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Client Alert

Corporate Governance

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SEC Proposes Rules Standardizing Climate-Related Disclosures

On March 21, 2022, the Securities and Exchange Commission (SEC) proposed widely anticipated rules that would require registrants to provide specified climate-related information in registration statements and periodic reports.[1] The proposal represents the next step in the SEC's ambitious agenda to enhance and modernize public company disclosures, coming less than two weeks after its recent proposal regarding cybersecurity disclosures (see our recent client alert). The comprehensive and extensive proposed rules are intended to standardize climate-related disclosures to address demands of climate-concerned investors. Comments are due by the later of May 20, 2022 and the date 30 days after publication of the proposed rules in the Federal Register.

Proposed Disclosure Requirements

The proposed disclosures would be required in registration statements and annual reports, with the requisite disclosures (other than the financial statement metrics) provided in a separate, appropriately captioned section, or alternatively, incorporated by reference into the separate, appropriately captioned section from another section of the filing (such as Risk Factors, Description of Business, or Management's Discussion and Analysis). The proposed disclosures generally fall into five broad categories, as described below.

1. Financial Statement Metrics

The proposed rules would require a registrant to disclose certain disaggregated climate-related financial statement metrics in a note to its audited financial statements, with the requisite disclosure falling under three categories of information:

- financial impact metrics;
- expenditure metrics; and
- financial estimates and assumptions.

According to the release, the objective of including these metrics is to increase transparency about how climate-related risks impact a registrant's financial statements. These would be the only proposed disclosures subject to audit by an independent registered public accounting firm and falling within the scope of the registrant's internal control over financial reporting.

2. GHG Emissions Metrics Disclosures and Assurance

The proposed rules would require disclosure of GHG emissions for the most recently completed fiscal year as follows:

- Direct GHG emissions (Scope 1) and indirect GHG emissions from purchased electricity and other forms of energy (Scope 2), separately disclosed, expressed both by disaggregated constituent greenhouse gases and in the aggregate, and in absolute terms, not including offsets, and in terms of intensity (per unit of economic value or production); and
- Indirect GHG emissions from upstream and downstream activities in a registrant's value chain (Scope 3) in absolute terms, not including offsets, and in terms of intensity if Scope 3 emissions are material, *or* if the registrant has set a GHG emissions target or goal that includes Scope 3 emissions.

A registrant that is an accelerated filer or large accelerated filer would be required to include in the relevant filing an attestation report covering the disclosure of Scope 1 and Scope 2 emissions, and to provide certain related disclosures about the service provider. The proposed rules include a phase-in around assurance levels for the attestation engagement, requiring "limited assurance" in fiscal years 2 and 3 after Scopes 1 and 2 emissions disclosures are required, and "reasonable assurance" in fiscal year 4 and beyond.

3. Climate-Related Risks and Their Impacts

The proposed rules would require disclosures around both physical risks and transition risks (with relevant proposed definitions substantially similar to the TCFD's definitions of climate-related risks and climate-related opportunities) as follows:

- How any climate-related risks identified by the registrant have had or are likely to have a material impact on its business and consolidated financial statements, which may manifest over the short-, medium-, or long-term; and
- How any identified climate-related risks have affected or are likely to affect the registrant's strategy, business model, and outlook.

4. Governance and Oversight of Climate-Related Risks

The proposal would require companies to disclose information about:

- The oversight and governance of climate-related risks by the registrant's board and management; and
- The registrant's processes for identifying, assessing, and managing climate-related risks and whether any such processes are integrated into the registrant's overall risk management system or processes.

5. Climate-Related Targets and Goals, and Transition Plans

The proposed rules contemplate extensive additional disclosures relating to targets and goals, and transition plans, including as follows:

  - If the registrant has publicly set climate-related targets or goals, information about:

  - The scope of activities and emissions included in the target, the defined time horizon by which the target is intended to be achieved, and any interim targets;
  - How the registrant intends to meet its climate-related targets or goals;
  - Relevant data to indicate whether the registrant is making progress toward meeting the target or goal and how such progress has been achieved, with updates each fiscal year; and
  - If carbon offsets or renewable energy certificates ("RECs") have been used as part of the registrant's plan to achieve climate-related targets or goals, certain information about the carbon offsets or RECs, including the amount of carbon reduction represented by the offsets or the amount of generated renewable energy represented by the REC;
- If the registrant has adopted a transition plan as part of its climate-related risk management strategy, a description of the plan, including the relevant metrics and targets used to identify and manage any physical and transition risks;
- If the registrant uses scenario analysis to assess the resilience of its business strategy to climate-related risks, a description of the scenarios used, as well as the parameters, assumptions, analytical choices, and projected principal financial impacts; and
- If a registrant uses an internal carbon price, information about the price and how it is set.

Timing and Other Changes

The proposed rules include phase-in periods for all registrants, dependent on filer status, plus an additional phase-in period for Scope 3 emissions disclosure, and an exemption from the Scope 3 emissions disclosure requirement for smaller reporting companies.

While the proposed rules will be subject to a comment period and to final approval, which means the ultimate timing of implementation remains a significant unknown, for explanatory purposes, the SEC provided the following illustration of how the phase-ins would operate, assuming the proposed rules are adopted with an effective date of December 2022 (and assuming the filer has a December 31st fiscal year-end):

Registrant Type	Disclosure Compliance Date	
	All proposed disclosures, including GHG emissions metrics: Scope 1, Scope 2, and associated intensity metric, but excluding Scope 3	GHG emissions metrics: Scope 3 and associated intensity metric
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)
Accelerated Filer and Non-Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)
SRC	Fiscal year 2025 (filed in 2026)	Exempted

Filer Type	Scopes 1 and 2 GHG Disclosure Compliance Date	Limited Assurance	Reasonable Assurance
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Fiscal year 2026 (filed in 2027)
Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Fiscal year 2027 (filed in 2028)

In addition, the proposed rules include a safe harbor from liability for Scope 3 emissions disclosure, and forward-looking statement safe harbors pursuant to the Private Securities Litigation Reform Act (to the extent that disclosures include forward-looking statements).

Initial Takeaways

In October 2021, the Biden administration announced a "comprehensive, government-wide strategy to measure, disclose, manage and mitigate the systemic risks" posed by climate change, noting that "climate change poses a systemic risk to our economy and our financial system."[2] The SEC's proposal is a meaningful step toward advancing the Biden Administration's broad commitment to a climate change agenda. In SEC Chair Gary Gensler's view, the proposal would "provide investors with consistent, comparable, and decision-useful information for making their investment decisions and would provide consistent and clear reporting obligations for issuers." However, in its current form, the proposal may raise as many questions as it answers. SEC Commissioner Hester Pierce, who did not support the proposal, sees the proposal as having the opposite impact – in her words, the proposed rules would "undermine the existing regulatory framework that for many decades has undergirded consistent, comparable, and reliable company disclosures." During the comment period and beyond, we expect the debate to continue around whether and to what extent it is appropriate or permissible for the SEC to require a set of climate disclosures that will be mandatory for all companies without regard for materiality. And in the meantime, companies will begin evaluating existing voluntary disclosures – particularly goals and targets – in light of the proposed rule to understand what changes and costs the rule would impose.

[1] The proposed rules are available here ("Proposing Release"), and the SEC's accompanying press release and fact sheet are available here and here, respectively.
[2] See FACT SHEET: Biden Administration Roadmap to Build an Economy Resilient to Climate Change Impacts available here.