

Environmental Activist Petitions the SEC Staff Alleging Material Omissions in an Issuer's Registration Statement

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The Chesapeake Climate Action Network (CCAN) has taken the novel approach of filing a [letter](#) with the SEC Directors at the Division of Enforcement and the Division of Corporation Finance, alleging that Dominion Midstream, a Dominion Resources affiliate, did not provide sufficient information about several environmental and related risks surrounding its Dominion Cove Point LNG Terminal export project in its registration statement filed with the SEC offering its limited partnership interests. The offering has not yet occurred. Betty Moy Huber, co-head of Davis Polk's Environmental Group, guides us through these unique proceedings and the possible implications.

What does CCAN allege is missing from the registration statement in its letter to the SEC?

CCAN lays out a laundry list of items it claims are missing, some more compelling than others. In general, CCAN alleges that various facts that add up to the financial precariousness of the Cove Point Project are absent from the disclosure in the registration statement. First, CCAN wants specific information regarding permitting delays surrounding the Project and whether these delays could trigger the termination of certain key contracts. Second, CCAN wants Dominion to disclose the risk of environmental litigation involving the Project that CCAN itself would likely bring, which litigation could result in further Project delays. Third, CCAN notes various other, arguably run-of-the-mill, environmental risks. Finally, CCAN urges disclosure of financial information of, and litigation involving, Dominion Resources, all in an effort to demonstrate the potential financial risks of investing in this Project.

These items, whether or not they are material under the U.S. securities laws, constitute information CCAN would like socialized insofar as it could help detract investors from purchasing the securities offered and thus harm the Project.

Why did CCAN approach the SEC in addition to energy or environmental regulators? What is the benefit of their strategy and their end goal?

We should probably start with CCAN's end goal, which is to block, in its entirety, the building of the Cove Point LNG Export Project. CCAN is concerned that this and other export terminals will simply increase natural gas exploration and production in the United States as well as increase greenhouse gases worldwide.

Prior to its petition to the SEC, CCAN had already approached other regulators and governmental officials in its fight against Cove Point. For instance, CCAN has already submitted comments to the Federal Energy Regulatory Commission, or FERC, in response to Dominion's application for FERC approval to build and operate this LNG export facility. In addition, CCAN recently signed a letter asking President Obama to direct FERC to complete a rigorous environmental review of Cove Point. Further, CCAN has solicited people to email Maryland senators to demand more meetings about Cove Point.

CCAN approached the SEC in hopes of legitimizing to some extent its questions about the Project's financing and overall viability. This strategy, while not yet used to challenge an individual project to my knowledge, has been used by various environmental groups in the past to further other environmental agendas. In fact, CCAN filed this petition jointly with an individual Dominion shareholder. The shareholder had previously filed a similar appeal to the SEC in November 2013 urging the SEC to examine the climate change disclosure relating to the biomass energy businesses of Dominion and two other companies. To my knowledge, the SEC has not acted on this request.

CCAN also sent this letter just one day before Dominion's annual shareholder meeting, likely with the goal of maximizing press coverage as well as to gain support for the greenhouse gas shareholder resolutions slated for vote. None of those proposals were approved.

Although the complaint is addressed to the SEC's head of enforcement as well, in this case an enforcement action is highly unlikely since the offering has not occurred, so it rests in the Division of Corporation Finance. What are the possible actions the SEC staff can take in light of this complaint?

One way or the other, Corp Fin will issue some comments to Dominion's registration statement as part of its standard and typical commenting process for all initial public offerings. It is possible, though highly unlikely, that the SEC has already issued comments in the few business days since the letter was sent, which are not yet publicly available. Corp Fin's eventual comment letter could exclude all of CCAN's requests, include some of them or (highly unlikely given the breadth and detail of CCAN's requests) include all of them. It is difficult to predict with certainty what Corp Fin might do. One could easily support the view that Corp Fin could ignore all of the comments given how politically charged this issue is and in light of the SEC's recent urging to respect its independence and not use the SEC as a vehicle to effect politically motivated disclosure. Alternatively, it is possible that Corp Fin submits a generic comment about permitting delays, environmental litigation and/or financing risk, which Dominion could probably resolve fairly easily.

The SEC staff has said that environmental risks can be material to an investment decision, and CCAN's letter appears to suggest that nearly every possible issue, such as permitting delays, and its attendant consequences, should be included in the registration statement. But clearly not all environmental-related issues require disclosure in SEC filings. How do companies navigate these issues?

Broadly speaking, registrants are required to disclose items specified in Regulation S-K, which include certain material environmental items such as environmental capital expenditures and environmental litigation, as well as other generic items that could require environmental disclosure, such as risk factors. These are the so-called "line item" disclosures. Registrants are also required to disclose material information the omission of which makes the existing disclosure, in light of the circumstances under which they were made, misleading. Companies new to the securities markets lean heavily on securities lawyers and other advisers to help gather information, and assess what of that information is material under the securities law in light of the facts and circumstances specific to that company. What can be material for one company may not be for another, larger and financially sound company. Issuers tend to disclose in broad strokes risks which give potential investors the overall flavor of material matters rather than disclosing each specific item and fact that a person might find material, so as to avoid information overload (of which the SEC has made various negative public statements in the recent past), or worse, misleading disclosure.

Will other environmental activists adopt similar methods of seeking assistance from the SEC to enforce their disclosure agenda? How should companies and market participants prepare for the use of this particular channel?

This is not the first nor will it be the last time environmental activists will appeal to the SEC to further their social agendas. Environmental groups were successful in petitioning the SEC to issue climate change disclosure guidance back in 2010. Those same groups recently issued a report with recommendations to the SEC on how the agency could do more with respect to that 2010 Climate Change Disclosure Guidance, including for Corp Fin to issue more greenhouse gas-related comments. It is fair to say this relatively inexpensive and easy appeal has become part of the environmental groups' collective playbook.

As for how companies and market participants should prepare, in the abstract, it is difficult to prevent this channel from being used against you since theoretically any registrant could be a target. That said, companies and/or their boards that proactively engage with environmental groups before they become targets are likely to be immune.

In Dominion's case, however, CCAN's petition was likely unavoidable because of the zero sum nature of what is at stake ? that is, either LNG export goes forward or not. But other companies facing activists with a less draconian endgame, for example, seeking better greenhouse gas disclosure from that particular company, can try to work with these groups earlier on, either by engaging with them in a dialogue, putting out their own "positive press" on their websites, or issuing communications showing that, despite their environmentally sensitive businesses, they are taking steps to be more sustainable.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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