Climate Change

Climate Change Disclosure: Creeping Up the Learning Curve – Will Disclosure Catch Up with Developments?

McGuireWoods LLP 2009 Disclosure Study Shows Modest Increase in Reporting, Compared to 2008 Baseline Study; Discusses Influences Affecting 2010 Disclosures

By: Jane Whitt Sellers, Karl M. Strait and Meredith Sanderlin Thrower[1]

Climate change disclosure practices of U.S. public companies have been gradually changing over the past several years. Possible explanations include the increasing likelihood of national regulation of greenhouse gas (GHG) emissions, and growing attention to the topic by investors and the media. Another influence may be the insurance industry, which at the prompting of its regulators, is planning to seek information on this topic from its customers and investees.

A few public statements by a member of the Securities and Exchange Commission (SEC) notwithstanding, the SEC has not yet called for any specific disclosures in this area, nor has it provided interpretative guidance regarding the application of existing disclosure requirements to climate change-related matters.

However, the SEC staff has put the topic on the list for consideration by its recently appointed Investor Advisory Committee, signaling that it may be closer to taking specific action than in the past[2]. In the meantime, public companies must vet these issues through their own disclosure controls processes, just as they do other disclosure issues.

Knowing the significant interest in the topic, and to assist our clients and others who are interested in understanding the environment in which climate change disclosures are being made, McGuireWoods LLP conducted a broad-based review of such disclosures in 2008. The 2008 study created a baseline against which future disclosure practices could be compared. In 2009, we conducted a second similar study. The results of our 2009 study, and a year-to-year comparison with the previous study, are presented in this article.

The clear picture that emerges from our 2009 10-K review is that through the main 2009 disclosure season, in spite of highly publicized calls for additional disclosures that have been occurring since the fall of 2007, the very real prospect of a cap and trade bill passing the Congress and anticipation of proposed rules by the Environmental Protection Agency (EPA) requiring disclosure of GHG emissions at a significantly expanded number of facilities, very few companies outside the utilities, energy companies and industrials are making any type of climate change or GHG-related disclosures in their SEC reports. However, despite the small numbers over all, there was some increase in the percentage of companies making these disclosures in almost every industry and company size category we reviewed.

When we think about the modest increase in climate change-related disclosures from 2008 to 2009, we must remember that most companies begin to address the disclosures they will make in their Form 10-K late in the fiscal year and on into the first month or two of the new year. When the period under consideration is October 2008 through February 2009, it is easy to understand that the need to deal with the current and pressing issues presented by the economy completely overshadowed many, if not most, other topics in 2009 10-Ks.

FOR MORE INFORMATION CONTACT:

Jane Whitt Sellers, Partner
704.373.8967
jsellers@mcguirewoods.com

Karl M. Strait, Partner
804.775.1133
kstrait@mcguirewoods.com

Meredith Sanderlin Thrower
804.775.1094
mthrower@mcguirewoods.com

www.mcguirewoods.com

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[1]The authors, partners Jane Whitt Sellers and Karl M. Strait, and associate Meredith Sanderlin Thrower, are in the McGuireWoods LLP M&A, Securities & Corporate Services Department and members of the Climate Change Team.

[2] Available at www.sec.gov/spotlight/invadvcomm/iacmeeting072709-briefingpaper.pdf.

It now is clear that the economic downturn and the change in administration in Washington delayed substantive change in the regulatory environment as it relates to climate change beyond the 2009 Form 10-K filing season.

Consequently, most 2009 disclosures were drafted in the context of uncertainties similar to those existing a year prior. Will the 2010 filing season be different? This remains to be seen. There is certainly greater awareness of the late 2008 Xcel Energy and Dynegy settlements with the New York Attorney General regarding their climate change disclosures. Earlier this year, it appeared that some form of climate change legislation would pass the Congress and help shape related disclosures. That outcome is now questionable. On the other hand:

- EPA recently issued the final version of its regulations for GHG emissions reporting[3].
- EPA announced it will propose regulations requiring large industrial facilities that emit at least 25,000 tons of GHG emissions a year to obtain construction and operating permits covering these emissions. These permits must demonstrate the use of best available control technologies and energy efficiency measures to minimize GHG emissions when facilities are constructed or significantly modified.
- The insurance industry is moving ahead with its call for mandatory reporting of climate change information from industry participants.

Climate change conferences at the United Nations, and coming up later in the year in Copenhagen, will continue to focus attention on the topic. As a firm, we maintain an active interest in this topic and will advise clients on it in connection with their 2009-2010 disclosure reviews.[4]

Constructing the 2009 Review

We constructed our 2009 review after considering:

- SEC disclosure requirements applicable to public companies that are most likely to evoke climate change-related disclosures.
- Petition for Interpretative Guidance on Climate Risk Disclosure filed with the SEC on Sept. 18, 2007, by Ceres and others (Ceres Petition)[5], as supplemented by a letter filed with the SEC on June 12, 2008, by Ceres and others[6].
- Settlement agreement between the New York Attorney General and Xcel Energy Inc. from August 2008[7] , and the settlement agreement between the New York Attorney General and Dynegy Inc. from October 2008[8] (collectively, "settlement agreements").
- The manner in which we conducted our 2008 review.

Based on this analysis, we looked at whether each company made disclosure in its 10-K filed in 2009, addressing one or more of the following issues that roughly correspond to the types of disclosure requested in the Ceres Petition and the settlement agreements:

- Amount of GHG emissions (that is, has the company performed some type of GHG emissions assessment and reported the results in its 10-K).
- Impacts/risks related to current or proposed GHG regulations.
- Impacts/risks related to the physical effects of climate change.
- Legal proceedings regarding GHG emissions or climate change.
- Efforts related to reducing GHG emissions or climate change.

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[3] Available at www.epa.gov/climatechange/emissions/downloads09/FinalMandatoryGHGReportingRule.pdf.

[4] Available at www.naic.org/documents/committees_ex_climate_climate_risk_disclosure_survey.pdf.

[5] Available at www.sec.gov/rules/petitions/2007/petn4-547.pdf.

[6] Available at www.sec.gov/rules/petitions/2008/petn4-547-supp.pdf.

[7] Available at www.oag.state.ny.us/media_center/2008/aug/xcel_aod.pdf.

[8] Available at www.oag.state.ny.us/media_center/2008/oct/dynegy_aod.pdf.

If a company made one or more of these types of disclosures in its 10-K, we also noted where in the 10-K the disclosures were made, including:

- Item 101 – Business
- Item 103 – Legal Proceedings
- Item 303 – Management's Discussion and Analysis (MD&A)
- Risk Factors
- Cautionary Statements Regarding Forward-Looking Statements
- Elsewhere in the 10-K (for example, in notes to financial statements)

Finally, we looked at whether each company's website had significant and prominent company-specific information regarding GHG emissions or climate change.

Companies Reviewed

We reviewed the 10-K filings made in 2009 of more than 400 companies included in the S&P 500, S&P MidCap 400, and S&P SmallCap 600 indices. The S&P indices assign companies to one of 10 industry sectors[9] : consumer discretionary, consumer staples, energy, financial, healthcare, industrials, information technology, materials, telecommunication services and utilities.

S&P 500 companies have a market capitalization in excess of $3.0 billion (and cover approximately 75% of the U.S. equities market); S&P MidCap companies, $750 million to $3.3 billion (covering more than 7% of the U.S. equities market); and S&P SmallCap companies, $200 million to $1 billion (covering approximately 3% of the U.S. equities market)[10].

While the limited number of companies reviewed, particularly in certain industry segments, may not always allow us to make statistically precise statements about disclosure patterns, we think the results of this review are, in most cases, indicative of the current state of SEC disclosure practices among public companies across industry sectors and by market capitalization.

General Observations

The number of companies that made any type of disclosure regarding GHG emissions or climate change in their 10-Ks filed in 2009 is still relatively small. Out of the more than 400 companies reviewed, only 71 (17.3%) made any 10-K disclosure whatsoever regarding GHG emissions or climate change. Of the companies making disclosures:

- 59 (83.1% of the 71 companies making some type of disclosure) addressed impacts/risks related to current or proposed regulation of GHG emissions.
- 25 (35.2%) discussed efforts related to reducing GHG emissions.
- 17 (23.9%) discussed physical impacts/risks related to climate change.
- 12 (16.9%) provided disclosure regarding the amount of their GHG emissions.
- 7 (9.9%) disclosed legal proceedings related to GHG emissions or climate change.

The risk factors section was the most common section in which disclosures appeared. Out of the companies making 10-K disclosures, 54 (76.1%) included risk factors addressing GHG emissions or climate change. Companies also made disclosures in the following sections of their 10-Ks: Item 101 – Business (36), Forward-Looking Statement Safe Harbor disclosures (28), MD&A (22), and Item 103 – Legal Proceedings (4).

Eleven companies made disclosures in other portions of the 10-K, typically in the notes to the financial statements. Some companies also made disclosures regarding the relationship between climate change/GHG initiatives and executive compensation.

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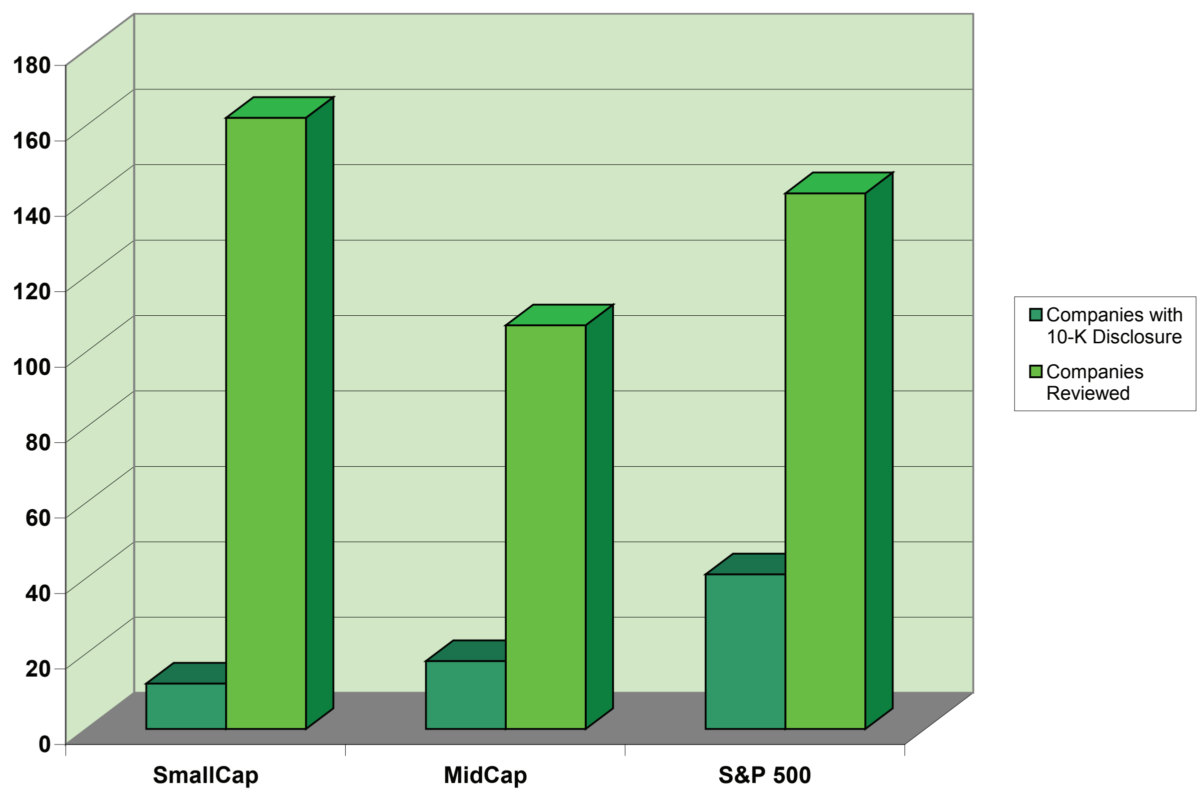
[9] Standard & Poor's uses the Global Industry Classification Standard (GICS®) which establishes a common, global standard of industry classifications for companies worldwide.

[10] Five hundred companies were selected for review, with roughly one-third coming from each of the S&P 500, S&P MidCap 400 and S&P SmallCap 600. The number of companies selected from each GICS Industry Sector was weighted to reflect the sector balance in each index. Out of these 500 companies, only companies that had filed a Form 10-K after December 31, 2008 were reviewed (this eliminated 89 of the companies originally selected).

Disclosure Practices by Company Size

In most cases, there is some correlation between whether disclosure is made, and the size of the company. In general, larger companies provide disclosure more often than smaller companies. S&P 500 companies were most likely (as a percentage of companies in the same market capitalization category) to provide disclosure (28.9%), followed by S&P MidCap companies (16.8%), and then S&P SmallCap companies (7.4%). We observed this pattern across all industry categories. See below for additional discussion regarding disclosure patterns by industry sector.

Companies That Provided 10-K GHG/CC Disclosures in 2009, Compared to Companies Reviewed, by Market Capitalization



The following tables summarize the types of disclosures made by S&P 500, S&P MidCap and S&P SmallCap companies in their 10-Ks filed in 2009, and where those disclosures where found in the 10-Ks.

Company Size (and # Reviewed)	Type of Disclosure (as % of Companies Reviewed)				
	Amount of GHG Emissions	Regulation of GHG Emissions	Physical Effects of CC	Legal Proceedings Related to GHG/ CC	Efforts to Reduce GHG Emissions/ CC
S&P 500 (142)	4.9%	23.2%	7.7%	2.8%	10.6%
S&P MidCap (107)	0.9%	15.9%	2.8%	1.9%	6.5%
S&P SmallCap (162)	1.2%	5.6%	1.9%	0.0%	1.9%
Total (411)	**2.4%**	**14.4%**	**4.1%**	**1.5%**	**6.1%**

In almost all cases, the percentage of companies that made these types of GHG/climate change disclosures in their 10-Ks filed in 2009 increased as market capitalization increased.

Company Size (and # Reviewed)	Location of Disclosure (as % of Companies Reviewed)					
	Item 101 Business	Item 103 Legal Proceedings	Item 303 MD&A	Risk Factors	Forward-Looking Statement Safe Harbor	Elsewhere in 10-K
S&P 500 (142)	13.4%	2.1%	11.3%	20.4%	13.4%	7.7%
S&P MidCap (107)	10.3%	0.9%	2.8%	13.1%	6.5%	2.8%
S&P SmallCap (162)	3.7%	0.0%	1.9%	5.6%	1.2%	1.2%
Total (411)	**8.8%**	**1.0%**	**5.4%**	**13.1%**	**6.8%**	**3.9%**

When looking at disclosures provided outside the 10-K setting, we observed a significant distinction based on the size of the company. S&P 500 companies are much more likely to provide company-specific climate change or GHG disclosure on their websites (51.4%), compared to S&P MidCap (12.1%) and S&P SmallCap (3.7%) companies. This may be due, in part, to the larger companies' larger investor following (and greater resources for preparing website content), which likely means more numerous and strident calls for disclosure of this information.

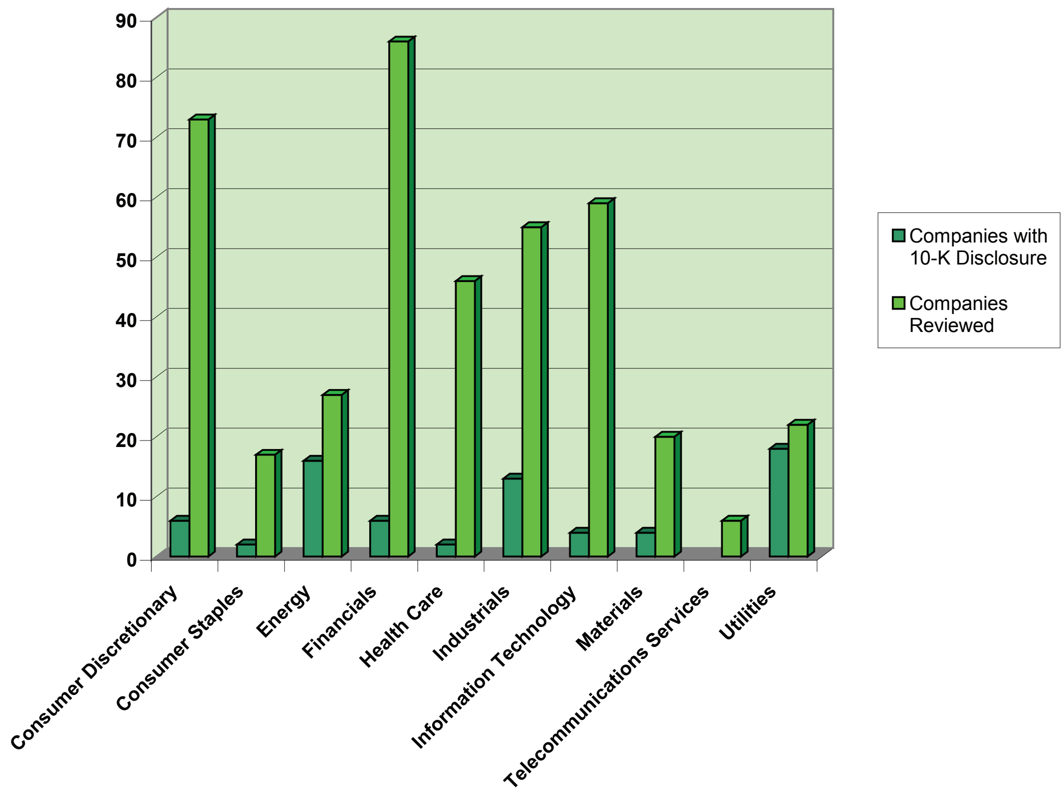
For example, larger companies are more likely to be recipients of shareholder proposals requesting that their boards conduct such assessments and make them publicly available. Negotiating withdrawal of such proposals often involves voluntary disclosures of such information, with websites as the preferred vehicle. Even when the proposal will be presented to shareholders, companies may make voluntary disclosures that may then be favorably cited, even when the proposal is opposed by the board of directors.

Disclosure Practices by Industry Sector

As indicated above, out of the more than 400 companies reviewed, only 71 provided any type of disclosure regarding GHG emissions or climate change in their 10-Ks filed in 2009. It will come as no surprise that the largest concentration of these companies were utility and energy companies, which together comprise 50.7% of companies making these kinds of disclosures.

When industrial companies are added, these three industries account for almost two-thirds (66.2%) of the companies making climate change or GHG disclosures, but constitute just over a quarter (25.3%) of the companies reviewed. In all five disclosure topics, utility and energy companies represent a majority (or just under a majority) of all companies making these kinds of disclosures.

Companies That Provided 10-K GHG/CC Disclosures in 2009, by GICS Industy Sector



Utilities

Of the 22 utility companies reviewed, 18 (81.8%) provided some type of 10-K disclosure regarding GHG emissions or climate change[11]. Of these 18 utility companies, all of them disclosed risks or impacts related to the regulation of GHG emissions. The next most common disclosure for utility companies was discussion of efforts to reduce GHG emissions (11), followed by disclosure of risks related to the physical effects of climate change (7).

These disclosures were made throughout the various 10-K sections: Item 101 – Business (13), MD&A (14), Risk Factors (17), Forward-Looking Statements Safe Harbor (10), and elsewhere (12). All but four of the 18 utility companies that made some type of 10-K disclosure also provided company-specific GHG emissions or climate change information on their websites.

Energy

Of the 27 energy companies reviewed, 16 (59.2%) provided disclosure in their 10-Ks. All but two of these companies disclosed risks/impacts related to regulation of GHG emissions. However, unlike the utility companies, energy companies made almost no other type of climate change or GHG-related disclosure. Only one of these companies (an S&P 500 company) provided information regarding the amount of its GHG emissions. Most disclosures were made in Risk Factors and Item 101 – Business. Only eight of the energy companies reviewed have website disclosure, which is half of the number of energy companies providing some type of 10-K disclosure, and all of these were S&P 500 companies.

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[11] It is somewhat surprising that four of the utility companies did not provide any type of climate change or GHG disclosures in their 10-Ks (one was an S&P MidCap company and three were S&P SmallCap companies).

Other Companies

Out of the 71 companies that made some type of disclosure in their 10-Ks, 37 were non-utility or non-energy companies:

Industrials	13
Consumer Discretionary	6
Financials	6
Information Technology	4
Materials	4
Consumer Staples	2
Healthcare	2

Out of the six telecommunications companies reviewed, none made disclosure of any type in their 10-Ks. However, one of these companies (an S&P500 company) did provide company-specific information on its website.

Industrials. Of the 55 industrial companies reviewed, 13 (23.6%) made climate change or GHG disclosures in their 10-Ks. The vast majority of these companies (10) discussed risks related to current or proposed regulation of GHG emissions and few made any other type of disclosure. The majority of industrial companies making 10-K disclosure were S&P MidCap companies (8). Of the industrial companies (including six companies making 10-K disclosure), 14 provided information on their websites about climate change or GHG emissions.

Consumer Discretionary. Six out of 73 (8.2%) consumer discretionary companies reviewed provided disclosure in their 10-Ks. Four companies discussed risks related to GHG regulations, three companies provided information regarding their efforts to reduce GHG emissions, one company disclosed the amount of its GHG emissions, and one disclosed legal proceedings related to GHG emissions or climate change. Of the companies reviewed, 11 (15.1%) made disclosures on their websites.

Financials. Six (7.0%) of the 86 financials companies reviewed provided disclosure. Four of the companies discussed regulation-related risks, and three disclosed the amount of their GHG emissions. Two companies discussed risks related to the physical effects of climate change, and two discussed efforts to reduce GHG emissions. Seven companies provided climate change information on their websites.

Information Technology. Of the 59 information technology companies reviewed, four (6.8%) provided disclosure in their 10-Ks. Three companies discussed regulation of GHG emissions, two companies discusses efforts to reduce GHG emissions, and one disclosed the amount of GHG emissions. Information technology companies were more likely to provide website disclosure. Of the companies reviewed, 14 (23.7%) included climate change information on their websites.

Materials. Of the 20 materials companies reviewed, four (20.0 %) provided some type of disclosure in their 10-Ks. All of these companies are S&P 500 companies. Three of the companies discussed regulation-related risks, and two discussed risks related to the physical effects of climate change. In addition, one of these companies discussed efforts to reduce GHG emissions, one and one disclosed information about its GHG emissions. Five S&P 500 companies (including all four companies making 10-K disclosure) and one S&P SmallCap company provided information about climate change or GHG emissions on their websites.

Consumer Staples. Of the 17 consumer staples companies reviewed, two (11.8%) provided disclosures in their 10-Ks. Both of these companies are S&P 500 companies. One discussed risks relating to physical effects of climate change, and one disclosed efforts relating to the reduction of GHG emissions. Of the companies reviewed, seven (41.2%) included climate change information on their websites.

Healthcare. The two healthcare companies, out of 46 reviewed, that made any type of climate change or GHG related disclosure are both S&P 500 companies. One company discussed regulation-related risks, and one discussed risks related to physical effects of climate change. Ten healthcare companies provided information on their websites.

As noted above, the most common type of disclosure made in each industry sector addresses risks/impacts related to the regulation of GHG emissions. Since the nature of that regulation remains largely undefined, the disclosures are necessarily general. Of the 71 companies that made any type of 10-K disclosure, 59 (83.1%) addressed this issue. All of the utility and energy companies making 10-K disclosure addressed regulation-related risks.

The following tables summarize the types of disclosures made by companies, by GICS category, in their 10-Ks filed in 2009, and where those disclosures where found in the 10-Ks.

GICS Sector (and # Reviewed)	Type of Disclosure (as % of Companies Reviewed)				
	Amount of GHG Emissions	Regulation of GHG Emissions	Physical Effects of CC	Legal Proceedings Related to GHG/CC	Efforts to Reduce GHG Emissions/CC
Consumer Discretionary (73)	1.4%	5.5%	0.0%	1.4%	4.1%
Consumer Staples (17)	0.0%	0.0%	5.9%	0.0%	5.9%
Energy (27)	3.7%	59.3%	7.4%	7.4%	11.1%
Financials (86)	3.5%	4.7%	2.3%	0.0%	2.3%
Healthcare (46)	0.0%	2.2%	2.2%	0.0%	0.0%
Industrials (55)	1.8%	18.2%	3.6%	1.8%	3.6%
Information Technology (59)	1.7%	5.1%	0.0%	0.0%	3.4%
Materials (20)	0.0%	15.0%	10.0%	0.0%	5.0%
Telecommunications (6)	0.0%	0.0%	0.0%	0.0%	0.0%
Utilities (22)	13.6%	81.8%	31.8%	16.7%	50.0%
Total (411)	**2.4%**	**14.4%**	**4.1%**	**1.5%**	**6.1%**

GICS Sector (and # Reviewed)	Location of Disclosure (as % of Companies Reviewed)					
	Item 101 Business	Item 103 Legal Proceedings	Item 303 MD&A	Risk Factors	Forward-Looking Statement Safe Harbor	Elsewhere in 10-K
Consumer Discretionary (73)	5.5%	1.4%	1.4%	4.1%	1.4%	0.0%
Consumer Staples (17)	5.9%	0.0%	0.0%	5.9%	0.0%	0.0%
Energy (27)	37.0%	3.7%	11.1%	44.4%	25.9%	11.1%
Financials (86)	1.2%	0.0%	1.2%	4.7%	1.2%	1.2%
Healthcare (46)	2.2%	0.0%	0.0%	0.0%	2.2%	0.0%
Industrials (55)	7.3%	0.0%	1.8%	21.8%	7.3%	0.0%
Information Technology (59)	3.4%	0.0%	0.0%	3.4%	0.0%	0.0%
Materials (20)	0.0%	0.0%	10.0%	15.0%	5.0%	0.0%
Telecommunications (6)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Utilities (22)	59.1%	9.1%	63.6%	77.3%	59.1%	54.5%
Total (411)	**8.8%**	**1.0%**	**5.4%**	**13.1%**	**6.8%**	**3.9%**

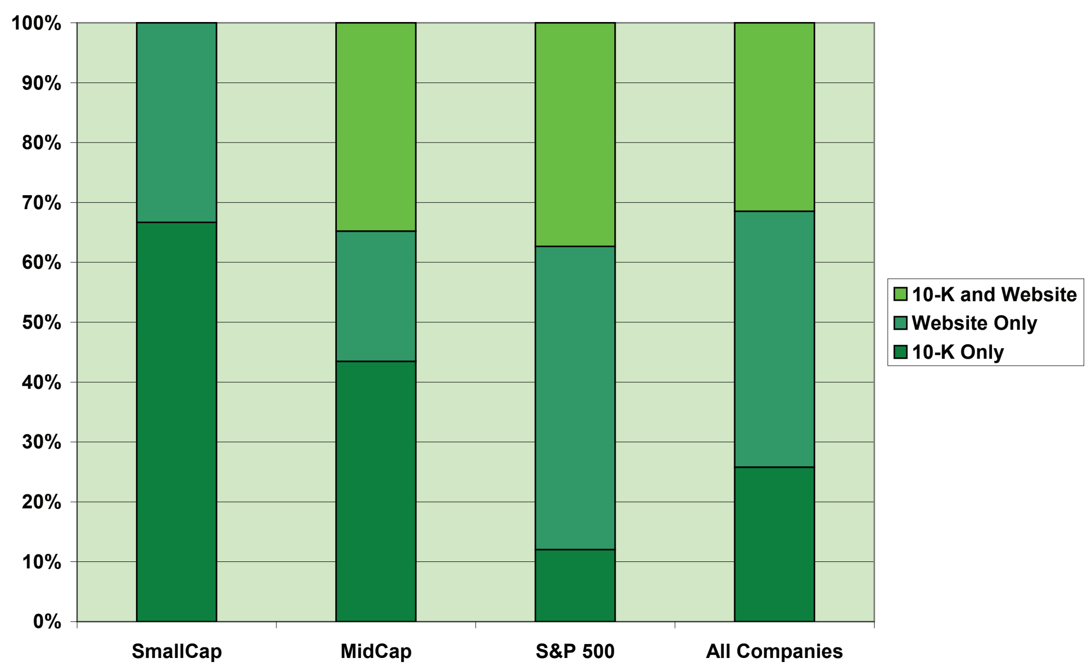
Website & Other Voluntary Disclosures

The limited number of companies that provided some type of climate change or GHG disclosure in their 10-Ks may seem somewhat surprising, given the number of companies that have elected to provide sometimes extensive disclosure in other, voluntary venues. While not widespread, significantly more of the companies reviewed provide company-specific information regarding climate change or GHG matters on their websites (92) than in their 10-Ks (71). There is less overlap than one might expect between the companies that provided 10-K disclosure and those that provide information on their websites.

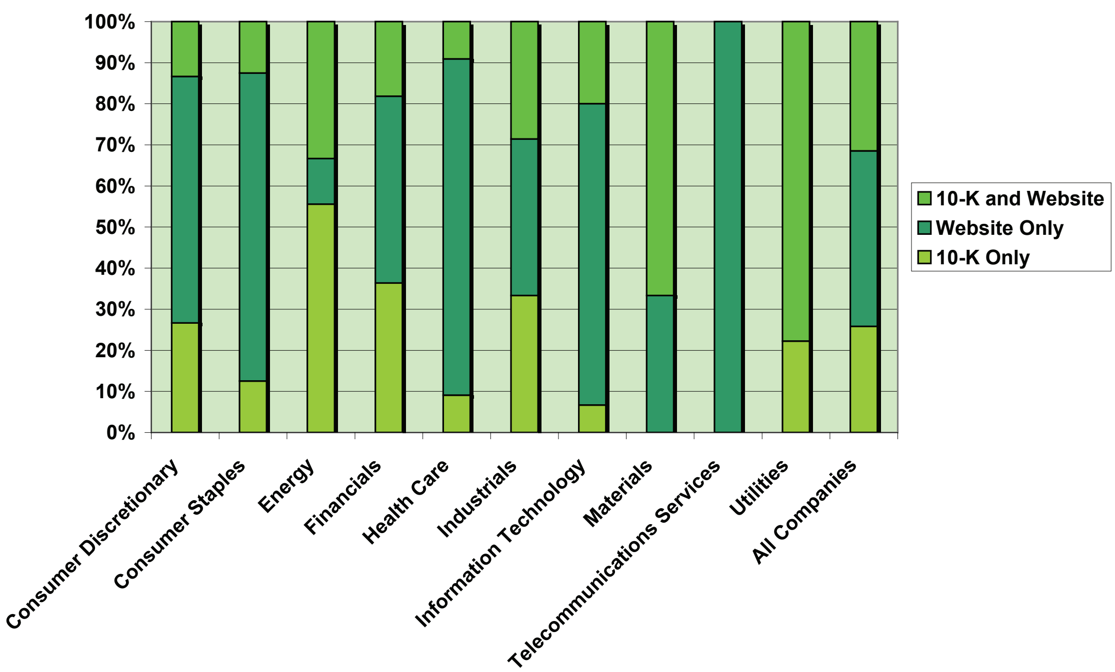
Of the 71 companies that provided 10-K disclosure, 39 (54.9%) also provide information on their websites. On the other hand, of the 92 companies that provide information on their websites, 53 (58.9%) provided no disclosure in their 10-Ks. Of the 92 companies that provide company-specific information related to GHG emissions or climate change on their websites, only 39 (42.4%) have, apparently, concluded that disclosure regarding these matters is material to their investors. Of the 39 companies that provide both 10-K disclosure and website information, 14 were utilities, six were energy companies, and six were industrials.

The following charts compare the percentage of companies making website and 10-K disclosures, by both industry sector and market capitalization.

2009 Website vs. 10-K Disclosure, by Size



2009 Website vs. 10-K Disclosure, by Industry Sector



The contrast between the number of S&P 500 companies that made disclosures regarding GHG emissions or climate change in their 10-Ks, and those that make voluntary disclosures regarding these matters in other forums, is striking. Voluntary GHG and climate change disclosure has occurred in a number of places, most notably the Carbon Disclosure Project (CDP), the Global Reporting Initiative, The Climate Registry, the World Economic Forum Global GHG Register, and the Global Framework for Climate Risk Disclosure. Of these, the Carbon Disclosure Project appears to be the largest repository of corporate greenhouse gas emissions data, serving as a secretariat for 475 institutional investors with more than $55 trillion of assets under management[12].

The information provided in these voluntary forums is interesting, to say the least, when compared to SEC reporting on similar topics. For example, the CDP in September 2009 released the results of its annual S&P 500 questionnaire[13]. According to the CDP, 332 (66%) of the S&P 500 companies responded to the questionnaire[14].

In contrast, only 41 (28.9%) of the 142 S&P 500 companies whose 10 Ks we reviewed provided any type of disclosure in their 10-Ks. In fact, at least one of the U.S. companies graded as a "top scorer" in the CDP's U.S. Carbon Disclosure Leadership Index provided no climate change or GHG disclosure whatsoever in its 10-K filed in 2009.

There may be reasonable explanations for this disparity. However, the fact remains that many S&P 500 companies make extensive disclosures regarding these matters in the CDP, and in many cases these companies identify climate change as posing "commercial risk" having a likelihood of "significant impact" or as a "potential material risk," and yet they do not reflect those risks in what is arguably their most important SEC report for the year.

On its website, the CDP states that it was launched to "collect and distribute high quality information that motivates investors, corporations and governments to take action to prevent dangerous climate change[15]." Several scenarios suggest themselves:

- A risk related to GHG emissions and/or climate change is discussed in a voluntary forum, but not in the company's SEC reports. That risk manifests itself and has a material impact on the results of operations or financial condition of the company. It will be evident that management was aware of the risk, but arguably did not disclose that risk to its investors or make them aware that the company's forward looking statements could be affected by such a risk.

- A risk related to GHG emissions and/or climate change is discussed in a voluntary forum, but not in the company's SEC reports. Even if the risk does not manifest itself, this inconsistency may raise questions about the adequacy of the company's disclosure controls, which must be certified in SEC filings quarterly by the company's senior executive officers.

- Information/data that is provided in a voluntary forum such as the CDP turns out to be inaccurate or misleading in some material respect. An investor, for whose benefit the CDP exists, makes a 10b-5 type claim against the company arguing that the company provided the information in a forum where it knew investors would rely on the accuracy and completeness of the information in making investment decisions.

At a minimum, companies need to examine the implications for making these types of voluntary disclosures, determine what disclosure controls and procedures should apply to them, and evaluate whether similar disclosures should be made in their SEC filings. In cases where a voluntary disclosure forum exists, at least in part, for the benefit of investors, a company must evaluate the potential liability that may attach to that disclosure.

Comparison: 2009 Results vs. 2008 Results

General Observations

Overall, the number of companies making disclosures about GHG emissions and climate change in their 10-Ks increased in 2009 compared to 2008. While different sets of companies were reviewed each year, each set was a random sampling from the companies included in the S&P indices.

Of the companies reviewed, 17.3% made some type of climate change or GHG disclosure in 2009, compared to 12.2% in 2008. That there was an increase in companies making disclosures is not surprising, as a growing number of vocal investors and organizations are focusing on GHG emissions and climate change.

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[12] Press Release, Carbon Disclosure Project S&P500 2009 Reports Launched at New York Climate Week (September 21, 2009) (www.cdproject.net/en-US/WhatWeDo/CDPNewsArticlePages/Carbon-Disclosure-Project-SP-500-2009-Reports-launched-at-New-York-Climate-Week.aspx).

[13] Id.

[14] Id.

[15] Carbon Disclosure Project: What We Do, www.cdproject.net/en-US/WhatWeDo/Pages/overview.aspx (last visited September 24, 2009)

In the later half of 2008, both Excel Energy and Dynegy entered into settlements with the New York Attorney General, and the disclosures required by those settlements were included in their 10-Ks filed in 2009. Shareholder proposals seeking corporate action on climate change continued to increase in 2009. Both the EPA and the National Association of Insurance Commissioners (NAIC) discussed mandatory reporting and disclosure requirements that were approved in 2009. The Obama administration entered office, having repeatedly emphasized the need for meaningful climate change legislation during the presidential campaign.

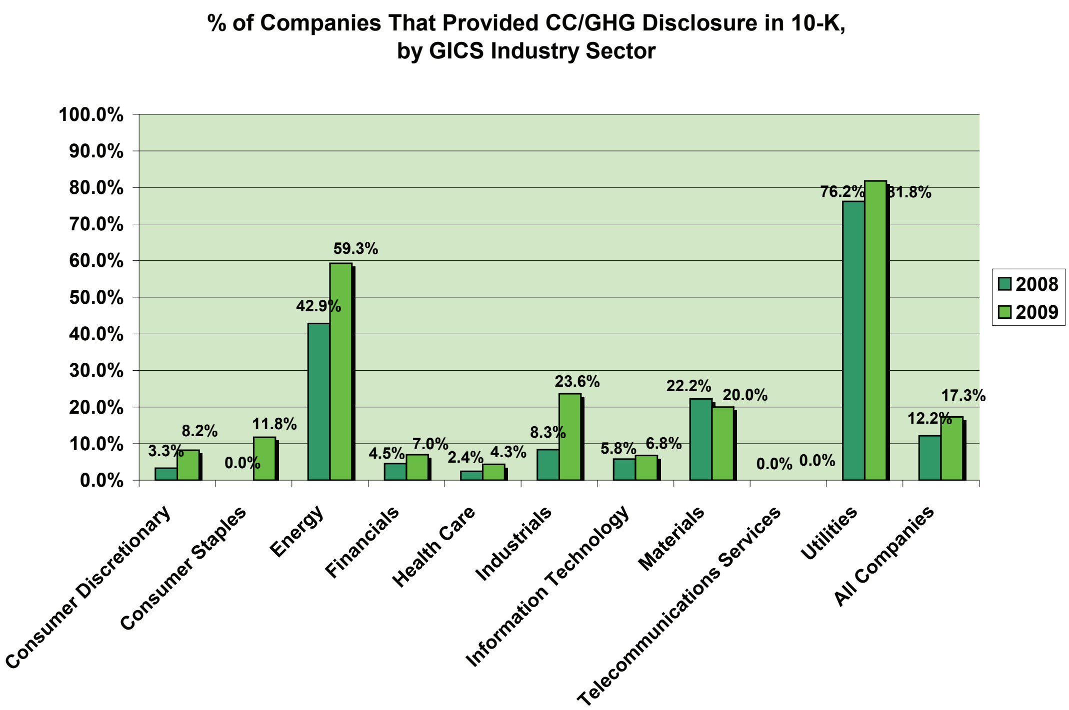
The types of disclosures that increased the most in 2009 addressed:

- Risks relating to current or probable GHG emission regulation (14.4% of the companies making some type of disclosure in 2009, compared to 9.9% in 2008).
- Risks related to physical effects of climate change (4.1% in 2009, compared to 1.7% in 2008).

Observations by Industry Sector

Compared to 2008, eight of the 10 industry sectors had increases in 2009 in the percentage of companies making 10-K disclosures. The two exceptions were materials, which had the same number of companies making 10-K disclosures (4), declining slightly on a percentage basis; and telecommunications, which still does not have any companies making 10-K disclosures.

Utilities continued to be the industry sector with the highest percentage of companies making 10-K disclosures. Of the utilities reviewed in 2009, 81.8% made 10-K disclosures versus 76.2% of the utilities reviewed in 2008. In 2009, a majority of the energy companies reviewed (59.3%) made 10-K disclosures, compared to 42.9% of the energy companies reviewed in 2008. The industrials sector also had a significant increase. The percentage of industrial companies making 10-K disclosures in 2009 almost tripled to 23.6%, compared to 8.3% in 2008.



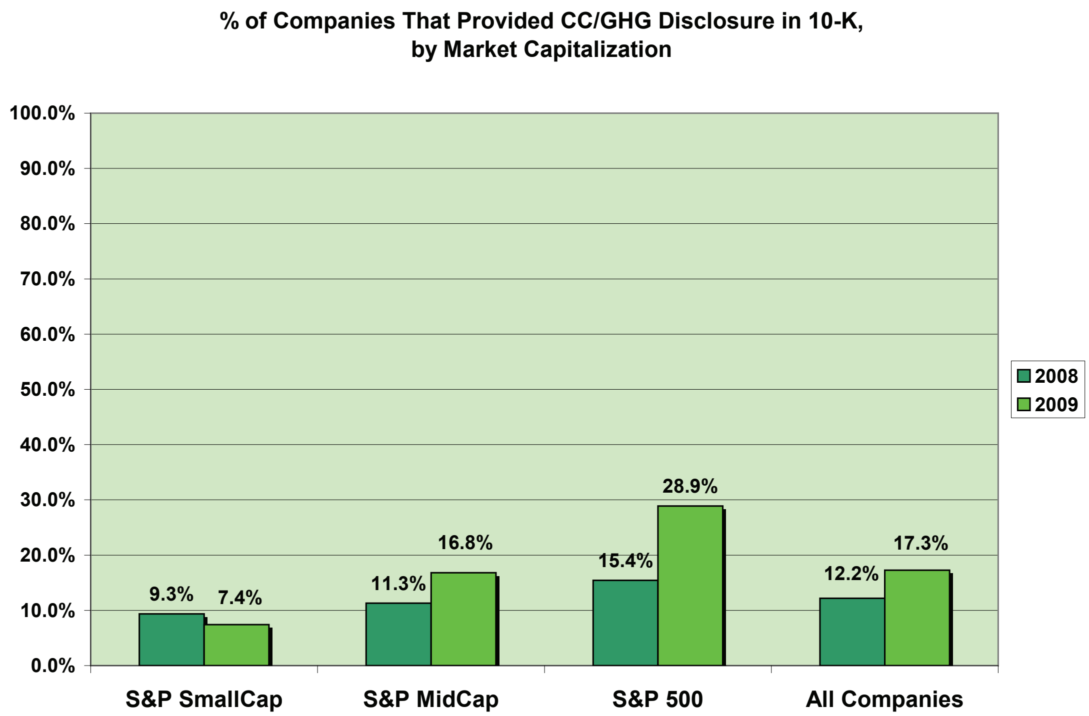
When looking the specific types of disclosures, there were significant increases in individual industry sectors. The percentage of utilities discussing risks related to physical effects of climate change more than tripled in 2009 when compared to 2008 (31.8% v. 9.5%). The percentage of industrial companies making regulation-related risk disclosures more than quadrupled in 2009 (18.2% v. 4.2%). Energy companies also had a considerable increase in regulation-related risk disclosures (59.3% v. 38.1%).

There was one decline in disclosures that stood out. Only half of the number of utilities reported their amount of GHG emissions in 2009 (3) as compared to 2008 (6). The three utilities making this disclosure in 2009 were among the five companies that received a climate risk disclosure subpoena from the New York Attorney General in 2007.

However, this result is not as surprising as it might first appear. To date, there has been no standard methodology for measuring GHG emissions. As a result, there has been increasing discussion regarding whether companies can measure and report GHG emissions such that meaningful comparisons can be made. The EPA's newly adopted GHG emission reporting rules may prompt more disclosure on this issue.

Observations by Company Size

The percentage of S&P 500 companies making 10-K disclosures almost doubled in 2009 to 28.9%, from 15.4% in 2008. There was also an increase in the percentage of S&P MidCap companies to 16.8% from 11.3%, but S&P SmallCap companies had a slight decrease to 7.4% from 9.3%.



The percentage of S&P 500 companies discussing the risks related to physical effects of climate change tripled to a still small 7.7% in 2009, compared to 2.4% in 2008. The S&P MidCap companies had a notable increase in regulation-related risk disclosures to 15.9% in 2009, from 7.8% in 2008. There was a slight decline in the number of S&P 500 companies disclosing their amount of GHG emissions. As noted above in our industry sector analysis, this result may reflect a more thoughtful approach to 10-K disclosures addressing GHG emissions.

Website Disclosure Observations

The percentage of companies making some type of website disclosure increased in 2009, to 22.4%, compared to 14.8% in 2008. It is interesting to note that the percentage increase in companies making website disclosures in 2009 to 22.4% from 14.5% in 2008, exceeded the percentage increase in companies making 10-K disclosures from 12.2% in 2008 to 17.3% in 2009.

Healthcare companies led the way, with 21.2% of the healthcare companies reviewed in 2009 discussing climate change on their websites, compared to 4.9% in 2008. Consumer staples companies (41.2% v. 23.1%) and consumer discretionary companies (15.1% v. 8.2%) also had significant increases in website disclosures, perhaps responding to trends in consumer media.

The percentage of S&P 500 companies that included climate change information on their websites increased sharply to 51.4% in 2009, compared to 27.6% in 2008. S&P MidCap companies increased slightly to 12.1% compared to 11.3% in 2008. Similarly, S&P SmallCap companies had only a slight increase from 2.8% in 2008 to 3.7% in 2009.

Conclusion: "Creeping Up the Learning Curve – Will Disclosure Catch Up with Developments?" 2010 will be the year for more public companies to reevaluate their disclosure practices, policies and procedures regarding GHG and climate change issues.

Even with mounting pressure, it appears most public companies are still waiting for the regulatory landscape to resolve itself before making climate change or GHG disclosures in their SEC reports. Even though the status of a national cap and trade program is uncertain, the recently adopted EPA rules that require the public reporting of GHG emissions should prompt more public companies to reevaluate their disclosure practices, policies and procedures regarding GHG emissions and climate change issues.

Similar to 2008, it is still the case that very few companies outside a few key industries made any type of GHG emissions or climate change-related disclosures in their 10-Ks in 2009. While utility, energy and industrial companies comprise only 25.3% of the companies reviewed in 2009, companies in those industries constitute almost two-thirds (66.2%) of the companies making climate change or GHG disclosures in their 2009 10-K filings.

Given the increased pressure in 2008 for voluntary, and sometimes not-so-voluntary, GHG and climate change disclosures, we had expected this state of affairs to change in 2009. However, the percentage of companies making climate change or GHG related disclosures in their 10-Ks increased only modestly, from 12.2% to 17.3% of the companies reviewed. We continue to believe that even in the absence of interpretive guidance from the SEC, more public companies should reevaluate whether, and to what extent, current rules and regulations require them to make company-specific disclosures regarding the risks and opportunities related to GHG and climate change matters.

While the implementation of a national cap-and-trade or carbon tax system may be uncertain in the current economic and political environment, it is unlikely that calls for more disclosure will abate. Three important recent developments reinforce this conclusion:

- The adoption of mandatory climate change risk disclosures by the NAIC in March 2009.
- The adoption of mandatory reporting of GHG emissions by the EPA, which the EPA estimates will draw data from approximately 13,000 facilities estimated to cover 85-90% of total U.S. GHG emissions. Specified sources must begin monitoring their GHG emissions in January 2010, and submit their first annual report on March 31, 2011[16].
- The decision of the 2nd Circuit in *Connecticut v. American Electric Power Co.* to allow a common law nuisance suit to proceed against a number of electric utility companies, which has been predicted to release a flood of similar litigation[17].

The conclusion for all public companies is that they should look closely at their disclosures, disclosure policies and procedures, regarding GHG and climate change matters.

For the vast majority of public companies that provide no GHG or climate change-related disclosure in their SEC reports, 2010 will be an important opportunity to reevaluate this situation. Each company that does not currently provide GHG or climate change disclosure will need to carefully evaluate whether that is a reasonable approach given the kinds of risks, and opportunities, that GHG and climate change issues present.

In particular, companies that make GHG or climate change disclosures in other forums, such as the Carbon Disclosure Project, must carefully evaluate the decision not to make similar disclosures in their SEC filings. Our 2009 review found that the gap between the percentage of S&P 500 companies that provide disclosure to the CDP (66% in 2009) compared to S&P 500 companies that make climate change or GHG disclosures in their 10-Ks (28.9% in 2009) is still wide. We also observed that the number of S&P 500 companies that provide some type of company-specific information regarding climate change or GHG issues on their websites grew from 27.6% in 2008 to 51.4% in 2009, and that the percentage of S&P 500 companies that provide website disclosure but do not provide disclosures in their 10-Ks increased from 18.7% in 2008 to 29.6% in 2009.

For the minority of companies that do include GHG and climate change disclosures in their SEC reports, 2010 will be an important year to reexamine and update those disclosures. While the SEC has not yet responded to calls for interpretive guidance in this area, a clearer picture has emerged regarding the types of disclosures various investors (for example, the CDP) and governmental parties (for example, the New York Attorney General) are requesting/requiring.

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[16] See the McGuireWoods LLP Legal Updates, "EPA Issues Final Greenhouse Gas Reporting Rule," at www.mcguirewoods.com/news-resources/item.asp?item=4257, and "Counting Carbon: Scope and Implications of EPA Green House Gas Registry Rule," at www.mcguirewoods.com/news-resources/item.asp?item=3794.

[17] See McGuireWoods LLP Legal Updates, "2nd Circuit Rejects 'Political Question' Dismissal of Key Climate Change Case" at www.mcguirewoods.com/news%2Dresources/item.asp?item=4252.

For example, public companies should consider their GHG and climate change disclosures for 2010 in light of the settlement agreements entered into by the New York Attorney General with Xcel Energy and Dynegy. Another helpful guidepost would be the request for interpretive guidance filed with the SEC by Ceres and other investors. Neither of these sources is binding on public companies, but they do provide helpful information regarding the types of disclosures that may be appropriate in this area.

Another player in this arena to monitor closely is the SEC's newly formed Investor Advisory Committee. The mandate of this committee is to be the SEC's eyes and ears in the investor community, and to advise the SEC on matters of interest to investors. Questions related to climate change disclosure practices were considered at the committee's first meeting this past July; and at least one SEC Commissioner, Elisse Walter, has indicated that she is listening carefully to calls for SEC guidance on this topic.

Recognizing that pressure is increasing for public companies to make GHG and climate change disclosures in their SEC reports does not make preparing those disclosures any easier. Many difficult issues arise when evaluating potential disclosure in these areas. For example, when considering risks related to the physical effects of climate change, difficult questions arise regarding the likelihood of the risk and the relevant time frame over which the risk may manifest itself. Until tangible effects begin to manifest themselves with respect to particular companies or geographic locations, or are far more imminent than they appear to be in much of the world today, the initial test for materiality (that is, whether the contingency is reasonably likely to occur) may not be met, leading to the conclusion that no disclosures are required.

On the other hand, if potential physical effects of climate changes are influencing management's decisions in any material respect, for example, regarding material capital expenditures or plant locations, that information should be disclosed to investors. In addition, it appears that some important public policy decision makers or influencers, including the Department of Defense and the United Nations, are beginning to make explicit references to the physical effects of climate change as a factor that must be considered in planning for the future.

Apart from disclosures that should be considered for formal SEC reports, there are other securities laws issues to take into account when informal GHG or climate change disclosures are made. The increasing number of public companies that provide GHG or climate change information to specific investors or groups of investors, including via their corporate websites, should examine whether the information being provided is subject to the same disclosure controls and procedures that apply to information included in their SEC filings. A company's message regarding GHG and climate change matters should be consistent across all disclosure channels and discussions of the related risks, and opportunities should be subject to consistent disclosure controls and procedures.

Disclosure controls processes generally call for review of peer practices, as well as consideration of any consensus developing among regulators, investors and disclosure professionals regarding materiality and the scope of the disclosure of included topics. Because climate change is a topic often addressed in forums in addition to, or other than, formal SEC reports, disclosure committees also would do well to inform themselves about statements their companies are making about climate change outside the context of formal disclosure, in order to be sure that the company's statements are consistent. Review of similar non-SEC disclosures by peers may also be appropriate.

Sending different messages to different audiences regarding the risks or opportunities presented by GHG and climate change issues, can at a minimum create an inconsistent and confusing mix of information for Rule 10b-5 purposes, and depending on the circumstances of the disclosure, may result in violations of the prohibition of selective disclosure under Regulation FD.

Another challenge posed by GHG and climate change matters is the substantive agenda motivating the calls for disclosure. It is clear that in many cases demands for "disclosure" in this arena are in reality attempts to affect corporate conduct and governance. For example, it appears that the governance and compensation-related disclosures mandated by the New York Attorney General have caused the utility companies entering those settlements to implement changes in the role of the board of directors in GHG and climate change matters. Those "disclosure" requirements also may have prompted some utility companies to consider environmental performance factors, including meeting climate change objectives, as a factor in setting executive compensation.

Despite the difficulties inherent in providing meaningful, company-specific GHG and climate change disclosures, the number of public companies that made GHG and climate change disclosures in their SEC reports increased in 2009, and we expect that trend to continue in 2010.

The fact that an increasing number of public companies are already making some type of voluntary GHG or climate change disclosure lends some urgency to this issue. It will become more difficult for companies to maintain a disparity going forward regarding the information they provide to various audiences. This issue will be particularly acute for companies who access the capital markets or engage in mergers and acquisitions in 2010, since underwriters, potential acquirors and their counsel are increasingly addressing these issues during due diligence.

If the decision is made to make these types of disclosures in connection with capital raising activities or business combinations, it will become even more difficult to justify omitting similar disclosures in a company's periodic reports filed with the SEC.