SEC Issues Long-Awaited Proposed Climate Change Disclosure Rule

March 24, 2022

On March 21, 2022, the U.S. Securities and Exchange Commission (the "SEC") released its long-awaited proposed rule on the "Enhancement and Standardization of Climate-Related Disclosures for Investors" (the "Proposed Rule"). The Proposed Rule is intended to require "consistent, comparable, and decision-useful information" on climate-related disclosures. If adopted, the Proposed Rule would constitute one of the most dramatic changes ever to SEC disclosure requirements, though it likely will generate numerous comments both for and against and ultimately face legal challenge.

The Proposed Rule would add new, often prescriptive climate-related disclosure requirements to Regulation S-K, which primarily governs qualitative disclosures, and Regulation S-X, which governs financial statements. In general, these disclosures would address various climate-related risks to registrants' business, operations and financial condition, including disclosure of registrants' greenhouse gas ("GHG") emissions. The Proposed Rule draws heavily from the Task Force on Climate-Related Financial Disclosures, which has developed a climate-related reporting framework that is familiar to many registrants and investors, and the Greenhouse Gas Protocol, which the SEC identifies as the leading accounting and reporting standard for GHG emissions.

Chair Gary Gensler and Commissioners Allison Herren Lee and Caroline Crenshaw voted in favor of the Proposed Rule, while Commissioner Hester Peirce, the sole Republican Commissioner, dissented. Chair Gensler, in his supporting statement, defended the Proposed Rule as well within the SEC's mandate, noting that, "[o]ver the generations, the SEC has stepped in when there's significant need for the disclosure of information relevant to investors' decisions." By contrast, in a blistering dissenting statement, Commissioner Peirce lamented that the Proposed Rule, unlike current SEC disclosure mandates, "forces investors to view companies through the eyes of a vocal set of stakeholders, for whom a company's climate reputation is of equal or greater importance than a company's financial performance."

Below we provide a high-level summary of the Proposed Rule's key provisions. In particular, the Proposed Rule requires domestic and foreign registrants to include the following information in their registration statements and periodic filings:

- **Greenhouse Gas Emissions.** Registrants would be required to disclose their GHG emissions, including Scope 1 (direct) and Scope 2 (indirect) emissions, regardless of whether these Scope 1 and Scope 2 emissions are material. Most registrants must also disclose Scope 3 emissions of upstream and downstream activities if (i) these emissions are material or (ii) even if not material, registrants have set GHG emissions reduction targets or goals that include Scope 3 GHG emissions. For Scope 3 emissions, the Proposed Rule includes a safe harbor from liability, an exemption for smaller registrants and a delayed compliance date. Accelerated and large accelerated filers must provide an attestation report from an independent attestation service provider covering at least the filer's Scope 1 and Scope 2 emissions, a requirement that will be phased in. The phase-in process will start with a limited assurance and transition to a reasonable assurance.

- **Impact of Climate-Related Risks on Business Outlook.** Registrants would be required to describe how any identified climate-related risks have affected, or will likely affect, their business model, strategy and outlook.

- **Risk-Management Processes.** Registrants would be required to describe their processes for identifying, assessing and managing climate-related risks, as well as whether those processes are integrated into the company's overall risk management program. If registrants use scenario analysis or an internal carbon price, then information about these items must be disclosed.

- **Corporate Governance.** Registrants would need to describe the oversight and governance of climate-related risks by the board and management.

- **Impact of Climate-Related Risks on Consolidated Financial Statements.** The Proposed Rule would require disclosure of how any climate-related risks identified by registrants (both physical and transition) have had or are likely to have a material impact on the business and consolidated financial statements, which may manifest over the short, medium or long term.

- **Financial Statement Metrics (Regulation S-X Amendments).** The Proposed Rule would require registrants to disclose information on the impact of climate-related risks on business and consolidated financial statements. This includes, among other requirements, information about how climate events will affect certain line items on consolidated financial statements and assumptions used in the financial statements.

- **Public Climate Goals (If Any).** If registrants have set climate-related targets or goals, the Proposed Rule would require disclosure of, as applicable, descriptions of: (i) the scope of activities and emissions included in the target; (ii) the unit of measurement, including whether the target is absolute or intensity based; (iii) the defined time horizon by which the target is intended to be achieved; (iv) the defined baseline time period and baseline emissions against which progress will be tracked; (v) any interim targets set by registrants; and (vi) how registrants intend to meet climate-related targets or goals. If applicable, registrants would be required to disclose certain information about their use of carbon offsets or renewable energy certificates to achieve set targets or goals.

- **Transition Plans.** If registrants have adopted a transition plan, the Proposed Rule would require them (i) to describe the plan, including relevant metrics and targets used to identify and manage physical and transition risks; (ii) to discuss how they plan to mitigate or adapt to any physical risks identified in their filings; and (iii) to update their disclosures about their transition plans each year by describing the actions taken during the year to achieve the plan's targets or goals.

The SEC has requested comment on the Proposed Rule by May 20, 2022 or 30 days after publication of the rule in the Federal Register, whichever is later.

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Please do not hesitate to contact us with any questions.

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