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The Convergence of Financial and ESG Materiality: Taking Sustainability Mainstream

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Sustainability reporting can be seen as an attempt to bring improved environmental, social, and governance (ESG) practices to mainstream business. However, this movement to mainstream is hampered by the disconnect between financial and ESG information. Both reporting streams use the concept of materiality to shape firms' disclosure obligations, but the term carries different meanings for different organizations. One sustainability organization, the Sustainability Accounting Standards Board (SASB), has developed reporting standards to merge sustainability and financial information by leveraging the definition of materiality for financial reporting purposes. This use of financial materiality positions SASB to collide with the Security and Exchange Commission's (SEC) hands-off attitude to ESG reporting. In the regulatory void left by the SEC's inaction on sustainability reporting, SASB provides the best route to reconceptualize materiality in line with society's interest in sustainable business.

Introduction

In 2014, Securities and Exchange Commission commissioner Daniel Gallagher publicly denounced attempts by "third parties" to influence the U.S. financial reporting regime.[1] According to Gallagher, shaping this disclosure system was the exclusive domain of the Securities and Exchange Commission (SEC).[2] The Commissioner specifically called out the Sustainability Accounting Standards Board (SASB), a U.S. non-profit organization that creates sustainability reporting standards,[3] stating it should be remembered that "groups like SASB have no role in the establishment of mandated disclosure requirements."[4] This, even though SASB bases its disclosure standards on exactly the same definition of material information as does the SEC.[5]

Corporate disclosure is defined by the concept of materiality, embodied in the requirement that firms disclose *material* information.[6] The definition of materiality has historically been controlled by the government, which focuses on a narrow concept of materiality confined to economic information.[7] Sustainability organizations, however, have argued

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[1]Commissioner Daniel M. Gallagher, *Remarks at the 26th Annual Corporate Law Institute, Tulane University Law School: Federal Preemption of State Corporate Governance*, Sec. Exchange Commission (March 27, 2014), https://www.sec.gov/news/speech/2014-spch032714dmg.html [hereinafter Gallagher Speech].

[2]*Id.*

[3]The terms "sustainability," "environment, social and governance (ESG)," and "corporate social responsibility" reporting have all been used to refer to reports with emphasis on environmental, social, or governance issues and to distinguish these reports from mandated financial disclosures. For example, the Global Reporting Initiative (GRI) defines a "sustainability report" as a report about environmental and social impacts. GLOB. REPORTING INITIATIVE, *What is Sustainability Reporting?* https://www.globalreporting.org/infnormation/sustainnablity-reportingn/Pages/default.aspx (last visited April 29, 2019). Others equate a corporate social responsibility (CSR) report with a sustainability report. *See* E-CSR, *CSR Report – Definition, Meaning, Benefits & examples of companies/Official & simple definition of a CSR report*, https://e-csr.net/definntions/csr-report-important-examples/#what-is-the-defintnion-of-a-csr-report (using the GRI definition of sustainability reporting for CSR reporting)(last visited April 27, 2019). Still others identify the common theme of disclosure of environmental stewardship, social responsibility, and corporate ethics in these reports, regardless of nomenclature. Georg Kell, *Five trends that show corporate responsibility is here to stay*, THE GUARDIAN (Aug. 13, 2014), https://www.theguardian.com/sustainable-businenss/blog/five-trends-corporate-social-responsibility-gloval-movement. For simplicity, this article uses the terms "sustainability" and "ESG" interchangeably to refer to environmental, social, and/or governance factors or reports.

[4]Gallagher Speech, *supra* note 1.

[5]*See infra* notes and accompanying text.

[6]*See infra* notes 43–48 and accompanying text.

[7]*See infra* notes 43 – 61 and 170-179 and accompanying text.

for a companion materiality concept that includes ESG information.[8] Disagreement over the definition of materiality have resulted in financial and ESG disclosure occupying separate domains, a result that hampers mainstreaming of sustainability by keeping ESG factors separate from business operations.

The separation of financial and ESG reporting can be pegged to different facets of materiality. The SEC represents the compliance aspect of materiality, wherein the government uses the concept to define specific legal obligations. The SEC's adherence to the traditional definition of materiality as encompassing solely financial information purports to reflect the investor protection focus of U.S. securities law and sets the threshold for complying with the legal duty to provide information to investors.[9]

Investors, on the other hand, represent the market aspect of materiality. Although ostensibly intended to protect them, investors show dissatisfaction with the traditional definition of materiality.[10] Increasingly, investors recognize the financial relevance of ESG issues, such as how companies respond to climate change, whether effective water management is in place, how companies manage their supply chains, and whether they have effective workplace safety policies.[11] Though once the domain of specialized socially responsible investing, mainstream investors now pursue ESG integration, where ESG impacts are factored into financial analysis.[12] However, attempting to integrate sustainability factors, as disclosed in a sustainability report, with financial factors, as disclosed in mandatory financial reporting, has proved unsatisfactory. Investors need disclosure that clearly identifies which ESG factors impact financial performance[13] and need that disclosure in a form that is "decision-useful."[14]

Unique among sustainability organizations, SASB calls for convergence of ESG and financial disclosure by leveraging the existing definition of materiality for financial reporting—the same definition used by the SEC.[15] Use of the same materiality definition should make SASB and the SEC allies. As Commissioner Gallagher's comments show, however, the SEC looks askance at SASB's efforts to bring ESG factors within the ambit of materiality. Gallagher's remarks may be read superficially as reflecting an aversion to third party influence on the SEC, as an attempt to protect the SEC's regulatory province. At a deeper level, the rift between the SEC and SASB indicates diverging understandings of the world. Although both organizations adhere to the same definition of materiality, that definition carries different meaning for each organization.

This article argues that SASB's use of materiality is an attempt to reconstruct the meaning of materiality to bring about the convergence of financial and ESG reporting. Part I describes the origin and development of the seemingly simple term materiality as it relates to corporate disclosure, and charts the differing meanings ascribed to the term. In Part II, the article uses the concept of social constructionism to examine what the diverse uses of materiality indicate about societal expectations. The article then identifies in Part III the conceptual and institutional obstacles to changing the

[8]*See infra* notes 72–84 and accompanying text.

[9]Roberta S. Karmel, Disclosure Reform – The SEC is Riding Off in Two Directions at Once, 71 BUS. LAW. 781, 786 (2016); Cynthia A. Williams, The Securities and Exchange Commission and Corporate Social Transparency, 112 HARV. L. REV. 1197, 1204 (1999) (noting that existing language could include social disclosure).

[10]See, e.g., Rachel Fixsen, Institutional Investors Dissatisfied with Companies' ESG Reporting, IP&E (Nov. 16, 2016), https://www.ipe.com/news/esg/institutional-investors-dissatisfied-with-companies-esg-reporting/www.ipe.com/news/esg/institutional-investors-dissatisfied-with-companies-esg-reporting/10016201.fullarticle; Ben Maiden, Investors Press for SEC Rule on ESG Disclosure, IR MAG. (Oct. 10, 2018), https://www.irmagazine.com/esg/investors-press-sec-rule-esg-disclosure (describing petition for rulemaking).

[11]Georg Kell, The Remarkable Rise of ESG, FORBES (Jul. 11, 2018, 10:09 AM), https://www.forbes.com/sites/georgkell/2018/07/11/the-remarkable-rise-of-esg/#1d05df221695; Christopher P. Skroupa, High ESG Performance Translates Into High Financial Performance, FORBES (June 16, 2017, 02:06 PM), https://www.forbes.com/sites/christopherskroupa/2017/06/16/high-esg-performance-translates-into-high-financial-performance/#78f787f8d708 (noting that two-thirds of institutional investors believe it is possible to build models showing the relationship between ESG factors and financial performance).

[12]Skroupa, supra note 10 (defining ESG integration); ESG Versus SRI: Successfully Aligning Your Investments and Values, RBC WEALTH MGMT., https://www.rbcwealthmanagement.com/cn/en/research-insights/esg-versus-sri-successfully-aligning-your-investments-and-values/detail/ (last visited Apr. 7, 2019) (distinguishing SRI from ESG investing); Julie Gorte, The Financial Performance of Sustainability: ESG and Risk, PAX WORLD FUNDS (Jan. 18, 2019), https://paxworld.com/the-financial-performance-of-sustainability-esg-and-risk/ (reviewing key ESG issues associated with financial performance). In 2018, funds that invest based on sustainability criteria passed the $1 trillion mark. Attracta Mooney, Rising Investor Interest Pushes ESG Funds Past $1tn, FIN. TIMES (Nov. 16, 2018), https://www.ft.com/content/f1e98ec7-083e-3b95-8c6b-ecc4810b988e.

[13]Skroupa, supra note 10.

[14]Maiden, supra note 9.

[15]See infra notes and accompanying text.

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meaning of materiality, focusing on the deference accorded administrative agencies as an obstacle to change. The article concludes by reviewing SASB's strategic positioning and prospects for advancing toward its goal of the convergence of financial and sustainability reporting.

I. The Development of Materiality

The question of defining materiality in the U.S. has its origin in the creation of the mandatory financial disclosure regime. Later, as groups sought disclosure of ESG information, they brought their own concepts of materiality, some of which challenged the existing definition. This section provides an overview of the development of materiality from the early twentieth century to the present.

A. The Role and Significance of Materiality

The concept of materiality is significant to business along two aspects. First, materiality has compliance implications. Securities regulation in the U.S. is based on information disclosure, with materiality as the guiding principle.[16] Materiality acts to set information disclosure thresholds,[17] separating what should be disclosed from what could be disclosed as part of required reporting.[18] For example, the line items on Form 10-K are presumptively material for all listed companies, while Item 303 (the Managers' Discussion and Analysis) leaves application of the term to the reporting firm.[19] Thus, the government uses materiality to construct the legal obligation of listed companies to disclose information. Historically, the use of materiality has been defined to include strictly financial information.[20]

In addition to this compliance aspect, materiality also has a market aspect and is increasingly important in accessing capital. The U.S. securities disclosure regime was instituted in the name of investor protection, with the government definition of materiality presumed to serve investor interests.[21] Developments in the investing terrain call this presumption into question. While the SEC has demonstrated little interest in the disclosure of ESG information, the investing community increasingly wants this information. Two examples are illustrative. Many institutional investors are signatories to the UN Principles for Responsible Investment (UN PRI), pledging to incorporate ESG factors into their investment decisions.[22] The UN PRI has over 2,300 investor signatories to the Principles.[23] In addition to institutional mechanisms such as the UN PRI, individual investor actions also signal the importance of ESG information to them. BlackRock Investments releases each year a letter to potential investees, discussing global trends of importance to the firm in making its investment decisions.[24] These letters frequently cite environmental and social issues as affecting decision-making.[25]

These examples show that, while the government uses materiality to shape legal obligations, investors use materiality to encapsulate the sum total of information they actually deem important for investment decisions. Investors recognize the impact of sustainability factors in three areas of business value creation.

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[16] *See infra* notes 40-46, and accompanying text.

[17] Chloe Ghoogassian, Note, *Evading the Transparency Tragedy: The Legal Enforcement of Corporate Sustainability Reporting*, 11 HASTINGS BUS. L.J. 361, 377-78 (2015); Robert G. Eccles & Tim Youmans, *Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality* 4 (Harv. Bus. Sch., Working Paper No. 116-023, 2015).

[18] Amy Deen Westbrook, *Sunlight on Iran: How Reductive Standards of Materiality Excuse Incomplete Disclosure Under the Securities Laws*, 7 HASTINGS BUS. L.J. 13, 18, 23-24 (2011).

[19] *See* Miller, *infra* note 41, at 1654; *see also* notes 45-46 and accompanying text.

[20] *See infra* note 71, and accompanying text.

[21] Karmel, *supra* note 8, at 781.

[22] *About the PRI*, UN PRI, https://www.unpri.org/pri/about-the-pri (last visited Apr. 9, 2019). The UN PRI was launched in 2006 specifically to encourage investors to commit to incorporation of sustainability factors into investment decisions and to provide an information-sharing forum for development of best practices. *Id.*

[23] *Id.*

[24] BlackRock is the world's largest asset manager with close to $6 trillion in assets under management in 2018. Josh Friedman & Noah Buhayar, *BlackRock Seeks $10 Billion to Buy Stakes in Companies*, BLOOMBERG (Feb. 14, 2018, 6:29 PM; updated Feb. 8, 2018, 11:20 AM), https://www.bloomberg.com/news/articles/2018-02-08/blackrock-is-said-to-seek-10-billion-to-buy-stakes-in-companies.

[25] *See, e.g.*, Larry Fink, *Larry Fink's 2019 Letter to CEOs, Purpose & Profit*, BLACKROCK, https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter?cid=ppc%3ABlackRock_USWA%3Agoogle%3Asitelink-larryfinkletter&gclid=EAIaIQobChMI0uKEgY284QIV0RZ9Ch287QN0EAAYASABEgJVq_D_BwE&gclsrc=aw.ds (last visited Apr. 9, 2019). The 2019 letter specifically identifies environmental risks and opportunities as part of BlackRock's engagement strategy for the year. *Id.*

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Cost Reductions and Efficiency

Basic information on energy management, greenhouse gas emissions, and water and raw material usage helps investors gauge a firm's efficiency, especially as it may be affected by resource scarcity (for example, in the case of water) or future regulation (for example, imposition of a carbon tax). In 2008, private equity firm Kohlberg Kravis Roberts & Co. L.P. (KKR) created a Green Portfolio program, which recognizes how poor environmental and social performance has direct impact on company value.[26] The KKR Green Portfolio is comprised of companies chosen as representing "opportunities that improve both financial and environmental performance in KKR's portfolio companies."[27]

Risk Assessment and Management

Investors understand that ESG factors signal volatility and risk in a variety of ways.[28] For example, investors are becoming attuned to the issue of stranded assets.[29] Stranded assets are assets that have undergone unanticipated or premature devaluation, often as a results of environment-related risks.[30] Fossil fuels provide an example of this risk as estimates suggest that a significant proportion of fossil fuel reserves, with a value in the trillions of dollars, would be considered "unburnable" if the world is to avoid disastrous climate change.[31] Failure to address potential stranded assets poses clear risks to the financial health of the company. Companies may also face new regulatory risks associated with sustainability impacts. The Dodd-Frank Act's provisions on conflict minerals highlighted the social impact of the mining of certain minerals that are crucial inputs for many electronics.[32] Businesses were sensitive enough to the reputational risk of having to make the disclosure contemplated by the Act that they mounted a constitutional challenge to the reporting requirements.[33] Last, the insurance industry, whose polestar is risk management, is investigating the impact of ESG risks on its business. Recent developments include a UN-led initiative to create insurance underwriting guidelines for ESG risks.[34]

Lost Opportunities

Companies that ignore ESG issues may also miss out on opportunities for market growth. Consumer preference for sustainably produced goods is growing, as is evidenced by so-called green products and practices,[35] as well as the growth of the Fair Trade movement.[36] Product certifications encompassing environmental and/or social criteria

[26]*See Partnering with our Portfolio,* KKR, http://www.kkr.com/responsibility/esg-management/partnering-our-portfolio (last visited Apr. 9, 2019) (providing current environmental and social topic initiatives, including green solutions, worker safety, and responsible sourcing).
[27]KKR, *KKR's Green Portfolio Program Continues Global Expansion* (May 23, 2012), available at https://ir.kkr.com/node/26701/pdf (identifying Program companies' cost savings as $365 million for the first three years of the Program). In 2015, based on the success of the original Green Portfolio Program, KKR expanded the mandate of its ESG efforts and rebranded the initiative as the Green Solutions Platform. Elizabeth Seeger, *Building on the past, focusing on the future: Green Solutions Platform*, KKR (Dec. 22, 2015), http://www.kkr.com/global-perspectives/kkr-blog/building-past-focusing-future-green-solutions-platform.
[28]ROBERT G. ECCLES & MIRTHA D. KASTRAPELI, THE INVESTING ENLIGHTENMENT: HOW PRINCIPLES AND PRAGMATISM CAN CREATE SUSTAINABLE VALUE THROUGH ESG 6 (2018). For argument that accounting for both financial and nonfinancial risk can drive firm and portfolio performance, see Virginia E. Harper Ho, *Risk-Related Activism: The Business Case for Monitoring Nonfinancial Risk*, 41 J. CORP. L. 647, 653 (2016).
[29]*See, e.g.*, BEN CALDECOTT ET AL., LLOYD'S OF LONDON, STRANDED ASSETS: THE TRANSITION TO A LOW CARBON ECONOMY (2017) (reviewing stranded assets potential impact on insurance industry investment strategies).
[30]BEN CALDECOTT ET AL., STRANDED ASSETS: A CLIMATE RISK CHALLENGE 2 (2016).
[31]*Id.* at 3.
[32]Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §1502, 124 Stat. 1376, 2218 (2010) (codified at 15 U.S.C. § 78m (2012)) [hereinafter Dodd-Frank Act]. Section 1502 required the SEC to implement a rule requiring issuers to investigate and disclosure whether their products contained conflict minerals from the Democratic Republic of the Congo.
[33]Section 1502 was subsequently struck down as a violation of the First Amendment. *Nat'l Ass'n of Mfrs. v. SEC*, 748 F.3d 359, 373 (D.C. Cir. 2014). For an examination of the First Amendment issues related to mandatory disclosure, see Celia R. Taylor, *The Unsettled State of Compelled Corporate Disclosure Regulation After the Conflict Mineral Rule Cases*, 21 LEWIS & CLARK L. REV. 427 (2017).
[34]*Underwriting Environmental, Social and Governance Risks in Non-Life Insurance Business*, UNEP FI (Feb. 27, 2019), available at https://www.unepfi.org/psi/underwriting-esg-risks/.
[35]Freya Williams, *Meet the nine billion-dollar companies turning a profit from sustainability*, THE GUARDIAN (Jan. 2, 2016, 11:01 AM), https://www.theguardian.com/sustainable-business/2016/jan/02/billion-dollar-companies-sustainability-green-giants-tesla-chipotle-ikea-nike-toyota-whole-foods (analyzing the success of nine companies that generate a billion dollars or more in annual revenue from products or services that have sustainability or social good at their core); Jeff Gelski, *Sustainable Product Market Could Hit $150 billion in U.S. by 2021*, FOODBUSINESSNEWS (Jan. 10, 2019), https://www.foodbusinessnews.net/articles/13133-sustainable-product-market-could-hit-150-billion-in-us-by-2021 (plotting the trajectory of sustainable product sales from 2014 to projected 2021 sales).
[36]Fair Trade is a global movement that aims to create sustainable development for disadvantaged producers. Peter Leigh Taylor, *In the Market But Not of It: Fair Trade Coffee and Forest Stewardship Council Certification as Market-Based Social Change*, WORLD DEVELOPMENT, Vol. 33, No. 1, pp. 129-147, 132 (2005). Fair Trade issues include environmental stewardship in production, income sustainability for all those in the supply chain, and community well-being. *Why Fair Trade*, FAIR TRADE CERTIFIED, https://www.fairtradecertified.org/ (last visited Apr. 9, 2019). Fair

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provide the opportunity to meet market demand for sustainable products.[37] The potential value of ESG opportunities is recognized by the emergence of "green finance."[38] Companies and financial institutions have created a variety of green finance mechanisms, to specifically channel capital to environmentally sound projects.[39]

Investor interest in the impact ESG factors have on financial value signals a change in the investing climate. Mainstream investors increasingly seek sustainability information from firms as part of investment decision-making.[40] However, current sustainability disclosure models do not meet investors' needs for robust information that is comparable across companies.[41] Moreover, the SEC's failure to incorporate sustainability factors into its interpretation of materiality leaves investor needs in the hands of a multiplicity of non-standardized voluntary reporting frameworks, none of which draw the necessary connection between ESG materiality and financial materiality.[42] The compliance aspect of materiality is out of step with the market aspect of materiality and this divergence threatens the fundamental premise of U.S. securities regulation – investor protection. To understand the gap between compliance materiality and market materiality requires reviewing the evolution of the materiality concept.

B. The Origin of Materiality

The impetus to impose federal regulation on securities markets originated with the stock market collapse of 1929 and the resulting desire to protect investors from the abuses that lead to the crash. The prevailing political current premised regulation on market principles: markets need informed investors to function efficiently and investors need information on listing companies to protect their investments.[43] The Securities Act of 1933 and the Securities

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Trade produce certification regimes have been established for such products as coffee, chocolate, and athletic and casual apparel. *Fair Trade Certified Products*, FAIR TRADE CERTIFIED, https://www.fairtradecertified.org/products (last visited Apr. 9, 2019).

[37]In his study of forest certification schemes, Professor Cashore coined the term "non-state market-driven" mechanisms to refer to sustainability-related product certification programs that did not rely on "state-centered sovereign authority but rather from companies along the market's supply chain." BENJAMIN CASHORE ET AL., GOVERNING THROUGH MARKETS: FOREST CERTIFICATION AND THE EMERGENCE OF NON-STATE AUTHORITY 4 (2004).

[38]"Green finance" refers to the incorporation of environmental factors into decisions made by financial institutions, including reducing environmental impacts of its financing decisions, proactively financing green companies and technologies, and developing new green financial products. Yunwen Bai, Michael Faure, and Jing Liu, *The Role of China's Banking Sector in Providing Green Finance*, 24 DUKE ENVTL. L. & POL'Y F. 89, 95-96 (2013).

[39]See Stephen Kim Park, *Investors as Regulators: Green Bonds and the Governance Challenges of the Sustainable Finance Revolution*, 54 STAN. J. INT'L L. 1, 8-11 (2018) for an overview discussion of various green finance instruments. For examples of commercial banks' green financing initiatives, see IN^2, the Wells Fargo Innovation Incubator, founded Wells Fargo. *Advancing Technologies for Smart and Connected Communities*, IN^2, https://in2ecosystem.com/ (last visited Apr. 9, 2019). IN^2 is a technology incubator and platform funded by the Wells Fargo Foundation and co-administered by the National Renewable Energy Laboratory (NREL), to provide commercialization opportunities for early-stage clean energy and agriculture technologies. *Id.* Bank of America has issued a series of green bonds over the past several years, the proceeds of which are earmarked for renewable energy development. *Bank of America Has Issued Four Corporate Green Bonds, Raising a Total of $4.35 Billion for Renewable Energy Projects*, BANK OF AMERICA, https://about.bankofamerica.com/en-us/green-bond-overview.html#fbid=HcK87ko35WX (last visited Apr. 9, 2019); Matthew Heimer, *How a Big Bank Fueled the Green Energy Boom*, FORBES (Aug. 20, 2018), http://fortune.com/2018/08/20/bank-of-america-wind-solar-energy/.

[40]*See, e.g.*, Fink, *supra* note 23; *ESG Investing*, STATE STREET GLOBAL ADVISORS, https://www.ssga.com/our-insights/viewpoints/esg-investing.html (last visited Apr. 9, 2019) (noting that investing responsibly entails "full integration of material ESG factors into [] investment processes," requiring "quality data").

[41]*See infra* notes 92–94, and accompanying text.

[42]*See infra* note 95 and accompanying text.

[43]Troy A. Paredes, *Blinded by the Light: Information Overload and Its Consequences for Securities Regulation*, 81 WASH. U. L. Q. 417, 418, 422–424 (2003).

Exchange Act of 1934 (Securities Acts or Acts) were intended to build efficient capital markets and protect investors by requiring listing companies to publicly disclose information on their financial condition.[44] More broadly, they introduced an expectation of transparency for companies listing on stock exchanges.[45]

Focusing on the need for information surfaced the obvious question of specifically what information firms would be required to disclose. Investors did not need, and could not effectively use, all possible information on a company.[46] Regulators, thus, looked for a way to separate information that needed to be disclosed to investors from information that did not. The Securities Acts created two types of disclosure obligations for companies.[47] In addition to specific line item disclosures, the Acts also created a more general obligation for companies to disclose information that was material to understanding the overall financial position of the company.[48] The requirement to disclose material information continues to the present, most noticeably in Item 303 of the required 10-K annual report, Management's Discussion and Analysis.[49]

The concept of materiality developed as the threshold for information that the mandatory reporting system would require firms to disclose.[50] Thus, the definition of materiality for securities law constitutes the primary framing mechanism for financial reporting. Although the Securities Acts used the term "material," the original laws did not define this term, leaving its definition to the judiciary.[51]

The U.S. Supreme Court has considered the definition of materiality in a variety of securities contexts.[52] However, the key case setting out the current accepted definition of materiality concerned claims that material facts had been omitted from a proxy statement. In *TSC Industries, Inc. v. Northway, Inc*., the Court took on the task of clarifying the definition of materiality for purposes of Rule 14(a) actions.[53] A fact is material, the Court said, if there were a

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[44]Williams, *supra* note 8, at 1240. Focusing attention on the lack of disclosure sent the message of belief in the power of information to affect behavior, in this case to promote informed investment decisions. Alison B. Miller, *Navigating the Disclosure Dilemma: Corporate Illegality and the Federal Securities Laws*, 102 GEO. L. J. 1647, 1652 (2014). Debate over the merits of mandatory versus voluntary corporate disclosure continued even once the securities acts were in place. One school of thought advanced arguments against mandatory disclosure, claiming that market forces would lead corporations to disclose whatever information investors truly wanted. *See, e.g.*, George J. Stigler, *Public Regulation of the Securities Markets*, 37 J. BUS. 117, 120-121, 124 (1964) (arguing that evidence did not support the need for mandatory disclosure). Others argued that market failures would inevitably result in information asymmetries between company and investors. John C. Coffee, Jr., *Market Failure and the Economic Case for a Mandatory Disclosure System*, 70 VA. L. REV. 717, 725-727(1984)(arguing that the nature of information as a public good results in it being under-provided). Most recently, Prof. Horton produced an empirical study to demonstrate that disclosure before the securities acts was inadequate, necessitating a mandatory system. *See* Brent J. Horton, *In Defense of a Federally Mandated Disclosure System: Observing Pre-Securities Act Prospectuses*, 54 AM. BUS. L. J. 743 (2017). For criticism of mandated disclosure generally as a regulatory tool, *see, e.g.*, Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. PENN. L. REV. 647, 665-679, 734-742 (2011) (concluding that mandated disclosure often fails as a regulatory tool either because it does not accomplish its purpose or because its costs outweigh its benefits).

[45]Richard C. Sauer, *The Erosion of the Materiality Standard in the Enforcement of the Federal Securities Laws*, 62 BUS. LAW. 317 (2007).

[46]Miller, *supra* note 41, at 1653; Sauer, *supra* note 42, at 355 (identifying issues with too much disclosure). Commentators have also noted the cost to business of having to disclose more information than investors need. *See, e.g.*, Sauer, *supra* note 42, at 355.

[47]Karmel, *supra* note 8, at 784-46. The 1933 Act related to initial securities registration statements, while the 1934 Act created the requirements of annual and periodic reporting by listed companies. For purposes of this Article, the obligations and definitions are the same.

[48]Miller, *supra* note 41, at 1653.

[49]*See* Management's discussion and analysis of financial condition and results of operations, 17 C.F.R. § 229.303 (2017). The "MD&A" regulation requires companies to disclose a host of information related to the company's fiscal years and interim periods. Most of the disclosure items are couched in the concept of materiality. For example, companies are required to disclose any "material" commitments for capital expenditures, events or trends that could increase or decrease the company's liquidity in a "material" way, and off-balance sheet arrangements that could have an effect "material" to investors. 17 C.F.R. §§ 229.303(a)(1)–(2), (4).

[50]Sauer, *supra* note 42, at 618 (labeling materiality as the "dividing line" between information that influences investor decisions and all other information); Yvonne Ching Ling Lee, *The Elusive Concept of "Materiality" Under U.S. Federal Securities Laws*, 40 WILLAMETTE L. REV. 661, 662 (2004) (identifying materiality as separating "essential" information from irrelevant information).

[51]LuAnn Bean & Deborah W. Thomas, *The Development of the Judicial Definition of Materiality*, 17(2) THE ACCT. HISTORIANS J., 113, 115 (Dec. 1990); Kurt S. Schulzke & Gerlinde Berger-Walliser, *Toward a Unified Theory of Materiality in Securities Law*, 56 COLUM. J. TRANSNAT'L. L. 6, 15 (2017). Rule 405 accompanying Regulation S-K now provides a definition of material information as "those matters to which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to purchase the security registered." 17 C.F.R. § 230.405 (1982).

[52]*See* Bean & Thomas, *supra* note 48, at 115–16.

[53]426 U.S. 438, 444-45 (1976).

"substantial likelihood" that disclosure of the fact would be viewed by the "reasonable investor" as having altered the "total mix" of information made available.[54] In 1988, the Supreme Court extended this definition of materiality to Rule 10(b) actions[55] and it has become the backdrop for all discussions of the concept of materiality.[56]

While the Supreme Court was grappling with the contours of materiality, so too was the Securities and Exchange Commission (SEC). The 1934 Act made the SEC the official standard-setting body for financial accounting and reporting.[57] As part of the agency's rule-making authority, it delegated the creation of accounting standards to the Financial Accounting Standards Board (FASB).[58] Materiality for FASB was connected to the information needs of financial decision makers, specifically, investors.[59] More recently, FASB proposed revisions to its definition of materiality that would align it with the Supreme Court's *TSC* definition.[60] SEC staff accountants have also cited the *TSC* definition in agency documents.[61]

Academic investigation of financial materiality reflects the diverse aspects of this important concept. One of the most obvious applications of the term is with regard to securities fraud cases brought under section 10(b) of the 1934 Act.[62] These cases demonstrate the challenges inherent in the broad statutory and judicial definition of materiality and a large body of academic literature explores what exactly courts have interpreted the term to mean. Commentary on this issue emphasizes lack of a precise definition of materiality and the resulting confusion in lower court decisions.[63]

Scholars have criticized the *TSC* definition of materiality, and its implementation, along a host of parameters. Generally, the definition is characterized as "murky"[64] and "elusive,"[65] leading to difficulties for reporting companies in determining what is material and, therefore, required to be disclosed.[66] Some scholars bemoan the tendency to over-reporting and information overload, fostered by the uncertainty around what is material.[67] Others criticize the

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[54]*Id*. at 449.

[55]Basic, Inc. v. Levinson, 485 U.S. 224, 249 (1988).

[56]Basing disclosure on the materiality concept leaves corporations with considerable flexibility to determine what to disclose. Nina Hart, Note, *Moving at a Glacial Pace: What Can State Attorneys General Do About SEC Inattention to Nondisclosure of Financially Material Risks Arising from Climate Change?*, 40 COLUM. J. ENVTL. L. 99, 102-03 (2015). However, the inherent ambiguity of the Supreme Court definition has been criticized as leading to extensive litigation to resolve disagreements regarding the definition and how it impacts disclosure obligations. *See, e.g.*, David Monsma & Timothy Olson, *Muddling Through Counterfactual Materiality and Divergent Disclosure: The Necessary Search for a Duty to Disclose Material Non-Financial Information*, 26 STAN. ENVTL. L.J. 137, 140 (2007).

[57]Jean Rogers & Robert Herz, *Corporate Disclosure of Material Information: The Evolution – and the Need to Evolve Again*, 25 J. APPLIED CORP. FIN. 50, 50-51 (2013).

[58]FASB originated as an outcome of a study conducted by the American Institute of Certified Public Accountants (AICPA) into the state of accounting standard setting. *See* Stephen A. Zeff, *The Wheat Study on Establishment of Accounting Principles (1971-72): A Historical Study*, 34 J. ACCT. PUB. POL'Y 146, 146 (2015). The Wheat Study on Establishment of Accounting Principles (Wheat Study) revealed deficiencies in the accounting standard-setting regime, most notably that standard-setting for the accounting profession was dominated by the major accounting firms. Rogers & Herz, *supra* note 54, at 51. The Wheat Study recommended establishing a separate, independent body for creating accounting standards. FASB was created in 1973. Zeff, *supra*, at 163.

[59]Fin. Accounting Standards Bd., *Statement of Financial Accounting Concepts No. 2*, FASB CON2-3 (1980) https://www.fasb.org/jsp/FASB/Document_C/DocumentPage?cid=1218220132599&acceptedDisclaimer=true. The document's discussion of materiality stated that materiality was defined in terms of "what makes a different to a decision maker" and that a decision not to disclose information may be made because "investors have no need" for the information.

[60]Fin. Accounting Standards Bd., Proposed Amendments to Statement of Financial Accounting Concepts, Chapter 3: Qualitative Characteristics of Useful Financial Information, FASB 3 (2015) https://asc.fasb.org/imageRoot/23/73531923.pdf.

[61]See, e.g., SEC. EXCH. COMM'N, SEC STAFF ACCOUNTING BULLETIN: NO. 99 – MATERIALITY (1999) (quoting TSC definition of materiality).

[62]Section 10(b) is the 1934 Act's primary anti-fraud provision and prohibits the use of "any manipulative or deceptive device" in connection with the purchase or sale of securities. 15 U.S.C. §78j.

[63]See, e.g., Thomas M. Madden, Significance and the Materiality Tautology, 10 J. BUS. & TECH. L. 217, 217 (2015) (describing the "fundamental void" in defining materiality left by the Supreme Court decision in Matrixx Initiatives, Inc. v. Siracusano); Richard A. Booth, The Two Faces of Materiality, 38 DEL. J. CORP. L. 517, 518-19 (2013) (noting the Supreme Court's apparently conflicting approaches to materiality in the context of a class action suit brought under the fraud on the market theory); Matthew Ady, Living in a Material World: Does a Violation of Item 303 or Regulation S-K Satisfy the Materiality Element in a Rule 10B-5 Cause of Action?, 17 WAKE FOREST J. BUS. & INTELL. PROP. L. 401 (2017) (surveying the apparent split in federal circuit courts on the definition of materiality for purposes of Item 303); and Matthew C. Turk & Karen E. Woody, The Leidos Mixup and the Misunderstood Duty to Disclose in Securities Law, 75 WASH. & LEE L. REV. 957, 978, 986–994 (2018) (reviewing what it terms the "illusory" circuit split over whether Item 303 disclosures create a duty that is actionable under federal securities law). Commentators have also noted the confusion among courts of appeal over the distinction between the duty to disclose information and the concept of materiality. See, e.g., Donald C. Langevoort & G. Mitu Gulati, The Muddled Duty to Disclose Under Rule 10b-5, 57 VAND. L. REV. 1639, 1643-45 (2004); Ady, supra, at 407–411; Turk & Woody, supra.

[64]Schulzke & Walliser-Berger, supra note 48, at 8.

[65]Lee, supra note 47, at 663–668.

[66]Lee notes that this difficulty often results in a standard that is determinable only ex post facto in a shareholder suit or SEC enforcement action. Id. at 664.

[67]Paredes, supra note 40, at 417; Schulzke & Walliser-Berger, supra note 48, at 10.

reductionist potential of the vague definition, leading to nondisclosure of critical information.[68] More recently, a school of criticism has developed that explores the limits of the concept of the "reasonable investor," a core component of materiality.[69]

A second stream of materiality scholarship focuses on what is termed "qualitative materiality."[70] The first iteration of this concept grew out of the SEC's dissatisfaction with the traditional, rather narrow, focus on economic materiality.[71] Qualitative materiality posited that conduct that was not financially significant to the company could still be material to investors, as it reflected management integrity.[72] Professor Miller, for example, has argued that uncharged criminal conduct may be material for purposes of corporate disclosure.[73] Other commentators, however, viewed qualitative materiality's focus on ethics as moving disclosure away from its original goal of creating a transparent market.[74]

[68]Georgiev, for example, has argued that large firms can avoid disclosing information because their size raises the materiality threshold. George S. Georgiev, Too Big to Disclose: Firm Size and Materiality Blindspots in Securities Regulation, 64 UCLA L. REV. 602, 606 (2017). See also Westbrook, supra note 16, at 15-16 (contending that the current materiality standard permits companies to deny the materiality of information where costs are not currently quantifiable).

[69]See, e.g., Margaret V. Sachs, Materiality and Social Change: The Case for Replacing "the Reasonable Investor" with "the Least Sophisticated Investor" in Inefficient Markets, 81 TULANE L. REV. 473 (2006) (proposing an alternative materiality standard for unsophisticated investors); David A. Hoffman, The "Duty" To Be a Rational Shareholder, 90 MINN. L. REV. 537 (2006) (examining the disparity between judicial assumptions of "rational" investor behavior and actual investor behavior); Steven M. Davidoff & Claire A. Hill, Limits of Disclosure, 36 SEATTLE U. L. REV. 599 (2013) (exploring the use of information in human decision-making).

[70]*See, e.g.*, John M. Fedders, *Qualitative Materiality: The Birth, Struggles, and Demise of an Unworkable Standard*, 48 CATH. U. L. REV. 41(1998).

[71]Id. at 45-46.

[72]*Id.* at 46. The SEC developed this concept largely in response to the Watergate scandal in the early 1970's, and allegations of improper campaign contributions by corporations. *Id.* at 49–50. In the mid 1970's, the SEC also began focusing on bribes and other questionable practices by corporations, and corporate efforts to hide these payments through their accounting practices. *Id.* at 50–51.

[73]Miller, *supra* note 41, at 1665-1666 (claiming that corporate illegality may be important to investors where it has quantitative impact on the company).

[74]*See, e.g.,* Sauer, *supra* note 42, at 317–357, 330. By the 1990's, the SEC confronted a new disclosure issue, in the form of "earnings management," that it included in qualitative materiality. Earnings management consisted of a variety of accounting practices whereby companies took advantage of the imprecise definition of materiality to improve the appearance – but not the substance – of their financial results. For example, companies had begun to set financial thresholds for the materiality of key metrics, for purposes of disclosure. James J. Park, *Assessing the Materiality of Financial Misstatements*, 34 J. CORP. L. 513, 516–17 (2009). In addressing the earnings management issue, the SEC utilized the materiality concept, noting that information is material if investors view it as altering the "total mix" of information, including both quantitative and qualitative factors. SEC, Staff Accounting Bulletin 99, *supra* note 58. Under the "qualitative" materiality standard, then, even small financial misstatements could be "material" if they met certain qualitative criteria. Park, *supra*, at 516–17. *See* SEC SAB 99, *supra*, for examples of relevant qualitative factors.

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Despite the different formulations developed to define materiality, the overall meaning of the legal disclosure regime was clearly focused on the information needs of investors, in keeping with the investor-protection purpose of the 1933 and 1934 Acts.[75] Further, the SEC has consistently interpreted materiality to mean economic materiality.[76] Thus, the range of information that is presumed will protect investors is narrowly confined.

C. Materiality and Stakeholders

For nearly 50 years, the meaning of materiality for corporate disclosure purposes was largely unquestioned. But in the 1990's, dissatisfaction with corporate reporting's focus on exclusively financial information led new actors with interests in environmental and/or social issues to advocate for expanded corporate disclosure. This section assesses the development of materiality through the lens of the organizations that have created the most widely used sustainability reporting frameworks: the Global Reporting Initiative (GRI), the CDP, and the International Integrated Reporting Council (IIRC). [77]

Founded in 1997, the GRI administers the oldest and most widely used voluntary sustainability reporting framework globally.[78] GRI's overarching disclosure principle is that companies report "material" environmental, social and governance information.[79] CDP (formerly the Carbon Disclosure Project) was organized in 2000 by a coalition of non-profit organizations and institutional investors.[80] CDP focuses exclusively on voluntary disclosure of environmental impacts associated with climate change, forests, and water use. Companies report to CDP through its

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[75]*See supra* notes 40-41 and accompanying text.

[76]See Karmel, supra note 8, at 786; Williams, supra note 8, at 1264. Prior to 1971, there was no SEC requirement to disclose non-financial information. David A. York, SEC as Environmentalist: The Reluctant Champion, 53 NOTRE DAME L. REV. 985, 991 (1978). Despite the absence of a generalized environmental or social disclosure requirement, businesses may have certain specific obligations to disclose environmental or social information to regulators. For example, Regulation S-K can create the obligation to report information to the SEC under several items. Item 101 contains the most straightforward reporting requirement. Item 101 requires that a reporting company describe its business, including its principal products and services, sources of raw materials, and its competitive condition. 17 C.F.R. § 229.101 (2006). This Item also requires disclosure with regard to the effect that compliance with environmental laws and regulations may have on the company's capital expenditures, earnings and competitive position. 17 C.F.R. § 229.101(c)(1)(xii) (2006). A companion item, Item 103, requires companies to describe any "material pending legal proceedings, other than ordinary routine litigation…." 17 C.F.R. § 229.103 (2006). Instructions for the Item specifically exclude environmental proceedings from the category of "ordinary routine litigation." Id. at Instruction 5. Therefore, where environmental-related litigation meets any of the stated thresholds, the company must disclose it. Perry E. Wallace, Climate Change, Fiduciary Duty, and Corporate Disclosure: Are Things Heating Up in the Boardroom? 26 VA. ENVTL. L. J. 293, 304 (2008). Last, Item 303 Management's Discussion and Analysis (MD&A) can be interpreted to require reporting of environmental and/or social information. The goal of the MD&A is to give investors a look at the company through the eyes of management, with emphasis on the company's prospects for the future. SEC. EXCH. COMM'N, MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS, SECURITIES ACT RELEASE NO. 6835, EXCHANGE ACT RELEASE NO. 26,831, INVESTMENT COMPANY ACT RELEASE NO. 16,961, 54 FED. REG. 22,227, 22,436 (1989) [hereinafter MD&A RELEASE]; Wallace, supra, at 306; Megan R. Dimitt, Electric Utilities & Climate Risk Disclosure in SEC Filings: Clearing the Air, 35 IOWA J. CORP. L. 449, 454 (2009). The reporting company must identify trends, demands, commitments, and uncertainties that will have economic or financial impact on it and disclose those items unless it determines that the event is not reasonably likely to occur. MD&A RELEASE, supra, at 22,430; Wallace, supra, at 307. Scholars have argued that the MD&A requires disclosure of impacts due to climate change. See, e.g., Wallace, supra, at 309–310. Businesses may also have to disclose environmental and/or social information to regulators outside of the financial reporting system. Some substantive environmental laws carry with them an obligation to disclose information to the regulatory agency. Examples include the Toxic Release Inventory, a U.S. federal law that requires disclosure to the Environmental Protection Agency of the release amounts of each of a list of chemicals. Emergency Planning and Community Right-to-Know Act (EPCRA) § 313, 42 U.S.C. § 11001 et seq. (1986). Similarly, federal employment discrimination laws require many employers covered by the laws to report annually to the Equal Employment Opportunity Commission. See, e.g., 29 C.F.R. § 1602.7 (1991) (requiring employers subject to Title VII of the Civil Rights Act of 1964 to file an EEO-1 report). Finally, states may also impose their own disclosure requirements on companies. In 2012, the California Transparency in Supply Chains Act went into effect, requiring certain large companies to disclose to the public the extent of their efforts, if any, to ensure that workers who are enslaved, coerced, or otherwise forced into service or who have been the victims of human trafficking do not produce the goods they sell. CAL. CIV. CODE § 1714.43 et seq. (West 2012); KAMALA D. HARRIS, CAL. DEP'T OF JUSTICE, THE CALIFORNIA TRANSPARENCY IN SUPPLY CHAINS ACT: A RESOURCE GUIDE 3 (2015). Enforcement of the Act is by the California Attorney General. Id.

[77]These are organization names, but the acronyms are also commonly used to refer to the reporting mechanisms created by the organizations.

[78]Since its creation, more than 12,000 organizations have prepared reports using the GRI framework; more than 30,000 reports have been created in accordance with GRI frameworks. See Sustainability Disclosure Database, GLOB. REPORTING INITIATIVE, http://database.globalreporting.org/ (last visited Apr. 7, 2019).

[79]For a discussion of GRI's definition of materiality, see infra text accompanying notes 79-80, 173.

[80]Ans Kolk, David Levy & Jonatan Pinkse, Corporate Responses in an Emerging Climate Regime: The Institutionalization and Commensuration of Carbon Disclosure, 17(4) EUROPEAN ACCT. REV. 719, 724 (2008). CDP has over 525 investor signatories, representing $96 trillion in assets. About Us, CDP, https://www.cdp.net/en/info/about-us (last visited Apr. 27, 2019). See also, CDP, Understanding climate risks and maximizing financial rewards: The benefits to signatories and members 3, available at https://6fefcbb86e61af1b2fc4-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rackcdn.com/comfy/cms/files/files/000/000/788/original/2017_investor_brochure_pages_web_v2.pdf.

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disclosure questionnaires, pre-determined sets of disclosure items related to either climate change or water use.[81] In 2011, the IIRC introduced the concept of "integrated reporting,"[82] an attempt to combine financial and non-financial reporting.[83] The IIRC framework is a broad set of guidelines, with no suggested disclosure items or questionnaire. Reporting companies have discretion to decide what to report consistent with the IIRC materiality definition.[84]

The approach to materiality plays out differently between GRI and the IIRC, on one hand, and CDP on the other. Both GRI and the IIRC eschewed the specific line item disclosures that are a part of mandatory financial reporting. Instead, each framework leaves reporting companies with broad discretion to determine the boundaries of the report. To guide the use of this discretion, they frame disclosure around the concept of materiality, charging reporting companies to disclose material information related to ESG issues.[85] In keeping with its stakeholder focus, GRI defines materiality as information on topics that "reflect the reporting organization's significant economic, environmental, and social impacts; or substantively influence the assessments and decisions of stakeholders."[86]

The IIRC utilizes an apparently more focused, but also apparently inconsistent, materiality approach. The IIRC framework defines material information as that which relates to the business's ability to create value in the short, medium, and long term.[87] This appears to reflect the IIRC's position that the purpose of integrated reporting is to provide information to providers of financial capital.[88] At the same time, however, the reporting framework contains a requirement that reporting companies discuss the organization's relationships with its key stakeholders.[89] Stakeholder interests are implicitly a part of the materiality determination process, insofar as stakeholders provide insight on issues that can affect the firm's short, medium, or long term value creation.[90] Thus, the IIRC process seems to ask companies to consider interests beyond those of investors in deciding what to report, but does not give guidance as to how to accomplish this balancing. In any event, both GRI and the IIRC approach to materiality leaves important decisions about report content in the hands of reporting companies.

The CDP process differs markedly from that of GRI or the IIRC, in that reporting to CDP is through a questionnaire. This approach is more akin to the line item portion of financial reporting, where an authority has predetermined the items to be disclosed and companies have little discretion to construct the content boundaries of their reporting.[91] The assumption is that all items on the questionnaire are material for all companies and, therefore, are required disclosure under the framework. Despite the fragmented nature of the definition of materiality that the GRI, IIRC, and CDP frameworks evidence, these key organizations had one critical factor in common. All three materiality approaches conceptualize ESG reporting as separate and distinct from financial reporting.

While non-profit organizations built reporting frameworks around new definitions of materiality, scholars attempted to connect ESG issues to the traditional notion of materiality. In a seminal article, Professor Williams argued that the SEC's legislative mandates gave the agency the authority to require expanded environmental and social disclosure

[81]A basic climate change questionnaire (without supply chain-related questions) for CDP consists of approximately 100 pages of questions. For an example of a climate change questionnaire, see *Questionnaires*, CDP, https://guidance.cdp.net/en/guidance?cid=2&ctype=theme&idtype=ThemeID&incchild=1&microsite=0&otype=Questionnaire&tags=TAG-646%2CTAG-605%2CTAG-599 (last visited Apr. 7, 2019).

[82]Accounting for Sustainability, *Our Impact/Timeline/2011*, https://www.accountingforsustainability.org/en/impact/timeline.html#item-2011 (noting launch of a Discussion Paper on the proposed framework in September 2011).

[83]*See The IIRC*, INTEGRATED REPORTING, http://integratedreporting.org/the-iirc-2/ (last visited Apr. 7, 2019). The IIRC defines an integrated report as communication about how an organization's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value in the short, medium and long term. INTEGRATED REPORTING, http://integratedreporting.org/ (LAST VISITED Apr. 7, 2019); *The International <IR> Framework*, INTEGRATED REPORTING ¶ 1.1 (2013), http://integratedreporting.org/resource/international-ir-framework/ [hereinafter *IIRC Framework*].

[84]*Id.* at ¶ 1.3–1.6.

[85]*See Consolidated Set of GRI Sustainability Reporting Standards 2016*, 3, 7, Glob. Reporting Initiative, https://www.globalreporting.org/standards/gri-standards-download-center/ (last visited Apr. 7, 2019) [hereinafter *GRI Reporting Standards*]; *IIRC Framework*, *supra* note 77, at ¶ 3.17–3.18.

[86]*GRI Reporting Standards*, *supra* note 79, at 10.

[87]*IIRC Framework*, *supra* note 77, at ¶ 3.17.

88Id. at ¶ 1.7 (stating that the purpose of an integrated report
is to explain to "providers of financial capital how an organization creates value over time.").

89Id. at ¶3.10.

[90]The framework outlines materiality determination as identifying, evaluating, and prioritizing matters that affect the firm's value creation. *Id.* at ¶3.18. The framework also specifically recognizes that stakeholders provide insights on economic, social, and environmental issues that affect the organization's ability to create value. *Id.* at ¶3.12.

[91]Although responding to CDP is technically voluntary and companies could choose to not respond to certain questionnaire items, CDP scores and rates reporting companies in a way that penalizes non-responsiveness. *See Climate change scoring methodology*, CDP, https://www.cdp.net/en/scores-2017/climate-change-scoring-methodology (last visited Apr. 7, 2019).

and articulated reasons why the reasonable investor would want this additional information.[92] Other authors further developed Williams' position by advancing empirical arguments that reasonable investors were, in fact, demanding ESG information.[93] A second line of inquiry focused on the use of mandated disclosure to achieve social aims.[94] A recent example is the conflict mineral disclosure rules that were part of the Dodd-Frank Act.[95] A related research stream draws connections between corporate disclosure and corporate governance.[96] Recent work in this vein sees federal disclosure requirements enacted since the 2008 financial crisis as focusing more on shareholder power to influence corporate conduct, and less on the creation of efficient capital markets.[97] Other scholars characterize ESG disclosure as a risk management practice.[98]

The contribution of GRI, CDP, and the IIRC materiality concepts to increasing the amount of raw information available is undeniable. However, information users remain unhappy with the state of corporate disclosure.[99] The broad scope of GRI's materiality definition presents challenges as it tries to be all things to all stakeholders. While CDP and IIRC ostensibly incorporate investor concerns through their definitions of materiality, CDP reporters disclose information on limited factors and the IIRC approach results in broad and inconsistent disclosure.[100] Thus, the materiality definitions developed for these ESG reporting frameworks produce information that is either incomplete or not comparable across companies.[101]

D. New Materiality for Investors

Continued separation of financial and ESG reporting particularly limited the value of sustainability information for investors.[102] The disconnect between financial and sustainability information created a persistent sense that companies did not really understand how sustainability factors impacted core operations, nor did the existing reporting financial and sustainability reporting frameworks require them to do so. The most recent developments in corporate reporting reflect attempts to remedy the shortcomings of the existing disconnect between financial and ESG reporting by reframing the *TSC* materiality definition.

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[92]Williams, *supra* note 8, at 1276–1290 (identifying compliance with the law, environmental and social practices that exceed the law, and management integrity as factors with economic relevance that should be the subjects of expanded disclosure).

[93]*See, e.g.,* Mitchell F. Crusto, *Endangered Green Reports: "Cumulative Materiality" in Corporate Environmental Disclosure After Sarbanes-Oxley*, 42 HARV. J. ON LEGIS. 483, 493–497 (2005) (identifying institutional investors and the insurance industry as key constituents pushing for expanded corporate environmental disclosure); Monsma & Olson, *supra* note 53, at 176–180 (arguing that social and environmental information is "tangibly related to the economic reality of a firm" and, therefore, desired by investors).

[94]An early article examined the materiality of companies' business relationships with countries and governments that are subject to U.S. economic sanctions. Note, *Should the SEC Expand Nonfinancial Disclosure Requirements?*, 115 HARV. L. REV. 1433 (2002).

[95]*See supra* note 30 and accompanying text. Professor Choudhury contends that social disclosure rules like the conflict mineral rules can advance social aims by forcing corporations to acknowledge social issues within the business environment. Barnali Choudhury, *Social Disclosure*, 13 BERKELEY BUS. L. J. 183, 216 (2016).

[96]*See, e.g.,* Faith Stevelman, *Transparency and Accountability: Rethinking Corporate Fiduciary law's Relevance to Disclosure*, 34 GA. L. REV. Rev. 505 (1999-2000) (articulating the connection between corporate fiduciary law and corporate disclosure to shareholders); Roberta S. Karmel, *Realizing the Dream of William O. Douglas – The Securities and Exchange Commission Takes Charge of Corporate Governance*, 30 DEL. J. CORP. L. 79 (2005) (arguing that the disclosure provisions of the Sarbanes-Oxley Act constitute the federalization of corporate governance).

[97]Ann M. Lipton, *Reviving Reliance*, 86 FORDHAM L. REV. 91,104-106 (2017).

[98]Virginia Harper Ho, *Nonfinancial Risk Disclosure and the Costs of Private Ordering*, 55 AM. BUS. L. J. 407, 411-13 (2018) (arguing that the current model of nonfinancial risk disclosure is ineffective); David Monsma & John Buckley, *Non-Financial Corporate Performance: The Material Edges of Social and Environmental Disclosure*, 11 U. BALT. J. ENVTL. L. 151, 161, 176-181 (2003–2004)(exploring the responsibility of firms for their non-financial disclosures and the risk of poor environmental and social performance on firm reputation and value).

[99]*See*, *e.g.,* Jeff Leinaweaver, *Is Corporate Sustainability Reporting a Great Waste of Time?*, THE GUARDIAN (Jan. 6, 2015), https://www.theguardian.com/sustainable-business/2015/jan/06/corporate-sustainability-reporting-waste-time; Robert Eccles et al., *The Need for Sector-Specific Materiality and Sustainability Reporting Standards*, 24(2) J. APPLIED CORP. FIN., 65, 65, 71 (2012); Neil Parmar, *Messy with Metrics*, CORP. KNIGHTS 41, 41-42 (Winter 2015)..

[100]*See* Mary Shapiro, *Investors Want More From Sustainability Reporting, Says Former SEC Head*, CFO J. (Nov. 12, 2015, 9:32 AM), https://blogs.wsj.com/cfo/2015/11/12/investors-want-more-from-sustainability-reporting-says-former-sec-head/; Leinaweaver, *supra* note 92.

[101]*See* Marianne Bradford et al., *Sustainability Reports: What Do Stakeholders Really Want?*,16 MGMT. ACCT. Q. 13, 13-14 (2014).

[102]A variety of studies surfaced shortcomings in existing reporting from the perspective of investors. A 2014 study conducted by PwC on investor attitudes on sustainability reporting found that most investors were dissatisfied with current reporting, especially insofar as it generally did not connect sustainability to business strategy. *Sustainability Goes Mainstream*, PWC, 7–8 (May 2014), http://www.truevaluemetrics.org/DBpdfs/Sustainability/PwC/pwc-sustainability-goes-mainstream-investor-views.pdf. In a follow-up survey, PwC discovered that only 29% of investors expressed confidence in the quality of the sustainability information they received from companies. *Investors, Corporates, and ESG: Bridging the Gap*, PWC, 7 (Nov. 11, 2016), http://www.corporatecomplianceinsights.com/investors-corporates-bridging-gap/. An EY investor survey echoed these complaints. A significant portion of investors responding to the survey stated that the inconsistency and lack of comparability of sustainability information kept them from considering sustainability issues in their investment decisions. *Is your non-financial performance revealing the true value of your business to investors?*, EY, 23–24 (2017), http://integratedreporting.org/wp-content/uploads/2017/04/EY_Is_your_nonfinancial_performance_revealing.pdf.

In 2007, a coalition of parties petitioned the SEC for interpretive guidance that would clarify the connection between climate change risk and materiality.[103] Petitioners claimed that "companies must consider climate risk in their review of information that may be *material* and subject to disclosure."[104] The 2007 Petition specifically incorporated the *TSC* definition of materiality, arguing that investor demand for climate-related information demonstrated that reasonable investors considered climate risk as part of the mix of information important in their decisions.[105] The 2007 Petition was hotly contested and highly politicized.[106] Nevertheless, in 2010, the SEC issued interpretive guidance, identifying climate change risk as potentially material information, as defined in *TSC*.[107]

Despite the apparent success of the 2007 Petition, its focus on a single ESG issue – climate – limited its impact. The Sustainability Accounting Standards Board (SASB) launched a more holistic and concerted attempt to leverage existing financial reporting mechanisms to advance the state of corporate reporting and move sustainability into the mainstream.[108]

Formed in 2011, SASB functions as an independent standard-setting organization for sustainability accounting standards.[109] SASB's mission is to create sustainability accounting standards for public corporations to disclose material information to investors in SEC filings, including the Form 10-K annual report.[110] SASB's dissatisfaction with the then-existing framing of the information asymmetry problem led to a vision and mission that emphasized investors as the leverage point to drive improved ESG performance.[111] SASB fully embraced the potential of *TSC* materiality to change corporate behavior in a way that improved sustainability outcomes.[112] Thus, its objective was to capture all factors associated with a firm's value creation by extending reporting to include material sustainability

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[103]CERES et al., *Petition for Interpretive Guidance on Climate Risk Disclosure 2*, U.S. SEC. & EXCH. COMM'N (Sept. 18, 2007), https://www.sec.gov/rules/petitions/2007/petn4-547.pdf [hereinafter *2007 Petition*]; Letter from Mindy Lubber, President, Ceres, to Mary Jo White, Chair, SEC (July 21, 2016) (available at https://www.sec.gov/comments/s7-06-16/s70616-214.pdf). Supplemental petitions were filed in 2008 and 2009 by the same signatories of the 2007 Petition. Each re-affirmed the petitioners request for clearer guidance from the SEC on climate risk disclosure requirements. CERES et al., *Request for Interpretive Guidance on Climate Risk Disclosure*, U.S. SEC. & EXCH. COMM'N (June 12, 2008), https://www.sec.gov/rules/petitions/2008/petn4-547-2008.pdf; CERES et al., *Supplemental Petition for Interpretive Guidance on Climate Risk Disclosure*, U.S. SEC. & EXCH. COMM'N (Nov. 23, 2009), https://www.sec.gov/rules/petitions/2009/petn4-547-2009.pdf. The Petitioners included investors and environmental groups. Institutional investors signing the petition included the California Public Employees' Retirement System (CalPERS) and state officials responsible for public pension funds in California, New York, Florida, North Carolina and several other states. *2007 Petition*, *supra*, at A-1 to A-3; 57–58. Environmental groups included Ceres, Environmental Defense, and Friends of the Earth. *Id.* at 57–58. The petitioners based their petition on claims of poor climate-related disclosure by corporations, arguing that the absence of government-mandated climate risk disclosure led to the use of voluntary disclosure mechanisms, yielding inadequate information. *Id.*, at 39.

[104]*2007 Petition*, *supra* note 96, at 9 (emphasis added).

[105]*Id.* at 14.

[106]Joel Kirkland, *SEC Issues Climate-Risk Guidance Despite Tough Political Environment*, NY TIMES (Jan. 28, 2010), https://archive.nytimes.com/www.nytimes.com/cwire/2010/01/28/28climatewire-sec-issues-climate-risk-guidance-despite-tou-27171.html. Opponents objected to the 2007 Petition for a variety of reasons, including the uncertainty of climate science and the cost of reducing greenhouse gas emissions. *Id.*

[107]*Id.* The Guidance went into effect on February 8, 2010. *See* SEC. & EXCH. COMM'N, Climate Guidance Regarding Disclosures Related to Climate Change, 17 CFR PARTS 211, 231 and 241, https://www.sec.gov/rules/interp/2010/33-9106.pdf (last visited Apr. 7, 2019).

[108]SASB's Conceptual Framework identified five "sustainability dimensions:" the environment, social capital, human capital, business model and innovation, and leadership and governance. *SASB CF 2017*, *supra* note 101, at 2-3. SASB standards are based on the TSC definition of materiality. *SASB's Approach to Materiality for the Purpose of Standards Development* 4, Staff Bulletin No. SB002-07082017, SUSTAINABILITY ACCT. STANDARDS BD. (2017), http://library.sasb.org/wp-content/uploads/2017/01/ApproachMateriality-Staff-Bulletin-01192017.pdf?hsCtaTracking=9280788c-d775-4b34-8bc8-5447a06a6d38%7C2e22652a-5486-4854-b68f-73fea01a2414 [hereinafter *SASB Staff Bulletin*].

[109]*SASB Rules of Procedure*, SUSTAINABILITY ACCT. STANDARDS BD., 4 (Feb. 2017), https://www.sasb.org/wp-content/uploads/2017/02/SASB-Rules-of-Procedure.pdf [hereinafter *SASB Rules*]; *SASB Conceptual Framework*, SUSTAINABILITY ACCT. STANDARDS BD., 1 (Feb. 2017), https://www.sasb.org/wp-content/uploads/2017/02/SASB-Conceptual-Framework.pdf [hereinafter *SASB CF 2017*]. SASB is a U.S. 501(c)(3) non-profit organization. Diane K. Schooley & Denise M. English, *SASB: A Pathway to Sustainability Reporting in the U.S.*, CPA J., Apr. 2015, at 22, 24

[110]*SASB CF 2017*, *supra* note 101, at 1; *SASB Rules*, *supra* note 101, at 4; *Why SASB?*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/why-sasb/ (last visited Apr. 13, 2019).

[111]SASB envisions an "investment universe where a shared understanding of companies' sustainability performance enables companies and investors to make informed decisions that drive improved sustainability outcomes." *Mission*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/governance/ (last visited Apr. 27, 2019). To achieve this vision, SASB sees its mission as "establish[ing] disclosure standards on sustainability matters that facilitate communication by companies to investors of decision-useful information." *Id.* SASB's Conceptual Framework defined "sustainability" as "corporate activities that maintain or enhance the ability of the company to create value over the long term." *SASB CF 2017*, *supra* note 101, at 2, 4–7.

[112]Steve Lydenberg et al., *From Transparency to Performance* iv (2010) [hereinafter IRI Report], https://iri.hks.harvard.edu/links/transparency-performance-industry-based-sustainability-reporting-key-issues. *See also* Jaclyn Jaeger, *Sustainability Reporting's Focus Now on Materiality*, COMPLIANCE WEEK 22, 22-23 (Aug. 2014) (noting SASB's work developing reporting standards that challenge companies to consider how to incorporate sustainability issues into business strategy).

topics.[113] SASB's name and function are modeled on FASB, the organization charged by the SEC with creating financial accounting standards.[114] SASB sees itself as the sustainability equivalent of FASB, crafting standards to disclose ESG impacts in SEC filings.[115] SASB's works to extend accounting infrastructure to incorporate material sustainability factors, drawing a direct link between ESG factors and financial materiality.[116] More importantly, SASB's approach to sustainability disclosure parallels the logic underlying U.S. securities laws by focusing on sustainability factors that are most likely to be material, as defined under *TSC*.[117] SASB explicitly utilizes the *TSC* materiality definition as the basis for its standard-setting process, which defines operational metrics on ESG topics likely to be material.[118] To date, SASB has created disclosure standards for 77 industries.[119]

E. Leverage for Change: Investor Desire

The SEC's failure to include ESG factors into the mandatory reporting framework ignores the market signals of the importance of these issues and hampers progress toward more sustainable business in two interconnected ways. Relegating sustainability disclosure to voluntary reporting systems discounts the practical value of a mandatory system. Commentators note the importance of legal requirements – what Professor Williams calls the "power of legality" - in driving changes in behavior.[120] As long as sustainability disclosure remains separate from required disclosure, changes in corporate conduct will be few and slow. The leverage point for change lies with investors, and investors desire improved ESG information.[121] Investor attempts to access ESG information outside the mandatory disclosure system (such as BlackRock's annual letter) are an indication of investor interest. Thus, the SEC's position ignores the wants of those it is supposed to protect by thwarting ESG integration.[122]

Having separate bodies of information for financial and sustainability data makes it difficult to identify how ESG performance affects the financial value of a company, which stymies the use of ESG factors in investment decisions.[123] Business acts largely as incentivized, either through costs and penalties(such as increased regulation) or through rewards. Inadequate ESG information means that investors cannot effectively offer the reward of investor dollars to foster changes in corporate behavior.[124] Corporate changes to improve sustainability performance are slow because the incentives are uncertain and unclear. However, better information could unleash investment in favor of sustainability, incentivizing business to bring its practices in line with investor interests, moving sustainability forward.

SASB's reporting framework can act as a mechanism to provide investors the information needed to serve ESG integration. The convergence of financial materiality and ESG materiality speaks to investors' desire for decision-useful sustainability information. With SASB's industry-specific KPIs, investors have a tool to pressure companies to disclose information in a way that allows for allocation of investment funds to promote sustainability along two avenues. First, investors can channel money to reward good sustainability performers and incentivize them to continue their beneficial practices. Investors can also take the approach of KKR and target companies that are ESG laggards,

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[113] *SASB CF 2017*, *supra* note 101, at 4-5.

[114] *See Industry-Based Sustainability Standards to Guide Corporations and Investors on Material Issues for Disclosure in the Form 10-K*, SUSTAINABILITY ACCT. STANDARDS BD. 12 (Dec. 7, 2011) [hereinafter *SASB Briefing Document*].

[115] *Id.* at 15.

[116] SASB CR 2017, *supra* note 101, at 4-5 (explaining that sustainability accounting extends traditional financial accounting by incorporating material sustainability related issues such as risks associated with mismanagement of ESG issues); *SASB Staff Bulletin*, *supra* note 108, at 4 (noting that SASAB identifies only sustainability factors that have material impacts and warrant standardized disclosure).

[117] *SASB Staff Bulletin, supra note 116, at 3-4.*

[118] *SASB CF 2017*, *supra* note 69, 5, 9–10; *SASB Staff Bulletin*, *supra* note 109, at 4. SASB's disclosure standards are in the form of industry-specific key performance indicators (KPIs) on ESG issues that may meet the threshold of *TSC* materiality. *IRI Report*, *supra* note 104, at 10; *SASB CF 2017*, *supra* note 101, at 12. The ultimate decision on whether a particular metric meets the definition of materiality for a specific company remains in the hands of the reporting company. *SASB Staff Bulletin*, *supra* note 109, at 1-2.

[119] *Standards Overview*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/standards-overview/ (last visited Apr. 13, 2019).

[120] *See* Cynthia A. Williams, *The Global Reporting Initiative, Transnational Corporate Accountability, and Global Regulatory Counter-Currents*, 1 UC IRVINE J. INT'L, TRANSNAT'L, & COMP. L. 67, 81–82 (2016) (noting that the evidence indicates that disclosure must be mandatory to have operational effects). *But cf.*, Gerlinde Berger-Walliser & Inara Scott, *Redefining Corporate Social Responsibility in an Era of Globalization and Regulatory Hardening,* 55 AM. BUS. L. J. 167 (2018) (discussing the drawbacks of the legalization of corporate social responsibility).

[121] *See supra* notes 92-95, and accompanying text.

[122] ESG integration is defined as incorporating environmental, social and governance factors into business and investment decisions. Eccles & Kastrapeli, *supra* note 26, at 5.

[123] *Id.* at 13–15 (noting the lack of specific types of ESG data and the impact on decision making).

[124] *Id.* at 15 (arguing that without data on material issues, it is "impossible" for investors to have the necessary knowledge for their investment decisions).

using investment to mitigate their worst practices and start them on a trajectory toward sustainability.[125] Either way, SASB's reporting framework lays the groundwork for an infusion of capital to foster improved corporate sustainability performance.

On its surface, the development of the materiality concept is about the mechanics of corporate disclosure. With SASB's adoption of *TSC* materiality, the term's meaning appears to have come full circle, with return to focus on investors' information needs. This would suggest that the SEC and SASB are natural partners in the field of corporate reporting. In fact, the SEC's public denigration of SASB's work demonstrates its antipathy toward SASB's goals. The field of sociology provides a useful framework to interpret the divide between SASB and the SEC, and to better understand the trajectory of materiality.

II. Understanding the Social Meaning of Materiality

The gap between SASB and the SEC centers on the term materiality and exists at the level of meaning. How can a word be defined the same way yet carry different meaning? The sociological theory of social constructionism helps unpack the idea of meaning, and its ramifications for materiality and corporate reporting.

A. Defining Social Meaning

Social constructionism holds that our knowledge of the world is not objective or the result of direct perception of the world.[126] The true nature of things in the world is a product of social interactions; meaning exists as it is defined in and by a society.[127] Social constructionism argues that the meaning of phenomena is created through social interactions.[128] Social interactions can be seen as sensemaking activities, where people make their world logical and meaningful.[129] Groups negotiate and construct shared understandings of what things in the world mean; these understandings reflect the group's norms and its social order.[130]

This shared interpretation of phenomena is referred to as social meaning. Social meaning is a product of the processes of collective definition by a given group.[131] It is the shared agreement on what specific phenomena mean and the concepts and language used to describe the phenomena.[132] Context heavily influences the creation of social meaning,[133] with cultural, historical, and socioeconomic factors all affecting social meaning.[134] Thus, different groups may have different ideas for categorizing phenomena, and for articulating these categorizations.[135] The issue of homelessness provides an illustrative example. In the 1970's, Washington, D.C. was among the first cities to recognize the emerging social problem of homelessness. The main non-profit organization focusing on the issue initially framed homelessness around the characteristics of many homeless as capable of making rational choices, but unwilling to cooperate with the rules imposed at government-run shelters.[136] Gradually, their framing evolved to focus on economic inequality as the cause of homelessness.[137] The eventual social meaning of homelessness centered on

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[125] *See supra* note 91 and accompanying text (identifying incorporation of ESG criteria as risk management).

[126] VIVIEN BURR, SOCIAL CONSTRUCTIONISM 2–3, 6 (2d ed. 2003). Social constructionism has its intellectual roots in work on the sociology of knowledge, the study of how social forces construct knowledge, a field pioneered by Berger and Luckmann. Joel Best, *Constructionist Social Problems Theory*, 36 ANNALS INT'L COMM. ASS'N 237, 239 (2013). Their work is related to ethnomethodology, a discipline that studies how people construct and make sense of social life. BURR, *supra*, at 12–13; James A. Holstein & Gale Miller, *Social Constructionism and Social Problems Work*, *in* **RECONSIDERING SOCIAL CONSTRUCTIONISM** 151, 151-153 (James A. Holstein & Gale Miller eds., 1993). Social constructionism rejects essentialism. *See* Burr, *supra*, at 13; *cf.* Natasha J. Silber, Note, *Unscrambling the Egg: Social Constructionism and the Antireification Principle in Constitutional Law*, 88 N.Y.U. L. REV. 1873, 1880 (2013) (noting essentialism is treated with suspicion).

[127] Timothy F. Malloy, *The Social Construction of Regulation: Lessons from the War Against Command and Control*, 58 BUFF. L. REV. 267, 273-74 (2010); Best, *supra* note 118, at 239; JONG S. JUN, THE SOCIAL CONSTRUCTION OF PUBLIC ADMINISTRATION 11, 48 (2006); Joseph W. Schneider, *Social Problems Theory: The Constructionist View*, 11 ANN. REV. SOC. 209, 210 (1985) (describing a call for a revised conceptualization of social problems as viewed through a constructivist lens); Stephen Hilgartner & Charles L. Bosk, *The Rise and Fall of Social Problems: A Public Arenas Model*, 94 AM. J. SOC. 53 (1988).

[128] Best, *supra* note 118, at 239; Jun, *supra* note 119, at 11; Malloy, *supra* note 119, at 273–74; Silber, *supra* note 118, at 1880.

[129] Catrien J.A.M. Termeer, *Barriers to New Modes of Horizontal Governance*, 11 PUB. MGMT. REV. 299, 301 (2009). Social constructionist scholars identify meaning making as a key aspect of human life. *See, e.g.*, Silber, *supra* note 118, at 1880

[130] Holstein & Miller, *supra* note 118, at 153-54.

[131] Hilgartner & Bosk, *supra* note 119, at 53.

[132] Holstein & Miller, *supra* note 118, at 153.

[133] Cynthia J. Bogard, Claimsmakers and Contexts in Early Constructions of Homelessness: A Comparison of New York City and Washington, D.C., 24 SYMBOLIC INTERACTION 425, 427–28 (2001); Silber, supra note 80, at 1880.

[134] Burr, supra note 118, at 3–4.

[135] Id.; Holstein & Miller, supra note 118, at 154; Miller, supra note 122, at 350.

[136] Bogard, supra note 125, at 434-435.

[137] *Id.* at 436.

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prevailing economic conditions, rather than the personal characteristics of the homeless population. Proposed policy solutions centered on meeting the immediate needs of the homeless by providing shelter with dignity.[138] By contrast, New York City defined homelessness around the personal deficiencies of homeless persons. New York state budget cuts had resulted in the deinstitutionalization of patients from state psychiatric hospitals and New York City officials claimed that a significant percentage of the City's homeless were former psychiatric facility patients.[139] For New York City officials, many advocacy groups for the homeless, and major media outlets, the homeless problem, was, thus, a mental health issue.[140] New York state government officials, on the other hand, portrayed the City's homeless population as victims of the City's own housing policies and increasing gentrification.[141]

This example illustrates two important and related aspects of social meaning. First, different parties can and do understand and characterize the same phenomenon differently; they attach different social meaning to the same set of facts. This occurs because social meaning is based on a specific experience of the situation and a specific idea of what the situation is about.[142] More importantly, the social meaning of a phenomenon can change, even though the phenomenon itself has not.[143] Since social meanings are "constructed," change from one social meaning to another happens through specific interventions, not mere evolution.[144] Changing social meaning proceeds by breaking up the understandings currently attached to phenomena and replacing them with new characterizations of those phenomena, as occurred in Washington D.C.[145] These new characterizations represent alternate social norms, advocated for by specific groups.[146] At the point where the new characterizations become widely accepted, the phenomena has acquired a new social meaning.[147]

Social constructionist scholarship focuses on the social processes used to change and shape social meaning around specific conditions (such as financial collapse or homelessness).[148] The activity of making complaints or demands around existing social meaning is called *claimsmaking*.[149] Claimsmaking is comprised of intervention activities (such as writing an opinion article for the newspaper, staging a demonstration or boycott, or submitting a petition to a legislator) that seek to define social meaning.[150]

Spector and Kitsuse propose a natural history model to analyze claimsmaking activities (CMA), which highlights the interactions between government and non-government actors in the claimsmaking process.[151] The model is based around stages that can be used to analyze the trajectory of intervention activities, as well as to create strategy for CMA. At the initial stage, claimsmakers attempt to assert the characterization of some situation as undesirable and to define the problem through their characterization of the problem. This is where parties identify the concepts and language used to describe the phenomena that constitute the frame for its social meaning.[152] The frame reflects a particular

[138] *Id.* at 432–35.
[139] *Id.* at 437–38.
[140] *Id.* at 437–38. The New York Times, for example, adhered to the argument that deinstitutionalization of mental health patients was a major cause of homelessness in the City. *Id.* at 438 (commenting on the Times' allegiance to deinstitutionalization as a causal model as evidenced by a 19809 article).
[141] *Id.* at 438. Then-mayor Ed Koch had resisted calls to create more homeless shelters, arguing that such shelters had a damaging effect on neighborhood property values. *Id.* at 437.
[142] MALCOLM SPECTOR & JOHN I. KITSUSE, CONSTRUCTING SOCIAL PROBLEMS 76, 78–79 (Cummings Pub. Co. 1977)
[143] For example, the state of New York eventually acknowledged the role that its deinstitutionalization of psychiatric patients played in the increase of homelessness. Bogard, *supra* note 125, at 438–39.
[144] Lawrence Lessig, *The Regulation of Social Meaning*, 62 U. CHI. L. REV. 943, 961–62 (1995).
[145] *Id.* at 962.
[146] Social constructionism is often used as a tool of change to challenge the status quo. Silber, *supra* note 118, at 1880.
[147] Lessig, *supra* note 136, at 962.
[148] Malloy, *supra* note 119, at 276; Silber, *supra* note 118, at 1880; SPECTOR & KITSUSE, *supra* note 134, at 76.
[149] SPECTOR & KITSUSE, *supra* note 134, at 75.
[150] Malloy, *supra* note 119, at 277; SPECTOR & KITSUSE, *supra* note 134, at 78–79.
[151] Hilgartner & Bosk, *supra* note 119, at 54. Natural history models are used to chart the development of issues over time and through different stages of a development process. *Id.*; *see also* SPECTOR & KITSUSE, *supra* note 134, at 142.
[152] Schneider, *supra* note 119, at 214; Best, *supra* note 118, at 246–47. The term "frame" is most commonly used in the study of social movement organizations. It is the equivalent of the concept of rhetoric in claimsmaking. *Id.* at 246.

experience of the social condition.[153] Frames often interpret the world in ways that differ from and challenge the existing characterizations of situations.[154] They can serve a transformative function by recharacterizing phenomena and, thus, redefining the issue.[155]

Frames are also an outcome of the negotiation of shared meaning and the process of creating social meaning.[156] Determining the frame and language used to frame the situation has important pragmatic impacts on CMA because frames are used to attract adherents to a particular social meaning. Frames exist in what Best has termed a "social problems marketplace," where claims compete for attention and institutional response.[157] Attracting supporters to a claim requires that the claimsmaker's frame align with the potential adherents' frame.[158] Framing also indicates the claimsmaker's attempt to exert control, or *ownership*, over the social meaning of the issue.[159] Different claimsmakers, including government actors, may all be vying for control of framing of the situation; some claims may challenge the status quo while others may favor maintaining the status quo.[160]

If claimsmakers are successful in pressing their claim, government or some other institution with authority over the situation, may respond to the CMA by recognizing the legitimacy of the claimsmakers.[161] This official response may, in some circumstances, decrease the claimsmaker's control over the claim, as an agency with its own frame exerts control over the problem.[162] The government, for example, both initiates and receives claims[163] and may have institutionalized a specific meaning around a given situation.[164] Thus, government itself can control, and even change, the meaning of a situation through framing that is created and controlled by bureaucrats.[165] Further, recognition is no guarantee that government will actually address the social issue. The authority may recommend no change, recommend a change that does not satisfy the claimsmakers, or recommend a change that is not subsequently enacted.[166]

Where official action on the claimsmakers' complaints yields unsatisfactory results, new CMA may surface. Often, claims at this stage relate to inadequate, ineffective, or unjust government procedures, rather than to the original social issue.[167] They attempt to push government to address what are perceived to be inadequate or ineffective government measures around a social problem. At some point, claimsmakers may decide that it is no longer possible to "work within the system" to achieve satisfactory change.[168] Activities become premised on challenging the legitimacy of the established authority and its processes for addressing the claims.[169] The claimsmakers' focus may shift from complaints about the established procedures to the creation of alternative procedures that function outside the government framework.[170]

[153] Robert D. Benford & David A. Snow, *Framing Processes and Social Movements: An Overview and Assessment*, 26 ANN. REV. SOC. 611, 614–15 (2000); Hilgartner & Bosk, *supra* note 119, at 58. Framing is another aspect of the construction of meaning. David A. Snow, *Framing and Social Movements*, *in* THE WILEY-BLACKWELL ENCYCLOPEDIA OF SOCIAL AND POLITICAL MOVEMENTS (David A. Snow et al. eds., 2013), available at https://onlinelibrary.wiley.com/doi/abs/10.1002/9780470674871.wbespm434.
[154] Benford & Snow, *supra* note 145, at 614.
[155] Snow, *supra* note 145. Snow identifies two additional functions served by frames: frames focus attention on what is relevant in the situation and articulate a connected set of meanings about the situation.
[156] *See* Benford & Snow, *supra* note 145, at 614. Benford & Snow note that framing is a contested process, with different parties advocating for different language in the frame. *Id.* at 625. Lessig recognizes language itself as "constitutive social activity." Lessig, *supra* note 136, at 976.
[157] Best, *supra* note 118, at 245–47; Malloy, *supra* note 119, at 281.
[158] Best, *supra* note 118, at 247. Benford and Snow describe this as the "resonance" of the frame with potential adherents. Benford & Snow, *supra* note 145, at 619–21. Claimsmakers will sometimes utilize distinctive terminology in framing to attract adherents. A. Clay Schoenfeld et al., *Constructing a Social Problem: The Press and the Environment*, 27 SOC. PROBS. 38, 39–40 (1979).
[159] Malloy, *supra* note 119, at 278.
[160] SPECTOR & KITSUSE, *supra* note 134, at 148; Malloy, *supra* note 119, at 278–79.
[161] SPECTOR & KITSUSE, *supra* note 134, at 148.
[162] Holstein & Miller, *supra* note 118, at 169. If the government takes over the issue, it may disenfranchise the original group, sometimes threatening the group's ability to survive. SPECTOR & KITSUSE, *supra* note 134, at 149.
[163] Schneider, *supra* note 119, at 216.
[164] Holstein & Miller, *supra* note 118, at 169; Benford & Snow, *supra* note 145, at 626 (noting the potential impact of framings by "institutional elites").
[165] Malloy, *supra* note 119, at 277-79; Schneider, *supra* note 119, at 216–17; Hilgartner & Bosk, *supra* note 119, at 69 (noting that government professionals act as meaning "gatekeepers," exerting control over social meaning).
[166] SPECTOR & KITSUSE, supra note 134, at 149.
[167] *Id*. at 151–52.
[168] *Id*. at 153.
[169] *Id.*
[170] SPECTOR & KITSUSE, *supra* note 134, at 153.

B. The Changing Social Meaning of Materiality

The actual course of CMA and social meaning development is not linear. Social meaning itself is constructed and, therefore, can be de-constructed and re-constructed differently.[171] The dynamism of this process means that claimsmaking activities move forward and backward through the phases of Spector and Kitsuse's model as societal norms and expectations evolve. The development of materiality can be viewed as a series of interventions where claimsmakers acted to shape the direction of materiality as reflecting societal expectations.

1. Materiality as Financial Information

Following the 1929 stock market collapse, government attention centered on whether the collapse indicated the need for regulation of the market. Those who opposed regulation framed the situation as a normal, if unfortunate, market mechanism that would purge the system and self-correct without regulation.[172] However, the majority of Congress saw the collapse as an issue of financial misdealing and misdeeds.[173] Their claimsmaking activities framed the discussion in terms of bad companies and bad bankers who had acted in ways that jeopardized the economy and the savings of many citizens. They argued that those who created the collapse would not voluntarily change their behavior, leaving regulation as the only viable option.[174] Some advocates of regulation framed the issue as the need for government supervision of listed companies, while other framed the issue as an information asymmetry problem.[175] Those who saw the fundamental cause of the market collapse as inadequate information for investors eventually won the day and created our mandatory disclosure system with its focus on materiality.[176]

The social meaning embedded in the political debate over regulation of financial markets reflected changing attitudes toward the relationship between business and society. Imposition of a regulatory regime carried the message that financial misdeeds needed regulating, and that society could not rely on bankers to self-regulate or the market to self-correct. Creating a legal requirement to disclose information communicates the belief that, absent such a requirement, companies simply will not reveal information about themselves. Construction of a complex legal apparatus for corporate reporting also acted as a norm catalyst, creating a nascent expectation of transparency in investors.[177] The narrow focus of the Securities Acts reflects the claimsmakers' narrow view of business impacts on society. Policy advocates argued that business behavior led to the stock market collapse and therefore directly impacted investors;[178] the social meaning of their framing was thus limited to the financial information needed to protect investors and resurrect the economy.

Although the government had been slow to become involved in the recovery from the stock market collapse, the accelerated rate of involvement with the change of presidential administrations is an example of the power of government as claimsmaker. Government has at its disposal several unique tools to utilize in its CMA. For example, Congress convened public hearings to publicize the misdeeds that led to collapse of the market and rallied the public

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[171]Termeer, *supra* note 121, at 301.

[172]The incumbent Presidential administration of Herbert Hoover, along with bankers and Wall Street executives, were adherents to this position. JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET 3-12 (Aspen Publishers, 3d ed. 2003). Some Republicans, including President Hoover, questioned whether the federal government had the authority to regulate the stock exchanges. *Id.* at 5.

[173]Congressional feeling was fueled by public hearings held by the Senate Banking and Currency Committee to investigate the causes of the collapse. *Id.* at 5. The hearings documented the practices of Wall Street bankers and executives that ostensibly caused the collapse, including unsound lending and borrowing practices and high executive compensation. *Id.* at 23-26. For a detailed discussion of the hearings, see *id.* at 21 – 38.

[174]*Id.* at 5.

[175]Some advocated for a degree of national industrial planning and a greater role for government in judging the financial value of companies. *Id.* at 41. Proposals included the creation of a national Economic Council to provide "integrated industrial planning." *Id*. Calls for reconsideration of federal merit review of securities offerings resurface in times of economic collapse. In the wake of the 2008 financial collapse, for example, scholars returned to arguments for merit review. *See generally* Daniel J. Morrissey, *The Road Not Taken: Rethinking Securities Regulation and the Case for Federal Merit Review*, 44 U. RICH. L REV. 647 (2009–2010).

[176]This group included new President Franklin Roosevelt. In a message to Congress, Roosevelt wrote that the government "should not take any action which might be construed as approving or guaranteeing that newly issued securities are sound….There is, however, an obligation upon us to insist that every issue of new securities…shall be accompanied by full publicity and information…." Seligman, *supra* note 164, at 53.

[177]For a detailed discussion of the connection between norms and law, *see* Lessig, *supra* note 136; Cass R. Sunstein, *Social Norms and Social Roles*, 96 COLUM. L. REV. 903 (1996). *See also* Larry Cata Backer, *Transparency Between Norm, Technique and Property in International Law and Governance: The Example of Corporate Disclosure Regimes and Environmental Impacts*, 22 MINN. J. INT'L L. 1 (2013) (discussing hard and soft law as embedding norms).

[178]Professor Williams notes that the chair of the Senate Banking and Currency Committee, Senator Fletcher, defined the cause of the stock market collapse as people having been persuaded to invest their money in securities without being given any information on the securities. *Williams, supra* note , at 1232-1233. Williams identifies investor protection as "a major goal" of the Securities Acts. *Id.*, at 1234.

to the need for regulation.[179] President Roosevelt favored regulation of a specific type and had sufficient influence over Congress to give government control over the definitions and framing of the issue, as well as much of the social meaning of the situation.[180] The result was the Securities Acts and the now-familiar mandatory disclosure regime with its focus on material information.

Embedding transparency in legal constructs gave the government the upper hand in setting and controlling the social meaning of the corporate reporting regime. The exclusive focus on investor protection is understandable, given the context of the market collapse that catalyzed creation of the disclosure regime. The limited range of information reflects society's concerns at the time. But the focus on exclusively financial information also reflects societal expectations in a broader sense. There was no awareness of or interest in environmental issues among the population as a whole, nor did we have the global supply chains that exist now, with the attendant social issues.

The 1970's saw some dissatisfaction with the strictly financial focus of the existing disclosure framework, as evidenced by the attempts to define qualitative materiality to incorporate ethics issues into mandated disclosure.[181] However, this movement enjoyed only weak support from the SEC, which still favored a purely economic definition of materiality. Thus, the first frame for materiality – a focus on financial information for investors as epitomized by the *TSC* definition of materiality – was largely uncontested.

2. Materiality and Sustainability Information

Toward the end of the 20th century, societal expectations began to change, with increased interest in sustainability issues such as pollution and workers' rights.[182] New claimsmakers challenged the status quo of corporate reporting practices and reframed the idea of materiality.[183] These claimsmakers represented stakeholder groups, other than investors, who wanted information on corporate operations to better assess business's impact on the world.[184] They included environmental groups, human rights organizations, and civil rights groups.[185] For them, defining materiality in terms of investor needs carried with it the message that business's responsibilities were to its investors only. These claimsmakers argued that, since business had impacts beyond its investors, it also had responsibilities beyond its investors, including responsibilities to disclose non-financial information.[186] They redefined the issue as not merely fostering efficient markets, but fostering a better world.[187] The existing mandatory reporting scheme, which focused nearly exclusively on disclosure of financial information, did not meet the information needs of these groups, nor did it reflect their view of what was material information.

Sustainability claimsmakers framed the problem around expanded responsibilities for business to society.[188] They viewed the information asymmetry issue to include information users beyond investors and information in addition to financial information.[189] Their definitions of materiality reflect this broader social meaning. GRI's materiality

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[179]The hearings featured testimony by high-profile Wall Street bankers, called to garner media attention and gain popular support for regulation. *See* Steve Thel, *The Original Conception of Section 10(b) of the Securities Exchange Act*, 42, STAN. L. REV. 385, 434 (1990). As the press reported details of the bankers' testimony, the public grew outraged at the apparent greed of the bankers and favored regulation of the securities industry. *Id.* at 408–09.

[180]SELIGMAN, *supra* note 164, at 41–42

[181]*See supra* notes 67-70, and accompanying text.

[182]*See, e.g.*, Stacy J. Silveira, Comment, *The American Environmental Movement: Surviving Through Diversity*, 28 B.C. ENVTL AFF. L. REV. 497, 503–11 (2001), for an account of the modern environmental movement in the U.S.

[183]*See supra* notes 77 – 90 and accompanying text.

[184]Williams, *supra* note , at 1246-1247 (recounting efforts in the 1970's to expand social disclosure).

[185]*Id.*

[186]*Id.* GRI based its call for expanded corporate reporting on the claim of business impacts on "the economy, the environment, and/or society." *GRI Reporting Standards*, *supra* note , GRI 101: Foundation 3.

[187]GRI, for example, founded its claims on the concept of sustainable development and adopted the Brundtland Commission definition of "development which meets the needs of the present without compromising the ability of future generations to meet their own needs." *GRI Reporting Standards*, *supra* note , GRI 101: Foundation 3. Since all organizations contribute either positively or negatively to the goal of sustainable development, GRI argued that organizations should disclose their contributions to that goal. *Id.*

[188]*See supra* notes 188 – 189 and accompanying text.

[189]*See supra* note 186 and accompanying text.

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definition, with its focus on the information needs of stakeholders, has been influential in expanding the discussion of materiality.[190] Although the CDP and IIRC materiality definitions lack the breadth of GRI's, they carry with them the presumption that the concept of materiality includes ESG information.[191]

We might expect that these different framings around ESG disclosure would attract different types of adherents to the claimsmakers' initiatives. In fact, this has not been the case. Use by companies undertaking ESG reporting has increased for all three frameworks.[192] All three organizations partner with a variety of other non-profit organizations, professional organizations, and intergovernmental organizations.[193] While CDP's database of reported information is intended to be used by investors to a greater extent than it appears are GRI or IIRC reports, this difference is not surprising, given CDP's structure and framing.[194] The coalescence of adherents around all three organizations may reflect the nature of ESG reporting at this stage. Each of the organizations' framings align partially with the frames of potential adherents, leaving no clear winner in the competition for attention.[195]

All three of these organizations have garnered considerable power in the ESG reporting field. However, they do not appear to try to use this power to control the social meaning of ESG disclosure within the context solely of ESG reporting. Each has its own concepts defining materiality for reporting purposes, but the field seems constructed to tolerate differences in problem definition.[196] In a new field where ideas are in the process of development, tolerance for different definitions may help evolution of the field, as it allows for experimentation with multiple different possibilities.[197]

The social meaning of the ESG reporting movement's definition of materiality – that business carries responsibility for economic, environmental and social impacts and must disclose information on all three – reflects increased societal expectations for business. However, its notion of materiality conceptualizes ESG impacts as separate from financial impacts, and ESG reporting and separate from financial reporting. Even the CDP's focus on providing information for investors did so outside the parameters of financial reporting. Bisecting the information asymmetry problem into financial and non-financial categories sent two separate but related messages. First, it echoed the prevailing belief that environmental and social performance had no impact on financial performance. It separated these categories at the operations level, not merely the information level. Since environmental and social issues were not conneed to core operations, business could continue to treat them as secondary concerns, isolated at the periphery. Thus, in the minds of many businesses, ESG reporting and performance improvements were convenient extras to pursue for improved

[190] *See, e.g.*, *Materiality*, SUSTAINABILITY, https://sustainabilty.com/materiality/ (last visited Apr. 7, 2019) (identifying stakeholder expectations as important in determining materiality of issues); *Statement of Common Principles of Materiality of the Corporate Reporting Dialogue*, CORP. REPORTING DIALOGUE (2016), https://corporatereportingdialogue.com/wp-content/uploads/2016/03/Statement-of-Common-Principles-of-Materiality.pdf (identifying the information needs of report stakeholders as a common principle of corporate reporting frameworks. Firms also routinely connect materiality and stakeholders. For an empirical analysis of the corporate use of materiality and stakeholder engagement in the GRI and <IR> reporting frameworks, see Ruth Jebe, *Corporate Sustainability Reporting and "Material Information:" An Empirical Study of Materiality under the GRI and <IR> Frameworks*, 33 CONN. J. INT'L L. 95 (2017).
[191] *See supra* notes 81–84 and accompanying text.
[192] GRI had about 400 reports prepared in accordance with its standards in 2005; by 2010, this number increased to over 1800 report. *A new phase: the growth of sustainability reporting*, GLOB. REPORTING INITIATIVE 7 (2010/2011), https://www.globalreporting.org/resourcelibrary/GRI-Year-In-Review-2010-2011.pdf. CDP has shown similar growth. In 2010, approximately 2,500 organizations were responding to CDP questionnaires. *CDP Releases 2010 Reports for Global 500 and S&P 500*, ECONOMETRICA, https://econometrica.com/article/cdp-releases-2010-reports-for-global-500-and-sp-500 (last visited Apr. 17, 2019). Currently, 7,000 companies report to CDP. *About us*, CDP, https://www.cdp.net/en/info/about-us (last visited Apr. 17, 2019).
[193] For example, GRI works with the Organization for Economic Cooperation and Development (OECD), the UN Global Compact, and ISO, an international standard-setting organization. *GRI's Alliances and Synergies*, GLOB. REPORTING INITIATIVE, https://www.globalreporting.org/information/about-gri/alliances-and-synergies/Pages/default.aspx (last visited Apr. 27, 2019). CDP collaborates with the World Business Council for Sustainable Development (WBCSD), the Climate Disclosure Standards Board, and the World Wildlife Fund. CDP, *Our collaborations*, https://www.cdp.net/en/info/collaborationns (last visited Apr. 27, 2019). The IIRC also collaborates with the WBCSD, as well as with professionals groups such as the International Federation of Accountants (IFAC) and the Chartered Institute of Management Accountants (CIMA). IIRC, *IIRC Partners*, https://integratedreporting.org/the-iirc-2/iirc-partners/ (last visited Apr. 27, 2019).
[194] The CDP website offers data specifically for investors as part of its investor membership category. CDP, *Explore CDP's data for cities, companies, and investors/Data for investors*, https://www.cdp.net/en/data (last visited Apr. 27, 2019); CDP, *Become a member*, https://www.cdp.net/en/investor/signatories-and-members (last visited Apr. 27, 2019)(noting that CDP provides investor members with environmental data infrastructure and access to CDP data).
[195] *Cf.* Best, *supra* note 118, at 247 (discussing competing claims in a social problems marketplace).
[196] The sustainability reporting community is a fairly small group that appears to have strong internal ties: each of the three organizations discussed here actively collaborates with the other two. *See supra* note 176.
[197] Spector and Kitsuse note that, even where counterclaims are raised in response to CMA, the resulting conflict can serve to increase the visibility of debate and generate greater public awareness. SPECTOR & KITSUSE, *supra* note 134, at 148.

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reputation, but were also expendable if need be. The voluntary nature of ESG reporting, coupled with the mindset of sustainability as nice but not necessary, led to inconsistent and subpar ESG disclosure.[198] Companies could and did use sustainability reports to burnish their reputations, rather than to engage in candid disclosure.

Significantly, none of these organizations positions ESG reporting in the larger context of corporate disclosure generally. Framing in such a way that ESG reporting and mandatory financial reporting intersect would have reduced the difference in the social meaning of traditional corporate reporting and sustainability disclosure. It would also have pushed government to a decision on the legitimacy of GRI, CDP, and the IIRC as sustainability claimsmakers. Instead of attempting any degree of frame alignment, the organizations have made no attempt to directly engage the U.S. government or to impact government-mandated reporting. Their frameworks were constructed and operate outside the financial reporting system. As part of the larger field of corporate reporting, they maintain control of the framing of ESG reporting exactly because they do not engage the government on this issue.[199] The U.S. government neither recognizes nor contests the legitimacy of these groups because they do not attempt to use the government as a mechanism for change.[200] Working outside the existing reporting system may have been a strategic choice on behalf of the organizations, indicating distrust of the government as change agent.[201] But it may also signal a different meaning, specifically, these organizations may have pursued a trajectory separate from financial reporting because they view ESG reporting and financial reporting as separate parts of business. They did not try to bring the two reporting fields together because they do not see them as connected.[202]

Dissatisfaction with the lack of progress in improving ESG performance led some claimsmakers to question the separation of financial and sustainability disclosure.[203] They saw the potential to tie ESG factors to firms' financial performance, and thus to leverage the power of capital markets for sustainability.[204] The missing link was that between standards for financial disclosure and ESG factors. These claimsmakers identified the point of convergence between ESG disclosure and financial disclosure as materiality. Providing more useful ESG information to investors could foster an understanding of ESG impacts in those with the power to influence corporate behavior. But this would require framing that incorporated *TSC* materiality and sustainability. Two key initiatives illustrate the potential for leveraging the financial reporting regime to build a more complete definition of materiality.

3. The Convergence of Financial and Sustainability Information

The 2007 Petition seeking climate risk guidance from the SEC was the earliest effort to frame ESG reporting in the language of the investing world, and to bridge the divide between ESG and financial disclosure. The coalition of petitioners was an unlikely mix of financial and environmental groups.[205] However, the framing of their claims makes plain the connection between the two camps, for the petition justified its request on the basis of investor protection.[206]

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[198] *See supra* notes 92, 94–95, and accompanying text.

[199] This is not to say that the organizations have no connections to government. GRI, for example, provides guidance for government agencies wishing to use its frameworks for their sustainability reports. *See GRI Reporting in Government Agencies*, GLOB. REPORTING INITIATIVE (2010), https://www.globalreporting.org/resourcelibrary/GRI-Reporting-in-Government-Agencies.pdf. Governments that require sustainability reporting sometimes mandate use of the GRI Reporting Standards. For example, Sweden requires all state-owned enterprises to report using the GRI framework. *Corporate Social Responsibility in Sweden*, SWED., https://sweden.se/business/csr-in-sweden/ (last visited Apr. 7, 2019). Governments may also use CDP data as part of climate change policy analysis and formulation. *Governments*, CDP, https://www.cdp.net/en/policy-and-public-affairs (last visited Apr. 7, 2019).

[200] There are advocacy non-profit organizations that have used litigation against regulatory agencies to challenge the existing financial reporting regime, most notably the National Resources Defense Council (NRDC). *See* Williams, *supra* note 8, at 1247-58, for an account of a major NRDC campaign against the SEC. Litigation is not a strategy utilized by GRI, CDP, or the IIRC.

[201] Spector and Kitsuse hypothesize that, at later stages of the claimsmaking process, claimsmakers may question the legitimacy of the established institutions and lack confidence in the institutions' willingness to change. SPECTOR & KITSUSE, *supra* note 134, at 153.

[202] GRI, for example, defines the economic dimension of its reporting framework as encompassing business impacts on the economic conditions of stakeholders and on economic systems, rather than as the firm's financial performance. *GRI Reporting Standards*, *supra* note , GRI 201: Economic Performance 3. The integrated reporting framework recognizes circumstances where an integrated report may provide the context for financial statements. *IR Framework, supra* note , ¶1.14. However, the framework differentiates integrated reporting from other corporate reporting, including financial reporting. *IR Framework*, *supra* note , About <IR> 2 (claiming that integrated reporting is constituent with developments in other reporting, but differs from other reporting); *Id.*, ¶1.13 (explaining that an integrated report is not merely a summary of information from other reports such as financial statements).

[203] *See supra* notes 100 – 109 and accompanying text.

[204] Connecting sustainability factors explicitly to core business operations and value creation makes the most compelling case for business uptake of sustainability measures. Tim Koller, *When sustainability becomes a factor in valuation*, MCKINSEY & CO. (Mar. 2017), https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/when-sustainability-becomes-a-factor-in-valuation.

[205] *See supra* note 96.

[206] For example, the 2007 Petition argued that the state of current disclosure left investors "in the dark" about the financial implications of environmental issues and liabilities because disclosure under voluntary standards did not address the specific effects that climate change had on

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As part of building this link to investor protection, the 2007 Petition based its arguments on the concept of materiality, specifically citing the *TSC Industries* definition of the concept.[207] Throughout, the 2007 Petition returned to the idea that climate change risk could be material, within the meaning used for financial reporting, and therefore subject to disclosure.[208]

While using the language of financial materiality may seem inconsequential, in fact, the Petition's framing marked a new trajectory for the social meaning of sustainability issues. It was the first time that a major sustainability effort framed its work in the context and language of financial reporting. While the 2007 Petition was limited in scope to climate risk information, it represents the first steps in changing the social meaning of sustainability issues from a niche to a mainstream concern. This repositioning is evident in the fact that the investor Petitioners represented mainstream investors.[209] Reframing the issues as financial, and working within the established legal infrastructure, also provided the claimsmakers a mechanism to establish their legitimacy and set the stage for future claimsmaking activities.

Claims for the Climate Guidance focused on a single topic, the impact of climate change on business. SASB viewed sustainability more holistically, thinking across ESG impacts and across industries.[210] This broader framing challenges the existing social meaning of materiality and creates greater opportunities to advance the cause of sustainability through the materiality concept."

SASB views its standards as driven by market demand for rigorous sustainability information, a demand driven by investors.[211] SASB would take the awareness of the power of investors and capital markets and frame its claims in the context of the financial world. SASB's framing is straightforward: it sees the convergence of ESG reporting with financial reporting and strives to integrate ESG KPIs into mainstream financial reporting.[212] For SASB, investors are the main audience for SASB disclosure standards.[213] SASB's argument to investors in support of convergence is that traditional financial statements do not capture all factors that contribute to a firm's ability to create value over time.[214] ESG accounting, coupled with financial accounting, provides a more complete view of material factors.[215] SASB deepened the alignment with financial reporting by invoking the legal concept of the reasonable investor as defined by securities law and specifically utilized the *TSC* definition of materiality, articulating the connection between ESG factors and the disclosure required under SEC regulations.[216]

The social meaning of SASB's framing reflects a societal expectation that firms have not only ESG disclosure responsibilities, but that they also have sustainability performance responsibilities. Thus, firms must change their behavior and results on sustainability factors by connecting ESG factors with business performance.[217] The leverage point for this operational change is investors, who need relevant and useful information on which to re-evaluate their own decision-making on ESG factors.[218] SASB's use of the *TSC* materiality definition as the basis for its standards

corporate performance or operations. *2007 Petition*, *supra* note 96, at 45. This made it impossible for investors to utilize the disclosure in investment decisions. *Id*. at 45, 48, 50.

[207]*Id.* at 14.

[208]For example, the Petition argued that "assessment of materiality of climate related risks [was] the same process that registrants have undertaken with respect to other risks." *Id.* at 55. The Petition further contained a discussion of evaluative factors in assessing the materiality of climate risk. *Id.* at G-4 – G-6. Finally, the 2007 Petition contains an extensive explanation of how climate change information can relate as "material" to Items 101 and 303 of the 10-K report. *Id.* at 15–20.

[209]*See supra* note 102.

[210]SASB's Conceptual Framework identified five "sustainability dimensions:" the environment, social capital, human capital, business model and innovation, and leadership and governance. *SASB CF 2017*, *supra* note 101, at 2-3. The Framework argued that industry-specific standards were needed to recognize the sustainability issues common to companies in a given industry. *Id.*, at 16.

[211]*Why SASB?/Why Companies are using SASB*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/why-sasb/ (noting increasing demand from investors for information on how sustainability factors impact corporate value creation)(last visited April 27., 2019).

[212]*IRI Report*, *supra* note 104, at 14. SASB further attempts to align its framing with the existing financial reporting structure by positioning itself as the sustainability equivalent of FASB. *SASB Briefing Document*, *supra* note 106, at 12.

[213]*SASB Briefing Document*, *supra* note 106, at 13–15.

[214]*SASB CF 2017*, *supra* note 101, at 4.

[215]*Id.* at 4–5.

[216]*Id.* at 9–10. SASB uses the concept of materiality to develop its accounting standards and then recognizes that reporting entities utilize the concept in determining which standards are "material" for their operations and reporting. *Id.*

[217]*SASB CF 2017*, *supra* note 101, at 8 (explaining that focus on material sustainability factors correlates with outperformance on several criteria and can help managers identify operations that are underperforming0.

[218] SASB refers to this as investors' need for "decision-useful" information. *SASB CF 2017*, *supra* note 101, at 10.

reimagines the concept of materiality, incorporating material ESG factors with material financial factors to provide a holistic picture of business performance. This convergence of financial and ESG reporting mirrors society's expectations for business.

Close alignment with the framing of financial reporting was key in attracting adherents to SASB's work. The framing of GRI, CDP, and the IIRC did not seem to be yielding much progress[219] SASB decided to look to the one party no company can afford to ignore – its investors. To aid recruitment, SASB utilized two specific mechanisms. To begin building connections and establishing credibility with the investor community, SASB leveraged key former government officials and regulators.[220] SASB's strategy seems to have been to build tiers of adherents, enlisting specific first level supporters with ties to networks of potential second level supporters. In addition, both the development of its Conceptual Framework, which sets out the basic concepts, principles, and definitions that guide the standard-setting process,[221] and its industry-specific standards are multi-stakeholder processes. The public comment periods on the Conceptual Framework provided the opportunity for potential adherents to engage in creating SASB's governance documents.[222] The process for creating the actual accounting standards provides even more opportunities for engagement by both corporations and investors.[223] These multi-stakeholder processes serve as mechanisms to foster greater alignment of frames between SASB and its main constituents.

SASB undoubtedly reaps rewards in the form of attracting supporters from aligning its framing with that of financial reporting. However, this strategy also comes with a cost. SASB cannot directly control the meaning of the frame it uses, since much of the context's meaning is embedded in the legal infrastructure of mandatory financial reporting. SASB is using a frame created and controlled by government (including the SEC and the courts), which makes the crucial decisions on the concepts and contours of the reporting laws. The argument that the concept of materiality as defined by securities laws includes ESG issues is SASB's attempt to add further dimension to a frame controlled by the government. SASB has foregone formal control over meaning for the sake of attracting supporters. By specifically utilizing government-created structures (i.e., the 10-K report) and definition of materiality, SASB publicly contends for influence over the meaning of materiality. SASB's unique strategy is that it does not contest the government-sanctioned definition. Rather, it attempts to transform our understanding of materiality in a way that runs contrary to the SEC's focus. This is a gamble that positions the organization for conflicts with government, especially since SEC resistance to mandatory ESG disclosure remains high.[224]

SASB has important strategy decisions to make in light of its own mission, investor demands, and government inaction to improve sustainability reporting. To understand its strategy options and choices, we must first examine the challenges, especially the institutional obstacles, to changing the social meaning of materiality.

III. Challenges to Changing Social Meaning

[219]*See supra* notes 98-100 and accompanying text.

[220]For example, former FASB chair Robert Herz, former SEC Commissioner Elisse Walter, and former New York City mayor Michael Bloomberg were all early supporters of SASB as directors on the SASB Foundation Board of Directors. The SASB Foundation Board of Directors, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/governance/foundation-board/ (identifying former members of the SASB Board). Mr. Herz frequently blogs about SASB. *See, e.g.*, Robert Herz, *Meet the new standard setter for sustainability*, COMPLIANCE WK. (Apr. 30, 2013), https://www.complianceweek.com/blogs/robert-herz/meet-the-new-standard-setter-for-sustainability (last visited Apr. 27, 2019).

[221]*SASB CF 2017*, *supra* note 101, at 1.

[222]The public comment period on the 2013 exposure draft of the Conceptual Framework generated 87 pages of comments. *See SASB Conceptual Framework – Record of Public Comment*, SUSTAINABILITY ACCT. STANDARDS BD. (Jan. 6, 2014), http://www.sasb.org/wp-content/uploads/2014/01/Conceptual-Framework-Public-Comments-Table_-Rev-1-6-14.pdf. The revised Conceptual Framework, opened for public comment in 2016, resulted in 115 pages of comments. *See Comments on SASB Concept Draft*, SUSTAINABILITY ACCT. STANDARDS BD. (July 6, 2016), https://www.sasb.org/wp-content/uploads/2016/07/All-comments-received-compilation_Redacted.pdf.

[223]The SASB standard setting process follows a multi-year cycle. *Codification Process and Documents*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/standards/public-meetings-sasb/ (last visited Feb. 7, 2019). The five-step process begins with research on and consultation with the industry that is the focus of the standard. *Id.* An exposure draft of the proposed reporting standard is released for public comment, revision, and eventual ratification. *Id.* Standards are open for 90 days for public comment. *SASB Rules*, *supra* note 101, at 15. Industry participates in drafting the standards through a formal Industry Working Group (IWG) structure. *Industry Working Groups*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/about-the-sasb/industry-working-groups/ (last visited Apr. 7, 2019). SASB's IWG process has attracted such companies as Levi Strauss, Sysco, Georgia-Pacific, and Royal Philips Electronics. *Id.* SASB also has an Investor Advisory Group (IAG) that facilitates investor input into the process for creating reporting standards. *Investor Advisory Group*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/investor-use/supporters/ (last visited Apr. 17, 2019). Members of the IAG include BlackRock, UBS, Goldman Sachs, and CalPERS. *Id.*

[224]*See, e.g.*, *Chairman Clayton Says Companies Should Not be Required to Disclose Environmental and Social Matters*, THOMSON REUTERS TAX & ACCT. (Jan. 2, 2019), https://tax.thomsonreuters.com/news/chairman-clayton-says-companies-should-not-be-required-to-disclose-environmental-and-social-matters/.

As we saw in Section II, SASB defines success for itself as achieving the convergence of sustainability reporting with financial reporting.[225] Success depends, therefore, on SASB re-making the social meaning of financial reporting to include ESG factors. But changing social meaning can be problematic, especially where that meaning is embedded in legal infrastructure. This section examines key conceptual and institutional barriers for SASB's claimsmaking and considers the ramifications for SASB's CMA strategy.

A. The Inertia of Existing Social Meaning

Claimsmakers face a key obstacle in promoting change in the fact that social meanings are tenacious; acceptance of a social meaning itself inhibits change of that very social meaning.[226] To create a new social meaning requires both dismantling the old meaning and implementing a new meaning, increasing the collective action problem.[227] This makes it is easier to defend an existing social meaning than to succeed in changing social meaning.[228]

The power to create and change social meaning derives from concerted action.[229] Transformation of social meaning is a social good that comes with attendant collective action problems.[230] Transforming social meaning requires that claimsmakers achieve collective acceptance of the proposed new meaning from enough of society to make that new meaning the dominant construction.[231] However, social meaning is not changed by fiat. Rather, claimsmakers must work to change the incentives around adherence to the existing meaning to foster change.[232] Sunstein describes this as creating a "norm bandwagon" – the condition where the costs of non-compliance with the new meaning are high enough to induce acceptance of the meaning.[233] CMA can be seen as initiatives to change the cost of adherence to new meanings by creating dissatisfaction with the existing social meaning of an action.

B. Institutional Barriers to Changing Social Meaning: The Power of Law

Significantly, law and government often play a crucial role in maintaining existing social meaning. Scholars have recognized the power of law as an expression of values and norms, which drive expectations in a specific direction.[234] Thus, law, as a statement of values, affects social meaning.[235] The reality is that government and law are often acting in support of an existing social meaning and orthodoxy.[236] The inherent power of law to maintain the status quo can create institutional barriers to changing social meaning. Where the law puts its resources behind a specific social meaning, there will be disincentives to challenging that meaning. But the law can go beyond merely defending meaning on a rhetorical level and can create actual barriers to change in the form of specific legal infrastructure and institutions.

Agencies have broad latitude in interpreting the statutes they administer and in crafting regulations, , each of which presents challenges for advancing new conceptions of materiality.[237] In the field of corporate reporting, this gives the SEC the ability to control much of the meaning of materiality, as well as focusing enforcement resources away from ESG reporting. This deference can act as a barrier to change.

[225] *See supra* notes 191–95 and accompanying text.
[226] Lessig, *supra* note 136, at 997–98; Termeer, *supra* note 121, at 301-02.
[227] Lessig, *supra* note 136, at 999. Lessig calls this "defensive construction." *Id.* The tenacity of existing meaning is bolstered by the fact that expectations around the existing meaning often impose costs on non-compliance with the current meaning. *Id.* at 998.
[228] *Id.* at 999–1000.
[229] Sunstein, *supra* note 168, at 927-928.
[230] Lessig, *supra* note 136, at 993; Sunstein, *supra* note 168, at 911. The term "collective action problem" describes a situation in which multiple individuals would all benefit from a certain action, but has an associated cost making it implausible that any individual can or will undertake and solve it alone. For explication of the concept, see MANCUR OLSON, **THE LOGIC OF COLLECTIVE ACTION**, HARVARD ECONOMIC STUDIES 9-10 (1971).]
[231] Lessig, *supra* note 136, at 993, 1000; Sunstein, *supra* note 168, at 925–26.
[232] Lessig, *supra* note 136, at 997-98, 1000.
[233] Sunstein, *supra* note 168, at 912.
[234] *Id.* at 953.
[235] *Id*. at 964.
[236] Lessig, *supra* note 136, at 948, 957.
[237] *See, e.g*., Patricia M. Wald, *The Fiftieth Anniversary of the Administrative Procedures Act: Past and Prologue: Judicial Review in Midpassage: The Uneasy Partnership Between Courts and Agencies Plays On*, 32 TULSA L. J. 221, 226-228 (1996) (noting the recent history of judicial deference to agency reasoning, to agency interpretation of statutes, and agency decisions not to act); Susan K. Goplen, Note, *Judicial Deference to Administrative Agencies' Legal Interpretations After Lechmere, Inc. v. NLRB*, 68 WASH. L. REV. 207, 209-212 (1993)(discussing the judicial deference accorded to agency determinations of questions of fact and questions of law).

Supreme Court jurisprudence is clear in limiting the power of the judiciary to review administrative agency actions interpreting statutes that the agency administers. Where the statute is silent or ambiguous on a particular issue, the court can review only whether the agency's interpretation of the statute is a "permissible construction" of the statute.[238] A court may not substitute its own interpretation of the statute, or its own policy preferences, for that of the agency.[239] The *Chevron* Court viewed reconciliation of policy conflicts as part of the political process, for which the judiciary was not suited.[240] Thus, courts may not second guess agency action, where the agency's interpretation of relevant statutes was a "reasonable choice within [the] gap left open by Congress."[241]

Similarly, agencies have broad discretion in creating regulations to implement statutory mandates. Generally, courts are authorized to set aside agency actions found to be arbitrary, capricious, or an abuse of discretion.[242] However, the scope of review of an action claimed to be arbitrary and capricious is narrow; courts are not permitted to substitute their judgment for that of the agency.[243] In *State Farm,* the Supreme Court limited judicial review of agency regulations to examining whether the agency considered relevant factors in its decision and whether there is a rational connection between the facts found in agency proceedings and the regulations.[244] Judicial review under the arbitrary and capricious standard, then, is largely to determine whether a regulation is procedurally defective as a result of flaws in the agency's decision-making process.[245] Where the agency has examined the relevant data and offers a "rational" connection between the data and the regulations, the court must defer to the agency's decision.[246]

Under the *Chevron* and *State Farm* standards, the SEC has significant discretion to shape the contours of materiality. The *TSC* definition of materiality is sufficiently broad to leave much of the elaboration of its meaning in the agency's hands. *TSC* materiality is based on two key concepts - the reasonable investor and the total mix of information – neither of which was defined by the Court.[247] It is left to the SEC to define what constitutes a reasonable investor and what is included in the total mix of information that investor desires. The SEC has considered reasonable investors to be concerned with only the financial returns on their investments and to need only financial information to make investment decisions.[248] Given the historical framing of financial reporting as focused solely on financial factors, this definition is among the permissible constructions of materiality. Additionally, as the SEC evaluates the ramifications of different interpretations, it could resolve policy tensions in favor of a policy to reduce burdens on business. As long as there is evidence in the administrative record supporting this policy decision, the *Chevron* and *State Farm* standards would protect the SEC's determination from judicial overturning.

The judicial hands-off attitude represented by the standard of judicial review of agency actions means that agencies retain power to control regulations but also to heavily influence the social meaning of regulatory arenas. The SEC's narrow focus on solely economic factors as impacting financial returns has led it to limit its conception of the total

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[238]Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 843 (1984) [hereinafter *Chevron*]. *Chevron* involved a challenge to U.S. Environmental Protection Agency (EPA) regulations implementing the federal Clean Air Act Amendments of 1977. The Chevron decision identified a two-step process for judicial review of the agency's interpretation. *Id.* at 842. The court first ascertains whether Congress has directly spoken to the specific issue. If not, the second question for the court is whether the agency's interpretation is based on a "permissible construction" of the relevant statute. *Id.* at 843.

[239]*Id.* at 844. The *Chevron* Court found deference to the agency appropriate due to the policy ramifications of an administrative agency's statutory interpretation and the need for agency expertise in assessing policy issues. Catherine M. Sharkey, *Cutting in on the Chevron Two-Step*, 86 FORD. L. REV. 2359, 2364 (2018). The Court viewed ambiguities in legislation as an "express delegation of authority" to the administrative agency to administer programs, including reconciling conflicting policies. *Chevron*, 467 U.S. at 843–44. The *Chevron* decision identified three factors arguing for deference. Deference to agency action is appropriate where "the regulatory scheme is technical and complex, the agency considered the matter in a detailed and reasoned fashion, and the decision involves reconciling conflicting policies." *Id.* at 865.

[240]*Id.* at 865–66. Competing policy issues in Chevron were the need to foster economic growth and the need to protect the environment (specifically, the air) from pollution. *Id.* at 866.

[241]*Id. at* 866.

[242]Administrative Procedure Act, 5 U.S.C. §706(2)(A) (2011).

[243]Motor Vehicle Manufacturers Association v. State Farm Auto Mutual Insurance Co., 463 U.S. 29, 43 (1983) [hereinafter *State Farm*].

[244]*Id.* at 43. The Court elaborated that an agency rule would be considered arbitrary and capricious if the agency relied on factors Congress did not intend to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that ran counter to the evidence, or was "implausible." *Id.* at 43.

[245]Sharkey, *supra* note 215, at 2376–77; JARED P. COLE, CONG. RESEARCH SERV., R44699, AN INTRODUCTION TO JUDICIAL REVIEW OF FEDERAL AGENCY ACTION 19 (2016) (referring to the arbitrary and capricious standard as determining whether the agency engaged in "reasoned decisionmaking").

[246]*State Farm*, 463 U.S. at 43, 52.

[247]*See supra* notes 50–51, and accompanying text.

[248]Douglas Y. Park, *Investor Interest in Nonfinancial Information: What Lawyers Need to Know*, BUS. L. TODAY, Jan. 2015, at 1, 1–4, available at https://businesslawtoday.org/2015/01/investor-interest-in-nonfinancial-information-what-lawyers-need-to-know/; Williams, *supra* note 8, at 1252, 1262.

mix of information important to investors. This power to control agency framing has contributed to maintaining the psychological and normative distinction between financial information and sustainability information.[249] Since agency regulations need only have some degree of factual support, the SEC can largely ignore claims for policy revisions and advances, further entrenching the existing social meaning. Limited judicial review of agency action also allows the perpetuation of patterns of action or inaction. For example, the court in *Natural Resources Defense Council, Inc. v. SEC*, a 1979 case, noted favorably that the SEC had instituted additional proceedings related to expanding corporate disclosure.[250] Since then, however, there has been essentially no change in the SEC's position on corporate sustainability reporting. The question becomes whether this lack of change accurately reflects society's expectations or whether it reflect the inertia of the existing orthodoxy.

The deferential standard of judicial review of agency action is only one part of the legal infrastructure that can be used to entrench the status quo. Agency control of enforcement resources can also serve to hamper change, as is evident with implementation of the 2010 Climate Guidance. The teeth of any regulatory scheme is in adequate and effective enforcement, without which compliance will be viewed as discretionary. In the context of required disclosure, this may mean that reporting entities view non-disclosure as low risk and, therefore, decide not to disclose.

The years following promulgation of the 2010 Climate Guidance reflect the dynamic between disclosure and enforcement. The SEC's follow-up to the Guidance was generally muted,[251] and promised support for reporting entities, in the form of SEC-sponsored disclosure roundtables, never materialized. A study of post-Guidance climate disclosure revealed the rather dismal disclosure and enforcement landscape.[252] The study found that, while there had been an increase in the quantity of climate-related disclosure immediately following issuance of the Guidance, this figure reflected that more companies were mentioning climate in their annual reports, generally, climate disclosures had decreased in quality, consisting mostly of broad, vague statements and boilerplate language.[253] Where disclosure is sub-par, one might expect to see the agency institute aggressive enforcement. However, this has not been the case. Of the more than 45,000 enforcement letters issued in the study's time period, only 52 of those letters contained questions on Guidance-related disclosure.[254] Enforcement since the Ceres study seems to have remained lax. A New York Times article in 2016 reported the efforts of a loose coalition of investors, including representatives of large pension funds, and 35 members of Congress to catalyze the SEC's enforcement actions.[255] The SEC, the article reported, had no plans to require companies to improve their disclosure on climate change risk.[256]

The SEC's pattern of lax enforcement of the 2010 Climate Guidance sends a clear message to reporting companies: the agency does not find the issue of climate change important enough to allocate enforcement resources toward the Guidance. Lax enforcement may also indicate that the agency retains its blindspot on the connection between

[249]Holstein and Miller have noted the power of frames to reflect and perpetuate specific cultural understandings. Holstein & Miller, *supra* note 118, at 153.

[250]Nat. Res. Def. Council, Inc. v. SEC, 606 F.2d 1031, 1055(D.C. Cir. 1979). The case was the culmination of a series of actions brought by the Natural Resources Defense Council beginning in 1974, challenging the SEC's rulemaking around environmental disclosure. *See* Williams, *supra* note 8, at 1246–58 for a summary of the litigation.

[251]Stuart Hammer & Lauren M. Boccardi, *Climate Change Disclosure*, NAT'L ASS'N CORP. DIRECTORS (July 26, 2011), http://www.directorship.com/climate-change-disclosure-in-sec-filings/print/.

[252]Jim Coburn & Jackie Cook, *Cool Response: The SEC & Corporate Climate Change Reporting*, CERES (Jan. 30, 2014), https://www.ceres.org/resources/reports/cool-response-sec-corporate-climate-change-reporting. The study investigated two issues. First, it examined rates of corporate climate-related disclosure by surveying 10-K reports of S&P 500 companies from 2009 through 2013. *Id.* at 11. Reviewers looked both at whether there was any climate-related disclosure and also assessed the quality of any such disclosure. *Id.* Second, the study examined SEC enforcement of the Guidance by searching for and reviewing SEC enforcement letters for the years 2010 through 2013. *Id.* at 20. The study authors reviewed all letters that mentioned climate change issues related to the Guidance, based on identified climate-related keyword searches. *Id.*

[253]*Id*. at 13.

[254]*Id*. at 20. The pattern of issuance also reflected the SEC's "cooling off' toward enforcement: by 2012, two years after the Guidance went into effect, the SEC issued only three enforcement letters raising climate disclosure issues; in 2013, no enforcement letters contained climate-related disclosure questions. *Id.* at 21.

[255]David Gelles, *S.E.C. Is Criticized for Lax Enforcement of Climate Risk Disclosure*, NY TIMES (Jan. 23, 2016), https://www.nytimes.com/2016/01/24/business/energy-environment/sec-is-criticized-for-lax-enforcement-of-climate-risk-disclosure.html.

[256] *Id.* The Government Accountability Office (GAO) subsequently conducted a study on enforcement of the 2010 Climate Guidance. U.S. GOV'T ACCOUNTABILITY OFFICE, CLIMATE–RELATED RISKS: SEC HAS TAKEN STEPS TO CLARIFY DISCLOSURE REQUIREMENTS GAO-18-188 (Feb. 2018). The report reviewed the results of the Ceres study and collected new data, which demonstrated the same pattern of lax enforcement. *Id.* at 30. The GAO study found that the SEC issued 41,000 comment letters between January 1, 2014 and August 11, 2017; 14 of those letters related to climate risk disclosure. *Id.* at 14.

environmental factors and financial performance, that it does not accept that climate change factors can meet the definition of materiality for purposes of disclosure. By taking a hands-off enforcement approach, the SEC supports the pre-Guidance status quo, where environmental and financial information were distinct and separate.

IV. Implications for SASB's Strategy

SASB's decision to frame its claims for corporate reporting in line with the legal structure for mandatory reporting forces the issue of the social meaning of reporting as no other claimsmaker in the reporting movement has. As we have seen, however, the SEC has made no significant change in mandatory reporting since it issued the Climate Guidance in 2010. Spector and Kitsuse's natural history model hypothesizes a late stage where claimsmakers grow dissatisfied with government action on their claims.[257] For SASB, this stage involves evaluating whether the current definition of materiality meets its investor protection goals. The escalation of SASB activities is evidence of SASB's continuing dissatisfaction with the lack of convergence between financial and sustainability reporting.[258]

Discontent with government action raises the question implicit in the natural history model: what are claimsmaking strategy options, in light of government inadequacy? Spector and Kitsuse's model investigates this space where the claimsmaker decides to reject formal processes, finding it no longer possible to work within the system.[259] Some aspects of SASB's situation fit within the boundaries of this stage, but SASB has also acted in ways that question some of the model's assertions. To some extent, SASB can be seen as rejecting aspects of the formal processes available to it. SASB seems to have learned lessons from the previous failed attempts to use legal processes to force the SEC to expand corporate disclosure, failures that are connected directly to the realities of the formal agency processes. The SEC's control over the legal structure of mandatory reporting and the power it wields as an administrative agency give it formal control over the social meaning of materiality. While the same processes are still available to SASB, they are not necessarily the best strategy to attempt meaning change and SASB seems to know this. Rather than a complete rejection of engagement with formal processes, as Spector & Kitsuse hypothesize, SASB pursues a hybrid strategy, one where it burns no bridges with those currently officially controlling reporting, but also does not surrender to the system.

At Spector and Kitsuse's final stage, claimsmakers have given up on government action as a solution to their claims and begin to raise claims that challenge the legitimacy of the established institutions.[260] Rather than completely reject all connections with the regulator, SASB continues to participate in available government-sanctioned activities related to corporate reporting. In 2016, the SEC issued a concept release as part of its normal rule-making procedures.[261] Among other topics, the concept release included questions on updating disclosure requirements relating to "sustainability matters."[262] SASB submitted extensive written comments to the concept release,[263] as well as participating in meetings on the concept release conducted by the SEC Investor Advisory Committee.[264] These activities demonstrate that SASB remains ready to fully engage in with formal regulatory processes. SASB also

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[257] SPECTOR & KITSUSE, *supra* note 134, at 151.
[258] For example, in 2017 SASB constituted its inaugural SASB Standards Board, with overall responsibility for SASB standard-setting process. *Announcing New Members of the SASB Standards Board*, PR NEWSWIRE (May 11, 2017), https://www.prnewswire.com/news-releases/announcing-new-members-of-the-sasb-standards-board-300455499.html. SASB has issued disclosure standards for 77 industries. *See supra* note 118 and accompanying text.
[259] SPECTOR & KITSUSE, *supra* note 134, at 153.
[260] *Id.*
[261] Business and Financial Disclosure Required by Regulation S-K, 81 Fed. Reg. 23916 (April 22, 2016) [hereinafter SEC Concept Release]. The concept release was intended to seek public comment on modernizing specified business and financial disclosure requirements in Regulation S-K. Press Release, SEC Solicits Public Comment on Business and Financial Disclosure Requirements in Regulation S-K, SEC. EXCH. COMM'N (April 15, 2016), https://www.sec.gov/news/pressrelease/2016-70.html.
[262] SEC Concept Release, *supra* note 258, at 23969-23973. The Request for Comment on sustainability items included questions related to identification of specific issues of important to investors, the advisability of creating line item disclosure requirements, and use of existing sustainability reporting frameworks. *Id*. at 213–15.
[263] *Response to Concept Release on Business and Financial Disclosure Required by Regulation S-K*, SUSTAINABILITY ACCT. STANDARDS BD. (July 1, 2016)., available at https://www.sec.gov/comments/s7-06-16/s70616-25.pdf.
[264] *Minutes of the Meeting on July 14, 2016*, SEC. EXCH. COMM'N, https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac071416-minutes.htm (last visited Apr. 27, 2019)(identifying SASB CEO Jean Rogers as a panelist for the discussion of sustainability reporting). For the text of Rogers' remarks, see *Remarks to the SEC Investor Advisory Committee*, SUSTAINABILITY ACCT. STANDARDS BD. (July 14, 2016), available at https://www.sec.gov/comments/265-28/26528-265.pdf. The Investor Advisory Committee was created in 2011 by the Dodd-Frank Act to advise the SEC on various regulatory matters. *Investor Advisory Committee*, SEC. EXCH. COMM'N, https://www.sec.gov/spotlight/investor-advisory-committee.shtml (last visited Apr. 7, 2019).

maintains less formal ties to relevant regulatory bodies: the organization's Board of Directors includes two former SEC chairs and a former chair of FASB.[265] This strategy of engagement in formal processes makes sense, given SASB's overarching desire for convergence of financial and sustainability reporting.[266]

At the same time that SASB avails itself of opportunities in formal government processes, it clearly is not counting on immediate SEC action to expand corporate reporting, nor is it waiting for the SEC to reevaluate the concept of materiality. Spector and Kitsuse argue that, when claimsmakers reject government action, they focus on the creation of alternatives.[267] At this stage, the model posits an either/or choice between two possible strategies. One possibility is for a claimsmaker to withdraw from the existing institutional system and create an alternative that provides a limited resolution of some of their claims.[268] To a certain extent, SASB's reporting standards reflect this approach. Companies can use the standards to report sustainability impacts without the SEC's formal approval and, in fact, outside of the financial reporting system. SASB's standards, thus, can be seen as answering a limited portion of SASB's claims.

SASB has seen the potential of pursuing both this and the second alternative posed by the model: create an alternative institution to develop a social and political base for challenging the existing procedures.[269] SASB seeks to change the social meaning of materiality by building an alternative that meshes with the expectations and view of reality of potential supporters better than does the existing system. In this process, SASB utilizes a unique feature of information disclosure systems. Unlike substantive regulation, where only the agency can alter the regulations, an information disclosure system has a leverage point other than the regulator – i.e., the end user of the information. SASB appeals directly to the intended beneficiary of the U.S. financial reporting system, investors, as potential adherents to SASB's framing of materiality and uses a market mechanism to change the social meaning of the concept.

SASB's drive toward the convergence of financial and ESG disclosure answers much of the dissatisfaction expressed by investors with the existing reporting regime.[270] Further, the convergence of financial and sustainability factors reflects evolving societal norms that are driving changes in investing. The growth of fossil fuel divestment campaigns,[271] increases in shareholder resolutions on environmental and social issues,[272] and spreading environmental activism[273] are all indications of society's interest in key ESG issues. Societal norms and investor desire to incorporate

[265] SASB directors Mary Shapiro and Elisse Walter are former SEC chairs; director Robert Herz chaired FASB. *The SASB Foundation Board of Directors*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/sasb-foundation/board-directors/ (last visited Apr. 7, 2019).

[266] SASB's efforts to engage with the SEC extend even to those commissioners most hostile to SASB. SASB's CEO Jean Rogers used the occasion of Commissioner Gallagher's negative remarks regarding SASB as an opportunity to reach out to the Commissioner. In a letter to Gallagher, Rogers articulated the frame alignment between the two organizations and offered to brief Commissioner Gallagher on how SASB could "support the SEC's mission." Letter from Jean Rogers, CEO, Sustainability Accounting Standards Bd., to Daniel M. Gallagher, Comm'r, Sec. Exch. Comm'n (April 4, 2014) (available at http://www.sasb.org/wp-content/uploads/2014/04/SASB-Letter-to-Commissioner-Gallagher.pdf).

[267] SPECTOR & KITSUSE, *supra* note 134, at 153.

[268] *Id.* at 153–54.

[269] *Id*. at 153.

[270] See *supra* notes 92–95 and accompanying text for discussion of investor dissatisfaction. Investors continue to express their dissatisfaction directly to the SEC. In October 2018, a coalition of investors filed a formal petition for rulemaking with the SEC, requesting that the Commission take action toward mandatory ESG disclosure. Petition for Rulemaking from Prof. Cynthia A. Williams et al., to Brent J. Fields, Secretary of the Securities and Exchange Commission (Oct. 1, 2018) (available at https://www.sec.gov/rules/petitions/2018/petn4-730.pdf). Other investors have shown support specifically for SASB's reporting standards. SASB investor members include BlackRock, CalPERS, Morgan Stanley Investment Management, State Street Global Advisors, and Wells Fargo Asset Management. *Support from Investors*, SUSTAINABILITY ACCT. STANDARDS BD., https://www.sasb.org/investor-use/supporters/ (last visited Apr. 14, 2019). In addition, proxy advisor Glass Lewis has announced that it will include SASB's guidance on materiality as part of its research and vote management. Cooley LLP, *SASB issues sustainability accounting standards for 77 industries*, https://www.jdsupra.com/legalnews/blog-sasb-issues-sustainability-35429/.

[271] For discussion of divestment campaigns, *see, e.g.*, Elizabeth Lewis et al., World Resources Institute, Navigating the Sustainable Investment Landscape 2, 15–16 (Dec. 2016); *see* also Damian Carrington, *Fossil Fuel Divestment Funds Rise to $6tn*, THE GUARDIAN (Sep. 10, 2018), https://www.theguardian.com/environment/2018/sep/10/fossil-fuel-divestment-funds-rise-to-6tn.

[272] Meaghan Kilroy, *Environmental, Social Issues Big in Proxy Season*, PENSIONS & INVESTMENTS (July 9, 2018), https://www.pionline.com/article/20180709/PRINT/180709889/environmental-social-issues-big-in-proxy-season (noting that environmental and social concerns dominated shareholder proposal submissions in 2018); *Shareholders Press Boards on Social and Environmental Risks*, EY, https://www.ey.com/us/en/services/specialty-services/climate-change-and-sustainability-services/shareholders-press-boards-on-social-and-environmental-risks---take-action (last visited Apr. 14, 2019)(advising companies that risks related to sustainability, including climate change risk and other environmental issues, are important to shareholders)

[273] For example, the Keystone XL oil pipeline generated multiple protests. *See, e.g.,* Belle Fourche, *County Preps for Keystone XL Pipeline Protests*, BROOKINGS REGISTER (Jan. 7, 2019), https://brookingsregister.com/article/county-preps-for-keystone-xl-pipeline-protests; Nick Cunningham, *Canada's Most Crucial Pipeline Comes Under Fire*, OILPRICE.COM (Feb. 3, 2019), https://oilprice.com/Energy/Crude-Oil/Canadas-Most-Crucial-Pipelinen-Comes-Under-Fire.html.

ESG factors into financial analysis and decisions change the incentives for firms' conception of materiality. Adherence to the legal definition of materiality may impact a firm's access to capital, as investors pressure firms to disclose material ESG information, regardless of whether the SEC requires such disclosure or not.[274]

SASB standards operate as soft law, but without the key drawback to soft law mechanisms: lack of accountability.[275] Investor involvement and demand for use of SASB's reporting standards should mitigate accountability issues, as investors have the financial power to expect improved ESG disclosure. Creation of an alternative reporting construct, even as soft law, changes the context of reporting by *showing how* sustainability impacts are material. Leveraging the existing legal architecture of reporting reduces some of the cost of changing meaning: since it is an architecture with which reporting companies and investors are familiar, there is less uncertainty than in a completely new reporting framework. While SASB does not appear to want to supplant the SEC itself, its effort to add dimension to the definition of materiality is intended to become the accepted institutional frame for dialogue around corporate reporting, thereby changing the social meaning of reporting.[276] SASB's reporting standards are not so much an alternative as a companion process with the potential to alter actual reporting practice by bringing the concept of materiality in line with new expectations.[277]

Aside from government resistance to the evolving social meaning of sustainability, SASB's main challenge is the potential limitation of framing sustainability in line with the *TSC* materiality definition. Financial reporting may be an effective engine to drive some aspects of the sustainability movement forward, but it may stall where investor and societal expectations and interests diverge. Investors, for example, may elect not to push for changes in corporate behavior, leaving externalities in place.[278] SASB seems to recognize this potential limitation and refrains from claiming that it is the sole avenue to advance sustainability.[279] What is clear from the slow progress of the sustainability movement to date is that no significant progress will be made without aligning investor interests and sustainability. Insofar as SASB frames materiality in the context of mainstream investor concerns, it should serve as a critical step in advancing sustainability.

Conclusion

Although materiality would appear to be a simple concept as originally conceived, the story of its development shows it to be anything but simple. As societal expectations of business increased to environmental and social impacts, the definition of materiality became contested. The division between financial and ESG factors ill-served key stakeholders, especially investors and society in general, because it largely failed to foster change in corporate behavior toward greater sustainability.

Pursuing the convergence of financial and sustainability factors and disclosure is a step forward to bringing sustainability into the mainstream. But this convergence requires leveraging the definition of financial materiality. Despite calls for the SEC to use its authority to act on ESG disclosure,[280] action in the foreseeable future seems unlikely. Absent government action, SASB has taken on the task of bringing financial materiality into the twenty-first century by recognizing the impact environmental, social, and governance factors have on financial performance. SASB's work to alter the social meaning of materiality – to build a model that merges ESG and financial factors – has the potential to harness the power of investors to advance sustainability into mainstream corporate practice.

[274]*See supra* notes 21 – 40 and accompanying text.
[275]*See* Stephen Kim Park & Gerlinde Berger-Walliser, *A Firm-Driven Approach to Global Governance and Sustainability*, 52 AM. BUS. L. J. 255, 300 (2015) (pointing to GRI reporting mechanism as lacking accountability).[
[276]*Id.* at 280 (explaining that soft law can serve as the "institutional language" for discourse among parties to consolidate shared values).
[277]Park & Berger-Walliser also argue that soft law framing can become the dominant framing as soft law norms are converted into legal rules. *Id.* at 279–80.
[278]For a discussion of the inherent limits of attempting to regulate through information disclosure, see Stephen Kim Park, *Targeted Social Transparency as Global Corporate Strategy*, 35 NW J. INT'L L. & BUS. 87, 100–03 (2014).
[279]For example, SASB has attempted to diffuse the debate that tries to pit it against GRI and the IIRC through public statements made in conjunction with GRI. *See* Tim Mohin & Jean Rogers, *How to Approach Corporate Sustainability Reporting in 2017*, SUSTAINABILITY ACCT. STANDARDS BD. (Mar. 20, 2017), https://www.sasb.org/blog-sasb-gri-pen-joint-op-ed-sustainability-reporting-sychronicity/ (arguing that the GRI and SASB frameworks are intended for different audiences, and, therefore, can both be used for most robust sustainability reporting).
[280]*See, e.g.*, Harper Ho, *supra* note 91, at 474.