MINING COMPANY SETTLES SEC ESG-RELATED CHARGES

The Securities and Exchange Commission (SEC) announced this week that a Brazilian mining company that holds itself out as the largest producer of iron ore, and whose ADSs trade on the New York Stock Exchange, has agreed to pay $55.9 million to settle charges brought by the SEC. The charges relate to allegedly false and misleading disclosures about the safety of the company's dams prior to the collapse in 2019 of its Brumadinho dam that killed 270 people. (My earlier briefing note outlining the charges is available here.) The SEC's complaint alleged that, for years, the dam did not meet internationally-recognized safety standards even as Vale's public statements assured investors that all of its dams were certified as stable.

The company, Vale S.A., which had disclosed as recently as last month that it would contest the allegations, issued its own statement following the SEC announcement.

The settlement remains subject to approval by the US District Court for the Eastern District of New York.

The launch of the enforcement action by the SEC, and the subsequent settlement, underscore the potential liability that SEC reporting companies face under the antifraud provisions of the US securities laws for material misstatements and omissions in their ESG-related disclosures, as they would for any other material misstatements or omissions. The complaint cited actionable statements in a company investor presentation, the company's Form 20-F annual report and "filed" Form 6-K disclosures, CEO statements at an investor meeting, two of the company's sustainability reports and an ESG webinar published on the company website. In its press release, the SEC specifically noted the connection between statements in sustainability reports and potential liability under the securities laws.

The charges brought against Vale are part of the SEC's focus on climate and ESG from an enforcement perspective (announced concurrently with the establishment in 2021 of its Climate and ESG Task Force). This action is separate from the pending SEC rulemaking on climate-related disclosures. The prospective enforcement efforts expressly were to be based on existing standards of disclosures (and hence liability) under the securities laws.

The focus on ESG disclosure was tied, at the time the enforcement action was announced last April, to the growing reliance by investors on ESG disclosures in sustainability reports and other public filings. As the Director of the SEC's Division of Enforcement noted last April, "By allegedly manipulating those disclosures, Vale compounded the social and environmental harm caused by the Brumadinho dam's tragic collapse and undermined investors' ability to evaluate the risks posed by Vale's securities." The SEC noted in its complaint that "concealment of the true condition of the Brumadinho and other tailings dams … misled investors regarding the stability of Vale's dams; the nature of Vale's safety practices in the wake of [a prior] dam disaster; and the actual risk of catastrophic financial consequences should any of its high-risk dams, like the Brumadinho dam, collapse.

While the timing and final contours (and, potentially, its fate, if challenged) of the pending SEC rulemaking remain uncertain, the conclusion of the Vale enforcement action is a timely reminder that disclosure principles apply equally in the context of ESG claims and equally to disclosures in voluntary reporting (such as sustainability reports, which have become widespread, but are not mandated by disclosure rules). Ironically, SEC commissioners opposed to the SEC climate-related disclosure rulemaking cited the adequacy of existing disclosure rules to cover material climate risk as a basis for their opposition to line-item climate disclosure obligations (*see, e.g.*, ["We are Not the Securities and Environment Commission - At Least Not Yet")]().

It is not surprising that an increasing number of asset owners/asset managers (from an investment perspective) and companies (both from an operational perspective, as well as in response to demands for decision-useful, consistent and comprehensive ESG information from investors as well as other stakeholders ranging from suppliers to customers) are taking the high road in a fast-changing ESG landscape as they confront an array of considerations relating to climate and other ESG themes. This tendency needs to be carefully balanced against the underlying facts. Disclosure that finds its way into public materials can arise from a variety of internal sources, and ESG themes may not necessarily emerge from the same channels that typically feed into public disclosure. The bedrock principle of disclosure remains, if speakers choose to speak and if the statements are material, they must be free of material misstatements and omissions.

It is noteworthy that, in its 76-page complaint, the SEC made a point of addressing the role, responsibility and control of specific company personnel responsible for dam safety risk management (including three senior executives with managerial responsibilities and sub-certifications duties, and a manager) and, in particular, their role as the source of Vale's allegedly false statements to investors. The SEC went so far as to provide a schematic setting out reporting lines, all the way up to the CEO and the Executive Board. It is also noteworthy that the complaint provided an exhaustive chronology of internal events. Finally, it is noteworthy that the complaint set out the basis for the SEC's conclusions on materiality.

The message was clear at the time the SEC filed its complaint: no matter how complex or complicated technical issues may be, even in large companies, if technical data form the basis of public misstatements or omissions by SEC reporting companies, and those misstatements or omissions are material, liability can, and will be, actionable under the securities laws. This week's settlement underscores that message.

Admittedly, this was an egregious set of alleged facts, but lest there be any confusion about the role of the SEC here in terms of overstepping its bounds and/or seeking to regulate the environment, that is not the case. The crux of the action is set out in paragraph 272 of the complaint: "shortly after the true condition of the Brumadinho dam [(obscured by deceptive conduct and misstatements)] became known to investors as a result of its catastrophic collapse, Vale's market capitalization declined by over $4 billion, its American Depositary Shares lost more than 25% of their value, and its corporate credit rating was downgraded to junk status."

As companies consider how they can best respond to demands for climate and other ESG information, today without, but with an eye towards, the pending SEC rulemaking, there is an urgency to creating and refining the methodologies and internal data infrastructures that can produce the inputs for climate-related disclosures. At the same time, there is an urgency from the perspective of climate, in particular, to creating the internal governance processes that enable boards to undertake their oversight responsibilities and enable management to properly discharge their responsibilities. Finally, to return to the SEC enforcement action, the foregoing needs to be accompanied by an internal control environment able to effectively understand and vet public disclosures.

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Mark S. Bergman
<u>7Pillars Global Insights, LLC</u>
Washington, D.C.
March 31, 2023