ESG reporting and attestation: A roadmap for audit practitioners

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Purpose

The building blocks of reliable, comparable and relevant environmental, social, and governance (ESG) information begin with a foundation of quality reporting by company management.

The American Institute of CPAs and Center for Audit Quality have teamed up to provide audit practitioners (hereinafter referred to as practitioners) with an overview of ESG reporting and the related risk and legal considerations associated with a company's decision to report ESG information in SEC submissions and engage an independent accounting firm to perform an attestation engagement related to such information.

In this relatively new landscape of ESG reporting, companies are wrestling with what ESG information to report and where and how to communicate it to stakeholders. Company reporting must be of high quality for investors and other stakeholders, who rely upon such data for their decisions. Independent auditors, in their public interest role, play a part in the flow of reliable information for decision making. Third-party assurance from an independent accounting firm can enhance the reliability of ESG information reported by companies, in a manner similar to the process that occurs with audits of financial statements and internal control over financial reporting.

The purpose of this roadmap is to assist practitioners in supporting companies with their ESG reporting goals. This roadmap can aid practitioners when they discuss with companies questions surrounding:

1. where and how to report ESG information (e.g., in an SEC submission),

2. whether to engage an independent accounting firm to perform an attestation engagement on the ESG information, and

3. where to include the attestation report or reference such report.

This resource is general in nature. It is not intended to be a definitive or all-inclusive list of risk, accounting, and legal considerations; it is not intended to serve as legal advice. It should be read in conjunction with other applicable rules, laws, and regulations; practitioners should seek legal counsel to advise as appropriate.

Background and overview

WHAT IS ESG REPORTING?

ESG reporting may include both qualitative discussions and quantitative metrics, such as measures of a company's performance against ESG risks, opportunities, and related strategies. The terms *ESG*, *sustainability*, and *corporate social responsibility* (*CSR*) often are used interchangeably to describe ESG reporting. For purposes of this resource, when we describe ESG reporting we are also referring to these terms.

The *E*, or environmental, component of ESG information encompasses how a company is exposed to and manages risks and opportunities related to climate, natural resource scarcity, pollution, waste, and other environmental factors, as well as a company's impact on the environment.[1]

The *S*, or social, component of ESG comprises information about the company's values and business relationships. For example, social topics include labor and supply-chain information, product quality and safety, human capital topics such as, employee health and safety, and diversity and inclusion policies and efforts.[2]

The *G*, or governance, component of ESG encompasses information about a company's corporate governance. This could include information on the structure and diversity of the board of directors; executive compensation; critical event responsiveness; corporate resiliency; and policies and practices on lobbying, political contributions, and bribery and corruption.[3]

1 See AICPA's Guide: *Attestation Engagements on Sustainability Information (Including Greenhouse Gas Emissions)* (AICPA sustainability attestation guide) for a more detailed listing of the information within that encompasses the E, S, and G.

2 Ibid.

3 Ibid.

Some narrowly associate ESG solely with climate change, such as a company's carbon footprint or greenhouse gas (GHG) emissions. Although climate change is part of the environmental component of ESG information—and has received significant market attention and has interdependencies with other ESG elements—it is one element with multiple dimensions under the broader ESG umbrella. Through ESG reporting, companies that effectively integrate ESG considerations into their business strategy and risk management practices can communicate how such considerations affect their business and are relevant to their stakeholders.

Companies report ESG information for many reasons. For example, ESG reporting can enable companies to:

+ communicate key ESG risks and opportunities and how they are managed;
+ relay progress on the company's commitments to the environment and society;
+ credibly demonstrate how the company's ESG strategy drives value for all stakeholders; and
+ increase confidence in how leadership is prioritizing and advancing ESG commitments.

WHAT IS DRIVING THE EXPANSION OF ESG REPORTING?

Companies have turned to ESG reporting as a way to meet the information needs of their stakeholders and to provide transparency about their commitments to identify, manage, and report on ESG risks. With most of the world's top 10 global risks (both by impact and likelihood)[4] as listed by the World Economic Forum (WEF) qualifying as ESG matters, it has never been more important to manage these risks.

There are many signs that ESG issues are growing in importance to companies, investors, and other stakeholders, for example:

+ Investors are looking for better management of, and greater transparency into, ESG matters – as demonstrated by separate letters from the CEOs of BlackRock and State Street Global Advisors (SSGA), announcing the importance of sustainability to their investment strategies, to investee company CEOs and Boards in 2020 – announcing the importance of sustainability to their investment strategies.
+ The Investment Company Institute Board called for enhanced ESG disclosure by public companies.[5]
+ Asset flows into sustainable funds in the United States continued at a record pace through the third quarter of 2020 to nearly $31 billion, $9 billion higher than asset flows attracted to sustainable funds in all of 2019, according to Morningstar.[6] Companies are increasingly reporting ESG information on a voluntary basis to help satisfy investor inquiries and provide greater insight into a company's enterprise value.

WHAT DOES THE CURRENT ESG REPORTING AND ASSURANCE LANDSCAPE LOOK LIKE?

In 2019, 90 percent of the S&P 500 companies voluntarily published sustainability reports,[7] which are designed to communicate performance on ESG matters. Companies use a variety of sustainability reporting frameworks and standards, including the Global Reporting Initiative (GRI) Standards, the Sustainability Accounting Standards Board (SASB), and the Task Force on Climate-related Financial Disclosure (TCFD) recommendations. Reporting frameworks provide principles-based guidance to help companies identify ESG topics to cover and determine *how* to structure and prepare the ESG information they disclose. Reporting standards provide specific and detailed requirements to assist companies in determining *what* specific information (i.e. both qualitative and quantitative) to disclose for each topic. (see appendix 1 for a high-level overview of common sustainability reporting frameworks and standards). ESG information is reported via different

4 See https://reports.weforum.org/global-risks-report-2020/chapter-one-risks-landscape/.
5 See https://www.ici.org/pressroom/news/20_news_esg.
6 See https://www.morningstar.com/content/dam/marketing/shared/pdfs/Research/Global_Sustainable_Fund_Flows_Q3_2020.pdf?utm_source=eloqua&utm_medium=email&utm_campaign=&utm_content=25660.
7 See https://www.ga-institute.com/research-reports/flash-reports/2020-sp-500-flash-report.html.

channels or disclosure mechanisms, which have largely included company websites and a variety of reports ranging from sustainability reports to integrated reports.[8]

Users of ESG information, including investors and other stakeholders, are seeking transparency about ESG initiatives, and also demanding high-quality, accurate, reliable information. Assurance engagements with respect to reported ESG information are intended to facilitate these goals. In 2019, 29 percent of S&P 500 companies subjected some or all of their sustainability information to some sort of third-party assurance.[9] This third-party assurance ranged from review or examination level attestation from an independent accounting firm to verification or certification services from engineering and consulting firms.

A review or examination level attestation from an independent accounting firm results in the issuance of an independent accountant's report that is designed to enhance the reliability of that information for the intended users of that attestation report by expressing a conclusion or opinion on that information (e.g., management assertions, data, and other disclosures made by management). Independent accounting firms adhere to robust requirements for independence, firm system of quality control, and subject matter competency. Obtaining any level of assurance by practitioners involves the evaluation of processes, systems, and data, as appropriate, and then evaluating the evidence obtained and the results of the procedures in order to form a conclusion in a review engagement or an opinion in an examination engagement.

HOW AND WHY IS ESG REPORTING BEING INCLUDED IN SEC SUBMISSIONS?

Sustainability reporting has historically taken place outside of SEC submissions. However, there is increasing interest by investors and others in disclosure of ESG information in SEC submissions (including proxy statements, annual reports, and quarterly reports). As noted above, there is growing appreciation of the value in having some or all of the information in said disclosures being subject to external attestation in accordance with attestation standards (e.g., AICPA attestation standards) by an independent practitioner.

To date, two domestic registrants and several Foreign Private Issuers have included, or referred to, an attestation report in their SEC submissions:

+ Vornado Realty Trust has presented its ESG information in a stand-alone Environmental, Social, & Governance report,[10] which includes both an independent accountants' examination report and an independent accountants' review report. In Vornado's case, the accounting firm performed an examination engagement over the specified metrics presented in accordance with SASB Standards and a review engagement over the sustainability disclosures in the GRI index in accordance with GRI Standards. The independent accountants' examination report states that the accounting firm performed an examination, using the attestation standards of the AICPA, of management's assertion that the specified metrics are presented in accordance with the SASB Real Estate sustainability accounting standard. The examination report states that, in the independent accountants' opinion, management's assertion is fairly presented in all material respects. The review report states that the accountants performed a review, using the attestation standards of the AICPA, of management's assertion that the sustainability disclosures in the Global Reporting Initiative Index are presented in accordance with GRI Standards – Core option and that, based on the review, the independent accountant is not aware of any material modifications that should be made to management's assertion. Vornado's 2019 ESG report, including the independent accountants' examination report and independent accountants' review report, were furnished to the SEC in a Form 8-K.

8 See appendix 1 for a high-level overview of Integrated Reporting.

9 See https://www.ga-institute.com/research-reports/flash-reports/2020-sp-500-flash-report.html.

10 See Vornado's 2019 ESG report.

- Etsy, Inc. included ESG information in the Risk Factors section of its Annual Report on Form 10-K for 2019.[11] The Form 10-K indicated the ESG metrics over which an external third party performed attestation procedures. There is a separate report of independent accountants outside of the Form 10-K,[12] which includes management's assertion related to the specific sustainability metrics on which the independent accounting firm performed a review, as well as the definition of the metric and assessment criteria in determining the metric. That separate report states that, based on the review, the independent accountants were not aware of any material modifications that should be made to management's assertion.

- UBS Group AG, a foreign private issuer, provided a *Sustainability Report 2019* in its Form 6-K furnished to the SEC. on March 5, 2020. The report included an independent assurance report stating that the practitioner performed a limited assurance engagement (i.e., the international equivalent of a review engagement) on the information disclosed as part of the sustainability reporting as required by local jurisdiction. The report also stated that the limited assurance engagement was conducted in accordance with International Standard on Assurance Engagements 3000 and included a summary of work performed and a conclusion.

CAN A COMPANY USE THE SAME INDEPENDENT ACCOUNTING FIRM FOR ITS FINANCIAL STATEMENT AUDIT AND ATTESTATION OVER ITS ESG INFORMATION?

Yes, performing a review or examination engagement of a company's ESG information would be considered a permissible service for the independent accounting firm performing the financial statement audit, subject to pre-approval from the audit committee. The performance of review or examination attestation services by an independent accounting firm requires that firm to meet certain independence requirements. In the examples above, the practitioners reporting on ESG information were from the same independent accounting firm that provided audit opinions on the financial statements. However, the work also could be done by another independent accounting firm.

Market and regulatory developments are driving the trend toward providing ESG information in SEC submissions. For example:

- The TCFD recommendations call for preparers of climate-related financial disclosures to provide such disclosures in their mainstream (i.e., public financial) filings. Since 2017, more than 1,340 companies,[13] representing a market capitalization of over $12 trillion, have committed to implementing the TCFD recommendations over a period of five years. Additionally, various jurisdictions have mandated reporting in accordance with the TCFD recommendations.

- The WEF International Business Council (IBC) report[14] calls for disclosure of specified ESG metrics in mainstream financial filings.

Further, in-progress developments that could drive additional ESG-related disclosures in public filings include:

- The SEC adopted amendments to Regulation S-K.[15] One of the key amendments involved revisions to the rules for the Description of Business to more broadly embrace a principles-based standard identifying a list of non-exclusive topics that may be addressed if material. A "description of registrant's human capital resources" is one of the topics included in the amendments.

11 See Etsy, Inc.'s Form 10-K.
12 See Report of Independent Accountants related to certain of Etsy, Inc.'s sustainability metrics.
13 See https://www.fsb.org/2020/10/2020-status-report-task-force-on-climate-related-financial-disclosures/.
14 See http://www3.weforum.org/docs/WEF_IBC_Measuring_Stakeholder_Capitalism_Report_2020.pdf.
15 See https://www.sec.gov/rules/final/2020/33-10825.pdf.

- The SEC Investor Advisory Committee's report encouraged the SEC to develop a framework for ESG reporting in SEC submissions.[16]
- The ESG Subcommittee update report to the SEC Asset Management Advisory Committee recommended the SEC should: require the adoption of standards by which corporate issuers disclose material ESG risks, utilize standard setters' frameworks to require the disclosure of material ESG risks; and require that material ESG risks be disclosed in a manner consistent with the presentation of other financial disclosures.[17]
- The International Organization of Securities Commissions (IOSCO) established a board-level Task Force on Sustainable Finance in an effort to explore the role of securities regulators in sustainable finance. According to a speech given by Paul Andrews, IOSCO's Secretary General, this group will work to translate the different standards from around the world into a more cohesive, more transparent, and more standardized system.[18]
- The International Financial Reporting Standards Foundation Trustees issued a consultation paper to assess the demand for global sustainability standards.[19]
- The European Commission's upcoming revisions to the EU Non-Financial Reporting Directive could—based on consultation responses received—expand the scope of the directive to more companies and could require additional disclosures of (and assurance engagements over) ESG matters in annual reports.[20]

16 See https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

17 See https://www.sec.gov/files/update-from-esg-subcommittee-12012020.pdf.

18 See https://www.ft.com/content/4d7accf7-5431-4ebb-a528-87db3cca1eb7.

19 See https://cdn.ifrs.org/-/media/project/sustainability-reporting/consultation-paper-on-sustainability-reporting.pdf?la=en.

20 See https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Revision-of-Non-Financial-Reporting-Directive/public-consultation.

Practitioner risk and legal considerations

As with any attestation engagement, practitioners should consider the risk and legal considerations relevant to providing attestation services on ESG information, particularly when such information will be included in an SEC submission. The AICPA Attestation Standards[21] in particular lay out several preconditions that should be met before accepting or continuing an engagement. These attestation standards and related guidance, such as the AICPA sustainability attestation guide, establish protocols for practitioners to consider when accepting an ESG attestation engagement.[22]

Practitioners' internal risk management, legal, and independence resources likely will need to be consulted during client acceptance and thereafter on an ongoing basis as part of evaluating how to structure, execute, and report on ESG matters.

AICPA Quality Control Standards (QC Standards) require independent auditors to evaluate whether to accept or continue a client relationship and whether to perform a specific engagement for that client. The QC Standards require that the firm establish policies and procedures to provide reasonable assurance that the firm:

+ minimizes the likelihood of association with a client whose management lacks integrity;
+ undertakes only those engagements that the firm can reasonably expect to be completed with professional competence; and
+ appropriately considers the risks associated with providing professional services in the circumstances.

Important decision attributes include, but are not limited to, (a) what information will fall within the scope of the attestation engagement (the subject matter); (b) what reporting criteria will the subject

21 See https://www.aicpa.org/research/standards/auditattest/ssae.html.

22 See SSAE No. 18, *Attestation Standards: Clarification and Recodification*, AT-C section 105, *Concepts Common to All Attestation Engagements*, as amended by SSAE Nos. 19 and 21 (AICPA, *Professional Standards*, AT-C sec. 105).

matter be measured against (e.g., GRI, SASB, company developed); (c) what level of attestation service will be provided (examination engagement, review engagement); and (d) how will the ESG information and attestation report be disclosed and used?

What information will be in the scope of the attestation engagement? As illustrated in the examples on pages 5 and 6, some companies may choose to have an attestation engagement performed over their entire sustainability report, others may elect to cover only select metrics or disclosures (e.g., GHG emissions). The scope of the attestation engagement is determined by management but will affect the practitioner's risk management considerations.

+ The practitioner's assessment of the appropriateness of the scope of the attestation engagement will be informed by consideration of required evidence, management's objectives in presenting specified information, management's determination of the materiality of that information, the messages the company is trying to communicate, the needs and expectations of the intended users and other factors.

+ The practitioner also is required to consider whether they will be able to obtain sufficient and appropriate evidence to achieve the intended level of assurance. Factors to consider could include the nature of the disclosure(s), the nature and sophistication of management's processes and controls of how they create the necessary information for the disclosures, and the report itself, among other factors.

What reporting criteria will the subject matter be measured against? Before an attestation engagement can be accepted, the practitioner is required to determine that the criteria applied in the preparation and evaluation of the subject matter are suitable and will be available.[23] Certain companies will prepare ESG information in accordance with sustainability reporting standards or frameworks (e.g., SASB, GRI, TCFD), while others will use company-developed or custom metrics that may or may not use existing standards as a starting point. The practitioner is required to assess if the criteria selected by the responsible party (i.e., the company) meets the attributes of suitability.

The criteria used by companies to report ESG information can be broadly classified into sustainability reporting standards or frameworks (e.g., SASB, GRI, TCFD) and company-developed or custom metrics.

+ ***Sustainability reporting standards or frameworks:*** Investors increasingly are expecting information to be presented in accordance with existing frameworks and standards. For example, large institutional investors such as BlackRock have specifically requested reporting in accordance with SASB and TCFD recommendations. Even when a company uses these recognized standards, the practitioner is still required to determine that the selected metrics are prepared in accordance with suitable and available criteria.

  Frameworks provide principles-based guidance that helps companies identify ESG topics to cover and determine how to structure and prepare the ESG information they disclose. Standards provide specific and detailed requirements that may assist companies in determining what specific metrics to disclose for each topic.[24] In most situations, the basic description of the criteria must be supplemented with additional details to establish that the criteria are clear enough for an assurance engagement in accordance with AICPA standards. This process involves considering the company's process for accumulating information and what information is available.

+ ***Company-developed or custom metrics:*** Consist of measures that do not conform to, or may diverge from or amend, existing standards and frameworks. Companies may prefer these metrics because they allow them to provide their unique perspective and enhance their disclosure(s) with relevant company-specific information. There can be valid purposes and rationales for why the

23 See AT-C sec. 105.
24 See the CAQ publication, *The Role of Auditors in Company-Prepared ESG Information: Present and Future*.

information is being presented using company-developed metrics. Accordingly, it is important to understand the purpose and rationale for why a company uses its own metrics.

- Company-developed metrics may pose certain challenges, including:
  - The company may have the ability to present more favorable outcomes than might be the case if sustainability reporting standards were used.
  - The evaluation of the suitability and availability of the criteria may be more challenging than if existing reporting standards and frameworks were used.
  - A company-defined metric may reflect only a small deviation from a metric defined by a sustainability reporting standard or framework, which may lead to questions as to why the sustainability reporting standard or framework was not used.
- These challenges may be mitigated by:
  - using the same methodology across periods;
  - providing disclosure and clarity about how the company-developed or custom metrics were selected; and
  - explaining that the metrics are not fully comparable with other existing standards or frameworks or similarly titled metrics used by other companies.[25]

Where necessary, the practitioner can advise the responsible party on the applicable requirements of the criteria and related considerations regarding adherence to the criteria. The practitioner also might advise the responsible party about how to satisfy the conditions of suitable criteria, subject to compliance with any applicable independence rules.

What level of attestation service will be obtained?[26]
Management will determine the level of attestation service it will request from the practitioner (e.g., whether a review or examination engagement will be performed) and base this decision on various factors, including management's objectives in presenting the information, management's determination of the materiality of the information, the company's intended messaging with stakeholders and the needs and expectations of users.

- The objectives of an **examination engagement** are to obtain reasonable assurance (a high but not absolute level of assurance) and express an opinion about whether the ESG information is in accordance with the criteria, in all material respects. A practitioner obtains the same level of assurance in an examination engagement as the practitioner does in a financial statement audit; accordingly, there may be less risk of users of the information misunderstanding the level of assurance, than in a review engagement where the practitioner obtains limited assurance. Where and how the ESG information will be disclosed also may influence the level of assurance the company obtains on the information. As a practitioner is evaluating the level of assurance, they should consider the perspective of the users of the report, usefulness to investors, and risk management.
- The objective of a **review engagement** is to obtain limited assurance and express a conclusion about whether the practitioner is aware of any material modifications that should be made to the ESG information in order for it to be in accordance with the criteria. Review engagements are substantially less in scope than an examination engagement that result in a meaningful but lower level of assurance. Management may determine a review level engagement is sufficient when the information will not be in a document filed with the SEC (e.g., company website).

25 Also see the SEC's *Commission Guidance on Management's Discussion and Analysis of Financial Condition and Results of Operations* which provides guidance on key performance indicators and metrics in the MD&A.
26 Also see Appendix 2 for AICPA sustainability attestation resources for practitioners.

+ A practitioner can assist the responsible party in understanding the requirements for each level of assurance and other considerations, including whether:
  - a review or examination will meet the objectives of the intended users; and
  - users will not understand the difference between examination and review engagements, and consequently, place greater reliance on a review engagement than is warranted.
+ Additional factors affecting the level of attestation service that company management seeks from the practitioner would include the nature of the intended users and the significance of the information to them.
  - An examination level engagement may be more appropriate than a review level engagement when ESG disclosures are being used for investment decision making.
  - An examination level engagement may be more appropriate for SASB metrics designed to meet investor needs.

If the responsible party determines that an attestation engagement is appropriate for their circumstances, the practitioner may want to consider whether a readiness engagement under the AICPA's Consulting Standards[27] makes sense in advance of the examination or review engagement. This could help identify in advance where preparers may need to refine or bolster disclosure controls and procedures or the criteria.

How will the ESG information and attestation report be disclosed and used? False or misleading statements can subject companies and practitioners to liability under federal securities laws, even if the information is not included in an SEC submission (e.g., different sections of the Form 10-K [Item 1 (Business), MD&A etc.], Form 8-K, proxy statement). Information included in an SEC submission will become subject to greater scrutiny from the SEC and users. Attestation can help identify issues in these statements before the information is made available for general use and reliance.

Practitioners should work with their internal risk management resources and legal counsel to determine whether and, if so, how assurance on ESG information provided in an SEC submission should be described or referenced. In particular, practitioners should consider whether disclosure will result in them being deemed an "expert" with respect to the information provided, with resulting liability – see pages 12 to 15 in this paper on Federal Securities Liability for more information.

OTHER REPORTING-RELATED MATTERS THAT MAY AFFECT PRACTITIONER RISK AND LEGAL CONSIDERATIONS

Is the ESG reporting consistent year over year? Consistent reporting that uses the same methodology year over year, with any changes clearly explained, could help to limit a company's ability to selectively choose, manipulate, or provide misleading information. Reported information that includes comparable prior year information also could limit a company's ability to selectively choose, manipulate, or provide misleading information.

Is the ESG reporting comparable with peer companies? Information and metrics that are comparable to the metrics and information disclosed by peer companies could assist users of the information in making comparisons between peer companies.

How to mitigate companies from selectively choosing the most beneficial metrics? The practitioner should evaluate whether the reported information is misleading within the context of the engagement, as required by AICPA standards (e.g., could be viewed as 'cherry-picking' favorable metrics).

Is the frequency and timing of ESG reporting sufficient and appropriate? Information reported on an annual (or more frequent) basis, similar to other forms of corporate reporting (i.e., the financial statements), promotes consistency and comparability.

27 See *Statement on Standards for Consulting Services No. 1*.

Reporting old or stale information could suggest that there may be certain deficiencies in a company's process and could potentially call into question the sufficiency or appropriateness of the reporting processes and related controls.

Are there appropriate governance and controls over the ESG reporting process? The preparation of ESG information generally does not fall under a company's system of internal control over financial reporting (ICFR). Disclosure controls and procedures (DCPs) are more broadly defined by the SEC and pertain to all information required to be disclosed by a company. ESG information disclosed in SEC submissions could become subject to DCPs. Establishing good governance, policies, and controls over the reporting process can enhance the rigor involved in the collection and reporting of ESG information. For example, consider whether:

+ defined roles and responsibilities with oversight for subject matter data owners exist;
+ subject matter data policy and procedures, including, but not limited to, reporting frequency, measurement, data aggregation and error evaluation methodologies exist and are documented;
+ controls are in place to collect data; and
+ there is Board oversight over the disclosure of ESG information, particularly disclosure in SEC submissions;[28] input on the level of assurance desired; and, after ESG information has been disclosed, the review of such information and the controls that are in place for timely and accurate reporting.

Without taking on the role of management in designing controls, the practitioner may advise the responsible party about the sufficiency of the client's governance structure and disclosure controls over the ESG reporting process.

For a discussion of key actions that a company can take to establish effective governance over its reported ESG information, please see Appendix 3.

CONSIDERATIONS OF WHERE TO REPORT ESG INFORMATION AND RELATED ATTESTATION REPORT

How does materiality affect whether ESG impacts should be disclosed? Consider if ESG reporting is material to the company and consider the nature and extent of ESG disclosures in SEC reports. Materiality for qualitative subject matters is often more challenging than for quantitative subject matters.

Public companies should consider whether ESG matters are material for SEC reporting purposes, and as a result, whether such matters warrant disclosure in their SEC submissions.

In addition, public companies may need to consider the disclosure obligations and liability that may arise under state securities laws, federal and state consumer protection laws, class action cases, state and municipal attorney general suits, and state law investor claims for books and records information.

What federal laws should practitioners keep in mind? Disclosure of ESG information (including the related attestation report) in SEC submissions subjects the information to various federal laws, as summarized below. Such information, if untrue, incomplete or misleading, may subject companies and potentially practitioners to significant liability under federal securities laws.

In considering federal securities law risks implicated by publication of an attestation report on ESG information, there are four principal methods by which such an attestation report might be disclosed:

+ Publicly by the company through other means outside of an SEC submission (e.g., posted on a corporate website).
+ Furnished, but not deemed "filed" for purposes of the Exchange Act (e.g., furnished as an exhibit to Form 8-K under Item 7.01, for Regulation FD information).

28 Note that disclosure in an SEC report would subject it to disclosure controls and procedures under SOX 302 and require CEO and CFO certification.

- In a periodic or current report filed under the Exchange Act, where the filing is not incorporated by reference into a registration statement).
- In a registration statement filed with the SEC under the Securities Act or incorporated into a registration statement from a periodic or current report filed under the Exchange Act.

Federal securities laws and regulations may provide investors an actionable claim against companies and potentially practitioners for material misstatements or omissions. For example:

- *Section 10(b) and Rule 10b-5* – Liability under Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder has the broadest application of potential liability for ESG disclosures, creating exposure for material misstatements and omissions in any SEC submission or potentially any other disclosure made by a public company. Rule 10b-5 provides that it is unlawful to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made not misleading.[29] The most common way that plaintiffs seek to establish liability under Section 10(b) is by alleging that the defendant made a *material* misstatement or omission. For these purposes, courts have indicated that a fact is material if "there is a substantial likelihood that a reasonable shareholder would consider it important" in making an investment decision. In determining materiality, the ESG disclosure will not be viewed in a vacuum; the question will be whether correct disclosure "significantly altered the 'total mix'" of available information. A similar SEC rule applies to materially untrue or misleading statements in proxy statements.
- *Securities Act Liability* – Under Sections 11 and 12(a)(2) of the Securities Act of 1933, companies may be strictly liable for material misstatements made in connection with securities offerings, like statements in registration statements and prospectuses. For example, Section 11 of the Securities Act imposes liability if any part of a registration statement, at the time it became effective, "contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading." Scienter is not required to establish liability under this provision. Section 11 liability only covers statements made in a registration statement (which would include an assurance report included or incorporated by reference in a registration statement). Note that an attestation report included in a periodic or current report filed under the Exchange Act will often be incorporated by reference into a registration statement and therefore may provide a basis for Section 11 liability. There may be potential defenses from this strict liability standard for statements of opinion included in attestation reports.
- *Control Person Liability* – "Control persons," such as public company CEOs and CFOs, could face liability under Section 20(a) of the Exchange Act if the public company's ESG disclosures included or hyperlinked in its submissions are not accurate.
- *Hyperlinked ESG Information* – Additionally, information incorporated by reference or hyperlinked (including attestation reports) in a public company's SEC submissions may be treated the same for purposes of liability as statements made directly in the filing itself. SEC regulations provide that "an external hyperlink within a filed document . . . will cause the filer to be subject to the civil liability and antifraud provisions of the federal securities laws with reference to the information contained in the linked material."

In addition to the securities laws described above, state law may allow for professional negligence claims against an audit firm. It is the performance of the underlying work that could give rise to a professional negligence claim, rather than the filing or furnishing of a report to the SEC.

29 In addition, a plaintiff must show that: (1) the material misstatement or omission was made with an intent to deceive, manipulate or defraud (that is, with scienter); (2) there is a connection between the material misrepresentation or omission and the plaintiff's purchase or sale of a security; (3) the plaintiff relied on the material misstatement or omission; (4) the plaintiff suffered economic loss; and (5) there is a causal connection between the material misrepresentation or omission and the plaintiff's loss. The SEC need only establish the first and second criteria.

How will the practitioner's report be referenced in an SEC submission? Referring to the fact that an attestation engagement was performed on the ESG information and specifying what was performed, the opinion/conclusion, the level of assurance obtained, and the attestation provider name can provide users with transparency over the attestation report. However, what information about the attestation report is disclosed in the ESG report also can impact the extent of exposure to liability associated with the report.

Practitioners whose reports or engagement will be referred to in a company's public filings (whether the practitioner is named or not) should consider whether they will be subject to liability under the federal securities laws as an "expert." Section 11(a)(4) of the Securities Act of 1933 establishes liability for accountants and other experts who prepare or certify any report used in connection with a registration statement or any part of the registration statement. Liability may arise for statements made directly in a registration statement or incorporated by reference from a company's other SEC filings, including Form 10-K, Form 10-Q or Form 8-K. Furthermore, Section 7(a) of the Securities Act of 1933 requires any person who is an expert for purposes of Section 11 to file a consent to be named as such.

Whether the SEC will deem someone an expert for purposes of the securities laws depends on multiple factors. For instance, the nature and scope of the person's or entity's report, the extent to which the report or their engagement is referred to in a filing, whether the company contemplated the report for use in the filing and the extent to which the ESG subject matter can be subjected to expert procedures.

Because of the potential for expert liability, practitioners should consider whether the terms of an engagement should explicitly allow or prohibit the engagement or report from being referenced in registration statements and SEC filings incorporated by reference into registration statements. If allowed, practitioners should be aware that the SEC may conclude that the practitioner is an expert and require the filing of both the report and the practitioner's consent to be named an expert in connection with the registration statement.

WHERE ESG INFORMATION AND RELATED ATTESTATION ARE REPORTED

What if the ESG information is disclosed in the proxy statement? There has been a growing trend in companies including ESG disclosures in the proxy statement.[30] Disclosing this information in a proxy statement enables the company to communicate to investors and other stakeholders as part of its broader discussion of governance matters. A practitioner would need to bear in mind the considerations discussed above to the extent any attestation report on the company's ESG information is included or referenced in a proxy statement.

What if the ESG information is disclosed in a Form 8-K? Some companies choose to disclose their ESG information in a Form 8-K. The company can file the information off cycle, if ESG disclosure and the attestation engagement does not line up with annual report or proxy. Including ESG disclosure and the related attestation report as an exhibit in a furnished 8-K under Item 7.01 (Regulation FD Disclosure), provides reduced liability relative to filing in a Form 10-K or filed Form 8-K (specifically, furnished documents are not subject to Section 18 of the 1934 Act; however, such disclosures are still subject to Section 10(b) and Rule 10b-5 liability, among other provisions, and present the same considerations discussed above in relation to expert liability to the extent a company determines to incorporate by reference the Form 8-K in a registration statement).

What if the ESG information is disclosed in a Form 10-K? Companies may disclose ESG information in their Annual Report on Form 10-K, for example, either in Item 1 (Business) or the MD&A. The timing presents challenges for both preparers and auditors to meet the 10-K filing deadline. For example, preparers may have to accelerate reporting and controls processes to meet the 10-K filing deadline. The ESG and financial statement audit teams should coordinate closely as they complete their respective engagements.

30 See *Four ESG Highlights From the 2020 Proxy Season*.

- ***Item 1 (Business)*** - To the extent there is other material information about a company's business (beyond the disclosures required by this item), Item 1 presents a logical place to include ESG information. Item 1 provides factual information and tends not to delve into disclosures about estimates or trends. There may be challenges in distinguishing between ESG disclosures that are historical and forward-looking, and companies may need to carefully update their forward-looking statements and disclaimers.

- ***MD&A*** - The MD&A requires that companies describe known trends, events, and uncertainties that are reasonably likely to have material effects on their financial condition or operating performance. ESG considerations and reporting align with the MD&A concepts of "known trends and uncertainties." However, there could be potential challenges and risks in assessing, and making disclosures about, known trends and uncertainties in relation to ESG issues. In particular, exposure to claims made with the benefit of hindsight about omissions or partial omissions of material information about known trends and uncertainties could arise.

If ESG information and the practitioner's attestation report are disclosed in a Form 10-K, practitioners should carefully consider the level of assurance they will provide, as well as the information on page 14 under "How will the practitioner's report be referenced in an SEC submission."

Conclusion

Because ESG information is increasingly used by the capital markets and other stakeholder groups, such information needs to be reliable, credible, and well supported.

This document is not intended to represent detailed guidance for practitioners; rather, it aims to support continued dialogue among practitioners, companies, and boards of directors to promote leading practices for companies disclosing ESG information and seeking attestation services on such information. This is a rapidly evolving area of reporting; as such, transparent engagement and information sharing among all market participants—preparers, practitioners, investors, and regulators—is important as this reporting continues to take shape.

There is no one-size-fits-all approach to reporting ESG information, but practitioners and company management nevertheless have important roles to play. They can help, through oversight and ongoing dialogue with other key stakeholders, to evolve ESG reporting and attestation practices to meet the needs of stakeholders who use this information for making decisions.

Appendix 1

Overview of key sustainability reporting frameworks and standards[31]

		Intended Use	Benefits	At-a-Glance
Standards: Specific, replicable and detailed requirements for "WHAT" should be reported for each topic	Sustainability Accounting Standards Board (SASB) Standards[32]	Can be used to identify, manage, and communicate financially material sustainability information to investors	Enables companies to report financially material metrics that are industry specific to meet the needs of investors globally and may be used as a basis for suitable criteria in an attestation engagement	Supports presentation of financially material information globally to inform capital allocation decisions
	Global Reporting Initiative (GRI) Standards	Can be used to help businesses understand and communicate the impact of business on critical sustainability issues to a broad range of stakeholders	Enables companies to report the impact of their social and environmental activities to various stakeholders and may be used as a basis for suitable criteria in an attestation engagement	Supports presentation of socially material information that can be tailored to cultures and geographies

31 See CAQ's *The Role of Auditors in Company-Prepared ESG Information: Present and Future.*
32 On November 25, 2020, the IIRC and SASB announced their intention to merge.

		Intended Use	Benefits	At-a-Glance
Frameworks: A set of principles-based guidance for "HOW" information is structured and prepared, and for what broad topics are covered	Task Force on Climate-related Financial Disclosures (TCFD) Recommendations	Focuses on climate-related financial disclosures to help investors and others understand material risks related to climate change	Principles-based recommendations serving as a foundation for global climate-related disclosures	Principles-based recommendations to manage and report on climate risk globally
	Integrated Reporting <IR> Framework	Can be used to explain to providers of financial capital how a company creates value over time by providing relevant information, both financial and non-financial	Promotes integrated thinking and reporting that enables providers of financial capital to understand the business model and how the business strategy drives value in the short, medium, and long term	Principles-based framework that does not prescribe any specific metrics or targets

Appendix 2

AICPA sustainability attestation resources for practitioners

Standards	Attestation engagements over sustainability information performed in accordance with AICPA *Statements on Standards for Attestation Engagements* (SSAEs or attestation standards) must be performed by CPAs. When performing examination engagements, the following sections of the attestation standards apply: + AT-C 105 *Concepts Common to All Attestation Engagements* AND + AT-C 205 *Assertion-Based Examination Engagements* OR + AT-C 206 *Direct Examination Engagements*[33] When performing review engagements, the following sections apply: + AT-C 105 *Concepts Common to All Attestation Engagements* + AT-C 210 *Review Engagements*
Guidance	Given that the attestation standards referred to above can be applied to various subject matters, the AICPA published a guide, *Attestation Engagements on Sustainability Information (Including Greenhouse Gas Emissions Information),* to assist practitioners engaged to perform sustainability attestation engagements. The guidance provides insight into planning, performing and reporting on sustainability attestation-based examination and review engagements in accordance with the AICPA attestation standards. The guide applies to attestation engagements over sustainability information broadly (so it can be applied to sustainability information prepared in accordance with various sustainability reporting standards [e.g., SASB Standards, GRI Standards etc.]).

33 Note that these standards become effective in 2022.

Self-study course	This self-study CPE course, *Sustainability Assurance Engagements*, provides insight into planning, performing and reporting on sustainability examination and review engagements in accordance with the AICPA attestation standards.
Other resources	Various other sustainability-related resources, including a sustainability toolkit can be accessed at: www.aicpa.org/sustainability. These include a sustainability assurance brochure which helps provide insight into assurance engagements and the related benefits. Further, given the sometimes qualitative nature of certain sustainability-related disclosures, the following paper may be useful: *Materiality considerations for attestation engagements involving aspects of subject matters that cannot be quantitatively measured*. The paper helps practitioners consider materiality when planning, performing and reporting in an examination or review engagement when aspects of the subject matter are not quantitatively measurable.

Appendix 3

Key actions for establishing effective governance over ESG reporting

Good governance plays a critical role in a company's ability to produce high-quality, accurate and reliable information. However, ESG initiatives are often managed separately from the rest of the business by functions such as sustainability, marketing, corporate communications, or public relations. As a result, sustainability information is generally prepared separately from the finance function and outside of the financial reporting systems—without the necessary governance and internal controls over the reporting process. The processes are generally very manual, often using spreadsheets and may differ among departments, business units and geographical regions.

To improve the credibility and reliability of sustainability information, effective governance and internal controls are required. The same level of rigor applied to the measurement and reporting of financial information should be applied to sustainability reporting. This precision will lead to greater user confidence in the information and help drive decisions that create value for the business and stakeholders.

The actions described below form part of an iterative process that will help a company to establish effective governance over reported ESG information (to a level that is acceptable for SEC reporting) and allow for continuous improvements over time.

FOR COMPANIES JUST STARTING OUT

Establishing appropriate governance over the reporting of ESG information is a journey. Companies that are just starting out should identify their most material matters to address, begin with them, and grow from there. This process takes time and should be viewed as a journey.

1. Conduct a materiality or risk assessment to determine which ESG topics are important or 'material' to the organization, its investors and other stakeholders.

Conducting a materiality assessment or risk assessment allows a company to identify and prioritize the ESG matters that are most critical to the business, its investors and other stakeholders.

This enables a company to focus its effort on its most critical (or 'material') ESG matters and also helps the company make optimal use of limited company resources. Although various efforts are underway to encourage companies to disclose a minimum set of pre-determined ESG metrics in public financial filings, a company would nevertheless still need to conduct its own materiality or risk assessment to ensure that it is focusing on ESG matters that are considered material to the company, its investors and other stakeholders.

Several existing resources share insights or tools for performing ESG materiality assessments. Certain sustainability reporting standards and frameworks provide considerations for how material matters should be identified when reporting in accordance with those standards and frameworks. During the materiality assessment phase, a company may not yet have decided which reporting standard or framework it plans to report in accordance with, but reviewing the various approaches provided in those standards and frameworks could provide a company with helpful considerations to use as a starting point for establishing its own materiality assessment process. Helpful resources include:

+ Sustainability Accounting Standards Board (SASB) Materiality Map – This map identifies sustainability issues that are likely to affect the financial condition or operating performance of companies within an industry.
+ Global Reporting Initiative (GRI) Standards – The discussion of the materiality reporting principle in *GRI 101: Foundation 2016* provides considerations for the identification and prioritization of material matters.
+ International Integrated Reporting <IR> Framework – The discussion of the guiding principle of materiality in the <IR> Framework sheds light on what "the materiality determination process" may involve.
+ Task Force on Climate-related Financial Disclosures - The Financial Stability Board established the TCFD to develop recommendations for more effective climate-related disclosures that could promote more informed investment, credit, and insurance underwriting decisions and, in turn, enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks.

2. Implement appropriate board oversight of material ESG matters.

As with other critical company matters, board members should be involved in the governance and oversight of material ESG matters. The board has an important role to play in setting the tone and seeing that company ESG efforts are appropriately prioritized. Further, just as boards play a role in providing independent oversight and establishing and maintaining effective governance over financial reporting, boards should assume a similar role in sustainability reporting. This is especially true for ESG matters that will be reported in a company's regulatory filings.

A company can take various steps to strengthen ESG governance at the board level. They include incorporating or making available ESG experience and expertise at the board level, clearly defining ESG-related roles and responsibilities of the board or other committees, ensuring board oversight of the most critical ESG matters, developing ESG-related policies, and implementing regular monitoring of company ESG performance.

Several existing resources offer insights for strengthening board oversight of material ESG matters.

+ ESG Oversight Framework for Directors: Demystifying ESG for Board Members- This SSGA publication includes guidance designed to help boards prioritize ESG within their organizations and is specifically geared toward SSGA investee company boards.
+ Guidance for Applying Enterprise Risk Management (ERM) to Environmental, Social and Governance (ESG)-related Risks-A comprehensive publication by the Committee of Sponsoring Organizations (COSO) and the World Business Council for Sustainable Development (WBCSD) shares guidance designed to help risk management and sustainability practitioners apply ERM concepts and processes to ESG-related risks. The chapter "Governance and culture for ESG-Related Risks" provides numerous insights into board involvement in ESG matters.

+ The Role of Auditors in Company Prepared ESG Information: Present and Future- Although this CAQ publication primarily outlines how investors are using ESG information and the evolving, more prominent role of auditors in advancing the reliability, comparability, and relevance of this reporting, the document also includes a section on ESG Considerations and Questions for Boards.

3. Integrate/align material ESG topics into the enterprise risk management process.

Given the pervasiveness of ESG-related risks and the fact that they constitute most of the world's top 10 global risks,[34] it is essential that these risks be managed as part of a company's overall ERM process - not as separate, standalone risks. Managing ESG risks as part of overall ERM will help ensure that all risks receive the appropriate attention and resources. Further, this will play an important role in reducing the possibility that material ESG-related risks reported in sustainability reports or on a company's website are not omitted from regulatory filings. According to a WBCSD study, which compared WBCSD member company sustainability and risk disclosures, on average only 29 percent of the areas deemed to be "material" in a sustainability report were disclosed in a company's legal disclosure of risks.[35]

A helpful resource that includes comprehensive guidance for incorporating ESG-related risks into broader enterprise risk management is the COSO and WBCSD publication, *Guidance for Applying Enterprise Risk Management (ERM) to Environmental, Social and Governance (ESG)-related Risks*. The guidance is designed to help risk management and sustainability practitioners apply ERM concepts and processes to ESG-related risks.

4. Integrate ESG matters into the overall company strategy.

Incorporating ESG into the overall strategic planning process will enable a company to develop an ESG strategy that is informed by the broader company vision and mission. Similar to integrating material ESG topics into the ERM process, having an integrated strategy will help to further reduce the risk of omission of material ESG-related matters from regulatory filings.

Resources that provide insights for integrating ESG matters into overall company strategy include:

+ *Guidance for Applying Enterprise Risk Management (ERM) to Environmental, Social and Governance (ESG)-Related Risks*- The chapter on *Strategy and objective-setting for ESG-related risks* provides insights for integrating ESG matters into the overall company strategy.

5. Implement effective internal control over the ESG data collection, processing and reporting process.

A company's ability to provide accurate and reliable ESG information to investors and other stakeholders depends, in large part, on the design and effectiveness of the company's internal controls (i.e., the processes, policies and procedures in place regarding measurement and reporting). Applying the same level of rigor to the processes and internal controls for measurement and reporting of ESG information as is applied in financial reporting could help improve internal control over ESG reporting. This is particularly important where ESG information is to be reported in regulatory filings alongside high quality, reliable financial information.

Actions that companies can take to improve internal control over ESG reporting include: setting the tone (see action 2 above), developing and documenting sustainability reporting policies and procedures, developing a data management system, developing and documenting control activities, involving the right functions/resources in the process (e.g., finance, internal audit), and taking steps to monitor policies and processes and make necessary improvements over time.

Leveraging the COSO Internal Control—Integrated Framework to Improve Confidence in Sustainability Performance Data, is a comprehensive resource

34 See https://reports.weforum.org/global-risks-report-2020/chapter-one-risks-landscape/.

35 See https://www.wbcsd.org/Programs/Redefining-Value/Business-Decision-Making/Assess-and-Manage-Performance/Resources/Sustainability-and-enterprise-risk-management-The-first-step-towards-integration.

which includes guidance for applying the COSO *Internal Control—Integrated Framework* to ESG reporting. The publication indicates that SEC registrants already have a control framework in place to evaluate and support assertions regarding the effectiveness of ICFR and that companies likely would find it most effective to leverage the control framework currently used in financial reporting to establish internal control over ESG reporting. The publication explores how this might be done and includes "Key Takeaways from Market Outreach" which shares practical insights gained from more experienced companies regarding leveraging existing expertise and controls, and enabling technologies and platforms to establish and maintain an effective system of internal control over ESG reporting.

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Endnotes

1 See AICPA's Guide: *Attestation Engagements on Sustainability Information (Including Greenhouse Gas Emissions)* (AICPA sustainability attestation guide) for a more detailed listing of the information within that encompasses the E, S, and G.

2 Ibid.

3 Ibid.

4 See https://reports.weforum.org/global-risks-report-2020/chapter-one-risks-landscape/.

5 See https://www.ici.org/pressroom/news/20_news_esg.

6 See https://www.morningstar.com/content/dam/marketing/shared/pdfs/Research/Global_Sustainable_Fund_Flows_Q3_2020.pdf?utm_source=eloqua&utm_medium=email&utm_campaign=&utm_content=25660.

7 See https://www.ga-institute.com/research-reports/flash-reports/2020-sp-500-flash-report.html.

8 See appendix 1 for a high-level overview of Integrated Reporting.

9 See https://www.ga-institute.com/research-reports/flash-reports/2020-sp-500-flash-report.html.

10 See Vornado's 2019 ESG report.

11 See Etsy, Inc.'s Form 10-K.

12 See Report of Independent Accountants related to certain of Etsy, Inc.'s sustainability metrics.

13 See https://www.fsb.org/2020/10/2020-status-report-task-force-on-climate-related-financial-disclosures/.

14 See http://www3.weforum.org/docs/WEF_IBC_Measuring_Stakeholder_Capitalism_Report_2020.pdf.

15 See https://www.sec.gov/rules/final/2020/33-10825.pdf.

16 See https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-of-the-investor-as-owner-subcommittee-on-esg-disclosure.pdf.

17 See https://www.sec.gov/files/update-from-esg-subcommittee-12012020.pdf.

18 See https://www.ft.com/content/4d7accf7-5431-4ebb-a528-87db3cca1eb7.

19 See https://cdn.ifrs.org/-/media/project/sustainability-reporting/consultation-paper-on-sustainability-reporting.pdf?la=en.

20 See https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12129-Revision-of-Non-Financial-Reporting-Directive/public-consultation.

21 See https://www.aicpa.org/research/standards/auditattest/ssae.html.

22 See SSAE No. 18, *Attestation Standards: Clarification and Recodification*, AT-C section 105, *Concepts Common to All Attestation Engagements*, as amended by SSAE Nos. 19 and 21 (AICPA, P*rofessional Standards*, AT-C sec. 105).

23 See AT-C sec. 105.

24 See the CAQ publication, *The Role of Auditors in Company-Prepared ESG Information: Present and Future*.

25 Also see the SEC's *Commission Guidance on Management's Discussion and Analysis of Financial Condition and Results of Operations* which provides guidance on key performance indicators and metrics in the MD&A.

26 Also see Appendix 2 for AICPA sustainability attestation resources for practitioners.

27 See *Statement on Standards for Consulting Services No. 1*.

28 Note that disclosure in an SEC report would subject it to disclosure controls and procedures under SOX 302 and require CEO and CFO certification.

29 In addition, a plaintiff must show that: (1) the material misstatement or omission was made with an intent to deceive, manipulate or defraud (that is, with scienter); (2) there is a connection between the material misrepresentation or omission and the plaintiff's purchase or sale of a security; (3) the plaintiff relied on the material misstatement or omission; (4) the plaintiff suffered economic loss; and (5) there is a causal connection between the material misrepresentation or omission and the plaintiff's loss. The SEC need only establish the first and second criteria.

30 See *Four ESG Highlights From the 2020 Proxy Season*.

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33 Note that these standards become effective in 2022.

34 See https://reports.weforum.org/global-risks-report-2020/chapter-one-risks-landscape/.

35 See https://www.wbcsd.org/Programs/Redefining-Value/Business-Decision-Making/Assess-and-Manage-Performance/Resources/Sustainability-and-enterprise-risk-management-The-first-step-towards-integration.