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June 11, 2021

The Honorable Gary Gensler
Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Public Input Welcomed on Climate Change Disclosures

Dear Chair Gensler –

The Center for Audit Quality (CAQ) is an autonomous public policy organization dedicated to enhancing investor confidence and public trust in the global capital markets. The CAQ fosters high quality performance by public company auditors; convenes and collaborates with other stakeholders to advance the discussion of critical issues requiring action and intervention; and advocates policies and standards that promote public company auditors' objectivity, effectiveness, and responsiveness to dynamic market conditions. Based in Washington, DC, the CAQ is affiliated with the American Institute of CPAs. This letter represents the observations of the CAQ but not necessarily the views of any specific firm, individual, or CAQ Governing Board member.

The CAQ appreciates the opportunity to share our views related to the March 15, 2021 request, [*Public Input Welcomed on Climate Change Disclosures*](#) (the Request for Input). The CAQ is supportive of the U.S. Securities and Exchange Commission's (SEC) efforts to seek input on climate change disclosures. As outlined in the Request for Input, "*Since 2010, investor demand for, and company disclosure of information about, climate change risks, impacts, and opportunities has grown dramatically.*" An initial focus on climate-related disclosures may allow the SEC to make progress in this priority area more quickly. While proceeding initially with climate, given the increasing importance of other Environmental, Social and Governance (ESG) matters to investors, we believe that the SEC also should consider addressing other ESG matters. Accordingly, our letter includes observations and recommendations that pertain to both climate-related disclosures and ESG reporting more broadly. Because of the interrelated elements of ESG matters, it will be important for there to be an adequate notice and comment period for any potential rulemaking related to climate-related or other ESG disclosures.

CAQ

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The key points of our letter, which are described in more detail below, are as follows:

- Any climate-related or other ESG disclosure requirements should be focused on the information needs of investors.
- The CAQ is supportive of a globally accepted ESG reporting system built from existing standards and frameworks that can be adapted to meet the needs of investors in different jurisdictions.
- We believe that a global standard setter is likely necessary for a globally accepted ESG reporting system to be implemented and to operate effectively.
- If the SEC determines that it is appropriate to require issuers to make certain ESG-related disclosures, we believe the SEC should consider:
 - The transition period needed for issuers in preparing to report complete, accurate and reliable information in such new areas.
 - The importance of strong governance processes and disclosure controls over the gathering and reporting of climate-related information.
- We believe that assurance over ESG-related reporting by an independent public company auditor offers increased investor protection compared with other forms of third-party assurance or verification.

General Observations

The CAQ has performed outreach with numerous stakeholder groups including institutional investors, preparers, public company board members and auditors to inform the perspectives we share in this letter. As discussed in more detail below, two of the biggest challenges we hear from investors, preparers and audit committees in assessing a company's ESG risks and opportunities are (1) the absence of broadly adopted ESG reporting standards and (2) the reliability of the reported ESG information. These contrast significantly with the well-established structure and standards that exist in the U.S. for reporting on a company's financial performance and the effectiveness of internal controls over financial reporting.

There are three principal methods by which a company may disclose ESG information today:

- Publicly through statements or reports outside of an SEC submission (e.g., sustainability reports or data posted on a corporate website).
- Furnished to the SEC, 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).
- Filed with the SEC under the Exchange Act or the Securities Act (e.g., in periodic or current reports, registration statements or proxy statements).

A number of factors may influence a company's determination of where it discloses its ESG information. Materiality, potential legal liability, maturity of the controls and procedures for collecting and reporting the information and the timing of when relevant information is available are all factors that may influence this decision.

Today, company prepared ESG reporting largely occurs outside of issuers' SEC disclosures and is dispersed across a variety of locations such as company websites and/or standalone



sustainability reports (e.g., environmental reports, corporate social responsibility reports). However, a small number of domestic issuers have voluntarily started to report certain ESG information in SEC submissions. As investors continue to demand high-quality, accurate, reliable information on climate and other ESG initiatives, we believe the SEC should consider how to respond to those demands. Jurisdictions around the world already are taking action, such as the [Corporate Sustainability Reporting Directive Proposal](#) (CSRD) in Europe. The IFRS Foundation's Sustainability Reporting Project¹ to address climate-related risk and other ESG priorities is another example of recent efforts. We believe that convergence of ESG reporting requirements would positively impact the quality of information.

ESG Frameworks and Standards

Global ESG Reporting System

In the Request for Input, there are questions about the advantages and disadvantages of disclosure requirements that draw on existing frameworks and standards. As the SEC is aware, there have been extensive developments in market-driven solutions to ESG reporting and, more recently, convergence of the existing frameworks and standards (as discussed below). We believe the SEC should leverage this extensive body of thought leadership and effort. As such, the CAQ is supportive of a globally accepted ESG reporting system built from existing standards and frameworks that can be adapted to the market needs in different jurisdictions. This would help support companies in presenting ESG information to investors that is comparable across companies, industries and geographies.

For purposes of this letter, we define frameworks and standards as follows:

- Frameworks provide principles-based guidance that helps companies identify ESG topics to report on and determine how to structure and prepare the ESG information they disclose.
- Standards provide specific and detailed requirements that assist companies in determining what specific metrics to disclose for each topic.

For example, the Task Force on Climate-related Financial Disclosures (TCFD) recommendations form a framework that provides principles-based recommendations for managing and reporting on climate risks globally. In addition, common standards used by companies today in their ESG disclosures, which may be considered in the development of an ESG reporting system designed to meet investors' needs, include those issued by the Global Reporting Initiative (GRI) and the Sustainability Accounting Standards Board (SASB). GRI standards focus on the presentation of socially material information to various stakeholders that can be tailored to local geographic needs. SASB standards focus on industry-specific, financially material sustainability information for global investors.

As the standards-setters have themselves identified, these different frameworks and standards can be used together to meet the information needs of a company's investors. The CDP, CDSB, GRI, IIRC and SASB [Statement of Intent to Work Together Towards](#)

¹ See IFRS Foundation's sustainability reporting project page: <https://www.ifrs.org/projects/work-plan/sustainability-reporting/#current-stage>.



[Comprehensive Reporting](#) further illustrates how existing frameworks and standards can be interoperable to meet ESG reporting needs. They also released [Reporting on enterprise value: Illustrated with a prototype climate-related financial disclosure standard](#), to illustrate how their frameworks and standards, along with elements of the TCFD framework, could provide a starting point for a global climate-related financial disclosure. In our comment letter to the IFRS Foundation Trustees we stated, “ESG reporting standards designed through the lens of investors being the primary users of this information (i.e., materiality focused on enterprise value/financial materiality) will attract the broadest range of global support and promote the international use of consistent and comparable standards needed by global capital markets.”

Furthermore, as the SEC considers potential ESG reporting requirements, we believe that the following will be important:

- **Scalability:** It is important that any potential ESG reporting requirements be scalable to public companies of all sizes and consider the differences in the potential ESG risks and opportunities of different industries and geographies.
- **Industry Specificity:** While comparability remains an important element of any potential globally accepted system, some level of industry specificity may be desirable in order to provide investors with meaningful information. Further, it will be important that the SEC remain cognizant of the developments and/or requirements of other industry specific regulators to minimize differing requirements to achieve the same objective(s).
- **Global Coordination and Collaboration:** The SEC’s continued involvement in the global dialogue through its participation in the International Organization of Securities Commissions’ (IOSCO) Monitoring Group and Technical Expert Group (TEG) remains critical to the development of a globally accepted ESG reporting system. We are encouraged by the fact that the SEC is co-leading IOSCO’s TEG as we understand that the TEG is intended to work closely with the IFRS Foundation’s working group that is focused on international sustainability standards and will be tasked with reviewing and assessing its technical recommendations focused on enterprise value creation.

Designated ESG Disclosure Body

We believe that in order for a globally accepted ESG reporting system to be implemented and to operate effectively, a global ESG standard setter likely will be necessary. The IFRS Foundation Trustees have consulted on whether or not there is a need for an international sustainability reporting standards board alongside the International Accounting Standards Board.² Subsequent to that consultation they have made a series of announcements regarding the continuation of their work on the establishment of an international sustainability reporting standards board.³

² See the CAQ comment letter: https://www.thecaq.org/wp-content/uploads/2020/12/caq_comment-letter_ifrs-foundation_sustainability-consultation.pdf.

³ See IFRS Foundation’s sustainability reporting project page: <https://www.ifrs.org/projects/work-plan/sustainability-reporting/#current-stage>.



If the SEC decides that a domestic ESG standard setter is necessary to deliberate the endorsement⁴ of a global set of ESG standards because of U.S. specific market needs, global coordination and collaboration will be critical from the outset to minimize differences. Further, we believe that such a body should be an independent organization and that it should have the ability to seek input on the endorsement process from a broad range of relevant stakeholders. For example, accounting standards derive their legitimacy from the confidence that they are established, interpreted and, when necessary, modified based on independent, objective considerations. The development process must be free – in both fact and appearance – of outside influences that inappropriately benefit any particular participant or group of participants.

Climate-related Disclosure Determination

We understand that the SEC staff currently is enhancing its focus on climate-related disclosure in public company filings, including the extent to which such companies have addressed topics included in its 2010 climate change guidance.⁵ As a result of these reviews, the SEC staff could issue a report summarizing key findings and emphasizing to issuers disclosure requirements that may bear on climate-related matters. Another way the SEC staff could continue to promote disclosure in this area where appropriate would be to consider feedback received from preparers on what updates to the guidance would help them navigate the types of climate-related disclosures that would be relevant for investors and where such disclosures should be located.

We also believe that the changes to the human capital disclosure rules and requirements this past year could serve as a useful case study in the efficacy of a solely principles-based disclosure regime on information that has both qualitative and quantitative aspects. We encourage the SEC to seek out and consider feedback from investors and preparers on whether the new human capital disclosures are meeting the intended objectives of updated rules. For example, were investors generally satisfied that human capital disclosures presented in accordance with the new requirements provided the information needed to make decisions? Did issuers believe that the new requirements incorporated a reasonable assessment of both the costs to comply with the new rules and the benefits from added transparency?

96% of S&P 100 companies are already reporting ESG information using or referencing one or more of the aforementioned standards and frameworks.⁶ It is important to note that beyond the S&P 100, when considering the full population of issuers, different companies are at different stages of maturity related to their ESG reporting. A globally accepted set of ESG reporting standards that focuses on matters that are material to enterprise value and incorporates the

⁴ For example, when a new standard is issued by the IASB, jurisdictions go through a specific endorsement process to determine whether the standard should be adopted and included in local regulations. This endorsement process helps to achieve the objective of worldwide accounting standards for listed companies.

⁵ See SEC climate change guidance: <https://www.sec.gov/rules/interp/2010/33-9106.pdf>.

⁶ As of March 12, 2021, based on research of publicly available information performed by the CAO.



significant progress made by existing framework and standard setters could assist with accelerating the timing of any potential new climate-related disclosures. A single set of standards also could reduce the complexity for preparers in disclosing this information and for investors in using this information to make economic decisions.

We acknowledge that developing and implementing a global system may take time and effort. We recommend that if the SEC is considering mandating certain climate-related disclosures before a globally accepted ESG reporting system is fully developed, the SEC draft any potential disclosure requirements that rely, at least in part, on principles such that they could conform to any independently developed global standard in the future.

Implementation Considerations

If the SEC determines that it is appropriate to require issuers to make certain climate-related disclosures, the SEC should consider the aspects of implementation, including transition periods, needed for issuers to reliably report such information. As discussed above, the CAQ has observed that different issuers are in different places on the climate-related and broader ESG reporting journey. Further, issuer materiality assessments of the impact of climate-related risks on its business and the timeline of when such risks may come to fruition also can vary from company to company. The myriad of complex issues to be considered for any potential new requirements also will impact the time period needed to prepare for implementation. While these considerations may evolve over time from initial to post implementation, we believe it is important for the SEC to consider the following:

- whether the forward-looking safe harbor applies to forward looking climate-related disclosures;
- whether initially such disclosures will be furnished to the SEC or filed;
- the time period covered and the reporting frequency of the climate-related disclosures (e.g., annually, quarterly etc.);
- the reporting deadlines, considering many companies ESG disclosures are not on the same reporting timeline as their financial reporting;
- the processes and disclosure controls issuers are expected to have in place over the reporting of any potential new climate-related disclosures (discussed further below); and
- whether assurance over the disclosures will be encouraged or mandated and if so at what level and scope.

Careful consideration of these matters will be important with respect to the implementation of any potential new requirements, as many companies will be reporting this information in SEC submissions for the first time. Further, depending on the nature and placement of any new disclosure requirements, companies may need adequate time to adapt their disclosure controls and procedures to cover the new disclosures. As appropriate, the SEC could consider a phased approach, by issuer type, to the adoption of new requirements, which is consistent with the manner in which the Internal Controls over Financial Reporting (ICFR) requirements were phased in following the adoption of the Sarbanes-Oxley Act in 2002.



Controls and Governance Over Climate-related Disclosures

Trust and confidence in the information companies disclose are essential to the efficient functioning of markets. The building blocks of reliable, comparable, and relevant ESG information begin with a foundation of quality reporting by company management. Strong governance processes and controls over the gathering and reporting of ESG information and an independent assessment of that information can contribute to its reliability. The U.S. financial statement reporting system contains key elements which we believe are fundamental to reliable, high-quality financial reporting. They are:

- Company management maintains and certifies the financial statements and internal controls over financial reporting
- Oversight by an audit committee
- Assurance from regulated, independent public company auditors

We believe that these elements have a track record of producing high-quality, reliable financial statements and that they should be considered in any potential future climate-related disclosure requirements, and ESG reporting more broadly. Our outreach with institutional investors has indicated that generally climate-related reporting today lacks the transparency as to the level of rigor of the disclosure controls and procedures over how the information is gathered and reported - which causes some to question the reliability of the information. Such transparency exists for financial statement reporting with respect to internal controls and oversight.

Assurance Over ESG-related Disclosures

The European Union's CSRD includes provisions that, if adopted, would initially require companies in the European Union to obtain limited assurance on reported sustainability information with an option to move towards reasonable assurance in the future. In the U.S. 80% of S&P 100 companies subject certain elements of their ESG information, including climate-related disclosures such as greenhouse gas emissions, to some type of third party assurance or verification;⁷ and 11% of S&P 100 companies obtain such assurance from a public company auditor.⁸ Like the audits of financial statements and ICFR, we believe that third-party assurance from a public company auditor enhances the reliability of ESG information, including climate-related disclosures, presented by companies to investors and other stakeholders.

The accounting profession has acknowledged the value of ESG information to investors and others, and in their public interest role play a part in the flow of reliable information for decision making. As part of the audit of the financial statements, public company auditors are required to understand the methods, assumptions, data, and relevant controls used by management to develop accounting estimates. For example, certain climate-related risks may have a material effect on the useful life assumptions of assets reflected in financial statement accounts and subject to financial statement audit procedures. The auditor's understanding informs the auditor's risk assessment and development of procedures to obtain sufficient appropriate audit

⁷ As of March 12, 2021, based on research of publicly available information performed by the CAQ.

⁸ Ibid.



evidence, which serves as a basis for the auditor's conclusion on the financial statements. Climate-related and other ESG risks, like any other risk, will vary from company to company. The time horizon for when those risks become material to the financial statements and reflected in the underlying financial statement accounts also can vary from company to company. To the extent that climate and ESG risks are material to the underlying financial statement accounts, public company auditors already are considering those risks as part of their audit of the financial statements. The knowledge that public company audit firms gain from the execution of the financial statement and ICFR audits could lead to more effective execution of an engagement to audit climate-related information presented outside the financial statements.

Obtaining any level of assurance by a public company auditor involves the evaluation of processes, systems, and data, as appropriate, and then assessing the findings in order to support an opinion based on an examination or conclusion based on a review. We believe that assurance over climate-related reporting, specifically when performed by a public company auditor, offers increased investor protection compared with other forms of third-party assurance or verification because public company auditors:

- Are required to be independent of the companies they audit, in accordance with applicable independence standards for such attest services.
- Are skilled in gaining an understanding of a company, its business cycles, processes and how the company creates value through experience gained from financial statement and ICFR audits.
- Have access to specialists that encompass most areas of ESG information, including climate-related areas such as greenhouse gas emissions.
- Are required by the applicable standards to plan and perform assurance engagements with professional skepticism.
- Are experienced in reporting on compliance with various established standards and frameworks.
- Have a long history and experience of independently evaluating information that is then used in making capital allocation decisions.
- Are required to maintain a system of quality control that is designed to provide the public company audit firm with confidence that its auditors complied with applicable standards and the reports issued by the public company auditor are appropriate.
- Are required to adhere to continuing professional education, ethics and experience requirements, including specialized training.

An accountant's assurance report is designed to assist intended users in evaluating the reliability of information disclosed by management by providing an objective and impartial assessment of the assertions, data, and other disclosures made by management.

In the current environment, assurance by a public company auditor over ESG information is generally provided through either a review or examination type engagement. The following describes both:



- The objective of a review engagement is to obtain limited assurance and for the public company auditor to express a conclusion about whether they are aware of any material modifications that should be made to the ESG information in order for it to be fairly stated or in accordance with the relevant criteria. Review engagements are substantially narrower in scope than examination engagements.
- The objective of an examination engagement is to obtain reasonable assurance for the public company auditor to express an opinion on whether the ESG information is in accordance with the relevant criteria, in all material respects. An examination engagement is more thorough than a review engagement.

We believe that assurance from a regulated independent public company auditor is one element of our high-quality financial statement reporting system here in the U.S. and that it should be considered with respect to company prepared ESG information, including climate-related disclosures.

On June 3, 2021, the CAQ convened a multi-stakeholder roundtable with board members, investors, company management, and auditors to discuss the Request for Input. We will submit a summary of that roundtable to the SEC by the end of June 2021. We appreciate the opportunity to provide our views on the Request for Input. We would be pleased to discuss our comments or answer any questions regarding the views expressed in this letter. Please address questions to Dennis McGowan (dmcgowan@thecaq.org).

Sincerely,

A handwritten signature in black ink, reading "Catherine Ide".

Catherine Ide
Vice President, Professional Practice
Center for Audit Quality

cc:

SEC

Caroline A. Crenshaw, Commissioner
Allison Herren Lee, Commissioner
Hester M. Pierce, Commissioner
Elad L. Roisman, Commissioner
John Coates, Acting Director, Division of Corporate Finance
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