



SEC Issues Interpretive Guidance Regarding Climate Change Disclosure

February 8, 2010

On January 27, 2010, the Securities and Exchange Commission ("SEC") voted (in a 3-2 vote) to issue an interpretive release providing guidance for disclosures relating to climate change.¹ While the Release imposes no new disclosure obligations, it does serve to remind reporting companies that a number of existing SEC disclosure regulations may require disclosure of certain matters relating to the potential effects of climate change. The Release focuses on four climate change topics that may warrant disclosure, depending on an issuer's² particular circumstances:

- impacts of existing and pending laws and regulations relating to climate change;
- impacts of foreign and international treaties and accords relating to climate change;
- indirect impacts of legal, technological, political and scientific developments regarding climate change; and
- physical impacts of climate change.

THE INTERPRETIVE RELEASE

The SEC prefaces its guidance with a lengthy discussion of recent legal and regulatory developments, both domestic and foreign, addressing climate change-related matters. Having reviewed these developments, the SEC indicates that climate change-related matters may need to be disclosed under existing securities laws and regulations, including pursuant to Item 101 of Regulation S-K (Description of Business), Item 103 of Regulation S-K (Legal Proceedings), risk factors disclosure made pursuant to Item 503(c) of Regulation S-K, and management's discussion and analysis of financial condition and results of operations ("MD&A") required pursuant to Item 303 of Regulation S-K, and similar, although in some instances less prescriptive requirements, applicable to foreign private issuers. The SEC states that in determining whether disclosure is appropriate under these, or other applicable provisions of

¹ *Commission Guidance Regarding Disclosure Related to Climate Change*, Release Nos. 33-9106, 34-61469, available at 75 Fed. Reg. 6,290 (Feb. 8, 2010) and <http://www.sec.gov/rules/interp/2010/33-9106.pdf>.

² The climate change disclosures discussed in the Release are applicable to disclosures made in registration statements and prospectuses as part of offerings registered under the Securities Act of 1933, as amended, and disclosures contained in the periodic and current reports filed by reporting companies pursuant to the Securities Exchange Act of 1934, as amended. The term "issuer" in this memorandum refers to companies making disclosures pursuant to the Securities Act or the Securities Exchange Act.

securities law, an issuer may need to consider any of four topics discussed in the Release. These topics are offered as examples, not as an exhaustive list.

The first topic the SEC focuses on is the impact, both positive and negative, of existing and pending laws and regulations relating to climate change. Examples include:

- Costs to purchase, or profits from sales of, allowances or credits under a “cap and trade” system;
- Costs required to improve facilities and equipment to reduce emissions in order to comply with regulatory limits or to mitigate the financial consequences of a “cap and trade” regime; and
- Changes to profit or loss arising from changes in demand for the issuer’s goods and services resulting directly from legislation or regulation, and indirectly from changes in costs of goods sold.

With regard to disclosure that may be appropriate in light of pending legislation relating to climate change, the SEC counsels that a two-part analysis would be appropriate. Unless management determines that the legislation is unlikely to be enacted, it must proceed to a second stage of analysis based on the assumption that the legislation will indeed be enacted. Then, unless management determines that a material effect is not reasonably likely, disclosure of the potential impact of the legislation would be required.

Secondly, the SEC states that issuers should similarly consider the impact of foreign and international treaties and accords relating to climate change, such as the Kyoto Protocol and the European Union’s Emissions Trading System.

The SEC’s third focus is the indirect impact, both positive and negative, of legal, technological, political and scientific developments regarding climate change. The SEC provides the following examples of such developments in the Release:

- Decreased demand for goods that produce significant greenhouse gas emissions;
- Increased demand for goods that result in lower emissions than competing products;
- Increased competition to develop innovative new products;
- Increased demand for generation and transmission of energy from alternative energy sources;
- Decreased demand for services related to carbon based energy sources, such as drilling services or equipment maintenance services; and
- Adverse impacts to reputation.

The fourth topic the SEC discusses at length in the Release is the physical impact of climate change, such as the impact of increasingly severe storms, rising sea levels, altered arability of land, and altered availability and quality of water. The SEC includes the following examples of such impacts:

- Property damage and disruptions to operations, including manufacturing operations or the transport of manufactured products that may be experienced by issuers with operations concentrated in coastal areas;
- Indirect financial and operational impacts from disruptions to the operations of major customers or suppliers from severe weather, such as hurricanes or floods;
- Increased insurance claims and liabilities for insurance and reinsurance companies;
- Decreased agricultural production capacity in areas affected by drought or other weather-related changes; and
- Increased insurance premiums and deductibles, or a decrease in the availability of coverage, for issuers with plants or operations in areas subject to severe weather.

The Release does not require that issuers calculate their “carbon footprints.” Several State officials and environmental and investor advocacy groups had urged the SEC, in a formal petition, to specifically require that issuers calculate their greenhouse gas emissions pursuant to a particular protocol. While the calculation of greenhouse gas emissions may be otherwise required for some issuers,³ the SEC has not mandated the calculation of greenhouse gas emissions. Instead, the SEC states that in analyzing the possible impacts of legislation or a regulation, management “should ensure that it has sufficient information regarding the issuer’s greenhouse gas emissions and other operational matters to evaluate the likelihood of a material effect arising from the subject legislation or regulation.” The SEC also observes that issuers “should be aware” that information such as the issuer’s greenhouse gas emissions generated for other purposes may be required to be disclosed under existing SEC disclosure requirements.

As an interpretive release, the Release is not subject to formal proposal and public comment requirements. However, the SEC has announced its intention to hold a public roundtable meeting in the spring of this year addressing climate change issues. The results of the roundtable will be used by the SEC to help determine whether further guidance or rulemaking regarding climate change is necessary or appropriate. In addition, the SEC indicates in the Release that it will monitor the impact of the Release on filings by reporting companies as part of the SEC’s ongoing disclosure review program.

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³ U.S. Environmental Protection Agency regulations now require many larger emitters of greenhouse gases to measure and report their emissions to the Agency. See 74 Fed. Reg. 56,260 (October 30, 2009).

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For more information, please feel free to contact your relationship partner, any member of the Firm's Public Company Advisory Practice, or either of the following attorneys in the Firm's Environmental Practice Group:

Adeeb Fadil
(212) 455-7070
afadil@stblaw.com

Michael Isby
(212) 455-3915
misby@stblaw.com

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UNITED STATES

New York

425 Lexington Avenue
New York, NY 10017
+1-212-455-2000

Los Angeles

1999 Avenue of the Stars
Los Angeles, CA 90067
+1-310-407-7500

Palo Alto

2550 Hanover Street
Palo Alto, CA 94304
+1-650-251-5000

Washington, D.C.

1155 F Street, N.W.
Washington, D.C. 20004
+1-202-636-5500

EUROPE

London

CityPoint
One Ropemaker Street
London EC2Y 9HU
England
+44-(0)20-7275-6500

ASIA

Beijing

3119 China World Office 1
1 Jianguomenwai Avenue
Beijing 100004
China
+86-10-5965-2999

Hong Kong

ICBC Tower
3 Garden Road, Central
Hong Kong
+852-2514-7600

Tokyo

Ark Mori Building
12-32, Akasaka 1-Chome
Minato-Ku, Tokyo 107-6037
Japan
+81-3-5562-6200

LATIN AMERICA

São Paulo

Av. Presidente Juscelino Kubitschek, 1455
São Paulo, SP 04543-011
Brazil
+55-11-3546-1000