



Securities Law Alert

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Disclosure of financial risks due to climate change

On August 27, 2008, the New York attorney general announced an agreement with a large publicly traded utility company, Xcel Energy Inc., requiring the company to provide detailed disclosure of global climate change risks to its business. This is the first enforceable agreement requiring public disclosure of potential financial liabilities related to climate change. As Attorney General Andrew Cuomo stated, the “agreement sets a new industry-wide precedent that will force companies to disclose the true financial risks that climate change poses to their investors.” The importance of this action is twofold. First, it is likely to have an impact on public company disclosure not only in the utility industry, but among a host of industries who are affected by climate change and whose carbon emissions could be affected by regulations and legislation aimed at reducing greenhouse gas (GHG) emissions. Second, it is also important because it occurred absent an initiative by the Securities and Exchange Commission to require more fulsome disclosure of the financial risks associated with climate change in public reports filed by reporting companies.¹ This action is the result of subpoenas issued in September 2007 by the Attorney General to Xcel Energy and four other utility companies: AES Corporation, Dominion Resources, Dynegy and Peabody Energy.² As both federal and state legislatures turn their attention to regulating GHG emissions, the efforts by the New York attorney general highlight the risks public companies should be aware of even in areas outside their home jurisdiction or geographic area.

Although public utility companies have provided increased disclosure of risks due to environmental factors, including climate change, over the past few years, much of this disclosure has been focused on the costs associated with increased regulation. In contrast, the action by the New York attorney general requires extensive disclosure of Xcel Energy’s potential financial risks due to climate change and requires this disclosure to be provided in its annual report on Form 10-K. Among the disclosures required by the agreement with the attorney general, Xcel Energy must provide an analysis of:

¹ Although the SEC has taken no formal action in this area, several groups, including a coalition of institutional investors, state treasurers and executive officers have asked the SEC to provide interpretive guidance on public companies disclosure obligations concerning climate risk under existing law. See Petitions for Rulemaking located at <http://www.sec.gov/rules/petitions/2007/petn4-547.pdf> and <http://www.sec.gov/rules/petitions/2008/petn4-547-suppl.pdf>.

- any material financial and business risks due to present and probable future regulation of GHG emissions;
- a description of any litigation involving Xcel Energy related to climate change and the impact of any climate change-related judicial decisions that would have a material adverse effect on its business; and
- the material financial risks due to the physical impact, if any, of changes to the climate, including rising sea levels and changes in weather conditions.

The agreement further provided that, to the extent that Xcel Energy determines that its GHG emissions materially affect its disclosure of climate change risks, the company should provide disclosures that include its:

- current position on climate change;
- estimated current GHG emissions and expected future emissions from planned new coal-fired electric power plants;
- strategies for reducing, offsetting and otherwise limiting its GHG emissions, the anticipated effect of these strategies and results of any such strategies implemented to date; and
- corporate governance actions related to climate change, including the role of its board of directors and whether environmental performance objectives are incorporated into executive officer compensation.

In light of the precedent that this agreement sets regarding disclosure of climate change risks, companies facing such risks should review their current periodic reports and determine whether additional disclosure is warranted. While several of these disclosures would appropriately be placed within the “Risk Factors” section of a company’s Form 10-K, current SEC regulations dictate that material disclosure relating to the impact of climate change should not necessarily be limited to the risk factors. For instance, Item 101(c)(1)(xii) of Regulation S-K requires disclosure of the material impact that compliance with environmental regulations has on a company’s capital expenditures or competitive position. Item 103 of Regulation S-K requires disclosure of any material legal proceedings, and would include those related to climate change. In addition, Management’s Discussion and Analysis requires disclosure of any known trends, uncertainties or events that would have a material impact on a company’s business or operations. Climate change disclosures similar to those required by the attorney general may appear in one or more of these sections.

² The attorney general’s review of these companies is still ongoing.

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