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Insights: Alert

SEC Adopts New Climate-Related Disclosure Rules Without Scope 3 Greenhouse Gas Disclosure Requirement

March 11, 2024

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After much anticipation, the Securities and Exchange Commission (SEC) adopted last week its climate-related disclosure rules. The adoption of the rules included a press release available here and a fact sheet available here. The most welcome change for public companies from the SEC's March 2022 proposed rules is that Scope 3 greenhouse gas (GHG) disclosure will not be required for any SEC filers.

In last week's open meeting, SEC Chair Gary Gensler acknowledged that, while the SEC "is set up to be merit neutral" and "does not have a role for climate risk itself," the SEC has a role with regard to disclosures. He further noted that "[c]onsistent with [the SEC's] disclosure rules over the decades, [the] final rules are grounded in materiality," which is "a fundamental building block of the disclosure requirements under the federal securities laws." However, although there are more materiality qualifiers in the final rules than had been initially proposed by the SEC, the final rules remain generally prescriptive rather than principles based.

Key Points and Highlights

- ***Scope 1 and 2 GHG Emissions Disclosure***: The final rules require Large Accelerated Filers (LAFs) and Accelerated Filers (AFs) to disclose Scope 1 and 2 GHG emissions, if those emissions are material.
  - The rules require attestation reports for LAFs and AFs to give assurance to the Scope 1 and 2 disclosures.
  - Attestation reports must be at the limited assurance level for AFs. LAFs will initially be required to obtain attestation reports at the limited assurance level, and after a four-year transition period, they will be required to obtain attestation reports at the reasonable assurance level.
  - The rules also include an accommodation that allows Scope 1 and/or Scope 2 GHG emissions disclosure, if required, to be filed on a delayed basis under certain circumstances.
- ***No Scope 3 GHG Emissions Disclosure***: Unlike the proposed rules, the final rules do not require the disclosure of Scope 3 emissions for any SEC reporting companies.
- ***Other Climate-Related Disclosure Requirements***: The final rules also require, among other things, the disclosure of the following in registration statements and annual reports for all reporting companies (including for Smaller Reporting Companies (SRCs) and Emerging Growth Companies (EGCs)):
  - Climate-related risks that have had or are reasonably likely to have a material impact on the company's business strategy, results of operations, or financial condition;

    - The actual and potential material impacts of any identified climate-related risks on the company's strategy, business model, and outlook;
    - If, as part of its strategy, the company has undertaken activities to mitigate or adapt to a material climate-related risk, a quantitative and qualitative description of material expenditures incurred and material impacts on financial estimates and assumptions that directly result from such mitigation or adaptation activities;
    - Specified disclosures regarding the company's activities, if any, to mitigate or adapt to a material climate-related risk including the use, if any, of any strategy and implementation plan to reduce climate-related risks (otherwise known as a “transition plan”), scenario analysis, or internal carbon prices;
    - Any oversight by the board of directors of climate-related risks and any role by management in assessing and managing the company's material climate-related risks;
    - Any processes the company has for identifying, assessing, and managing material climate-related risks and, if the company is managing those risks, whether and how any such processes are integrated into the company's overall risk management system or processes; and
    - Information about the company's climate-related targets or goals, if any, that have materially affected or are reasonably likely to materially affect the company's business, results of operations, or financial condition, which would include material expenditures and material impacts on financial estimates and assumptions as a direct result of the target or goal or actions taken to make progress toward meeting that target or goal.
- ***New Financial Statement Requirements***: The final rules also include new disclosure requirements in the notes to financial statements, including, among other things, the disclosure of costs, expenses and losses incurred as a result of severe weather events and other natural conditions, such as sea level rise, or related to carbon offsets and renewable energy credits or certificates if used as a material component of the company's plans to achieve its climate-related targets or goals. In addition, if the estimates and assumptions the company uses to produce its financial statements were materially impacted by risks and uncertainties associated with severe weather events and other natural conditions, or any disclosed climate-related targets or transition plans, the company must also include in the notes to its financial statements a qualitative description of how the development of such estimates and assumptions was impacted.
- ***New Safe Harbor***: The final rules establish a new private liability safe harbor for disclosures concerning climate-related transition plans, scenario analyses, the use of internal carbon prices, and targets and goals, other than disclosures that relate to historical facts.
- ***No New Required Board Expertise Disclosure***: Unlike in the SEC proposed rules, the final rules do not require companies to disclose whether their board members have climate-related expertise.
- ***XBRL Tagging***: The final rules require companies to electronically tag climate-related disclosures in Inline XBRL, with a phase-in schedule based on filer status.
- ***Effective Date/Compliance Dates***: The final rules will become effective 60 days after their publication in the Federal Register. The new rule requirements will be phased in for all SEC filers with the compliance date dependent upon the status of the filer as a LAF, an AF, a non-accelerated filer (NAF), SRC, or EGC, and the content of the disclosure.Compliance dates begin for LAFs first. LAFs will be required to include certain disclosure items in reports on fiscal years that begin in calendar 2025, and will begin disclosing Scope 1 and 2 emissions in reports for fiscal years beginning in calendar 2026. AFs will be required to begin disclosing Scope 1 and 2 emissions in the fiscal year beginning in calendar 2028. The following chart, which was published in the SEC's fact sheet and posted on its website, details the compliance deadlines and disclosure requirements by filer status:

Compliance Dates under the Final Rules[1]						
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 1500[2]*
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.					

Comparison to Other Disclosure and Reporting Regimes

Many issuers will be subject to, and are tracking, multiple climate-related disclosure and reporting regimes, including the recent California climate-related disclosure laws (Climate Corporate Data Accountability Act and Climate-Related Financial Risk Act), and the European Union's Corporate Sustainability Reporting Directive (CSRD). While a full comparison of these disclosure and reporting regimes to the SEC's final rules is not the subject of this alert, below is a table that compares, at a high level, the SEC's final rules with the California laws and CSRD.

Requirements	**SEC Rules**	**California Laws**	**CSRD**
Form of Disclosures	In registration statements and annual reports, audited financial statements	One annual report on emissions; one report on risks every other year	Annual report "Equivalent" report as substitute
Data Reported	Scope 1 and 2 emissions, climate-related risks, any activities "to mitigate or adapt to a material climate-related risk," processes and oversight over "assessing and managing" those climate-related risks and climate-related targets or goals that have or reasonably likely to materially affect the business	Scope 1, 2 and 3 emissions, climate-related risks, and measures to reduce them	Extremely broad: covers 12 standards that cover all aspects of sustainability reporting.
First Disclosures	2025 and later; however Scope 1 and 2 emissions will be first reported in 2026	2026	2025 and later

Which companies does it affect?	It depends on the disclosure content. With regard to disclosing Scope 1 & 2 emissions, only Large Accelerated and Accelerated Filers must comply	Public and private firms operating in CA making more than $1 billion or more than $500 million per year	All companies with securities listed on an EU-regulated market; “large” EU companies that are not listed; EU companies that are parent of a “large group” and not listed
Third party verification required?	Yes for Scope 1 & 2 disclosures	Yes	Yes
In line with GHG Protocol/TCFD?	Partially modeled on GHG Protocol and TCFD	Yes	Yes
Materiality	Single materiality	Double materiality for SB261	Double materiality
Penalties	SEC can hold corporate directors personally liable for misstatements, which can be used in lawsuits	Fines up to $500,000 per reporting year for failing to meet requirements, up to $50,000 for inadequate report	Individual member states will have 18 months to phase-in CSRD criteria into laws. Specific EU countries will set their own enforcement and penalty rules
Any safe harbors?	Yes with regard to disclosures concerning transition plans, scenario analyses, the use of internal carbon prices, targets and goals because this disclosed information is considered a forward-looking statement	Yes, the only penalties on Scope 3 disclosures before 2030 are for not filing	Same as penalties

Next Steps

All SEC reporting companies, regardless of filing status, should start to consider how these final rules will apply to them, and, in particular, LAFs and AFs will want to begin the process of assessing the materiality of their Scope 1 and 2 GHG emissions and other climate-related items. Even if a LAF or AF does not think its Scope 1 or 2 GHG emissions are material, they may still want to conduct a formal analysis of their emissions to backstop their conclusions.

Also, not unexpectedly, on the same day as the SEC's final rules were adopted, ten states (Alabama, Alaska, Georgia, Indiana, New Hampshire, Oklahoma, South Carolina, West Virginia, Wyoming, and Virginia) filed a petition in the Eleventh Circuit asking the Court to declare the SEC's disclosure rule unlawful and vacate it. Petitioners argue

that the final rule exceeds the SEC's statutory authority and is otherwise arbitrary, capricious, an abuse of discretion, and not in accordance with law. Other lawsuits have followed, and it will be important to monitor their progress and potential outcomes as companies prepare to comply with the final rules.

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