Ceres

# 2024 Ceres Guidance for Investor Engagements with Directors on Climate Risk Governance

Climate change poses material risks to individual companies and systemic risks to investors' portfolios[1]. The extent of these risks, and that there is no avenue for investors to diversify away from them, means that reliable and comparable public disclosure is needed by investors to properly evaluate and understand the value of a company's business. Information about the systems and processes that companies have in place at the board and senior management levels to oversee climate-related risks and opportunities, otherwise referred to as climate risk governance, is a core component of the public disclosure needed by investors. Such governance determines how a company's board oversees management's approach to climate-related risks and opportunities and the company's plans for transitioning to operate in a net zero emissions economy.

Regulators in the U.S. and abroad have started to address these risks, with mandatory disclosures on the horizon.[2] Nearly all regulatory frameworks include baseline voluntary disclosure standards such as the Task Force on Climate-related Financial Disclosure (TCFD)[3] and the International Sustainability Standard Board's (ISSB) IFRS S1 and IFRS S2 standards for sustainability and climate-related disclosures. As reporting obligations are finalized in numerous countries, many investors continue to rely on widely accepted voluntary disclosure frameworks and company benchmarking tools, such as the Climate Action 100+ Net Zero Company Benchmark[4], to evaluate corporate climate risk governance as part of their investment decision-making and stewardship activities.

**The Ceres guidance, which builds upon these disclosure frameworks and expected regulations, serves as a resource for investors in their company engagements with independent directors. Companies may also want to use this guidance to prepare for stakeholder engagements and to help inform their public disclosures and practices to align with the direction in which all U.S. public companies should be moving on their respective journeys to address the net zero transition.**

- This updated guidance includes steps that investors have typically considered when engagements with directors of their portfolio companies do not progress in a meaningful way.
- The Appendix includes a list of sample questions that investors may want to consider when engaging with directors on climate-related issues. These questions are based on the roles and responsibilities of the board of directors, which are distinct from those of management.

## A. Effective Board Oversight of Climate-Related Risks and Opportunities, Greenhouse Gas Emissions Reduction Targets, and Climate Transition Action Plans

Companies should disclose independent board oversight of their climate-related risks and opportunities, including how the company has integrated these risks and opportunities into its strategy and operations. Disclosures should include how the board or a designated committee oversees the development, implementation, and disclosure of a comprehensive, forward-looking climate transition action plan that relies on science-based greenhouse gas (GHG) emission reduction targets for its scope 1, 2 and 3 emissions, as well as how the board monitors the company's annual progress towards meeting its short-, medium- and long-term targets. In disclosing how it monitors the company's progress, a description of whether and how climate-related considerations or performance metrics are factored into the development of executive remuneration plans should be provided.

Investors generally expect that a company's climate transition action plan will detail how it plans to meet science-based GHG emissions reductions that are aligned with the goals of the Paris Agreement to limit the worst impacts of climate change.

The board's oversight of climate-related risks and opportunities should be clearly reflected in a publicly available governance document on the company's website, such as a board committee charter or—if only at the full board level—corporate governance guidelines. Investors generally expect that, if climate oversight falls under a specific board committee and there are no regulatory requirements mandating that the committee is comprised entirely of independent directors[5], then the board should still form that committee with only independent members. This is due to the substantial duties involved in supervising climate change-related implications, which span material financial risks and strategic opportunities. Having a fully independent committee provides objectivity and credibility in governing such a critical issue for long-term value preservation and creation.

For additional climate transition action plan resources, see Ceres' Blueprint for Implementing a Leading Climate Transition Action Plan.

## B. Effective Management Responsibility for Assessing and Managing Climate-Related Risks and Opportunities, Emissions Reduction Targets, and Climate Transition Action Plans

Companies should disclose the existence of an effective cross-functional senior management committee that is responsible for company-wide management of climate-related risks and opportunities, GHG reduction targets, and climate transition action plans. The management committee should generally report to the CEO and disclose its policies and key actions to the full board or the board committee responsible for oversight of climate change-related issues.

The cross-functional senior management committee could include members from the following corporate departments/teams: audit, human resources (including those responsible for executive compensation), investor relations, finance/treasury, marketing, government affairs, legal, operations, product development, strategy, real estate, research & development, risk management, information technology, and supply chain management/procurement.

## C. Sufficient Board-level Capabilities and Competencies to Oversee Climate-Related Risks and Opportunities

Companies should disclose sufficient information to reveal the climate competency of their boards. Such disclosure could be in a company's proxy statements or corporate social responsibility (CSR) reports, using disclosures such as board matrices and director biographies that credibly support the experiences and skills listed in the board matrices.

No one director will make a climate competent board. Rather, a board should assess and be able to explain how the different directors' experiences contribute to the board's oversight of the company's strategy to manage its climate-related risks and opportunities (including, but not limited to, its GHG emissions reduction targets and its climate transition action plan). Boards should consider and disclose how their continuing education helps directors maintain and update the competencies and skills that are necessary to effectively oversee and guide the company's response to its evolving climate-related risks and opportunities.

For additional resources, see Ceres' report Lead From the Top: Building Sustainability Competence on Corporate Boards.

## D. Sufficient Audit Committee Oversight of Climate Risks and Disclosures

Audit committees should be aware of the climate-related reporting requirements the company may be subject to globally, including any related assurance requirements, and should oversee management's preparation for such disclosure requirements.

Audit committees should direct the company's internal audit department and its independent auditors to include in their respective annual work scopes: (1) sufficient testing of the impacts of climate change risk on the company's operations and (2) review of the related disclosures in the company's audited and interim financial statements, including, for example, whether any asset valuation write-downs are appropriate, with clear disclosure of assumptions used in their testing, including the use of base-case and downside climate-related scenarios.

The audit committee should review and discuss with management, the company's internal audit department, and independent auditors the critical audit matters addressed during the audit of the company's financial statements.

Consideration may be given to shifts in demand, technology, and regulations associated with climate change that could impact company accounts, including future cash flows, asset values, asset impairments, and asset retirement obligations.

The final TCFD implementation guidance (page 8) affirms that a company's audit committee should be among those reviewing TCFD disclosures prior to publicly issuing them, regardless of whether the disclosures are in a financial or nonfinancial report. In light of upcoming mandatory climate risk and sustainability disclosure rules, boards should update their committee charters and meeting agendas to reflect the new financial reporting oversight responsibilities that they will have.

For additional resources, see the International Federation of Accountants' report: Key Questions for Audit Committees Overseeing Sustainability-Related Disclosure.

## E. Sufficient Board and Senior Management Response to Majority-Supported Investor Votes

Investors generally expect boards to take meaningful action in response to majority-supported investor votes (including majority votes against a director's election or re-election), and to do so within a reasonable time after a vote takes place. For shareholder proposals or vote-no director campaigns that receive considerable minority support, often defined as greater than 20% or 30%, investors typically expect the company to disclose its shareholder outreach efforts to understand and address the concerns raised by those supporting votes[6].

Investor expectations extend to climate-related matters and would apply in cases where:

1. A director failed to receive more than 50% of the votes cast, which was the result, at least in part, of climate-related concerns.
2. A climate-related shareholder proposal received a majority of investor votes cast in any of the company's shareholder meetings over the past three years. The focus of a company's response should be on the RESOLVED clause of the proposal, since that is what shareholders voted on. If shareholders determine that the rigorousness of implementation is questionable, they may refer to the rest of the shareholder proposal to help determine what investors voted FOR.
    - For a shareholder proposal that passed at the most recent shareholders meeting, investors generally expect that the company disclose a plan for timely implementation.
    - For a shareholder proposal that receives a majority of non-insider votes, investors generally expect that the company engage with the proponent of the shareholder proposal and/or its shareholder base and disclose its shareholder outreach efforts in publicly available reports (such as the company's sustainability report or its proxy statement).
    - For a shareholder proposal that receives between 20% and 50% support, investors generally expect that the company disclose its outreach efforts to its shareholder base after the vote and/or the rationale for the degree of company implementation, while taking into consideration the level of support that similar shareholder proposals at the company have received in the past.

### F. Sufficient Board and Senior Management Response to Climate-Related Controversies or Failures

Investors generally expect companies to adequately address and disclose the reasons for—along with mitigating actions taken in response to—any material climate-related controversy or failure (including a significant asset write-down related to the controversy or failure) that in the past year has resulted in significant or serial fines or sanctions from regulatory bodies or significant adverse legal judgments or settlements.

### G. Sufficient Availability of Independent Directors to Engage with Shareholders on Climate-Related Issues

Company boards should make one or more independent directors available to engage constructively with significant shareholders on financially material climate-related risks and opportunities. The significance of a shareholder or a shareholder group should be determined not only with respect to assets under management, but also by other factors, such as a shareholder's recognized leadership on governance and climate-related topics.

### H. Effective Governance of Paris Agreement-Aligned Climate Lobbying

Company boards should have explicit oversight, either directly or through board committees, for reviewing company policies and practices to determine whether their companies lobby directly or indirectly (through each of their trade or other associations) for public policies that support the transition to a low-carbon economy consistent with the goals of the Paris Agreement.

If the board or committee determines that the company has lobbied (directly or indirectly) against Paris-aligned policies (or in favor of actions that would delay, negate, or obstruct such policies), it should oversee public disclosure explaining the reasons behind this misalignment, along with any steps the company is taking to address legal, financial, or reputational risks resulting from this misalignment.

For additional resources, please refer to the Global Standard on Responsible Corporate Climate Lobbying. The standard was designed to help companies and investors assess and ensure that corporate lobbying efforts support meeting the Paris Agreement goals. Investors and companies may also find the Responsible Policy Engagement Analysis published by Ceres in November 2022, the Responsible Policy Engagement Benchmarking for Banks published by Ceres in August 2023, the Responsible Policy Engagement Benchmark for Power Companies published by Ceres in January 2024, and the Responsible Policy Engagement for Automotive Companies published by Ceres in May 2024, to be useful resources on lobbying and policy influence practices.

### I. Sufficient Disclosures Pursuant to the TCFD Recommendations or IFRS S2

Until the mandatory climate-related disclosures are implemented, companies should continue to disclose according to the TCFD recommendations or IFRS S2 standards. If a company's reporting does not fully cover all 11 TCFD recommendations or all the core elements of IFRS S2, the company should disclose its plan for making all the recommended disclosures public within a specified timeframe. Subject to superseding regulations, these disclosures should appear in a company's annual financial reporting, sustainability report, or standalone TCFD report on a company's own website.

## Board Accountability for Climate-Related Risk Governance

In cases where an investor decides to escalate its engagement with a company on climate-related issues, Ceres notes the following sample board-level engagement tactics and additional steps, as well as mitigating factors, that investors may consider in their engagements with companies regarding their climate-related risk governance.

For investors engaging with companies that they consider have not taken appropriate steps to address financially material climate-related risks and opportunities, this guidance may be used to help inform their engagements with directors who are responsible for overseeing different elements of climate-related risks and opportunities.

Investors have typically considered the following board-level engagement tactics, which may be taken privately or publicly:

**Privately, an investor may consider:**

- Writing to or meeting with select directors **in advance of** a company's annual shareholders meeting, explaining why an investor may consider a vote against these directors, with reasons tied to the topics that the investor has engaged the company and its independent directors with over the past year(s). The explanation provided by an investor could reference how the company's actions or disclosures have fallen short of the investor's stated proxy voting policies. If there is sufficient time in advance of the annual shareholder meeting, investors can consider inviting further engagement with relevant independent directors in their private letter.

- Writing to or meeting with select directors **either before or after** a company's annual shareholders meeting, letting them know that this is the last meeting at which those directors can be assured of an investor's support for re-election if meaningful progress is not forthcoming on the topics on which the investor has engaged the company and its independent directors over the past year(s).

- Writing to or meeting with select directors **after** a company's annual shareholders meeting, explaining why an investor voted against these directors, with reasons tied to the topics on which the investor has engaged the company and its independent directors over the past year(s), while inviting further engagement with relevant directors. The investor's explanation could also reference how the company's actions or disclosures have fallen short of the investor's stated proxy voting policies.

**Publicly, an investor may consider:**

- Publicly pre-declaring their votes against select directors on an investor's website, a third party's website (such as the PRI Proxy Voting Website), or (upon the advice of the investor's own legal counsel) in an exempt solicitation filed with the U.S. Securities and Exchange Commission (SEC), with reasons tied to the topics on which the investor has engaged the company and its independent directors over the past year(s).

- Launching a "vote-no" campaign against select directors in a letter to other company shareholders, which (upon the advice of the investor's own legal counsel) may be filed as an exempt solicitation with the SEC, with reasons tied to the topics on which the investor has engaged the company and its independent directors over the past year(s).

- Alerting one or more proxy advisory firms to the investor's public actions, for their consideration in formulating their own annual shareholder meeting recommendations for the company's directors.

- Depending on the vote outcomes for select directors, writing **publicly or privately after** a company's annual shareholders meeting to these directors to ask how they intend to respond to the vote outcomes, as well as to inquire about the feedback the directors have received from other shareholders regarding the reasons behind the negative votes. This direct outreach would allow investors to convey their perspectives, understand the board's planned actions, and assess whether those actions sufficiently address shareholder concerns raised through the vote outcomes.

**Investors who have taken board-level escalation steps have often included one or more of the following types of directors in their engagements:**

- Chairs of the most relevant board committees.

- All members of the most relevant board committees.

- For situations without specified committee climate oversight responsibility, one or more of the following:

  - Audit committee chair (or all audit committee members), since audit committees are generally responsible for risk oversight.

  - Nominating/governance committee chair (or all nominating/governance committee members), since nominating/governance committees are responsible for recommending to the full board the delegation of appropriate board committee oversight of relevant risk issues.

  - Public affairs/sustainability committee (or equivalent committee) chair (or all committee members), since they may have relevant oversight responsibilities.

  - Independent chair or lead independent director.

  - All members of the board of directors.

  - Directors with problematic or insufficient experience or expertise

In evaluating whether to initiate any escalation steps with one or more directors, investors often consider additional context for individual companies, including the specific industry's pace of decarbonization (as determined by leading groups such as the Science Based Targets initiative and the International Energy Agency's Net Zero by 2050 Roadmap) and related disclosures, geographies, and technological advances. When considering board-level engagement tactics, it is important for investors to identify and prioritize dialogue with directors whose specific backgrounds, committee memberships, and oversight responsibilities are most relevant to the climate risk issues or opportunities being raised. Prioritizing the right directors helps ensure substantive discussion with those accountable for overseeing the specific areas of climate change preparedness that investors find lacking, including enhanced oversight disclosures.

## Additional Resources

Climate Action 100+ Net Zero Company Benchmark 2.0 (March 2023)

Climate Action 100+ Benchmark 2.0 2023 Results (October 2023)

TCFD Implementation Guidance Update (October 2021)

TCFD 2023 Status Report (October 2023)

ISSB IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information (June 2023)

ISSB IFRS S2 Climate-related Disclosures (June 2023)

Comparison of the IFRS S2 Climate-related Disclosures with the TCFD Recommendations (July 2023)

EU's Corporate Sustainability Reporting Directive

EU's Corporate Sustainability Due Diligence Directive (May 2024)

KPMG: Global Implications of the EU's Corporate Sustainability Reporting Directive (June 2024)

KPMG: Impact of EU Supply Chain Laws on US Companies (May 2024)

This guidance was authored by Rob Berridge, Senior Director of Shareholder Engagement, and Jay Zubillaga, Senior Manager of Shareholder Engagement, with the assistance of Rhonda Brauer, President, RLB Governance LLC. As climate risk oversight expectations and investor practices continue to evolve, Ceres expects to continue to update this guidance.

### About Ceres

Ceres is a nonprofit advocacy organization working to accelerate the transition to a cleaner, more just, and sustainable world. United under a shared vision, our powerful networks of investors and companies are proving sustainability is the bottom line—changing markets and sectors from the inside out. For more information, visit ceres.org.

# Appendix

## Guidance on Director Engagement Questions

A company's board of directors has a distinct role and certain specific responsibilities within an organization that differentiates it from company management. While both have a legal duty to act in the best interests of the company and its shareholders, the legal distinctions should help inform, at a general level, the types of questions that investors could consider asking independent directors in corporate engagements on climate-related issues.

Under state corporate law in the U.S., the board is responsible for the direction and management of the company. However, public-company boards typically delegate broad authority to management to run the business on a day-to-day basis. Certain key functions cannot be delegated, including hiring, evaluating, paying, and firing the CEO and senior members of their team, and providing strategic and financial guidance in the context of overseeing, for example, corporate performance, financial objectives and reporting, major plans and transactions, major changes in auditing and accounting principles and practices (including independent auditor selection), internal controls, risk management, ethics, and compliance.

Ultimately, the board is responsible for ensuring that the company has a comprehensive risk management framework in place that will help management and the board understand and evaluate the company's specific financial, operational, legal, and reputational risks that are associated with climate change. In addition, and again more specifically as it relates to climate-related risks and opportunities, boards have a responsibility to oversee the accuracy and transparency of the company's financially material climate-related disclosures to ensure that there is alignment with regulatory requirements and to ensure that the company is well-prepared to adapt to the physical and transition risks that climate change presents to the company's strategy and business operations.

The board has two primary fiduciary duties that inform the below questions: its duty of care, which requires it to act on an informed basis and in good faith; and its duty of loyalty, which requires it to not let any personal interest take precedent over the interests of the company and all of its shareholders.

Investors may want to consider the following questions as a guide that could help inform agendas in director engagements with specific companies on climate-related issues, keeping in mind the day-to-day duties that the board of a public company generally delegates to management:

## Questions about Board Oversight of Development, Implementation, Monitoring, and Disclosure of Company Decarbonization Plans

- What steps do your board and board committees take and how often to oversee meaningful company efforts to make progress toward developing, implementing, monitoring, and disclosing science-based greenhouse gas emission reduction targets over the short, medium, and long term?

- How does your board stay informed about the potential climate-related risks and opportunities that do or could impact the company's businesses, strategy, financial planning, and long-term value?
    - o Which managers and external independent third parties provide briefings to your board and board committees on these issues? And how often?

- How does your board oversee the integration of climate-related risks and opportunities into the company's overall business strategy, risk management framework, financial disclosures, significant capital allocation decisions, and other related decision-making processes?

- How does your board use climate-related scenario analyses (as set forth in your TCFD disclosures or otherwise) to evaluate whether to proceed with capital expenditures proposed by management?
    - Does your board consider both upside and downside scenarios, considering—among other factors—U.S. policies (and those in other major jurisdictions in which the company operates) that do or may encourage a phaseout of fossil fuels and an increased use of renewable energy and electric vehicles?
    - How does your board determine and monitor whether the percentage of the company's capital expenditure budget (and its R&D expenditures) allocated to company decarbonization efforts is sufficient to achieve the company's decarbonization targets?
    - Has your board discussed with management any climate transition action plans that management has given or is preparing to give the company's lenders, which are increasingly required to help lenders meet their own decarbonization goals?
        - *With this line of questions, investors are seeking confidence that the company's decarbonization targets and climate-related scenario analyses are being properly overseen to ensure responsible long-term capital deployment and the creation of long-term value for the company.*

- [**Questions specific to utility companies**]**:** As part of your company's consideration of investments in innovative technologies, has company management discussed with your board whether these investments could be financed by clean energy loans offered by the **U.S. Department of Energy's Loan Program Office** (LPO), when this debt financing may not be available from commercial banks at all or at higher rates than those offered by the LPO?
    - Has management discussed with your board the role that these loans could play to make your company's electricity more affordable to your customers, thereby securing regulatory and stakeholder support?

- [**Questions specific to financial institutions**]**:** As part of your institution's efforts to decarbonize its lending portfolio, how does your board stay informed of the climate transition plans of the companies in your institution's lending portfolio?
    - What has management discussed with your board in terms of any scenario analysis that is required to be—or voluntarily—included in those climate transition action plans, as a condition for providing financing or otherwise?

### Questions about Audit Committee Oversight of Climate-Related Risks and Disclosures

- In your discussions with the company's internal and external auditors, how do your audit committee and management team review and discuss climate-related risks relevant to the respective annual work scopes of these auditors?
    - How does your board and audit committee integrate upside and downside climate-related scenario analyses (as set forth in your TCFD disclosures or otherwise) into your review of the company's current portfolio of assets, including whether their reasonably estimated future revenues are sufficient to justify their currently estimated lives, as reflected in the company's audited financial statements?
    - How and how often does your audit committee discuss with the company's independent auditors the impact of the company's scenario analyses on the valuation of the company's assets? What has the audit committee learned from these discussions, including best practices that these auditors have shared from other industry clients?
        - *Investors would like to better understand whether and how your audit committee directs the company's internal audit department and independent auditors to include in their respective annual work scopes sufficient testing of the impacts of climate-related risks on the company's operations and review of the related disclosures in the company's audited and interim financial statements, including any assumptions and scenario analyses used in their respective work scopes.*

- How does your audit committee review and discuss with the company's independent auditors the inclusion (or lack thereof) of climate-related risks and the energy transition in the Critical Audit Matters (CAMs) included in their independent auditor opinion on the annual financial statements?

- How does your audit committee ensure that the company is telling a consistent story internally and across its public reporting, for example, that the climate-related financial statement inputs are directionally aligned with climate-related risks and targets disclosed by the company?
  - *Investors would like to better understand the audit committee's processes for ensuring that financial statement price assumptions, production estimates, remaining asset lives, and any asset retirement obligations (AROs) timing are directionally consistent with information discussed internally and disclosed in sustainability/climate reports and investor presentations.*

- How often and how does your audit committee review with your independent auditors and company management the costs associated with the retirement of company assets with indeterminate retirement dates (for instance, oil, gas, and coal), when such assets may be retired as part of the transition to a low-carbon economy?
  - What triggers such reviews?
  - What is your audit committee's understanding of how uncertainty is incorporated into the identification and measurement of the company's AROs?
    - For example, does your audit committee review a range of potential settlement dates, based on each asset's estimated economic life, including the probabilities associated with such potential settlement dates in the context of the climate-related scenario analyses used and disclosed by the company? If not, why not?
    - Based on known information, how does the company deal with the possibility that these assumptions and estimates (including discount rates used for estimating values of AROs) will likely change in the near to long term, again in the context of the climate-related scenario analyses used and/or disclosed by the company?
  - In the case of the company's AROs, does your audit committee receive from management and your independent auditors the current undiscounted values of such AROs (the amount to settle the associated liabilities today)? If not, why not, as not knowing these values could impact the legal ability of your board to declare dividends and to authorize share repurchases?
    - Would you encourage the company to disclose these amounts in an audited report, as companies like bp and Shell[7] currently do?
      - *This information would allow investors to make their own assessments of the timing for when those liabilities will arise, which may differ from the company's own projections.*
  - If the company plans to repurpose an asset, and therefore claims it will not need retire it, does the audit committee receive information from management on the costs associated with repurposing such asset?
    - Apart from early planning and the provisioning of funds, has management reviewed and presented to the audit committee alternative options that the company may consider to reduce the cost of its AROs?
      - For example, has the company explored financing options through the Energy Infrastructure Reinvestment (EIR) category of the Title 17 Clean Energy Financing Program from the the U.S. Department of Energy's Loan Programs Office (LPO) for repurposing, retrofitting, or replacing energy infrastructure that has ceased operations or enables operating infrastructure to avoid or reduce air pollutants or GHG emissions?
      - If so, have your independent auditors shared with the audit committee the accounting implications of pursuing such an option and industry best practices they have seen with other clients?
        - *Investors encourage companies in the coal, oil and gas, utility, nuclear, and manufacturing sectors to thoroughly evaluate the potential benefits of loans offered by the Energy Department's LPO and through the EIR program. These loans present a unique opportunity to not only enhance individual*

*company performance but also contribute to the broader national goal of leveraging existing energy infrastructure and skilled workforce to facilitate the energy transition. It is important to note that the favorable terms of EIR debt financing may not be readily available through commercial banking channels, if at all. When such financing is accessible via traditional means, it often comes at significantly higher interest rates compared to those offered by the LPO.*

### Questions about Board Oversight of the Company's Voluntary Climate-Related Disclosures (TCFD or the ISSB's IFRS Sustainability Standards) and Upcoming Mandatory Disclosures

- What is the board's understanding and oversight of the company's TCFD reporting or disclosures according to the ISSB Standards, particularly when it is unclear if all 11 TCFD disclosure recommendations or all four of the core IFRS S2 climate-related disclosures are fully covered?
  - o *The global acceptance of the TCFD's recommendations and the ISSB's IFRS Sustainability Standards (especially given the support of the G20*[8]*) makes the company's voluntary disclosure of critical importance to investors seeking financially material information about their portfolio companies and their climate-related risks and opportunities.*

- How is your board being kept updated on the "gap analysis" work being conducted by management, to determine what new mandatory disclosures will soon be required in the jurisdictions in which the company does business?
  - o How, and how often, is your board and audit committee discussing with the company's independent auditors how the assurance for these new requirements will be provided?
  - o What has your board and audit committee learned from these discussions with the company's independent auditors about, for example, their experience with their other clients in your industry?
    - *In the case of CSRD, investors expect that companies within the value chain of EU-based entities may begin receiving requests for climate-related data as early as 2024, given that many EU-based entities are mandated to file their inaugural CSRD disclosures in 2025.*

### Questions about Board Oversight of Company Policies and Practices Related to Climate Lobbying

- How does your board oversee the company's direct and indirect lobbying activities?
- How does your board review the company's lobbying activities (direct or indirect through industry associations and similar collaborations) and their consistency with the Paris Agreement or the company's public statements (including targets and goals) concerning climate-related issues?
- If not already done, would your board consider encouraging the company's senior management team to establish forward-looking climate-related public policy priorities that would align with and support the company's ability to meet its GHG emission reduction targets or other climate-related goals?
- If not already done, would your board encourage the company's senior management team to privately share the results of a third-party independent assessment of the company's climate policy influence activities and the alignment of such activities with the company's own climate-related commitments and policy priorities, as other public companies have done?[9]

### Questions about Climate Change Expertise/Capacity of the Company's Board of Directors

- How does your board assess and publicly disclose the ways in which you and your fellow directors' expertise and experience contribute to thoughtful board discussions about the company's long-term strategy, business operations, risk management, financial planning, and financial and non-financial public reporting, particularly given the unique climate-related risks and opportunities that the company faces?

## Endnotes

1 Most investors maintain highly diversified portfolios designed to capture the returns of the overall market. For such investors, climate change poses a systemic risk that could broadly impact economic productivity, resource availability, supply chains, infrastructure, and social stability across sectors and geographies. Since these portfolios are essentially invested in the entire market, widely diversified investors cannot effectively mitigate climate risks through portfolio rebalancing alone. The pervasive and escalating effects of climate change have the potential to disrupt economic systems and markets as a whole, threatening the long-term performance of broadly diversified portfolios. As a result, climate change represents a systemic portfolio risk that could impair returns for investors seeking to replicate overall market performance.

For additional resources on systemic risk management and portfolio materiality, see:

- A Legal Framework for Impact: Sustainability Impact in Investor Decision Making (Freshfields Bruckhaus Deringer, July 2021)
- Managing Climate Risk in the U.S. Financial System (Commodity Futures Trading Commission, September 2020)
- Addressing Climate as a Systemic Risk (Ceres, June 2020)

2 In the U.S., the U.S. Securities and Exchange Commission (SEC) has approved a rule that will require registrants to report on their material climate risks in a manner consistent with the Task Force on Climate Related Financial Disclosure (TCFD) framework, as well as material scope 1 and 2 greenhouse gas (GHG) emissions. Under the final rule, disclosure would begin on a timeline that starts in 2026 based on FY 2025 information for large accelerated filers. Compliance dates are phased in based on the content of the disclosure and the filer status of the registrant, with smaller and more newly public companies reporting at later dates and on less information. The SEC's final rule was set to take effect on May 28, 2024; however, SEC commissioners voluntarily stayed the rule on April 4, 2024, pending completion of litigation proceedings in the U.S. Court of Appeals for the Eighth Circuit.

In the EU, The Corporate Sustainability Reporting Directive (CSRD) will require many large entities based in the EU, including subsidiaries of an estimated 10,000 non-EU companies, to disclose climate and sustainability information as defined by the European Sustainability Reporting Standards (ESRS), including material Scope 1, 2, and 3 GHG emissions. The CSRD employs a unique double materiality test, meaning companies will report not only on how their business is affected by sustainability issues (financial materiality), but also on how their activities impact society and the environment (impact materiality). The CSRD is a more complex sustainability disclosure regime than pure climate disclosure regulations such as the SEC rule. The EU will require companies to disclose information on dozens of key performance indicators that encompass biodiversity, resource use, pollution, workforce, and other topics. Reporting will start in 2025 (based on FY 2024 information) for EU companies already subject to the Non-Financial Reporting Directive; large subsidiaries of non-EU parent companies (based on revenue, assets, and employee headcount) will be required to report in 2026 based on FY 2025 data. In addition, to meet their own reporting obligations, EU companies will likely pass CSRD data requirements down to their major non-EU suppliers through contractual terms, questionnaires, and/or engagement. In addition, the EU's Corporate Sustainability Due Diligence Directive (CSDDD) will require certain large EU and non-EU companies that meet employee and net turnover thresholds to address adverse environmental impacts because of their own operations and to implement and disclose a climate change mitigation transition plan.

In Australia, Canada, Brazil, Japan, the United Kingdom and other non-US markets, regulatory bodies have consulted on or are planning to incorporate the International Sustainability Standard Board's (ISSB) sustainability and climate-related reporting standards (IFRS S1 and IFRS S2) into their mandatory corporate disclosure rules. The ISSB IFRS S2 guidelines, which cover the climate-related reporting standards, have incorporated the TCFD framework.

3 The Financial Stability Board's (FSB) TCFD is a widely accepted framework for company reporting of climate-related financial information that was introduced in 2017 (and was a focus of the previous iteration of this Guidance). The TCFD was fully absorbed by the International Financial Reporting Standard (IFRS) Foundation and incorporated into the IFRS Foundation's ISSB Standards which were issued on June 26th, 2023. The IFRS Foundation agreed to take over the responsibility of monitoring company progress on climate-related disclosures starting in 2024. Accordingly, the Financial Stability Board announced that the work of the TCFD has been fulfilled, and that TCFD has been incorporated into ISSB's IFRS S1 (General Requirements for Disclosure of Sustainability-related Financial Information) and IFRS S2 (Climate-related Disclosures) disclosure standards. While monitoring of companies' climate-related disclosures has transitioned from the TCFD to the ISSB, the TCFD's recommendations remain an accepted framework that companies can continue utilizing. As individual countries and regulators update their disclosure guidance to reference the ISSB standards, many companies will be expected to align with the new ISSB framework over time. However, reporting that follows the TCFD recommendations will likely still be viewed as providing decision-useful climate information to investors during this transitional period.

4 The Climate Action 100+ Net Zero Company Benchmark assesses the performance of focus companies against the initiative's three high-level goals: emissions reduction, governance, and disclosure on and implementation of net zero transition plans. Four sets of company assessments against the Benchmark have been released since March 2021. For further information, see www.climateaction100.org/net-zero-company-benchmark/.

5 The New York Stock Exchange and Nasdaq require that the audit, compensation, and nominating/governance committees for all listed companies, with some limited exceptions, be composed entirely of independent directors.

6 See pg. 07 of Ernst & Young's Five Top Takeaways from the 2024 Proxy Season at www.ey.com/content/dam/ey-unified-site/ey-com/en-us/campaigns/board-matters/documents/ey-five-top-takeaways-from-the-2024-proxy-season.pdf

7 See, e.g., bp Annual Report and Form 20-F, 2023, p. 341, at www.bp.com/content/dam/bp/business-sites/en/global/corporate/pdfs/investors/bp-annual-report-and-form-20f-2023.pdf, and Shell Annual Report and Accounts 2023, at reports.shell.com/annual-report/2023/consolidated-financial-statements/notes/climate-change-and-energy-transition.html?tabc=1e7.

8 See pg. 15-16 of September 2023 G20 New Delhi Leaders' Declaration at www.consilium.europa.eu/media/66739/g20-new-delhi-leaders-declaration.pdf.

9 See, e.g., the 2023 Climate Policy Engagement Review for Unilever at www.unilever.com/files/unilever-climate-policy-engagement-review.pdf and bp's 2022 Our Participation in Trade Associations: Climate Review at www.bp.com/content/dam/bp/business-sites/en/global/corporate/pdfs/sustainability/our-participation-in-trade-associations-climate-review-2022.pdf