self-established ESG commitments. Concerns over greenwashing of in-demand "green" financial products have also drawn the attention of the U.K.'s Financial Conduct Authority (FCA). In July 2021, a "Dear Chair" letter was published by the FCA to set out guiding principles for interpretation of current rules on the design, delivery, and disclosure in respect to ESG and sustainable investment funds to stem greenwashing.

In the coming years, regulatory scrutiny and enforcement risk are only going to increase along with shareholder activism that can quickly turn into mis-selling—or fraud—claims over misleading promotion of the positive environmental impact. The aim is for in-house legal teams to be able to accurately report that their operations are helping, or at least not harming, the environment.

Embedding Climate Considerations Into the Day-to-Day

The legal function can also feed back into growth initiatives by identifying the ESG areas that responsible stakeholders seek in their due diligence questions and RFPs. In addition, it's important to consider how legal teams or external lawyers take ESG risks and opportunities to account during internal due diligence. Empowered with better visibility, they can flag these issues for the executive board and help frame appropriate risk management strategies.

Besides, legal departments can use their spending power to prioritize sustainability in the legal services they procure by mandating that service providers they work with have robust and verifiable environmental pledges. It will need legal departments to stretch beyond the traditional objectives to minimize costs and be ready to back more strategic aims.

Climate-Conscious Contracting

In-house lawyers can adopt climate-aligned drafting, such as that of The Chancery Lane Project (TCLP), to ensure all legal agreements signed by their organization address the climate risks and impacts of the underlying transactions.

Contracts are powerful tools with the ability to create and drive opportunity. As discussed above, they can be incredibly useful to implement ESG strategies, goals, and targets without undermining the commercial goals.

Climate conscious contracting is being supported by numerous organizations with free-to-use content and thousands of participating legal professionals.

However, drafting is the first step and it's important to ensure that the strategy flows across the organization. It can be done by aiming for net-zero supply chains, which is touted as the next big opportunity for business and a key area of ESG focus. Individuals should also be made accountable for taking specific clauses forward to ensure a linked and consistent execution.

One Step Ahead of Legislation

There is, and will be, a time lag in legislative reform attempting to reduce environmental harm as the threat is constantly evolving. But there will certainly be legislative reforms and those not prepared could face significant disruption.

Historically, legal counsel has reacted to legislation with a somewhat defensive approach. But with net-zero, there's a real opportunity and incentive to be on the front foot and taking part in shaping legislation. For example, it would take significant time to establish standard ESG reporting targets by the way of legislation that can help increase transparency into complex supply chains. However, companies have the ability to immediately include enforceable clauses that encourage vendors to reduce and report emissions. The transactions a company undertakes is shaped by legal counsel, which is therefore wellpositioned to influence a net-zero strategy that can have an immediate and lasting impact.

OVERVIEW:

Sustainable Operations Management

Sustainable operations management (SOM) is the way organizations formalize the processes, procedures, and best practices that produce both a profitable and sustainable business. It is closely linked, and often viewed as a precursor, to the rapidly maturing environmental, social, and governance (ESG) movement in corporate disclosure. See Overview – ESG & Sustainability Governance Structure.

The formal concepts of sustainable operations management can be traced back to the theories of triple bottom line (TBL) management, which is a strategic construct that directs companies to prioritize profit, people, and planet equally. The term was coined by John Elkington in 1994 and has significantly influenced the arc of mainstream corporate sustainability trends.

The performance outcomes engendered by SOM and TBL reflect a changing business landscape that has increasingly prioritized diverse stakeholder interests and has widely accepted a shifting definition of corporate purpose, one that places a business' commitments to customers, employees, suppliers, and communities on equal footing with its commitment to generating pecuniary value for shareholders.

Sustainable Operations Leadership Responsibilities

Chief sustainability officers, sustainability directors, and sustainability managers are the formalized corporate roles that are often responsible for sustainable operations management. These professionals are important stakeholders for ESG programming within an organization or firm, and a growing number of companies have established these roles. See Overview – ESG & Sustainability Governance Structure.

Sustainable operations managers (specific job titles can vary from company to company) carry a diverse set of responsibilities, which include but are not limited to:

- Assuring environmental, health, and workplace safety (EHS) compliance (See Overview – EPA Enforcement Actions and Checklist – ESG Workplace Health & Safety Risks);
- Achieving higher performance levels than is required by EHS laws and regulations, often called "performance excellence";
- Developing and implementing sustainability policies (See Form – Sustainability Policy (Annotated);
- Setting performance goals and key performance indicators (KPIs) (See Checklist – ESG Reporting Process (Annotated));
- Making the ESG/sustainability business case to leadership (See Overview – Role of the Board of Directors and Overview – Role of the General Counsel);
- Communicating sustainability program developments within the company (See Table – ESG Communications Strategies (Annotated);
- Measuring and reporting sustainability performance to internal and external stakeholders (See Checklist – Stakeholder Engagement);
- Identifying reporting priorities and frameworks (See Table – ESG Frameworks).

Sustainable Operations in Supply Chains

For sustainable operations managers, establishing and maintaining sustainable supply chains is an exceedingly important and challenging responsibility. Extending sustainable operations priorities outward into supply chains can be accomplished through various mechanisms, including contractual obligations in vendor agreements, ESG due diligence practices in procurement, supply chain risk analysis, and supply chain auditing processes, among others. See Checklist – Establishing a Sustainable Supply Chain Policy; Checklist – Supply Chain Oversight; and Form –Sustainable Supply Chain Policy (Annotated).

Role of Legal Departments

Chief legal officers, corporate counsels, and in-house legal teams are all involved with different aspects of sustainable operations, acting as both a support system for sustainability managers and as a conduit to other departments or to senior leadership. The general counsel is uniquely situated to take the lead with regard to a company's environmental, social, and governance (ESG) initiatives, and is increasingly acting as a hub for the many stakeholders involved in corporate sustainability activities and initiatives. The sustainable operations unit, whatever its companyspecific title may be, occupies a vital position in an organization's ESG structure and will likely coordinate closely with legal departments to achieve ESG and/or sustainability goals. See Overview – Role of the General Counsel.

CORPORATE COMPLIANCE:

Reputational Risk Overview

What is Reputational Risk?

As a starting point, make sure your organization defines reputational risk—the most common attributes include:

- An interpretation or perception of an organization's trustworthiness or integrity
- That the reaction involves stakeholders
- That there is an impact on brand, influence, earnings or value
- A negative impact that results in some loss (for example, revenue, clients, engagements, employees, brand value)
- That the effect can be immediate or gradual

Pulling together these elements, think of reputational risk as the potential risk of losses, damage to brand, or another adverse effect arising from actions or inaction that could negatively impact stakeholders' perception of the company. Those actions or inaction intersects strongly with corporate communication of policies, responses to customer and public concerns, and willingness or resistance to adopting best practices.

What types of triggers are there for reputational risk?

Next, identify reputational risk events based on the types of scenarios or triggers that can impact the organization's reputation. Examples of trigger categories to help identify reputational risk events include:

- Products and Services: Issues that can negatively impact stakeholders' outlook on delivery or quality of products and services. In addition to issues such as labor practices, materials sourcing, and environmental impact, consider health and safety aspects of manufacture, packaging, and delivery at all points of production and the health and safety aspects of customer service.
- Employment and Workplace: Issues that can negatively impact stakeholders' view of employment and workplace practices. Workplace policies and procedures can influence consumer and public perception of a company's brand, especially during crises; decisions about action or inaction regarding updating the employee handbook and relevant policies (e.g., sick leave, remote work) need to account for the reputational risk of a perception as having a negative workplace environment.
- Governance: Issues that can negatively impact stakeholders' outlook about an organization's internal controls. Economic, public health, and other crises will eventually expose gaps and problems with auditing and operational processes, regulatory compliance, and other areas of reporting.
- Corporate Citizenship: Issues that can negatively impact stakeholders' outlook about an organization's corporate citizenry. Companies' various responses to the economic and human impact of the Covid-19 pandemic provide a clear illustration of how corporate action and communication will reflect back on the corporate reputation.
- Leadership: Issues that can negatively impact stakeholders' outlook on leadership's abilities to achieve goals and strategies.
- Crisis Management: Issues that can negatively impact stakeholders' outlook about ability responses to address emergencies. Failure to respond efficiently and with the abovementioned risks in mind is difficult to recover from, and would be nearly impossible to recover from twice.
- Financial Performance: Issues that can negatively impact stakeholders' outlook on an organization's business viability. Risk identification and proper preparation for the highest-risk, highest-likelihood possibilities (see Reputational Risk Matrix) will influence the cascade of decisions necessary during a crisis; financial concerns and projection of a company's ability to continue operating, providing products/services, and maintaining its existing geographic footprint will be elevated.

What are the consequences of having little or no reputational risk controls?

- Greater damage than for an organization that has a reputational risk program, even if the organization has done very little to contribute to the initial issue

- Significant negative impact on share price, earnings, and/or the balance sheet, and the less measurable impact of continuous brand degradation
- Cascading reputational damage, and additional financial consequences, as a result of mishandling a reputational crisis than the initial incident itself

Who should own the reputational risk program?

Every employee (and third parties as based on contractual terms) should be accountable, but ultimately reputational risk management starts at the top. Strong board oversight is vital to sustaining reputation, and as a result, the board's presence in the program should be prominent.

Senior management/executives should also support and promote the program and in turn compel their line managers to do the same.

The program should not be an operation of a control group, such as Legal, Risk, or Compliance, solely. The program should be a cross-functional responsibility with visible ownership and ongoing support from the highest levels of management.

- Engage senior management to set the tone from the top in supporting reputational risk as part of the organization's culture and overall governance.
- Employ a proactive approach to identify, better understand and mitigate risks to reputation, including risks that arise out of global circumstances.
- Be prepared to demonstrate a thoughtful approach to protect the organization from lasting damage to its reputation and brand.
- Regularly assess potential damage to the reputation of known effects (loss of revenue, share price declines, customer loss, etc.), and potential unknowns such as a social media backlash impact on the brand.
- Engage a cross-functional team to help Identify scenarios and quantify their impact on your reputation as well as the success of proposed response measures.
- Continuously promote corporate actions aligned with full legal and regulatory compliance as the best safeguards against reputational challenges.

In the end, your organization's reputation resides on an ongoing commitment to promote and maintain an ethical culture that is best maintained through a dedicated framework such as a Reputational Risk Program. Such a program will be most effective if integrated into existing corporate programs, which, depending on an organization's operations and regulatory scheme, might include oversight of: significant transactions (based on transaction amounts); mergers and acquisitions; new product development processes; crisis management and communications protocols; escalation processes; periodic assessments; governance, risk and compliance protocols; code of conduct; employee handbook; conflict of interest measures; and third-party governance structures.

CORPORATE COMPLIANCE:

Rule 10b-5 Liability

Environmental, social, and governance ("ESG") reporting by public companies can pose significant risks in terms of liability under the federal securities laws. Companies may face risks of federal securities class action suits based on Exchange Act Section 10(b) and Rule 10b-5. These provisions impose liability for fraudulent or deceitful misstatements and omissions of material fact. Unlike other securities law provisions, such as Securities Act Sections 11 and 12(a)(2), Rule 10b-5 applies broadly to corporate communications. The Securities Act provisions apply to misstatements or omissions contained in a prospectus or registration statement. Rule 10b-5, however, covers SEC filings, as well as a wide range of statements, such as press releases, advertisements, analyst calls, earnings projections, and for ESG purposes, sustainability reports. There have been few reported cases involving ESG issues in securities class actions. As investor interest in ESG concerns grows, companies will likely face more actions from shareholders in the future and should consider this possibility when assessing their risk profiles.

Elements of Rule 10b-5 Liability

Exchange Act Rule 10b-5 generally prohibits fraudulent conduct in connection with a purchase or sale of securities. Although the statute and the rule are silent on the question of whether investors may recover, the courts have long recognized an implied private right of action. To recover under this provision, a plaintiff must demonstrate several specific elements of the cause of action.

- **Material Misrepresentation or Omission**. Any claimed misrepresentation or omission must be "material" to be actionable. In 1988, the Supreme Court held that information would be considered material if there was "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."

  Defendants often argue that their charged statements were vague, immaterial statements of corporate optimism, known as "puffery." Courts have found statements such as a company had structures in place that were "highly disciplined and designed to preserve the integrity" of the risk management process, and that a company aspired to "be clear leaders in corporate citizenship" and was "going to lead in corporate social responsibility" to be non-actionable puffery.

  Companies should exercise care in expressing optimistic or aspirational statements, however. The inclusion of specific facts can move the statement from immaterial puffery to actionable misrepresentation or omission. In a case arising from a dam collapse in Brazil, a federal district court held that statements about the company's "values and commitment to health, safety, and the environment" were not actionable. However, a statement that the company mitigated "operational risk with new controls and improvement of existing ones" was a statement of historical fact rather than aspirational puffery, and could be actionable.
- **"In Connection With" a Purchase or Sale of a Security.** While Rule 10b-5 is not a general antifraud provision for financial transactions, the courts have construed the "in connection with" requirement broadly. As the Supreme Court stated in its 2002 SEC v. Zandford decision, "neither the SEC nor this Court has ever held that there must be a misrepresentation about the value of a particular security in order to run afoul of the Act."
- **Scienter, or a Fraudulent Intent to Deceive.** The various circuit courts have put their own take on what specifically constitutes the requisite fraudulent intent, but these are variants on the Supreme Court's conclusion that scienter is "a mental state embracing intent to deceive, manipulate or defraud." Because scienter sounds in fraud, plaintiffs must plead the facts showing scienter with particularity.
- **Reliance.** Plaintiffs must demonstrate that they relied to their detriment on the fraudulent statements or omissions. This is a difficult standard for class plaintiffs to meet, because a lack of actual reliance by class members could defeat the commonality element required for class certification. The Supreme Court eased this burden by establishing the "fraud on the market" presumption. For securities traded in an efficient market, such as an exchange, plaintiffs may plead that they relied on the integrity of the stock's market price, which reflected the fraudulent statements or omissions.

- **Loss Causation.** Plaintiffs must show that the alleged misconduct actually caused their financial harm. Under Supreme Court precedent, it is insufficient to allege the inflation of the stock price without more, as other economic factors may have contributed to the price change.
- **Damages.** Plaintiffs in Rule 10b-5 actions cannot recover more than their actual financial damages.

Risk Mitigation

Company counsel should carefully vet any ESG comments or disclosures to ensure that they are factually accurate and do not omit any material information. This is particularly important in the case of an event that could generate litigation, such as an accident or data breach.

ESG disclosures and statements should be consistent across the company. Counsel may want to frame statements in aspirational terms rather than in historic ones, and incorporate disclaimers. Forward-looking statements should be identified as such, and accompanied by meaningful cautionary language.

The company should provide training to individuals authorized to speak for the company, and develop policies and procedures related to public comment and use of social media. Counsel should also take steps to ensure that the board is informed concerning the company's risk profile and the risk mitigation procedures.

ESG, SAMPLE POLICY:

Sustainable Supply Chain Policy (Annotated)

[Name of the company] is committed to continuously improving ethical, social, and environmental performance throughout our supply chain. Our supply chain is an integral part of the company value chain; therefore, we highly value relationships with our suppliers and contractors. We adhere to the highest ethical business standards and seek to engage with suppliers and contractors who also adhere to the responsible business practices as described in this policy, as a minimum. This policy extends to all purchases of products and services for our company. We are a signatory to the United Nations Global Compact (UNGC) and adhere to the UNGC 10 principles. These principles are based on the Universal Declaration of Human Rights; the International Labour Organisation (ILO)'s Declaration on Fundamental Principles and Rights at Work; the Rio Declaration on Environment and Development; and the UN Convention against Corruption. We have developed internal policies, which govern our procurement activities, in line with these universally accepted frameworks. These policies include, for example:

- Code of Conduct – outlining our mission, values, and level of commitment to ethical business practices and defining how our employees should act on a day-to-day basis;
- Supplier Code of Conduct – outlining minimum requirements on the conducts of our suppliers and contractors;
- Human Rights Policy – outlining our position on human rights;
- Diversity and Inclusion Policy – outlining our position on diversity and inclusion; and
- Sustainability Policy – outlining our position on environmental, social, and governance (ESG) and sustainability.

Practice Tip: The list of policies above provides examples of key basic policies that companies may consider adopting to communicate their commitment to sustainable supply chain, sourcing, and procurement. It is not an exhaustive list and companies can develop ones that are most suitable for their organization's objectives and culture. Sample policy documents on various topics may be found here.

In addition to the requirements set forth in our Supplier Code of Conduct, as a minimum, we request that our suppliers:

- Comply with applicable local laws and regulations;
- Pay appropriate wages;
- Do not use child or illegal labor;
- Do not require excessive working hours;
- Do not allow discrimination practices;
- Do not allow an unauthorized sub-contracting; ensure safe and hygienic working conditions;
- Ensure that employment is freely chosen;
- Respect freedom of association and the right to collective bargaining; and
- Ensure the protection of the environment.

Practice Tip: Companies may consider including environmental requirements that suppliers must comply with, unless these are already mentioned elsewhere. For instance, these may include requirements for suppliers to establish a company-wide plan and goals to reduce carbon emissions and minimize waste generation, increase the use of renewable energy resources, and improve energy efficiencies, among others.

To ensure sustainability throughout our supply chain, we will:

- Integrate environmental, social, and governance (ESG) objectives into our supply chain strategy and relevant policies and procedures;
- Inform all employees, clients, suppliers, contractors, and vendors of this policy and other relevant policies and procedures;
- Ensure that all departments at all levels of the company who engage in the activities of acquiring goods or services develop necessary procedures to ensure the compliance with this policy;
- Support and encourage our suppliers to extend sustainability practices across their own supply chain;
- Ensure transparency in all procurement activities in accordance with our Code of Conduct;
- Ensure the inclusion of diverse groups in procurement planning;
- Carry out an annual supplier sustainability assessment to ensure that ESG and sustainability related risks are identified and develop an action plan to manage or mitigate those risks accordingly; and
- Report to all relevant internal and external stakeholders on the result of an annual supplier sustainability assessment, the company's performance on human capital management, and its efforts to eradicate human trafficking from its global supply chains on an annual basis.

This policy will be reviewed annually as part of the management review process.

Approved by:

Name: CEO/Chairman of the Board/Managing Director

Date:

COMPARISON TABLE:

ESG Frameworks

For companies endeavoring to report on ESG issues, many implement one or several voluntary reporting frameworks to help do so. Employing the guidance of a voluntary ESG framework can help with the determination of which particular issues to disclose, the form that the disclosure takes, and may facilitate the verification of information contained in your company or client's report. For most, the determination of an appropriate framework stems from a company's individual ESG objectives and the desired audience for their disclosure.

See **Overview – Global Reporting Initiative; Overview – Sustainability Accounting Standards Board; Overview – United Nations Global Compact**; and **Overview – Task Force on Climate Related Financial Disclosures**.

	Global Reporting Initiative (GRI)	**Sustainability Accounting Standards Board (SASB*)**	**United Nations Global Compact (UNGC)**	**Task Force on Climate-related Financial Disclosures (TCFD)***
Summary	An international independent standards organization that helps businesses, governments and other organizations understand and communicate their impacts on issues such as climate change, human rights, and corruption. GRI is the most widely used reporting framework, with 82% of the world's largest 250 corporations reporting in accordance with GRI Standards.	A sector-based, industry specific guidance framework used primarily to help publicly traded companies determine the financial materiality of sustainability related information for disclosure to the SEC and the public.	A voluntary initiative based on CEO commitments to implement universal sustainability principles; A way for companies to support and advance the UN's Sustainable Development Goals, which have been adopted by all UN member states.	A voluntary framework of recommendations on climate-related financial disclosures that are applicable to organizations across sectors and jurisdictions. Organizations can use the Recommendations to help them prepare more consistent and comparabledisclosures of their material, climate related risks and opportunities, and how they manage them.
What is the framework's structure?	There are two primary groups: Universal Standards and Topic-specific Standards. The Universal Standards, also called the "100 Series of the GRI Standards" includes three standards to use in preparing a sustainability report: • GRI 101: Foundation 2016 • GRI 102: General Disclosures 2016 • GRI 103: Management Approach 2016. The Topic-specific Standards include: • GRI 200: Economic Standards • GRI 300: Environmental Standards • GRI 400: Social Standards.	The SASB standards are broken down by industry, making SASB metrics comparable from company to company within an identified peer group. There are 77 identified industries in the SASB Standards, in 11 different Sectors.	The Global Compact consists of 10 Principles intended for incorporation into companies' value systems and business operations. The SDG program provides 17 lofty goals with a 2030 target date for attainment. They aim to end poverty and environmental degradation, reduce inequality, expand access to healthcare and education, and engender sustainable economic growth	The TCFD Recommendations are designed to help organizations comply with existing mainstream reporting requirements, rather than impose additional reporting standards.

	Global Reporting Initiative (GRI)	Sustainability Accounting Standards Board (SASB*)	United Nations Global Compact (UNGC)	Task Force on Climate-related Financial Disclosures (TCFD)*
Is there a prescribed reporting format?	Reports will be company/ organization specific, but will include an "in accordance" designation, meaning the report was written in accordance with GRI Standards. To claim that a report has been prepared in accordance with the GRI Standards, look to GRI 101: Foundation for guidance.	Sustainability information and performance metrics that are "financially material" should be incorporated into a reporting company's scheduled SEC disclosures and in that company's sustainability, impact, CSR, or ESG report.	Communication on Progress (CoP): The CoP is an annual reporting requirement wherein companies set out key information regarding their Global Compact-driven activities.	Organizations are encouraged to disclose material climate-related issues in their mainstream financial filings, whether with the SEC, other regulatory agencies, or ESG/ sustainability reports.
Can the framework be employed in conjunction with other frameworks?	**YES –** GRI is intended as a guide for developing a company specific sustainability report and including metrics and reporting information from other frameworks within the report is encouraged and facilitated.	**YES –** Because SASB is intended to identify financially material sustainability information, the subsequent data, metrics, and narrative are wholly intended to be integrated into both regulatory filings and published sustainability reports.	**YES –** The UNGC and SDGs are both intended as aspirational frameworks used by companies to reach sustainability goals and increase equity across all sectors of society. The principles of the UNGC and the SDGs can be incorporated into sustainability communications, reports, and regulatory filings.	**YES –** The Recommendations were also developed in alignment with other existing reporting frameworks (e.g., CDP, SASB, CDSB, GRI, and IIRC). Therefore, organizations reporting under those frameworks may already have tools that would be useful for the collection and reporting of climate-related information under the TCFD framework.
Does the framework require a materiality assessment?	**YES –** GRI requires an organization to identify material topics in order to establish the scope and included issues covered by a company's report. GRI's framework contemplates that materiality may meaning for different stakeholders. Therefore, material topics are those that may reasonably beconsidered mportant for reflecting the organization's economic, environmental, and social impacts, or influencing the decisions of stakeholders.	**YES –** SASB is intended to identify financially material sustainability information. Materiality under the SASB framework is determined exclusively through the lens of the "reasonable definition of which has been established by the courts. See Point of Law (POL).	**NO –** The UNGC and SDGs are not intended to be used to narrowly identify specific material information, but rather as goal oriented guideposts for companies seeking to themselves.	**YES –** The Task Force recommends that organizations assess materiality for climate-related in the same way they determine the materiality of other information included in their financial filings.

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