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The SEC's Climate Disclosure Rules

March 2024

Although mandatory climate-related disclosure faces an uncertain road in the United States, the U.S. Securities and Exchange Commission's (the "**SEC**") adoption of new disclosure rules is potentially a significant milestone in SEC-reporting requirements for public companies.

The final rules, adopted in March 2024, amend Regulation S-K by adding new subpart 1500 prescribing climate-related disclosures in the body of certain SEC filings and amend Regulation S-X by adding new Article 14 to govern climate-related disclosures in the financial statements.

If the rules remain in place, SEC registrants (i.e., SEC-reporting companies and companies filing registration statements) will have to make certain climate-related disclosures, described at a high level in the chart below, in their annual reports and registration statements.

In March 2024, the Fifth Circuit Court of Appeals stayed but then lifted its stay of the rules, following the selection of the Eighth Circuit as the court in which to consolidate the multiple petitions for review of the rules.

The timing, implementation and content of the rules, as well as whether the rules will come into effect at all, are subject to substantial uncertainty. This note discusses the rules as adopted by the SEC, assuming they come into effect as set out by the SEC.

Key differences from other reporting regimes

The SEC's final rules are less onerous than climate-reporting regimes such as the EU's Corporate Sustainability Reporting Directive ("**CSRD**"), the International Sustainability Standards Board ("**ISSB**") and California's climate disclosure legislation. Among other things, the SEC rules:

> do not require Scope 3 greenhouse gas ("**GHG**") emissions disclosure;

> only require certain issuers to make Scope 1 and Scope 2 emissions disclosures, and only if material;

> do not require "double materiality" analysis; and

> focus financial statements disclosure on severe weather events and other natural conditions.

For further details, our global comparison of key sustainability reporting regimes will be available soon.

	Climate-related disclosure requirements
Governance	> Board oversight and management's role.
Strategy	> Climate-related risks that have materially impacted or are reasonably likely to materially impact the registrant, and actual and potential material impacts on strategy, business model and outlook. > Use of transition plans, scenario analysis and internal carbon prices.
Risk management	> Processes for identifying, assessing and managing material climate-related risks.
Targets and goals	> Any climate-related target or goal if it has materially affected or is reasonably likely to materially affect the registrant's business, results of operations, or financial condition. > Use of carbon offsets or renewable energy certificates if material component of plan to achieve targets.
GHG emissions	> Large accelerated filers and accelerated filers must disclose their Scope 1 and Scope 2 emissions, if material, and include attestation reports.
Financial statements	> Focused on expenditures expensed, capitalized costs, losses and charges as a result of severe weather events and other natural conditions.

Who is required to make disclosures?

The SEC's climate-related disclosure rules apply to all registrants, except for asset-backed issuers and Canadian registrants that file on Form 40-F.

Foreign private issuers must comply with the same disclosure requirements as U.S. domestic companies. The SEC considered but opted not to allow foreign private issuers to substitute compliance with the SEC's rules through disclosures made in response to other jurisdictions' requirements. The SEC intends to observe how reporting under other standards develops first.

Although SRCs and EGCs are exempt from the GHG emissions disclosure requirements, they must comply with the other climate-related disclosure rules, including the financial statement requirements.

The rules do not provide an exemption or transitional relief for registrants engaged in an IPO.

A **smaller reporting company** ("**SRC**") is an issuer that has a public float of less than US$250m; or has annual revenues of less than US$100m and either: (i) no public float or (ii) a public float of less than US$700m.

An **accelerated filer** ("**AF**") is a reporting company that has a public float between US$75m and US$700m as of the last business day of its most recently completed second fiscal quarter, has been filing periodic reports for at least 12 months, has previously filed at least one annual report and is not an SRC.

A **large accelerated filer** ("**LAF**") is a reporting company meeting the same conditions as an AF but with a public float of US$700m or more, as of the last business day of its most recently completed second fiscal quarter.

An issuer is an **emerging growth company** ("**EGC**") if it has total annual gross revenues of less than US$1.235bn during its most recently completed fiscal year. It continues to be an EGC for its first five fiscal years after its IPO, unless its total annual gross revenues are US$1.235bn or more; it has issued more than US$1bn in non-convertible debt in the past three years; or it becomes a LAF.

Where and how should the disclosures be made?

In general, disclosures must be made in a registrant's annual report on Form 10-K or 20-F, and in certain registration statements. The disclosures must be "filed" rather than "furnished," subjecting them to potential liability pursuant to Section 18 of the Securities Exchange Act of 1934 (the "Exchange Act") and, if included in or incorporated by reference into a registration statement filed under the Securities Act of 1933 (the "Securities Act"), Section 11 liability as well.

A registrant may, but is not required to, place the subpart 1500 disclosures in a separately captioned "Climate-Related Disclosure" section. The disclosures may also be made in current sections of registration statements or annual reports (e.g., the Risk Factors, Description of Business, or MD&A).

A registrant may also incorporate by reference some of the climate-related disclosures from other registration statements or reports filed under the Exchange Act.

Issuers do not have to include their GHG emissions disclosure in their annual reports when the annual reports are due. Rather, domestic issuers are permitted to disclose their annual GHG emissions in their Form 10-Q for the second fiscal quarter or in an amended annual report on Form 10-K no later than the due date for the second quarter Form 10-Q. Foreign private issuers will have up to 225 days after the end of the fiscal year to amend their Form 20-F to add the disclosure. If the registrant opts to include its GHG emissions disclosure in its amended Form 10-K or 20-F, or in its second quarter 10-Q, the registrant must include an express statement in its annual report indicating its intention in this regard.

GHG emissions metrics must be disclosed in registration statements as of the most recently completed fiscal year that is at least 225 days prior to the date of effectiveness of the registration statement.

When must the disclosures be made?

In the final rules, the SEC provided for phased-in compliance dates dependent upon the status of the registrant and the content of the disclosure, as set out in the chart below (with "FYB" meaning any fiscal year beginning in the calendar year listed). For example, an LAF with a fiscal year beginning on January 1 and ending on December 31 will not have to comply with most of the Regulation S-X and S-K requirements until its annual report for its 2025 fiscal year, filed in 2026. It will not be required to disclose its Scope 1 and/or Scope 2 emissions until its annual report for its 2026 fiscal year, filed in 2027. These emissions disclosures would not be subject to the requirement to obtain limited assurance until the LAF's annual report for its 2029 fiscal year, due in 2030, and would not be subject to the requirement to obtain reasonable assurance until its annual report for its 2033 fiscal year, due in 2034.

Registrant	Reg S-K and S-X disclosure, other than as noted	Material expenditure disclosure	Scope 1 and Scope 2 emissions	Limited assurance	Reasonable assurance	Inline XBRL
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	NA	FYB 2026
SRCs, EGCs and NAFs	FYB 2027	FYB 2028	NA	NA	NA	FYB 2027

Like the TCFD recommendations, subpart 1500 focuses on governance (Item 1501), strategy (Item 1502), risk management (Item 1503) and metrics (Item 1504). The SEC's changes to its originally proposed requirements – generally, to make them less prescriptive and to add materiality qualifiers – underscore that these new items are meant to be disclosure requirements that do not mandate particular governance, strategies or targets. For example, registrants are required to disclose certain transition plans they have adopted to manage material transition risk and scenario analyses, but the rules do not require them to adopt transition plans or use scenario analyses. The final rules are also designed to give registrants more flexibility in tailoring responsive disclosure to their particular facts and circumstances.

Governance

Item 1501 requires the following disclosure about a registrant's governance of climate-related risks:

- **Board of directors** – Registrants must describe board oversight of climate-related risks.
  - If applicable, they must identify any board committee or subcommittee responsible for the oversight of climate-related risks and the processes by which the board or the committee or subcommittee is informed about such risks.
  - If there is a climate-related target or goal or transition plan disclosed, registrants must describe whether and how the board oversees progress against the target or goal or transition plan.

> The climate-related governance disclosure requirements are similar to those in the SEC's recently adopted cybersecurity disclosure requirements. As with the cybersecurity rules, the SEC decided not to adopt the proposed requirement that specific board members be identified for their expertise.

- **Management** – Registrants must describe management's role in assessing and managing their material climate-related risks. Registrants should address, as applicable, the following non-exclusive list of disclosure items:
  - Whether and which management positions or committees are responsible for assessing and managing climate-related risks and the relevant expertise of such position holders or committee members in such detail as necessary to fully describe the nature of the expertise;
  - The processes by which such positions or committees assess and manage climate related risks; and
  - Whether such positions or committees report information about such risks to the board of directors or a committee or subcommittee of the board of directors.

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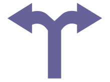
What are climate-related risks?

Item 1500 defines "climate-related risks" as the actual or potential negative impacts of climate-related conditions and events on a registrant's business, results of operations or financial condition.

> The SEC removed the reference to negative climate-related impacts on a registrant's "value chain" from the proposed definition of climate-related risks. However, the SEC also said that such value-chain risks should be disclosed if they were material to the registrant.

Climate-related risks include the following:

- **Physical risks** include both acute risks and chronic risks to the registrant's business operations. **Acute risks** are event-driven and may relate to shorter-term severe weather events, such as hurricanes, floods, tornadoes and wildfires, among other events. **Chronic risks** relate to longer term weather patterns, such as sustained higher temperatures, sea level rise and drought, as well as related effects such as decreased arability of farmland, decreased habitability of land and decreased availability of fresh water.
- **Transition risks** are the actual or potential negative impacts on a registrant's business, results of operations or financial condition attributable to regulatory, technological and market changes to address the mitigation of, or adaptation to, climate-related risks, including such nonexclusive examples as increased costs attributable to changes in law or policy, reduced market demand for carbon-intensive products leading to decreased prices or profits for such products, the devaluation or abandonment of assets, risk of legal liability and litigation defense costs, competitive pressures associated with the adoption of new technologies, and reputational impacts (including those stemming from a registrant's customers or business counterparties) that might trigger changes to market behavior, consumer preferences or behavior, and registrant behavior.



Strategy

Item 1502 requires registrants to make the following strategy disclosures:

> **Climate-related risks** – Describe climate-related risks that have materially impacted or are reasonably likely to have a material impact on the registrant, including describing whether each risk is reasonably likely to manifest in the short term (i.e., next 12 months) or long term (i.e., beyond the next 12 months).

The TCFD recommends the disclosure of whether risks are reasonably likely to manifest in the short, medium or long term, but the SEC chose to focus the disclosure on short- and long-term risks, consistent with the temporal standards in the MD&A. However, a registrant may break down its description of risks into medium- and long-term risk, if that is consistent with its assessment and management of the climate-related risk.

> **Physical vs transition risk** – Describe whether the risk is a physical or transition risk, providing information necessary to an understanding of the nature of the risk presented and the extent of the registrant's exposure to the risk, including the following non-exclusive list of disclosures, as applicable:
> > 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.
> > 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. A registrant that has significant operations in a jurisdiction that has made a GHG emissions reduction commitment should consider whether it may be exposed to a material transition risk related to the implementation of the commitment.

> **Impact on strategy** – Describe the actual and potential material impacts of the disclosed climate-related risks on the registrant's strategy, business model and outlook, risk, including the following non-exclusive list of disclosures, as applicable:
> > Business operations, including the types and locations of its operations;
> > Products or services;
> > Suppliers, purchasers, or counterparties to material contracts, to the extent known or reasonably available;
> > Activities to mitigate or adapt to climate-related risks, including adoption of new technologies or processes; and
> > Expenditure for research and development.

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> **Integration into strategy** – Describe whether and how the registrant considers any such disclosed impacts as part of its strategy, financial planning, and capital allocation, including, as applicable:
> > Whether the impacts of the described climate-related risks have been integrated into the registrant's business model or strategy, including whether and how resources are being used to mitigate climate-related risks; and
> > How any targets or transition plans required to be disclosed under the rules relate to the registrant's business model or strategy.

The final rule limits the scope of this specific topic to include only material impacts on the registrant's suppliers, purchasers, or counterparties to material contracts and further limits the information that should be disclosed about those impacts to information that is known or is reasonably available.

> **Impact on business and mitigation activities** – Discuss how any disclosed climate-related risks have materially impacted or are reasonably likely to materially impact the registrant's business, results of operations, or financial condition, including quantitative and qualitative disclosure of material expenditures incurred and material impacts on financial estimates and assumptions that in management's assessment, directly result from activities to mitigate or adapt to climate-related risks.

Item 1502 also requires registrants to make the following strategy-related disclosures:

- **Transition plans** – If the registrant has adopted a transition plan manage a material transition risk, describe the plan, including quantitative and qualitative disclosure of material expenditures incurred and material impacts on financial estimates and assumptions directly resulting activities to mitigate or adapt to climate-related risks. Registrants must update their annual report disclosure about the transition plan each fiscal year by describing any actions taken during the year under the plan, including how such actions have impacted the registrant's business, results of operations or financial condition.

When considering the qualitative and quantitative analysis of material expenditures resulting from a transition plan or directly resulting from targets or goals, registrants must also consider the aggregate expenditure of specific actions.

- **Scenario analysis** – If the registrant is using scenario analysis to assess the impact of climate-related risks on its business, results of operations or financial condition, and if, based on the results on such scenario analysis, the registrant determines that a climate-related risk is reasonably likely to materially impact it, the registrant must describe the scenario analysis, including parameters, assumptions and expected material impacts.

Companies with experience using scenario analysis will need to consider the appropriate level of disclosure, as the SEC indicated that it would expect more quantitative disclosure as scenario analysis becomes more sophisticated.

- **Internal carbon pricing** – If the registrant uses an internal carbon price that is material to how it evaluates and manages its disclosed climate-related risk, disclose:
  - The price per metric ton of CO_2e; and
  - The total price, including how the total price is estimated to change over the short term and long term, as applicable.

  If a registrant uses more than one internal carbon price to evaluate and manage a material climate-related risk, it must provide the disclosures required by this section for each internal carbon price and disclose its reasons for using different prices.

  If the scope of entities and operations involved in the use of the described internal carbon price is materially different from the organizational boundaries used for the purpose of calculating a registrant's GHG emissions, the registrant must briefly describe this difference.

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A **transition plan** is a registrant's strategy and implementation plan to reduce climate related risks, which may include a plan to reduce its GHG emissions in line with its own commitments or commitments of jurisdictions within which it has significant operations.

Scenario analysis means a process for identifying and assessing a potential range of outcomes of various possible future climate scenarios, and how climate-related risks may impact a registrant's business strategy, results of operations, or financial condition over time.

Internal carbon price means an estimated cost of carbon emissions used internally within an organization.

Organizational boundaries means the boundaries that determine the operations owned or controlled by a registrant for the purpose of calculating its GHG emissions.

Risk management

Item 1503 requires registrants to describe any processes for identifying, assessing and managing material climate-related risks. Registrants should address, among other things, how they:

> Identify whether they have incurred or are reasonably likely to incur material physical or transition risk;

> Decide whether to mitigate, accept or adapt to a particular risk; or

> Prioritize whether to address the climate-related risk.

If managing a material climate-related risk, registrants must also disclose whether and how any processes described pursuant to the requirements above have been integrated into their overall risk management system or processes.

Targets and goals

Item 1504 requires a registrant to disclose any climate-related target or goal if such target or goal has materially affected or is reasonably likely to materially affect the registrant's business, results of operations or financial condition.

The requirement to disclose climate-related targets or goals if they have materially affected or are reasonably likely to materially affect the business, results of operations or financial condition applies even if the target or goal has not previously been made public by the registrant or adopted by the board or CEO.

If disclosing targets or goals, registrants must provide any additional information or explanation necessary to an understanding of the material impact or reasonably likely material impact of the target or goal, including, as applicable, but not limited to a description of:

> The scope of activities included in the target;

> The unit of measurement;

> The defined time horizon by which the target is intended to be achieved, and whether the time horizon is based on one or more goals established by a climate-related treaty, law, regulation, policy, or organization;

> If the registrant has established a baseline for the target or goal, the defined baseline time period and the means by which progress will be tracked; and

> A qualitative description of how the registrant intends to meet its climate-related targets or goals.

The final rules do not include "emissions" in the list of information that must be disclosed if necessary to an understanding of the material impact or reasonably likely material impact of a target or goal. But if a registrant has set a material target or goal to reduce emissions, it will be required to disclose this when explaining the scope of activities included in the target.

Registrants must also disclose any progress made toward meeting the target or goal and how any such progress has been achieved. This disclosure must be updated every year by describing the actions taken during the year toward meeting the target or goal.

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Quantitative and qualitative analysis

The disclosure must include a discussion of any material impacts to the registrant's business, results of operations, or financial condition as a direct result of the target or goal or the actions taken to make progress toward meeting the target or goal. It must also include quantitative and qualitative disclosure of any material expenditures and material impacts on financial estimates and assumptions as a direct result of the target or goal or the actions taken to make progress toward meeting the target or goal.

Carbon offsets or RECs

Section 1504 also requires disclosure about the use of carbon offsets or renewable energy credit or certificate ("REC") if they constitute a material component of a registrant's plan to achieve its climate-related targets or goals. A REC is a credit or certificate representing each megawatt-hour (1 MWh or 1,000 kilowatt-hours) of renewable electricity generated and delivered to a power grid.

Registrants must separately disclose the amount of carbon avoidance, reduction or removal represented by the offsets or the amount of generated renewable energy represented by the RECs, 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.

The level of GHG emissions reporting is one of the key differences between the SEC's final rules and the TCFD recommendations, and the requirements of the ISSB and the EU CRSD. The SEC had originally proposed requiring certain issuers to disclose their Scope 3 GHG emissions, and requiring all issuers to disclose Scope 1 and Scope 2 GHG emissions. The final rules, however, limit the Scope 1 and Scope 2 GHG reporting requirements to certain registrants and do not mandate any Scope 3 GHG emissions reporting.

Scope 1 emissions are direct GHG emissions from operations that are owned or controlled by a registrant.

Scope 2 emissions are indirect GHG emissions from the generation of purchased or acquired electricity, steam, heat, or cooling that is consumed by operations owned or controlled by a registrant.

Scope 3 emissions are all indirect GHG emissions not otherwise included in a registrant's Scope 2 emissions, which occur in the upstream and downstream activities of a registrant's value chain.

Item 1505 requires registrants that are LAFs or AFs to disclose their Scope 1 emissions and/or Scope 2 emissions, if such emissions are material. Smaller reporting companies and emerging growth companies are exempt.

If a registrant's Scope 1 emissions are material but its Scope 2 emissions are not, then the registrant must disclose its Scope 1 emissions but it is not required to disclose its Scope 2 emissions (and vice versa).

The disclosures must cover their most recently completed fiscal year and, to the extent previously disclosed in an SEC filing, the historical fiscal year(s) included in the consolidated financial statements in the filing.

The Scope 1 and 2 emissions must be disclosed separately, in terms of CO_2e. Emissions must be disclosed in the aggregate; however, if any constituent gas of the disclosed emissions is individually material, the registrant must disclose such constituent gas disaggregated from the other gases.

The registrant must also disclose Scope 1 and/or Scope 2 emissions in gross terms by excluding the impact of any purchased or generated offsets, which must be disclosed separately.

The extent to which a registrant will exclude RECs from its gross emissions will depend on the methodology it uses. One of two common methods for calculating Scope 2 emissions, the market-based method, may involve the use of RECs. A registrant is required to describe its methodology, and in the case of Scope 2 emissions, it should include a description of whether and how RECs factor into its gross emissions calculation.

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Registrants must describe the methodology, significant inputs, and significant assumptions used to calculate their disclosed GHG emissions. The description must include:

> The organizational boundaries used when calculating the disclosed GHG emissions, including the method used to determine those boundaries. If the organizational boundaries materially differ from the scope of entities and operations included in the registrant's consolidated financial statements, the registrant must provide a brief explanation of this difference in sufficient detail for a reasonable investor to understand;

> A brief discussion of the operational boundaries used, including the approach to categorization of emissions and emissions 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 may be used to disclose GHG emissions as long as the registrant also describes the underlying assumptions and its reasons for using the estimates.

To the extent Scope 1 and/or 2 emissions disclosure are required, the SEC acknowledges that Exchange Act Rule 12b-21, which provides accommodations for information that is unknown and not reasonably available, would be available if the following conditions are met:

> The registrant gives such information on the subject as it possesses or can acquire without unreasonable effort or expense, together with the sources thereof; and

> The registrant includes a statement either showing that unreasonable effort or expense would be involved or indicating the absence of any affiliation with the person within whose knowledge the information rests and stating the result of a request made to such person for the information.

Attestation requirements

AFs and LAFs required to disclose Scope 1 and/or Scope 2 emissions must obtain an assurance report at the "limited assurance" level, beginning with the third fiscal year after the compliance date for their disclosure of GHG emissions (as set out on page 2). LAFs required to disclose Scope 1 and/or Scope 2 emissions must obtain an assurance report at the "reasonable assurance" level beginning with the seventh fiscal year after the compliance date for the disclosure of GHG emissions (as set out on page 2).

The attestation report must be provided pursuant to standards that are publicly available at no cost or that are widely used for GHG emissions assurance and established by a body or group that has followed due process procedures, including the broad distribution of the framework for public comment.

The attestation report must be prepared and signed by a GHG emissions attestation provider. The provider must be:

> An expert in GHG emissions by virtue of having "significant experience" in measuring, analyzing, reporting or attesting to GHG emissions; and

> Independent with respect to the registrant and any of its affiliates during the attestation and professional engagement period.

The provider is not independent if it is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that it is not, capable of exercising objective and impartial judgment on all issues encompassed within the attestation provider's engagement.

In determining whether an attestation provider is independent, the SEC will consider:

> Whether a relationship or the provision of a service creates a mutual or conflicting interest between the attestation provider and the registrant (or any of its affiliates), places the attestation provider in the position of attesting to such attestation provider's own work, results in the attestation provider acting as management or an employee of the registrant (or any of its affiliates), or places the attestation provider in a position of being an advocate for the registrant (or any of its affiliates); and

> All relevant circumstances, including all financial or other relationships between the attestation provider and the registrant (or any of its affiliates), and not just those relating to reports filed with the SEC.

It would be difficult for an expert that has assisted a registrant in calculating or preparing its GHG emissions data to meet the independence requirements. However, registrants should be able to use their financial statement auditor as their GHG emissions attestation provider consistent with the independence requirement in the final rules.

The attestation report covering GHG emissions at a limited assurance level and any description of the assurance regarding the GHG emissions disclosure will not be considered part of the registration statement and not subject to strict liability under Securities Act Section 11 for material misstatements and omissions. The exemption from liability does not apply to attestation engagements performed at a reasonable assurance level.

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Liability for climate-related disclosures

The final rules provide protection for certain climate-related disclosures under the safe harbors for forward-looking statements established by the Private Securities Litigation Reform Act of 1995 ("PSLRA").

Under Item 1507, disclosures other than historical facts regarding transition plans (Item 1502(e)), scenario analysis (Item 1502(f)), internal carbon pricing (Item 1502(g) and targets and goals (Item 1504) will be deemed forward-looking statements under the safe harbors, as long as the other safe harbor conditions are met (such as being accompanied by meaningful cautionary language).

Further, such climate-related statements made by issuers and/or in connection with transactions currently excluded from the PSLRA statutory safe harbor – including IPOs and offerings by blank check companies – will be eligible for the safe harbor.

However, the final rules' forward-looking safe harbor will not be available for statements consisting solely of historical fact, such as information related to carbon offsets or RECs described pursuant to Item 1504 (Targets and goals). The SEC also expressly declined to include the Scope 1 and Scope 2 emissions disclosures within the scope of any safe harbor.

The PSLRA safe harbor also does not apply to forward-looking statements included in financial statements prepared in accordance with GAAP. In addition, any forward-looking statements that are incorporated by reference from the financial statements into a registrant's subpart 1500 disclosures will not be eligible for the Item 1507 safe harbor.

In *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, the Supreme Court is expected to decide soon if the failure to disclose a "known trend or uncertainty" under Item 303 of Regulation S-K can support a claim under Section 10(b) of the Exchange Act. As the SEC noted in its adopting release, registrants may have an obligation to discuss climate-related information in MD&A if the information meets the requirements for disclosure under Item 303 of Regulation S-K.

XBRL

Both the narrative and quantitative climate-related disclosures must be electronically tagged in Inline eXtensible Business Reporting Language ("Inline XBRL"). Registrants will have to comply with the Inline XBRL requirements on a phased basis, as set out on page 2.

In Article 14 of Regulation S-X, the SEC chose to narrow the climate-related financial statement disclosure requirements compared to what it had proposed, focusing on requiring disclosures relating to severe weather events and other natural conditions, carbon offsets and RECs. Notably, Article 14 only requires disclosure of income statement and balance sheet impacts, and not impacts on registrants' cash flows.

"Severe weather events and other natural conditions" include hurricanes, tornadoes, flooding, drought, wildfires, extreme temperatures and sea level rises. The list is non-exclusive and meant to allow flexibility for registrants to determine which severe weather events and other natural conditions affect them in light of their particular facts and circumstances.

Registrants must include the financial statement disclosures in any filing that is required to include disclosure pursuant to subpart 1500, even if it does not have information to disclose pursuant to subpart 1500, and that also requires the registrant to include its audited financial statements.

Expenditure effects

Article 14 requires the following financial statement disclosures:

> **Expenditure expenses and losses** – A registrant must disclose the aggregate amount of expenditures expensed and losses, excluding recoveries, incurred as a result of severe weather events and other natural conditions, if the aggregate amount of such expenditures expensed and losses is 1% or more of the absolute value of income or loss before income tax expense. No disclosure is required if the amount is less than US$100,000 for the relevant fiscal year. The registrant must separately identify where the expenditures expensed and losses are presented in the income statement.

> **Capitalized costs and charges** – A registrant must disclose the aggregate amount of capitalized costs and charges, excluding recoveries, incurred as a result of severe weather events or other natural conditions, if the aggregate amount of the absolute value of capitalized costs and charges incurred is 1% or more of the absolute value of shareholders' equity or deficit. No disclosure is required if the amount is less than US$500,000 for the relevant fiscal year. The registrant must separately identify where the capitalized costs and charges are presented in the balance sheet.

> **Carbon offsets or RECs** – If carbon offsets or RECs have been used as a material component of its plans to achieve its disclosed climate-related targets or goals, the registrant must disclose the aggregate amount of carbon offsets and RECs expensed, the aggregate amount of capitalized carbon offsets and RECs recognized, and the aggregate amount of losses incurred on the capitalized carbon offsets and RECs, during the fiscal year. The registrant must also disclose the beginning and ending balances of the capitalized carbon offsets and RECs for the fiscal year and separately identify where the expenditures expensed, capitalized costs, and losses are presented in the income statement and the balance sheet.

The final rules include an attribution principle that limits the required disclosure to circumstances where the severe weather event or other natural condition was a "significant contributing factor" in incurring the capitalized cost, expenditure expensed, charge, or loss.

The attribution principle applicable does not apply to the expenditure disclosure required by subpart 1500.

Regulation S-X

Article 14 Disclosure of Severe Weather Events and Other Information.

§ 14-01 Instructions related to disclosure of severe weather events and other information.

§ 14-02 Disclosures related to severe weather events and other information.

Financial estimates

Registrants must also disclose whether the estimates and assumptions used to produce the consolidated financial statements were materially impacted by exposures to risks and uncertainties associated with, or known impacts from, severe weather events and other natural conditions, or any disclosed climate-related targets or transition plans. If so, they must provide a qualitative description of how the development of estimates and assumptions were impacted by such events, conditions, targets, or transition plans.

Contextual information

Article 14 also requires the disclosure of contextual information, describing how each specified disclosed financial statement effect was derived, including a description of significant inputs and assumptions used, significant judgments made, other information that is important to understand the financial statement effect and, if applicable, policy decisions made by the registrant to calculate the specified disclosures.

Periods required to be presented

Disclosure must be provided for the registrant's most recently completed fiscal year, and to the extent previously disclosed or required to be disclosed, for the historical fiscal year(s), for which audited consolidated financial statements are included in the filing. For example, subject to the compliance date, a registrant that files its annual report will only be required to provide the applicable disclosure for the registrant's most recently completed fiscal year for which audited financial statements are included in the filing. For each subsequent fiscal year's annual report, the registrant will be required to provide the applicable disclosure for an additional fiscal year until the required disclosure is provided for the entire period covered by the registrant's financial statements.

Due to the SEC requiring Article 14 disclosure on a prospective basis only, ultimately a registrant that is required to include balance sheets as of the end of its two most recent fiscal years and income statements as of the end of its three most recent fiscal years would be required to disclose two years of the financial statement effects that correspond to the balance sheet and three years of the financial statement effects that correspond to the income statement.

Keep on top of legal developments

The Fifth Circuit stayed and then lifted its stay of the rules following the selection of the Eighth Circuit as the court in which to consolidate the multiple petitions for review of the rules brought by several different coalitions of U.S. states, energy companies and the Sierra Club. The petitioners have asked the Eighth Circuit to issue a stay as well. There are likely to be multiple legal decisions over the rules, and registrants should make sure they understand how the decisions affect compliance with the rules.

Think carefully about how to manage disclosure in different jurisdictions

Many registrants that will have to comply with the SEC's rules will also be subject to the climate disclosure rules of another jurisdiction, such as the EU CSRD, which requires certain large and listed companies and other entities, including non-EU entities, to report on sustainability-related issues in line with the European Sustainability Reporting Standards ("ESRS"). The SEC estimates that about 70 SEC registrants will likely be subject to reporting under the initial set of ESRS in fiscal year 2024, and that many of the 3,700 SEC registrants (including a number of U.S. domestic companies) that trade on a European exchange will be subject to CSRD reporting once it is fully implemented. Further, other jurisdictions, including the UK, Australia, Canada, Hong Kong, Japan and Singapore, have also announced plans to adopt some form of climate disclosure regime. And while also subject to legal challenge (and budget problems), California's new climate disclosure rules require certain large U.S. public and private companies that conduct business in California to make climate-related disclosures that generally exceed those required under the new SEC rules.

Since the SEC has not provided for substituted compliance, issuers subject to another reporting regime will need to consider whether to include all of their home jurisdiction climate disclosures in their annual reports on Form 20-F. On the one hand, companies want to provide investors in all their reporting jurisdictions with the same or similar information. On the other hand, including climate-related disclosures that are not required by the SEC rules – such as Scope 3 emissions or immaterial Scope 1 and Scope 2 emissions – subjects companies to U.S. securities law liability for those disclosures and could cause confusion.

Don't forget about ICFR

The new Regulation S-X disclosure requirements implicate internal controls over financial reporting and other Sarbanes-Oxley considerations, and registrants should consider how and when they begin preparing for these disclosures in consultation with their auditors.

Focus on materiality

In the adopting release, the SEC makes clear that it is focused on material climate-related risks, and it added a number of materiality qualifiers to its proposed requirements, including to the Scope 1 and Scope 2 emissions disclosure requirements.

What is "material"?

Under the final rules, many disclosures are only required if "material." Under the U.S. federal securities laws, information is material if there is a substantial likelihood that a reasonable investor would consider the information important in deciding how to make an investment decision. In relation to an omission of information, such information is material if there is a substantial likelihood that disclosure of the omitted facts would have been viewed by the reasonable investor as having significantly altered the "total mix" of information available.

Even though the SEC ultimately chose not to require certain specific disclosures (such as of climate-related opportunities), it emphasized that companies are still subject to a fundamental obligation not to make materially misleading statements or omissions and may need to provide additional information to keep disclosures from being misleading.

The materiality analysis can be particularly difficult where another jurisdiction applies a different materiality rule with respect to certain climate-related disclosures (such as the "double materiality" concept under the CSRD) or mandates certain disclosures without a materiality qualifier. Disclosure of the same information mandated by another reporting regime in SEC filings risks confusing investors with respect to what is material to the company under U.S. law.

Remember attestation report providers must be independent

While some of the SEC's reporting deadlines are still some time away and the potential for delay, alteration or invalidation of the rules is very real, it is worth getting an early start with compliance, particularly if an attestation report will be required, as there may be a limited number of attestation report providers and they are likely to be incredibly busy as the compliance deadlines approach. Companies that already have an attestation provider (an estimated 40% of Russell 1000 Index companies obtained third party assurance for their sustainability reports in 2022) should ensure that their providers satisfy the SEC's independence and other requirements.

Among other things, the attestation provider cannot be in the position of attesting to such attestation provider's own work. Thus, it would be difficult for an expert that helped prepare a registrant's GHG emissions data to meet the SECs independence requirements.

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