Securities Regulation Daily Wrap Up, TOP STORY—Commissioners Peirce and Roisman puzzled by SEC's new focus on ESG disclosure violations, (Mar. 4, 2021)

Securities Regulation Daily Wrap Up

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The SEC will initially focus its newly announced ESG enforcement task force on climate risk issues by mining issuers' filings for "material gaps or misstatements" as measured by current regulations.

The SEC announced that it will create a Climate and ESG Task Force to be located within the Division of Enforcement that will look for potential violations by mining issuers' filings and evaluate related whistleblower complaints. The task force also will review how investment advisers and funds are complying with SEC regulations with respect to funds' ESG strategies. Commissioners Hester Peirce and Elad Roisman issued a statement in response to the announcement in which they suggested they were puzzled by the new emphasis on ESG-themed enforcement and what that means for issuers and investors.

The ESG task force announcement comes just more than one week after Acting SEC Chair Allison Herren Lee announced that the Division of Corporation Finance will review issuers' filings regarding climate-related disclosures. The task force announcement follows yesterday's publication of the Division of Examination's 2021 examination priorities, which include ESG issues. With respect to climate risk, the Division of Examinations said: "As climate-related events become more frequent and more intense, we will review whether systemically important registrants are considering effective practices to help improve responses to large-scale events." The SEC's several ESG initiatives also come at a time when SEC Chair nominee Gary Gensler was just pressed by Senators about how far he might push the agency's mission and mandates to include new or changed climate risk and other ESG disclosure requirements.

ESG task force. Kelly L. Gibson, Acting Deputy Director of Enforcement, has been tapped to lead the taskforce. According to the announcement, the task force will have a division-wide scope and will be staffed by 22 members from across SEC headquarters, SEC regional offices, and specialized units within the agency's Enforcement function. The task force also will "complement" the work of others at the SEC, including Satyam Khanna, who was recently named Senior Policy Advisor for Climate and ESG within Lee's office, and the work of other SEC divisions and offices.

"The task force announced today will play an important role in enhancing and coordinating the efforts of the Division of Enforcement, the Office of the Whistleblower, and other parts of the agency to bolster the efforts of the Commission as a whole on these vital matters," said Lee.

Gibson also remarked on the task force's proactive role in identifying gaps in issuers' disclosures. "This task force brings together a broad array of experience and expertise, which will allow us to better police the market, pursue misconduct, and protect investors," said Gibson.

The initial emphasis will be on identifying material gaps or misstatements in climate-risk-related disclosures. That goal would likely dovetail with the CorpFin review of issuer filings and the Division of Examination's 2021 priorities.

However, there is a much heavier enforcement component implied by the task force announcement in that the SEC will use "sophisticated data analysis to mine and assess information across registrants, to identify potential violations" and that the SEC staff will consider whistleblower complaints about climate risk and other ESG matters. Moreover, the SEC will review investment advisers' compliance with regulations with respect to ESG fund strategies.

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Peirce-Roisman statement. Commissioners Peirce and Roisman jointly issued a statement responding to the task force announcement and concluding that the import of the announcement is unclear. The commissioners reiterated that the initiatives are likely an extension of other SEC efforts to monitor how companies apply existing SEC rules and guidance on climate and other ESG disclosures. They also reiterated that materiality is the key to SEC disclosures.

Moreover, Peirce and Roisman observed that SEC climate risk guidance has been in place since 2010, although one of Lee's goals is to update that guidance following CorpFin's review of issuers' filings (For additional background on the SEC's existing ESG guidance and recent ESG legislative proposals, see the ESG section in the Wolters Kluwer 2020 year-end review of Congress and the Supreme Court (pages 9-17).

However, Peirce and Roisman suggested that the Commission had not yet considered new Commission-level climate standards, although staff can issue guidance or exemptive relief consistent with Commission policy. As a result, Peirce and Roisman draw several observations about the nature of the ESG task force:

- ***Timing issues—***"The timing of this release—just before many public companies were due to file their annual reports—underscores its apparent function as a re-framing of the ongoing work, rather than the announcement of anything new."
- ***Regulatory approach—***"So the new announcement cannot foreshadow a plan for the staff to issue guidance that would elicit more specific line items or otherwise convert the Commission's generally principles-based approach to a prescriptive one."
- ***Enforcement—***"Some of those violators might be public companies or advisers whose climate- or ESG-related statements are false or misleading, but such actions would not be based on any new standard; we have always pursued violations of our antifraud provisions."

More generally, Peirce and Roisman suggested that the task force announcement may have had as its goal to provide weight to the CorpFin climate disclosure review announcement and the Division of Examination's announcement that it will look at firms' handling of climate matters. Both commissioners said this would be "odd" because a new enforcement focus should follow the results of the CorpFin and Division of Examinations reviews. Said Peirce and Roisman: "Either way, we must continue to review any alleged securities violations in light of the regulations and guidance in existence at the time of the conduct in question."

The Pierce and Roisman statement, while emphasizing the need to await the results of ongoing agency studies of ESG disclosures, did not mention that the next permanent SEC chair will ultimately direct the SEC's longer-term policy toward ESG disclosures.

Genslser nomination hearing. The day before the task force announcement, the Senate Banking Committee held a hearing on Gary Gensler's nomination to be the next permanent SEC chair. Much of the hearing focused on whether and to what extent Gensler may lead the SEC to adopt regulations that could push the boundaries of the SEC's congressional mandates on topics like climate risk, diversity, or corporate political donations.

Gensler told senators he would follow the construct of economic materiality in creating and applying regulatory standards. However, Gensler appeared to push back against a hypothetical suggested by one senator in which the senator suggested that the small size of an expenditure on electric power would make that item nonmaterial for purposes of climate risk disclosures about renewable energy sources. Gensler suggested that the size of the expenditure alone would not drive the materiality determination because materiality is ultimately decided by the investor community, which he said has been vocal about demanding more climate and other ESG disclosures from public companies.

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