Pace International Law Review

Volume 35 | Issue 2 Article 3

May 2023

Determining an Effective Regulatory Framework for Businesses to Report on the Environment, Climate, and Human Rights

Paco Mengual
Elisabeth Haub School of Law at Pace University

Recommended Citation
Paco Mengual, *Determining an Effective Regulatory Framework for Businesses to Report on the Environment, Climate, and Human Rights*, 35 Pace Int'l L. Rev. 224 (2023)
DOI: https://doi.org/10.58948/2331-3536.1428
Available at: https://digitalcommons.pace.edu/pilr/vol35/iss2/3

DETERMINING AN EFFECTIVE REGULATORY FRAMEWORK FOR BUSINESSES TO REPORT ON THE ENVIRONMENT, CLIMATE, AND HUMAN RIGHTS

Paco Mengual

ABSTRACT

The objective of this article is to identify the existing dynamics and clarify the reasoning behind reporting on environmental, climate, and human rights information in search of effective and binding frameworks to enhance transparency. To that effect, this article relates the evolution from a corporate sustainable business focus to reporting on environmental social and governance and increasing corporate accountability. It then expands on defining non- financial information and ESG reporting with regards to recent European Union Regulations (SFDR, Taxonomy) as well as the challenges associated with defining sustainable investments. This article aims to compare and understand the various regulatory strategies and frameworks around the world on environmental, social, and climate-related disclosure. Finally, this article questions the level of reporting on human rights and the relevance of upcoming human rights due diligence laws in the European Union (Corporate Sustainability Reporting Directive) and global initiatives to enhance human rights transparency. In conclusion, this article suggests that an effective reporting framework combines mandatory disclosures, guided reporting rules, and definitions tailored to social and environmental realities to enable companies to demonstrate greater transparency.

Keywords: ESG, corporate law, sustainable business, international law, SDFR, climate disclosure, human rights

TABLE OF CONTENTS

I. INTRODUCTION

Global carbon emissions must be halted by 2025 to limit global warming to 1.5°C and avoid catastrophic climate disruption in the coming decades.[1] The International Panel on Climate Change's Sixth Assessment Report considered a "'code-red' for humanity,"[2] alerting that the global surface temperature will continually increase "until at least mid-century under all [greenhouse gas] emissions scenarios."[3] Total warming will soon exceed 1.5°C-2°C unless a deep cut in CO2 and greenhouse gas emissions occur.[4] Current development patterns are incompatible with long-term sustainability objectives and perpetuate the ecological hazards accelerating climate change.[5]

Sustainability has become an integral part of climate change mitigation strategies.[6] Goal 13 of the United Nations 2030 Agenda, for example, calls for climate action in close connection with the Sustainable Development Goals ("SDGs").[7] All institutions, whether private or public, must commit to immediately employing greater efforts to mitigate climate change. Because consistent, reliable, scientific climate data contributes to making well-informed

---

*Paco Mengual received an LLM in Environmental Law from the Elisabeth Haub School of Law at Pace University in White Plains, New York. He is a French jurist experienced in legal compliance and business ethics in the financial and banking industry as well as within the United Nations organization.

[1] *See* Press Release, Intergovernmental Panel on Climate Change [IPCC], The Evidence is Clear: The Time for Action is Now. We can Halve Emissions by 2030 (Apr. 4, 2021) (on file at https://www.ipcc.ch/report/ar6/wg3/resources/press/press-release/) [hereinafter Press Release, IPCC].

[2] *See IPCC report: 'Code Red' for Human Driven Global Heating, Warns UN Chief*, UN NEWS (Aug. 9, 2021), https://news.un.org/en/story/2021/08/1097362.

[3] Intergovernmental Panel on Climate Change [IPCC], *Climate Change 2021 The Physical Science Basis*, at 14, (Oct. 2021), https://www.ipcc.ch/report/ar6/wg1/downloads/report/IPCC_AR6_WGI_SPM_final.pdf.

[4] Press Release, IPCC, *supra* note 1.

[5] Joyashree Roy et al, *2018: Sustainable Development, Poverty Eradication and Reducing Inequalities*, *in* GLOBAL WARMING OF 1.5°C 450, 452 (V. Masson-Delmotte et al. eds., 2018).

[6] Erling Holden et al, *Sustainable Development: Our Common Future Revisited*, SCI. DIRECT (May 14, 2014), https://www.sciencedirect.com/science/article/pii/S0959378014000727; *see also* World Comm'n on Envt. Dev. [Brundtland Comm'n], *Our Common Future* (1987).

[7] *See Climate Action*, U.N. SUSTAINABLE DEV. (2018), https://www.un.org/sustainabledevelopment/climate-action/ (last visited Jan. 30, 2023).

climate policies, transparency is central to achieving the SDGs.[8] Stakeholders to the Paris Agreement recognize this, accounting for the transparency of implementation measures and the achievement of climate objectives necessary to keep track of global climate action.[9] Under the Paris Agreement, signatory countries are required to regularly report on the implementation and achievement of global objectives in their Nationally Determined Contributions (NDCs), specifically reporting on post-2020 actions to determine long-term objectives and enhance global progress.[10]

The private sector also holds substantial responsibility for climate change, as unsustainable business practices have detrimental impacts on human rights and the environment.[11] Poor industry sector practices, however, can "generate or exacerbate environmental degradation, corruption, conflict and human rights abuses."[12] Additionally, reliance on fossil fuels pushes the human species to the brink of extinction.[13] Aside from consumption patterns, fossil fuel-reliant business practices are at the core of today's environmental injustices, often causing climate change displacement and forced migration.[14] Beyond the climatic benefits of sustainable efforts, Additionally, the economic development occurring in response to effective natural resource management can also work to combat poverty.[15]

For the first time, the Human Rights Council recognized the human right to a clean, healthy and sustainable environment and

---

[8] *See* Candida Rodriguez, *We Won't Win the Fight Against Climate Change Without Transparency*, U.N. DEV. PROGRAM [UNDP] BLOG (2021), https://perma.cc/CY6H-96YK (last visited Jan. 30, 2023).

[9] *See* U.N. Framework Convention on Climate Change, *Introduction to Transparency* (2022), https://perma.cc/4KTG-H9UE (last visited Jan. 30, 2023).

[10] U.N. Framework Convention on Climate Change, *Nationally Determined Contributions (NDCs)* (2021), https://perma.cc/JY9Q-Y3MD (last visited Jan. 30, 2023).

[11] *See* Erika R. George, *Shareholder Activism and Stakeholder Engagement Strategies: Promoting Environmental Justice, Human Rights, and Sustainable Development Goals*, 36 WIILJ 298, 298 (2019).

[12] *Id.*

[13] *See generally* UN Climate Action, *The UN Secretary-General Speaks on the State of the Planet*, U.N., (2021), https://perma.cc/5C93-B923 (last visited May 1, 2022) (describing in December of 2020 the state of the planet, specifically the role of fossil fuels and human activities on the climate and emphasizing a need for reduction of fossil fuel emissions).

[14] George, *supra* note 11 at 1.

[15] *Id.*

called for a global recognition of the interconnected stakes of human rights and climate change.[16]

Recent regulatory developments in ESG disclosure indicate a clear intention to deepen and standardize a favorable framework for reporting and transparency.[17] In the last ten years, the EU has established a comprehensive, normative sustainable finance disclosure framework, intending to expand its requirements for large companies to disclose information on how they operate and manage social and environmental challenges.[18] The US government also recently announced that it will accelerate its efforts to build an economy resilient to climate change and require enhanced climate-related disclosure.[19] Other jurisdictions around the world offer effective and comparable systems based on private and public benchmarks.[20]

A global movement towards greater corporate responsibility in environmental and social matters is underway. Yet, recent international developments with the war in Ukraine highlight two global phenomena that weaken this international momentum. First, global economies are strongly interconnected, and climate change increasingly appears as a systemic threat. Second, foreign fossil fuel reliance suggests that international governmental collaboration is needed to impose tougher sanctions with regards to business and human rights.[21] National regulations on sustainability disclosure are not sufficient alone, but can be strengthened by cooperation and definitional agreements between public and private sectors. The objective of this article is to take a comparative approach to sustainable reporting mechanisms in search of effective and binding frameworks to enhance transparency. To that

[16] *Access to a Healthy Environment, Declared a Human Right by UN Rights Council*, U.N. NEWS (2021), https://perma.cc/EMT6-Q449 (last visited Feb. 1, 2023).
[17] Anilya Krishnan et al., *Regulating ESG Disclosure*, REGUL. REV. (Jan. 28, 2023), https://www.theregreview.org/2023/01/28/saturday-seminar-regulating-esg-disclosure/.
[18] *Sustainable Finance Package*, EUR. COMM'N (2021), https://perma.cc/9DXD-N29M (last visited Feb. 1, 2023).
[19] *Fact Sheet: Biden Administration Roadmap to Build an Economy Resilient to Climate Change Impacts*, THE WHITE HOUSE (2021), https://perma.cc/9A8S-6Q3F (last visited Feb. 1, 2023); *see also* Alex Friedman, *The SEC's Climate Proposal May Fundamentally Change Private Markets*, BARRON'S (Apr. 4, 2022), https://perma.cc/ZA53-ZHLD (last visited Feb. 1, 2023).
[20] *See infra* Part IV.B (*see* footnote 238, discussing the G7 nations agreement on mandatory climate-related disclosures).
[21] Aron Cramer, *Ukraine: the Business Response*, BUS. SOC. RESP. (Mar. 1, 2022), https://perma.cc/7VMA-QY3K (last visited Feb. 1, 2023).

effect, Part II relates the evolution from a sustainable business focus to reporting on environmental, social, and governance information. Part III expands on defining non-financial information and ESG reporting as well as the challenges associated with defining sustainable investments and implementing taxonomies. Part IV exposes the various regulatory schemes within ESG reporting and unravels the dynamics behind mandating climate-related disclosure. Part V questions reporting on human rights due diligence and the relevance of international business and human rights due diligence laws.

II. SUSTAINABLE BUSINESS AND ESG REPORTING

A. *Originating Sustainable Business*

"Business as usual" threatens human existence and jeopardizes human rights.[22] It is *de facto* the antithesis to "sustainable business," referring to doing business without negatively impacting the environment, community, or society as a whole.[23] While "sustainable business" is becoming mainstream,[24] there is, however, no agreed standard or universal definition "for what makes a business 'sustainable.'"[25] Uniform and accurate assessments of sustainable practices facilitate a collective action to measure corporate environmental, social, and governance performance along with sustainability standards.[26] Attempts to discern uniform metrics are hampered by the large number of definitions, rankings, and rating

---

[22] Josephine M. Balzac, *Corporate Responsibility: Promoting Climate Justice Through the Divestment of Fossil Fuels and Socially Responsible Investment*, 47 ENVT. L. REP. 10151, 10151 (Jan. 2017).

[23] *See* Alexandra Spiliakos, *What Does "Sustainability" Mean in Business?*, BUS. INSIGHTS (Oct. 10, 2018), https://online.hbs.edu/blog/post/what-is-sustainability-in-business.

[24] Andrew Winston, *Sustainable Business Went Mainstream in 2021*, HARV. BUS. REV. (Jan. 6, 2022), https://hbr.org/2021/12/sustainable-business-went-mainstream-in-2021.

[25] Becky L. Jacobs & Brad Finney, *Defining Sustainable Business - Beyond Greenwashing*, 37 VA. ENVT. L.J. 89, 90 (2019).

[26] *See id*. at 90-91 (explaining the negative of impacts of failing to achieve uniformity while noting the importance).

systems worldwide,[27] making sustainability a "container term."[28] It becomes interchangeable with other comparably "green" general terms, such as Corporate Social Responsibility (CSR) and Triple Bottom Line (TBL), which aim to consider the people, planet, and financial performance.[29] External rating and indexes use a multitude of sustainability criteria and key performance indicators based on environmental, social, and governance concerns.[30] This density increases confusion for consumers, investors, and the general public about the scope of sustainability.[31] Whether intentional or not, companies take advantage of their alleged sustainable practices and products while not always meeting investor or consumer demands.[32]

However, sustainable business does not only pertain to the definition of sustainable development.[33] It also fits within a long-term perspective.[34] Hence, a sustainable business looks into the future to create both financial and non-financial value.[35] Companies associate sustainable business with economic and social performance.[36] With adequate Corporate Social Responsibility (CSR) policies, they factor social and environmental issues in business operations, taking into consideration stakeholders' concerns.[37] CSR and ESG work to build a positive and socially responsible image of the company while also supporting sustained financial growth and long-term

[27] *See* Alex Davidson, *What's a Sustainable Company? It's Hard to Define*, WALL ST. J. (Apr. 3, 2016, 10:05 PM), https://www.wsj.com/articles/whats-a-sustainable-company-its-hard-to-define-1459735511?cb=logged0.11772449807204644 (showing the disparity across ranking systems for singular entries that leads to confusion).
[28] Colin Myers & Jason J. Czarnezki, *Sustainable Business Law? The Key Role of Corporate Governance and Finance*, 51 ENV'T L. 991, 996 (2022).
[29] *Id.*
[30] *Id.* at 998.
[31] *See* Chris Macdonald, *Sustainability Rankings, the Global 100, and Greenwashing*, BUS. ETHICS BLOG (Feb. 1, 2011), https://perma.cc/2V4E-ZZWA (referring to the term "sustainability" as an "ambiguous" term that "means different things to different people").
[32] *See Eco-Friendly Product Claims Often Misleading*, NPR (Nov. 30, 2007, 12:01 AM), https://perma.cc/8KS8-Y5LZ (outlining the six sins of greenwashing which companies use to convince consumers that their products are "green").
[33] Myers & Czarnezki, *supra* note 28, at 996-97.
[34] *Id.* at 997.
[35] *Id.*
[36] *Id.* at 995, 997.
[37] *What is CSR?*, U.N. INDUS. DEV. ORG. (2021), https://www.unido.org/our-focus/advancing-economic-competitiveness/competitive-trade-capacities-and-corporate-responsibility/corporate-social-responsibility-market-integration/what-csr (last visited Feb 1, 2023).

development.[38] Building on a culture of corporate ethics, sustainable businesses articulate CSR and environmental protection. A successful example of CSR is Socially Responsible Investment (SRI), or sustainable investing.[39]

The screening of investment opportunities with SRI encourages investors to align their financial flows with social and environmental values closer to their ethical standards.[40] The foundation for today's ESG criteria,[41] SRI primarily introduced ethics into the financial sphere through both exclusionary and inclusionary standards.[42] SRI funds seek to guide corporate conduct to address stakeholder concerns based on varying individual and moral considerations.[43] It fostered the development of "social finance," with alternative lending and investment approaches for financing projects that require the projects to generate positive impacts on society, the environment, or sustainable development, as well as improve financial returns.[44] In recent years, increased public attention to issues such as the climate crisis and environmental sustainability

[38] Carl Hung, *Three Reasons Why CSR And ESG Matter To Businesses*, FORBES (Sep. 23, 2021), https://www.forbes.com/sites/forbesbusinesscouncil/2021/09/23/three-reasons-why-csr-and-esg-matter-to-businesses/?sh=5c1d8f0639b9.

[39] *See* GLOB. SUSTAINABLE INV. ALL., GLOBAL SUSTAINABLE INVESTMENT REVIEW 7 (4th ed. 2018) (providing that sustainable investing is defined as an investment approach that considers ESG factors in portfolio selection and management).

[40] *See* Alice Martini, *Socially responsible investing: from the ethical origins to the sustainable development framework of the European Union*, 23 ENV'T, DEV., & SUSTAINABILITY 16881 (2021) (stating that, prior to the American Revolution, religious communities and Quakers refused to invest in "sin stocks" that involved tobacco, alcohol or gambling until the 1970's when SRI practices emerged as part of the Pax World Fund aiming to divest the Vietnam War).

[41] *See generally* Tom Fanter et al., *The History & Evolution of ESG*, RMB CAPITAL (Dec. 15, 2021), https://rmbcapital.com/news-insights/history-evolution-esg (summarizing the history and evolution of ESG).

[42] *See* Martini, *supra* note 40, at 16878; *see* Fanter et al., *supra* note 41, at 16882 (stating, "[o]ne of the first SRI index is The Domini 400 Social Index (now MSCI KLD 400 Social Index) launched in May 1990, a capitalization weighted index of 400 US securities providing exposure to companies with outstanding ESG ratings and excluding companies whose products have negative social or environmental impacts.").

[43] Martini, *supra* note 40, at 16876.

[44] *See* Francesco Rizzi et al., *The Structuring of Social Finance: Emerging Approaches for Supporting Environmentally and Socially Impactful Projects*, 170 J. CLEANER PROD. 805, 805 (2018), https://fardapaper.ir/mohavaha/uploads/2018/04/Fardapaper-The-structuring-of-social-finance-Emerging-approaches-for-supporting-environmentally-and-socially-impactful-projects.pdf (providing examples of social financing approaches include crowdfunding, social impact bonds or micro-financing).

has enhanced SRI's popularity.[45] Green finance exemplifies the mobilization of the banking and financial industries to reconcile financial logic with sustainability.[46] Banking institutions and issuers have dedicated financing techniques, such as green bonds or green loans, enabling them to expand their business strategies and capitalize on growing interest for SRI to maximize performance.[47]

B. ESG and Corporate Accountability

While future climate disruption requires prompt adaptation,[48] CSR increasingly appears as "a public relations tool"[49] because many companies "lack the will or vision" to make systemic changes.[50] On the other end, ESG focuses on a metrics-based approach that allows for corporate accountability.[51] More than a mere vehicle for sustainable finance, ESG becomes an imperative. Companies use ESG data to advance performance management and for external reporting purposes, which investors and other stakeholders use to hold the company responsible.[52] ESG appears as a tool to assess corporate progress on social and environmental performance.[53] In defining metrics and key performance indicators

---

[45] *See* Matthew Blume, *A Beginner's Guide to Socially Responsible Investing*, HARV. BUS. REV. (Dec. 9, 2021), https://perma.cc/8PXY-J6CQ (stating, "[a]t the close of 2020, investors raised a record $12.2 billion in funds that claimed to invest based on environmental, social, and governance (ESG) factors. SRI is estimated to represent $50 trillion in the next 20 years").

[46] *See* Green Financing, UNEP, https://perma.cc/6KUJ-2AWZ (last visited Feb. 6, 2023).

[47] *See* Michael Doran & James Tanner, *Green Bonds' Growing Pains,* 2019 INT'L FIN. L. REV. 22, 22 (Oct./Nov. 2019); *See also* Ryan Chan, *Ensuring Impactful Performance in Green Bonds and Sustainability-Linked Loans*, 42 ADEL. L. REV. 221, 225-226 (2021) (defining "green bonds" as "debt security issued by a government entity, multilateral institution, or corporation in order to raise capital from investors for the financing of green projects, assets, or business activities").

[48] *See* Press Release, Intergovernmental Panel on Climate Change [IPCC], IPCC Sixth Assessment Report Press Release (Feb. 28, 2022), (on file at https://perma.cc/5BAZ-8XLG).

[49] *See* Czarnezki & Myers, *supra* note 28, at 997.

[50] Autumn Spanne, *Corporate Social Responsibility and the Environment: Why It Matters*, TREEHUGGER (June 8, 2021), https://perma.cc/8ACR-CHH6.

[51] *See* Myers & Czarnezki, *supra* note 28, at 998.

[52] *Id.*

[53] *Why ESG is Replacing CSR — and What this Means to Your Business,* NPOWER BUS. SOLS. (Apr. 25, 2020), https://npowerbusinesssolutions.com/resources/blogs/why-esg-is-replacing-csr-and-what-this-means-to-your-business.

(KPIs), companies encompass long-term strategies and use ESG to monitor progress and meet their environmental, social, and governance goals.[54] ESG criteria can account for corporations' actions towards climate change, how they handle their labor force and protect human rights with regards to their supply chain, and more.[55] Because ESG represents accurate sources of potential risk for investors, the integration of ESG criteria into investment strategies is part of "an overall risk analysis aimed at contributing to more stable financial returns."[56]

Over the past two decades, a growing number of investors, both individual and institutional, have paid more attention to ESG criteria in their investment strategies, making ESG an indispensable part of today's business practices.[57] Public and private sector organizations have defined global principles for corporate disclosure and reporting of climate-related risks, albeit voluntarily.[58] Today, most information currently embedded into ESG analysis largely comes from voluntary disclosures or survey responses to rating firm's questionnaires.[59] However, the "lack of comparable, relevant ESG information is a barrier in the transition to a more sustainable economy."[60]

During COP26 in Glasgow, the International Financial Reporting Standards Foundation addressed the need for larger harmonization of ESG criteria,[61] launching the International Sustainability Standards Boards (ISSB), a new set of sustainability disclosure

---

[54] Myers & Czarnezki, *supra* note 28, at 998.
[55] Javier El-Hage, *Fixing ESG: Are Mandatory ESG Disclosures the Solution to Misleading Ratings?*, 26 FORDHAM J. CORP. & FIN. L. 359, 363 (2021); Georg Kell, *The Remarkable Rise of ESG*, FORBES (July 11, 2018, 10:09 AM), https://www.forbes.com/sites/georgkell/2018/07/11/the-remarkable-rise-of-esg/?sh=a4bae2716951.
[56] Martini, *supra* note 40, at 16875.
[57] *Id.*; *see* Inside the Strategy Room, *Why ESG is Here to Stay*, MCKINSEY & Co., at 2:35 (May 26, 2020), https://www.mckinsey.com/capabilities/strategy-and-corporate-finance/our-insights/why-esg-is-here-to-stay (demonstrating that $12 trillion, a quarter of all the assets under management in the United States, are ESG-rated investments which makes this a crucial part of what influences business practices).
[58] Martini, *supra* note 40, at 16875.
[59] *See* El-Hage, *supra* note 55, at 363.
[60] Katie Kummer & Leo van der Tas, *What to Watch as Global ESG Reporting Standards Take Shape*, EY (Nov. 11, 2021), https://perma.cc/35EZ-ZXHY.
[61] *IFRS Foundation Announces International Sustainability Standards Board, Consolidation with CDSB and VRF, and Publication of Prototype Disclosure Requirements*, INT'L FIN. REPORTING STANDARDS FOUND. (Nov 3. 2021), https://perma.cc/WYF9-2B33.

standards to meet investors' information needs and consolidate sustainability disclosure standards.[62] Universal ESG Accounting Standards are the way forward to create uniform standards that integrate all previous standards and frameworks focused on investor needs, promoting a sustainable long-term corporate strategy.[63]

Public institutions have similarly become increasingly concerned with the ESG market and meeting demands.[64] The European Union (EU) set up a comprehensive regulatory framework to put ESG criteria at the heart of the financial system, placing the EU at the forefront of sustainable finance regulation worldwide.[65] Since 2018, the European Commission has also launched several initiatives, including the Action Plan on Financing Sustainable Growth to a New Sustainable Finance Strategy as part of the European Green Deal, and its strategy for financing the transition to a sustainable economy.[66] The EU aimed to make not only the financial sector, but all major economic players, more transparent and accountable for their business practices.[67] Transparency remains a pivotal legislative underpinning of the Non-Financial Reporting Directive (NFRD),[68] which requires large companies with more than five hundred employees - including listed companies, banks, or insurance companies - to publish regular reports on the social and environmental impacts of their activities as related to environmental matters, respect for human rights, and anti-corruption and bribery. On

[62] *Id.*
[63] Robert G. Eccles & Bhakti Mirchandani, *We Need Universal ESG Accounting Standards*, HARV. BUS. REV. (Feb. 15, 2022), https://hbr.org/2022/02/we-need-universal-esg-accounting-standards.
[64] *Making Sense of the Environmental Pillar in ESG Marketing*, OECD ILIBR., https://www.oecd-ilibrary.org/sites/bebb0add-en/index.html?itemId=/content/component/bebb0add-en#section-d1e2331 (last visited Feb. 8, 2023).
[65] *Overview of Sustainable Finance*, EUR. COMM'N, https://finance.ec.europa.eu/sustainable-finance/overview-sustainable-finance_en (last visited Feb. 15, 2023).
[66] *Id.*; *see also Renewed Sustainable Finance Strategy and Implementation of the Action Plan on Financing Sustainable Growth*, EUR. COMM'N (Mar. 8, 2018), https://finance.ec.europa.eu/publications/renewed-sustainable-finance-strategy-and-implementation-action-plan-financing-sustainable-growth_en (discussing the European Union Commission's renewed strategy to support the framework of the European Green Deal).
[67] European Commission Press Release IP/22/1145, Just and Sustainable Economy: Commission Lays Down Rules for Companies to Respect Human Rights and Environment in Global Value Chains (Feb. 23, 2022).
[68] Directive 2014/95/EU, of the European Parliament and of the Council of 22 Oct. 2014 Amending Directive 2013/34/EU as Regards Disclosure of Non-Financial and Diversity Information by Certain Large Undertakings and Groups, 2014 O.J. (L 330) 1, 1.

April 21, 2021, the Commission issued its proposal for a Corporate Sustainability Reporting Directive (CSRD) to extend NFRD's scope to all large companies listed on regulated markets, audit reported information, and introduce more detailed reporting requirements.[69] Financial players are already subject to the Sustainable Finance Disclosure Regulation (SFDR), which requires them to integrate sustainability risks and consider adverse sustainability impacts with regards to their financial products.[70] To help identify sustainable investments, the EU Taxonomy regulation provides criteria for determining whether an economic activity qualifies as environmentally sustainable.[71] It applies not only to all large companies and financial market participants, but also to all decisions taken by the EU, member states, or governmental bodies.[72] For a business to qualify as "environmentally sustainable," its business practices must align with the UN Guiding Principles on Business and Human Rights (UNGPs) and the OECD Guidelines for Multinational Enterprises, which together establish a mandatory framework for EU human rights due diligence law.[73]

In contrast to the European approach, ESG criteria gradually became prominent in the United States within a purely self-determined environment.[74] In the U.S., some form of reporting is required, as public companies must disclose information on environmental, labor, and human rights practices.[75] A number of targeted

[69] *Corporate Sustainability Reporting*, EUR. COMM'N (2022), https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en#standards (last visited Feb. 15, 2023); *Sustainable Finance Package*, EUR. COMM'N (Apr. 21, 2021), https://finance.ec.europa.eu/publications/sustainable-finance-package_en#csrd (last visited Feb. 19, 2023).

[70] Commission Regulation 2019/2088 of Nov. 27, 2019, Sustainability-related Disclosures in the Financial Services Sector, 2019 O.J. (L 317) 1, 7 [hereinafter *Commission Regulation, Sustainability-related Disclosures*].

[71] Commission Regulation 2020/852 of June 18, 2020, Establishment of a Framework to Facilitate Sustainable Investment, and Amending Regulation (EU) 2019/2088, O.J. (L 198) 13, 22 [hereinafter *Commission Regulation, Framework for Sustainable Investment*]

[72] *Id.* at 17.

[73] Thomas Voland et al., *The EU Taxonomy Regulation – A Market Standard of Human Rights Due Diligence?*, CLIFFORD CHANCE (Nov. 10, 2020), https://perma.cc/JRJ7-B2R2.

[74] Talib Visram, *ESG Investing Continued to Soar in 2021. The Government Could Boost it Even More*, FAST CO. (Dec. 28, 2021), https://perma.cc/U87D-ZT65 (providing that ESG funds were particularly resilient during the COVID-19 pandemic, demonstrating its resilience in the face of external threats and pressures).

[75] *See* Virginia Harper Ho, *"Comply or Explain" and the Future of Nonfinancial Reporting*, 21 LEWIS & CLARK L. REV. 317, 323 (May 13, 2017).

sustainability-related disclosure regulations are implemented at the state and federal level.[76] U.S. companies are required to establish monitoring and reporting systems, such as the greenhouse gas emissions disclosure for large emitters as demanded by the Environmental Protection Agency (EPA).[77] However, these requirements only provide partial information to measure ESG risks for investors, who have difficulty integrating this information into investment analysis, largely due to the lack of enacted uniform ESG disclosure regulations.[78]

ESG factors are often associated with risk analysis, with legal, regulatory, and reputational risks considered as significant factors of financial and market risk subject to disclosure.[79] The Security and Exchange Commission (SEC) has a greater responsibility to regulate ESG and provide accurate information to the financial markets.[80] The Commission's focus has consistently aimed to protect investors and ensure the market's efficient operation while requiring public companies to regularly publish information relevant to investors to help them make informed decisions about their investments.[81] The SEC requires public companies to complete Form 10-K, which ensures disclosure of material information to investors.[82] Gradually, the commission went from rejecting investor's demands for mandatory environmental and social disclosures to admitting the materiality of climate change for issuers.[83] The SEC periodically evaluates, when contextually related to the integrated disclosure system, its regulation of climate change disclosures.[84] In March 2021, the SEC created the "Climate and ESG Task-Force" in

[76] *See* Myers & Czarnezki, *supra* note 28, at 1015.
[77] *Greenhouse Gas Reporting Program (GHGRP)*, EPA, https://www.epa.gov/ghgreporting (Jan. 6, 2023).
[78] *See Commission Regulation, Sustainability-related Disclosures*, *supra* note 70.
[79] *Id.*
[80] John Coates, *ESG Disclosure - Keeping Pace with Developments Affecting Investors, Public Companies and the Capital Markets,* SEC (Mar. 11, 2021), https://www.sec.gov/news/public-statement/coates-esg-disclosure-keeping-pace-031121.
[81] *See* Myers & Czarnezki, *supra* note 28, at 1009-10.
[82] *Id.*
[83] *See generally id.* at 1010 (explaining the SEC's process for determining materiality and informing investors of such).
[84] Allison Herren Lee, *Public Input Welcomed on Climate Change Disclosures*, SEC (Mar. 15, 2021), https://www.sec.gov/news/public-statement/lee-climate-change-disclosures.

the Division of Enforcement.[85] The key goal of the Task Force is to identify any material gaps, misstatements, or compliance issues in the disclosures of climate risks put forth by investment advisers and funds, as well as monitoring their ESG strategies.[86] With academics and market participants advocating for some form of mandatory ESG disclosure, no federal legislation has successfully passed Congress.[87] President Biden's May 2021 Executive Order, however, requires federal agencies to develop comprehensive climate risk strategies to identify and disclose climate-related financial risks to government programs, assets, and liabilities.[88] Although the strategy should be in line with fulfilling net-zero by 2050, the SEC is focused on creating rules to implement mandatory climate-related risk disclosure.[89]

III. DEFINING ESG REPORTING

Comprehensive efforts are being made in the EU and in the U.S., but also in many other jurisdictions around the world, to regulate ESG disclosure and reporting.[90] To better understand ongoing regulatory dynamics, this discussion follows with a preliminary analysis of non-financial information and reporting. To enforce reporting regulations suited to the concerns of investors, issuers, or any company subject to such rules, jurisdictions need to design a consistent framework for defining what reporting is and what information should be disclosed up front. Although they may positively influence participants' conduct and promote transparency, sustainable finance and taxonomy regulations shed light on the complexities and mismatches that may persist between the perception of public institutions and the reality experienced by those involved.

A. Defining a Regulatory Framework for Reporting

[85] Press Release, U.S. Securities and Exchange Commission, SEC Announces Enforcement Task Force Focused on Climate and ESG Issues (Mar. 4, 2021), https://www.sec.gov/news/press-release/2021-42.
[86] *Id.*
[87] *See* El-Hage, *supra* note 55, at 390.
[88] Climate-Related Financial Risk, 86 Fed. Reg. 27967, 8 (May 20, 2021).
[89] *See infra* Part IV. C. 1.
[90] Graham Caswell, *G7 Nations Agree on Mandatory Climate-related Disclosure*, GREEN CENT. BANKING (June 8, 2021), https://perma.cc/3EUA-E6XZ.

Defining Non-Financial Information

Reporting non-financial information reflects an increased awareness of corporate social responsibility.[91] It can be viewed both as a communication mechanism between the company and its stakeholders as well as a source of valuable information for investors' decision-making, enabling them to assess the value of the company.[92] More than a mere performance indicator, the publication of social and environmental information in the financial report meets external expectations of stakeholders, including customers, suppliers, employees, local authorities, NGOs, and the public.[93] In recent years, non-financial reporting has widely expanded, with varying definitions across public and private institutions.[94] Over the past ten years, more than sixty governments, international institutions, and organizations have encouraged non-financial reporting and offered a set of definitions and indicators.[95] Diversity of non-financial reporting comprises rather heterogeneous underlying concepts, potentially creating a sense of confusion.[96] Sustainability, ESG, non-financial, CSR, and integrated reporting are some examples of the many forms in which reporting can occur.[97]

The following reviews various definitions provided by Monciardini et al. in their article on "Rethinking Non-Financial

[91] *See* David Monciardini et al., *Rethinking Non-Financial Reporting: A Blueprint for Structural Regulatory Changes*, 10 ACCT. ECON. & L. 1, 25 (2020), https://doi.org/10.1515/ael-2020-0092 (highlighting the "emerging EU regime for corporate social and environmental accountability).

[92] *Communication from the Commission to the European Parliament, The Council, The European Economic and Social Committee and the Committee of the Regions*, at 11, COM (2011) 681 final (Oct. 25, 2011).

[93] *Id.* at 3.

[94] *See* Hervé Stolowy & Luc Paugam, *The Expansion of Non-financial Reporting: An Exploratory Study*, 48 ACCT. & BUS. RSCH. 525, 525 (2018) (providing that recent years have seen a rapid expansion in non-financial reporting).

[95] *See* Virginia Harper Ho & Stephen Kim Park, *ESG Disclosure in Comparative Perspective: Optimizing Private Ordering in Public Reporting*, 41 U. PA. J. INT'L L. 249, 252-54 (2019) (providing that the United Nations, the OECD, the G20, the International Organization of Securities Commissions (IOSC) and the International Accounting Standards Boards (IASB) have all implemented some type of non-financial reporting measures or guidelines).

[96] *See* Monciardini et al., *supra* note 91, at 8 (stating that there are a variety of reporting mechanisms employed internationally).

[97] *Id.* at 19 (discussing the confusion that resulted from use of various terms such as ESG, sustainability, social and environmental reporting).

Reporting" to illuminate contradictions, divergent perspectives, and dynamics that may arise when using such reporting as means of clarifying reporting strategies.[98] For instance, GRI's definition of sustainability reporting is the "organization's practice of reporting publicly on its economic, environmental, and/or social impacts, and hence its contributions – positive or negative – towards the goal of sustainable development."[99] Although the focus is on sustainable development, the Sustainability Accounting Standards Board (SASB) extends this definition.[100] SASB relates to sustainability as the

> [ESG] dimensions of a company's operation and performance…[including] both the management of a corporation's environmental and social impacts, as well as the management of environmental and social capitals necessary to create long-term value. It also includes the impact of environmental and social factors on innovation, business models and corporate governance.[101]

Deloitte and the Integrated Reporting Framework (IIRC), on the other hand, provide a very narrow definition of a non-financial report.[102] IIRC, for example, defines an integrated report as a "concise communication about how an organization's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation…of value over the short, medium and long term."[103] It is the combination of financial statements and sustainability reports into a coherent whole that explains the company's ability to create value as the process of integrated reporting.[104] Corporate Social Responsibility reporting simply incorporates CSR principles into a report as narrated by the European Commission.[105]

From a holistic perspective, the EU's Non-Financial Reporting Directive defines non- financial information as the "information to the extent necessary for an understanding of the group's

---

[98] *See id.*
[99] GRI 101: FOUNDATION 2016 3 (Glob. Reporting Initiative 2018).
[100] Monciardini et al., *supra* note 91, at 11.
[101] SUSTAINABILITY ACCT. STANDARDS BD., CONCEPTUAL FRAMEWORK OF THE SUSTAINABILITY ACCOUNTING STANDARDS BOARD 7 (2013).
[102] *A Directors' Guide to Integrated Reporting*, DELOITTE 9-11 (2015), https://www2.deloitte.com/content/dam/Deloitte/na/Documents/audit/na_za_Directors_Guide_on_Integrated_Reporting.pdf; *International <IR> Framework*, INTEGRATED REPORTING 10 (2021), https://perma.cc/R2KQ-DSAB.
[103] *International <IR> Framework*, *supra* note 102, at 10.
[104] *See* Monciardini, *supra* note 91, at 5.
[105] *Id*. at 19.

development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti- corruption and bribery matters[…]".[106] It is not limited to environmental, social, and governance aspects and specifically addresses human rights, anti-corruption, and bribery while considering company's conduct, performance, and the impact of their activities.[107] The EU's definition provides a blueprint for non-financial reporting regulations placing the emphasis on the *raison d'être* (purpose) of these companies.[108] It incorporates potential environmental and social impacts of companies into a more sophisticated regulatory framework.[109]

Reporting on Potential Adverse Impacts

Most academic writings use "ESG reporting," "sustainability reporting," and "disclosures" interchangeably, since these terms are easily identifiable rather than the mere non-financial information no longer reflective of actual needs and concerns.[110] The European Commission's recent proposal for a Corporate Sustainability Reporting Directive (CSRD) no longer refers to non-financial information.[111] Instead, Article 3 of the proposal incorporates new definitions, such as "adverse environmental impact" resulting from a violation pursuant to international environmental conventions, or "adverse human rights impact" on protected persons resulting from the violation of international conventions on human rights.[112] "Severe adverse impacts" refer to both environmental and human rights violations, "especially significant by its nature, or affects a

[106] *Id.* at 23, fn 56.
[107] *What is the EU Non-Financial Reporting Directive?*, ASSENT.COM, https://www.assent.com/resources/knowledge-article/what-is-the-eu-non-financial-reporting-directive/ (last visited Feb. 16, 2023).
[108] Non-financial Reporting Directive, EUR. PARL. DOC. PE 654.213 (2021).
[109] *Id.*
[110] *See* Grazia Cafagna & Fabrizio Tocchini, *The ABCs of ESG reporting: What are ESG and Sustainability Reports, Why are They Important, and What do CFOs Need to Know*, WOLTERS KLUWER (Mar. 9, 2022), https://www.wolterskluwer.com/en/expert-insights/the-abcs-of-esg-reporting.
[111] *Proposal for a Directive of the European Parliament and of the Counsel on Corporate Sustainability Due Diligence and amending Directive (EU) 2019/1937*, COM (2022) 71 final (Feb. 23, 2022).
[112] *Id*. art. 3.

large number of persons or a large area of the environment, or which is irreversible, or is particularly difficult to remedy."[113]

CSRD enriches NFRD with the most recent climate agreements and commitments, such as the European Climate Law,[114] the Glasgow Climate Pact[115] and recent EU corporate due diligence obligations.[116] The EU regulation regards adverse impacts of businesses as a significant step forward to fight greenwashing.[117] One of the objectives of SFDR is to require financial market participants and financial advisers to disclose "specific information regarding their approaches to the integration of sustainability risks and the consideration of adverse sustainability impacts."[118] The emerging Principle Adverse Impacts, or "PAI" regime, is a particularly challenging aspect of SFDR.[119] It will mandate certain firms to disclose relevant ESG metrics, such as emissions.[120] Article 4 of SFDR requires financial market participants to publish and maintain a statement on their websites on whether and why or why not they consider PAIs in their investment decisions, including, where relevant, information as to whether and when they intend to consider such adverse impacts.[121] SFDR also distinguishes between certain types of firms for publishing these PAIs.[122] As part of the Level 1 regulation,

---

[113] *Id*. art. 3, at (l).
[114] *See* Regulation 2021/1119 of the European Parliament and of the Council of 30 June 2021 establishing the Framework for Achieving Climate Neutrality and amending Regulations (EC) No 401/2009 and (EU) 2018/1999 ('European Climate Law') PE/27/2021/REV/1, OJ (L 243).
[115] *See "Glasgow Climate Pact"* - Conference of the Parties Serving as the Meeting of the Parties to the Paris Agreement to the Framework Convention on Climate Change, Oct. 31-Nov. 12, 2021, FCCC/PA/CMA/2021/L.16.
[116] *See generally* Resolution 474/11, of the European Parliament of 10 March 2021 with Recommendations to the Commission on Corporate Due Diligence and Corporate Accountability, 2021 O.J. (C 474/02) A (showing similar language to the other EU documents cited in this statement to link international corporate finance with environmental goals).
[117] *See* Hortense Bioy, *Will the SFDR Prevent Greenwashing?*, MORNINGSTAR UK (June 29, 2021), https://www.morningstar.co.uk/uk/news/213385/will-the-sfdr-prevent-greenwashing.aspx (explaining how the SFDR requirements bring this about).
[118] Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 Nov. 2019 on Sustainability-related Disclosures in the Financial Services Sector 2019 O.J. (L 317) 8.
[119] Yannick Arbaut et al., *New SFDR Principal Adverse Impacts (or PAI) Regime – Key Points*, JD SUPRA (Aug. 3, 2021), https://perma.cc/HF7R-7UZ6.
[120] *Id.*
[121] *Id.*
[122] *See id.* (noting that the "opt out" option no longer applies from June 30th 2021 to participants with more than 500 employees that must publish and

which entered into force on March 10, 2021, financial market participants need to disclose information in the form of a narrative statement.[123] They must then disclose the sustainability features of their financial products, within pre-contractual agreements and prospectuses by June 30, 2023.[124] Regulatory Technical Standards submitted by the European Supervisory Authorities provide fourteen key indicators with nine indicators related to the environment and five covering social factors for assessing adverse sustainability impacts.[125] Participants must also report at least one additional environmental indicator and one additional social indicator.[126] SFDR appears to create a substantial administrative burden to meet this disclosure requirement,[127] but its normative impact is far-reaching for financial market participants.[128] By including the definition and disclosure of potential adverse impacts, SFDR primarily requires companies to "make strategic decisions about their approach to sustainability."[129] To disclose a product's sustainability impact, for example, participants would need to decide whether and how to measure the impact of the product, whether the established measurement system is effective, and whether there are products in place to minimize PAIs.[130]

B. *Defining Sustainable Investments*

maintain on their websites a statement on their due diligence policies with regards to PAIs).

[123] Anne Schoemaker, *Momentum Around Principal Adverse Impact Data Remains Strong Despite SFDR Delays*, SUSTAINALYTICS (Nov. 2, 2021), https://perma.cc/F2DD-HWGR.

[124] *EU: Commission Delays SFDR RTS Implementation to 2023*, BAKER MCKENZIE (Dec. 8, 2021), https://perma.cc/M33K-9VRY.

[125] *Final Report on Draft Regulatory Technical Standards*, at 60-64 (2021), https://www.esma.europa.eu/sites/default/files/library/jc_2021_03_joint_esas_final_report_on_rts_under_sfdr.pdf.

[126] *Id.* at 13.

[127] David Henry Doyle, *What is the Impact of the EU Sustainable Finance Disclosure Regulation (SFDR)?*, S&P GLOB. (Apr. 1, 2021), https://www.spglobal.com/marketintelligence/en/news-insights/blog/what-is-the-impact-of-the-eu-sustainable-finance-disclosure-regulation-sfdr (last visited Feb. 21, 2023).

[128] *Id.*

[129] *Id.*

[130] *Id.*

Determining a Taxonomy

Companies need clear-cut definitions and benchmarks to rely upon and disclose relevant information. Interpretation of the terminology should leave as little ambiguity as possible, as national legislations set the course of action for these companies and guide their performance to meet climate commitments. The recent introduction of Taxonomy and SFDRs paves the way for increased caution on the regulatory side to define sustainable products.[131] SFDR offers specific definitions for the first time in EU law, including not only "sustainable investment," referred to as an investment within an economic activity that contributes to an environmental or social objective, but also "sustainability risk" and "sustainability factors."[132] However, regulations are not sufficiently precise in their definitions in connection with the taxonomy, creating serious descriptive and reporting hardships for financial market participants. Article 8 of SFDR introduces "light green products" which are products that promote environmental or social characteristics.[133] Article 9 of SFDR introduces "dark green" products, more demanding, with a sustainable investment strategy aligned with the taxonomy's environmental objectives.[134] All other products not falling under the category of Articles 8 and 9 are subject to Article 6, which requires integration of sustainability risks.[135] However, the "vague" definition of Article 8 funds under SFDR may increase the risk of greenwashing, a growing concern in the market.[136] Only one year after the implementation of SFDR in March 2021, Article 8 is

[131] *Commission Regulation, Sustainability-related Disclosures*, *supra* note 70, at 5, ¶ 21.
[132] *Id.* at 9, ¶ 24 ("'Sustainability factors' mean environmental, social and employee matters, respect for human rights, anti- corruption and anti-bribery matters").
[133] *See Sustainable Finance Disclosure Regulation - Article 8 Funds or "Light Green Funds"*, DELOITTE (2021), https://perma.cc/Q2P9-YC7P (giving a broad definition on what constitutes an Article 8 fund).
[134] *See EU Sustainable Finance Disclosure Regulation Article 8/9 "Cheat Sheet"*, EVERSHEDS SUTHERLAND
(2021), https://perma.cc/XH3N-2DR7 (last visited Mar 5, 2023) (showing a table describing what is categorized as article 8 and 9).
[135] *Commission Regulation, Sustainability-related Disclosures*, *supra* note 70.
[136] *See* Tom Eckett, *SFDR: "Vague" Article 8 Definition Increases Risk of Greenwashing*, ETF STREAM (2021), https://perma.cc/8ANG-6Y8S (last visited Mar 5, 2023) (describing how SFDR defines "Article 8 Funds" as "promoting ESG characteristics).

already becoming a "catch-all category" and the definition of these products largely remains subjective.[137] SFDR's objective to tackle greenwashing is a semi-tinted result.[138] Despite a notable growth of Article 8 and 9 products in the European market in 2021, the reclassification of products not subject to these categories led asset managers to simply formalize an existing ESG process or apply a "light touch" for their products to fall into these categories.[139] In addition, fossil fuel exposure in Article 8 and 9 funds increased in late 2021 since investors directed their investments towards "transitioning companies," including oil and gas companies that pledged to move away from carbon intensive activities and sett net-zero emission targets, as well as utilities that are involved in renewable energy but also partially operate fossil fuel businesses.[140] Clarification is expected from EU regulators in setting minimum standards for these products.[141]

Originally, the introduction of the Taxonomy Regulation was a major step in defining established standards for sustainable investments. The EU taxonomy aims to facilitate a secure environment for investors, protect them from greenwashing, help all businesses to conduct climate-friendly operations, mitigate market fragmentation, and help shift investments to impulse the ecological transition.[142] To that end, the Taxonomy enumerates six environmental objectives: climate change mitigation, climate change adaptation; the sustainable use and protection of water and marine resources; the transition to a circular economy; pollution prevention and control; the protection and restoration of biodiversity and;

---

[137] *Id.*; *See* Susanna Rust, *SFDR Article 8 Fund Label Questionable in 20% of Cases, Analysis Suggests*, IPE (2022), https://perma.cc/7LH3-L35D.
[138] *Id.*
[139] *See* Dominic Webb, *SFDR Reclassifications Raise "Legitimate" Greenwashing Concerns, Warns Morningstar*, RESPONSIBLE INV.(2022), https://perma.cc/8SB3-WKG5; *See also* Nathalie Kenway, *One Year on from SFDR: More Confusion and Greenwashing?*, ESG CLARITY (2022), https://perma.cc/D6PZ-DH32 (explaining how Morningstar expects AUM and Article 8/9 funds to increase).
[140] Webb, *supra* note 139.
[141] *See* Michael Sholem, *Supervisory Statement on the Application of the EU Sustainable Finance Disclosure Regulation and the EU Taxonomy Regulation*, JD SUPRA (2022), https://perma.cc/7LPM-ZVST (providing that, on March 25th, 2022, the three main European supervisory authorities – EBA, ESMA and EIOPA published a joint statement on the application of SFDR and provide new guidance on the application of SFDR and Taxonomy).
[142] *The EU Taxonomy: What is the Impact for Investors and Corporates?*, BNP PARIBAS (Nov. 16, 2021), https://perma.cc/EK24-TT3V.

ecosystems, all of which have definitions reproduced in the text.[143] To be considered environmentally sustainable, an economic activity must contribute significantly to one of the six objectives or more, not harm any of the objectives, and be carried out in compliance with minimum guarantees set forth by the regulation.[144] The first section of the Taxonomy applies to all participants since January 1, 2022. U.S. or foreign investors may use the Taxonomy to assess whether a potential investment supports an "environmental objective," such as adaptation to or mitigation of climate change, despite being non-binding on non-EU financial market participants.[145] The philosophy of this taxonomy since the EU implemented their comprehensive Sustainable Finance Regulation Framework was never to provide a mere enumerative list of green assets, but rather to offer a flexible, dynamic model that considers technological and scientific changes while maintaining market integrity.[146] However, recent implementation of the Taxonomy regulation unveils actual discord as what to include as a sustainable investment making it even more of an uphill battle for concerned participants.[147]

On February 2, 2022, the European Commission adopted a Complementary Climate Delegated Act (the "CCDA") and included natural gas and nuclear power in the taxonomy, prompting a fierce debate between member states to determine which activity should be described as sustainable.[148] The Act is a continuation of

[143] *Commission Regulation, Framework for Sustainable Investment*, *supra* note 71, at 13, 17.
[144] David Henry Doyle, *A Short Guide to the EU's Taxonomy Regulation*, S&P GLOB. (May 12, 2021), https://www.spglobal.com/esg/insights/a-short-guide-to-the-eu-s-taxonomy-regulation.
[145] Alexandra Farmer & Sarah Thompson, *The Ripple Effect of EU Taxonomy for Sustainable Investments in U.S. Financial Sector,* HARV. L. SCH. F. CORP. GOVERNANCE (June 10, 2020), https://perma.cc/JJF5-KCS7.
[146] *See generally Sustainable Finance Package*, *supra* note 18 (explaining the purpose, which touches on how the act intends to provide the necessary framework that allows investors to re-orient themselves based on that framework).
[147] *See* Hadewych Kupier, *Current Implementation of EU Taxonomy Leads to Distorted Picture*, TRIODOS INV. Mgmt. (Aug. 2, 2022), https://www.triodos-im.com/articles/2022/current-implementation-of-eu-taxonomy-leads-to-distorted-picture (showing that there is indication of confusion between what is a sustainable activity and what is not, going so far as to indicate that the framework itself contains activities that are non-sustainable, which would easily fuel further confusion).
[148] *EU Taxonomy: Complementary Climate Delegated Act to Accelerate Decarbonisation*, EUR. COMM'N (Feb. 2, 2022), https://finance.ec.europa.eu/publications/eu-taxonomy-complementary-climate-delegated-act-accelerate-decarbonisation_en; *E.U. Lawmakers Classify Natural Gas and Nuclear as Sustainable Energy Investments*, PBS NEWS HOUR (July 6, 2022),

the rules establishing green economic activities under taxonomy published in April 2021, but the European Commission delayed its decision on whether to incorporate natural gas and nuclear power.[149] The commission's Complementary Climate Delegated Act now sets out strict conditions, subject to which certain nuclear and gas activities can be added as transitional activities.[150] These activities must contribute to the transition to climate neutrality; for nuclear power, it must fulfill nuclear and environmental safety requirements; and for gas, it must contribute to the transition from coal to renewables, introducing additional specific disclosure requirements for businesses related to their activities in gas and nuclear energy sectors.[151] Some countries in the EU heavily rely on fossil fuels by using natural gas as a transient power source, and while France has most of its electricity coming from nuclear energy, Germany is currently closing their nuclear power plants.[152] All of this is taking place in a context of soaring energy prices exacerbated by the ongoing conflict in Ukraine, which began in February 2022.[153] The EU also signed the pledge at COP 26 to accelerate the transition and phase-out from coal energy.[154] Although the debate has little influence on asset manager's conduct over ESG investment,[155] it sheds light on the current challenges of managing the energy transition and emphasizes how sustainable finance taxonomies drive the path towards clean energy and climate neutrality.

With regards to SFDR, financial market participants must explain how to use taxonomy in order to determine the sustainability of their investments. However, Article 9 products aim to reduce carbon emissions and may have to specifically exclude gas and

https://www.pbs.org/newshour/world/e-u-lawmakers-classify-natural-gas-and-nuclear-as-sustainable-energy-investments.

[149] Sanne Wass, *EU Publishes 1st Green Taxonomy Criteria, Delays Decision on Gas and Nuclear*, S&P GLOBAL (Apr. 21, 2021), https://perma.cc/7Q78-ZZFB.

[150] Press Release, European Commission, EU Taxonomy: Commission Presents Complementary Climate Delegated Act to Accelerate decarbonisation (Feb. 2, 2022) (on file with author).

[151] *Id.*

[152] Jennifer Laidlaw, *What the Inclusion of Gas and Nuclear in the EU Taxonomy Could Mean for Investors and Asset Managers*, S&P GLOBAL (Feb. 22, 2022), https://perma.cc/WV6N-57XM.

[153] *Id.*

[154] Nikos Tsafos, *The Battle for Coal at COP26*, CSIS (Nov. 15, 2021), https://www.csis.org/analysis/battle-coal-cop26.

[155] Laidlaw, *supra* note 152 (discussing the fact that many investors already exclude fossil fuels from their portfolios, adding that nuclear has increasingly been excluded from many portfolios since the 2011 nuclear disaster in Fukushima, Japan).

nuclear exposure.[156] Likewise, Article 8 products are dominant among European ESG funds, but may have their natural gas exposure increase.[157] Ultimately, regulations would have to be amended in the near future to reflect economic, political, and transitional developments.[158]

C. *International Initiatives to Implement Sustainability Taxonomies*

The EU's Sustainable Finance framework, however, is widely praised and influences other jurisdictions around the world.[159] As an example, within the EU, France already issued its own reporting requirement specific to biodiversity aligning with the EU's taxonomy.[160]

Article 29 of the law on Energy and Climate provides details on expected disclosures across both biodiversity and climate. It requires financial institutions to publish information on the portion of their assets complying with the environmental criteria set out in the EU Taxonomy.[161]

---

[156] *Id.*
[157] *Id.*
[158] *See Eurosif Statement on Risks Arising from Inclusion of Natural Gas & Nuclear Energy in the EU Taxonomy*, EUROSIF (2021), https://www.eurosif.org/news/eurosif-statement-on-risks-arising-from-inclusion-of-natural-gas-nuclear-energy-in-the-eu-taxonomy/ (highlighting that Eurosif warned that the inclusion of nuclear and natural gas energies in the taxonomy would require "rethinking the SFDR reporting"); *see also The Inclusion of Gas and Nuclear Undermines the Credibility of the EU Taxonomy*, EUROSIF (2022), https://www.eurosif.org/news/the-inclusion-of-gas-and-nuclear-undermines-the-credibility-of-the-eu-taxonomy/.
[159] Cédric Merle & Garnik Gondjian, *Sustainable Taxonomy Development Worldwide: a Standard-Setting Race Between Competing Jurisdictions*, NATIXIS CORP. & INV. BANKING (2021), https://gsh.cib.natixis.com/our-center-of-expertise/articles/sustainable-taxonomy-development-worldwide-a-standard-setting-race-between-competing-jurisdictions.
[160] *See* Décret n° 2021-663 du 27 mai 2021 pris en application de l'article L. 533-22-1 du code monétaire et financier [Decree no. 2021-663 of 27 May 2021 implementing Article L.533-22-1 of the Monetary and Financial Code], J. OFFICIEL DE LA REPUBLIQUE FRANCAISE [J.O] [OFFICIAL J. OF THE FRENCH REPUBLIC], May. 28, 2021 (adopting EU regulation on "sustainability-related disclosures in the financial services sector.")
[161] *France's Law on Energy and Climate Adds Coverage of Biodiversity, Ecosystems, and Renewable Energy to Investors' Non-Financial Reporting*, GREEN FIN. PLATFORM (2021) [hereinafter *France's Law on Energy and Climate*], https://perma.cc/N6PJ-AKLA.

A decree was issued in May 2021 to implement Article 29, using double materiality to require the disclosure of biodiversity- and climate-related risks,[162] with financial institutions required to disclose their strategies for reducing biodiversity impacts, meeting specific targets, and measuring compliance with international biodiversity goals.[163] For some years now, China has worked to identify green investments, and although there is no strict definition or taxonomy as such, the People's Bank of China released the 2021 edition of Green Bond, which was endorsed Project Catalogue to provide key uniform regulations for China's green bond market.[164] The Catalogue covers main classes of sustainable activities: energy conservation, pollution prevention and control, resource conservation and recycling, clean transportation, clean energy, ecological protection, and climate change adaptation.[165] On November 4, 2021, the International Platform on Sustainable Finance published a Common Ground Taxonomy (CGT), a comparative study of the green taxonomies of China and the EU.[166] However, this report does not intend to create a common or single taxonomy, but rather seeks to identify areas with overlaps and compare their objectives, eligibility criteria, activities and threshold.[167] The CGT is a first attempt to mitigate the fragmentation of sustainable finance taxonomies and work together with jurisdictions to improve the clarity and usability of these frameworks globally for future taxonomies.[168] As part of its ongoing sustainable finance initiative, South Africa's National

[162] *See What is "Double Materiality" and Why Should You Consider it?*, GREENSTONE PLUS (2021), https://perma.cc/PTH4-HBB2 ("The concept of double materiality acknowledges that a company should report simultaneously on sustainability matters that are financially material in influencing business value and material to the market, the environment, and people"); *See also* Matthias Täger, *"Double Materiality": What is it and Why Does It matter?*, GRANTHAM RSCH. INST. CLIMATE CHANGE & ENV'T (2021), https://perma.cc/D3LC-L3KC.

[163] *France's Law on Energy and Climate*, *supra* note 161; Direction Générale du Trésor, *Publication of the Implementing Decree of Article 29 of the Energy-Climate Law on Non-financial Reporting by Market Players*, MINISTÈRE DE L'ECONOMIE DES FINANCES ET DE LA RELANCE (June 8, 2021), https://perma.cc/G3FG-DNVS.

[164] Brian Yang, *Green Finance Standards: The EU Taxonomy and China's "Catalogue"*, ENERGY POST (Sept. 17, 2021), https://perma.cc/S7JS-N72X.

[165] *Id.*

[166] *Common Ground Taxonomy – Climate Change Mitigation Instruction report*, INT'L PLATFORM SUSTAINABLE FIN. (2021), https://perma.cc/GY4P-TMYH.

[167] *Id.*

[168] Cédric Merle & Gong Yuanyuan, *EU-China Common Ground Taxonomy, a Painkiller to Taxonomy Headaches?*, NATIXIS CORP. INV. BANKING (2021), https://perma.cc/SZT8-JXEL.

Treasury recently published a draft Technical Paper "Financing a Sustainable Economy" to define sustainable finance for all parts of the South African financial sector including banking, retirement funds, insurance, asset management and capital markets, but also to consider global and national financial sector policy and regulatory actions in dealing with environmental and social risks and opportunities.[169] Launched on April 1st, 2022, South Africa offered a framework modeled on the European Taxonomy and its six environmental objectives to help investors and stakeholders assess and report environmental assets within their portfolio, identify market barriers to sustainable finance, and discover implementation best practices to characterize current gaps in the existing regulatory framework.[170] South African regulatory authorities, as part of the Intergovernmental Sustainable Finance Working Group and the Prudential Authority, will now be providing guidance on the application of the taxonomy framework within the country.[171] Mexico is also developing a "green finance taxonomy" with the Association of Mexican Banks (ABM) in cooperation with the GIZ, UNEP/UNDP and the Network for Greening the Financial System modeled in part on the EU Taxonomy regulation.[172]

IV. REGULATING ESG DISCLOSURE

While EU regulatory frameworks illustrate how complex achieving a common definition of sustainable investment is, consolidated disclosure regulations do have a tangible impact on companies' performance and decision-making capacity. In comparing different jurisdictions and systems of disclosure, it is noteworthy that outcomes in terms of business conduct evolve in divergent patterns. For example, the EU and the US are not uniform in regulating ESG investing and sustainability disclosures.[173] The U.S. is

[169] Ezra Davids & Ryan Kitcat, *International Comparative Legal Guides - Environmental, Social & Governance Law - Chapter - South Africa*, ICLG (2021), https://perma.cc/AA68-9JJN.
[170] Gina Gambetta, *"It's Very Investable": South Africa Praised for New Green Taxonomy*, RESPONSIBLE INV. (2022), https://perma.cc/NSQ3-DVE9.
[171] *Id.*
[172] *See* Merle & Yuanyuan, *supra* note 159; *Mexico Starts Dialogue with Central Bank about Greening the Finance Sector*, BIOFIN (2021), https://perma.cc/5KYT-YDTW.
[173] Addisu Lashitew, *The Risks of US-EU Divergence on Corporate Sustainability Disclosure*, BROOKINGS (Sept. 28, 2021), https://www.brookings.edu/blog/future-

following a *laissez-faire* approach, essentially allowing self-governing, voluntary private sector guidelines, while the EU is following a more concrete disclosure approach.[174] Other countries offer alternatives and combine a regulated and private approach to sustainability disclosure which have proven to be effective in guiding agents' conduct towards greater environmental transparency.[175] Although a fully regulated approach to ESG disclosure seems to be the preferred approach to strengthen disclosure, it does imply collaboration between public and private actors. Similarly, more countries today are relying on climate-related disclosure as part of their binding rules, particularly with regards to the Task Force on Climate-Related Disclosure's recommendations ("TCFD").[176] A critical analysis of these distinct methods and their implications on the reporting practices of the parties involved provides a clearer picture of preferred and effective reporting policies.

A. *Mandatory v. Voluntary Disclosure: A Preferred Private-Public Approach*

A public-private approach to regulate disclosure may improve quality and quantity of non-financial information.[177] Demand for increased transparency evolved from NGOs, consumers, and public stakeholders to shareholders, creditors, insurers, and rating agencies. Most institutional investors now expect companies to make materiality decisions based on environmental and social business practices with increased transparency.[178] Because governmental response was slow, private organizations took the lead to create voluntary reporting standards and frameworks.[179] Proliferation of private standards and lack of alignment between voluntary

development/2021/09/28/the-risks-of-us-eu-divergence-on-corporate-sustainability-disclosure/.

[174] *Id.*

[175] *See generally* Myers & Czarneki, *supra* note 28, at 1023 (indicating that over 110 governments around the world are participating in the TCFD system, which will undoubtedly lead to further transparency based on the recommendations of the TCFD).

[176] *Id.*

[177] *See* Harper Ho, *supra* note 75, at 330 (showing that the proposed "comply or explain" method, which also heavily relies on a mixing of hybrid public-private and mandatory-voluntary methodologies is an attractive approach).

[178] *See id.* at 318 (showing that with securities regulators and stock exchanges worldwide having acknowledged that ESG information is materially important to investors).

[179] Michael P. Vandenbergh, *Private Environmental Governance*, 99 CORNELL L. REV. 129, 161 (2013).

reporting and corporate annual reports or public filings reduce the viability of ESG information for investment analysis.[180] Voluntary disclosures pose practical problems because of inconsistent methodologies.[181] Some companies' ESG scores vary greatly depending on certain rating agencies, giving an inaccurate picture of reality.[182] Current disclosures may mislead the market as they are not consistently being audited.[183] Methodologies offered by agencies display a number of biases related to the size, sector or geographic location of companies that influence ESG scoring performance.[184] The difficulty Agencies have in identifying ESG risks from failing businesses with high ESG scores as well as a general lack of market data to make appropriate investment decisions, are both arguments against of a purely voluntary reporting system;[185] directing non-financial reporting from corporate voluntary practice to mandatory disclosure.[186]

Mandatory disclosure regulations offer benefits, such as standardizing ESG and modifying cost reduction for companies that are making voluntary ESG disclosure.[187] In the US, many support the idea of more restrictive regulations as compared to the current model.[188] Mandatory disclosure is expected to prove beneficial for US capital markets and corporate governance institutions as it makes ESG information more reliable and actionable.[189] More and more investors and companies are pro-reporting.[190] In providing clearer information about risks and opportunities and standardized disclosures, the SEC would increase confidence in the capital market.[191] Studies confirmed beneficial effects of mandated ESG

---

[180] El-Hage, *supra* note 55, at 368-69.
[181] *Id.* at 368
[182] *Id.* at 370.
[183] *Id.* at 369.
[184] *Id.* at 370-73.
[185] *Id.* at 368, 374-75.
[186] *See* Monciardini et al., *supra* note 91.
[187] El-Hage, *supra* note 55, at 390.
[188] *Id.* at 376.; *see also Americans Overwhelmingly Support Mandatory Climate Disclosure for U.S. Companies*, CERES (2022), https://www.ceres.org/news-center/press-releases/americans-overwhelmingly-support-mandatory-climate-disclosure-us (depicting agreement that Congress or SEC should seriously consider making some form of ESG disclosure mandatory).
[189] *See* El-Hage, *supra* note 55, at 376 (stating that, in 2018, U.S.-domiciled assets using SRI grew 38% from 2016 numbers).
[190] *Id.* at 383.
[191] *Id.* at 379; *see, e.g.*, Cynthia A. Williams & Jill E. Fisch, *Request for Rulemaking on Environmental Social and Governance (ESG) Disclosure*, SEC (Oct. 1, 2018), https://perma.cc/53UF-ZESE.

disclosure around the world.[192] Mandatory ESG disclosure increases availability and quality of ESG reporting among firms with low ESG performance, helps improve a firm's financial information environment, with analysts' earnings forecasts becoming more accurate and less dispersed when ESG disclosure becomes mandatory.[193] Negative ESG incidents and stock price crashes are less likely to happen after mandatory ESG disclosure is enacted.[194] Governments and regulators will also benefit fromESG risk disclosure, allowing them to design well-informed public policy and financial information and provide clear-cut definitions to encourage a company's involvement, as discussed above.[195]

The rationale behind public regulated disclosure jurisdictions is not to achieve "full- disclosure" but instead to reach an optimal level of disclosure which balances the issuer's costs to obtain, report, and audit information.[196] These obligations are limited to "significant" or "material" information, but companies are still free to base their own materiality judgment approach to disclosure even in systems of mandatory disclosure.[197] For instance, SFDR offers a set of voluntary PAI indicators that participants may adapt to their operations as they see fit.[198] The SEC's proposed climate-related disclosure rules are modeled in part on the voluntary framework and recommendations from the TCFD recommendations and draws upon the Greenhouse Gas Protocol.[199] The main objective of disclosure is to encourage companies to reduce the negative impacts of their operations on corporate stakeholders leading companies to define materiality in terms of stakeholder concerns under private non-financial reporting instead of financial risk and return.[200] This is even more so when mandatory disclosure aims to

---

[192] Philipp Krueger et al., *The Effects of Mandatory ESG Disclosure around the World*, N°21-44 SWISS FIN. INST. RSCH. PAPER SERIES (2021).
[193] *Id.*
[194] *Id.*
[195] *See* Harper Ho, *supra* note 75, at 342.
[196] *Id.*
[197] *Id.*
[198] *See New SFDR Principal Adverse Impacts or PAI Regime In - Key Points,* ALLEN & OVERY, https://www.jdsupra.com/legalnews/new-sfdr-principal-adverse-impacts-or-4944077/ (last visited May 17, 2023).
[199] Colin J. Diamond et al., *SEC Proposes Long-Awaited Climate Change Disclosure Rules*, WHITE & CASE (2022), https://perma.cc/9SZM-7Q8U (providing that the Greenhouse Gas Protocol is a widely-used global greenhouse gas accounting standard, created as part of an alliance between the World Resources Institute and the World Business Council for Sustainable Development).
[200] *See* Harper Ho, *supra* note 75, at 323, 324.

regulate climate related risk that could also affect global capital markets if large-scale risk events turn into reality.[201] When reporting on climate related risks, companies are also disclosing information on the external impacts of their operations to their stakeholders, which could potentially contribute to financial risk on a systematic basis and affect whole segments of the market itself because of aggregated or networked effects.[202] As the SEC is moving forward with climate mandated disclosure, the Commission should align with global allies to address pressing environmental and social issues, meeting the needs of investors and issuers in terms of ESG information and leave aside its reluctance to impede disclosure regulation.[203] On the other hand, voluntary disclosure often leads to private reporting regulation.

Private governance is recognized as an alternative to traditional government regulation and self-regulation by private firms themselves, including policies, codes of conduct, certification, reporting, and processing standards often based on international organizations' models or business conduct policies.[204] NGOs, and non-state actors are responsible for creating and enforcing these standards.[205] Although the SEC requires some form of mandatory reporting, private regulators in the US mostly take on the responsibility to enforce ESG disclosure because regulation is primarily deferred to private ordering.[206] It can take many forms, including shareholder engagement, third-party assessment, or shareholder litigation to promote disclosure accuracy and reliability.[207] Companies can be held accountable for material misstatements when making SEC filings, and for statements outside the filings in investor presentations or voluntary reports.[208] Shareholder litigation can be

---

[201] *Id.*
[202] *Id*; *see* Tom C.W. Lin, *Reasonable Investor(s)*, 95 B.U. L. REV. 461, 510 (2015).
[203] *See* Cynthia A. Williams & Donna M. Nagy, *ESG and Climate Change Blind Spots: Turning the Corner on SEC Disclosure*, 476 LEGAL STUDIES RSCH. PAPER SERIES 1453, 1485 (2021) (bridging the gap from overcoming reluctance to protection of institutional legitimacy and better ability to address pressing social and environmental issues).
[204] Harper Ho, *supra* note 95, at 274.
[205] *Id.*
[206] *See generally id.* at 295 (showing that private governance, in the realm of public-private interaction, follows the more privatized side when it comes to private regulation).
[207] *Id.*
[208] *See* Myers & Czarnezki, *supra* note 28, at 1015-16 (expanding and showing that companies can be held accountable under section 10(b) of the Securities Exchange Act and SEC Rule 10b covering fraudulent statements to investors andy

leverage for companies not diligent in disclosing non-financial information and will intensify as market appetite grows for greater ESG information, which will subject company ESG performance and disclosure to greater scrutiny in the court of public opinion, ultimately spawning new litigation.[209]

B. Comply or Explain Reporting Efficiency

The distinction between voluntary sustainability reporting and mandatory financial reporting is growing increasingly obsolete.[210] Most global disclosure regulations are based on comply or explain policies to improve the quality and reliability of relevant information for market participants.[211] Companies can comply with the rules as required or explain why they have elected not to comply.[212] In a comply-or-explain regime, a company complies by doing either of the above, while noncompliance occurs only when a company does neither.[213] Comply or explain represents an intermediate approach to regulation, and views diverge on whether comply or explain is in fact a mandatory or voluntary approach.[214] Because of the lack of federal and uniform mandatory disclosure, the SEC could adopt "comply or explain" disclosure rules and improve non-financial disclosure, as it has proved to be efficient in other jurisdictions following an approach to self-regulatory disclosure.[215] For example, Nasdaq's new ESG listing rule adopts a comply or explain mandate for board diversity addressed to most listed companies.[216] The rule approved by the SEC requires companies listed on Nasdaq's US exchange to publicly disclose consistent, transparent diversity statistics regarding the composition of their boards or

---

can also be held accountable under Sections 11 and 12(a)(2) of the Securities Act for material misstatements made in registration statements and prospectuses).

209 David Hackett et al., *Growing ESG Risks: The Rise of Litigation*, 50 ENV'T L. REP. 10849 (Oct. 2020).

210 Harper Ho, *supra* note 75, at 323.

211 *Id.* at 348.

212 Virginia Harper Ho, *How a "Comply or Explain" Rule Would Improve Nonfinancial Disclosure*, CLS BLUE SKY BLOG (Mar. 14, 2017), https://perma.cc/99GR-VM7P.

213 *Id.*

214 *Id.*

215 Harper Ho, *supra* note 75, at 320, 344-45.

216 Myers & Czarnezki, *supra* note 28, at 1021; *see, e.g.*, *Nasdaq's Board Diversity Rule: What Nasdaq-Listed Companies Should Know*, NASDAQ [hereinafter *Nasdaq*], https://perma.cc/7DQK-WG56 (last visited Mar. 26, 2023) (stating that each company with a board of directors of five or fewer members would need to have, or explain why it does not have, at least one board member who is diverse).

explain why they do not meet the objective set.[217] Although companies are choosing to ignore quotas set by the listing and attempt to give an explanation of the lack of diverse directors, Nasdaq's mandatory disclosure rules may give investors the possibility to hold companies accountable, which could not be done through voluntary disclosure alone.[218]

Outside the US, regulators widely embraced this approach as a self-regulatory instrument in ESG transparency and corporate governance.[219] South Africa's non-financial reporting regulation mostly relies on private regulation with a form of "apply or explain" policy.[220] "ESG disclosure in South Africa revolves around the King Code of Corporate Governance"[221] Under King Code IV, an organization must explain how the Code's principles are implemented and how such measures achieve the principles' contemplated outcomes.[222] In addition, the Johannesburg Stock Exchange ("JSE") requires implementation of the King Code as a condition to list companies.[223] Brazil also introduced a voluntary "report or explain" regulation for non-financial information.[224] The country's largest stock exchange, B3, regulates non-financial reporting and offers its own sustainability-report in accordance with GRI

---

[217] *Nasdaq*, *supra* note 216.

[218] Christina Milhomem & Harlan Tufford, *Nasdaq's New Board Diversity Rules: What's the Impact?*, MSCI (Feb. 1, 2022), https://www.msci.com/www/blog-posts/nasdaq-s-new-board-diversity/02986008433.

[219] *See e.g.*, Sarbanes-Oxley Act of 2002 , 15 U.S.C. §7264(a)-(b) (2002) (stating that firms are required to disclose whether they have adopted a code of ethics for senior financial officers or to explain why they have not).

[220] *See* Harper Ho, *supra* note 95, at 295, 297.

[221] *Id.*; *see* Inst. of Dirs. in Southern Africa, *King IV: Report on Corporate Governance for South Africa, 2016 38* (2016), https://perma.cc/YU6Z-K6SM (last visited Mar 26, 2023) ("the organization's governing body [such as the board of directors] has the discretion to determine where King IV compliant disclosures are made, for example, in the integrated report, sustainability report, social and ethics committee report, or other online or printed information or reports." It can be an integrated report or within "distinguishable, prominent and accessible part of another report," such as a sustainability report or social and ethics committee report).

[222] *See* Harper Ho, *supra* note 95, at 297.

[223] *Id*. at 298; *see, e.g.*, JSE Limited Listings Requirements, ¶ 8.63(a), https://perma.cc/48MW-2MZS (last visited Mar 26, 2023).

[224] *See* Harper Ho, *supra* note 95, at 299; *see, e.g.*, Edemir Pinto, *External Communication - Proposal to Adopt "Report or Explain" Sustainability Reporting Model for Listed Companies* (2011), https://bvmf.bmfbovespa.com.br/en-us/markets/download/EC-017-2011-Relate-ou-Explique-Ingles.pdf.

standards.[225] B3's non-financial reporting encourages listed companies to disclose whether they published a sustainability report or an integrated report, indicate where the report is published, or explain why they do not publish a report.[226] Brazil's Security and Exchange Commission (*Comissio de Valores Mobilidrios*, or "CVM") include mandatory sustainability requirements in its CVM report in the form of a mandatory periodic template.[227] In partnership with the Global Compact, GRI, and the IRCC, B3 provides guidance on its ESG disclosure to align its sustainability reporting with the United Nations SDGs.[228] In December 2021, the CVM issued disclosure criteria for companies with CVM Resolution 59 requiring them to disclose ESG information, align with SDGs, provide TCFD recommendations, audit ESG performance, carry out GHG emissions, or explain why they have not done so, reinforcing its comply or explain mechanism.[229] Brazil's Central Bank ("BCB") enriches the country's non-financial reporting regulation with rules and recommendations to better assess, disclose, and manage social, environmental, and climate related risk.[230] To another extent, they provide comprehensive "comply or explain" policies.[231] Considered as a central element in the corporate governance of the EU,[232] the comply or explain principle is reflected in a number of compliance and disclosure standards in its member states such as the United Kingdom, Germany, and the Netherlands.[233] Recent legislation on

---

225 *See* Harper Ho, *supra* note 95, at 299-300; *see* B3, NEW VALUE-CORPORATE SUSTAINABILITY 12 (2016), https://perma.cc/TLN9-GQ68 (last visited Mar 26, 2023).
226 *See* Harper Ho, *supra* note 75, at 328.
227 *Id.*; *see* CVM, Instruction No. 480 (2009), https://perma.cc/NV3X-7PZ3.
228 *See* Harper Ho, *supra* note 75, at 341.
229 Beatriz Lavigne et al., *Brazilian Securities Commission Establishes ESG Information Disclosure Criteria for Listed Companies*, EYE ON ESG (2021), https://perma.cc/5G45-LZV2.
230 *See* Luis Gustavo Bezerra et al., *Brazil's Central Bank and National Monetary Council Publish New Rules on Disclosure and Management of Social, Environmental and Climate-related Risks*, EYE ON ESG (2021), https://perma.cc/UR78-JSU3.
231 *Id.*
232 European Commission Press Release IP/06/2069, Corporate Governance: European Forum Clarifies "Comply or Explain" Principle and Issues Annual Report (Mar. 6, 2006).
233 *See generally* Annika Galle, *"Comply or Explain" in Belgium, Germany, Italy, the Netherlands and the UK: Insufficient Explanations and an Empirical Analysis*, 12 CORP. OWNERSHIP & CONTROL 862 (2014) (detailing how the study delves into the application of the principle for companies in the stated countries and more).

sustainable finance disclosure replaces the principle at the forefront of its new transparency requirements with the PAIs.[234]

C. Mandating Corporate Climate Related Disclosure

Regulatory Focus on Corporate Climate Related Disclosure

National "comply or explain" policies offer shortcomings to impose global strategies and reach climate adaptation goals. With the release of TFCD recommendations, many firms, investors, asset managers, and governments have shared their support for enhanced climate risk disclosure and have aligned with these recommendations.[235] They allow for clearer and more reliable information to induce market participants into allocating capital efficiently and support an accelerated transition to a low-carbon economy.[236] Climate-related disclosure enforcement is deemed necessary to reach net-zero emissions. Several countries today acknowledge that there is a strong need to mandate climate related disclosure.[237] For example, New Zealand became the first country ever to mandate climate-related disclosures in line with the TCFD recommendations, applying them to about 200 large financial institutions.[238] In the United Kingdom, companies are mandated to provide strict TCFD-aligned disclosures.[239] The Financial Conduct Authority ("FCA") introduced the Listing Rules (Disclosure of Climate-Related Financial Information) Instrument in December 2020 requiring companies with a UK premium listing to report against all TCFD recommendations on a comply-or-explain basis in

---

234 *See infr*a Part III.A(2).

235 *See* Brandon D. Stewart, *Shining Some Sunlight on Mandatory Corporate Climate-Related Disclosure*, 17 McGill J. Sust. Dev. L. 36 (2020).

236 *See* John Armour et al., *Mandatory Corporate Climate Disclosure: Now but How?*, 2021 Columbia Bus. L. Rev. 1144 (2021) (building the link between attention being given to the increased understanding of economic consequences of transition to transition acceleration).

237 *See* Stewart, *supra* note 236, at 34 (explaining that the development of new legislation is highly probably in several countries); *see also* Graham Caswell, *G7 Nations Agree on Mandatory Climate-related Disclosure*, Green Cent. Banking (June 8, 2021), https://greencentralbanking.com/2021/06/08/g7-nations-mandatory-climate-related-disclosure/.

238 Myers & Czarnezki, *supra* note 28, at 1023.

239 *Id.* at 1024.

their annual reports.[240] The UK is set to become the first G20 country to put into legislation these requirements, which will require Britain's largest companies and financial institutions to report on climate-related risks.[241] Since April 6th 2022, more than 1,300 of the largest UK-registered companies and financial institutions must disclose climate-related financial information including many of the UK's largest traded companies, banks and insurers, along with private companies with over 500 employees and £500 million in turnover.[242] These developments consolidate UK's position as a global leader in promoting non-financial reporting and increasing mandatory approach.[243]

Further, this trend is occurring in Hong Kong, where the Hong Kong's Securities and Futures Commission ("SFC") published its conclusions and proposed amendments to the Fund Manager Code of Conduct ("FMCC") which will require fund managers to consider climate-related risks in their governance, investment, and risk management processes as early as August 20th, 2022.[244] These amendments generally align with the TCFD recommendations.[245] Hong Kong does not legally impose institutional investors to take into account ESG factors when making investment decisions;instead the Hong Kong Stock Exchange ("HKEX") introduced mandatory requirements for listed companies to publish annual reports and other disclosures on a comply or explain basis.[246] In supporting a flexible comply or explain mandate,[247] HKEX seeks to become a major contributor to sustainable finance and stimulate the growth of Asia's sustainable finance market while increasing awareness,

---

[240] Listing Rules (Disclosure of Climate-Related Financial Information) Instrument 2020, FCA 2020/75, art. 9.8.6 (U.K.).
[241] Press Release, Department for Business, Energy & Industrial Strategy, HM Treasury, John Glen MP, and The Rt Hon Greg Hands MP, UK to enshrine mandatory climate disclosures for largest companies in law, GOV.UK (Oct. 29, 2021).
[242] *Id.*
[243] *Id.*
[244] Mark Uhrynuk & Alexander W. Burdulia, *Hong Kong SFC Finalizes Climate Risk Requirements for Fund Managers*, EYE ON ESG (Aug. 27, 2021), https://www.eyeonesg.com/2021/08/hong-kong-sfc-finalizes-climate-risk-requirements-for-fund-managers/.
[245] *Id.*
[246] *See* Harper Ho, *supra* note 95, at 310-11; *see e.g.*, HONG KONG STOCK EXCH., ENVIRONMENTAL, SOCIAL, AND GOVERNANCE GUIDE 2 (2016); *see also* Clinton Morrow et al., *ESG in Hong Kong - the Regulatory Implications*, LAW. MONTHLY (Nov. 24, 2021), https://www.lawyer-monthly.com/2021/11/esg-in-hong-kong-the-regulatory-implications/.
[247] *See* Harper Ho, *supra* note 95, at 311.

accessibility, and transparency of green and sustainable investment products.[248]

A mandatory climate disclosure regime is the course of action for the SEC.[249] Following Acting Chair Lee's public statement welcoming public input on climate change disclosures in March 2021, the SEC stated it would modify its 2010 Climate Guidance to consider recent developments in terms of climate change disclosure.[250] In climate-related proposed rules published on March 21st 2022, the SECresponded to investors and capital markets' concerns with regards to climate-risk transparency with a consistent framework.[251] Specifically, these new "long awaited" rules would add a new Article 14 to Regulation S-X with regards to the contents of financial statements, and a new Subpart 1500 to Regulation S-K governing the rules related to disclosures other than financial statements required in registration statements, proxy statements, and annual reports.[252] Companies will be required to describe the board of director's oversight of climate-related risks and, if applicable, climate-related opportunities with Regulation S-K Item 1501(1).[253] Companies will also have to disclose their processes for identifying, assessing, and managing climate-related risks, characterize physical risks (severe weather events or other natural conditions) and

---

[248] Financial Services Development Council of Hong Kong, *Hong Kong Backs Sustainable Development with ESG Focus*, FORBES (Nov. 1, 2021), https://www.forbes.com/sites/hongkong/2021/11/01/hong-kong-backs-sustainable-development-with-esg-focus/?sh=1e8f3dbc3d21.

[249] *See* Myers & Czarnezki, *supra* note 28, at 1012 ("recent actions taken by the SEC with regard to ESG-related issues"); *see e.g.*, Press Release, U.S. SEC, SEC Division of Examinations Announces 2021 Examination Priorities (Mar. 3, 2021); Press Release, U.S. SEC, SEC Announces Enforcement Task Force Focused on Climate and ESG Issues (Mar. 4, 2021).

[250] *Id.*

[251] The Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 Fed.Reg. 21334, (proposed Apr. 11, 2022) [hereinafter Proposal].

[252] *See* Press Release, U.S. SEC, Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors (2022), https://perma.cc/STH8-MNVL (last visited Apr 16, 2023); *see also* Shannon S. Broome et al., *What's Worth Understanding: The SEC Proposes a Mandatory Climate Disclosure Regime for Public Companies*, NAT'L L. REV. (2022), https://perma.cc/4ZPR-PKAQ (last visited Apr 16, 2023).

[253] *See* Proposal, *supra* note 252, at 21467 (discussing how proposed 17 CFR 229.1501(a)(1)(i), 17 CFR 229.1501(a)(1)(ii) includes identity of board members or committees responsible for oversight, a description of the processes and frequency by which the board or board committee discusses climate-related risks, whether and how the board or board committee considers climate-related risks as part of its business strategy, risk management, and financial oversight and how the board sets climate-related targets or goals).

transition risks in short, medium, and long-term horizons, and evaluate impacts on the company's strategy, business model, and outlook.[254] These companies must expand on processes integrated into their overall risk management system or procedures. Concurrently, the proposed rules require disclosure of GHG emissions, precisely mandatory disclosure of "total" Scope 1 direct emissions and Scope 2 indirect emissions separately as well as upstream and downstream scope 3 emissions and intensity, if material or if the company set a GHG emissions reduction target or goal including these emissions.[255] Now that the long-awaited rules are public, they are subject to a public comment period which will be considered by the SEC in voting a final rule taking many months in the process.[256]

Constraints of Mandatory Corporate Climate-Related Disclosures

Following the publication of the SEC rules, a number of rather motivated comments on some key legal and regulatory issues emerged.[257] Criticism came from within the SEC itself, with Commissioner Hester M. Pierce speaking out against the proposal, stating that fundamental changes to the disclosure regime cannot be made without harming investors, the economy, and the agency.[258] Commissioner Pierce points out that the rules force investors to view companies through the lens of a "vocal set of stakeholders, whom a company's climate reputation is of equal or greater importance than a company's financial performance."[259] Much of the criticism against these new rules apply to the current regulatory framework behind mandatory corporate climate- related disclosure rules.[260] One of the central points of contention is that it essentially lacks materiality with rules applying to all companies regardless of

[254] *See id.* at 21467 (stating requirement of that board must show proposed 17 CFR 229.1501(a)(1)(iii-v)).
[255] *See id.* at 21468-9 (listing requirements and metrics on GHG emissions in proposed 17 CFR 229.1504).
[256] Tara K. Giunta et al., *A New Era: Mandatory Climate Disclosures*, PAUL HASTINGS (2022), https://www.paulhastings.com/insights/client-alerts/a-new-era-mandatory-climate-disclosures#_edn17.
[257] *Id.*
[258] Hester M. Pierce, *We are Not the Securities and Environment Commission - At Least Not Yet*, SEC (2022), https://www.sec.gov/news/statement/peirce-climate-disclosure-20220321#_ftn49.
[259] *Id.*
[260] *See id.*.

how they consider the information to be material.[261] Materiality is the bottom line in developing any new disclosure requirements related to ESG.[262] Assessing climate-related risks may not come easy for some companies in determining short, medium, or long-term perspectives, especially given the "dynamic nature of climate related risks."[263] Specifically, with regards to GHG emissions regulations, a number of companies are already subject to report Scope 1 and Scope 2 emissions to the EPA on an annual basis.[264] With rules extending to even more companies, they are now required to report the new Scope 3 emissions.[265] Although smaller companies are not affected, the SEC does not offer any quantitative metrics for material emissions, unless it represents a "substantial likelihood that a reasonable investor would" consider it material.[266] Scope 3 emissions are essentially "based on what third parties do in contributing to the company's creation, processing, or transport of its products or when using and disposing of the company's products."[267] Many of them may not even be able to get the information they need to calculate these emissions.[268] Companies may have to turn to third-party consultants to help them determine scope 3 emissions.[269] This also increases the cost for companies that are subject to other voluntary climate disclosure and need to audit this information.[270]

[261] Pierce, *supra* note 259 (providing that, in recalling *TSC Industries v. Northway*, Commissioner Pierce emphasizes on the "reasonable investor" rule with a "clear link between materiality of information and its relevance to the financial return of an investment); *see, e.g.*, Div. of Corp. Fin., Sec's & Exch. Comm'n, Sample Letter to Companies Regarding Climate Change Disclosures (2021), https://www.sec.gov/corpfin/sample-letter-climate-change-disclosures.

[262] Pierce, *supra* note 259 (referencing Former Commissioner Elad Roisman's explanation of the concept of materiality in the federal securities laws in Section II.B of *Can the SEC Make ESG Rules that are Sustainable?* (2021), https://www.sec.gov/news/statement/peirce-climate-disclosure-20220321).

[263] *See* Proposal, *supra* note 252, at 21352.

[264] Melissa Horne et al., *SEC Publishes Proposed Rule Requiring Climate Disclosures*, ENV'T L. AND POLICY MONITOR (Mar. 28, 2022), https://www.environmentallawandpolicy.com/2022/03/sec-publishes-proposed-rule-requiring-climate-disclosures/.

[265] *Id.*

[266] *See* 17 C.F.R. 240.12b-2 (2013) (showing how the rule itself does not offer any quantitative metrics, which can lead to confusion).

[267] Pierce, *supra* note 259.

[268] *Id.*

[269] *Id.*

[270] *Id.*

The proposal would also not convene "comparable, consistent, reliable disclosures."[271] For Scope 3 emissions, companies would have to speculate about the habits of their suppliers, customers, and employees.[272] In anticipating transition risks, companies must also consider future changing climate policies, regulations, and legislation as well as technology and market evolution to reflect the ongoing transition to a low-carbon economy.[273]

A suitable remedy to the uncertainty created by this situation would be to provide guidance to support these companies. Commissioner Pierce suggests that the Commission lacks the authority to propose these rules and that doing so would exceed the statutory limits given by Congress.[274] The proposal would not comply with First Amendment limitations on compelled speech when ordering companies to disclose non-material information.[275] Even without a "clear directive" from Congress, the SEC was already engaged in regulating climate-related financial disclosure since its 2010 guidance.[276] The new rules would still not prevent Congress from passing some form of mandatory ESG reporting through federal legislation or Regulation of S-K.[277]

It is reasonable to assume that mandatory corporate climate-related disclosures increase transparency by capturing firms that fail to voluntarily disclose climate-related financial information.[278] Stewart offers several reasons that tend to weigh down the impact of these disclosures on market efficiency and accelerating the low-carbon transition.[279]

First, "it takes time for companies to comply with any mandatory disclosure requirements and deliver high quality climate-related disclosure relevant to its recommendations."[280] In the TCFD's 2021 Status Report, it outlined a 5-year implementation plan for

[271] *Id.*
[272] *Id.*
[273] Pierce, *supra* note 259.
[274] *Id.*
[275] *Id.*
[276] *Id.*
[277] *See generally* Myers & Czarnezki, *supra* note 28, at 1012-1013 (stating "some mandatory form of ESG reporting might arise…such as amending Regulation S-K or promulgating a new regulation").
[278] *See* Stewart, *supra* note 236, at 41.
[279] *Id.* at 34.
[280] *Id.* at 42.

companies to assess potential financial impacts and have broad estimates of relative shifts in capital expenditures.[281]

Second, the comply or explain approach to mandatory climate disclosure may confuse companies and yield counterproductive responses.[282] Differing levels of materiality directs companies to provide low-quality and non-comparable explanations for why they are not disclosing TCFD-aligned climate change information, increasing the risk for intentional or accidental greenwashing statements by such firms.[283]

Third, disclosures may also not fully align with the TCFD recommendations, as each country modifies their own regulations to adapt to their specific needs.[284] Climate change appears as a growing systemic risk to interconnected public markets and calls for a global harmonization of standards.[285]

Finally, compliance and enforcement strategies pose problems for enhanced market efficiency.[286] There is still a large enforcement gap in many jurisdictions and regulators do not feel eager to enforce compliance with mandatory climate-related rules yet.[287] Thus, governments are expected to explore new schemes to accelerate the carbon transition and accompany businesses in the delivery of these climate disclosures by providing guidance and monitoring their progress while maintaining a high level of mandatory requirements.[288] One thing is certain: without bolstered regulatory

[281] *See id.*

[282] See generally *id.* at 46-47 (describing some of the drawbacks of comply or explain).

[283] *Id.*; *see, e.g*, David Carlin, *Can the EU's Green Taxonomy Wipe Out Greenwashing?*, FORBES (Feb. 25, 2020), https://perma.cc/UEF3-MND7; *see, e.g.*, Russell Gold, *PG&E: The First Climate-Change Bankruptcy, Probably Not the Last*, WALL ST. J. (Jan. 18, 2019), https://perma.cc/44WG-SJXA (giving an example of a bank going bankrupt because of climate change).

[284] *See* Stewart, *supra* note 236, at 48.

[285] Carol Adams, *The TCFD Recommendations: A Missed Opportunity for Harmonization?*, CLIMATE DISCLOSURE STANDARDS BD. (Jan. 30, 2017), https://perma.cc/NE9K-YNPZ.

[286] *See* Stewart, *supra* note 236, at 46.

[287] *Id.* at 46, 52 (providing that implementation of TCFD remains somewhat technical for many companies that have to deal with sophisticated TCFD rules and are still in development like scenario analysis. Instead, many jurisdictions like France implement committees to monitor climate commitments of banking and financial industries); s*ee ACPR Establishes Climate and Sustainable Finance Committee*, MOODY'S ANALYTICS (Oct. 15, 2019), https://www.moodysanalytics.com/regulatory-news/oct-15-19-acpr-establishes-climate-and-sustainable-finance-committee.

[288] *See* Stewart, *supra* note 236, at 52.

requirements and benchmarks from governments and public institutions, environmental and human rights abuses will be sustained.

V. HUMAN RIGHTS DUE DILIGENCE AND TRANSPARENCY

Corporate human rights due diligence is a way for companies to proactively manage potential and adverse human rights impacts.[289] Many jurisdictions introduced innovative legislation to enforce human rights in Europe, placing the emphasis on corporate responsibility.[290] Companies are encouraged to pay greater care to the prevention of negative human rights impacts in their operations.[291] While there is a lot of attention and excitement about ESG reporting, the reality is that human rights information is much less widespread than environmental information despite all current legislation.[292] Efforts are being made to push international initiatives and impulse mandatory human rights due diligence, and should be sustained to improve transparent human right reporting.[293]

A. Enforcing Human Rights Disclosure

While searching for an effective and binding disclosure mechanism, divestment policies can help reduce fossil-fuel financing to prevent adverse impact on human rights and the environment. The climate crisis partly generated by fossil fuel industries is seriously aggravating the realm of human rights violation.[294] In financing oil and gas industries, corporate investment banks contribute to worldwide greenhouse gas emissions and human rights violations.[295] Hence, divestment strategies are central to ensure climate

---

[289] *See* Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect, and Remedy" Framework, ¶ 11, U.N. Doc. HR/PUB/11/04 (2011).

[290] *See id.* ¶ 13.

[291] *See id.* ¶ 14.

[292] *See* Paloma Muñoz Quick, *Bridging the Human Rights Gap in ESG*, BSR (Mar. 22, 2022), https://www.bsr.org/en/blog/bridging-the-human-rights-gap-in-esg.

[293] *See id.*; *see* Eileen Gavin et al., *The Small "s" in ESG is About to Get a Lot Bigger*, VERISK MAPLECROFT (Oct. 13, 2021), https://www.maplecroft.com/insights/analysis/the-small-s-in-esg-is-about-to-get-a-lot-bigger/.

[294] Annalisa Savaresi & Marisa McVey, *Human Rights Abuses by Fossil Fuel Companies*, CLIMATE DEFENDERS 3 (2020).

[295] *See* Isabella Kaminski, *Fossil Fuel Firms "Could be Sued" for Climate Change*, INDEPENDENT (Dec. 9, 2019, 6:10 PM), https://www.independent.co.uk/climate-

change mitigation and temper human rights violation, but only if they are properly and promptly implemented. According to a report published on March 30th 2022 by Rainforest Action Network,[296] more than 60 Corporate Investment Banks worldwide massively fund fossil fuels in direct contradiction to international commitments.[297] Fossil fuel financing declined in 2020 in the context of the Covid-19 pandemic but is rising again in 2021 with an increase in tar sands oil financing and continued financial support for artic, offshore, and fracked oil and gas from North American banks, and coal mining and coal power mostly by Chinese banks.[298] The report also highlights the abuses suffered by indigenous populations and the negative impacts of oil companies on indigenous lands neglecting the right to Free, Prior, and Informed Consent as articulated in the U.N. Declaration on the Rights of Indigenous Peoples.[299]

The inclusion of ESG criteria and CSR in investment decisions is leading companies to practice SRI.[300] Thus, voluntary divestment decisions can contribute positively to greater social justice by reducing greenhouse gas emissions and supporting indigenous populations.[301] Discrepancies between fossil fuel financing and commercial practices suggest the need for more stringent compliance regulations. However, many companies do not sufficiently appreciate the consequential negative impact of fossil fuel industrie,s and would benefit from more reliable and accurate indicators on quantifying and monitoring human rights impacts.[302] Through specific

change/news/cop25-madrid-climate-change-greta-thunberg-fossil-fuel-lawsuit-a9239601.html (building the logical connection between the financing of oil and gas industries and responsibility for the human rights violations of those industries).

[296] *Banking on Climate Chaos, - Fossil Fuel Finance Report 2022*, RAINFOREST ACTION NETWORK, 78 (2022), https://www.ran.org/wp-content/uploads/2022/03/BOCC_2022_vSPREAD-1.pdf.

[297] *See id.* at 8-11 (showing through a detailed chart laying out the report's findings that in the six years since the adoption of the Paris Agreement, the world's 60 largest private sector banks financed fossil fuels with USD $4.6 trillion).

[298] *Id.* at 3.

[299] *Id.* at 22, 23; Dallas Goldtooth et al., *Indigenous Resistance Against Carbon*, INDIGENOUS ENV'T NETWORK & OIL CHANGE INT'L 3 (Aug. 2021), https://www.ienearth.org/wp-content/uploads/2021/09/Indigenous-Resistance-Against-Carbon-2021.pdf.

[300] Josephine M. Balzac, *Corporate Responsibility: Promoting Climate Justice through the Divestment of Fossil Fuels and Socially Responsible Investment*, 47 ENV'T L. REP. NEWS & ANALYSIS 10151, 10159 (2017).

[301] *Id.* at 10156.

[302] *See* Savaresi & McVey, *supra* note 295, at 4 (attributing some of the most severe corporate human rights abuses to fossil fuel companies).

indicators, companies are encouraged to accurately evaluate their compliance with human rights standards. For example, in the Internet Communications and Technology sectors ("ICT") social media corporations are deeply concerned with issues revolving around the right to freedom of expression and right to privacy.[303] Metrics such as the Ranking Digital Rights help the ICT companies evaluate the world's most powerful digital platforms and telecom companies on how well they uphold human rights.[304] Another index, the Global Network Initiative ("GNI"), was founded in 2008 to help companies respect freedom of expression and privacy rights when faced with government pressure to deliver user data, remove content, or restrict communications.[305] Such rankings help improve human rights business policies and "can influence the progressive development of corporate governance and international standards in the absence of agreement on a binding international instrument to regulate the environmental and social impacts of global business enterprises."[306]

As such regulating corporate disclosure of potential adverse human rights impacts turns inevitable, sustainability disclosure in the finance sector and taxonomy for sustainable activities consisting of human rights due diligence into an integral part of corporate responsibility. SFDR explicitly states that human rights are part of the "sustainability factors."[307] Financial market participants must include in their websites or in their pre-contractual documents how they align with the OECD guidelines and UNGP, adding greater pressure on companies and stakeholders to tackle the "S" in ESG.[308] However, companies are not living up to the challenge when it comes to identifying human rights and social risk; there is still a lot of work to be done to improve human rights due diligence in ESG

---

[303] Erika George, *Corporate Social Responsibility and Social Media Corporations: Incorporating Human Rights through Rankings, Self-Regulation and Shareholder Resolution*s, 28 DUKE J. COMPAR. & INT'L L. 521, 532, 533 (2018).
[304] *Id.* at 530.

[305] GLOBAL NETWORK INITIATIVE, https://globalnetworkinitiative.org/ (last visited Apr. 15, 2023).
[306] George, *supra* note 304, at 538.
[307] *Commission Regulation, Sustainability-related Disclosures*, *supra* note 70, ¶ 24.
[308] Noura Hanna, *Human Rights Due Diligence – An Essential Step for Corporate Social Sustainability*, SUSTAINALYTICS (Dec. 9, 2021), https://www.sustainalytics.com/esg-research/resource/investors-esg-blog/human-rights-due-diligence#:~:text=SFDR%20explicitly%20mentions%20respect%20for.

reporting.[309] With a growing interest for ESG regulation, litigation arises against companies with alleged ESG-related performance and operational deficiencies held accountable for supplier misconduct.[310] A path to consider in ESG litigation is to challenge potentially misleading, erroneous, or incomplete reports.[311] ESG is also driving multi-country class action cases to greater focus on steward practices between responsible investors.[312] Originally driven by climate change issues, ESG-related litigation is expanding into other areas and across a range of asset classes.[313] Investors can hold publicly-traded companies accountable by employing class action litigation to promote legal business practices and maintain ethical standards.[314] Additionally, beyond ESG-related statements, companies could be liable for human rights issues throughout the supply chain.[315] In the US, companies are liable under the Alien Tort Statute ("ATS") and the Trafficking Victims Protection Act ("TVPA").[316]

Companies are also liable under common law claims based on their supplier activities, including climate claims.[317] Companies are therefore encouraged to devote particular attention to the content of their ESG reporting.[318] On September 30th 2020, the US Department of State issued recommendations on implementing the UN Guiding Principles for transactions linked to foreign government end-users for products or services with surveillance capabilities.[319] These guidelines encourage US businesses to integrate human rights due diligence into compliance programs, including training on relevant human rights considerations or development of

---

309 *Id.*; CORPORATE HUMAN RIGHTS BENCHMARK, CORP. HUM. RTS. BENCHMARK & WORLD BENCHMARK ALL. 3 (2020).
310 David Hackett et al., *Growing ESG Risks: The Rise of Litigation*, 50 ENV'T L. REP. 10849 (2020).
311 *Id.*
312 Duncan Paterson & Jeff Lubitz, *ESG as the Driving Factor in Multi-Country Class Action Cases*, HARV. L. SCH. F. CORP. GOV. (Oct. 7, 2021), https://perma.cc/Y6KZ-K46F.
313 Hackett et al., *supra* note 311.
314 Paterson & Lubitz, *supra* note 313.
315 Hackett et al., *supra* note 311, at 10856.
316 *Id.*
317 *See* Subodh Mishra, *The Rise of Climate Litigation*, HARV. L. SCH. F. CORP. GOV. (Mar. 3, 2022), https://corpgov.law.harvard.edu/2022/03/03/the-rise-of-climate-litigation/ (providing that one of the common categories of climate litigation is rooted in traditional theories of corporate law and liability).
318 Hackett et al., *supra* note 311, at 10852.
319 *Guidance on Implementing the UN Guiding Principles for Transactions Linked to Foreign Government End-Users for Products or Services with Surveillance Capabilities*, U.S. DEPT. STATE (2020), https://perma.cc/7TBP-QBA7.

appropriate policies, systems, and processes to mitigate risk of human rights abuses and violations.[320] However, this is not intended to impose any requirements under US law.[321] For example, on December 23rd, 2021, President Biden signed H.R. 6256, banning imports from the Xinjiang Uyghur Autonomous Region ("Xinjiang") of the People's Republic of China and imposing sanctions on foreign individuals responsible for forced labor in the region.[322] Products that are made in whole or in part in the province are no longer able to enter the USmarket unless the companies manage to demonstrate that they were not made with forced labor.[323] Yet, the non-mandatory approach suggested by the USin the line of voluntary ESG reporting is neither adequate nor sufficient to strengthen human rights compliance and reporting requirements.

B. Global Human Rights Due Diligence Regulations

The State duty to protect human rights extends to the corporate world, imposing a responsibility to conduct human rights due diligence.[324] EU member states have adopted advanced human rights legislation, such as France's landmark Corporate Duty of Vigilance Law (2017),[325] the Dutch Child Labor Due Diligence Law (2017),[326] Germany's Act on Corporate Due Diligence in Supply Chains Law

---

320 *Id.*
321 *Id.*

322 Press Release, The White House, Bill Signed: H.R. 6256 (Dec. 23, 2021), https://www.whitehouse.gov/briefing-room/legislation/2021/12/23/bill-signed-h-r-6256/.
323 *See id.*
324 Désirée Abrahams, *A Decade After the UN Guiding Principles, Companies Have a New Responsibility*, REUTERS EVENTS SUSTAINABLE BUS. (Aug. 3, 2021), https://www.reutersevents.com/sustainability/decade-after-un-guiding-principles-companies-have-new-responsibility.
325 Loi n° 2017-399 du 27 Mars 2017 Relative au Devoir de Vigilance des Sociétés Mères et des Entreprises Donneuses d'Ordre [Law No. 2017-399, 27 March 2017, on the Duty of Vigilance for Parent and Other Companies], Journal Officiel de la République Française [Official Journal of the French Republic] art. 1 (Fr.).
326 Wet Zorgplicht Kinderarbeid [Child Labor Due Diligence Act], No. 34 506, Staatsblad van het Koninkrijk der Nederlanden [Official Gazette of the Kingdom of the Netherlands] (Neth.).

(2021),[327] or the Norwegian Transparency Act (2022).[328] French and Dutch laws were the first to introduce reporting requirements regarding the impact of an employer's operations and supply chains on human rights.[329] Recent German and Norwegian laws give new impetus to mandatory measures to foster corporate respect for human rights, including future regulations in the EU.[330] Taking effect on July 1st 2022, the "Transparency Act" requires companies doing business in Norway to conduct regular human rights due diligence, publish an annual human rights statement, and respond to third party requests for information with regards to adverse human rights impacts.[331] Human rights include international standards such as fundamental human rights, workplace health, safety, environmental issues, and living wages.[332] Due diligence includes mapping adverse human rights impacts, including analysis of conditions that directly relate to services, activities, or products throughout the supply chain.[333] Companies must produce annual statements, signed by all board members, that report on certain aspects required under the Transparency Act.[334]

On the other hand, the purpose of the German Act is to enforce corporate due diligence obligations on prescribed businesses with respect to human rights and environmental risks to a significant

---

[327] Lieferkettensorgfaltspflichtengesetz [German Supply Chain Act], Bundesgesetzblatt Teil I [Federal Law Gazette Part I] art. 1(2021) (Ger.) [hereinafter German Act].

[328] *Act Relating to Enterprises' Transparency and Work on Fundamental Human Rights and Decent Working Conditions (Transparency Act)*, LOVDATA (Dec. 10, 2021), https://lovdata.no/dokument/NLE/lov/2021-06-18-99.

[329] Michael G. Congiu et al., *Dutch and French Legislatures Introduce New Human Rights Due Diligence Reporting Requirements*, LITTLER (Mar. 13, 2017), https://www.littler.com/publication-press/publication/dutch-and-french-legislatures-introduce-new-human-rights-due-diligence.

[330] Markus Krajewski et al., *Mandatory Human Rights Due Diligence in Germany and Norway: Stepping, or Striding, in the Same Direction?*, 6 BUS. & HUM. RTS. J. 550, 550 (2021).

[331] Michael R. Littenberg et al., *New Norwegian Mandatory Human Rights Due Diligence Law Creates Obligations for U.S.-based Multinationals Doing Business in Norway*, ROPES & GRAY (Dec. 15, 2021), https://www.ropesgray.com/en/newsroom/alerts/2021/December/New-Norwegian-Mandatory-Human-Rights-Due-Diligence-Law-Creates-Obligations-for-US#:~:text=The%20law%20is%20intended%20to.

[332] Fiona Webster & Stéphanie Rosseau, *Norway: Companies Face New Human Rights Due Diligence*, MERCER (Jan. 19, 2022), https://www.mercer.com/our-thinking/law-and-policy-group/norway-companies-face-new-human-rights-due-diligence-reporting.html.

[333] *Id.*

[334] *Id.*

degree.[335] The German Act defines a human rights risk as a situation that may result in a violation of internationally recognized human rights and contains a list of potential violations including forced labor, violations of occupational health and safety obligations, the right to freedom of association, discrimination, violation of adequate remuneration, and other rights protected by the International Labor Organization Conventions, the ICESCR and ICCPR.[336] Companies must establish an appropriate and effective risk management system to comply with due diligence obligations and have to conduct an annual risk analysis to identify human rights and environment-related risks in the business' own business area, and that of its direct supplier.[337] They must also take preventive measures and remedial action where a violation of human rights or the environment occurred.[338] The German Act requires companies to issue a policy statement on their human rights strategy but must also document and report information to publish on their website.[339]

Both the Norwegian and German laws implement novel due diligence requirements, paving the way for more to follow suit, both within the EU and beyond.[340] Despite their significant non-financial reporting requirements, concerns arise as to whether this will prevent human rights due diligence from becoming a "check-the-box" exercise.[341]

The EU Parliament reckoned that voluntary due diligence standards are largely insufficient to prevent human rights violation and environmental harm.[342] It pushed for a larger framework to all companies established in EU territory or operating in the internal market as well as publicly listed SMEs.[343] CSRD seeks to foster responsible, sustainable corporate behavior in the global value chain

[335] *See* Littenberg et al., *supra* note 332.
[336] Krajewski et al., *supra* note 331, at 9.
[337] German Act, *supra* note 328, art. 1, div. § 1, 4.
[338] *Id.* art. 1, div. 2, §§ 6, 7.
[339] *Id.* art. 1, div. 2, §§ 6, 10.
[340] Krajewski et al., *supra* note 331, at 9.
[341] *Id.*
[342] European Commission Parliament Briefing PE.729.424, EPRS, Corporate Sustainability Due Diligence: Could Value Chains Integrate Human Rights and Environmental Concerns? 5 (May 2022), https://www.europarl.europa.eu/RegData/etudes/BRIE/2022/729424/EPRS_BRI(2022)729424_EN.pdf.
[343] *Id.* at 6.

to protect human rights.[344] "The definition of "value-chain" as understood in CSRD is broader in scope that the business "supply chain", comprising all activities, operations, business relationships and investment chains of an undertaking and includes entities with which the undertaking has a direct or indirect business relationship, upstream and downstream."[345] The proposed directive ensures the robustness of companies' commitments and introduces an extension of the scope to all listed companies excluding SMEs.[346] It requires a certification for sustainability reporting, detailed and standardized standards for public information disclosed by these companies, and guarantees improved and more accessible information by requiring publication in a dedicated section of the companies management reports.[347]

The EU's approach tends to raise companies' accountability with regards to human rights due diligence.[348] The proposed directive offers a broad range of public and private enforcement mechanisms with supervisory authorities to impose effective, proportionate, and dissuasive sanctions comprising fines and compliance orders and ensuring that victims have the opportunity to hold companies accountable by taking legal action to obtain compensation for damages that could be avoided or mitigated with appropriate due diligence measures.[349] CSRD suggests the implementation of adapted mitigation processes for "adverse human rights and environmental impacts in [companies'] value chains, integrating sustainability into corporate governance," aligning business decisions with human rights, climate, and environmental impacts to strengthen corporate long-term resilience.[350] In the same way, the directive aims to complement the recent Taxonomy regulation in providing detailed information to the investors on how to allocate

[344] European Commission Press Release, Just and Sustainable Economy: Commission Lays Down Rules for Companies to Respect Human Rights and Environment in Global Value Chains (2022), https://perma.cc/LY2A-Y6NQ.
[345] *See* Lavanga Wijekoon et al., *Europe and Canada Seek to Mandate Human Rights Due Diligence and Transparency Obligations on Companies and Their Global Partners*, LITTLER MENDELSON P.C. (2021), https://perma.cc/3VYG-3Y7V.
[346] European Council of the European Union Press Release, Council Adopts Its Position on the Corporate Sustainability Reporting Directive (CSRD) (2022), https://perma.cc/HEV9-QWHD.
[347] *Id.*
[348] *See generally id.* (exemplifying the EU's approach).
[349] Gauthier Van Thuyne et al., *The EU Commission's Proposal for a Directive on Corporate Sustainability Due Diligence*, ALLEN & OVERY (2022), https://perma.cc/6HJ7-FBK3.
[350] *See* Proposal, *supra* note 11.

capital to responsible and sustainable companies.[351] As well, it will substantiate SFDR and financial markets' obligations to publish a statement on due diligence policies with regards to PAI of investment decisions on sustainability factors on a comply or explain basis.[352] However, the implementation of these obligations will not take place until 2023, with companies reporting the information on sustainability risks, opportunities, and impacts only in 2024, despite calls from investors, asset managers, and members of civil society for improved corporate sustainability data by 2024.[353]

May this push towards corporate sustainability reporting facilitate the adoption of a binding international treaty on business and human rights? Progress is well underway, albeit through hard law, however, companies will have to comply with strict regulations aimed at ensuring consistent standard of performance instead of using the flexibility offered by soft law solutions.[354] Still, a multiplication of domestic legislation may not be the optimal solution. Harmonizing standards and sanctions is critical to achieving the goal of fostering sustainability and addressing human rights risks on a global level.[355] The third revised draft treaty on Business and Human Rights published in August 2021 aims to broaden the scope of the treaty and clarify its provisions to cover all internationally recognized human rights, but faces obstructions from participants such as the USopposing systematic sanctions for violations and pushing for alternatives such as framework agreement based on the UN Guiding Principles on Business and Human Rights.[356]

---

[351] *Id.*
[352] *Id.*
[353] *Id.* art. 30 (lining up with the final draft of the proposal being established in 2022).

[354] Angelica Bonfati & Marco Pertile, *How Can a Treaty on Business and Human Rights Fit with International Law? Assessing the Development of International Rules on Corporate Accountability and their Relationship with Other International Legal Regimes*, QUESTIONS INT'L L. (July 31, 2021, 5:34 PM), http://www.qil-qdi.org/how-can-a-treaty-on-business-and-human-rights-fit-with-international-law-assessing-the-development-of-international-rules-on-corporate-accountability-and-their-relationship-with-other-international-l/.
[355] *See* Josua Loots, *Of Aims and Means: More Coordination and Harmonization of Efforts are Critical to Further Progress on Business and Human Rights*, INST. HUM. RTS. & BUS. (Oct. 29, 2014), https://www.ihrb.org/other/treaty-on-business-human-rights/of-aims-and-means-more-coordination-and-harmonization-of-efforts-are-critic (stating how critical harmonization is despite the polarization occurring).
[356] Carlos Lopez, *The Third Revised Draft of a Treaty on Business and Human Rights: Modest Steps Forward, But Much of the Same*, OPINIO JURIS (Mar 9, 2021),

Accountability and remedy measures are the focus of the instrument but largely remain insufficient with many provisions still vague or ambiguous.[357] Many states and stakeholders missed the opportunity to actively engage and expand the scope of the text, keeping it mostly unchanged.[358]

UNGP can provide guidance to businesses operating in Ukraine to adopt responsible business conduct in times of war.[359] Since Russia launched the invasion of Ukraine on February 24th 2022, numerous violations of humanitarian and human rights law have been documented, including deaths of civilians from indiscriminate attacks on civilian areas and infrastructure, strikes on schools and hospitals, use of indiscriminate weapons or cluster bombs that may all qualify as "war crimes."[360] The Business and Human Rights Resource Center is currently surveying companies operating in Ukraine and Russia about human rights due diligence to increase transparency of business human rights and promote good practices.[361] Companies from all sectors, banking, ITC, food and beverage, and oil and gas that haven't responded until now, sent general statements condemning the violence, others sharing their financial donations in support of Ukraine and some sharing their human rights due diligence process in Ukraine and risk mitigation.[362] Notwithstanding the international momentum to put economic coercion on Russia and donations for Ukraine, these tragic events are a considerable occasion for all companies to reflect deeply on their corporate responsibility and business ethics with regard to the protection of human rights in the context of warfare

https://opiniojuris.org/2021/09/03/the-third-revised-draft-of-a-treaty-on-business-and-human-rights-modest-steps-forward-but-much-of-the-same/.

[357] *Id.*

[358] *Id.*

[359] Phil Bloomer & Ella Skybenko, *Ukraine: Responsible Business Conduct in a War of Aggression*, BUS. & HUM. RTS. CTR. (Mar. 18, 2022), https://www.business-humanrights.org/en/blog/ukraine-responsible-business-conduct-in-a-war-of-aggression/.

[360] *Ukraine: Apparent War Crimes in Russia-Controlled Areas*, HUM. RTS. WATCH (Apr. 3, 2022), https://www.hrw.org/news/2022/04/03/ukraine-apparent-war-crimes-russia-controlled-areas#.

[361] *Russian Invasion of Ukraine: What Companies Have to Say About their Human Rights Due Diligence*, BUS. & HUM. RTS. CTR. (Nov. 21, 2022), https://www.business-humanrights.org/en/latest-news/russian-invasion-of-ukraine-what-companies-have-to-say-about-their-human-rights-due-diligence/.

[362] *Id.*

and the constant spreading of false information.[363]

VI. CONCLUSION

In light of the social, environmental, climate and economic crises we are experiencing, all public and private institutions have a responsibility to redouble their efforts to foster transparency and collaboration to temper these downturns. The gradual consideration of environmental, social, and governance criteria has clearly proven that companies are capable of reconciling performance and positive impact in conducting sustainable business. In this respect, non-financial reporting is a highly powerful tool because it allows regulators to drive corporate behavior and demonstrate initiative in the disclosure of environmental and human rights issues. However, regulators need to carefully adapt their rules and definitions to the practical circumstances faced by companies while guiding them further in the reporting process. It is very clear that mandatory regulations are necessary and voluntary disclosures are not at all sufficient to achieve environmental, climate, and social objectives, but they must also comprise a certain level of flexibility. An effective non-financial reporting system is one that provides clarity of definition, evolves with environmental and social realities and the demands of businesses, requires a certain amount of mandatory disclosure with potential penalties for non-compliance, yet provides guidance on how to report relevant information and potential adverse impacts.

[363] Kayla W. Green, *Rapid Human Rights Due Diligence During Political and Armed Conflict: A Business Response to Ukraine*, BSR (Apr. 7, 2022), https://www.bsr.org/en/blog/rapid-hrdd-during-political-and-armed-conflict-business-response-ukraine.