

SEC's Upcoming Proposed Rule for Climate Disclosures: Will It Be as "Decision-Useful" as the Ingredients Label for "Fat-Free Milk"?

Publications

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The Securities and Exchange Commission ("SEC") is meeting this Monday, March 21, to determine whether to propose amendments to existing law to "enhance and standardize registrants' climate-related disclosures." The SEC's expected proposed rule is more than a decade in the making and would be the SEC's most visible step yet to pursue disclosure improvements related to Climate and ESG issues. While speculation on what the SEC will announce runs rampant, the SEC itself has given a few clues as to what to expect. This article traces the history of the SEC's focus on climate related disclosures and highlights the most important recent developments that could highlight a possible approach. As detailed below, the SEC's goal is to making disclosures "consistent," "comparable" and "decision-useful."

The 2010 Guidance

In early 2010, the SEC issued "Guidance Regarding Disclosure Related to Climate Change." This interpretive release advised companies of the "existing disclosure requirements" with respect to climate change. The guidance noted that while there were increasing legislative and executive actions with respect to climate, a registrant would be required to file would be governed existing rules and law. With respect to climate-related impacts, companies would be required to disclose "such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading." The SEC recommended that companies consider the positive and negative impacts of US and international legislation, regulation, and accords and other legal, technological, political and scientific developments, as well as the physical impacts of climate change, such as severe weather events. The guidance concluded by referring further evaluation of this issue to the SEC's Investor Advisory Committee.

Democratic Commissioners Call for Climate-Related Disclosure in 2019

The issue of mandated climate-related disclosures remained primarily on the sidelines until the two democratic commissioners, Robert J. Jackson Jr. and Allison Herren Lee, raised the issue in 2019. When the Commission as a whole proposed revisions to Regulation S-K (which requires disclosure of specific material, qualitative material) without addressing climate change, Jackson and Lee issued a statement making their views clear. The statement decried the revised amendment's "absence of

[guidance] on the topic of climate risk.” They concluded that “what is clear is that investors of all kinds view [climate] risk as an important factor in their decision-making process, and that “research shows that we are long past the point of being unable to meaningfully measure a company’s sustainability profile.”

The SEC’s Early 2021 Emphasis on Climate and ESG Issues

After becoming Acting Chair in January 2021, Lee continued to proactively seek additional climate-related disclosures. In February 2021, she directed the SEC staff to review climate-related disclosures, and then in March 2021, she announced a Climate and ESG Task Force as part of the Division of Enforcement to focus on material misstatements or omissions relating to climate risk disclosures, and “beyond climate,” on the “the broader array of ESG disclosure issues.” On March 15, 2021, Acting SEC Chair Lee issued a formal request for public comment on a potential rule, with fifteen “Questions for Consideration,” and soliciting comments on how the SEC can “best regulate climate change disclosure.”

Recent Developments Highlighting Possible Approach

The SEC’s request for comments generated over 6,000 comments (including many form letters that were re-submitted). In initial response to the public input, SEC Chair Gary Gensler stressed, in July 2021 and again in September 2021 and December 2021, that climate risk disclosures must be “consistent,” “comparable,” and “decision-useful,” including providing sufficient detail that the investor understands the bases for a company’s disclosure and for investment funds describing themselves as “sustainable” or “green.”

In September 2021, SEC staff in its Division of Corporation Finance published a sample letter that companies may receive based on existing rules and the 2010 Climate Change guidance. This letter would ask the receiving company to explain the lack of climate-related disclosure issues, such as:

1. An explanation as to why the company provided a “more expansive disclosure in its corporate responsibility report” than in its SEC filings.
2. The material effects of transition risks related to climate change.
3. The effects of significant developments in international accords and federal and state legislation and regulation on the business.
4. To the extent material, the indirect consequences of climate-related regulation or business trends.
5. The material effect of physical effects of climate change, including severe weather and fires and water availability.
6. The material effect of purchase or sale of carbon credits or offsets.

Most recently and perhaps most tellingly, Chairman Gensler’s March 3, 2022 appearance on his “Office Hours” YouTube video, explained that he wants investors to understand and be able to compare ESG disclosures as easily as a consumer in a grocery store can understand and compare the ingredients in different brands of fat-free milk. While over-simplifying the issues, the Office Hours video demonstrates that the Chairman is committed to his basic goal of “consistent,” “comparable,” and “decision-useful” disclosures regarding climate impacts. The March 21, 2022 meeting will demonstrate how close he came to these high aspirations.

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