SEC on Climate

SEC mandates climate disclosures and assurance

March 7, 2024

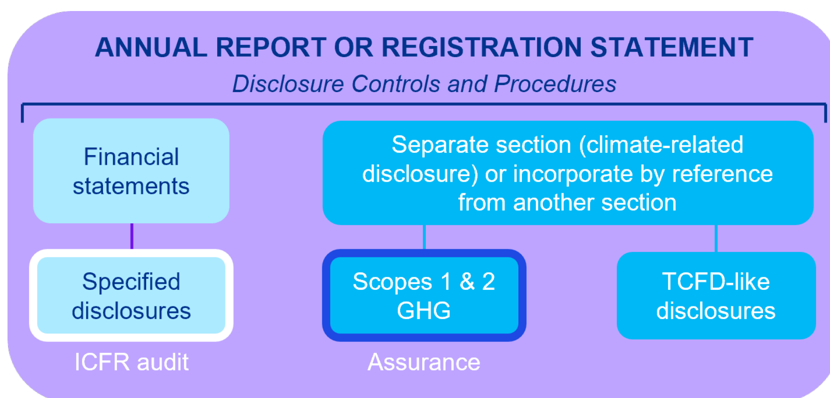
The SEC has responded to concerns while crafting meaningful disclosures for investors.

Source and applicability

- SEC Release Nos. 33-11275; 34-99678, The Enhancement and Standardization of Climate-Related Disclosures for Investors
- Registrants with Exchange Act reporting obligations pursuant to Exchange Act Section 13(a) or Section 15(d), and companies filing a Securities Act or Exchange Act registration statement; *including* foreign private issuers; *excluding* Canadian issuers reporting under the Multijurisdictional Disclosure System and asset-backed issuers.

Fast facts, impacts

The following is a general representation of the required disclosures and their placement in the annual report or registration statement, which are explained throughout this Defining Issues.



- An audit of internal control over financial reporting (ICFR) is not required for all registrants.
- Greenhouse gas (GHG) emissions disclosures (and assurance thereon) are not required for all registrants.
- TCFD is the Task Force on Climate-related Financial Disclosures.

The earliest compliance date is the fiscal year beginning in calendar year 2025 for large accelerated filers. Registrants will first be required to present the financial statement disclosures and most climate risk disclosures; other disclosures, including GHG emissions, follow one year later and assurance on GHG emissions three years after that. Other filers trail by one to two years to the extent requirements apply.

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Background

In 2010 the SEC published guidance on climate-related disclosures, which has driven its expectations of registrants' disclosures in the years that followed. That guidance includes disclosure reminders outside the scope of the newly issued climate rule (e.g. related to risk factors) and will remain in effect.

The specific events that culminated in adoption of the climate rule on March 6, 2024, began in March 2021 when the SEC requested public input on climate-related disclosures to help evaluate its then current rules and guidance. This was followed in March 2022 by issuance of the SEC's proposed climate reporting rules. Over the last two years, the SEC considered more than 4,500 unique comment letters (over 20,000 letters in total) as it drafted its final rules.

Components of the disclosures

As highlighted in the diagram on page 1, there are two distinct components to the disclosures.

- Reg S-X financial statement disclosures, which will be part of the audited financial statements and therefore in the scope of the registrant's internal control over financial reporting.
- Reg S-K climate-related disclosures in the registrant's annual report or registration statement. These disclosures can be included in a separately captioned 'Climate-Related Disclosure' section of the annual report or registration statement, or incorporated by reference from another section. The disclosures can also be incorporated by reference from another filing, subject to certain conditions.

The two sets of disclosures are connected because the Reg S-K disclosures require quantitative and qualitative disclosure of any material expenditures incurred and material impacts on financial estimates and assumptions that directly result from certain items. See section, Specific quantitative disclosures.

Financial statement disclosures require disaggregation

Certain disclosures are required in a note to the financial statements for the registrant's most recent fiscal year. The disclosures relate to:

- severe weather events and other natural conditions, which are not defined terms; and
- carbon offsets or renewable energy credits or certificates (RECs).

The following table summarizes the disclosures and when they are required. For each financial statement effect disclosed, the registrant describes appropriate contextual information, such as significant inputs and assumptions used, and significant judgments made; and provides certain specific disclosures if applicable, such as any recoveries recognized and accounting policies for offsets and RECs.

Severe weather events / natural conditions	Disclosure threshold
Expenditures	
• Disclose the aggregate amount of expenditures expensed as incurred and losses (excluding recoveries) on an absolute value basis. • Separately identify where the expenditures are presented in the income statement.	• Required if the aggregate amount of expenditures expensed as incurred and losses is ≥ 1% of the absolute value of income or loss before income tax expense or benefit for the relevant fiscal year. • However, if the aggregate amount for the fiscal year is < $100,000, no disclosure is required.

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Severe weather events / natural conditions	Disclosure threshold
Capitalized costs	
• Disclose the aggregate amount of capitalized costs and charges (excluding recoveries) on an absolute value basis. • Separately identify where the capitalized costs are presented in the balance sheet.	• Required if the aggregate amount of capitalized costs and charges is ≥ 1% of the absolute value of stockholders' equity or deficit at the end of the relevant fiscal year. • However, if the aggregate amount for the fiscal year is < $500,000, no disclosure is required.
Financial estimates / assumptions	
Qualitatively describe how any of the following materially impacted estimates and assumptions that are used to produce the consolidated financial statements: • severe weather events and other natural conditions; or • any climate-related targets or transition plans disclosed by the registrant.	Required if material.
Carbon offsets and RECs	**Disclosure threshold**
• Disclose the aggregate amount of carbon offsets and RECs expensed, the amount capitalized and any losses thereon. • Separately identify where the amounts expensed, capitalized costs and losses are presented in the financial statements. • Disclose the beginning and ending balances of the capitalized carbon offsets and RECs for the fiscal year.	Required if the use of carbon offsets or RECs is a material component of the registrant's plans to achieve its disclosed climate-related targets or goals.

The final rules introduce an attribution principle, which uses the concept of 'significant contributing factor' to determine amounts required to be disclosed. In essence, if a severe weather event or other natural condition is determined to be a significant contributing factor in incurring the cost, expenditure, charge, loss or recovery, the entire amount of the expenditure or recovery is included in the financial statement disclosure calculation.

The attribution principle simplifies the determination of the amount required to be disclosed by eliminating the need to allocate portions of costs and expenditures. The determination of significance is expected to be consistent with that applied under the registrant's GAAP.

Climate risk disclosures follow consistent structure

The climate risk disclosures outside of the financial statements are arranged under the broad categories of governance, strategy and risk management, which is consistent with the structure in the SEC's recent rule on cybersecurity reporting and disclosures; read our Defining Issues.

In addition, these categories will be familiar to registrants who follow the recommendations of the TCFD, albeit the disclosures are not as extensive as those of the TCFD.

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The following tables highlight some of the key disclosures required.

◆ Indicates disclosures that require forward-looking statements. The climate rules provide a safe harbor from certain forms of liability in connection with making these disclosures, provided all applicable conditions are met.

■ Indicates certain quantitative and qualitative disclosures that have a longer phase-in to compliance. See section, Specific quantitative disclosures.

Governance and risk management processes	• Disclose the board's oversight of climate-related risks and, if applicable, identify the (sub)committee responsible for such oversight and describe the process by which the board or such (sub)committee is informed about such risks. • Describe management's role in assessing and managing material climate-related risks, and the relevant expertise of such individuals. • Disclose the registrant's process for identifying, assessing and managing climate-related risks and integration into its overall risk management system or processes.
Strategy, business model and outlook	• Disclose any climate-related risks that have materially impacted or are reasonably likely to have a material impact in the short-term (the next 12 months) and long-term (>12 months) – including on the registrant's strategy, results of operations or financial condition. • Include in these disclosures information about physical and transition risks.
Scenario analysis ◆	If the registrant concludes that a climate-related risk is reasonably likely to have a material impact by using scenario analysis, describe the scenarios, parameters and assumptions used, analytical choices made and any expected material impacts, including financial impacts, on the registrant under each relevant scenario.
Carbon offsets or RECs	If the registrant uses carbon offsets or RECs as a material part of its plan to achieve climate-related targets or goals, disclose certain information about the amount of carbon avoidance, reduction or removal represented by the offsets or the amount of renewable energy generated by the RECs.
Internal carbon pricing ◆	If the registrant uses internal carbon pricing and considers it material to how it evaluates and manages climate-related risks, disclose certain information about its pricing, including the price in units of its reporting currency per metric ton of carbon dioxide equivalent.

In addition, registrants will need to disclose the following information associated with transition plans and targets or goals they have set.

Climate risk mitigation, adaptation ■	Disclose whether and how the registrant considers any climate-related risks as part of its business model, strategy, financial planning and capital allocation.
Transition plans ◆■	If the registrant has adopted a transition plan, disclose a description of its plan, including the relevant metrics and targets used to identify and manage physical and transition risks.
Targets and goals ◆ ■	Disclose information about any climate-related targets or goals that have materially affected or are reasonably likely to materially affect the registrant. Include the scope of activities included in the target, unit of measurement, any established baseline, time horizon and progress to date.

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	Discussion is also required for any material impacts to the registrant from: • the targets or goals; or • any actions taken to make progress toward achieving the targets or goals.

Specific quantitative disclosures

The above disclosures denoted with ■ require quantitative and qualitative disclosure of any material expenditures incurred and material impacts on financial estimates and assumptions that directly result from the registrant's:

- activities to mitigate or adapt to climate-related risks;
- transition plan; and
- targets or goals, or actions taken to make progress toward achieving those targets or goals.

Registrants have an extra year to comply with these disclosures; see Phased transition.

Flexibility in measuring scopes 1 and 2 GHG emissions

Large accelerated filers and accelerated filers (except for smaller reporting companies and emerging growth companies) are required to disclose gross scope 1 and/or scope 2 GHG emissions, if material. The disclosures are presented outside of the financial statements (see diagram on page 1), and comparative information is required only to the extent it was previously disclosed in filings.

Scope 1	Scope 2
Direct GHG emissions from operations that are owned or controlled by the registrant.	Indirect GHG emissions from the generation of purchased or acquired electricity, steam, heat or cooling that is consumed by operations owned or controlled by the registrant.

The rules do not prescribe a specific approach to be followed, instead requiring the registrant to describe the methodology, significant inputs and significant assumptions used to calculate GHG emissions, including the:

- organizational boundaries;
- operational boundaries; and
- protocol or standard used, with details about the calculation approach, data and tools.

In our experience, the most commonly used reference point currently for the calculation of GHG emissions is the standards and guidance of the GHG Protocol. This is acknowledged in the rules, and the above scope definitions are substantially the same as those of the GHG Protocol. Therefore, a registrant currently following the GHG Protocol could continue doing so, including using operational control to determine its organizational boundary. For further discussion and to learn more about the GHG Protocol, see KPMG Handbook, GHG emissions reporting.

The registrant may use reasonable estimates when disclosing GHG emissions, as long as it describes the underlying assumptions and explains its reasons for using the estimates.

Attestation

Scopes 1 and 2 GHG emissions will be subject to assurance. Limited assurance will be required three years after the disclosures are first required. For large accelerated filers only, reasonable assurance will be required four years later (a total of seven years after disclosures are required). See Phased transition.

The rules require the registrant to include an attestation report provided pursuant to attestation standards that (1) are publicly available or widely used for GHG emissions assurance, and (2) were established by a

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body or group that has followed due process procedures – e.g. the AICPA attestation standards or assurance standards issued by the IAASB.

The registrant must disclose additional information such as whether the attestation provider is subject to oversight inspections and whether there has been a change in attestation provider. The attestation provider needs to have significant experience relevant to GHG emissions and be independent of the registrant and its affiliates.

Additional disclosures are required for registrants that voluntarily obtain assurance over GHG emissions after the compliance date – e.g. an accelerated filer voluntarily obtains reasonable assurance or a non-accelerated filer voluntarily obtains assurance over voluntarily disclosed GHG emissions.

Disclosure relief

If the registrant's GHG emissions disclosures are not included in the annual report on Form 10-K or Form 20-F, the disclosures may be either:

1. incorporated by reference from the registrant's Form 10-Q (for domestic registrants) for the second fiscal quarter in the fiscal year immediately following the year to which the GHG emissions disclosures relate; or

2. included in an amended annual report on Form 10-K or Form 20-F no later than the due date for the Form 10-Q described in (1), or 225 days after the end of the fiscal year to which the GHG emissions relate for foreign private issuers using foreign filing forms.

When taking advantage of this relief, the registrant is required to make a statement in the annual report indicating the approach that will be used to file the required information.

No change in materiality lens, but some considerations

The SEC indicated that materiality for purposes of the rules will be viewed consistently with the interpretation of materiality set out in the securities laws. Information is deemed material if "there is a substantial likelihood that a reasonable investor would consider it important" in making an investment decision, or if omitted it "significantly alters the 'total mix' of information made available."

Registrants will need to thoroughly and objectively evaluate the total mix of information, considering all relevant facts and circumstances surrounding any climate-related risk – including both quantitative and qualitative factors – to determine whether the risk is material.

Climate-related risks can vary significantly in magnitude and probability over time. The rule requires registrants to describe risks that have materially impacted or are reasonably likely to have a material impact over the short-term and separately in the long-term. This approach is generally consistent with the standard used for MD&A, but registrants are not precluded from breaking down components into medium and longer-term risks.

The same definition of materiality applies to the assessment of the materiality of scopes 1 and 2 GHG emissions. Materaility is not determined solely by the amount of these emissions. For example, disclosure may be material if it enables investors to understand whether emissions:

- are currently or are reasonably likely to be subject to increased taxes or financial penalties;
- trigger a material transition risk due to foreign or state GHG emissions reporting requirements; or
- demonstrate progress toward achieving a target or goal or a transition plan the registrant has disclosed.

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Inline XBRL reporting

The disclosures will be tagged in Inline XBRL format. Submission in this format is intended to help investors and market participants more easily identify, locate, extract and analyze disclosures.

Phased transition

The following table summarizes the compliance dates for registrants based on filer status for both annual reports and registration statements that are required to include information for the full fiscal year indicated in the table.

For fiscal years beginning in calendar year:	LAFs[1]	AFs[2]	NAFs[3], SRCs, EGCs
Financial statement disclosures	2025	2026	2027
Climate risk disclosures			
Climate risk disclosures, except those below	2025	2026	2027
Disclosures in the Specific quantitative disclosures section	2026	2027	2028
GHG emissions			
Scopes 1 and/or 2 disclosures	2026	2028	N/A
Limited assurance	2029	2031	N/A
Reasonable assurance	2033	N/A	N/A
Inline XBRL	2026	2026	2027

Notes:
1. Large accelerated filers
2. Accelerated filers (except smaller reporting companies (SRCs) and emerging growth companies (EGCs))
3. Non-accelerated filers

Periods to be disclosed

In the initial year of compliance, the financial statement and GHG emissions disclosures are required for the most recently completed fiscal year. In addition, if these disclosures were provided in a previous SEC filing for the historical year(s) presented, that historical disclosure is also required. Practically, for most registrants, that means these disclosures will be phased in over a two- to three-year period.

For example, in the second year after compliance, registrants will present the required disclosures for both the most recently completed fiscal year and the preceding fiscal year. However, they will not be required to present the required disclosures for the earliest year presented if that information has not been previously filed, to the extent they present three years of financial statements.

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Changes from the proposal

The following is a selection of key changes from the March 2022 proposal, but is not exhaustive.

- **Financial statement disclosures.** The granular line item analysis was withdrawn; the requirements have been tightened so that amounts can be determined from the registrant's books and records; and no disclosures related to transition risk are required.
- **GHG emissions.** The requirement for registrants to disclose scope 3 GHG emissions in certain circumstances was withdrawn; scopes 1 and/or 2 GHG emissions disclosures are only required if material and only for larger registrants; and the proposed requirement to set organizational boundaries consistent with the financial statements was withdrawn.

The implications for interoperability

Even before the contents of the final climate rule were known, there were two significant differences between the SEC's proposal, IFRS® Sustainability Disclosure Standards (ISSB Standards) and European Sustainability Reporting Standards (ESRSs).

- The SEC's rules focus on the disclosure of climate-related information, which is only one component of sustainability. Both the ISSB Standards and ESRSs focus on a broader range of sustainability topics.
- The SEC's remit is disclosures for the benefit of investors. This is similar to the approach under the ISSB Standards but ESRSs are based on double materiality, which is a multi-stakeholder approach.

Taking these differences as foundational starting points, US companies currently preparing for compliance with ISSB Standards and/or ESRSs are well positioned as they begin to analyze the SEC's climate rule.

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