

## CORPORATE AND SECURITIES LAW ALERT

NEWS FOR THE CLIENTS AND FRIENDS OF BASS, BERRY & SIMS PLC

### **Climate Change Disclosure in SEC Filings**

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As discussed in a [previous alert](#), the Securities and Exchange Commission recently issued interpretive guidance regarding climate change disclosures in SEC filings.

It is important to note that the SEC has not proposed new disclosure rules with this guidance. The SEC's stated objective in publishing the guidance is to provide clarity on the SEC's existing disclosure requirements as they apply to climate change. The interpretive guidance does not create new legal requirements or modify existing ones, but it does express the SEC's views regarding when climate change disclosures may be required under current securities laws and regulations. Accordingly, reporting companies should carefully consider whether modification of their historic climate change and other environmental disclosures, if any, is needed in light of the interpretive guidance. SEC Chairman Mary Schapiro stressed that by issuing the interpretive guidance the SEC is not taking a position on any facts relating to climate change or global warming.

#### **Why Climate Change?**

Climate change – specifically the risk of changes to the global climate resulting from man-made emissions of greenhouse gases – has become a topic of intense public discussion in recent years. It is also an area with rapidly changing legal implications. Current federal, state and local laws regulate various aspects of greenhouse gas emissions, and binding international treaties have affected companies with overseas operations for years. Most prominently, effective January 2010, federal regulations mandate the reporting of greenhouse gas emissions from certain industries to the U.S. EPA. The EPA has also taken steps to regulate greenhouse gas emissions from mobile and stationary sources under the Clean Air Act. Last year, the House of Representatives passed comprehensive, economy-wide climate change legislation, although the Senate has not voted on a comparable bill. State laws associated with regional initiatives in the northeastern and western states have included mandatory greenhouse gas emission reductions from certain industries. More stringent and comprehensive federal laws and international treaties and accords are anticipated in the years to come. Alleged harms associated with climate change, both actual and potential, have been the subject of an increasing amount of litigation in recent years. In addition, climate change and other environmental disclosures have been the subject of state securities enforcement actions and numerous shareholder proposals calling for additional disclosures.

#### **Effects of Climate Change Highlighted by Release**

The interpretive guidance emphasizes four areas where climate change related issues may impact a registrant's disclosure obligations:

- Impact, both positive and negative, of significant developments in federal and state legislation, including the effect of pending legislation or regulation, and the difficulties involved in assessing the

timing and effect of pending environmental legislation, especially for registrants that are particularly sensitive to greenhouse gas regulation;

- Impact of international treaties or accords concerning climate change on businesses, especially for registrants with operations outside the United States that are or will soon become subject to such standards;
- Indirect consequences of legal, technological, political and scientific developments, such as increased demand for goods that result in lower greenhouse gas emissions, decreased demand for goods that produce significant greenhouse gas emissions, or reputational damage arising from the public's perception of any publicly available data relating to the registrant's greenhouse gas emissions; and
- Physical impact of climate change, including the potential effects of severe weather conditions (for example, floods or hurricanes), sea levels and water availability and quality.

Registrants should consider these potential sources of climate change impacts on their business when preparing disclosures for their Form 10-Ks, annual reports to shareholders and other disclosure documents.

### Where Climate Change Disclosure May Be Required

The interpretive guidance highlighted four previously existing items of Regulation S-K that set forth most of the potential scope of climate change disclosure:

- **Description of Business.** Item 101 of Regulation S-K requires a registrant to describe its business and that of its subsidiaries, including, among other topics, the material effects that compliance with environmental laws may have upon capital expenditures, earnings and competitive position, as well as material estimated capital expenditures for environmental control facilities.
- **Legal Proceedings.** Item 103 of Regulation S-K requires a registrant to briefly describe any material pending legal proceeding to which it or any of its subsidiaries is a party, generally including proceedings arising under environmental laws that are material to its business or financial condition, involve an amount that exceeds 10 percent of consolidated current assets, or to which a governmental authority is a party involving potential monetary sanctions of \$100,000 or more.
- **Risk Factors.** Item 503(c) of Regulation S-K requires a registrant to discuss the most significant factors that make an investment in the registrant speculative or risky.
- **Management's Discussion and Analysis.** Item 303 of Regulation S-K requires disclosure known as the Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"). MD&A should provide material historical and prospective textual disclosure, enabling investors to assess the financial condition and results of operations of the registrant by providing the context within which the financial information should be analyzed. Among other things, MD&A should discuss important trends, demands, commitments, events or uncertainties that could have a material impact on the registrant's liquidity, capital resources or results of operations. A significant portion of the climate change interpretive guidance focuses on MD&A disclosure requirements, both generally and as that disclosure may be impacted specifically by climate change issues. The SEC reminded registrants in the guidance that MD&A disclosure should highlight issues that are reasonably likely to cause reported financial information not to be indicative of future operating performance or of future financial conditions. According to the SEC, when determining whether to disclose trends, demands, commitments, events and uncertainties generally, registrants should:
  - consider financial, operational and other information known to the registrant;

- identify, based on this information, known trends and uncertainties; and
- assess whether these trends and uncertainties will have, or are reasonably likely to have, a material impact on the registrant's liquidity, capital resources or results of operations.

Analyzing the materiality of known trends, events or uncertainties related to climate change issues (particularly proposed climate change legislation) may be challenging for registrants preparing MD&A disclosure. When a trend, demand, commitment, event or uncertainty is known, management must make two assessments when considering whether disclosure is required under existing SEC guidance:

- Is the known trend, demand, commitment, event or uncertainty likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required.
- If management cannot make that determination, it must evaluate objectively the consequences of the known trend, demand, commitment, event or uncertainty, on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the registrant's financial condition or results of operations is not reasonably likely to occur.

### **Carbon Footprint Disclosure; Voluntary Disclosures**

While the SEC stressed the importance of registrants properly disclosing the impact of climate change issues on their businesses as discussed above, the SEC emphasized that the interpretive guidance does not impose any new legal requirements for disclosure or change the materiality standard applicable to SEC disclosure questions. Information continues to be material if there is a substantial likelihood that a reasonable investor would consider the information important in deciding how to vote or make an investment decision, or, put another way, if the information would alter the total mix of available information. Specifically, the interpretive guidance does not, in and of itself, create a new requirement for a registrant to disclose its carbon footprint or the steps it is taking to reduce emissions. However, the SEC commented that registrants that voluntarily reported information about their greenhouse gas emissions or other environmental matters publicly, such as through the Carbon Disclosure Project, should consider whether that disclosure is consistent with disclosure in SEC filings.

### **Revisit Disclosure Control Procedures**

The interpretive guidance is expected to cause registrants to take a harder look at whether climate change issues are reasonably likely to have a material impact on them, whether they should disclose climate change matters in their SEC filings and, if they have been making such disclosure, whether it is adequate. Although the SEC has advised registrants not to dilute the usefulness of their disclosure with immaterial information, registrants in business sectors sensitive to climate change impact may receive comments by the SEC staff if their filings omit any discussion of matters covered by the interpretive guidance.

The full text of the release is available at <http://www.sec.gov/rules/interp/2010/33-9106.pdf>.

Bass, Berry & Sims PLC's Periodic and Current Reporting Subgroup monitors and advises on developments in SEC reporting, including quarterly, annual and current SEC reports and proxy statement disclosures as well as XBRL compliance. If you have any questions regarding the issues addressed in this alert, please feel free to communicate with your regular contacts in our Corporate and Securities Group, or attorneys in our Periodic and Current Reporting Subgroup, including those responsible for this alert listed below.

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Our environmental lawyers also monitor and advise on climate change developments including federal and state laws and regulations, as well as regional initiatives. Two recent articles we have prepared are available [here](#) and [here](#). Our environmental lawyers also advise clients on potential business opportunities associated with carbon offset markets. For more information about our environmental lawyers involved in climate change issues, please contact any of the attorneys listed below.

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### Bass, Berry & Sims PLC Corporate and Securities Group

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