# Being Underway, Not in Delay, on Climate Change-Related Disclosure

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*Confusion among companies over what is adequate in environmental disclosure, in general, sets an unfortunate stage for contemplating the newer matter of climate change-related disclosure. Companies waiting for new legislative and regulatory outcomes before contending with climate change disclosure, however, are in exposed and inadvisable delay on the matter. Existing regulations and standards pertain and instruct, if indirectly, on what is to be disclosed and accrued, and when. Their requirements, the possibility of enforcement actions, and recent evidence of costly consequences to former executives from improper environmental financial disclosure reinforce corporate management's need for disclosure diligence, including on climate change. The future is here.*

## I. RECENT EVENTS CALL ATTENTION TO THE ISSUE OF ADEQUATE FINANCIAL DISCLOSURE ON CLIMATE CHANGE

Two recent events have called attention to the issue of adequate disclosure of financial information on management of greenhouse gas (GHG) emissions and consequences of climate change.[2]

1. **Energy companies subpoenaed by state Attorney General's office**. The office of the New York State Attorney General, John Cuomo, subpoenaed five large energy companies for information provided investors on plans for new coal-fired power plants. In letters dated September 14, 2007 that accompanied the subpoenas, the attorney general's office questioned whether investors had received adequate information on the financial liability of anticipated emissions of carbon dioxide, a greenhouse gas, from the

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plants, such emissions being linked by scientists to the exacerbation of climate change (Barringer and Hakim, 2007).

2. **SEC petitioned by high-level money managers**. A group of high-level money managers, including state financial officers and institutional investors, contended in a letter petition to the U.S. Securities and Exchange Commission (SEC),[3] dated September 18, 2007, that lack of information on how climate change affects company financial conditions can prevent them from making sound investment decisions. The letter petition asked the SEC for an *interpretive release* making clear to companies that material climate information must be part of corporate disclosures (Investors, 2007a).

The management of GHG emissions and the consequences of climate change is a newly risen and potentially complex issue for many companies at this time. There are no federal laws and regulations enacted yet to define the nature and extent of the management need. So, that companies exhibit uncertainty and even avoidance on disclosure of how management of GHG emissions and climate change may affect company operation and financial conditions is not particularly surprising, even if it is an inadequate response.

The investors in their September 18, 2007 petition letter to the SEC contended, “The low rate of meaningful climate risk disclosure and the inconsistency in how companies are addressing this subject in their filings are denying investors the information they need and demand about climate risk.” (Investors, 2007a) In an additional letter to the SEC, this to the Director of SEC’s Division of Corporation Finance—which has 10-K and 10-Q review responsibilities—the investors asked that “particular attention [be given] to the adequacy” of climate change disclosures in 10-K and 10-Q filings (Investors, 2007b). The petitioners were financial officers from ten states and New York City and several institutional investors, including representatives of the massive California Public Employees’ Retirement System and the California State Teachers’ Retirement System, which total $400 billion in assets and are the country’s two largest public pension funds (Investors, 2007a).

In their December 6, 2007, letter to the Chairman of the SEC, Senators Christopher Dodd, Chairman, and Jack Reed of the U.S. Senate Committee on Banking, Housing, and Urban Affairs added their voices to those calling

[3] It is the SEC that implements federal regulations and policy that require and oversee regular, periodic disclosure in *financial statements* of information *material* to the operation and financial condition of public companies. Financial statements, or financial reports, are used by companies to portray their financial performance, typically over a year, and their financial condition, both current and future, including identification of what can affect cash flow, annually using SEC Form 10-K, quarterly using Form 10-Q, and periodically in response to material events using Form 8-K. Material is the status of a financial item being relevant to a reasonable person or investor. There is no criterion with a constant value for materiality. What is material differs among companies of different size and nature, and it varies within a company when financial conditions vary. Application of a numerical threshold value, e.g., less than five percent of income or assets, may be an initial step in assessing materiality, but “cannot appropriately be used as a substitute for a full analysis of all relevant considerations.” (SEC, 1999; Rogers, 2005) Information is material if there is a substantial likelihood that a reasonable investor would find its omission would alter the “total mix” of information made available, according to the U.S. Supreme Court (TSC, 1976).

on the SEC for an "interpretive release" to guide climate change disclosure, for "greater consistency and completeness." (Dodd and Reed, 2007)

These recent events concerning climate change-related disclosure (or, simply, climate change disclosure) underscore the need to resolve the matter of its requirements. The parties initiating these recent events resorted to available but blunt tools, subpoenas and a letter petition, in seeking resolution on their disclosure issues.

Their actions beg the question of how climate change disclosure is being seen to in proposed federal legislation, the most direct means for its resolution.

Probably more relevant in the near term for many organizations, it directs attention to what a company's most appropriate actions are at this time concerning climate change disclosure.

## II. PAST EFFORTS TO OBTAIN CLARIFICATION ON DISCLOSURE HAVE NOT PRODUCED DESIRED RESULTS

In its letter to Dominion Resources, one of the five power companies subpoenaed, the Attorney General's office stated, "A public company must disclose information material to a shareholder's investment decision." (Kennedy and Gaul, 2007) The letter also asserted, "Selective disclosure of favorable information or omission of unfavorable information concerning climate changes is misleading." (Kennedy and Gaul, 2007) The letter said that the New York Common Retirement Fund is a significant holder of Dominion stock.

These are disclosure concerns that a company seemingly could avoid by implementation of relevant federal regulations and standards associated with generally accepted accounting principles (GAAP). Existing federal regulations and GAAP standards make only limited direct reference to environmental disclosure, however, and none to the newer matter of climate change disclosure.

The subpoena is an indirect method for contending with disclosure complications. According to the *New York Times*, the subpoenas likely are part of efforts by the Attorney General and other state officials and environmentalists to curtail construction of coal-fired plants over environmental concerns, which may help explain why such a dramatic, if blunt, tool was used ostensibly to clarify a disclosure issue (Barringer and Hakim, 2007).

Appealing to the SEC does not necessarily produce timely or desired results. Before the letter petition of September 18, 2007, other letters have been sent to the SEC requesting clarification on climate change disclosure. In a letter petition dated June 14, 2006, the Investors Network on Climate Risk (INCR), in an earlier representation of many of the organizations that signed the September 18, 2007 letter, asked the SEC for a meeting to discuss how the SEC could improve disclosure of climate risk in securities filings. INCR noted in that 2006 letter it had sent two previous letters on the matter in 2004 (Investor Network on Climate Risk, 2006).

In a letter petition to the SEC dated September 20, 2002, the Rose Foundation, an environmental advocacy group that describes itself as "advancing the positive intersections of the environment and the economy," made its case for the SEC to promulgate two new rules to help clarify environmental disclosure requirements (Rose Foundation for Communities and the Environment, 2002). In a meeting on March 14, 2005, the Financial Accounting Standards Board (FASB), a developer of standards that companies use in implementing SEC requirements, chose to take no immediate action on the request (Duke, 2005).

A *clarification* on an SEC matter can seem to miss the mark. FASB released FASB Interpretation No. (FIN) 47 in 2005 to clarify FASB Statement (FAS) 143, which it issued in 2001 and which pertains to accounting for certain environmental costs and disclosing them, as will be portrayed in more detail in the following section (FASB, 2001; FASB, 2005). In a study of the SEC filings of 166 companies, each with annual revenues of at least $500 million, a group called the Controllers' Leadership Roundtable concluded, however, that disclosure of those costs by the companies it surveyed was variable and inconsistent in the first year after FIN 47 release (Controllers' Leadership Roundtable, 2006). The clarification intended with FIN 47 seems not to have obtained, at least among this significant group of companies in the initial period following its release. It is possible, as well, that this study confirms what reasonably could be expected, and that is an initial reluctance among companies to add to their workload—particularly as the task may seem complicated to implement and may require the commitment of additional resources to accomplish, and left undone may seem to bring only a small likelihood of being detected as deficient.

There is confusion about both the extent to which environmental disclosure by companies is believed to be deficient and what constitutes adequate disclosure. In 2001, the U.S. Environmental Protection Agency (EPA) instructed its Regional enforcement offices to remind public companies of their responsibilities on disclosure of environmental legal proceedings under Item 103 of SEC Regulation S-K, citing statistics from studies that showed disclosure being typically deficient (USEPA, 2001a). Also in 2001, EPA issued an *Enforcement Alert* to remind companies of disclosure responsibilities under Items 101 and 303 of SEC Regulation S-K, in addition to Item 103, and of potential legal and monetary consequences from failure to disclose, including possible fines of $5,000 to $500,000 for each violation (EPA, 2001b). In a 2004 report, the U.S. General Accountability Office found that, despite various studies over the preceding ten years, little is known about the adequacy of environmental information in SEC filings (GAO, 2004). The perception prevails, however, of a "significant deficit in corporate environmental disclosure." (Ewing, et al., 2005) This perception of inadequate disclosure and confusion over what is adequate sets an unfortunate stage for the newer matter of climate change disclosure.

## III. WHAT IS THE POSSIBILITY OF CLARIFICATION IN RECENTLY PROPOSED FEDERAL LEGISLATION?

What does legislation proposed in the 110$^{th}$ Congress require on corporate disclosure of climate change information? On its Web site on

November 12, 2007, the Pew Center on Global Climate Change indicated that more than 125 bills, resolutions, and amendments on climate change have been introduced in the 110th Congress as of mid-July 2007. Eleven of the bills currently before Congress address GHG emissions reporting and seven, including two of the previous 11, address cap-and-trade. Those 16 were examined for requirements on climate change disclosure, since they were believed to be the bills most likely to have the sort of records-management concerns that relate to disclosure.

Three of the 16 bills—HR 2651, S 309, and S 485—were found to have climate change disclosure elements, and those elements are portrayed in the Appendix A table. In all three bills, companies would be required to disclose: estimated financial exposure from their own GHG emissions and the potential economic impact of global warming on the company. The bills additionally would have the FASB or an equivalently appropriate organization develop a uniform format for companies to use in disclosing climate change information. The bills would have, as well, the SEC provide an *interim interpretive release* (to serve while new climate change regulations are being developed) that recognizes: global warming as a *known trend* and U.S. commitments (under the United Nations Framework Convention on Climate Change, New York, May 9, 1992) to reduce GHG emissions as a *material effect.*

Here's how disclosure elements differ among the proposed bills:

- Only companies with market capitalization of $1 billion or more must provide climate change disclosure under S 485, but that disclosure requirement applies to both privately- and publicly-held companies.
- HR 2651 and S 309 apply to all issuers of securities, i.e., there is no threshold value to meet in market capitalization.
- Only HR 2651 requires disclosure of GHG emissions and a statement of whether or not the GHG emissions information was independently verified.
- HR 2651 requires the SEC to finalize its regulations on climate change disclosure within a year of the law's enactment, while S 309 and 485 allow two years for the SEC to finalize regulations.

There is no knowing when federal climate change legislation will be enacted and whether it will contain disclosure elements. As well, the development of regulations following legislation will take time. For example, the proposed bills with disclosure elements allow for another one or two years for regulations to be finalized, which is not abnormal

A company waiting for new legislative and regulatory outcomes before contending with climate change disclosure, however, *is in exposed and inadvisable delay on the matter*. The section that follows will show with some clarity that existing regulations and standards pertain and instruct, if indirectly, on the matter of climate change disclosure. Those proposed climate change bills indicated above with disclosure elements require disclosure of information that figures into what already is expected under Item 303 of SEC Regulation S-K. Important, as well, Item 303 has the benefit of a considerable body of SEC information that already is available to assist companies in its application, e.g., statements, interpretations, and reports. (See, for example, SEC, 2002, 2003, and 2006.) Those proposed bills require disclosure of how a company's GHG emissions and global warming affect business, and that is a ready application of Item 303 to climate change disclosure. The remaining issue in applying Item 303 to climate change disclosure is a company's decision to acknowledge climate change as a "known trend," and that is addressed below. There are requirements in other already-existing regulations and standards that pertain on climate change disclosure, as well, and they, along with Item 303 requirements, are portrayed briefly in the section that follows.

## IV. WHAT ARE THE MOST APPROPRIATE ACTIONS AT THIS TIME FOR CLIMATE CHANGE DISCLOSURE?

There are SEC regulations and FASB standards that instruct on disclosure that have application to climate change disclosure. Following are key elements of those regulations and standards, beginning with the SEC regulations, with disclosure criteria and cost accrual requirements summarized in the Appendix B table.

- **Disclosure of material effects from compliance with environmental laws.** Under Item 101(c)(xii) of SEC Regulation S-K, companies are required to disclose material effects from compliance with federal, state, and local environmental laws.

  What does this mean for a company in terms of climate change disclosure? While there are no federal climate change laws, some state and local laws have been enacted. So, it means disclosure of the costs a company has for its program of compliance with the state and local climate change laws that apply. It means, as well, disclosure of the material effects that compliance with those laws is expected to have on company business, in particular, on "capital expenditures, earnings, and competitive position." (SEC Regulation S-K, Item 101(c)(xii)) A company will have to set about analyzing and determining those effects. If a company plans capital expenditures for environmental control facilities to comply with climate change laws, disclosure must include those costs, if material.

  For companies having facilities outside the U.S., Item 101 does not appear to require disclosure for compliance with non-U.S. climate changes laws.

- **Disclosure of material legal proceedings.** Under Item 103(5) of SEC Regulation S-K, companies must disclose material pending legal proceedings against the company arising from federal, state, and local environmental laws.

  What does Item 103 mean for a company's climate change disclosure? Absent exposure from federal climate change laws, a company must disclose material legal proceedings from application of state and local climate change laws. For example, there could be lawsuits by parties seeking damages or there could be enforcement actions by governmental authorities. No disclosure is required, however, if a claim for damages is less than 10 percent of company assets or if the monetary sanction from a governmental authority-initiated proceeding will not exceed $100,000.

Item 103 disclosure requirements apply not only to climate change proceedings already initiated, but to those a company knows are contemplated by governmental authorities. For companies having facilities outside the U.S., Item 103 does not appear to require disclosure of legal proceedings arising from non-U.S. climate changes laws, as with Item 101.

- **Disclosure of material effects of known trends.** Under Item 303 of SEC Regulation S-K, companies must disclose the material effects of *known trends* or uncertainties on company operation and financial conditions.

  How does this requirement of Item 303 apply to climate change disclosure? First of all, a company must make its decision about whether climate change, or global warming, constitutes a *known trend*. If it concludes so, then the company must set about using available resources to analyze and determine what it believes to be the effects of climate change on its business, i.e., on its operation and financial conditions. This is no small task, and there currently is little in precedent or guidance for companies to follow. It likely will be the most difficult and time-intensive part of climate change disclosure for most companies.

  Why should a company decide to recognize climate change as a known trend? *There are strong factors indicating it is.* It is an expressed conclusion by many scientists that global warming already is occurring, and that adverse consequences from it will worsen until mitigating actions are begun. The current Congress has seen the introduction of many bills, resolutions, and amendments on climate change, as already noted. Some state and local governments, prominently, the state of California, already have enacted their own laws on climate change. These indicate a contention, broadly-held by individuals in scientific advisory and political leadership roles, that climate change is underway, i.e., is a known trend. As mentioned previously, the currently proposed federal climate change bills that have disclosure requirements go directly to the point by simply requiring the SEC to declare it is a known trend, so that companies clearly would know to apply the existing SEC disclosure requirements in Item 303 to the matter of climate change disclosure until new, climate change-specific regulations could be developed.

  The work involved in disclosure of climate change effects under Item 303 is daunting for companies to consider, *and that's because the subject of climate changes is, also*. For example, companies must anticipate new laws that will limit GHG emissions. Electric power and transportation rates may well increase. How much and how it

> affects company operation and financial conditions will have to be assessed. Companies must anticipate physical effects, too, like changing temperatures, rising sea levels, and more severe storms, which may affect a variety of things like water supplies, insurance rates, and disease vectors, for example. *Many companies understandably may feel that never for purposes of disclosure have they needed to consider so many unfamiliar and complicated factors, using information resources in such early stages of development*.

There are FASB standards and interpretations, accepted by the SEC as qualified under GAAP (generally accepted accounting principles), that apply to climate change disclosure. Following are key elements from those instructions.

- **Disclosure of material loss contingencies.** Under FAS 5 – FIN 14, which is the pairing of a FASB standard and a subsequently issued FASB interpretation of that standard, companies must disclose material loss contingencies, which are contingent liabilities or asset losses or impairments (FASB, 1975; FASB, 1976).

  In a loss contingency, a financial exposure is recognized that requires the occurrence of one or more future events in order to resolve uncertainty, and that resolution precedes the incurrence of an actual cost of responding. In fact, the resolution might indicate no need for responding and hence no cost. Before the resolving events, however, an estimated response cost, if *material*, must be shown on company books (accrued) and reported in the financial statement when a company recognizes that a need to respond is *probable* and that the cost is *estimable*.

  How does FAS 5 – FIN 14 apply to climate change disclosure? Loss contingencies for a company may develop from climate change-related *litigation, claims, and assessments*. For example, a company with GHG-emitting facilities may have claims brought against it that seek reduction or elimination of those emissions. If a company can estimate the cost of those damages, and the cost is material and the likelihood of incurring the cost is probable, then the company would appear to have a loss contingency that needs disclosure and accrual. Disclosure must be considered for both pending and threatened litigation. Unlike with Item 103 of SEC Regulation S-K, under FAS 5 – FIN 14 a company with facilities outside the U.S. will need to consider disclosure of legal proceedings that arise from laws applying at those non-U.S. locations.

  Loss contingencies may develop, also, from the *write-down of operating assets*. For example, altered economic conditions from climate change may result in expenses exceeding income for some products associated with high GHG-emitting assets. The write-down of those assets may qualify as loss contingencies. In the same context, under altered economic conditions caused by climate change, a company may have situations of *uncollectible receivables*, and they may qualify as loss contingencies.

The concept of a loss contingency is not necessarily easy to apply. A loss contingency derives from what already has happened, not from what might happen. So, the anticipation of future GHG emissions will not likely be the basis for a present loss contingency. A possible litigation will not likely qualify as a loss contingency, although a pending or threatened litigation might, but which still requires evaluation for being probable, estimable, and material.

There are other types of loss contingencies described in FAS 5 – FIN 14. They should be reviewed, as well, and considered in the context of a company's business, in addition to the three broadly-applicable types sketched above using some climate change-related examples.

- **Disclosure of material asset retirement obligations.** Under the instructions of FAS 143 – FIN 47, companies must disclose material asset retirement obligations, which are commitments for actions to be taken in the future before those assets can be retired (FASB, 2001; FASB, 2005).

  Retirement would be sale, abandonment, recycling, or disposal in some manner. If the fair value of an asset retirement obligation can be *estimated* and is *material*, then the asset retirement obligation must be disclosed and its cost must be accrued on company books as soon as the retirement obligation is incurred, i.e., when the legal obligation for a retirement action is known, instead of waiting until the retirement action begins; and it must be kept on the books until the obligation is resolved.

  How does FAS 143 – FIN 47 apply to climate change disclosure? Asset retirement obligations may be discerned as a company attends to retirement of higher GHG-emitting assets as part of an emissions reduction strategy. Some assets historically may have contained, stored, or used hazardous materials or petroleum products. As a result, companies may have obligations to perform remediation actions before those assets can be retired. For example, asbestos-containing materials must be removed before a building can be demolished or sold, which would be an asset retirement obligation under FAS 143 – FIN 47, assuming the removal cost is estimable and material. In another example, the results of normal containment loss from petroleum-carrying underground piping systems may have to be remediated before an asset can be retired, and that may qualify as an asset retirement obligation.

  To qualify, in fact, there must be a *legal obligation* to take an action, such as a remediation, and the necessity for the action must result from *normal operation* of the asset. So, *normal leakage* might occur from normal operation (and maintenance and care) administered at a system. By comparison, improper operation could result in abnormal leakage or a spill, the remediation of which should have consideration as a loss contingency under FAS 5 – FIN 14. As the reader might suspect, however, there is not a *bright line* distinction between normal and improper operation to assist in deciding whether FAS 5 – FIN 14 or FAS 143 – FIN 47 applies. A company

> might determine, in fact, that it has a combination of asset retirement obligations and loss contingencies. (See Deatherage, 2006 for the transcript of a panel discussion on making distinctions between loss contingencies and asset retirement obligations.)
>
> When a company makes a distinction between an asset retirement obligation and a loss contingency, it determines when disclosure is made and how cost is calculated and accrued. For a material asset retirement obligation, disclosure is made immediately, although resolution of the obligation may occur much later, discounting is used to calculate a present value for the future cost, and cost is accrued immediately on company books. For a material loss contingency, disclosure and accrual generally are made near the time of the action or other resolution, and discounting is not used in calculating cost. So, for an asset retirement obligation as compared with a loss contingency, disclosure and accrual are more immediate and the initially disclosed cost has the benefit of discounting.

In addition to instructions on what is to be disclosed and accrued, and when, there are requirements that apply to corporate *controls* on the disclosure and financial reporting process, and these extend to the matter of climate change. Under Item 307 of SEC Regulation S-K, a company's financial report must have a statement of management's conclusions on the effectiveness of the company's *disclosure controls and procedures*. Under Item 308, the financial report also must have a statement of management's conclusions on the effectiveness of the company's *internal controls for financial reporting*, including a description of how that effectiveness was assessed. The company's public accounting firm must supply a statement, as well, attesting to that assessment.

Under Sections 302 and 906 of the Sarbanes-Oxley Act, management must *certify* "that information contained in the periodic report fairly presents, in all material respects, the financial condition and results of operations of the issuer;" with criminal penalties for a statement "that does not comport" potentially bringing fines up to $5,000,000 and imprisonment up to 20 years (Sarbanes-Oxley, 2002). Clearly, these SEC and Sarbanes-Oxley requirements place great importance on the sufficiency and integrity of an *information and control system* that enables analysis and decision-making for financial reporting—and that also should enable confirmation and maintenance of compliance with the requirements and standards that pertain to climate change disclosure.

In fiscal years 2000 through 2006, the SEC initiated fewer than 700 enforcement actions a year, as shown in the Appendix C table, with roughly a quarter being *financial disclosure* enforcement actions (Farrell, 2006; Johnson, 2006). These are such small numbers compared with the many thousands of public companies registered with the SEC that perhaps fear of an enforcement action is relatively small motivation on its own for diligence in disclosure.

*The exposure of top corporate executives is evident, however*, in the recent resolution of several financial disclosure enforcement actions brought by the SEC, in which there was improper reduction of environmental reserve accounts. Besides penalties for the companies, which were Safety-Kleen Inc., ConAgra, and Ashland, Inc., the resolutions brought costly fines and possible imprisonment for individuals formerly in key management positions, e.g., chief executive officer, chief financial officer, controller, vice president. For example, the former chief financial officer of Safety-Kleen could receive up to $2.25 million in fines and 45 years in prison for his guilty plea before the SEC on June 22, 2007 (Grayson, 2007). In a separate class action suit, institutional investors already had won in 2005 a $200-million judgment against this chief financial officer and his former chief executive officer (Cook, 2005).

Taken together, the requirements for management certifications under Items 307 and 308 of SEC Regulation S-K and under Sections 302 and 906 of Sarbanes-Oxley, the possibility of SEC enforcement actions, and the recent evidence of costly consequences to former top executives from improper environmental financial disclosure reinforce corporate management's need for disclosure diligence, including on climate change.

## V. A WELL-MANAGED COMPANY MUST MAKE ITS OWN WAY AT THIS TIME ON CLIMATE CHANGE DISCLOSURE

1. Two events occurring recently and nearly simultaneously—subpoenas from the New York Attorney General's office sent on September 14, 2007 to five large energy companies questioning the adequacy of disclosure to shareholders on possible financial liability from anticipated GHG emissions and a letter petition from a group of high-level money managers sent on September 18, 2007 to the SEC contending that insufficient disclosure by companies on climate change prevents sound investment decisions—have directed relatively high-profile attention to the matter of climate change disclosure.

2. There currently are no federal climate change laws and regulations. That companies exhibit uncertainty and even avoidance on climate change disclosure is not particularly surprising, even if it is an inadequate response.

3. Not only is there is a perceived history of inadequate environmental disclosure, in general, by companies, there is confusion among companies over what is adequate—which sets an unfortunate stage for contemplating climate change disclosure.

4. There is no knowing when federal climate change legislation will be enacted and whether it will contain disclosure elements. As well, the development of regulations following legislation will add to the time line before climate change-specific instructions can be available to companies.

5. A company waiting for new legislative and regulatory outcomes before contending with climate change disclosure, however, is in exposed and inadvisable delay on the matter.

6. Existing regulations and standards pertain to the matter of climate change disclosure and instruct, if indirectly, on what is to be disclosed and accrued, and when.
7. There are requirements, as well, for corporate controls on disclosure and reporting, and these extend to climate change disclosure.
8. Despite the relatively small number of enforcement actions advanced annually by the SEC, recent resolutions of previously pending enforcement actions involving improper environmental financial disclosure indicate that top corporate executives are exposed on the matter, those resolutions bringing costly fines and potential imprisonment to individuals formerly in key management roles.
9. Taken together, these requirements, the possibility of SEC enforcement actions, and recent evidence of costly consequences to former top executives from improper environmental financial disclosure reinforce corporate management's need for disclosure diligence, including on climate change.
10. A well-managed company essentially must make its own way on this matter, setting about systematically on its interpretation of existing regulations and standards for application to climate change disclosure; and such a company must be underway, not in delay.

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## Appendix A. Disclosure Elements in Climate Change Legislation Proposed in the Current, 110th Congress

| Climate Change Disclosure Elements | HR 2651[a] | S 309[b] | S 485[c] |
|---|---|---|---|
| **Proposed legislation *applies* to these issuers of securities under the Securities Exchange Act of 1934:** | | | |
| • *All* issuers of securities | X | X | |
| • Issuers with market capitalization of *$1 billion or more*, both publicly- *and privately-held* companies | | | X |
| **Issuers will be required to *disclose*:** | | | |
| • Estimated *financial exposure* of the company from its own emissions | X | X | X |
| • Potential *economic impact* of global warming on the company | X | X | X |
| • Table of *GHG emissions* and a link or address to a complete GHG emissions report | X | | |
| • Statement of whether or not the GHG emissions report was *independently verified* | X | | |
| **Facilities Accounting Standards Board (FASB) or an equivalently appropriate organization will *develop*:** | | | |
| *Uniform format* for issuers to use in disclosing the information | X | X | X |
| **Securities and Exchange Commission (SEC) will *prepare*:** | | | |
| *Regulations* that codify what issuers will disclose, and the regulations will be finalized within: | | | |
| • *One* year of enactment of the legislation | X | | |
| • *Two* years of enactment of the legislation | | X | X |
| *Interim interpretive release* instructing issuers to use Items 101 and 303 of Regulation S-K for disclosure instructions until regulations are finalized, and to recognize that: | | | |
| • U.S. commitments[d] to reduce GHG emissions are considered a *material effect* | X | X | X |
| • Global warming constitutes a *known trend* | X | X | X |

[a] HR 2651, "Greenhouse Gas Accountability Act of 2007," Rep. Eliot Engel (D-NY)

[b] S 309, "Global Warming Pollution Reduction Act," Sen. Bernard Sanders (I-VT)

[c] S 485, "Global Warming Pollution Reduction Act of 2007," Sen. John Kerry (D-MA)

[d] Under United Nations Framework Convention on Climate Change, New York, May 9, 1992

## Appendix B. Disclosure Criteria and Requirement for Cost Accrual in SEC Regulation S-K and GAAP Pertaining to Climate Change

| Disclosure Criteria | |
|---|---|
| **SEC Regulation S-K** [a] | |
| • Item 101(c)(xii), Effects from compliance with environmental laws | |
| Material | |
| • Item 103(5), Legal proceedings from environmental laws | |
| Material, damages >10 % of assets or monetary sanctions >$100,000 | |
| • Item 303, Effects of known trends | |
| Material | |
| **GAAP,** [b] **FASB**[c] **Standards** | **Cost Accrual Required** |
| • FAS 5 – FIN 14,[d] Loss contingencies | |
| Material, probable, estimable, or | **X** |
| Material, probable, *not* estimable, or | |
| Material, reasonably *possible*, estimable | |
| • FAS 143 – FIN 47,[e] Asset retirement obligations | |
| Material, estimable, or | **X** |
| Material, *not* estimable | |

[a] U.S. Securities and Exchange Commission (SEC) Regulation S-K, 17 CFR Subpart 229.101, 103, and 303

[b] Generally accepted accounting principles

[c] Financial Accounting Standards Board

[d] FASB Statement of Financial Accounting Standards No. 5, "Accounting for Contingencies," and FASB Interpretation No. 14, "Reasonable Estimation of the Amount of a Loss, an Interpretation of FASB Statement No. 5"

[e] FASB Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" and FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations, an Interpretation of FASB Statement No. 143"

**Appendix C. Number of SEC Enforcement Actions, including on Financial Disclosure, in Fiscal Years 2000 to 2006**

| **Enforcement Actions** | **Fiscal Year** | | | | | | |
|---|---|---|---|---|---|---|---|
| | **2000** | **2001** | **2002** | **2003** | **2004** | **2005** | **2006** |
| Total Enforcement Actions | 503 | 484 | 598 | 679 | 639 | 630 | 574 |
| On Financial Disclosure | 103 | 112 | 163 | 199 | 179 | 185 | 128 |
| Percent of Total Actions | 20 | 23 | 27 | 29 | 28 | 29 | 24 |

Sources: Farrell, Greg, "SEC Enforcement Activity Lags," *USA Today*, August 20, 2006, http://www.usatoday.com/money/companies/regulation/2006-08-20-cox-usat_x.htm?csp=34 and Johnson, Sarah, "SEC Enforcement Declines 8.9 Percent," *CFO.com*, November 3, 2006, http://www.cfo.com/article.cfm/8127167.