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SEC Adopts Comprehensive Package of Climate-Related Disclosure Rules; Scope 3 Emission Metrics Excluded

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Go-To Guide:

- SEC adopts comprehensive climate-related disclosure rules for public companies in their registration statements and periodic reports.
- Compliance dates phased in by registrant status, beginning as early as fiscal year 2025.
- Greenhouse gas (GHG) emission disclosure scaled back and limited to Scope 1 and Scope 2 for large accelerated filers and accelerated filers, subject only to materiality determinations.
- Emerging growth companies (ECGs), smaller reporting companies, and non-accelerated filers exempted from GHG emission disclosure.
- Foreign private issuers (FPIs) must comply unless otherwise in an exempted category; no ability to substitute compliance with requirements from other jurisdictions or standard-setters.
- Financial statement disclosures narrowed from the proposed rules; electronic tagging required for narrative and quantitative disclosures.
- Companies should review the implications of the new rules on their existing climate risk-management systems, including GHG accounting efforts.

On March 6, 2024, the Securities and Exchange Commission (SEC) adopted by a 3-2 vote a series of new and extensive disclosure rules that will require all registered companies, including FPIs, to include detailed climate-related information in their registration statements and periodic reports, and climate-related financial statement metrics in a note to their audited financial statements. Following the rule's initial proposal in March 2022, the SEC received a record-setting 24,000+ comment letters and has spent the intervening period considering key aspects of the proposed rules, particularly with respect to disclosure metrics and requirements for GHG emissions.

The newly adopted rules will require accelerated and large accelerated SEC reporting companies to engage an independent outside expert to provide an attestation report relating to additional quantitative disclosure on GHG emissions. The rules are intended to enhance as well as standardize climate-related disclosures to aid investors in their investment and voting decisions.

A safe harbor has been included in new Item 1507 of Regulation S-K with respect to information required to be disclosed in connection with transition plans, scenario analyses, use of internal carbon prices, and targets and goals, except for historical facts and statements about material expenditures actually incurred. These disclosures will be considered forward-looking statements for the purposes of the existing statutory safe harbors provided in Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934.

Compliance with the rules will be phased in by size and status of registrant between fiscal year 2025 and fiscal year 2031. The rules apply to both domestic registrants and FPIs (apart from Canadian issuers reporting on Form 40-F). Private companies party to a business combination registered on Form S-4 or F-4 will not be required to comply with the new rules. Notably, there is no accommodation or reciprocity for issuers subject to similar reporting obligations in other jurisdictions, such as the European Union’s Corporate Sustainability Reporting Directive (CSRD) adopted Jan. 3, 2023.

This GT Alert summarizes the final rule amendments, which impact both Regulation S-K as well as the financial reporting rules under Regulation S-X. The rules become effective 60 days after publication in the Federal Register, although a coalition of 10 state attorneys general have already filed a petition for review in the U.S. Court of Appeals for the Eleventh Circuit seeking to have the rules vacated, and two other petitions for review have been filed in the U.S. Court of Appeals for the Fifth Circuit.

Many public companies may already have in place climate risk management systems and GHG accounting efforts for a variety of purposes. Those systems and efforts may affect compliance obligations under these new rules, and companies may want to consider modifications to the existing systems in light of these rules.

Amendments to Regulation S-K

New Items 1500 - 1508 of Regulation S-K will require quantitative and qualitative disclosure in registration statements and annual reports of a company’s (1) GHG emissions metrics relating to Scopes 1 and 2 emissions; (2) independent attestation or assurance report on those GHG emissions disclosures; (3) governance of climate-related risks; (4) material climate-related impacts on its strategy, business model, and outlook; (5) climate-related risk management; and (6) climate-related targets and goals, if any.

- **GHG Emissions Metrics (S-K Item 1505)**

A key disclosure area that elicited significant comment from the public relates to GHG emission metrics. The SEC concluded that investors view Scopes 1 and 2 emissions as a “central measure and indicator of the registrant’s exposure to transition risk” and to assess the registrant’s management of transition risk and progress towards established targets or goals. The final rules require large accelerated filers and accelerated filers to disclose their Scope 1 emissions and/or Scope 2 emissions, *if those emissions are material*, for the registrant’s most recently completed fiscal year and, to the extent previously disclosed in an SEC filing, for the historical fiscal years included in the registrant’s consolidated financial statements included in the filing. Hence, disclosures will not be required for historical periods prior to the initial compliance date. “Materiality” for purposes of the rules utilizes the same principles for determination under existing federal securities laws and Regulation S-K. Disclosure of immaterial emission data is not required. The rules define “Scope 1 emissions” as direct GHG emissions from operations owned or controlled by the registrant and “Scope 2 emissions” as indirect GHG emissions from the generation of purchased or acquired electricity, steam, heat, or cooling consumed by operations owned or controlled by the registrant.

In a key change from the proposed rules, EGCs, smaller reporting companies, and non-accelerated filers are exempt from this reporting requirement. In addition, the SEC declined to adopt disclosure requirements relating to Scope 3 emissions (indirect emissions not otherwise included in Scope 2 that occur in the upstream and downstream activities of a company’s value chain), departing from standards adopted by the IFRS International Sustainability Standards Board, the EU’s CSRD, and California’s Climate Corporate Data Accountability Act (SB 253). Companies that operate internationally and/or in California may need to assess how to reconcile the different reporting regimes and whether to rely on website disclosures of non-SEC required disclosures or otherwise disclose certain Scope 3 emissions metrics in their SEC filings for consistency.

Scope 1 and Scope 2 emissions are to be disclosed separately, but each expressed in the aggregate, in terms of carbon dioxide equivalent (CO2e). Further, if any of the constituent gas of the disclosed emissions is individually material, emissions of those gases must be disaggregated and disclosed separately. Disclosure must include the methodology, significant inputs, and significant assumptions used to calculate the emissions, including

- organizational boundaries used in the calculations and the method to determine those boundaries;
- a brief discussion of the operational boundaries used, including the approach to categorization of emissions and sources; and
- a brief description of the protocol or standard used to report the GHG emissions, including the calculation approach, the type and source of any emission factors used, and any calculation tools used to calculate the GHG emissions.

Reasonable estimates are permissible as long as the underlying assumptions and the reasons for using estimates are disclosed.

Recognizing that many companies currently report GHG emissions metrics outside of SEC filings after completion of the second fiscal quarter, the final rules provide that any GHG emission metrics required to be disclosed in a registrant’s annual report on Form 10-K may be incorporated by reference from the company’s Form 10-Q for the second fiscal quarter in the fiscal year immediately following the year to which the GHG disclosure relates, or may be included in an amended Form 10-K no later than the due date for such Form 10-Q. To provide comparable treatment for FPIs, the information may be disclosed in an amendment to Form 20-F (and not on a Form 6-K) and due no later than 225 days after the end of the fiscal year to which the GHG emissions metrics relates. In each case, the registrant must include an express statement in its annual report indicating its intention to incorporate the information from either a quarterly report on Form 10-Q or an amended annual report to notify investors as to where the required GHG emissions metrics disclosure can be found. Disclosure in registration statements under the Securities Act of 1933 or on Form 10 under the Securities Exchange Act of 1934 must be provided as of the most recently completed fiscal year that is at least 225 days prior to the effective date of the registration statement.

- **Independent Attestation Report (S-K Item 1506)**

A company required to provide Scope 1 and Scope 2 emissions disclosures must include an attestation report in its filing covering that disclosure, subject to a transition period. This requirement was also the subject of extensive public comment due to the expected additional cost burden on companies. The GHG emissions attestation report must be prepared and signed by a GHG emissions attestation provider who

- is an expert in GHG emissions by virtue of having significant experience in measuring, analyzing, reporting, or attesting to GHG emissions; and
- is independent with respect to the company and its affiliates for whom it is providing the attestation report during the attestation and professional engagement period.

The GHG emissions attestation report must follow the requirements set by the attestation standard used by the GHG emissions attestation provider. In addition, the registrant must disclose certain information about the attestation provider, including any oversight inspection program and prior attestation engagements for the registrant (including any disagreements). Limited assurance is required initially for both large accelerated and accelerated filers beginning in the third year following the initial Scope 1 and Scope 2 reporting compliance date. However, beginning the seventh fiscal year after the initial compliance date for GHG emissions reporting, the attestation engagement for large accelerated filers must be at a reasonable assurance level. Limited assurance is considered equivalent to what is commonly referred to as a “review” of a company’s interim financial statements included in a Form 10-Q, whereas reasonable assurance is considered equivalent to the level of assurance provided in an audit of a company’s financial statements.

- **Governance of Climate-Related Risks (S-K Item 1501)**

Board Oversight. Companies will be required to disclose certain information concerning the board of directors’ oversight of climate-related risks, including

- the identity of any board committee or subcommittee responsible for the oversight of climate-related risks;
- the processes by which the board or board committee/subcommittee is informed about climate-related risks; and
- if the board sets climate-related targets, goals, or transition plans, a description of whether and how the board oversees progress against such targets/goals or plan.

Notably, these disclosures are not required for a registrant that does not exercise board oversight of climate-related risks.

Management Oversight. The final rules also require a company to disclose certain information concerning management’s role in assessing and managing material climate-related risks, including

- whether and which management positions or committees are responsible for assessing and managing climate-related risks and, if so, the relevant experience of the position holders or members in enough detail to fully describe the nature of the experience;
- the processes by which the responsible managers or management committees assess and manage climate-related risks; and
- whether the responsible positions or committees report to the board or a committee/sub-committee of the board on climate-related risks.
- **Material Climate-Related Impacts on Strategy (S-K Item 1502)**

Companies will now be required to disclose climate-related risks that are likely to have materially impacted or are reasonably likely to have a material impact on the company's business, including its strategy, results of operations, or financial condition. The disclosure must include risks that are reasonably likely to manifest in the short term (i.e., the next 12 months) as well as the long term beyond 12 months, and whether those risks are physical risks (relating to the physical impacts of climate change) or transition risks (relating to a potential transition to a lower carbon economy). Disclosure of climate-related risks should specify the nature of the risks presented and describe the extent of the registrant's exposure to the risk, including

- if a physical risk, whether it may be categorized as an acute or chronic risk, and the geographic location and nature of the properties, processes, or operations subject to the physical risk; and
- if a transition risk, whether it relates to regulatory, technological, market (including changing consumer, business counterparty, and investor preferences), or other transition-related factors, and how those factors impact the registrant.

The discussion must also include how these risks have materially impacted or are reasonably likely to materially impact the company's business, results of operations, or financial condition. This discussion must include a quantitative and qualitative analysis of the material expenditures incurred and the material impacts on financial estimates and assumptions that directly result, in management's view, from mitigation activities.

If a transition plan has been adopted to manage a material transition risk, that plan must be described and updated annually in the registrant's annual report. The discussion should include any actions taken during the year under the plan and how those actions have impacted the business, results of operations, or financial condition. Quantitative and qualitative disclosure of material expenditures is required, as well as a discussion of the material impacts on financial estimates and assumptions as a direct result of the transition plan.

Companies should disclose scenario analyses, where used, including a description of the parameters, assumptions, and analytical choices employed, as well as expected material impacts under each scenario.

Once a company has described the climate-related risks reasonably likely to have a material impact on the company's business, results of operations, and financial condition, the company then must describe the actual and potential material impacts of those risks on its strategy, business model, and outlook, including material impacts on the company's

- business operations, including the types and locations of its operations;
- products or services;
- suppliers, purchases, or counterparties to material contracts, to the extent known and reasonably available;
- activities to mitigate or adapt to climate-related risks, including adoption of new technologies or processes; and
- expenditure for research and development.

Further, the registrant is required to discuss whether and how it considers any of the identified factors impact its business strategy, financial planning, and capital allocation, including whether the impacts have been integrated into the company's strategy and how resources, if any, are being used for risk mitigation. Similarly, a discussion of whether and how any of the disclosed targets/goals or transition plans relate to the business strategy is required.

If a company uses carbon offsets or renewable energy credits or certificates (RECs) as part of its emissions reduction strategy, the company will need to disclose the role that carbon offsets or RECs play in the company's climate-related business strategy.

If a company maintains an internal carbon price that is material to how it evaluates and manages climate-related risks, the company is required to disclose (in its reporting currency) for each such price

- the price per metric ton of CO_2e;
- the total price, including how the total price is estimated to change over the short and long terms;
- if multiple prices are used, the rationale for selecting different prices; and
- the boundaries for measurement of overall CO_2e on which the total price is based, if different from the GHG emission organizational boundary requirement.
- **Climate-Related Risk Management (S-K Item 1503)**

The processes a company utilizes for identifying, assessing, and managing material climate-related risks will need to be discussed, including, as applicable, how the registrant

- identifies whether it has incurred or is reasonably likely to incur a material physical or transition risk;
- decides whether to mitigate, accept, or adapt to a particular risk; and
- prioritizes whether to address climate-related risks.

If the registrant is managing a material climate-related risk, the registrant must also describe whether and how any processes have been integrated into its overall risk management system.

- **Climate-Related Targets and Goals (S-K Item 1504)**

If a company has set any climate-related targets or goals, then the company must provide certain information about those targets or goals if they have materially affected or are reasonably likely to materially affect the company's business, result of operations, or financial condition. Specifically, the rules require companies to disclose, as applicable, a description of

- the scope of activities included in the target or goal;
- the unit of measurement;
- the defined time horizon by which the company intends to achieve the target or goal, and whether the time horizon is consistent with one or more goals established by a climate-related treaty, law, regulation, policy, or organization;
- the defined baseline time period and means against which progress will be tracked; and
- how the company intends to meet its climate-related targets or goals.

Further, under the final rules, companies must describe any progress made toward meeting the target or goal, how that progress was achieved, and any material impacts on the business, results of operations, or financial condition as a direct result of the target/goal or actions taken, updating the disclosure annually. The discussion should include a quantitative and qualitative analysis of any material expenditures and material impacts on any financial estimates and assumptions. If a company has used carbon offsets or RECs as a material component of a plan to achieve climate-related targets or goals, the company will be required to disclose separately the amount of carbon avoidance, reduction, or removal represented by the offsets or the amount of generated renewable energy the RECs represent, the nature and source of the offsets or RECs, a description and location of the underlying projects, any registries or other authentication of the offsets or RECs, and the cost of the offsets or RECs.

Amendments to Regulation S-X

The final rules include adoption of new Article 14 of Regulation S-X, "Disclosure of Severe Weather Events and Other Information." Under Article 14-01, a registrant will be required to include in the relevant filing disclosure in the notes to the financial statements when climate-related information is provided pursuant to Item 1500 of Regulation S-K. Disclosure is provided for the most recently completed fiscal year and for any historical fiscal years for which audited financial statements are included in the filing, provided that Item 1500 information was previously disclosed or required to be disclosed for those years.

Under Article 14-02, a company must disclose certain disaggregated climate-related financial statement metrics falling under the following three categories of information: (1) financial impact metrics; (2) expenditure metrics; and (3) financial estimates and assumptions. The company must describe how each specified financial statement effect was derived, including a description of significant inputs and assumptions used, significant judgments made, how estimates and assumptions were materially impacted by exposures to risks and uncertainties, other information necessary to understand the effect and, if applicable, policy decisions to calculate the specified disclosures.

Certain disclosure thresholds apply, including aggregate expenditure expenses as incurred and losses equal to or exceeding one percent of the absolute value of income of loss before income tax expense/benefit for the relevant fiscal year; provided, however, that no disclosure is required if the aggregate amount of expenditures or losses is less than $100,000 for the relevant year. In addition, disclosure of aggregate capitalized costs and charges incurred is required if the aggregate absolute value equals or exceeds one percent of the absolute value of stockholders' equity/deficit at the end of the fiscal year; provided, however, no disclosure is required if the aggregate amount of the capitalized costs/charges is less than $500,000 for the relevant year.

The rules require disclosure of the expenditures incurred and losses, including recoveries, from severe weather events and other natural conditions (collectively, SWEs), such as hurricanes, tornadoes, wildfires, flooding, drought, extreme temperatures, and sea level rise. Disclosure is also required with respect to capitalized costs and charges, excluding recoveries, incurred from SWEs. These could include, for example, amounts incurred to restore operations or relocate assets affected by the event, such as amounts incurred to relocate assets from areas at high risk from wildfires. Aggregate amounts expensed and recognized, and losses incurred, in connection with RECs and carbon offsets must be disclosed to the extent these comprise a material component of the registrant's disclosed targets or goals.

Transition Periods

As noted above, the final rules provide a transition period for all registrants based on status as a large accelerated filer (LAF), accelerated filer (AF), non-accelerated filer (NAF), EGC, or smaller reporting company (SRC). Below is a chart identifying the various compliance dates under the new rules, as published in the SEC's Fact Sheet.

Compliance Dates under the Final Rules1

Registrant Type	Disclosure and Financial Statement Effects Audit		GHG Emissions/Assurance			Electronic Tagging
All Reg. S-K and S-X disclosures, other than as noted in this table	Item 1502(d)(2), Item 1502(e)(2), and Item 1504(c)(2)	Item 1505 (Scopes 1 and 2 GHG emissions)	Item 1506 - Limited Assurance	Item 1506 - Reasonable Assurance	Item 1508 - Inline XBRL tagging for subpart 15002	
LAFs	FYB 2025	FYB 2026	FYB 2026	FYB 2029	FYB 2033	FYB 2026
AFs (other than SRCs and EGCs)	FYB 2026	FYB 2027	FYB 2028	FYB 2031	N/A	FYB 2026
SRCs, EGCs, and NAFs	FYB 2027	FYB 2028	N/A	N/A	N/A	FYB 2027

1 As used in this chart, “FYB” refers to any fiscal year beginning in the calendar year listed.

2 Financial statement disclosures under Article 14 will be required to be tagged in accordance with existing rules pertaining to the tagging of financial statements. See Rule 405(b)(1)(i) of Regulation S-T.

Notwithstanding the applicable transition periods, given the additional disclosures that will now be required, public companies should begin analyzing what they will be required to disclose, to the extent that this process has not previously been initiated. To start, this would include determining what information the company currently collects and discloses, together with analyzing whether any metrics currently calculated would comply with what are expected to be the proposed technical disclosure requirements and their ability to be attested to by third parties. Further, public companies should review existing goals and targets communicated by the company publicly and to third parties and consider potential disclosure obligations when setting new targets or goals. The company’s approach to governance of climate-related risks should be evaluated with the goal of strengthening risk-management structures for oversight of these risks. The company’s audit committee may also consider communicating with the company’s external auditors to understand how the rules will impact the preparation and presentation of the company’s financial statements.

There will be no one-size-fits-all solution for developing compliance systems under the final rules. Companies subject to IFRS, CSRD, California, or other local disclosure requirements will have an extra burden, both in terms of time and resources, in reconciling the varying requirements and timeframes for reporting.

For additional information about the proposed rules, please refer to our May 2022 GT Alert.

Footnotes

[1] State of West Virginia v. United States Sec. & Exch. Comm’n, No. 24-10679 (11th Cir. filed March 6, 2024).

[2] Liberty Energy v. United States Sec. & Exch. Comm’n, No. 24-60109 (5th Cir. filed March 6, 2024), and a petition reportedly filed by the states of Louisiana, Texas, and Mississippi but not yet docketed as of this writing.

[3] See SEC Release, 33-11275 (March 6, 2024), p. 244.

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