



## The SEC's Proposed Rule on Climate- Related Disclosures for Investors Fact Sheet

April 11, 2022

On March 21, 2022, the U.S. Securities and Exchange Commission (SEC) released its proposed rule, "The Enhancement and Standardization of Climate-Related Disclosures for Investors." [Read the SEC's fact sheet.] The SEC's proposal has been called one of the Biden Administration's key policies to combat the climate crisis.

The proposed rule has no immediate effect. It kicked off a public comment period in that generated the most stakeholder responses ever to an SEC proposed regulation.

If finalized, the proposal would become the first-ever rule requiring all companies, funds, and lenders registered with the SEC to report, measure, and quantify material risks related to climate change in their periodic filings (such as Form 10- K).

A final rule from the SEC has been delayed for months. The delay is reportedly due to concerns that the proposal was too aggressive in its approach requiring disclosures of indirect Scope 3 emissions in a company's "value chain." Litigation against the SEC has also been widely reported as highly probable whenever the Commission releases a final rule. When – or even if – companies must comply with any SEC climate reporting rule thus remains shrouded in uncertainty.

Below is a summary of key takeaways that might be useful as Roundtable members — and their legal, accounting, and environmental experts and consultants — review the SEC's complex, 510— page proposal on climate risk reporting. The Roundtable will prepare a new fact sheet summarizing any SEC final rule whenever it is released.

### Scope 1 & 2 GHG Emissions Disclosures

**SEC registrants would be required to report and quantify Scope 1 and Scope 2 GHG emissions each year. Scope 1 and 2 reporting would require registrants to define and disclose how they determine their "organizational" and "operational" boundaries.**

- Scope 1 and 2 emissions would need to be "disaggregated" and reported separately.
- "Organizational boundaries" for GHG emissions disclosure would track the same "scope of entities... and other holdings" based on the accounting principles that the registrant uses for its "consolidated financial statements."
- "Operational boundaries" would require "identifying emissions sources within [the registrant's] plants, offices, and other facilities that fall within organizational boundaries;" and then "categorizing



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the emissions as either direct or indirect emissions." A registrant should explain its approach and describe its methodology for determining "operational boundaries."

- **The SEC does not specifically address how to bucket Scope 1 and 2 emissions in the building owner- tenant context. General principles on setting "organizational" and "operational" boundaries would need to be consulted in this regard.**
- A registrant would have the discretion to explain and disclose its emissions calculation approach. Examples: emissions per building floor area, kilowatt-hour (kWh) of electricity used, etc.
- A registrant would have the discretion to select emissions factors — and the SEC favorably references those factors published by U.S.-EPA. Whatever emissions factors the registrant decides to use, it must identify the factors and their source.
- A registrant would be able to use publicly-available tools to calculate its emissions. While not mentioned specifically, U.S.-EPA's Portfolio Manager Building Emissions Calculator seems to be the type of tool that the SEC has in mind.

### Scope 3 Reporting

**SEC registrants would report Scope 3 emissions if the company has announced a Scope 3 reduction goal — or if investors would find the registrant's Scope 3 emissions "material."**

- Scope 3 "indirect" emissions definitions follow the World Resources Institute's Greenhouse Gas Protocol "Scope 3" standard. The GHG Protocol is referenced heavily as a non-binding standard throughout the SEC's proposal. The SEC also repeatedly refers to the Task Force on Climate-Related Disclosures (TCFD) as another basis for its proposed emissions reporting framework.
- While the SEC does not propose a quantitative threshold for determining materiality, it "notes that some companies rely on a quantitative threshold, such as 40 percent, when assessing the materiality of Scope 3 emissions."





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- If a registrant determines that its Scope 3 emissions are not “material,” “it may be useful to investors” to explain why the registrant came to that conclusion.
- Under the GHG Protocol as cited in the SEC proposal, a building owner’s “downstream” Scope 3 emissions would include tenant-based Scope 1 and 2 emissions.
- Likewise, if the tenant is a registrant subject to SEC rules, then their “upstream” emissions would include owner-based Scope 1 and 2 emissions.
- “As more companies make their Scope 1 and 2 emissions publicly available, these data can serve as the input for other companies’ Scope 3 calculations.”
- Review the [15 categories of Scope 3 emissions](#) (including employee commuting, business travel, purchased goods, etc.) discussed in the GHG Protocol’s Scope 3 guidance.

### Scope 3 “Safe Harbor”

**With regard to Scope 3 disclosures only, the SEC proposes a “safe harbor” for certain liability under the federal securities laws.**

- Under specific provisions of the proposed rule, “safe harbor” indicates that “disclosure of Scope 3 emissions [by a] registrant would be deemed not to be fraudulent statement” unless it was made “without a reasonable basis or was disclosed other than in good faith.”
- The “safe harbor” extends to “any statement regarding Scope 3 emissions” in a document filed with the SEC under Reg S-K.
- The SEC recognizes the data collection, verification, and other difficulties in estimating emissions up and down a registrant’s supply chain. It thus proposes a “targeted safe harbor for Scope 3 emissions data in light of the unique challenges associated with this information.”

### Third-Party Assurances

**Scopes 1 and 2 disclosures would require independent third-party assurances.**

- As part of the proposed requirements, registrants need to file an “attestation report” for Scopes 1 and 2 disclosures.
- “Limited assurance” is required in the first two years of compliance and scales up to “reasonable assurance” thereafter.



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- "Reasonable assurance" is equivalent to the level of assurance provided in an audit of the financial statements included in a 10-K.
- Scope 3 assurances would be optional.
- Assurances would only be required from "large accelerated filers" and "accelerated filers" (See "compliance" summary below).
- "Attestation report" would need to be prepared and signed by a third-party "attestation provider" who has "significant experience" in GHG measurement and reporting. The provision is modeled after the SEC's existing rules to ensure that auditors reviewing financial statements are independent from their clients.

### Reporting on "Transition Risks"

**Registrants would need to report on "transition risks" such as regulatory compliance costs with federal, state, and local climate laws.**

- While not specifically mentioned by the SEC, "transition risks" would likely encompass the costs and burdens of real estate stakeholders to comply with so-called energy "benchmarking," "building performance standards," and similar laws imposed by state and local governments.
- Other similar risks associated with the potential transition to a cleaner economy would include reduced market demand for carbon-intensive "products," devaluation or abandonment of assets, climate-related litigation risks and fines, and changes in "consumer behavior."
- Transition risk disclosure can also include optional reporting on "climate-related opportunities" such as capital expenditures, costs savings, and "new markets" that arise from energy- and water-efficiency investments; and increased uses of renewable energy; and purchase of renewable energy certificates ("RECs").

### Reporting on "Physical Risks"

**In addition to GHG emissions, registrants would also need to report on material "physical risks" to buildings and other assets posed by climate change. Examples of material "physical risks" mentioned in the SEC's proposal include:**

- Percentage of buildings located in flood hazard areas





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- Potential diminution in value of coastal properties subject to rising sea levels
- Amount of assets (*e.g.*, book value and as a percentage of total assets) in regions of “high” or “extremely high” water stress and scarcity
- Ability of construction laborers to work safely outdoors during heat waves which could delay operations and reduce earnings

### Compliance Timeline

**Compliance would start in 2024 for the biggest registrants and phase-in for other companies.**

- Registrants with a global value of \$700 million or more — “large accelerated filers” — would need to comply first.
  - Compliance for Scope 1 and 2 disclosures for filings in 2024 (covering FY 2023 emissions)
  - Compliance for Scope 3 disclosures for filings in 2025 (covering FY 2024 emissions)
- Registrants with a global value of \$75 million or more up to \$750 million — “accelerated filers” — would need to comply next.
  - Compliance for Scope 1 and 2 disclosures for filings in 2025 (covering FY 2024 emissions)
  - Compliance for Scope 3 disclosures for filings in 2026 (covering FY 2025 emissions)
- Smaller reporting companies have the most time to comply.
  - Compliance with Scope 1 and 2 disclosures for filings in 2026 (covering FY 2025 emissions)
  - Exempt from Scope 3 reporting

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