DISCLOSING CLIMATE CHANGE RISKS IN SEC FILINGS

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To Our Clients and Friends:

As companies begin to prepare their annual reports on Forms 10-K or 20-F, they should consider whether it may be necessary or desirable to include disclosure relating to the climate change risks affecting them. Mounting scientific, political and public attention to climate change is increasing pressure on companies to disclose climate-related risks in their Securities and Exchange Commission ("SEC") filings. However, because it is unclear what disclosure is mandated under existing SEC requirements, the extent and nature of climate change disclosure varies widely among companies. Some companies do not mention climate change issues in their SEC filings, while others disclose risks such as those relating to government regulation of greenhouse gas ("GHG") emissions and the physical effects of climate change.

Recent comments by SEC Commissioner Elisse Walter indicate that the SEC may soon issue guidance clarifying climate change disclosure obligations. In addition, various developments in 2009 regarding climate change legislation, regulation and litigation may be relevant to public companies as they determine whether they are adequately disclosing climate change-related risks.

RECENT SEC ACTIVITY

To date, the SEC has not provided guidance concerning the obligations of reporting companies to disclose climate change-related risks. However, Commissioner Walter recently stated that the SEC has been closely examining this issue. Specifically, the SEC has been studying climate change disclosure requirements and has held meetings with advocates of increased climate risk disclosure. While the SEC studies climate change-related issues, Commissioner Walter advised public companies to consider whether they have climate-related disclosure obligations under the current rules, particularly with respect to the Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") disclosure.

The SEC's recent focus on climate change disclosure has in part been prompted by the attention drawn to the issue by several large institutional investors. In 2007, a coalition of pension fund managers, investment fund managers and state comptrollers and treasurers petitioned the SEC to undertake a review of climate change disclosure obligations. In November 2009, a group of institutional investors managing over $1 trillion in assets filed a supplement to the original petition seeking interpretive guidance as to what climate-related material risks public companies should disclose.

In addition, a recent change in SEC rules may make it easier for shareholders to force public companies to disclose climate-related risks to investors. In October, the SEC issued a staff bulletin addressing the exclusion of shareholder proposals from proxy statements under Rule 14a-8(i)(7). In contrast to past practice, which excluded proposals focusing on internal risk assessments, a shareholder proposal will no longer be excludable if (i) the underlying subject matter transcends the day-to-day business matters of the company and raises significant policy issues, and (ii) a sufficient nexus exists between the nature of the proposal and the company. This new approach may make it more difficult to exclude shareholder proposals relating to climate change disclosure and could increase pressure on public companies to disclose climate change risks in their SEC filings.

RECENT CLIMATE CHANGE DEVELOPMENTS

In 2009, there were several important developments concerning climate change that will affect how climate change issues are disclosed in SEC filings:

- **Federal Legislation Gains Momentum.** In June, the U.S. House of Representatives passed a bill that would create a nationwide cap-and-trade program designed to curb emissions of carbon dioxide ("CO_2"), methane and other GHGs. The bill institutes a cap on GHG emissions and establishes a program to trade emissions allowances. To comply with the cap, covered sources could reduce actual emissions by implementing technological or other changes, or purchase emissions allowances on the open market. A similar bill has been introduced in the U.S. Senate and debate on the proposed legislation is scheduled for the spring of this year.

- **EPA Regulates GHG Emissions.** The U.S. Environmental Protection Agency ("EPA") has indicated that it will regulate GHG emissions in the absence of Congressional passage of a comprehensive climate change bill. On December 7, 2009, the EPA issued its "endangerment finding," which concluded that GHG emissions endanger human health and should be regulated. The finding opens the door for the EPA to regulate GHG emissions under the Clean Air Act. The EPA has already proposed rules that could regulate certain large sources of GHG emissions as early as this year by imposing permit requirements under the Clean Air Act. In addition, in September, the EPA finalized a rule requiring certain large emitters of GHGs to report their annual GHG emissions to the EPA beginning this year. The EPA estimates the rule will require reporting from approximately 10,000 facilities.

- **State and Regional Mandates Address Climate Change.** In the absence of federal climate change legislation, various state and regional initiatives are regulating GHG emissions by requiring emissions reporting, setting emission reduction targets and launching energy efficiency campaigns. For example, in November, California proposed a draft rule that would regulate GHG emissions from electricity generators, oil refineries and other industrial facilities and create a state-wide cap-and-trade program in 2012. The Regional Greenhouse Gas Initiative, a regional cap-and-trade system for CO_2 emissions from power plants involving 10 states in the northeastern U.S., is already up and running.

- **Global Initiatives Affect U.S. Businesses.** Internationally, various initiatives, including those implemented by developed countries that are signatories to The Kyoto Protocol to the United Nations Framework Convention on Climate Change, regulate GHG emissions. In December, high-profile negotiations in Copenhagen resulted in a non-binding accord to curb GHG emissions by 2020. Many U.S. companies with European operations are already subject to the European Union's Emissions Trading System, the largest international emissions trading scheme, and more companies may become subject to EU requirements.

- **Energy Companies Settle with New York Attorney General.** In the fall of 2007, the New York State Attorney General subpoenaed executives of five major energy companies seeking information about the climate change risks faced by the companies and the adequacy of related disclosure in SEC filings. Three companies have reached settlements with New York's Attorney General, the most recent of which was announced in November. The terms of the settlements require the companies to disclose in their SEC filings risks posed by federal and state climate change legislation and regulations, risks of climate change litigation, physical risks to assets and infrastructure arising from climate change, quantitative GHG emissions data and information concerning strategies for reducing GHG emissions.

- **Climate Change Litigation.** Two recent decisions may encourage lawsuits against large emitters of GHGs. In September, the U.S. Court of Appeals for the Second Circuit reversed a lower court decision and allowed several states and land trusts to proceed with a public nuisance suit brought against large emitters of GHGs. Plaintiffs had sued six large electric utilities claiming that the utility companies' GHG emissions contributed to climate change, which threatened public health and natural resources, caused environmental damage and constituted a public nuisance. Less than one month later, the U.S. Court of Appeals for the Fifth Circuit reached a similar decision. It ruled that a group of Mississippi property owners who suffered losses in Hurricane Katrina could proceed with a suit against several oil and chemical companies whose GHG emissions allegedly contributed to plaintiffs' damages. In both instances, the appellate courts disregarded the defendants' challenge that the issue raised a political question outside the court's jurisdiction that could more appropriately be addressed through climate change legislation.

CURRENT PUBLIC COMPANY DISCLOSURE

Currently, companies that discuss climate change issues in their public filings generally do so in the MD&A, Business, Legal Proceedings and Risk Factors sections. Disclosure generally addresses some combination of the following topics:

Legislation or Regulation. Many companies discuss the status of foreign, federal, state and regional climate change initiatives and the impact of such initiatives on their business operations. Depending on the nature of a company's operations, new legislation or regulations could require that the company purchase emissions allowances, invest in new equipment, incur significant compliance or operational costs or comply with stricter permitting requirements.

Litigation. Companies that are defendants in climate change suits often disclose the nature of those proceedings. Some companies in carbon-intensive sectors that are not parties to climate change suits have described the risk of future suits being filed against them.

GHG Emissions. Some companies disclose quantitative data concerning their GHG emissions, including the total amount of their annual emissions. Others disclose the initiatives they are implementing to reduce their GHG emissions. Some companies provide their emissions information in other forums, such as on their websites, in their sustainability reports or through organizations such as the Carbon Disclosure Project (a not-for-profit organization that compiles data on companies' GHG emissions). In addition, some insurance companies may soon disclose climate change information pursuant to a National Association of Insurance Commissioners initiative, which requires insurers with annual premiums of at least $500 million to submit a climate risk disclosure survey to the department of insurance in the state in which their company reports the largest volume of premiums annually.

Physical Risks. Some companies discuss the increased physical risks of floods, hurricanes and other natural disasters resulting from climate change. Climate-related events can affect coastal or other assets, increase the cost of key commodities, impair production capabilities and disrupt a company's supply chain.

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In 2010, the SEC may provide companies with guidance clarifying climate change disclosure obligations. In the meantime, reporting companies, particularly those with carbon-intensive businesses, may want to consider 2009's developments when determining whether any updates might be necessary or desirable in upcoming SEC filings.

We will continue to monitor developments in the area of climate change disclosure. Please feel free to contact us with any questions.

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