Today we continue our looking at proposals – and some initial steps – to radically remake the corporation. We consider how disclosure mandates can be used to focus management attention on CSR matters, thus bringing CSR into the world of “what gets measured gets managed.” Our focus is on the SEC’s recent interpretive guidance to public companies that identifies climate change (and its risks and opportunities) as sometimes requiring disclosure in SEC filings.

The first reading is from a law review article by a “reformist” corporate law scholar who describes the history of the SEC using disclosure as a means to “cajole” management into new habits of corporate governance. For example, he points out that disclosure requirements on the “independence” of directors may actually compel companies to be mindful and thus more proactive in putting independent individuals on the board. You will come to understand that securities disclosure has a moral dimension.

The next reading is the 2010 SEC Guidance on Climate Change Disclosure. You will have a chance to read how the US “financial disclosure agency” talks to its constituents – namely, public companies. The guidance describes the growing importance of climate change (and increasing regulatory initiatives to control carbon emissions) on the operations, assets, and business opportunities of US public companies. You will also get a sense for the types of “forward looking” disclosures required of US companies, where management is asked to anticipate what the future holds for the company and its investors.

After reading the SEC guidance, you’ll have a chance to see how a major US law firm – Davis Polk Wardell -- described the release and the impact it would have on company disclosure obligations. These “law firm memos” are an important (and relatively new) source of information about what is happening in the legal world. Such memos are often written to attract new business to the firm, either from existing clients or new clients. You’ll notice that Davis Polk seems interested in advising clients on climate change matters.

The next reading is an interesting report by Ceres on how companies should be reporting climate change risk and opportunity. Notice that climate change is also a business opportunity! The Ceres report describes what the SEC disclosure rules require and also goes beyond the SEC guidance to suggest what forward-thinking, CSR-aware companies should be “measuring and managing.” You’ll want to compare how Ceres views company disclosure obligations compared
to how Davis Polk explained the obligations to its business clients. At the end of the Ceres report, you’ll find a study on how well the ten largest oil/gas companies in the world (all required to file with the SEC) are disclosing climate-change risks and opportunities.

Finally, you will read a recent story from the New York Times about how US companies are now assuming that their carbon emissions will be taxed. That is, they are building into their models for calculating future profits that there will be “carbon emission costs” imposed through some still-to-be-created tax on carbon emissions. The story raises the question whether the new regulatory environment of climate-change disclosure is also permeating company business planning. After all, “what gets measured gets managed.” No?

Readings:
- Brown, *Corporate Governance, the SEC, and the Limits of Disclosure* (2007)
- SEC, Climate Change Guidance (2010)
- Davis Polk, Environmental Disclosures in SEC Filings – 2011 Update
- Ceres, Disclosing Climate Risks and Opportunities in SEC filings (2011)
CORPORATE GOVERNANCE, THE SECURITIES AND EXCHANGE COMMISSION, AND THE LIMITS OF DISCLOSURE

J. Robert Brown, Jr.


States regulate the substance of corporate governance. Fiduciary duties, director qualifications, and the rights of shareholders all emanate from state law. Regulation of disclosure, on the other hand, falls to the Securities and Exchange Commission (SEC), at least for public companies.

This neat dichotomy has been long accepted but little examined. In fact, it is not a particularly accurate description. In the public company, disclosure means little, absent adequate governance. No matter how many accounting standards are implemented, enforcement proceedings brought, or items added to Regulation S-K, the quality of disclosure hinges on management's commitment to the process.

When Congress adopted the Securities Exchange Act in 1934, the central issue of corporate governance was the absence of adequate disclosure. Management took advantage of secrecy to self perpetuate, pay excessive salaries, and engage in other abusive practices. With such secrecy, substantive corporate governance mattered far less.

Congress sought to fix corporate governance by addressing this secrecy. The disinfectant effect of disclosure had a corresponding impact on the substantive standards, but not the one expected. Self interest did not abate; it merely lost the protection of secrecy. Instead, pressure built on states to loosen substantive standards. Over time, the duty of care evolved into little more than a wooden process, and the duty of loyalty into a standard largely unmoored from fairness.

At the same time, the disclosure regime implemented by the SEC itself impacted the substance of corporate governance. Under state law, shareholders had the inherent right to make proposals or nominate directors from the floor of the meeting. The SEC proxy rules, however, made the meeting itself a formality with votes cast as part of the proxy process prior to the meeting. Actions were destined to fail unless shareholders competed for proxies. But the rules made this prohibitively expensive, effectively depriving shareholders in public corporations of their substantive rights.

Recognizing a link between disclosure and substance, the SEC tried to regulate substance using a variety of mechanisms, including disclosure. In the 1970s, Congress increased the SEC's authority to regulate the way management assembles financial information. In the 1980s the SEC increased enforcement proceedings and regulatory admonitions to cajole management behavior.

None of these had the desired effect. By the 1990s, the Commission began to use disclosure aggressively to alter the substantive behavior of officers and directors. [This was something
different from the Commission's past efforts. Much of the required information was, at best, marginally material to investors or shareholders. Disclosure was instead designed to cause changes in corporate behavior by illuminating practices that could result in embarrassment or legal liability.

The approach, however, was only marginally effective. Sometimes the requirements resulted in a morass of boilerplate—such as in “going private” transactions in which management acquired corporate ownership. In other instances, substantive behavior—such as the setting of executive pay—did not change even with disclosure, in part because of the continuing downward evolution of standards under state law. The result was often an additional wave of even more complex disclosure.

More effective authority to influence governance came from the SEC’s growing authority to regulate management’s involvement in the disclosure process. The Sarbanes-Oxley Act of 2002 required management to develop and assess the internal controls used to formulate financial disclosure—and imposed personal liability on executives who failed to do so properly. The SEC determined the role particular individuals would play in the process, thus imposing standards of behavior on officers and directors, at least in the context of financial disclosure. As a result, the governance process changed.

This Article will do several things. First, it will briefly examine the divided role of the states and the SEC in corporate governance. Second, it will identify some of the consequences of this division. Third, it will look at the SEC efforts to break from disclosure to regulate the substantive behavior of officers and directors.

I. SUBSTANCE, DISCLOSURE, AND THE REGULATION OF CORPORATE GOVERNANCE

Adopted during the Great Depression, the Securities Exchange Act of 1934 delegated to the SEC the authority to regulate the disclosure of public companies. Specifically, section 13(a) enabled the agency to prescribe the “information and documents” required to be filed, which evolved into a system of annual and quarterly reports.

The Exchange Act also addressed governance concerns with respect to shareholders. Section 14(a) of the Exchange Act gave the Commission the authority to regulate proxies, an area of state regulatory failure. The abuses included the use of proxies “by unscrupulous corporate officials to retain control of the management by concealing and distorting facts” and to obtain approval for “vast bonuses out of all proportion to what legitimate management would justify.”

The idea of the Exchange Act was that disclosure, coupled with the authority of shareholders under state law, would solve the identified concerns of corporate governance. But little or no effort was made to ensure accountability or mandate a particular disclosure process. Only where the process culminated in inaccurate disclosure did the Commission act, but then only on a case-by-case basis.
At the same time, substantive standards of governance continued to weaken. The duty of care evolved into a shill, reduced by an expansive interpretation of the business judgment rule and the ubiquitous presence of waiver of liability provisions. The duty of loyalty ceased to be about fairness, with “independent” director approval eliminating any review of the substance of the transaction. The evolution favored the interests of management over the rights of shareholders.

The decline in substantive standards and the resulting impact on the disclosure process surfaced with a vengeance in the 1970s. Arising out of the Watergate investigation, the SEC uncovered a pattern of foreign bribes and illegal campaign contributions by public companies. But when confronted with this corporate impropriety, the SEC Chairman specifically disclaimed the need for federally imposed “behavioral standards.” The Exchange Act was amended to require the maintenance of adequate books, records, and internal controls. The new requirements, however, did not address accountability.

Although the SEC brought some enforcement proceedings in which the agency sought to emphasize the duties of directors to oversee a system of internal controls, the SEC lacked authority to alter generally the governance structure of public companies.

II. SUBSTANCE AND DISCLOSURE: THE EARLY YEARS

With continued concerns about both the governance process and accountability, the Commission found itself back at the beginning, largely limited to disclosure to affect practices. Increasingly, therefore, the Commission began to use disclosure to directly influence substantive behavior of directors and officers.

A. Disclosure and Compliance

Early efforts to regulate substantive behavior of officers and directors focused on improving compliance with the securities laws. This occurred most noticeably in connection with ownership reports by corporate insiders and large shareholders.

Frustrated by widespread noncompliance, the SEC required company policing by requiring that proxy statements reveal violations of the reporting obligations. The idea was to embarrass the company into compelling compliance by insiders. The SEC all but admitted this disclosure was meant to increase compliance rather than to provide investors with material information.

The SEC’s effort worked. Behavior changed. Compliance by executive officers and directors improved.

B. Disclosure and Leverage

Other disclosure requirements sought to improve the governance process by increasing the leverage of dissenting directors. Companies were made to disclose any disagreement that resulted
in a director resigning. Ostensibly meant to assist shareholders in assessing the “quality of management,” the provision had the purpose and effect of giving dissenting directors bargaining power. Any resignation over a disagreement would result in public disclosure of the conflict, potentially generating bad publicity and inviting legal scrutiny.

The provision’s impact on governance, however, has always been limited. The provision applies only to conflicts at the board level. It does nothing to ensure that the board has any particular information about the activities of the company, or that conflicts or problems are addressed at the board level in the first instance.

In the 1990s, the SEC turned to disclosure as a mechanism to regulate the deliberative process within corporate boardrooms. It did so in three broad ways.

**Board Independence.** First, the Commission sought to use disclosure to achieve greater director independence.

In the aftermath of Enron and Worldcom, the exchanges and NASDAQ – under pressure from the SEC -- adopted stringent listing standards that boards of listed companies had to have a majority of independent directors and to create three specific committees--nominating, compensation, and audit--with each containing only independent directors. In addition, the definition of independence was strengthened, with the addition of categorical disqualifications.

To create a system of company “self enforcement,” SEC disclosure rules required public companies to reveal compliance with the exchange listing requirements on director independence. While compliance of the listing standards rested with the lax exchanges, compliance with the disclosure requirements rested with the SEC. In addition, shareholders and investors could bring actions for misstatements about compliance with listing standards.

**Limits on CEO Influence.** Second, the SEC sought to increase the transparency of the board’s decision making.

With respect to compensation decisions, SEC rules in the 1990s required a report by the board’s compensation committee in the proxy statement, which included the criteria used in making pay awards and the policies for determining the CEO’s compensation. In particular, the report had to discuss the relationship between the CEO’s performance and his compensation.

Although the SEC said it was not trying to change substantive behavior, the provision was intended to do exactly that. With the increased disclosure, boards presumably would be less inclined to pay CEOs what they asked for. But the compensation reports proved uninformative, and the CEO “pay spiral” continued upward.

With respect to the nomination of directors, SEC rules required how the nomination committee had identified and evaluated director candidates – in particular, who had brought the candidate to the
committee’s attention. Because of this greater transparency, the SEC sought to encourage consideration of shareholder nominees and to reveal the role of the CEO in the process. But the strong presence of the CEO in the nomination process has not changed.

**Disclosure and SOX.** Third, the SEC has designed disclosure requirements to limit the influence of the CEO in the governance process. [The article describes how Sarbanes-Oxley imposed substantive obligations -- such requirements on internal controls, the authority of the audit committee, and the stricter definitions of independent directors. The article identifies how certain SEC disclosure rules complement the new substantive rules.]

**IV. THE SEC AND SUBSTANTIVE BEHAVIOR**

At this point, a number of observations can be made about the role of the SEC in the corporate governance.

Disclosure works best where it relates to a preexisting substantive right and creates the specter of increased legal attention. For example, the disclosure of conflicts of interest by fiduciaries can influence officer and director behavior, given the risk of substantive liability.

But in the absence of strong underlying legal obligations, the use of disclosure as a tool to regulate substantive behavior is far less effective. While the threat of embarrassment may affect behavior, embarrassment only goes so far. For example, a director may not appreciate public disclosure that he missed a large number of board meetings, but this disclosure is unlikely to result in a resignation, leaving shareholders with little recourse. At most, it imposes modest pressure to attend more meetings the following year.

The disclosure requirements can also be counterproductive. For instance, disclosure may produce a wealth of complicated but ultimately unimportant information – that neither executives nor shareholders pay attention to. Moreover, disclosure may have unintended consequences. There is reason to believe that detailed disclosure of executive compensation actually accelerated the upward trend in compensation.

**V. CONCLUSION**

The SEC has real authority to ensure accountability within public companies, particularly with respect to the board of directors. Over time, the SEC should impose specific requirements and specific roles on the board. Directors will come to learn that inattention in a topic identified by the SEC will create the specter of liability under the securities laws and will respond accordingly.
Commission Guidance Regarding Disclosure Related to Climate Change

SUMMARY: The Securities and Exchange Commission ("SEC" or "Commission") is publishing this interpretive release to provide guidance to public companies regarding the Commission’s existing disclosure requirements as they apply to climate change matters.

EFFECTIVE DATE: February 8, 2010.

I. Background and purpose of interpretive guidance

A. Introduction

Climate change has become a topic of intense public discussion in recent years. Scientists, government leaders, legislators, regulators, businesses, including insurance companies, investors, analysts and the public at large have expressed heightened interest in climate change.

This release outlines our views with respect to our existing disclosure requirements as they apply to climate change matters. This guidance is intended to assist companies in satisfying their disclosure obligations under the federal securities laws and regulations.

B. Background

1. Recent regulatory, legislative and other developments

In the last several years, a number of state and local governments have enacted legislation and regulations that result in greater regulation of greenhouse gas (GHG) emissions. Climate change related legislation is currently pending in Congress. The House of Representatives has approved a bill, and a similar bill was introduced in the Senate in the fall of 2009. This legislation, if enacted, would limit and reduce GHG emissions through a “cap and trade” system of allowances and credits, among other provisions.

The Environmental Protection Agency has been taking steps to regulate GHG emissions. On January 1, 2010, the EPA began to require large emitters of GHGs to collect and report data with respect to their GHG emissions. This reporting requirement is expected to cover 85% of the nation’s GHG emissions generated by roughly 10,000 facilities.11 In December 2009, the EPA issued an “endangerment finding” for GHGs under the Clean Air Act, which will allow the EPA to craft rules that directly regulate GHG emissions.
Some members of the international community also have taken actions to address climate change issues on a global basis. One such effort in the 1990s resulted in the Kyoto Protocol. Although the United States has not ratified the Kyoto Protocol, many registrants have operations outside of the United States that are subject to its standards. Another important international regulatory system is the European Union Emissions Trading System (EU ETS), which was launched as an international “cap and trade” system of allowances for emitting carbon dioxide and other GHGs, based on mechanisms set up under the Kyoto Protocol. In addition, the United States government is participating in ongoing discussions with other nations, which may lead to future international treaties focused on remediying environmental damage caused by GHG emissions. Those accords ultimately could have a material impact on registrants that file disclosure documents with the Commission.

The insurance industry is already adjusting to these developments. A 2008 study listed climate change as the number one risk facing the insurance industry. Reflecting this assessment, the National Association of Insurance Commissioners recently promulgated a uniform standard for mandatory disclosure by insurance companies to state regulators of financial risks due to climate change and actions taken to mitigate them. We understand that insurance companies are developing new actuarial models and designing new products to reshape coverage for green buildings, renewable energy, carbon risk management and directors’ and officers’ liability, among other actions.

2. Potential impact of climate change related matters on public companies

For some companies, the regulatory, legislative and other developments noted above could have a significant effect on operating and financial decisions, including those involving capital expenditures to reduce emissions and, for companies subject to “cap and trade” laws, expenses related to purchasing allowances where reduction targets cannot be met. New trading markets for emission credits related to “cap and trade” programs could present new opportunities for investment.

In addition, there may be significant physical effects of climate change that have the potential to have a material effect on a registrant’s business and operations. These effects can impact a registrant’s personnel, physical assets, supply chain and distribution chain. They can include the impact of changes in weather patterns, such as increases in storm intensity, sea-level rise, melting of permafrost and temperature extremes on facilities or operations. Changes in the availability or quality of water, or other natural resources on which the registrant’s business depends, or damage to facilities or decreased efficiency of equipment can have material effects on companies. Physical changes associated with climate change can decrease consumer demand for products or services; for example, warmer temperatures could reduce demand for residential and commercial heating fuels, service and equipment.

For some registrants, financial risks associated with climate change may arise from physical risks to entities other than the registrant itself. For example, climate change-related physical changes and hazards to coastal property can pose credit risks for banks whose borrowers are located in at-risk areas.
Companies also may be dependent on suppliers that are impacted by climate change, such as companies that purchase agricultural products from farms adversely affected by droughts or floods.

3. **Current sources of climate change related disclosures regarding public companies**

There have been increasing calls for climate-related disclosures by shareholders of public companies. This is reflected in the petitions for interpretive advice submitted by large institutional investors and other investor groups. The New York Attorney General’s Office recently has entered into settlement agreements with three energy companies to enhance their disclosures about their GHG emissions and potential liabilities to the companies resulting from climate change and related regulation.

Although some information relating to GHG emissions and climate change is disclosed in SEC filings, much more information is publicly available in voluntary disclosures. For example, **The Climate Registry** provides standards for and access to climate-related information. The Registry is a non-profit collaboration among North American states, provinces, territories and native sovereign nations that sets standards to calculate, verify and publicly report GHG emissions into a single public registry. The Registry supports both voluntary and state-mandated reporting programs and provides data regarding GHG emissions.

The **Carbon Disclosure Project** collects and distributes climate change information, both quantitative (emissions amounts) and qualitative (risks and opportunities), on behalf of 475 institutional investors. Over 2500 companies globally reported to the Carbon Disclosure Project in 2009; over 500 of those companies were U.S. companies. Sixty-eight percent of the companies that responded to the Carbon Disclosure Project’s investor requests for information made their reports available to the public.

The **Global Reporting Initiative** has developed a widely used sustainability reporting framework developed by GRI participants drawn from business, labor and professional institutions worldwide. The GRI framework sets out principles and indicators that organizations can use to measure and report their economic, environmental, and social performance, including issues involving climate change. Sustainability reports based on the GRI framework are used to benchmark performance with respect to laws, norms, codes, performance standards and voluntary initiatives, demonstrate organizational commitment to sustainable development, and compare organizational performance over time.

II. **Historical background of SEC environmental disclosure**

The Commission first addressed disclosure of material environmental issues in the early 1970s. The Commission issued an interpretive release in 1971 stating that registrants should consider disclosing in their SEC filings the financial impact of compliance with environmental laws, based on the materiality of the information. Throughout the 1970s, the Commission considered specific rules mandating disclosure of litigation and other business costs arising out of compliance with environmental laws. After a decade
of evaluation and experience, the Commission adopted rules in 1982 (that are still current) that specifically address disclosure of environmental issues.

In addition, beginning in 1968, we began to develop requirements for management to discuss and analyze their company's financial condition and results of operations. As developed during the 1970s and 1980s, materiality standards for disclosure under the federal securities laws provide that information is “material” if there is a substantial likelihood that a reasonable investor would consider it important in deciding how to vote or make an investment decision -- or, put another way, if the information would alter the total mix of available information.

III. Overview of rules requiring disclosure of climate change issues

When a registrant is required to file a disclosure document with the Commission, the requisite form will largely refer to the disclosure requirements of Regulation S-K (general non-financial disclosure rules) and Regulation S-X (accounting disclosure rules). In addition, Securities Act Rule 408 and Exchange Act Rule 12b-20 require a registrant to disclose “such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading.” We next describe the most pertinent non-financial statement disclosure rules related to climate change. Then in the following section, we discuss disclosure of certain specific climate change related matters.

Description of business. Item 101 of Regulation S-K requires a registrant to describe its business and that of its subsidiaries -- including principal products and services, major customers, and competitive conditions. Item 101 expressly requires disclosure regarding certain costs of complying with environmental laws, including “material effects of [environmental] compliance ... upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries.”

Legal proceedings. Item 103 of Regulation S-K requires a registrant to briefly describe any material pending legal proceeding to which it or any of its subsidiaries is a party. A registrant also must describe material pending legal actions in which its property is the subject of the litigation, including “environmental litigation” that is material to the business or financial condition of the registrant.

Risk factors. Item 503(c) of Regulation S-K requires a registrant to provide a discussion of the most significant factors that make an investment in the registrant speculative or risky, and specify how the particular risk affects the particular registrant.

Management’s discussion and analysis. Item 303 of Regulation S-K requires disclosure (known as the Management’s Discussion and Analysis of Financial Condition and Results of Operations, or MD&A). The MD&A requirements are meant to provide a narrative of the registrant through the eyes of management, to provide the context for analyzing financial information, and to
provide information about the quality of, and potential variability of, a registrant's earnings and cash flow – with particular emphasis on the registrant's prospects for the future.

For example, registrants must identify and disclose known trends, events, demands, commitments and uncertainties that are reasonably likely to have a material effect on financial condition or operating performance. The time horizon of a known trend, event or uncertainty may be relevant to a registrant's assessment of the materiality of the matter and whether or not the impact is reasonably likely. Registrants should address, when material, the difficulties involved in assessing the effect of the amount and timing of uncertain events, and provide an indication of the time periods in which resolution of the uncertainties is anticipated.

IV. Climate change related disclosures

Each of the items discussed above may require disclosure regarding the impact of climate change. The following are specific topics registrants may need to consider.

Impact of legislation and regulation. Developments in federal and state regulation regarding climate change and GHG emissions may trigger disclosure obligations under Items 101, 103, 503(c) and 303 of Regulation S-K. Item 101 requires disclosure of any material estimated capital expenditures for environmental control facilities. Item 503(c) may require risk factor disclosure regarding existing or pending climate-change legislation or regulation. For example, registrants in the energy sector may face significantly different risks from climate change legislation or regulation compared to registrants in the transportation sector.

Item 303 requires registrants to assess whether any enacted (and even pending) climate change legislation or regulation is reasonably likely to have a material effect on the registrant’s financial condition or results of operation. For pending legislation or regulation, management must evaluate whether it is reasonably likely to be enacted. Unless management determines that it is not reasonably likely to be enacted, it must proceed on the assumption that the legislation or regulation will be enacted. Then management must determine whether the legislation or regulation, if enacted, is reasonably likely to have a material effect on the registrant’s financial condition or results of operations.

A registrant should not limit its evaluation of disclosure of a proposed law only to negative consequences. Changes in the law or in the business practices of some registrants in response to the law may provide new opportunities for registrants. For example, if a “cap and trade” type system is put in place, registrants may be able to profit from the sale of allowances if their emissions levels end up being below their emissions allotment. Likewise, those who are not covered by statutory emissions caps may be able to profit by selling offset credits they may qualify for under new legislation.
International accords. Registrants also should consider, and disclose when material, the impact on their business of treaties or international accords relating to climate change. We already have noted the Kyoto Protocol, the EU ETS and other international activities in connection with climate change remediation. The potential sources of disclosure obligations related to international accords are the same as those discussed above for U.S. climate change regulation.

Indirect consequences of regulation or business trends. Legal, technological, political and scientific developments regarding climate change may create new opportunities or risks for registrants. These developments may create demand for new products or services, or decrease demand for existing products or services. (For example, recent legislation will ultimately phase out most traditional incandescent light bulbs. This has resulted in the acceleration of the development and marketing of compact fluorescent light bulbs.)

Another example of a potential indirect risk from climate change is the impact on a registrant’s reputation. Depending on the nature of a registrant’s business and its sensitivity to public opinion, a registrant may have to consider whether the public’s perception of any publicly available data relating to its GHG emissions could expose it to potential adverse consequences to its business operations or financial condition resulting from reputational damage.

Physical impacts of climate change. Significant physical effects of climate change, such as effects on the severity of weather (for example, floods or hurricanes), sea levels, the arability of farmland, and water availability and quality, have the potential to affect a registrant’s operations and results. A 2007 Government Accountability Office report states that 88% of all property losses paid by insurers between 1980 and 2005 were weather-related. Severe weather can have a devastating effect on the financial condition of affected businesses. The GAO report cites a number of sources for the view that severe weather will increase as a result of climate change brought on by an overabundance of GHGs. Among other effects, this could increase insurance premiums and deductibles, or a decrease in the availability of coverage, for registrants with plants or operations in areas subject to severe weather.

V. Conclusion

This interpretive release is intended to remind companies of their obligations under existing federal securities laws and regulations to consider climate change and its consequences as they prepare disclosure documents to be filed with us and provided to investors. We will monitor the impact of this interpretive release on company filings. In addition, the Commission’s Investor Advisory Committee is considering climate change disclosure issues as part of its overall mandate to provide advice and recommendations to the Commission, and the Commission is planning to hold a public roundtable on disclosure regarding climate change matters in the spring of 2010.
Executive Summary

In the past year, we have witnessed a great deal of interest in environmental and climate change disclosure in SEC filings. The SEC and New York Attorney General's ("NY AG") office have sought to enhance such disclosure.

Most significant was the SEC's adoption in February 2010 of its landmark climate change interpretive guidance ("Release"). Following the Release, however, the SEC has de-emphasized climate change disclosure -- perhaps because of pressing financial reform issues, as well as strong criticism from the U.S. Congress and some companies.

Nonetheless, the newly elected NY AG has continued to press for improved climate change disclosure, along with climate-change shareholder proposals, have kept the issue alive.

Observed Trends in Climate Change Disclosure

Based on our review of SEC filings made in 2010, we saw (1) an increase in discussion of generic weather risk factors; (2) new disclosure on potential changes in demand for products and services and on increases in fuel prices; (3) little disclosure of actual or potential reputational harm due to climate change; and (4) a minimal increase in climate change disclosure in the Management Discussion and Analysis ("MD&A") section of these SEC filings.

That said, registrants in greenhouse gas intensive industries, notably energy companies, have enhanced their disclosure – including by adding more lengthy factual updates of legislative, regulatory and litigation developments. It is unclear, however, whether this trend in energy company disclosure is due primarily to the Release, or is more a function of electric utility settlements with the NY AG.

Climate Change Regulatory Update

The Release explains that one of the "ways climate change may trigger disclosure" requirements is through the impact of climate change legislation, regulation and international accords. With respect to such regulatory matters, 2010 was a tumultuous year. In April 2010 the U.S. Environmental Protection Agency ("EPA") issued standards to regulate greenhouse gas emissions from vehicles and from newly constructed and modified industrial and commercial facilities. In addition, the EPA has announced plans to develop greenhouse gas emission standards for certain power plants and refineries.
In addition, beginning in 2010, certain companies with significant greenhouse gas emissions are required to report their annual emissions to the EPA, and the EPA has expanded the reporting obligations to include additional sources for subsequent years.

**SEC Developments After the Climate Risk Disclosure Release**

The Release notes the SEC’s commitment to hold a public climate change disclosure roundtable in Spring 2010 and to consider recommendations of its then-existing Investor Advisory Committee (“IAC”), formed in 2009. The SEC, however, did not convene the roundtable and has disbanded the IAC. “due to budget uncertainty”.

Further, the SEC (by our count) has issued only six climate change disclosure comments – to manufacturing and energy firms, to insurance companies, and even a beauty salon. With the exception of an instruction to a natural gas distribution company to elaborate on the expected impact of federal climate legislation on its business, the comments were generally cursory.

**Utilities’ Opposition to the Release**

The Edison Electric Institute (“EEI”), whose members generate approximately 60% of the total electricity supplied in the United States, met with the SEC in May 2010 and then sent a letter stating the Release (1) requires too much speculation by companies, including about weather patterns, the likelihood of laws passing, and possible reputational damage relating to climate change; (2) could discourage voluntary disclosures fearful of liability under securities laws; and (3) might require companies to conduct comprehensive reviews of climate change matters, which would be unduly burdensome and potentially unnecessary. The SEC did not respond.

**Congressional Opposition to the Release**

After the SEC Release, members in both houses of Congress introduced identical bills to block enforcement of the Release. In addition, some members of Congress voiced public disapproval of the Release, asserting it would require predictions about unforeseeable events, advanced a political agenda and imposing significant compliance costs on companies, and opposing the Release’s “onerous new mandate.” Again, the SEC said nothing.

**SEC Focus on Risk Factor Disclosure**

The SEC is currently focusing on risk factor disclosure. Meredith Cross, director of the SEC’s Division of Corporation Finance, has expressed her said that companies should pull away from “mind-numbing risk factors discourse to a more-targeted discussion of the principal risk facing the company.” Likewise, SEC Chair Schapiro has said the SEC is reevaluating whether its disclosure requirements could be “more meaningful to investors and to the markets.”
New York Attorney General Subpoena Update

Newly elected NY AG Eric Schneiderman said he would “continue to build on the successful program launched by former NY AG Andrew Cuomo to require carbon-intensive companies to disclose financial risks related to global warming.” This may lead to new subpoenas – beyond those issued to Dominion Resources and Peabody Energy – demanding better disclosure of company-specific risks related to climate change and GHG emissions.

NAIC Climate Change Disclosure Survey Update

In March 2010, the National Association of Insurance Commissioners (“NAIC”) issued a final model rule – for adoption by state insurance regulators – to require insurers complete and submit an annual climate risk disclosure survey. The final rule, however, is not mandatory and the surveys would not have to be disclosed to the public. Under the rule, the survey would require insurance companies to disclose

(i) what climate change risks the company faces;
(ii) what its risk management policies are;
(iii) how the company identifies and addresses these risks; and
(iv) how the company has changed its business or investment strategy as a result.

The rule has lost momentum and only California, New York, Pennsylvania and Washington have agreed to make the 2010 survey mandatory to their insurance companies and to make the results publicly available.

Climate Change Shareholder Proposals

Shareholder interest in climate change disclosure has been minimal. During the 2009 and 2010 proxy season shareholder activists submitted 78 climate change related proposals, but only two received majority support.

• IDACORP (electricity utility holding company). Shareholders (51.2%) approved a resolution asking the board to establish greenhouse gas reduction goals.

• Layne Christensen (energy company). Shareholders (60.3%) approved a resolution requiring the board to issue “a sustainability report describing the company's [environmental, social and governance] performance and goals, along with sustainable water management and greenhouse gas emissions and management plans for their reduction.

• Massey Energy (coal mining company). Shareholders (53.1%) approved a proposal requiring the company to set greenhouse gas reduction goals. (The company, however,
counted abstentions as disapprovals, and deemed the proposal to have received only 36.8% support."

**Conclusion**

We expect that environmental and climate change disclosure will continue to be of interest to the SEC in 2011. We will watch with great interest the SEC’s progress on updating risk factor disclosure standards and whether the NY AG takes any action to enhance climate change disclosure.

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If you have any questions regarding the matters covered in this publication, please contact Betty Moy Huber at 212 450 4764 (betty.huber@davispolk.com).
Ceres *

DISCLOSING CLIMATE RISKS & OPPORTUNITIES IN SEC FILINGS:
A GUIDE FOR CORPORATE EXECUTIVES, ATTORNEYS & DIRECTORS

February 2011

* Ceres is a national coalition of investors, environmental groups and other public interest organizations working with companies to address sustainability challenges such as global climate change. Ceres directs the Investor Network on Climate Risk, a group of 95 institutional investors with assets exceeding $9 trillion, by identifying the financial opportunities and risks in climate change and by tackling the policy and governance issues that impede investor progress toward more sustainable capital markets.

FOREWORD

As this report is being published, the costs of Australia’s epic January floods are still being assessed. Beyond the billions of dollars in infrastructure damage, shipping and agriculture suffered major losses, causing economic ripples globally. Disruption of coking coal exports, for example, caused global coal prices to rise 25 percent.

Climate change threatens many more such extreme weather events—like this one-in-200-year flood—and more material impacts on companies’ operations and future financial prospects.

At the same time, of course, governments worldwide are moving to limit the carbon emissions that cause climate change. India became the first nation last year to levy a carbon tax on coal producers. Japan, Australia, the European Union and South Korea are pursuing similar measures.

For years, investors managing trillions of dollars have been pressing companies to disclose material information on just these sorts of risks, as well as on the opportunities related to climate change, such as escalating demand for clean technologies. In February 2010, the U.S. Securities and Exchange Commission responded, issuing guidance for companies on climate change-related information they should be disclosing to investors.

Despite the SEC guidance, this report’s review of companies’ most recent 10-K filings shows that improvements in climate risk disclosure have been incremental at best. And while voluntary reporting on climate risks is helpful, it is not sufficient. Investors need information that is standardized and regulated, and they need to be able to find that information in one place.
This report aims to help companies review and improve their disclosure. It provides clear guidance for firms on how to assess and disclose climate risks and opportunities, as well as concrete examples of what investors view as quality disclosure.

At its heart, good disclosure is about specificity and quantification. It's about providing investors the concrete information they need to be able to evaluate a company’s risks or to compare that company to its peers.

Here are some examples of good disclosure:

- Chiquita Brands International describes in its most recent 10-K the physical climate risks, such as drought, temperature extremes, floods and hurricanes, which could reduce its crop size and quality. It quantifies those impacts, from the costs of shipping disruptions, to the costs of rehabilitating flooded farms and procuring replacement fruit.

- AES Corp. (an electric power company) disclosed in its 10-K estimated costs of its compliance with the U.S. Northeast's regional cap and trade program, as well as the model and methodology used to derive those estimates.

- Siemens disclosed in its 20-F [required for foreign private issuers in the United States] that it considers climate change to be a "global megatrend" that will impact all humanity, and that it has aligned its strategy and business activities to minimize carbon dioxide emissions.

To attain this level of disclosure, management must systematically analyze the company’s potential risks and opportunities related to climate change, and then use sound judgment to decide which risks and opportunities are material and therefore require disclosure. Creating sustainable governance systems and setting up a climate management team to oversee procedures for monitoring GHG emissions and analyzing risks will make this challenge easier.

This report lays out the practical steps for such a comprehensive approach.

Mindy S. Lubber
President, Ceres
Director, Investor Network on Climate Risk

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EXECUTIVE SUMMARY

Adjusting to a world profoundly shaped by climate change is one of the great challenges of the 21st Century. For companies, understanding and responding to the risks and opportunities from
climate change, whether from carbon-reducing regulations or physical impacts, has become a business imperative.

For investors, identifying firms that are ahead of the curve—and those that are behind—in responding to this growing business trend is equally vital. That is why growing numbers of investors in recent years have demanded that companies disclose material climate-related risks and opportunities and have pressed the Securities and Exchange Commission and other regulators to ensure that these disclosures satisfy securities law requirements and the needs of the public.

This Ceres report discusses the significance of major developments in climate disclosure and provides specific guidance to help companies improve their public filings, specifically with: (1) an overview of recent developments in climate disclosure, particularly the SEC’s 2010 interpretive guidance; (2) investor expectations concerning key categories of climate disclosure, including specific company examples from recent securities filings; and (3) an 11-point checklist to help companies improve the quality of their disclosure and position themselves to respond more effectively.

Climate Risk Disclosure and SEC Guidance

The SEC’s Guidance Regarding Disclosure Relating to Climate Change, released in February 2010, outlines public companies’ obligations under (settled) securities laws and SEC regulations to disclose to investors material information concerning climate-related risks and opportunities.

The Guidance is a watershed in the longstanding efforts by major investors, state law enforcement officials and others to focus companies’ attention on the quality of their climate-related disclosure. Combined with important new developments in federal and state GHG regulation, the Guidance signals the need for companies to take a fresh look at their climate change strategies and disclosure practices.

The SEC Guidance recognizes that climate change has become an important feature of the physical, economic, regulatory and physical environments in which companies operate.

- Carbon-reducing regulations may impose direct compliance costs or increase the cost of inputs.
- Changing weather patterns may affect a firm’s operating costs, threaten its water supplies, increase risks of catastrophic weather-related losses, or alter consumer demand for its products or services.
- Public awareness of the climate change issue can create reputational risks for firms with high GHG emissions.

At the same time, climate change can open significant new opportunities for businesses that offer low-carbon products, can profit from emissions trading markets, or provide services relating to adaptation to climate change.
Assessments of corporate disclosure practices on climate change show significant improvements in recent years, particularly in voluntary disclosures. However, overall disclosure continues to be highly inconsistent and often inadequate, particularly in mandatory filings, and frequently fails to meet the needs of investors.

Firms should also be aware, as the SEC Guidance notes, that disclosures now being made voluntarily, such as in corporate sustainability reports or Carbon Disclosure Project survey responses, may also need to be made as part of mandatory SEC filings.

**Climate Disclosure Best Practices in SEC Filings**

A review of SEC filings for the 2009 fiscal year, the most recent year for which 10-Ks are available, reveals an array of climate change reporting examples reflecting differing levels of comprehensiveness, detail and clarity, and too many companies that fail to address the issues at all.

Our report includes examples of reporting that reflect good, fair and poor disclosure. This report does not identify examples of exemplary disclosure because such examples are wanting. The overall level of disclosure, while improving, remains well below where it should be. For example, a recent report by ISS Corporate Services analyzed 2009 10-K filings by the 100 largest U.S. public companies, finding that just 51 made any reference to climate change, only 22 discussed climate change opportunities, and only 24 addressed physical risks to their assets from climate change.

Another study by the law firm McGuire Woods examining 10-K climate disclosure found significant differences based on company size:

> S&P 500 companies were most likely (as a percentage of companies in the same market capitalization category) to provide disclosure (28.9%), followed by S&P MidCap companies (16.8%), and then S&P SmallCap companies (7.4%).

Here is a summary of the McGuire Woods findings:
The Ceres report examines disclosure of the following key categories of climate risks and opportunities:

**Regulatory Risk and Opportunity:** Regulatory risk and opportunity refers to the consequences of proposed or enacted domestic regulations on a company's operations and financial prospects, such as changes in costs or profits from the sale of emissions credits, costs to comply with regulatory limits on emissions, or impacts from regulation-driven changes in demand for goods and service. Disclosure of the impact of international accords addressing climate change follows the same principles.

**Indirect Consequences or Business Trends:** Legal, economic, or technological developments associated with climate change may create new opportunities or risks by, for example, decreasing demand for goods or energy sources associated with high GHG emissions or increasing demand for “cleaner” products or energy sources, or by increasing competition to develop new products. Good quality disclosure of business trends requires a thoughtful and candid discussion of management’s understanding of how climate change affects its business.

**Physical Impacts:** Significant physical effects of climate change, such as increased incidence of severe weather, rising sea levels, reduced arability of farmland and reduced
water availability and quality, may materially affect a company's operations, competitiveness and results.

**GHG Emissions:** Obtaining data on GHG emissions—including both current emissions and trends over time—is usually necessary for a company’s own efforts to assess its climate change-related risks and opportunities, and for investors assessing a company’s financial condition and prospects. Investors worldwide have expressed a clear desire for standardized emissions reporting by companies.

**Strategic Analysis of Climate Risk and Emissions Management:** The Global Framework for Climate Risk Disclosure calls upon companies to provide analysis that identifies their future challenges and opportunities associated with climate change: specifically, management’s strategic analysis of climate risk, including a clear and straightforward statement about implications for competitiveness. The Global Framework urges companies to disclose a strategic analysis that includes: a statement of the company's current position on climate change; an explanation of all significant actions the company is taking to minimize its climate risk and identify opportunities (emissions management); and corporate governance actions relating to climate change, such as the establishment of any management or board committees to address climate risk.

The Ceres report looks at climate change disclosures by companies in a variety of industries, with an emphasis on large cap companies on the theory they face a larger array of climate risk and opportunity issues than smaller companies. In addition, electric power companies are emphasized in the report because they tend to report more climate change information than other companies.

For every company we found that had “poor” or “fair” disclosure—or no disclosure at all—dozens of similarly situated companies provided similar reporting. We found that “good” disclosure examples were rare, and we found no instances of disclosure we believed should be rated “excellent.” For example, this is how we assessed disclosures of regulatory risk:

**Poor disclosure** of regulatory risks does not mention existing or proposed regulations, or mentions them without analyzing possible effects on the company. For example, Dean Foods Company, a food processor and distributor, stated in its 2009 10-K filing that its “business operations are subject to numerous environmental and other air pollution control laws,” and noted that “various laws and regulations addressing climate change are being considered or implemented at the federal and state levels.” Unhelpfully vague or general references to regulatory risk of this type, often referred to as “boilerplate,” are common in the SEC filings of companies that mention climate change.

**Fair disclosure** of regulatory risk discusses legislation and its possible effects on the company, but makes no attempt to quantify the risks or place amounts in a meaningful context. Southern Company, an electric power company, discussed the possibility of “mandatory [climate change]
requirements related to GHG emissions, renewable energy standards, and energy efficiency standards” but offered only general statements about the financial impacts (compliance costs, capital expenditures, and operating restrictions) of those developments, which the company said “cannot be determined at this time.”

**Good disclosure** of regulatory risk discusses in detail the financial impacts of existing and proposed regulatory requirements on the company. For example, AES Corp., an electric power company, disclosed in its 2009 10-K the anticipated financial impacts of the Regional Greenhouse Gas Initiative (RGGI), a currently operating cap-and-trade regime in the U.S. Northeast: “The Company estimates that the RGGI compliance costs could be approximately $17.5 million per year from 2010 through 2011, when the first RGGI compliance period ends.”

**Indirect Consequences of Regulation or Business Trends**

The SEC Guidance states that “legal, technological, political and scientific developments regarding climate change may create new opportunities or risks for registrants,” by, for example, decreasing demand for goods that produce significant GHG emissions; increasing demand for goods that result in lower emissions than competing products; increasing competition to develop innovative new products; increasing demand for generation and transmission of energy from alternative energy sources; and decreasing demand for services related to carbon-based energy sources, such as drilling services.

Good disclosure of business trends will require a thoughtful and candid discussion of management’s understanding of how climate change is affecting business trends. General statements about possible impacts of climate change are of limited value, but detailed discussions of management’s views of climate change-related trends relevant to the company’s financial position or prospects, or ways in which the economy’s reaction to climate change and GHG regulation may indirectly affect the company’s operations, are more useful to investors.

**An 11-Point Checklist**

This report also includes a checklist to help companies identify, disclose and address climate risks and opportunities:

1. **Integrate consideration of climate risk and opportunity throughout the firm.** Climate change should be part of a company’s **overall sustainability strategy**, and consideration of climate risk should be integrated throughout all relevant components of the firm. Personnel responsible for preparing sustainability strategy and voluntary climate disclosures should be in close communication with those responsible for assessing financial risk and preparing and approving mandatory securities disclosures.
2. **Create a climate management team.** Creating a team of senior managers helps ensure that systematic, **high-level consideration of climate change issues** is integrated throughout a company's operations.

3. **Create a board oversight committee.** Companies should designate a committee of the board to assume **specific responsibility for oversight of climate change**, which, in addition to posing operational and managerial issues, implicates important matters of corporate strategy, reputation and capital investment that are appropriate for board consideration.

4. **Develop internal controls and procedures for gathering of GHG emissions data and other climate change-related information.** Reliable information on firm emissions, physical risks, enacted and proposed regulations, and climate-related initiatives is essential for management analysis, decision-making and disclosure to investors.

5. **Measure, benchmark, and inventory current GHG emissions from operations, electricity use and products.** Calculating emissions is an important first step in evaluating climate risk. A firm cannot, for example, **determine the potential impact** of regulations without knowing what its emissions are.

6. **Calculate past and projected emissions.** Analysis of past and projected future GHG emissions is necessary for a company to **understand its emissions trends** and assess future regulatory or competitiveness risks.

7. **Create specific emissions reduction targets and regularly report on progress.** For firms that adopt goals of reducing GHG emissions, specific, verifiable targets and deadlines provide invaluable means of **focusing employees’ energies on achieving greater energy efficiency** and providing concrete information for investors.

8. **Identify risks and opportunities; then assess materiality.** The heart of effective disclosure is systematic analysis of potential risks and opportunities relating to climate change, and **management's exercise of judgment** on which risks and opportunities are material and therefore require disclosure. Although climate-related risks can be classified in different ways, it is useful to consider them in terms of several broad categories:

   • **Physical risks.** Assess how changes in climate affect the business and its operations, including its supply chain.
   • **Financing and underwriting risks and opportunities.** Firms that insure, reinsure or indemnify properties or operations may be at a higher risk of harm due to climate change.
   • **Regulatory risks and opportunities.** Identify and analyzed regulatory measures that affect the firm's financial position and operations, as well as proposed measures reasonably likely to be enacted.
• **Litigation risks.** Companies must disclose litigation relating to climate change that is material or that satisfies thresholds set out in SEC regulations.

• **Indirect risks and opportunities.** Climate change can materially affect a company's financial position indirectly, such as increasing the costs of energy or by changing patterns of consumer demand.

• **Reputational risks.** Public perceptions about climate change and companies’ responses can importantly affect companies’ reputations and consumer demand for particular products.

• **Emissions.** As previously noted, all companies need to determine their GHG emissions in order to assess their climate risk. GHG emissions data is important to investors for valid comparisons among firms.

9. **Quantify emissions, risks and opportunities whenever possible.** Specific numbers, when reasonably attainable, are preferred over general statements.

10. **Discuss climate risks and opportunities for specific company assets and operations.** Investors interested in how companies will fare in a transitioning to a carbon-constrained world want particularized disclosure of both risks and opportunities, with reference to specific corporate operations, not generic “boilerplate” statements.

11. **Consider investors’ demands when assessing materiality.** The materiality standard that determines what information public companies must disclose ultimately turns on the needs of the “reasonable investor.”


**Follow-up report on oil/gas companies' disclosures**

In a [follow-up report](#), Ceres in 2012 evaluated how 10 of the world’s largest publicly-owned oil and gas companies had disclosed material climate risks and deepwater drilling risks -- in view of the 2010 British Petroleum oil spill in the Gulf of Mexico.

Looking at 2010 annual financial filings, the report rated disclosures as *Good, Fair, Poor or No Disclosure* in eleven categories, based on the SEC's Interpretive Guidance on climate risk disclosure and stated investor climate change disclosure interests. The first six categories dealt generally with climate risk disclosure and the next five with deepwater drilling risks:
Among the Ceres report’s conclusions about these companies’ climate change disclosure: “BP, Eni and Suncor provided relatively better climate risk disclosure than other companies reviewed, while Apache and ExxonMobil provided the lowest quality disclosure. Seven of the companies had poor or no disclosure of their corporate governance related to climate change.”
As to deepwater drilling risks, the Ceres Report concluded: “BP and Total provided relatively better deepwater drilling risk disclosure than the other companies reviewed. It should be noted that companies that have been criticized for inadequate environmental and safety performance scored relatively well on this report. Most notably, BP provided good disclosure in 4 of 5 deepwater drilling categories.”
WASHINGTON — More than two dozen of the nation’s biggest corporations, including the five major oil companies, are planning their future growth on the expectation that the government will force them to pay a price for carbon pollution as a way to control global warming.

The development is a striking departure from conservative orthodoxy and a reflection of growing divisions between the Republican Party and its business supporters. A new report by the environmental data company CDP has found that at least 29 companies, some with close ties to Republicans, including Exxon Mobil, Walmart and American Electric Power, are incorporating a price on carbon into their long-term financial plans.

Both supporters and opponents of action to fight global warming say the development is significant because businesses that chart a financial course to make money in a carbon-constrained future could be more inclined to support policies that address climate change. But unlike the five big oil companies — Exxon Mobil, ConocoPhillips, Chevron, BP and Shell, all major contributors to the Republican party — Koch Industries, a conglomerate that has played a major role in pushing Republicans away from action on climate change, is ramping up an already-aggressive campaign against climate policy — specifically against any tax or price on carbon. Owned by the billionaire brothers Charles and David Koch, the company includes oil refiners and the paper-goods company Georgia-Pacific.

The divide, between conservative groups that are fighting against government regulation and oil companies that are planning for it as a practical business decision, echoes a deeper rift in the party, as business-friendly establishment Republicans clash with the Tea Party.

Tom Carnac, North American president of CDP, said that the five big oil companies seemed to have determined that a carbon price was an inevitable part of their financial future. “It’s climate change as a line item,” Mr. Carnac said. “They’re looking at it from a rational perspective, making a profit. It drives internal decision-making.”
Companies do not know what form a future carbon price would take. Congress could one day vote to directly tax emissions. President Obama is moving forward with plans to regulate carbon pollution from coal plants, with or without action from Congress — and states could carry out those regulations by taxing carbon polluters. At climate change talks at the United Nations, State Department negotiators have pledged that the United States will cut its carbon emissions 17 percent below 2005 levels by 2020, and 80 percent by 2050.

Mr. Carnac said: “Companies see that the trend is inevitable. What you see here is a hardening of that understanding.”

Other companies that are incorporating a carbon price into their strategic planning include Microsoft, General Electric, Walt Disney, ConAgra Foods, Wells Fargo, DuPont, Duke Energy, Google and Delta Air Lines.

During the 2012 election, every Republican presidential candidate but one, Jon Huntsman, questioned or denied the science of climate change and rejected policies to deal with global warming. Opponents of carbon-pricing policies consider them an energy tax that will hurt business and consumers.

Mainstream economists have long agreed that putting a price on carbon pollution is the most effective way to fight global warming. The idea is fairly simple: if industry must pay to spew the carbon pollution that scientists say is the chief cause of global warming, the costs will be passed on to consumers in higher prices for gasoline and electricity. Those high prices are expected to drive the market away from fossil fuels like oil and coal, and toward low-carbon renewable sources of energy.

Past efforts to enact a carbon price in Washington have failed largely because powerful fossil-fuel groups financed campaigns against lawmakers who supported a carbon tax.

In 1994, dozens of Democratic lawmakers lost their jobs after Al Gore, who was vice president at the time, urged them to vote for a climate change bill that would have effectively taxed carbon pollution. In 2009, President Obama urged House Democrats to vote for a cap-and-trade bill that would have required companies whose carbon-dioxide emissions exceeded set levels to buy emissions rights from those who emitted less. The next year, Tea Party groups spent millions to successfully unseat members who voted for the bill.
But Exxon Mobil, which last year was ranked by the Fortune 500 as the nation’s most profitable company, is representative of Big Oil’s slow evolution on climate change policy. A decade ago, the company was known for contributing to research organizations that questioned the science of climate change. In 2010, Exxon Mobil purchased a company that produces natural gas, which creates less carbon pollution than oil or coal.

Exxon Mobil is now the nation’s biggest natural gas producer, meaning that it will stand to profit in a future in which a price is placed on carbon emissions. Coal, which produces twice the carbon pollution of natural gas, would be a loser. Today, Exxon Mobil openly acknowledges that carbon pollution from fossil fuels contributes to climate change.

“Ultimately, we think the government will take action through a myriad of policies that will raise the prices and reduce demand” of carbon-polluting fossil fuels, said Alan Jeffers, an Exxon Mobil spokesman.

Internally, Exxon Mobil now plans its financial future with the expectation that eventually carbon pollution will be priced at about $60 a ton, which Mr. Jeffers acknowledged was at odds with some of the company’s Republican friends.

“We’re going to say and do what’s in the best interest of our shareholders,” he said. “We won’t always be on the same page.”

It remains unlikely that any climate policy will move in today’s deadlocked Congress, but if Congress does take up climate change legislation in the future, Mr. Jeffers said Exxon Mobil would support a carbon tax if it was paired with an equal cut elsewhere in the tax code — the same policy that Mr. Gore has endorsed. “Exxon Mobil and many other large companies understand that climate change poses a direct economic threat to their businesses,” said Dan Weiss, director for climate policy at the Center for American Progress, a liberal research group with close ties to the Obama administration. “They need to convince their political allies to act before it’s too late.”

Koch Industries maintains ties to the Tea Party group Americans for Prosperity, which last year campaigned against Republicans who acknowledged the science of climate change. The company also contributes money to the American Energy Alliance, a Washington-based advocacy group that campaigns against lawmakers that it claims support a carbon price. This year, the American Energy Alliance says it
has spent about $1.2 million in ads and campaign activities attacking candidates who it says support a carbon price.

Robert Murphy, senior economist at the American Energy Alliance, said his group was not concerned that it had taken a different position from the major oil companies. “We’re not taking marching orders from Big Oil,” he said.

In fact, Koch has a longtime resentment of the biggest oil companies.

According to company history, Koch’s founder, Fred Koch, the father of Charles and David, invented a chemical process to more efficiently refine oil but was blocked from bringing it to the market by the nation’s largest oil companies, including Standard Oil of New Jersey, which today is known as Exxon Mobil.

People at Koch say sore feelings remain to this day.

This article has been revised to reflect the following correction:

Correction: January 6, 2014

An article on Dec. 5 about major American corporations’ moves to factor a carbon tax into their long-term financial planning misstated the circumstances that kept Fred Koch, founder of Koch Industries, from bringing a more efficient oil refining process to the market decades ago. The nation’s largest oil companies, including Standard Oil of New Jersey, blocked the process; John D. Rockefeller was not involved in the effort.