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Sustainability Assurance

Law Working Paper N° 871/2025
September 2025

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For helpful comments, we thank Régis Bismuth, Howell Jackson, Anne-Catherine Muller, Anne-Claire Rouaud, and Steven Schwarcz. Usual disclaimers apply.

Abstract

A robust literature examines sustainability disclosures by public corporations, but legal scholarship has largely overlooked the role of third-party assurance—or verification—of such disclosures. This is a notable omission given the extensive literature on the auditing of financial statements, a related form of assurance. This article responds by examining the role of assurance in sustainability reporting. In keeping with the theme of this symposium volume, it draws on US and EU law. Our discussion begins in Part I with sustainability disclosures, focusing on the requirements and practices of public companies. In Part II, we introduce sustainability assurance as well as assurance providers (or sustainability assurers)—a type of green gatekeeper that assures the accuracy of sustainability information. In Part III, we assess the market mechanisms that may constrain assurance providers, arguing that these mechanisms—reputational incentives, for the most part—may fail to prevent false sustainability assurances and will be less effective than those that constrain traditional gatekeepers, including auditors. We also generally examine the strength of primary regulation of sustainability claims. In Part IV, we sketch some considerations relevant to determining how policymakers should respond on the premise that regulation is justified.

Keywords: Assurance, Corporate Governance, Double materiality, ESG, Gatekeepers, Greenwashing, Sustainability reporting, Third-party certification

JEL Classifications: G18, G41, H20, K20, K32, L30, Q54, Q55, Q58

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A robust literature examines sustainability disclosures by public corporations, but legal scholarship has largely overlooked the role of third-party assurance—or verification—of such disclosures. This is a notable omission given the extensive literature on the auditing of financial statements, a related form of assurance.

This article responds by examining the role of assurance in sustainability reporting. In keeping with the theme of this symposium volume, it draws on US and EU law. Our discussion begins in Part I with sustainability disclosures, focusing on the requirements and practices of public companies. In Part II, we introduce sustainability assurance as well as assurance providers (or sustainability assurers)—a type of green gatekeeper that assures the accuracy of sustainability information. In Part III, we assess the market mechanisms that may constrain assurance providers, arguing that these mechanisms—reputational incentives, for the most part—may fail to prevent false sustainability assurances and will be less effective than those that constrain traditional gatekeepers, including auditors. We also generally examine the strength of primary regulation of sustainability claims. In Part IV, we sketch some considerations relevant to determining how policymakers should respond on the premise that regulation is justified.

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Introduction

Sustainability disclosures by public corporations are a crucial fixture of the financial markets policy debate, both because many investors value sustainability[1] and because sustainability has become one of the many battlegrounds in the US culture wars.[2]

Leaving big-picture issues and ideological fault lines aside, an often-overlooked fact is that, even as sustainability claims proliferate, investors often struggle to assess their accuracy. Where that is the case, investors face the dilemma of either ignoring the sustainability claims or, if they take them at face value, accepting the risk of providing capital to firms engaged in "greenwashing."[3] Assurance providers should help resolve this dilemma. Assurance providers are gatekeepers—information intermediaries that certify claims about products or firms, thereby reducing the information asymmetry between the makers of claims and the recipients of these claims.[4] Like other gatekeepers, assurance providers "rent" or "pledge" their reputations to their clients,[5] effectively vouching for the accuracy of clients' claims.[6] In so doing, assurance providers can help investors determine which sustainability claims they should trust.

A key question thus becomes whether assurance providers have incentives to only certify truthful sustainability claims. To date, legal scholars do not appear to have tackled this question.[7] In this Article,

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[1] *See* Cynthia A. Williams & Donna M. Nagy, *ESG and Climate Change Blind Spots: Turning the Corner on SEC Disclosure*, 99 TEXAS L. REV. 1453, 1474 (2021) (collecting sources).

[2] *See, e.g.*, "How ESG Became Part of America's Culture Wars," The Economist, June 21, 2023, https://www.economist.com/the-economist-explains/2023/06/21/how-esg-became-part-of-americas-culture-wars (explaining how ESG and concepts such as sustainability have been associated with "wokeness," which "is what got [them] mixed up in the culture wars.").

[3] A firm engages in greenwashing when it makes sustainability claims that overstate its true sustainability levels. *See* Sebastião Vieira de Freitas Netto, et al., *Concepts and Forms of Greenwashing: A Systematic Review,* 32 ENV. SCI. EUR. 19 (2020)

[4] Luca Enriques, Alessandro Romano & Andrew F. Tuch, *Green Gatekeepers*, 109 MINN. L. REV. 609, 612 (2024).

[5] *See* Ronald J. Gilson & Reinier H. Kraakman, *The Mechanisms of Market Efficiency*, 70 VA. L. REV. 549, 620 (1984) ("[T]he investment banker [as gatekeeper] rents the issuer its reputation."); JOHN ARMOUR ET AL., PRINCIPLES OF FINANCIAL REGULATION, 139 (2016) (The value of intermediaries "lies in their preparedness to pledge their costly to build, easy to lose reputation to vouch for an issuer's disclosures or their own information products").

[6] *See* JOHN C. COFFEE, JR., GATEKEEPERS: THE PROFESSIONS AND CORPORATE GOVERNANCE 2-3 (2006) ("Central to this [gatekeeping] model is the … idea that [reputational capital] can be pledged … by the gatekeeper's vouching for its client's assertions or projections.");

[7] Important contributions have examined assurance providers operating in specific settings or the services they provide. *See, e.g.*, Iris H-Y Chiu, *Standardization in Corporate Social Responsibility Reporting and a Universalist Concept of CSR? – A Path Paved with Good Intentions*, 22 FLORIDA J. INT'L L. 361, 387–91 (2010) (tracing the rise of assurance services for CSR reporting and its ramifications); Quinn Curtis et al., *Green Bonds, Empty Promises*, 102 N.C. L. REV. 131, 172–75 (2023) (critiquing certification frameworks for green bonds); Marco Dell'Erba & Michele Doronzo, *Sustainability Gatekeepers: ESG Ratings and Data Providers*, 25 U. PA. J. BUS. L. 355 (2023) (examining ESG ratings and data providers); Longjie Lu, *Regulating ESG Rating Firms as the Gatekeepers for ESG Finance*, 19 CAP. MKTS L.J. 184 (2024) (considering ESG rating firms as verifiers of public companies' ESG credentials); Paul Rose, *Sustainability Verification*, 72 AM. U.L. REV. 1017 (2022) (examining verifiers of issuers' environmental, social, and other claims in bond documents). For a recent contribution in the accounting literature, *see* Brandon Gipper, Samantha Ross & Shawn X. Shi, *ESG Assurance in the United States*, 30 REV. ACCT. STUD. 1753 (2025).

Legal scholarship examining sustainability disclosures has made associated references to sustainability assurances. *See, e.g.,* Jill E. Fisch*, Making Sustainability Disclosure Sustainable*, 107 GEO. L.J. 923, 927 (2019); Virginia Harper Ho, *Nonfinancial Risk Disclosure and the Cost of Private Ordering*, 55 AM. BUS. L.J. 407, 449–50 (2018); Virginia Harper Ho & Stephen K. Park, *ESG Disclosure in Comparative Perspective: Optimizing Private Ordering in Public Reporting*, 41 U. PA. J. INT'L L. 249, 269, 290 (2019); Sarah E. Light & Eric W. Orts, *Parallels in Public and Private Environmental Governance*, 5 MICH. J. ENV'T. & ADMIN. L. 1, 44-45 (2015); Lynn M. LoPucki, *Repurposing the Corporation Through Stakeholder Markets*, 55 U.C. DAVIS L. REV. 1445, 1489–90 (2022); Dan Esty & Todd Cort, *Toward Enhanced Corporate Sustainability Disclosure: Making ESG Reporting Serve Investor Needs*, 16 VA. L. & BUS. REV. 423, 1457–58 (2022); Stephen K. Park, *Green Bonds and Beyond: Debt Financing as a Sustainability Driver*, we specifically address the incentives of assurance providers, investigating the strength of their reputational constraints and drawing some preliminary conclusions on the role that regulation can play in supporting their function.

In principle, gatekeepers' certifications hold value only insofar as they are perceived as reliable by certification users,[8] namely, for the purpose of this Article, investors.[9] In turn, this gives gatekeepers incentives to build reputations for issuing accurate certifications.[10] However, as we argue in a related work,[11] this reputational mechanism may operate differently for gatekeepers who certify sustainability-related claims ("green gatekeepers"). We apply these arguments to assurance providers, a type of green gatekeeper.[12]

We identify three reasons why reputational mechanisms are likely to be less constraining for assurance providers than for traditional financial gatekeepers.

First of all, while certification users could punish inaccurate certifications by trading the securities of companies that engage in the related greenwashing, they may have limited incentives to investigate the veracity of the certifications and may even actively avoid negative information.[13] This is due to well-known psychological mechanisms: users may derive utility from green certifications even if these are inaccurate, so long as they do not find that out. Essentially, users want to experience the "warm glow" of having made what they understand to be a sustainable investment decision—an experience that investigating green claims' accuracy might actually preclude.

Second, even assuming that certification users have the incentives to investigate whether the certifications issued by assurance providers are accurate, they may have limited ability to do so, given the complex nature of sustainability claims. Sustainability claims are hard to verify and, unlike the certifications of traditional financial gatekeepers, often fall outside the core competencies of certification users.[14]

Finally, users of sustainability assurances have little reason to investigate claims when their inaccuracy does not impose costs on them. To understand why, consider that, closely following the EU's

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in CAMBRIDGE HANDBOOK OF CORPORATE LAW, CORPORATE GOVERNANCE AND SUSTAINABILITY 596, 604-05 (Beate Sjåfjell & Christopher M. Bruner eds, 2019).

8 *See infra* note 109 and accompanying text.

9 US federal securities regulation defines materiality from the perspective of investors. *See Basic Inc. v. Levinson,* 485 U.S. 224, 231–32 (1988) (materiality is satisfied when there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available.'). Although EU law's use of double materiality recognizes the perspectives of non-investors in addition to those of investors, we regard investors as the primary users of sustainability assurances and, hence, unless it is otherwise clear from context, focus on them exclusively throughout.

10 *See* Andrew F. Tuch, *Multiple Gatekeepers*, 96 VA. L. REV. 1583, 1595–96 (2010) (contrasting the incentives of gatekeepers and corporate issuers "to build and preserve [] reputation[s] for diligence and honesty . . . [and] to certify disclosures accurately.").

11 *See* Enriques, Romano & Tuch, *supra* note 4, *passim*.

12 *See also* text accompanying *infra* note **Error! Bookmark not defined.** (contrasting assurance providers with other green gatekeepers).

13 *See* Enriques, Romano & Tuch, *supra* note 11, at 645–50.

14 Almost by definition, sophisticated investors are more likely to be able to accurately price traditional financial information than sustainability information.

regulatory approach on this matter,[15] a firm's sustainability claims can fall within three categories: (*i*) double materiality, (*ii*) financially material-only*; (iii)* impact-material-only.[16]

Double-materiality information is relevant both from a *financial* perspective to the disclosing firm and has a material *impact*, e.g., on the environment, biodiversity, climate change, or stakeholders other than investors. For disclosures that have double materiality, investors who rely on inaccurate sustainability assurances face at least some private costs, as the information may have financial consequences.

Alternatively, information may be financially material-only. That is, it may affect the bottom line of the firm, but impose no significant externalities on the environment or other stakeholders. Investors who rely on inaccurate assurances related to *financial materiality* may bear private costs, because the relevant company may be more exposed to sustainability risks than anticipated, giving them incentives to verify the accuracy of these assurances, thereby exerting discipline on assurance providers.

However, for disclosures that are impact-material but not financially material (hereinafter, "impact-material-only"), investors incur no private costs if assurances are inaccurate.[17] As a consequence, they have weak incentives, if any, to monitor the accuracy of such assurances.

Against this background, we explain below that, other things equal, the strength of assurance providers' reputational constraints is a function of (1) the verifiability by users of sustainability assurances; and (2) the significance of private costs for users relying on inaccurate certifications.

Our paper proceeds as follows. Part I introduces the regulation surrounding sustainability disclosures in the US and in Europe. Part II turns to the assurance of sustainability disclosures, with a focus on assurance providers. Recognizing that gatekeeper regulation may supplement primary liability as a control strategy, Part III considers both the regulatory constraints on the makers of sustainability claims as well as the reputational constraints on assurance providers, arguing that these constraints together may fail to induce providers to issue accurate assurances. Finally, Part IV considers the shape that regulatory intervention might take for sustainability providers.

I. Sustainability Disclosures

In this Part, we focus on the sustainability-reporting requirements facing US and European public companies, as well as the actual practices of these companies.

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[15] See Commission Delegated Regulation (EU) 2023/2772 of 31 July 2023 supplementing Directive 2013/34/EU of the European Parliament and of the Council as regards sustainability reporting standards OJ L 2023/2772, annex 1, (hereinafter, ESRS 1), para. 3.4 & 3.5 (defining financial and impact materiality). *See also* EUR. FIN. REPORTING ADVISORY GRP., FINAL REPORT: PROPOSALS FOR A RELEVANT AND DYNAMIC EU SUSTAINABILITY REPORTING STANDARD-SETTING 7–8 (2021) (describing double materiality); 34 ("[T]he double materiality approach [is] intended to address the so-called 'outside-in' perspective (risks and opportunities for the entity [or financial materiality]...) as well as the so-called 'inside-out' perspective (positive and negative impacts of the entity [or impact materiality]...).").

[16] We make no claim here as to whether, and how often, sustainability matters may be material under a single dimension. Rather, we adopt the EU regulator's assumption that there can be cases of both double-materiality and single-materiality information as a working assumption and proceed as if such non-overlapping cases do exist. See Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting, recital 29 [2022] OJ L 322 (hereinafter, CSRD) ("undertakings should consider each materiality perspective in its own right, and should disclose information that is material from both perspectives as well as information that is material from only one perspective").

[17] So long as they are unaware of the inaccuracy, investors do not even suffer the harm entailed by finding out that their "warm glow" (as to which, see *infra* note 113 and corresponding text) was unwarranted.

A. Definitional Ambiguity

The question of sustainability disclosures is fraught. In the United States, the issue is often associated with the "culture wars," with opponents and proponents typically divided along political lines. The Securities and Exchange Commission (SEC) has not been immune to the controversy. In 2024, after "the most anticipated, and contested, rulemaking in the history of the SEC,"[18] the SEC adopted ambitious final rules requiring US public companies and foreign private issuers to disclose climate-related risks and metrics in periodic reports and registration statements.[19] Although these rules have been stayed and may be rescinded by the SEC itself or struck down by federal courts,[20] it is not unreasonable to foresee that in a more accommodating regulatory environment the SEC will restore these rules or adopt similar ones,[21] as some states have.[22]

Controversy and uncertainty also surround the meaning of sustainability in the context of public company disclosures. In this setting, the term is often used as a synonym for corporate social responsibility (CSR) and ESG investing—that is, investing with an eye toward not only business outcomes but also environmental, social, and corporate governance conditions.[23] However, these terms themselves have never been precisely defined. As Amanda Rose notes, ESG is "used as shorthand for a dizzyingly broad array of … topics affecting businesses," including "climate change, human capital management, supply chain management, human rights, cybersecurity, diversity and inclusion, corporate tax policy, corporate political spending, executive compensation practices, and more."[24] These topics, too, are of uncertain scope, "unwieldy and difficult to define."[25]

Most basically, sustainability, ESG, and CSR can have two interpretations. First, they may refer to the third-party effects of a corporation's activities or, otherwise put, the effects of a corporation's activities

[18] Summary of Comment Letters for the SEC's Proposed Climate Risk Disclosure Rule, The FinReg Blog, https://sites.duke.edu/thefinregblog/2022/09/01/summary-of-comment-letters-for-the-secs-proposed-climate-risk-disclosure-rule/.

[19] *See* The Enhancement and Standardization of Climate-Related Disclosures for Investors, 89 Fed. Reg. 21668, 21668 (Mar. 28, 2024) (to be codified at 17 CFR pts. 210, 229, 230, 232, 239, 249).

[20] Under the Biden administration, the SEC stayed these climate rules pending judicial review of challenges to its legality. The Enhancement and Standardization of Climate-Related Disclosures for Investors; Delay of Effective Date, 89 Fed. Reg. 25804, 25805 (Apr. 12, 2024) (to be codified at 17 C.F.R. pts. 210, 229, 230, 232, 239, 249) (announcing that the effective date of the final climate rules would be "delayed pending the completion of judicial review in consolidated proceedings in the Eighth Circuit"). Rescission would require notice-and-comment rulemaking under the Administrative Procedure Act, Section 553, but this approach would be time- and resource-intensive and not prevent a future administration from adopting similar provisions. *See* Era Anagnosti et al., *SEC's Climate Rule Litigation Update: Is it Actually Over?*, DLA Piper Insight, Apr. 17, 2025, https://www.dlapiper.com/en/insights/publications/2025/04/sec-climate-rule-litigation-update-is-it-actually-over.

[21] Even if the climate rules were rescinded, a future administration could adopt similar provisions. *See* Anagnosti et al., *supra* note 20.

[22] *See, e.g.,* CAL. HEALTH & SAFETY CODE § 38533 (Deering, LEXIS through 2024 Reg. Sess.); CAL. HEALTH & SAFETY CODE § 38532 (Deering, LEXIS through 2024 Reg. Sess.).

[23] *See, e.g.,* Business and Financial Disclosure Required by Regulation S-K, Securities Act Release No. 10,064, Exchange Act Release No. 77,599, 81 Fed. Reg. 23,916, 23,970 (proposed Apr. 22, 2016) ("Sustainability disclosure encompasses a range of topics … . These topics often are characterized broadly as environmental, social, or governance ("ESG") concerns.").

[24] Amanda M. Rose, *A Response to Calls for SEC-Mandated ESG Disclosure*, 98 WASH. U. L. REV. 1821, 1822 (2021). *See* also Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and Social Conscience*, 72 STAN. L. REV. 381, 387 (2020) ("ESG investing resists precise definition").

[25] *See, e.g.*, George Georgiev, *Human Capital Management*, 95 TULANE L. REV. 639, 676–77 (2021) (the concept of "human capital management" is "unwieldy and difficult to define").

on stakeholders other than its shareholders. Second, they may refer to the impact that sustainability factors—such as climate risk—may have on a corporation and, hence, its shareholders.

What is nevertheless clear about sustainability disclosures is that not all ESG metrics are material for all corporations and, given definitional and measurement problems, some ESG indicators will not capture the true sustainability of a firm. It is also clear that many investors increasingly have been demanding these disclosures and incorporating them into their investment decisions.[26] In addition, despite definitional uncertainties, claims of sustainability include hard data, as for greenhouse gas-emission metrics—data inviting scientific measurement and third-party assurance as to accuracy. Public corporations have increasingly provided these disclosures, in some cases in order to meet legal requirements but more often voluntarily.

B. Mandatory Sustainability Disclosures

US and EU law mandate sustainability disclosures, although these mandates take different approaches. Under US federal securities laws, public companies may need to disclose sustainability information incidentally, in order to comply with broader disclosure requirements or to prevent their other statements from being misleading.[27] In contrast, EU law directly mandates itemized sustainability disclosures.

1. US Sustainability Disclosure Requirements

SEC regulations include broad disclosure requirements. Most notable is Regulation S-K, which outlines non-financial information that public companies must disclose in SEC filings.[28] The regulation mandates that registrants describe their businesses,[29] disclose the material facts that make an investment in their securities "speculative or risky,"[30] and report on "material events and uncertainties"—including "known trends or any known demands, commitments, events or uncertainties"—that may cause fluctuations in future financial results.[31] While these requirements do not explicitly prescribe the disclosure of sustainability information, satisfying them may necessitate

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[26] *See e.g.,* Government Accountability Office, Public Companies; Disclosure of Environmental, Social, and Governance Factors and Options to Enhance Them, GAO-20-530 (2020) at 1 ("Investors are increasingly asking public companies to disclose information on [ESG] factors to help them understand risks to the company's financial performance or other issues"); Williams & Nagy, *supra* note 1, at 1474. *See also* Cynthia A. Williams & Jill E. Fisch, *Request for Rulemaking on Environmental, Social, and Governance (ESG) Disclosure*, U.S. SEC. & EXCH. COMM'N 16 (Oct. 1, 2018), http://www.sec.gov/rules/petitions/2018/petn4-730.pdf (investor petition seeking SEC rulemaking to mandate enhanced ESG disclosures

[27] Business and Financial Disclosure Required by Regulation S-K, Securities Act Release No. 10,064, Exchange Act Release No. 77,599, 81 Fed. Reg. 23,916, (proposed Apr. 22, 2016) ("[I]n specific cases some information of this type [regarding corporate social practices] might be necessary in order to make the statements in a filing not misleading or otherwise complete."). *See also* Basic Inc. v. Levinson, 485 U.S. 224, 239 n.17 (1988) ("Silence, absent a duty to disclose, is not misleading."); Gallagher v. Abbott Labs., 269 F.3d 806, 808 (7th Cir. 2001) (Easterbrook J.) ("firms are entitled to keep silent (about good news as well as bad news) unless positive law creates a duty to disclose."); Matrixx Initiatives, Inc. v Siracusano, 563 U.S. 27, 44 (2011) ("[Anti-fraud provisions] do not create an affirmative duty to disclose any and all material information. Disclosure is required under these provisions only when necessary 'to make … statements made, in the light of the circumstances under which they were made, not misleading.").

[28] Regulation S-K, 17 C.F.R. Pt. 229.

[29] Regulation S-K, item 101 (description of business).

[30] Regulation S-K, item 101 (risk factors).

[31] Regulation S-K, item 303 (management's discussion and analysis of financial condition and results of operations). This disclosure requirement has been described as a "natural home for ESG and climate disclosure." Williams & Nagy, *supra* note 1, at 1474 (2021).

that corporations disclose sustainability information. For example, if sustainability information indicates a risk to the company's business, or if a known climate trend may cause fluctuations in its financial results, then the company is required to disclose these issues in its filings.

In addition to these broad mandates, the SEC had adopted narrowly tailored rules requiring registrants to disclose information explicitly tied to sustainability topics. Most recently, the SEC approved climate rules, requiring that public companies make extensive climate-related disclosures, including of GHG emissions and climate-related financial metrics, in their periodic filings and registration statements.[32] As explained above, although the fate of these rules remains uncertain, they may still shape future rulemaking.[33]

Other sustainability-focused disclosure requirements relate to human capital management, board composition, executive compensation, and audit-committee structure.[34] There are also required disclosures concerning "conflict minerals"[35]—intended to address human rights problems associated with the sourcing of minerals[36]—and extractive-industry payment provisions,[37] which are intended to protect citizens of resource-rich countries.[38]

SEC disclosure requirements, both broad and narrow, are generally subject to a materiality threshold, which is satisfied by information that a "reasonable investor" would be substantially likely to "consider … important in making an investment decision in the context of the total mix of information available."[39] In addition, federal securities law requires the disclosure of "further material information … as may be necessary to make the required statements, in the light of the circumstances under which they are made[,] not misleading."[40] This qualification recognizes that disclosed information, though truthful, may itself be misleading in the absence of other relevant material information, and so this other material information must also be disclosed.

In sum, the US disclosure regime is a mixture of broadly worded and specifically tailored requirements, which are usually subject to a materiality qualification. Sustainability disclosures may be necessary to satisfy the broad requirements in some cases, even as these requirements do not specifically mention sustainability. Requirements explicitly mentioning sustainability matters are few and specific.

2. EU Sustainability Disclosure Requirements

In contrast to US sustainability requirements, EU sustainability requirements have become increasingly extensive and prescriptive.[41] This process started with the Non-Financial Reporting

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32 *See* The Enhancement and Standardization of Climate-Related Disclosures for Investors, 89 Fed. Reg. 21668, 21668 (Mar. 28, 2024) (to be codified at 17 CFR pts. 210, 229, 230, 232, 239, 249).
33 *See supra* notes 20 - 22 and accompanying text.
34 Modernization of Regulation S-K Items 101, 103, and 105, Securities Act Release No. 33-10825, Exchange Act Release No. 34-89670, 85 Fed. 63,726, 63,739 (Oct. 8, 2020) (to be codified at 17 C.F.R pts. 229, 239, and 240); U.S. GOV'T ACCOUNTABILITY OFF., GAO-20-530, PUBLIC COMPANIES: DISCLOSURE OF ENVIRONMENTAL, SOCIAL, AND GOVERNANCE FACTORS AND OPTIONS TO ENHANCE THEM (2020).
35 17 C.F.R. § 240.13p-1 (2024).
36 *See* Jeff Schwartz, *The Conflict Minerals Experiment*, 6 HARV. BUS. L. REV. 129 (2015).
37 17 C.F.R. § 240.13q-1 (2024).
38 Williams & Nagy, *supra* note 1, at 1463–65 (2021).
39 Basic Inc. v. Levinson, 485 U.S. 224, 231032 (1988) (quoting TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976)).
40 17 C.F.R. §§ 230.408(a), 240.12b-20 (2024).
41 For detailed discussion of this process and resulting initiatives, *see* Matthew T. Bodie, *Shareholders All the Way Down: EU Corporate Sustainability Reforms and the Structure of Corporate Governance* 52 GEORGIA J. INT'L & COMP. L. 559, 560–69 (2024).

Directive (hereinafter, "NFRD") in 2014,[42] which imposed the obligation to publish non-financial statements[43] on large undertakings.[44] Such statements were required to contain information relating to at least environmental matters, social and employee-related matters, respect for human rights, and anti-corruption and bribery matters.[45] Various disclosures were required: for instance, covered firms were obligated to describe and assess relevant policies and performance indicators[46] and to provide information on due diligence processes and business models.[47] In 2017 and 2019, the European Commission (EC) issued extensive non-binding guidance for complying with the NFRD.[48]

Disclosure requirements were substantially expanded by the 2019 Sustainable Finance Disclosure Regulation (hereinafter, "SFDR")[49] and the 2020 Taxonomy Regulation,[50] both of which sought to address greenwashing and mobilize capital for sustainable investments.[51] The SFDR introduced several investor-oriented disclosure obligations applied to financial market participants and financial advisers.[52] These include website and pre-contractual disclosures, at the entity and financial product levels, concerning sustainability risk policies, consideration of adverse sustainability impacts, integration of sustainability risks and related remuneration policies, a product's environmental or social characteristics, and investments claiming to be sustainable.[53] Periodic reports for financial products must also include certain sustainability-related information.[54] The Taxonomy Regulation supplemented disclosure obligations in the NFRD,[55] requiring that any undertaking obliged to publish a non-financial statement also publish an explanation of how and to what extent the undertaking's activities are associated with environmentally sustainable economic activities.[56] The Regulation also laid down a framework for defining such activities, with the EC subsequently issuing a 349-page

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42 Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups [2014] OJ L 330/1. For a detailed discussion of its contents, *see* Barry Connolly & John Quinn, *The Non-Financial Information Directive: An Assessment of Its Impact on Corporate Social Responsibility* 14 EUR. COMP. L. 15, 15–17 (2017).

43 These amendments supplemented generic requirements in relation to "non-financial key performance indicators" found in Accounting Directive art 19(1), para 3.

44 More precisely, the NFRD applied to listed companies, banks, insurance undertakings, and other public-interest entities—as defined by Member States—with more than 500 employees. Directive 2014/95/EU of the European Parliament and of the Council, art. 1(1), 2014 O.J. (L 330) 1 (amending Directive 2013/34/EU of the European Parliament and of the Council, art. 19a(1), 2013 O.J. (L 182) 19).

45 NFRD art 1(1), inserting art 19a(1), and art 1(2), inserting art 29a(1).

46 ibid art 1(1), inserting art 19a(1)(b)–(e), and art 1(2), inserting art 29a(1)(b)–(e).

47 ibid art 1(1), inserting art 19a(1)(a)–(b), and art 1(2), inserting art 29a(1)(a)–(b).

48 Communication from the Commission — Guidelines on non-financial reporting (methodology for reporting non-financial information) [2017] OJ C 215/1.; Communication from the Commission — Guidelines on non-financial reporting: Supplement on reporting climate-related information [2019] OJ C 209/1.

49 Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector [2019] OJ L 317/1.

50 Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (Text with EEA relevance) [2020] OJ L198/13.

51 SFDR recital 8; Taxonomy Regulation recitals 11 and 17; Bodie (n 1) 564.

52 For a detailed description of the SFDR, *see* Danny Busch, *EU Sustainable Finance Disclosure Regulation*, 18 CAP. MKTS. L.J. 303 (2023).

53 SFDR arts 3–10.

54 ibid art 11.

55 For detailed discussion, *see* Christos V. Gortsos, *The Taxonomy Regulation and Its Implementation*, *in* SUSTAINABLE FINANCE IN EUROPE 505 (Danny Busch, Guido Ferrarini & Seraina Grünewald eds, 2d ed, 2024).

56 Taxonomy Regulation, art 8.

delegated regulation specifying the technical criteria for identifying and disclosing environmentally sustainable economic activities.[57]

The NFRD provisions have since been superseded by the Corporate Sustainability Reporting Directive (CSRD),[58] which preserves but expands and reframes these earlier requirements. The CSRD, in addition to applying to a broader range of undertakings,[59] replaces the concept of non-financial information with information about "sustainability factors."[60] These include environmental, social, human rights, and governance matters, encompassing "sustainability factors" as defined in the SFDR.[61] The CSRD requires disclosure for each sustainability factor, including with respect to due diligence processes, the outcomes of sustainability policies, risks and risk management, and key performance indicators relevant to the business.[62]

Importantly, disclosures under these directives are subject to the double materiality test: undertakings must disclose not only sustainability matters that are material from a *financial* perspective to the undertaking (financial materiality) but also those that have a material impact on people, the environment, and other third parties (impact materiality), where materiality is defined in terms of severity of actual impacts and severity and likelihood of potential impacts.[63] In its insistence on both notions of materiality, the EU goes beyond SEC mandates, which focus on materiality from the perspective of investors—that is, financial materiality.[64] In-scope undertakings[65] are required to comply with the European Sustainability Reporting Standards (ESRS).[66] The 284-page ESRS lay down detailed requirements for disclosing impacts on, and dependencies with respect to, *inter alia*, climate, air, land, water, and biodiversity, as well as working conditions, equality, non-discrimination, human rights (including forced and child labor in value chains), and governance factors such as the roles of administrative, management, and supervisory bodies.

C. Comparability and Accuracy of Sustainability Disclosures

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57 Commission Delegated Regulation (EU) 2021/2139 of 4 June 2021 [2021] OJ L 442/1.

58 CSRD, *supra* note **Error! Bookmark not defined.**For a detailed discussion of the CSRD, and its relationship with the earlier NFRD, *see* Tania Pantazi, *The Introduction of Mandatory Corporate Sustainability Reporting in the EU and the Question of Enforcement*, 25 EUR. BUS. ORG. L. REV. 509, 512–19 (2024).

59 The CSRD applies to (i) large EU undertakings (whether listed or not), (ii) small and medium-sized EU undertakings with securities listed on an EU-regulated market (except micro-undertakings), and (iii) non-EU undertakings generating over EUR 150 million in net turnover in the EU and having a large EU subsidiary or a significant EU branch. Directive 2013/34/EU of the European Parliament and of the Council, arts. 19a(1), 29a(1), 40a(1), 2013 O.J. (L 182) 19, as amended by CSRD, art. 1(3). As discussed below, the Commission's proposed Omnibus I package would narrow its application.

60 CSRD recital 8.

61 ibid art 1(2)(b), inserting art 2(17) in the Accounting Directive.

62 ibid art 1(4), replacing art 19a(2) of the Accounting Directive.

63 Commission Delegated Regulation (EU) 2023/2772, *supra* note **Error! Bookmark not defined.**, at para. 3.4 (defining impact materiality). *See also* EUR. FIN. REPORTING ADVISORY GRP., FINAL REPORT: PROPOSALS FOR A RELEVANT AND DYNAMIC EU SUSTAINABILITY REPORTING STANDARD-SETTING 7-8 (2021) (describing double materiality); 34 ("[T]he double materiality approach [is] intended to address the so-called 'outside-in' perspective (risks and opportunities for the entity [or financial materiality]...) as well as the so-called 'inside-out' perspective (positive and negative impacts of the entity [or impact materiality]...).").

64 *See supra* note 38 and accompanying text. *See also* Roza Nurgozhayeva & Dan W. Puchniak, *Corporate Purpose Beyond Borders: A Key to Saving Our Planet or Colonialism Repackaged?*, 57 VAND. J. TRANS. L. 1339, 1354-57 (2024).

65 *See supra* note 59.

66 Commission Delegated Regulation (EU) 2023/2772 of 31 July 2023 supplementing Directive 2013/34/EU of the European Parliament and of the Council as regards sustainability reporting standards OJ L 2023/2772.

In light of the regulatory frameworks we have described in section I.B. investors in the US and the EU are likely to see different sustainability information. But even within each of the two systems, disclosure documents will often be hard to compare. In the US case, comparability is a challenge[67] whether companies are making required disclosures or voluntary ones, such as those to be found in "standalone sustainability reports, instead of in SEC filings."[68] And while it is too early to gauge the impact of the more recent EU disclosure regulation, evidence relating to the NFRD shows that, although the quality of non-financial disclosures has improved across the EU, there remains inconsistency across firms. Further, EU firms' disclosures may lack specificity and rely on selective metrics.[69]

Heterogeneity of sustainability information is of particular concern in the US, which has no equivalent of the ESRS. Unlike financial statement disclosures, which conform to the Generally Accepted Accounting Principles (GAAP), sustainability disclosures are not standardized. Presentation is therefore haphazard, making comparison across disclosures challenging. In Europe, the ESRS are intended to address this problem, as are the International Accounting Standard Board's Sustainability Standards.[70] As we discuss later, sustainability disclosures are also unevenly subjected to assurance, which itself varies according to the assurance standards applied, further exacerbating the comparison problem.

If sustainability disclosures are inconsistent, they may also be inaccurate. Even in the US, where disclosure errors are more likely to attract lawsuits than they are in Europe, litigation concerning false sustainability disclosures has been sparse. Among the reasons are the difficulty of assessing the materiality of sustainability information and the likelihood that such information will be regarded as puffery or protected as the contents of a forward-looking statement.[71]

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[67] *See* U.S. Chamber of Commerce Foundation and the Chamber's Center for Capital Markets Competitiveness, Corporate Sustainability Reporting: Past, Present, and Future (November 2018) at 3 (finding that the "vast differences" among the multiple voluntary disclosure frameworks available to U.S. issuers make comparisons across disclosures difficult); GOVERNMENT ACCOUNTABILITY OFFICE, PUBLIC COMPANIES; DISCLOSURE OF ENVIRONMENTAL, SOCIAL, AND GOVERNANCE FACTORS AND OPTIONS TO ENHANCE THEM, GAO-20-530 (2020) at 32-33 (identifying inconsistencies and lack of specificity in disclosure guidance concerning a selection of ESG topics, hampering comparability); The Center for Audit Quality, S&P 500 ESG Reporting and Assurance Analysis, June 2024, https://www.thecaq.org/sp-500-and-esg-reporting (providing evidence of cherry picking).

[68] GOVERNMENT ACCOUNTABILITY OFFICE, PUBLIC COMPANIES; DISCLOSURE OF ENVIRONMENTAL, SOCIAL, AND GOVERNANCE FACTORS AND OPTIONS TO ENHANCE THEM, GAO-20-530 (2020) at 23 ("Most companies tended to include more extensive ESG disclosures in their sustainability reports than in their [SEC-required] regulatory filings."); Jill E. Fisch, *Making Sustainability Disclosure Sustainable*, 107 GEO. L.J. 923, 944 (2019) ("Most sustainability information is disclosed not in issuer financial or securities filings, but in standalone sustainability reports.").

[69] *See* Ries Breijer & René P. Orij, *The Comparability of Non-Financial Information: An Exploration of the Impact of the Non-Financial Reporting Directive (NFRD, 2014/95/EU)*, 19 ACCT. IN EUR., 332 (2022).

[70] Int'l Fin. Reporting Standards Found., *IFRS S1: General Requirements for Disclosure of Sustainability-related Financial Information* (2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards-navigator/ifrs-s1-general-requirements.html/content/dam/ifrs/publications/html-standards-issb/english/2023/issued/issbs1/; id., *IFRS S2: Climate-related Disclosures* (2023), https://www.ifrs.org/issued-standards/ifrs-sustainability-standards-navigator/ifrs-s2-climate-related-disclosures.html/content/dam/ifrs/publications/html-standards-issb/english/2023/issued/issbs2/.

[71] *See* James J. Park, *ESG Securities Fraud*, 58 WAKE FOREST L. REV. 1149, 1165–79 (2023) (examining reasons why courts have often dismissed ESG securities fraud claims under Rule 10b-5); Enriques, Romano & Tuch, *supra* note 4, at 671-74 (examining impediments to liability for sustainability claims under federal securities law); Emily Strauss, *Climate Change and Shareholder Lawsuits*, 20 N.Y.U. J. L. & BUS. 95, 118 (2023) (examining impediments to climate-related lawsuits, including proof of shareholder loss).

II. Assurance of Sustainability Disclosures

In this Part, we turn to third-party assurance of sustainability disclosures and discuss the distinction between mandatory and voluntary assurance.

A. Assurance Providers and Standards

While much scholarly attention has focused on sustainability disclosures, far less has been paid to sustainability assurance. Nevertheless, assurance is a familiar topic in legal scholarship because the auditing of financial statements is a form thereof. Strictly speaking, assurance is a form of third-party verification, but verification need not result in assurance. While assurance services, including public companies' audits, are performed under professional standards intended to ensure the accuracy of information, verification can occur without regard to professional standards.[72]

Although parallels exist between sustainability assurance and financial auditing, the sustainability assurance industry is at a nascent stage of development, while financial audit services have been around since the 1800s.[73] Thomas Bourveau and co-authors liken the current state of sustainability assurance to that of financial auditing a century ago, observing that sustainability assurance practices are "heterogeneous and in flux" amid ongoing efforts to standardize them.[74] Evidence from S&P 500 firms shows that sustainability assurance practices vary widely, including as to the proportion of sustainability information assured, the assurance standards used, and the level of assurance provided—a contrast to the homogeneous practices of financial statement auditing.[75]

The variation in practices may stem from the absence of "generally accepted" assurance standards—uniform procedures that assurance providers are meant to follow before certifying sustainability disclosures. A wide range of standards may be applied, depending on the assurer and the nature of the claims.[76] Assurance is typically conducted at either a "limited" or "reasonable" level, with limited assurance being more common.[77] In the US, common standards include those issued by the American Institute of Certified Public Accountants (hereinafter, "AICPA"), the International Standardization Organization (ISO), AccountAbility, and the International Auditing and Assurance Standards Board.[78] Some assurance providers rely on proprietary standards.[79] This heterogeneity further hinders users' ability to compare sustainability disclosures, compounding the existing challenges posed by the lack

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[72] *See* The Enhancement and Standardization of Climate-Related Disclosures for Investors, 89 Fed. Reg. 21,668, 21,846 (Mar. 28, 2024) ("[A]ssurance services are services performed in accordance with professional standards that are designed to provide assurance, while in many cases verification services are not designed to provide assurance.").

[73] The American Institute of Certified Public Accountants (*see infra* text following note 77) was founded in 1887. *See, e.g.,* James D. Edwards & Paul J. Miranti Jr., *The AICPA: A Professional Institution in a Dynamic Society*, 163 J. ACCT. no. 5, at 22, 22 (1987).

[74] *See* Thomas Bourveau et al, *Public Company Auditing Around the Securities Exchange Act: Historical Lessons for ESG Assurance*, 100 ACCT. REV. 107 (2025).

[75] Gipper, Ross & Shi, *supra* note 7, at 3 (studying sustainability disclosure practices from 2010 to 2020).

[76] *See* Chiu, *supra* note 7, at 388-91.

[77] The Center for Audit Quality, S&P 500 ESG Reporting and Assurance Analysis, June 2024, https://www.thecaq.org/sp-500-and-esg-reporting (reporting that 79 out of 90 assurances by public company auditors of sustainability disclosures were performed at the limited assurance level).

[78] *See* Gipper, Ross & Shi, *supra* note 7, at Table 1, Panel D (reporting assurance standards by assurer type); THE CENTER FOR AUDIT QUALITY, S&P 500 SUSTAINABILITY REPORTING AND ASSURANCE ANALYSIS, June 2025, https://www.thecaq.org/sp-500-and-esg-reporting (identifying assurance standards for public accounting firms and non-public accounting firms).

[79] *See* Gipper, Ross & Shi, *supra* note 7, at Figure 3 (reporting data on assurer type).

of a standardized reporting system.[80] In contrast, financial audits follow clear norms: they are conducted under generally accepted audit standards and certify disclosures prepared in accordance with generally accepted accounting principles.[81]

But leaving aside standardization issues, the very nature of assurance providers differs from that of their counterparts in financial accounting. While financial statement audits are conducted almost exclusively by public accounting firms—primarily the Big Four—sustainability assurance is more diverse. In the US, engineering, consulting, and other non-public accounting firms perform roughly 80 percent of sustainability assurance for S&P 500 companies, a share that has increased in recent years.[82] As Brandon Gipper and coauthors note, these include "engineering firms with roots in the maritime industry (e.g., Bureau Veritas) and specialized engineering or consulting firms (e.g., Apex, LRQA)."[83] Internationally, public accounting firms dominate sustainability assurance, though non-accounting firms still conduct roughly 40% of engagements.[84]

Given these comparisons, it may come as no surprise that sustainability assurance has yielded less reliable assurance than financial auditing.[85] Yet recent initial evidence finds that it is positively associated with more specific and higher-quality sustainability disclosures.[86]

B. Mandatory and Voluntary Sustainability Assurance

There are several justifications for sustainability assurance mandates. Assurance may improve the quality of sustainability disclosures.[87] Furthermore, to the extent that investors value sustainability information, improving its quality may lead to more accurate pricing of sustainability-related risks such as climate risks.[88] Finally, a mandate may improve the comparability of sustainability disclosures. Nevertheless, only the EU has mandated sustainability assurance.

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[80] *See supra* Pt I.C.

[81] In the US, for example, public company audits were long performed in accordance with generally accepted auditing standards, which were set by AICPA. In the wake of the Enron and WorldCom scandals, the Public Company Accounting Oversight Board (PCAOB) took over the AICPA's role, under SEC supervision. For a detailed discussion of the institutional and legal structure of accounting, see HOWELL E. JACKSON, LOUIS KAPLOW, STEVEN M. SHAVELL, W. KIP VISCUSI & DAVID COPE, ANALYTICAL METHODS FOR LAWYERS 124-26 (2017, 3d ed.).

[82] *See* Gipper, Ross & Shi, *supra* note 7, at Table 1, Panel D.

[83] *See* Gipper, Ross & Shi, *supra* note 7.

[84] *See* https://www.aicpa-cima.com/news/article/sustainability-reporting-and-assurance-practices-of-largest-global-companies (reporting results of a study, including that "[a]ccountancy firms (as opposed to consultants or other service providers) handled 58% of the assurance engagements related to sustainability in 2022, a percentage point better than the previous year" while "[s]ome markets, notably the United States, fall well below 50%.").

[85] Accounting studies reveal that sustainability assurance is substantially less reliable than traditional gatekeeping. Financial auditing leads to the discovery of accounting errors before reporting, suggesting that auditing improves reporting quality. Sustainability assurance reports contain a comparatively high level of errors, suggesting that "mistakes are more likely to be made and less likely to be discovered before reporting." Giovanna Michelon, Dennis M. Patten & Andrea M. Romi, *Creating Legitimacy for Sustainability Assurance Practices: Evidence from Sustainability Restatements,* 28 EUR. ACCT. REV. 395, 395 (2019).

[86] *See* Gipper, Ross & Shi, *supra* note 7, at Figure 10 (reporting regression analyses of the association between ESG assurance and both ESG disclosure specificity (measured by Refinitiv) and ESG ratings (measured by Refinitiv and S&P). Evidence suggests that research analysts regard assurances of corporate social responsibility information as more credible than information without such assurances. *See* Ryan J. Casey et al., *Understanding and Contributing to the Enigma of Corporate Social Responsibility (CSR) Assurance in the United States*, 34 AUDITING: J. PRAC. & THEORY 97 (2015).

[87] *See supra* note 86 and associated text.

[88] Casey et al., *supra* note 88 (finding that CSR assurance is associated with lower cost-of-equity capital along with lower forecast errors and dispersion by research analysts).

1. US

Under US law, while public companies must have their financial statements audited by public accounting firms, nothing requires that they seek assurance of their sustainability disclosures. The SEC climate rules would have inaugurated a different regime, as it required accelerated filers and large accelerated filers—two categories of registrants enjoined to disclose material scope 1 and/or scope 2 GHG emissions—to file attestation reports prepared by attestation providers covering these items.[89] The rule contemplated "limited" and "reasonable" assurance, depending on the category of filer.[90]

Despite its voluntary nature, sustainability assurance has been common among US public companies in recent years. A study by the Center for Audit Quality found that 99 percent of S&P 500 companies reported sustainability information in 2023.[91] Of these, 73 percent obtained some form of assurance, an increase from previous years,[92] with 24 percent of these companies obtaining assurance from public accounting firms, a modest increase from 2021.[93] The scope of assurance obtained, while widening, remains narrow, meaning that companies obtained assurance of some sustainability disclosures but not others.[94] The study found that, among companies that obtained assurance from public accounting firms, the scope of assurance was restricted to "select metrics related to GHG emissions."[95] Like similar studies,[96] this one does not report whether issuers obtain assurance for sustainability disclosures in registration statements, a setting in which issuers face strict liability for disclosure errors.[97]

2. EU

Under the CSRD, which innovated on the NFRD in this respect, all mandatory sustainability reporting by EU-based undertakings[98] must be accompanied by an assurance opinion provided by a statutory auditor, audit firm, or, if a member state permits, independent assurance services provider.[99] Assurance opinions for EU undertakings are subject to detailed standards and assurance providers are subject to

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89 Reg. S-K, Items 1505, 1506. As to the SEC climate rules, see *supra* notes 32-**Error! Bookmark not defined.** and accompanying text.

90 For more detail, *see* Andrew F. Tuch, *Climate Disclosure and the Transformation of Gatekeeping*, BERKELEY BUS. L.J. (2025) (forthcoming)

91 THE CENTER FOR AUDIT QUALITY, *supra* note 78.

92 *Id.* ("Overall, we observed an upward trend in the number of companies that obtained assurance or verification."). For instance, the corresponding figure in 2022 was 70 percent. *Id.*

93 *Id.* Of the S&P 500 companies using public accounting firms for sustainability assurance, 94 percent used the auditor of their financial statements. *Id.*

94 *Id.* Of the 283 S&P 500 companies that obtained sustainability assurance from non-public accounting firms in 2023, 214 (or 75 percent) did so for GHG metrics only or GHG metrics plus between one and three additional sustainability metrics. *Id.*

95 Of the 87 S&P 500 companies that obtained sustainability assurance from public accounting firms in 2023, 66 (or 76 percent) did so for GHG metrics only or GHG metrics plus between one and three additional sustainability metrics. *Id.*

96 *See also* Gipper, Ross & Shi, *supra* note 7 (reporting data from "ESG reports," without identifying whether these reports are located in registration statements or not).

97 If they were identified as experts, assurance providers would also face strict liability for disclosure errors (for material they "expertised"), although they would benefit from due diligence defenses. *See* Securities Act § 11(b)(3)(A), 15 U.S.C. § 77k(b)(3)(A) (2024).

98 Third-country undertakings covered by the CSRD must also provide an assurance opinion but detailed standards on assurance opinions and conduct regulations are only mandated for assurance providers servicing EU-based undertakings.

99 Independent assurance services providers must comply with regulatory requirements equivalent to those governing auditors under the Audit Directive. This includes arrangements relating to a several matters, such as education and training, continuing education, quality assurance, professional ethics, independence, objectivity, confidentiality and professional secrecy, and investigations and sanctions. Accounting Directive art 34. As amended by the NFRD, the Accounting Directive only required the auditor to certify the presence of non-financial information in the management report (art 19a, para 5).

various conduct regulations. *Inter alia*, the Audit Directive provides that member states must establish systems of quality assurance for all statutory auditors and audit firms.[100] These provisions were amended to ensure that sustainability reporting assurances services are subject to review, including by persons who have obtained appropriate professional education and relevant experience in sustainability reporting assurance.

The assurance opinion may be based on a limited assurance engagement,[101] but the CSRD contemplates shifting to a more demanding requirement of reasonable assurance in the future. Reasonable assurance would then substitute for limited assurance from a date determined by the Commission.[102] Yet, the Commission's Omnibus I package, a legislative proposal that, as we write, is progressing through the European Parliament, would remove the possibility of imposing a reasonable assurance requirement.[103] Under the CSRD, the EC was supposed to lay down limited assurance standards by 1 October 2026, but the Omnibus I package also proposes eliminating this time limit.[104] Assurance must be based on national assurance standards, procedures, or requirements until the EC makes standards covering these matters.[105]

III. Accurate Certifications: The role of Reputation and Regulation

In this Part, we consider the reputational constraints on assurance providers, comparing them to those imposed on traditional gatekeepers and identifying the conditions under which they are likely to issue accurate certifications, as well as conditions in which inaccuracy may prevail. We also consider the potential of existing regulation to deter public companies or EU undertakings from making false sustainability disclosures.

A. Factors Weakening Reputational Sanctions

One fundamental question is whether reputational incentives are sufficient to ensure that assurance providers accurately certify sustainability claims. An assurance provider is a green gatekeeper: a third party that certifies claims about the environmental or sustainability-related attributes of products or firms, thereby reducing the information asymmetry between makers of sustainability claims and those claims recipients.[106] Like other gatekeepers, green gatekeepers are informational intermediaries that "rent" or "pledge" their reputations to their clients, effectively vouching for the accuracy of clients' claims.[107] As we explain elsewhere, green gatekeepers may perform two functions: first, setting standards—that is, specifying the requirements for their verifications—and second, verifying compliance with those standards, thereby certifying the accuracy of an issuer's statements.[108]

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[100] ibid art 29.
[101] Accounting Directive art 34(1)(aa).
[102] Accounting Directive art 26a(3), para 2.
[103] European Commission, 'Omnibus I – Second Directive' (n 6) 4, art 1.
[104] European Commission, 'Omnibus I – Second Directive' (n 6) 14, art 1. See also Directive (EU) 2025/794 of the European Parliament and of the Council of 14 April 2025 amending Directives (EU) 2022/2464 and (EU) 2024/1760 as regards the dates from which Member States are to apply certain corporate sustainability reporting and due diligence requirements, OJ L, 2025/794, Apr. 16, 2025, art 1 (postponing the sustainability reporting requirements by two years).
[105] Audit Directive art 26a(2).
[106] Enriques, Romano & Tuch, *supra* note 4, at 612.
[107] *See supra* notes 5-6.
[108] Enriques, Romano & Tuch, *supra* note 4, at 612.

In principle, gatekeepers' certifications hold value only insofar as market participants perceive them as reliable.[109] In turn, this gives gatekeepers incentives to build reputations for issuing accurate certifications. Yet there are several reasons why reputation is probably less constraining for assurance providers than for traditional financial gatekeepers.

First, as a result of "motivated reasoning" users of sustainability assurances have psychological reasons to take certifications at face value. Motivated reasoning refers to people's tendency to acquire and process information in ways that support their preferred conclusions.[110] True, this does not mean that any piece of information can justify any conclusion: as Kunda notes, "people motivated to arrive at a particular conclusion [do] attempt to be rational and to construct a justification of their desired conclusion that would persuade a dispassionate observer. They draw the desired conclusion only if they can muster up the evidence necessary to support it."[111] But while the wiggle room on which motivated reasoning relies on has limits, sustainability assurances may magnify it.[112]

Relatedly, some of the investors who invest in corporations that make sustainability claims may experience what behavioral scientists call a "warm glow." That refers to the utility derived from contributing to a public good, even when the actual benefits are questionable.[113] Indeed, evidence suggests that investors, like consumers, are largely indifferent to the actual environmental benefits generated by a financial instrument or a product. Instead, their willingness to pay is closely linked to the expressive value of the sustainability claim, which refers to the utility derived from expressing one's identity through investor or consumer choices.[114]

These factors suggest that users of sustainability assurances might derive a benefit by blindly trusting inflated assurances, or at least that they have limited incentives to investigate the veracity of such assurances.[115] As a result, users are unlikely to invest resources in checking the accuracy of assurances related to sustainability claims or in punishing assurance providers who inflate such assurances.[116]

Second, reputation may provide insufficient incentives because sustainability claims are very hard to verify and therefore to disprove. For instance, the criteria to evaluate the credibility of net-zero transition plans are extremely complex, as such plans are based on discretionary estimates and even,

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[109] Stephen Choi, *Market Lessons for Gatekeepers,* 92 NW. U. L. REV. 916, 961 (1998) (noting that the value of gatekeeper certifications rests on perceptions among purchasers of their accuracy); Claire A. Hill, *Regulating the Rating Agencies,* 82 WASH. U. L.Q. 43, 50 (2004) ("If markets think a firm can get a high rating just by paying for it, ratings won't be valued.").
[110] *See* Nicholas Epley & Thomas Gilovich, *The Mechanics of Motivated Reasoning,* 30 J. ECON. PERSPS. 133, 133 (2016) ("People generally *reason* their way to conclusions they favor, with their preferences influencing the way evidence is gathered, arguments are processed, and memories of past experience are recalled.").
[111] Ziva Kunda, *The Case for Motivated Reasoning,* 108 PSYCH. BULL. 480, 482-83 (1990).
[112] *See* Francesca Gino et al., *Motivated Bayesians: Feeling Moral While Acting Egoistically,* 30 J. ECON. PERSPS. 189, 189-90 (2016) ("people who appear to exhibit a preference for being moral may in fact be placing a value on feeling moral, often accomplishing this goal by manipulating the manner in which they process information to justify taking egotistic actions while maintaining this feeling of morality.").
[113] *See* Heidi Crumpler & Philip J. Grossman, *An Experimental Test of Warm Glow Giving,* 92 J. PUB. ECON. 1011, 1011 (2008).
[114] *See* Robert Sugden, *Public Goods and Contingent Valuation*, *in* VALUING ENVIRONMENTAL PREFERENCES: THEORY AND PRACTICE OF THE CONTINGENT VALUATION METHOD IN THE US, EU AND DEVELOPING COUNTRIES 131, 143 (Ian J. Bateman & Kenneth G. Willis eds., 1999) ("decisions about private contributions to public goods may reveal much more about the expressive value of contributions than they do about the instrumental value of those goods."); Florian Heeb et al., *Do Investors Care About Impact?,* 36 REV. FIN. STUD. 1737, 1738-39 (2023) (finding that "investors are willing to pay a substantial amount for a sustainable investment with some impact," but also that "investors' [willingness to pay] does not respond significantly to the level of impact that a sustainable investment offers").
[115] *See* Enriques, Romano & Tuch, *supra* note 11, at 645-50.
[116] *Id.*

to some extent, unfalsifiable assumptions.[117] The difficulty of verifying claims, combined with weak incentives to investigate those that make one feel good, creates major obstacles to reputational discipline.

Finally, users of sustainability assurances have little reason to investigate claims when inaccuracy imposes no costs on them. To understand how this works, recall the CSRD double materiality test. Financial materiality concerns the sustainability risks to which a corporation is exposed. Investors who rely on an inaccurate assurance related to this dimension of materiality may bear a private cost, even if they never discover that the assurance was inaccurate, because the relevant company may be more exposed to sustainability risks than they anticipated.[118] This provides users of sustainability assurances incentives to investigate these assurances and punish inaccurate assurers, or at least to verify their reputation.

However, consider impact-material-only disclosure, which by definition has no financial consequences to investors, for instance because no mechanisms exist that force firms to internalize harm to the environment or third parties. In this case, investors incur no private costs if impact-material-only statements are inaccurate, provided that, so long as they derive warm glow benefits therefrom, they do not discover that the certification is inaccurate. By definition, this type of information "triggers [no] material *financial effects* on the undertaking,"[119] and hence on its investors' wealth.[120]

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[117] For instance, a crucial step to set a net zero target is defining the share of global greenhouse gas emissions that a corporation can generate. Clearly, there is no single "correct" way to allocate such emissions and different criteria lead to drastically different results. Thus, second-guessing such an estimate is virtually impossible. Anders Bjorn et al., *From the Paris Agreement to Corporate Climate Commitments: Evaluation of Seven Methods for Setting 'Science-Based' Emission Targets,* ENV'T RSCH. LETTERS, May 2021, at 1, 1 (noting that the methods approved by the SBTi "vary greatly with respect to emission allocation principles").

[118] *Id.*

[119] ESRS 1, *supra* note **Error! Bookmark not defined.**, para. 3.5, at 49 (defining "financial materiality") (emphasis in the original).

[120] Admittedly, one may argue that firms that are caught making inaccurate sustainability statements may suffer a reputational sanction which would affect the stock price. However, on the one hand, it is unclear that financial markets have incentives to punish a firm that made an inaccurate statement on something that does not affect the company's performance. On the other hand, this reputational sanction presupposes that the information is proven to be inaccurate, but, as noted above, market players have limited incentives to investigate such certifications.

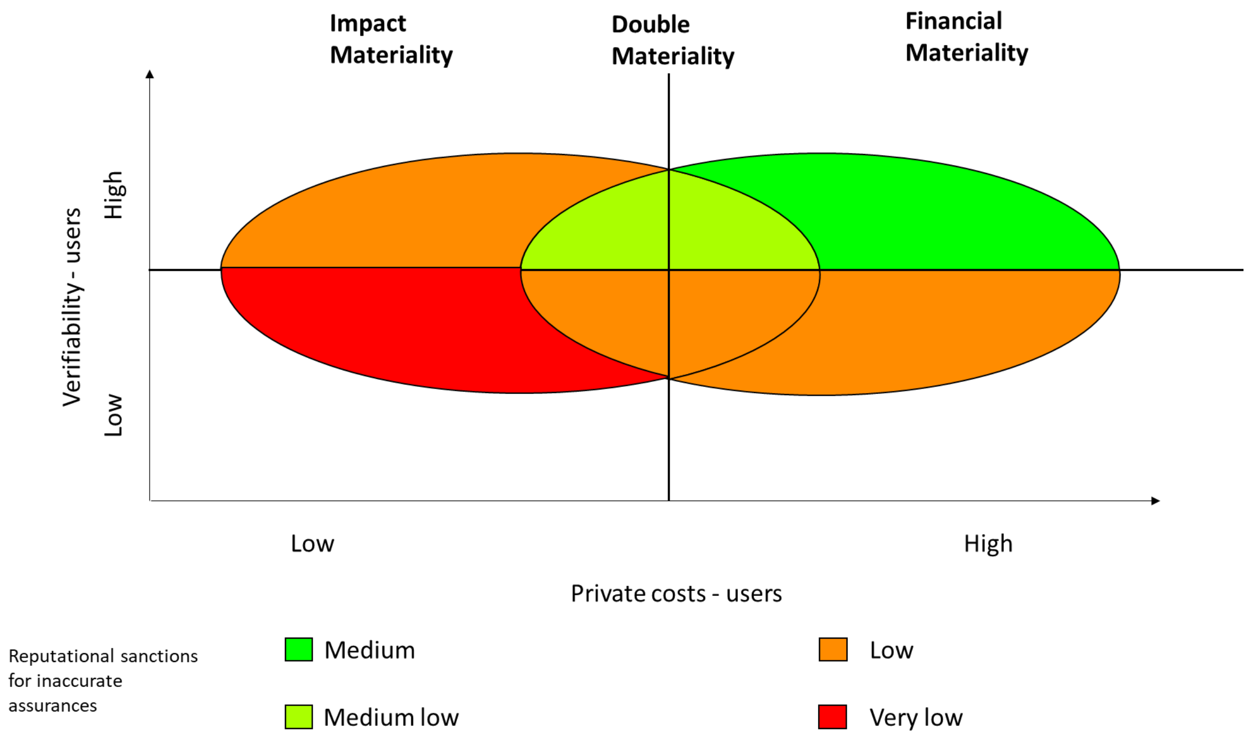

Figure 1: Mapping the relationship between verifiability by certification users, the private costs certification users face when relying on inaccurate certifications, and the intensity of reputational sanctions faced by assurance providers who issue inaccurate certifications

Figure 1 illustrates the variability of assurance providers' reputational constraints depending on certification users' incentives/ability to verify sustainability claims and the private costs they bear when unknowingly relying on inaccurate certifications. We suggest that, in all cases where either verification by users is hard or users face minimal private costs for unknowingly relying on inaccurate assurances, the reputational sanctions faced by assurers are likely to be low. By contrast, reputational mechanisms are likely to operate more intensely for assurances of sustainability matters that are financially material and that can easily be verified by users. In these circumstances, assurance providers' reputational constraints might rival those of traditional financial gatekeepers. In other circumstances, however, assurance providers face weaker reputational constraints than do traditional gatekeepers.[121]

B. Can existing regulation deter false sustainability claims?

Given the weaker reputational sanctions facing assurance providers compared to traditional gatekeepers, market mechanisms might not be sufficient to induce the former to issue accurate certifications. The natural follow-up question is whether the existing regulation of the firm making the sustainability disclosures complements reputational mechanisms to effectively prevent inaccurate sustainability certifications. We consider this question because sustainability assurance is a form of

[121] *See* Enriques, Romano & Tuch, *supra* note 11, at 644-45.

gatekeeping. As such, its regulation is justified only if primary liability—borne by the firm making the sustainability disclosures—fails to deter inaccurate sustainability claims.[122]

As we have argued elsewhere, false green claims aimed at investors are probably insufficiently deterred by primary liability under US law.[123] In brief, false sustainability-related claims are likely to escape liability under Section 11 of the Securities Act because they are commonly made outside the registration statements to which Section 11 applies—for instance, on websites and in sustainability reports.[124] Nor would actions under Rule 10b-5, which implements Section 10(b) of the Securities Exchange Act, have significant bite, since its force is limited by both scienter and materiality requirements.[125] Of course, to prevent false sustainability disclosures, policymakers might increase the severity and/or likelihood of sanctions on firms making false disclosures, but such a significant shift in federal securities law is unlikely for political reasons. Moreover, as the magnitude and probability of sanctions increase, firms face an increased risk of insolvency, which would blunt the deterrent force of sanctions.

Analysis of the justification for regulating assurance providers under EU law is less straightforward, because the liability rules and their private and public enforcement varies across member states. Suffice it to say that mandatory disclosure rules, whether in primary or secondary markets, have traditionally been underenforced within the EU.[126] It is unlikely that this will change in the foreseeable future, even more so with specific reference to sustainability reporting.

In short, the rare, if not absent, enforcement of the relevant securities law provisions, combined with our doubts about the strength of assurance providers' reputational constraints under certain conditions, suggests that direct regulation of sustainability claims is likely ineffective in deterring inaccurate sustainability information. Hence, we turn to possible policy responses with the goal of ensuring more accurate certifications.

IV. A way forward: The role of regulation

In other work addressing the broader question of regulating green gatekeepers, we argued that, *other things equal*, the appropriate policy mix for various types of green gatekeepers should depend on two factors: first, the significance of private costs for users relying on inaccurate gatekeeper certifications or assurances and, second, the extent to which policymakers and courts can verify these certifications or assurances, a factor in turn depending on the complexity of the methodologies underlying the certifications or assurances.[127]

We begin by reiterating that when we refer to certification users, we refer to investors. Therefore, we assume that policymakers rarely have an edge over certification users when it comes to verifying financially material information. Indeed, investors often possess greater expertise than regulators in

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122 Howell E. Jackson, *Reflections on Kaye, Scholer: Enlisting Lawyers to Improve the Regulation of Financial Institutions*, 66 S. CAL. L. REV. 1019, 1048 (1993) (describing gatekeeper liability in the field of financial regulation as "at most, a supplement to the dominant form of regulation in the field: direct controls over financial intermediaries"); Andrew F. Tuch, *The Limits of Gatekeeper Liability*, WASH. & LEE L. REV. ONLINE 619, 619-20 (2016) (same).
123 *See* Enriques, Romano & Tuch, *supra* note 4, at 671-74.
124 For other reasons, see *id.* at 671-73.
125 *Id.* at 673-74; *see also supra* note 71.
126 *See, e.g.,* Guido Ferrarini & Paolo Giudici, *Financial Scandals and the Role of Private Enforcement: The Parmalat Case*, *in* AFTER ENRON: IMPROVING CORPORATE LAW AND MODERNISING SECURITIES REGULATION IN EUROPE AND THE US 159, 189-196 (John Armour & Joseph A. McCahery eds, 2006).
127 Enriques, Romano & Tuch, *supra* note 4, at 675.

evaluating the financial implications of specific data, given the much stronger incentives to get it right. Conversely, when it comes to verifying at least some information with impact materiality, policymakers may hold an advantage over investors. For example, policymakers might be better positioned than investors to assess how a corporation's activities will affect biodiversity. Here, we consider the shape that regulatory intervention might take.

A. Ex-ante regulation and ex-post liability

Ex-ante regulations, a traditional approach to addressing market failures, consist of publicly imposed standards and prohibitions set by policymakers.[128] These rules are most effective when policymakers possess superior information about optimal standards and can reliably detect deviations. As per our working assumption, ex-ante regulations are less justified for information with financial materiality than for impact-material-only information. That is because, for financial materiality, reputational sanctions tend to be more effective, since users of financial certifications incur direct private costs if those certifications prove inaccurate. In contrast, policymakers often hold an informational advantage over certification users regarding impact-material-only information, making ex-ante intervention more suitable in that realm.

Ex-post liability operates through private lawsuits seeking monetary damages after harm has occurred, aiming to deter injurers.[129] In the case of financial materiality, certification users typically possess more accurate information than courts and have strong incentives to verify assurances—because they incur direct costs if they rely on incorrect financial data. As a result, holding assurers liable after the fact for faulty financially material certifications is unlikely to enhance market efficiency. By contrast, ex-post liability faces a specific challenge with impact-material-only information: since users of such information incur no direct private cost when those certifications are incorrect, it is difficult to identify the victims and quantify the harm they have suffered.

B. An unexplored lever: regulatory licenses

Many traditional gatekeepers can grant regulatory benefits—or regulatory licenses—by providing certifications. For instance, when regulators permit banks that hold assets with high credit ratings to have lower capital reserves, they confer on credit ratings agencies the ability to confer a regulatory license.[130] When the regulatory benefits tied to a certification are substantial, gatekeepers may find it more profitable to sell those benefits by adopting lax certification standards rather than by carefully analyzing information using rigorous methodologies and producing accurate, balanced assessments.[131]In such a setting, what matters to gatekeepers is their reputation not with investors but

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[128] Steven Shavell, *Liability for Harm Versus Regulation of Safety*, 13 J. LEGAL STUD. 357, 357 (1984) ("Standards, prohibitions, and other forms of safety regulations . . . are public in character and modify behavior in an immediate way through requirements that are imposed before, or at least independently of, the actual occurrence of the harm.").

[129] Charles D. Kolstad et al., *Ex Post Liability for Harm vs. Ex Ante Safety Regulation: Substitutes or Complements?*, 80 AM. ECON. REV. 888, 888 (1990) (defining ex post liability).

[130] *See, e.g.,* Howell E. Jackson, *The Role of Credit Rating Agencies in the Establishment of Capital Standards for Financial Institutions in a Global Economy, in* REGULATING FINANCIAL SERVICES AND MARKETS IN THE TWENTY FIRST CENTURY 311, 314 (Eilis Ferran & Charles A.E. Goodhart eds., 2001).

[131] Christian C. Opp, Marcus M. Opp & Milton Harris, *Rating Agencies in the Face of Regulation,* 108 J. FIN. ECON. 46 (2013) (showing formally that in the presence of significant regulatory benefits rating agencies find it more profitable to inflate ratings and sell regulatory benefits than to invest in information acquisition);

with the body that confers the power to grant regulatory licenses[132] and whether regulators can spot and punish inaccurate certifications.

When granted to traditional gatekeepers in financial markets, regulatory licenses are generally perceived negatively.[131] That is because these licenses—and the certifications they validate—displace other, finer-grained disciplinary mechanisms. Specifically, investors tend to be sophisticated and bear significant private costs when they rely on inaccurate certifications. Hence, these market players have both the ability and the incentives to impose reputational sanctions on gatekeepers who adopt lax standards. In contrast, regulators may be less capable of detecting inaccurate certification and may be unable to punish gatekeepers who adopt lax standards, for instance because regulatory licenses tend to be "sticky."[133] Thus, a common recommendation to policymakers is to minimize gatekeepers' ability to grant regulatory benefits with their certifications.[134]

In the sustainability reporting context, however, giving gatekeepers the ability to grant regulatory benefits with their certifications may *increase* the accuracy of certifications under certain conditions. Consider the red area in Figure 1, in which certification users cannot easily verify an impact-material-only issue and bear limited private costs if they rely on inaccurate assurance. In those circumstances, the reputational constraints imposed on assurance providers by market participants are already weak. Thus, there is very little to lose by displacing this reputational mechanism. At the same time, especially if regulators can verify assurances with reasonable accuracy, assurance providers might be incentivized to issue more accurate certifications in order to preserve the ability to confer regulatory benefits with their certifications—and to collect the rents that come with it.

C. Other regulatory tools

Another option for policymakers is to subsidize assurance providers that operate as non-profit entities. Because non-profit firms face strict limits on dividend distribution,[135] they have relatively weaker incentives to exploit ineffective market-based reputational sanctions.[136] One possible approach is to grant tax incentives to employees of non-profit gatekeepers. If accurate gatekeeper certifications yield positive externalities, providing such subsidies is economically justifiable.

Given the opacity of sustainability assurance, a further option worth considering is transparency requirements. Many assurance providers rely on in-house standards and protocols.[137] As of 2020, about one in five S&P 500 companies did not publish assurance reports alongside their sustainability disclosures, and in some cases, the reports were simply unavailable (for example, due to broken

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132 *See* Frank Partnoy, *The Siskel and Ebert of Financial Markets?: Two Thumbs down for the Credit Rating Agencies,* 77 WASH. U. L.Q. 619, 685 (noting that under the regulatory license view of ratings, "the limitation on the raters' behavior is not the raters' reputation in the market, it is the raters' reputation with the [regulator]").
133 *Id.* (noting that gatekeepers may be able to keep favorable regulations in place through their influence over the political process).
134 *Id.*
135 *See* Henry B. Hansmann, *Reforming Nonprofit Corporation Law*, 129 U. PA. L. REV. 497, 574 (1981); Peter Molk & D. Daniel Sokol, *The Challenges of Nonprofit Governance*, 62 B.C. L. REV. 1497, 1508–12 (2021).
136 Henry B. Hansmann, *The Role of Nonprofit Enterprise*, 89 YALE L.J. 835, 843–44 (1980) (discussing the advantages of the non-profit form when consumers cannot assess the quality of the product).
137 *See* Gipper, Ross & Shi, *supra* note 7 at Table 1 (Panel D).

weblinks).[138] Some providers obscure the level of assurance, using vague terms like "moderate" or "high," or omitting a descriptor altogether, instead of the standard industry labels ("limited" or "reasonable").[139] Requiring assurance providers to disclose their reports, the details of the standards used, and the level of assurance would enable certification users to better discipline them, thereby improving the reliability of certifications over time.

Conclusion

Assurance providers, a type of green gatekeeper, certify the accuracy of sustainability information, which investors have increasingly demanded. In this article, we analyzed the market for assurance services, asking whether and, if so, how they should be regulated. By certifying sustainability-related claims, assurance providers do with respect to sustainability-related claims what public accounting firms have long done with respect to financial statements, certifying the accuracy of claims by public companies. In doing so, assurance providers promise to reduce the information asymmetry between makers of sustainability claims and those exposed to these claims.[140]

To assess the possible basis for regulating assurance providers, we first considered their reputational incentives, explaining why these are likely to be weaker than those of traditional gatekeepers and explaining the conditions under which reputational mechanisms will likely underdeter inaccurate certifications. We then assessed the force of direct regulation, finding a possible basis for regulating assurance providers. In considering policymakers' responses, we drew on a framework we developed in earlier work, under which, *other things equal*, the appropriate policy mix for various types of green gatekeepers should depend on, first, the significance of private costs for users relying on inaccurate gatekeeper certifications or assurances and, second, the extent to which policymakers and courts can verify these certifications or assurances, a factor in turn depending on the complexity of the methodologies underlying the certifications or assurances. Applying this framework, we commented on the merits of several policy interventions.

138 *Id.* at Figure 6 (Panel A, including accompanying explanation).
139 THE CENTER FOR AUDIT QUALITY, *supra* note 78 (under "Terminology Used to Describe Assurance/Verification from Other Providers").
140 Enriques, Romano & Tuch, *supra* note 4, at 612.

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