Disclosure of ESG information in the capital market: a comparison between the Brazilian and North American models

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Considering the growing relevance of the theme "ESG" (Environmental, Social and Governance) for investors and for the market in general, the regulatory bodies of the Brazilian and North American capital markets have proposed new rules on the subject, especially regarding the dissemination and standardization of information of this nature. The form of disclosure of the companies' ESG policies and initiatives and the possibility of effective comparison between peers on this matter are still a central challenge in this area.

Brazilian capital market

In Brazil, companies registered with the Securities and Exchange Commission of Brazil (CVM) will now have to disclose information on ESG factors in their reference forms ("Formulário de Referência", in Portuguese), which did not have a specific section for dealing with the matter. In December 2021, CVM published CVM Resolution No. 59. This Resolution brought changes to the CVM Instruction No. 480 then in force (rule that regulated the registration and provision of periodic information on issuers of securities, recently revoked by CVM Resolution No. 80), starting to require detailed disclosure of information regarding ESG factors by companies.

In the new model of the reference form introduced by CVM Resolution No. 59, issuers registered in both "A" and "B" categories will have to disclose, as of 01.02.2023, specific information in relation to ESG issues (if the issuer discloses ESG issues in its annual report and the methodology or standard followed in preparing that report, for example), while only issuers registered in category "A" must also disclose the effects of state regulation on the issuer's activities regarding the main aspects related to the fulfillment of legal and regulatory obligations related to environmental and social issues. The new regulation of CVM introduced the "comply-or-explain" model, so that companies that choose not to disclose ESG information must justify the reason why they made such a decision. In this way, CVM seeks to disseminate the disclosure of ESG issues by companies.

Following this sustainability agenda in the Brazilian capital market, B3 SA – Brasil, Bolsa, Balcão (the Brazilian stock exchange) released, in August 2022, a public hearing notice that proposes the creation of an annex to the "Regulation for the Listing of Issuers and for the Admission of Securities for Trading", aimed at increasing the adoption of ESG practices by listed companies. Among other measures, B3 proposes the election of at least one woman and a member of minority communities (black or brown people, members of the LGBTQIA+ community, or people with disabilities) as effective members of the boards of directors or executive boards of companies. Through these measures, B3 seeks to promote diversity and inclusion in leadership positions of listed companies.

The proposal also suggests changes in the eventual policies of variable remuneration of the companies' management, which must include performance indicators linked to ESG themes or goals.

The changes proposed by B3 are not at all imposing, also following the logic of the "comply-or-explain" model adopted by CVM: companies that are unable to elect managers according to the diversity criteria, or that opt for variable compensation policies without ESG indicators, will need to explain to the market the reasons that made progress unfeasible and the reasons for the respective decision.

North American capital market

ESG issues have also played a prominent role in the agenda of the Securities and Exchange Commission (SEC), the regulatory body for the US capital markets. In March 2022, SEC approved a regulatory proposal to require standardized disclosure of environmental information by companies listed on US stock exchanges, including foreign issuers (and, consequently, Brazilian companies listed on the NYSE and Nasdaq, for example).

According to the proposal, all companies that have securities traded on the stock exchange will have to provide the following information in their annual financial statements: (i) the governance of climate risks and the processes adopted to manage these risks; (ii) how climate risks will have a material impact on its business, whether in the short, medium and long term; (iii) how climate risks have affected or may affect the company's operating strategy, as well as its business model and prospects; and (iv) the impact of severe weather events and other natural conditions and transition activities on the company's consolidated financial statements, as well as on its financial estimates and assumptions.

In addition, the rules proposed by SEC also provide that companies must disclose information about their carbon emissions, which are divided into the following scopes: Scope 1 – Emissions from the company's primary activities; Scope 2 – Emissions from energy acquired by companies to carry out their activities; Scope 3 – Emissions associated with the company's production chain (suppliers and consumers of products and services). Scope 3 is called "value chain emissions", being the most sensitive point of the regulatory proposal, as it imposes strict monitoring on companies throughout their production and consumption chain. According to the SEC, these proposals for disclosure of greenhouse gas emissions would provide investors with useful information in assessing an issuer's exposure to climate risk and its management.

Smaller companies are exempted from the obligation to disclose the information provided for in Scope 3, while large companies will have another obligation: the accounting of emissions in scopes 1 and 2 will have to be submitted to an independent audit.

If the proposal is approved, the new SEC rules – which follow the standards set by the Task Force on Climate-Related Financial Disclosures – will come into effect in fiscal year 2023, and will apply to the presentation of financial statements for fiscal year 2024.

In addition to the above, in May 2022, SEC proposed changes to the rules on the disclosure of ESG information by investment funds and their managers, so that investors have access to consistent and comparable data on ESG strategies adopted by asset managers. If the rules come into force, they will apply to asset managers, investment companies and business development companies.

The new rules proposed by SEC seek to categorize certain types of ESG strategies and require investment funds and their managers to make more specific disclosures in the funds' prospectuses and their annual reports. In more practical terms, the SEC proposal requires, in relation to investment funds that focus on the environmental aspect of "ESG", the disclosure of greenhouse gas emissions metrics related to their portfolios. Funds that seek a specific ESG impact, in turn, must describe it, as well as summarize their progress and the key factors that have contributed to it.

Both regulators – CVM and SEC – have made great advances in the sustainability agenda to meet market demands regarding the disclosure of ESG information, creating a consistent basis for comparability between companies. It cannot be overlooked, however, that if the SEC rule regarding the disclosure of ESG information is approved in the proposed form, the accounting of greenhouse gas emissions inventory, especially with regard to value chain emissions, will impose companies registered in the US a more rigorous process than the "comply-or-explain" model will impose on publicly traded companies in Brazil.

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