

March 28, 2022

# SEC Proposes Expansive Climate-Related Disclosure Rules

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**Would Require Public Companies to Disclose Detailed Greenhouse Gas Emissions, Climate Transition Plans, Targets and Progress Against Targets, Long-Term Climate Risks and Business Impacts, and Climate-Related Corporate Governance, Including New Information in Notes to Audited Financial Statements**

**Related Webinar Hosted on Tuesday, March 29, 2022**

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## SUMMARY

On March 21, 2022, the Securities and Exchange Commission proposed climate-related disclosure requirements (the “Proposed Rules”) that would require U.S. public companies and foreign private issuers to dramatically expand the breadth, specificity and rigor of climate-related disclosures in their SEC periodic reports and registration statements. The Proposed Rules, set out in a 510-page [proposing release](#), mark a significant departure from the SEC’s traditional principles- and materiality-based reporting framework and move towards a prescriptive climate-related disclosure regime that mandates reporting of detailed information regardless of its materiality. The Proposed Rules, if adopted, will meaningfully increase the cost and complexity of public reporting. To enable compliance, companies will need to expend significant advance effort to enhance, among other things, data collection procedures (including from third parties in their value chain), and internal processes and controls, which will require substantial internal and external resources (including audit oversight of novel financial statement requirements).

Key provisions of the Proposed Rules include:

- disclosure of greenhouse gas (“GHG”) emissions (both in absolute terms, not including offsets, and in terms of intensity in relation to business scale) that cover Scope 1, Scope 2 and—if material or if the company has set targets or goals that include Scope 3 emissions—Scope 3 GHG emissions,

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and third-party attestation (eventually at a “reasonable assurance” level) for Scope 1 and Scope 2 GHG emissions disclosures;

- disclosure of any climate transition plan, internal carbon price, climate-related targets or goals adopted by the company, and progress against such plan, targets and goals;
- disclosure of climate-related risks over the short, medium and long term and their impacts on business activities;
- disclosure of qualitative and quantitative climate risk and historical impact in the notes to a company’s audited financial statements, with information required to be presented on a disaggregated basis if the aggregated impact is 1% or more of the total line item; and
- disclosure of corporate governance of climate-related risks and risk management processes.

The disclosure requirements would apply to all SEC reporting companies (other than Canadian issuers using Form 40-F), even those with no publicly listed equity securities. The proposed disclosure requirements are based closely on the Task Force on Climate-Related Financial Disclosure (“TCFD”) disclosure framework (see [Appendix A](#) for a comparison between the TCFD framework and the Proposed Rules), and the GHG emissions disclosure requirements generally adhere to the GHG Protocol. Compliance would be phased in, with reporting for large accelerated filers beginning in 2024 with respect to fiscal year 2023 if the Proposed Rules become effective at the end of this year (see [Appendix B](#) for disclosure compliance dates).

The SEC voted 3 to 1 (Commissioner Peirce dissenting) to issue the Proposed Rules. The public comment period was initially open until May 20, 2022, but on May 9, 2022, the SEC extended the end of the public comment period to June 17, 2022.<sup>1</sup> The Proposed Rules are already generating intense debate and are widely expected to attract vigorous comments and legal challenges.

Key implications and takeaways of the Proposed Rules for companies, including those outlined below, were further discussed during Sullivan & Cromwell’s webinar entitled “Scope and Implications of the SEC’s Proposed Climate-Related Disclosure Rules” on Tuesday, March 29, 2022 (a recording of the webinar can be accessed [here](#)).

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## BACKGROUND AND POTENTIAL FUTURE CHALLENGES

According to the SEC, over the last decade, investors and other stakeholders have increasingly requested climate-related disclosures that are comparable, consistent and decision-useful.<sup>2</sup> In the absence of a regulatory framework in the United States, many investors, including some of the largest U.S. institutional investors, have urged companies to provide standardized disclosures on climate-related risks, impact, oversight and metrics based on frameworks developed by TCFD and other standard setters. In response, more U.S. public companies have begun to voluntarily disclose climate-related information, although to varying degrees of scope and specificity. Many U.S.-listed foreign private issuers, meanwhile, are already reporting under home country frameworks. These disclosures are generally made in sustainability or ESG reports rather than filed or furnished in SEC filings, which is consistent with the SEC’s 2010 guidance on

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climate-related disclosures. Under the SEC's existing disclosure framework as set forth in the 2010 guidance, disclosure of specific climate-related metrics is not mandatory. Rather, a company is required to disclose information about potential or actual impacts of climate change to the extent material to investors. Investors and other stakeholders have argued some level of regulatory involvement is required to bring consistency, comparability and reliability to these disclosures and therefore make them decision-useful, and to align with the global momentum towards mandatory climate disclosures.

Under the Biden Administration, climate change disclosure has been at the forefront of the SEC's agenda. Following then-Acting Chair Allison Herren Lee's announcements in March 2021 that the SEC will be "working toward a comprehensive ESG disclosure framework," the SEC solicited public input on climate disclosure from a broad range of stakeholders. Although some commenters criticized current disclosure practice for not producing consistent, comparable and reliable information, others argued that climate-related disclosures should only be required if the information in those disclosures is material to a company's business and would alter a reasonable investor's investment decision. Starting in September 2021, the SEC also selectively began sending comment letters to public companies regarding their climate-related disclosures (both within and outside of their SEC filings). Notably, based on publicly available responses, nearly all public companies that responded to the SEC's comment letters asking for additional disclosure on the basis of the 2021 guidance reported that they do not find climate change-related physical or transition risks to be material to their businesses.<sup>3</sup>

In proposing the new disclosure requirements, the SEC concluded based on feedback from stakeholders and the Staff's own experiences that the existing disclosure system is not eliciting information that enables investors to assess accurately the potential impacts of climate-related risks on a company's business or to gauge how a company's board and management are assessing and addressing those impacts, particularly as compared to similarly situated companies. The Staff also considered recent developments in other jurisdictions, which have been developing or revising their mandatory climate-related disclosure regimes. For example, the European Union has proposed a new Corporate Sustainability Reporting Directive<sup>4</sup> and the United Kingdom is currently implementing mandatory TCFD-aligned reporting,<sup>5</sup> each of which will apply to large companies and financial institutions, whether public or privately held. The United Kingdom has also mandated Scope 1 and 2 GHG emissions reporting for large companies.<sup>6</sup> According to the SEC, the Proposed Rules would help address an increasing global recognition of the need to improve companies' climate-related disclosures. Unlike the approach taken by the EU and other jurisdictions, which includes substantive requirements to align with the Paris Accord and voluntarily comply with initiatives such as the Glasgow Financial Alliance for Net Zero, the Proposed Rules do not require companies to reduce GHG emissions or make substantive changes to their business strategies.

The Proposed Rules represent one of the most far-reaching steps in the Biden Administration's "whole-of-government" approach for addressing climate change and achieving net zero emissions across the U.S.

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economy by 2050.<sup>7</sup> The Administration has faced significant political headwinds on its climate agenda and has been advancing its initiatives through funding allocated under the Bipartisan Infrastructure Law, federal procurement policies and federal regulatory agencies, which have promulgated new policies and focused on various aspects of climate change impact across different sectors of the U.S. economy. For example, the Commodities Futures Trading Commission,<sup>8</sup> the Federal Reserve Board<sup>9</sup> and the Financial Stability Oversight Council<sup>10</sup> have each recently warned that climate change threatens U.S. financial stability and have recommended increased disclosure of climate risks. In December 2021, the Office of the Comptroller of the Currency released draft principles designed to provide large banks with a high-level framework for managing climate-related financial risks and indicated that more detailed guidance will be issued in 2022.<sup>11</sup> The Department of Labor released rules in October 2021 that removed barriers to fiduciaries' ability to consider climate and other ESG-related disclosures when selecting investments.<sup>12</sup>

It is unclear whether the Proposed Rules will be adopted in the form currently proposed. The Proposed Rules will likely elicit vigorous comments and are widely expected to be subject to legal challenges, including on the basis that they exceed the SEC's statutory authority and violate First Amendment rights. A similar challenge was made in connection with the SEC's conflict minerals rules, which were partially struck down.<sup>13</sup> Notwithstanding this uncertainty, in light of the breadth, specificity and implications of the disclosures contemplated by the Proposed Rules, the speed with which they are proposed to be adopted, and the potentially lengthy time required to establish the controls and procedures necessary to enable such disclosures, companies should assess their compliance readiness soon. Companies should also monitor the Proposed Rules' potential impact on market practices regarding voluntary climate-related disclosures going forward, even if adoption of the Proposed Rules is delayed.

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### SUMMARY OF THE PROPOSED RULES

The Proposed Rules comprise new items in Regulation S-K and a new article in Regulation S-X. New Items 1500-1507 of Regulation S-K, modeled in part on the TCFD disclosure framework,<sup>14</sup> would require a company to disclose information about (i) its governance of climate-related risks; (ii) climate-related impacts on its strategy, business model and outlook; (iii) climate-related risk management; (iv) GHG emissions metrics; and (v) any internal carbon price or climate-related targets and goals. According to the SEC, the widespread adoption of, and alignment with, the TCFD framework could potentially facilitate more comparable disclosures globally while reducing the compliance burden for public companies, many of which have experience reporting under this framework. In addition, accelerated and large accelerated filers would be required to obtain attestation by an independent third party of their GHG emissions metrics.

Proposed Article 14 of Regulation S-X would require companies to include climate-related financial statement metrics (which would consist of disaggregated climate-related impacts on existing financial statement line items) and related disclosures in a note to their audited financial statements. These metrics

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would then be subject to audit by an independent registered public accounting firm and come within the scope of the company's internal control over financial reporting.

### A. DISCLOSURE OF CLIMATE-RELATED RISKS AND THEIR IMPACT

The Proposed Rules include detailed requirements for companies to disclose the actual and potential climate-related risks that are reasonably likely to have a material impact on the company's business or consolidated financial statements. These requirements include disclosure of both physical and transition risks over the short, medium and long term. Under the Proposed Rules, companies will have the ability to determine the most appropriate time periods for disclosure, although the SEC has requested comment on whether it should define these periods (e.g., whether long term should be defined "as 10-20 years, 20-30 years, or 30-50 years").

In addition, the Proposed Rules would require companies to describe any actual and potential impacts of those risks on their business, strategy and outlook, with specific financial statement disclosures regarding the impact of those risks. Although the proposed disclosures are based on the TCFD framework, the SEC acknowledged that only a minority of public companies that voluntarily report under TCFD actually disclosed the impact of climate-related risks and opportunities on their business in alignment with TCFD, and even companies that make such disclosures do not include the granular details proposed by the SEC.<sup>15</sup>

- **Physical Risks:** Companies would be required to provide detailed disclosures of material physical risks faced, including classification of the risk as acute (e.g., hurricanes) or chronic (e.g., sea level rise or the decreased availability of fresh water). Companies would also need to disclose the ZIP code or equivalent postal-type code for properties subject to physical risks, if material, as well as granular information about exposure to risks of flooding or water stress, if material.
- **Transition Risks:** Companies would be required to disclose how they are impacted by material transition risks, which are the risks associated with the impact of regulatory, technological and market changes related to mitigation of, or adaptation to, climate change. Companies would be required to identify whether these risks relate to regulatory, technological, market (including changing consumer, business counterparty and investor preferences), liability, reputational or other transition-related factors and how those factors impact the company.
- **Impact of Risks:** Companies also would be required to describe the actual and potential impact of these risks on their strategy, business model and outlook, and how such impacts are considered as part of their strategy, financial planning and capital allocation, on a current and forward-looking basis. The SEC—noting that many companies currently include only boilerplate discussions about the impact of climate-related risks—has proposed a specific list of the types of impacts a company would be required to discuss, including impacts on the types and locations of its operations, impacts on suppliers and impacts of any activities to mitigate climate-related risks. Although the risks themselves are qualified by materiality, the required discussion of the impact of those risks on a company's business strategy is not currently so qualified.

### B. DISCLOSURE AND ATTESTATION OF GHG EMISSIONS METRICS

The Proposed Rules would require disclosure of Scope 1 GHG emissions (direct GHG emissions from operations that are owned or controlled by the company) and Scope 2 GHG emissions (indirect emissions from the generation of purchased or acquired electricity, steam, heat or cooling that are consumed by the

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operations owned or controlled by the company, such as indirect emissions created by use of the company's sold products or emissions created by products and services bought by the company) without regard to materiality. In addition, companies would be required to disclose Scope 3 GHG emissions (all other indirect emissions not covered by Scope 2),<sup>16</sup> if such emissions are material or if a company has already set a GHG target or goal that includes Scope 3 emissions.<sup>17</sup> This new Scope 3 disclosure requirement is among the most controversial provisions of the Proposed Rules because, for many companies, Scope 3 emissions are both the largest source of emissions and the most difficult to reliably estimate. Smaller reporting companies would not be required to disclose Scope 3 emissions. For seasoned reporting companies, GHG emissions disclosure would be subject to a graduated framework of third-party attestation requirements (see [Appendix B](#) for attestation compliance levels and dates). The SEC notes that such disclosure could help mitigate instances of "greenwashing."

- **Definitions:** The definitions used in the Proposed Rules for GHG emissions are substantially similar to those provided by the GHG Protocol.<sup>18</sup> However, unlike the GHG Protocol, the Proposed Rules do not permit companies to elect an equity share approach or a control approach but instead would require reporting based on financial consolidation accounting principles and would require companies to report proportionate emissions from equity investees.
- **Required Scope 1 and Scope 2 Emissions:** The Proposed Rules would require a company to disclose its Scope 1 and Scope 2 GHG emissions for its most recent fiscal year and, where reasonably available, for the historical fiscal year(s) included in its consolidated financial statements. GHG emissions must be expressed both on a carbon dioxide-equivalent basis and disaggregated among seven separate GHGs (even those that are individually quantitatively immaterial) and must exclude any purchased or generated offsets. GHG intensity (per unit of revenue and per relevant unit of production) must also be reported, as well as detailed disclosures of the methodology, inputs and assumptions used to calculate the GHG metrics.<sup>19</sup> In addition, companies must disclose any material change to the methodology or assumptions underlying its GHG emissions disclosure from the previous fiscal year.
- **Potential Scope 3 Emissions Disclosures; Phase-In and Liability Safe Harbor:** Companies required to report Scope 3 emissions would be subject to similar disclosure requirements as discussed above, although companies could report Scope 3 emissions as a range if they disclose the reason for doing so and the underlying assumptions.<sup>20</sup> In response to widespread concerns from many commenters regarding the current lack of methodological consensus and data regarding Scope 3 emissions, the SEC proposed a longer phase-in period for Scope 3 emissions. The Proposed Rules also include a modified liability safe harbor under which disclosure of Scope 3 emissions would not be deemed a fraudulent statement unless it is shown that the disclosure was made or reaffirmed without a reasonable basis or was disclosed other than in good faith.
- **Reasonable Estimates and Gaps in Data:** In recognition of the challenges of reporting Scope 3 and other GHG data, the Proposed Rules would allow companies to use reasonable estimates when disclosing all GHG emissions, so long as they also describe the assumptions underlying the estimates and the reasons for using them. If there are gaps in data required to calculate GHG emissions, a company must disclose the method used to address the gaps, and how accuracy or completeness of disclosure may be impacted.
- **Reliance on Third-Party Data:** Because of the inherent difficulties associated with gathering GHG data—particularly Scope 3 emissions data—companies will need to rely on data compiled and created by third parties, which may potentially expose companies to liability for disclosures beyond their ability to verify and control. Notably, the Proposed Rules would require companies to disclose,

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to the extent material, the use of any such third-party data and the process used to assess such data.

- **Attestation Requirement:** Under the Proposed Rules, accelerated filers and large accelerated filers (including foreign private issuers) would need to include in relevant SEC filings an attestation report that covers the disclosure of its Scope 1 and Scope 2 emissions.<sup>21</sup> Attestation would be on a limited assurance basis for the first two years the requirement is effective and on a reasonable assurance basis thereafter (which is the standard applied to financial statements). The Proposed Rules would require that attestation reports be provided using standards that are publicly available at no cost and established by a body or group that has followed due process procedures, although the SEC declined to adopt a particular standard because of the evolving nature of the GHG emissions reporting and attestation landscape. Thus, companies and investors may be required to assess and compare multiple attestation standards.<sup>22</sup>

### C. CLIMATE-RELATED METRICS IN FINANCIAL STATEMENTS

Perhaps the most unexpected and unprecedented element of the Proposed Rules is the mandated qualitative and quantitative climate risk disclosures in the notes to a company's audited financial statements.

- **Financial Impact Metrics:** The Proposed Rules would require a company to describe the impact—whether positive or negative—of climate-related risks, such as severe weather events and transition activities, on financial statement line items on a line-by-line basis. The required disclosures are **not** limited by materiality. Instead, the narrative disclosure is triggered if the impacted amount is 1% or more of the related line item.<sup>23</sup> For example, a company would have to describe changes to general and administrative expenses due to new emissions pricing, if such changes equal 1% or more of the general and administrative expenses line item.
- **Expenditure Metrics:** The Proposed Rules also would require a company to disclose expenditures related to mitigating the risk of severe weather events and transition activities. Companies would be required to separately aggregate amounts of expenditure expensed and capitalized costs incurred. The expenditure metrics would be subject to the same 1% threshold as the financial impact metrics.
- **Financial Estimates and Assumptions:** Companies would be required to disclose how severe weather events and transition activities affected estimates and assumptions (e.g., estimates made in connection with an asset impairment analysis) related to the financial statements.

### D. GOVERNANCE OF CLIMATE-RELATED RISKS AND RISK MANAGEMENT PROCESSES

The Proposed Rules would mandate governance disclosures that go beyond the information currently required in proxy statements and the level of detail set forth under the TCFD framework.

Among other disclosures required with respect to directors' and management's roles in climate-related risk oversight and governance, companies would have to specify:

- any board members or board committees responsible for the oversight of climate risk;
- the processes and frequency by which the board or board committee discusses climate-related risks;
- how the board is informed about climate-related risks;

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- whether and how the board or board committees consider climate risk as part of a company's business strategy, risk management and financial oversight;
- whether and how the board sets climate-related targets and goals and how it oversees progress against those targets or goals, including the establishment of any interim targets or goals;
- whether certain management positions or committees are responsible for assessing and managing climate-related risks and the process by which such positions or committees are informed about and monitor climate-related risks;
- procedures for internal reporting and monitoring of climate risk;
- the extent to which management relies on in-house staff and/or third-party consultants with relevant expertise to evaluate climate-related risks and implement related plans of action; and
- whether the responsible positions or committees report to the board or board committee on climate-related risks and how frequently this occurs.

Companies are separately required to describe any processes in place for identifying, assessing and managing climate-related risks, and to provide granular details that include how the company:

- determines the relative significance of climate-related risks compared to other risks;
- considers existing or likely regulatory requirements or policies, such as GHG emissions limits, when identifying climate-related risks;
- considers shifts in customer or counterparty preferences, technological changes or changes in market prices in assessing potential transition risks;
- determines the materiality of climate-related risks, including how it assesses the potential size and scope of any identified climate-related risk;
- decides whether to mitigate, accept or adapt to a particular risk, as well as the process for prioritizing risks and determining how to mitigate a high priority risk; and
- whether and how climate-related risks are integrated into the company's overall risk management system or processes.

In addition, companies would be required to identify any board member with expertise in climate-related risks, with disclosure in such detail as necessary to fully describe the nature of the expertise. However, unlike board members with audit committee financial expertise or the proposed cyber expertise governance framework under the SEC's recently proposed cyber rules,<sup>24</sup> the Proposed Rules do not provide a safe harbor insulating a director identified as having climate risk expertise from liability. As a result, directors with such expertise may be viewed as having greater responsibility with respect to climate-related oversight and be exposed to greater scrutiny due to their expertise, and, compared to directors with other identified expertise, face greater liability.

The lack of a safe harbor is not the only way in which these new requirements deviate from the SEC's practice elsewhere regarding risk disclosure and management. Notably, the requirement to disclose information on risk mitigation deviates from the SEC's long-standing position that companies should not downplay material risks they may face by describing how such risks are being mitigated.

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The Proposed Rules do not require disclosure of whether executive compensation is connected to climate-related targets, but, given the proposed inclusion of financial statement disclosures, the Proposed Rules may nevertheless impact executive compensation if the SEC adopts changes to existing clawback rules. In 2021, the SEC reopened the comment period on potential new rules that would prohibit the listing of companies that do not develop and implement policies to recapture excess incentive compensation paid to an executive officer based on erroneous financial statements.<sup>25</sup>

### **E. TRANSITION PLAN/TARGETS AND GOALS**

Many companies have voluntarily disclosed their adoption of transition plans in sustainability reports or other public disclosures. The EU has recently proposed mandating adoption of a climate transition plan (consistent with a 1.5° warming scenario) by all large EU companies and by non-EU companies with significant EU revenues.<sup>26</sup> Under the Proposed Rules, if a company has adopted a transition plan, then (whether or not they have publicly disclosed the plan) they are subject to prescriptive disclosure requirements with respect to metrics and targets used to identify and manage physical and transition risks. Companies would be required to update their transition plan disclosures annually and to include narrative descriptions of the actions taken during the previous year to achieve the plan's targets or goals.

Similarly, the Proposed Rules would require disclosure of detailed qualitative and quantitative information if a company has set any climate-related targets or goals as many companies have voluntarily done, including pursuant to initiatives such as the Glasgow Financial Alliance for Net Zero. This includes not only targets and goals related to GHG emissions (e.g., net zero pledges), but also any related to energy or water usage, conservation or ecosystem restoration, as well as goals with regard to revenues from low-carbon products in line with anticipated regulatory requirements, market constraints or other goals established by a climate-related treaty, law, regulation, policy or organization. The Proposed Rules would require disclosure of the scope of activities and emissions included in the target, unit of measurement (e.g., absolute versus intensity-based targets), time horizon for achieving the target, baseline time period and baseline emissions against which progress will be tracked, as well as any interim targets.

Neither the transition plan nor the targets and goals disclosure requirements are conditioned on materiality.

### **F. OFFSETS/INTERNAL CARBON PRICING/SCENARIO ANALYSIS**

If, as part of its net emissions reduction strategy, a company uses carbon offsets or renewable energy credits or certificates ("RECs"), the Proposed Rules would require disclosure of the role that carbon offsets or RECs play in the company's climate-related business strategy. Additionally, if a company uses an internal carbon price when assessing climate-related factors, the Proposed Rules would require disclosures of (1) the price in units of the company's reporting currency per metric ton of carbon dioxide equivalent, (2) the total price and the boundaries for measurement on which the total price is based and (3) the rationale for selecting the internal carbon price applied. These disclosures also are not conditioned on materiality.

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Although companies are not required to conduct scenario analyses, if they do,<sup>27</sup> then they must disclose detailed information about such analyses, including the scenarios considered (e.g., an increase of no greater than 3°, 2° or 1.5°C above pre-industrial levels), as well as the parameters, assumptions and analytical choices, and the projected principal financial impacts on the company's business strategy under each scenario. This requirement to disclose the outcome of scenario analysis also is not conditioned on materiality. This would require companies that conduct scenario analysis to provide qualitative and quantitative information on not only the financial impacts of climate change on their business, but also the steps they are taking—or considering—to respond to hypothetical future climate scenarios.

### G. MECHANICS

The Proposed Rules would require companies to include the climate-related disclosures in SEC periodic reports and registration statements, including for initial public offerings, in a separately captioned “Climate-Related Disclosure” section and in the financial statements. The new disclosures would be on a “filed” (not “furnished”) liability basis, consistent with other required SEC disclosures (except any climate disclosures by foreign private issuers included on Form 6-K would be on a “furnished” basis, consistent with other 6-K disclosures). Companies would be able to continue to incorporate by reference certain disclosures from other parts of their registration statements or annual reports (e.g., Risk Factors, MD&A or the financial statements), or in some cases from their other filed or submitted reports.

The Proposed Rules include phase-in periods for companies as set forth on [Appendix B](#). The disclosure compliance date begins in 2024 with respect to fiscal year 2023 for large accelerated filers, in 2025 with respect to fiscal year 2024 for accelerated filer and non-accelerated filers, and in 2026 with respect to fiscal year 2025 for smaller reporting companies. All filers would have an additional year to comply with applicable Scope 3 disclosure requirements and smaller reporting companies would not be required to disclose Scope 3 emissions.

The Proposed Rules would require companies to tag climate-related disclosures in Inline eXtensible Business Reporting Language (“Inline XRBL”). The proposed requirement would include block text tagging and detail tagging of the new narrative and quantitative climate-related disclosures. The new financial statement disclosure requirements apply to all years included in the financials (i.e., fiscal years 2021, 2022 and 2023 in the 2023 annual report of a large accelerated filer), unless such information is not available without unreasonable effort or expense. GHG emissions data must be presented for historical periods if reasonably available.

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## IMPLICATIONS

The Proposed Rules, if adopted, will have immediate and significant ramifications on how companies collect, disclose and verify climate-related data and plans, and will meaningfully increase the cost and complexity of SEC compliance.

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**Compliance Timeline/Readiness Assessment.** Public companies will need to devote substantial human and financial resources to develop (or enhance the quality of) climate-related information required under the Proposed Rules. Given the limited comment and phase-in periods and the scope and complexity of the Proposed Rules, companies will need to assess their readiness now. Although these assessments will necessarily be individualized since companies are at different maturity levels in their climate reporting, some general areas of focus may include:

- Have cross-functional teams been organized to establish accountability for climate-related reporting?
- Are there knowledge gaps or staffing challenges that need to be addressed?
- Where does climate-related information come from within the organization and who are the owners within the company? Has data aggregation been standardized and automated within the company? Does the company need to integrate or combine systems in order to generate certain types of data?
- What information does the company need to collect from third parties? Are there any gaps in the company's ability to obtain and assess such third-party data? What procedures does the company have for assessing the quality of that information, and does the company have assurance that it will receive the required information on a timely basis (or at all)?
- Does the company subject its climate disclosures to disclosure controls and procedures?
- Has the company identified a qualified independent third-party attestation service provider? What does the company need to do to prepare for third-party auditing of its disclosures and how long will it take the company to become prepared?
- Has climate risk been integrated into existing risk management or compliance frameworks?
- Does the company need to add individuals with climate-related expertise to its board of directors and management team?

Even if a company already has a robust climate disclosure framework in place, the board and management team will need to reassess their current disclosure timeline and processes in light of the Proposed Rules.

**Accelerated Climate Reporting.** Currently, many companies publish their sustainability or ESG reports several months after they have completed the year-end audit process and filed their annual report, which gives them more time to collect data (including waiting for year-end data to be published by third parties such as power utilities/interconnections) and complete climate-related internal disclosure review and any third-party verification processes. Because the Proposed Rules require that the new climate-related disclosures be included in a company's annual report, U.S. domestic reporting companies will need to accelerate the timeline for preparing these disclosures, which could pose substantial challenges if there are constraints on the availability of information and internal and external resources. Some of the most significant aspects of the Proposed Rules (for example, Scope 2 and 3 emissions disclosure) require reliance on information outside of a company's control. The accelerated timeline will be impacted further by the attestation requirement for GHG emissions disclosures as well as the new audit procedures that will be required to be performed on climate disclosures included in the notes to the audited financial statements. Because all audit and assurance activities will have to be performed at the same time as the year-end

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financial statements, companies will need to evaluate, and potentially remedy, systems and resource constraints, which may be particularly acute for small and mid-sized companies. Although the SEC has proposed that companies be permitted to estimate their fourth quarter emissions for this purpose, the Proposed Rules would still represent a significant acceleration of reporting under current practices.

**Novel Approach to “Materiality.”** In the Proposed Rules, a limited number of disclosures are required only when material, which the SEC has indicated would adhere to the traditional definition of materiality established by the Supreme Court in *TSC Industries, Inc. v. Northway, Inc.*<sup>28</sup> The remaining disclosures required by the Proposed Rules, however, are not conditioned on materiality, or refer to a specific threshold well below any standard materiality determinations, marking a significant departure from the SEC’s long-standing principles-based disclosure regime. A few notable examples include:

- The proposed amendments to Regulation S-X require disclosure of certain climate-related impacts on existing financial statement line items to the extent the aggregate impact is 1% or more of the particular line item for a given year, which is significantly below the typical quantitative benchmark of 5% under SAB 99.<sup>29</sup>
- The Proposed Rules require detailed information (in some instances, both qualitative and quantitative without reference to materiality) regarding a company’s scenario analysis (at a far more granular level than called for under the TCFD framework), internal carbon pricing and transition plans, in each case, if used by the company.
- The Proposed Rules require disclosure of Scope 1 and Scope 2 emissions for each of seven GHGs separately (without any materiality threshold), as well as a description of the company’s methodology, including its organizational and operational boundaries, calculation approach (including any emissions factors used and the source of the emissions factors), and any calculation tools and third-party data used to calculate GHG emissions.

The Proposed Rules in this respect align more with the EU’s prescriptive requirements under the EU Taxonomy and Sustainable Finance Disclosure Regulations (and proposed Corporate Sustainability Reporting Directive).<sup>30</sup> Additional SEC rulemakings are expected on other ESG issues, including with respect to workforce issues, such as wage quality and equity and diversity. It is likely these rule proposals will similarly involve prescriptive disclosure obligations not qualified by materiality.

**Climate-Related Actions or Statements Can Trigger Ongoing Disclosure Requirements.** Some of the proposed disclosure requirements apply only if a company decides to take certain actions with respect to climate change. To avoid triggering an inadvertent or premature disclosure obligation, companies should be mindful of the Proposed Rules when making public statements on climate change or considering the implementation or expansion of climate-related plans. Examples include:

- If a company uses an internal carbon price, or if it uses analytical tools (such as scenario analysis) to assess the impact of climate-related risks on the business and financial statements, then the company would need to include the comprehensive information described above under “Offsets/Internal Carbon Pricing/Scenario Analysis.”

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- If a company has adopted a transition plan, it must describe the plan, including the relevant metrics and targets used to identify and manage physical and transition risks, as further discussed above under “Transition Plan/Targets and Goals.”
- If a company has set any targets or goals (even if these targets and goals have not been publicly disclosed), it is required to provide certain disclosure regarding those targets and goals as further discussed above under “Transition Plan/Targets and Goals.”

If a company has already taken these climate-related actions, the company would be required to make disclosures with respect to these actions if the Proposed Rules are adopted in their current form. Furthermore, certain foreign private issuers may be required by regulation in their home country to adopt transition plans or use scenario analysis, which would effectively make these disclosures mandatory for them. Similarly, if other U.S. regulators start to require companies subject to their jurisdiction to take climate-related actions subject to these disclosure requirements (e.g., scenario analysis by U.S. financial institutions), the disclosure requirements would effectively commence in connection with those regulatory requirements.

**Scope 3 Emissions.** The Proposed Rules would require disclosure of Scope 3 emissions only if material or if targets have been set. However, all companies will need to calculate (or at least estimate) Scope 3 emissions to determine materiality in the first instance, resulting in significant costs to a company even if they ultimately determine that no Scope 3 disclosure is required for that company. Moreover, companies may be concerned that their materiality determinations may be second guessed by the SEC. As Commissioner Pierce notes in her dissenting statement, the SEC suggests that such emissions generally are material and admonishes companies that “materiality doubts” should be resolved in favor of disclosure, noting that the proposing release suggests a possible mandatory reporting of Scope 3 emissions if they represent more than 40% of total GHG emissions.

Much controversy surrounds the disclosure of Scope 3 emissions, which are generated within a company’s value chain, including its upstream suppliers and downstream customers. Considerable uncertainty surrounds the reliability of data and methodologies used to delineate and measure Scope 3 emissions compared to more straightforward metrics for calculating Scope 1 (or even Scope 2) emissions. It can be challenging to delineate what constitutes a company’s value chain, and Scope 3 emissions inherently include a level of “double-counting” as one company’s Scope 1, 2 and/or 3 emissions may be another company’s Scope 3 emissions.

Third-party data is necessary to calculate upstream and downstream Scope 3 emissions calculation. Such third-party data, as well as the processes a company uses to obtain and assess the data, must be disclosed under the Proposed Rules if material. Companies may wish to begin examining the source of their emissions calculations, if applicable, with a view to disclosing the diligence they undertake around the quality of the sources, as well as identifying any limitations on their ability to publicly disclose the source. In addition, companies may consider modifying existing contractual arrangements to allow for effective

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capture of third-party data required for reporting purposes. To the extent data is not available, the SEC acknowledged that it may also be necessary for companies to rely heavily on estimates and assumptions to generate Scope 3 emissions data. For example, companies may need to rely on assumptions about how customers will use their products in order to calculate Scope 3 emissions from the use of sold products.

Many companies in the United States in the energy, chemicals, steel and other industrial sectors with significant emission sources are required to report some GHG emissions to the U.S. Environmental Protection Agency (“USEPA”) under the Clean Air Act or state analogues.<sup>31</sup> However, because USEPA’s reporting requirements are often facility-specific, rather than focused on the consolidated entity, and do not comprehensively cover Scope 1, 2 and 3 emissions, even these companies will need to develop and produce additional emissions-related information to comply with the Proposed Rules.

***Attestation of Disclosure.*** Scope 1 and 2 emissions data will be subject to attestation requirements by an independent and experienced third party. The Proposed Rules are extensive in their independence tests (similar to those for auditors), and also contain specific requirements for qualification. Companies should begin assessing potential attestation service providers, including with a view towards the independence requirements, particularly as they consider the use of consultants (who would not be independent) to assist them with the climate-related rules in general. Although the attestation provisions are subject to an additional one-year phase-in period, the assurance obligation will apply to all data presented, including data for historical periods. As such, companies should establish controls and procedures designed to ensure any emissions data disclosed prior to the effectiveness of the attestation obligation will also satisfy the standards for assurance.

For companies that already obtain third-party assurance over their voluntary GHG disclosures, the Proposed Rules may require them to reassess the qualifications of their attestation service providers. The cost of obtaining third-party assurance from highly-regarded providers may increase. Moreover, many companies that have obtained third-party assurances in the past have only done so with a limited subset of their GHG emissions data, and the attestation required by the Proposed Rules would therefore increase the time and cost associated with attestation.

***Financial Statement Metrics.*** One of the more significant changes in the Proposed Rules is the disclosure in the notes to the audited financial statements of quantitative, line-item disclosure (both revenue and expense) of the financial impact of certain severe weather events and other natural conditions, financial impacts related to transition activities, expenditures to mitigate climate-related risks, financial estimates and assumptions impacted by climate-related risks.

A company’s auditors will need to audit these new disclosures, some of which are quantitative but a large portion of which are qualitative. These additional audit procedures, particularly in the early years of the rules’ effectiveness, could add both significant time and expense to the annual financial reporting process.

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Certain of the disclosures require significant levels of judgment and subjectivity and may not be conducive to audits. For line items such as revenue, it may be difficult to determine whether a climate-related event, particularly a transition risk, had an impact on the line item. For example, if a company experiences a decline in sales due in part to consumers moving away from the product in favor of a more environmentally-friendly competing product, it may be hard to quantify the extent of the decrease in revenues attributable to the shift in consumer preference, as opposed to other effects (e.g., decline in economy or change in consumer preference for other reasons).

**ICFR, DCP and Oversight.** The Proposed Rules will necessitate the creation of additional oversight functions, both at the board and management levels. As new disclosures will be required in audited financial statements, audit committees will find themselves with added responsibilities.

- Internal control over financial reporting (ICFR) and DCP will need to be expanded to cover the new disclosures, and companies may need to add additional qualified personnel and integrate them into their ICFR and DCP procedures.
- Companies also will need to assess their existing disclosures and the climate information that has already been collected, much of which may have been done without third-party assurance. As companies begin to provide information on a go-forward basis under a mandatory reporting regime, one in which certain emissions disclosures require third-party attestation and certain other disclosures or calculations may be subject to audit, companies may identify deficiencies in their existing disclosures that require correction.

**Governance.** The Proposed Rules do not prescribe governance but rather require disclosure regarding both board and management oversight regarding climate-related risks. A number of the disclosure requirements are quite detailed, and we expect that many companies will implement processes to align with the disclosure requirements. For example, companies would be required to include a description of the process and frequency by which the board (or board committee) discusses climate-related risks, how the board is informed of climate-related risks, and how frequently the board considers climate-related risks.

In addition, the Proposed Rules require disclosure as to whether any member of the board has expertise in climate-related risks, with disclosure required “in sufficient detail to fully describe the nature of the expertise.” Boards may wish to begin considering whether they have members who may have such expertise and if not, whether additional board members may be warranted. As noted above under “Governance of Climate-Related Risks and Risk Management Processes,” unlike directors who are identified as having financial statement expertise or, under the proposed new cyber rules, cyber expertise, the Proposed Rules lack any safe harbor for directors identified as having climate expertise.

### **Impact on Private Companies, Mergers & Acquisitions, Equity Investees and Foreign Private Issuers.**

- **Private Companies.** The Proposed Rules do not provide a phase-in for newly public companies (beyond that which applies to the effectiveness of the Proposed Rules generally). The requirement to include climate-related disclosure with respect to future public offerings could delay, or even impede, private company access to U.S. public capital markets.

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The Proposed Rules would apply to a company with reporting obligations pursuant to Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 (the “Exchange Act”), and companies filing a registration statement under the Exchange Act or the Securities Act of 1933. Because private companies that issue registered debt securities may become subject to the reporting requirements under the Exchange Act, they would be obligated to comply with the proposed climate-related disclosures. The Proposed Rules may shift market practice for Rule 144A and other private securities offering disclosures as well.

- **Mergers & Acquisitions.** The Proposed Rules would have the effect of requiring public company acquirers registering the issuance of securities on Form S-4 to disclose some climate-related information regarding the target company (without regard to whether the target company is public or private). Because the Proposed Rules do not provide accommodations for these companies, they may have meaningful implications for the timing and complexity of M&A transactions.

The Proposed Rules also do not contain any accommodations for newly acquired entities, meaning that a public company acquirer would be required to include climate-related disclosures regarding an entity even if it has not had sufficient time to review that entity’s climate profile, emissions information and other data. This is in contrast, for example, to the rules on internal control over financial reporting, which permit companies and auditors to exclude from the ICFR assessment certain newly acquired entities.

Even if there are accommodations included in the final rules, companies should assess relevant climate-related matters when pursuing acquisition opportunities. By extension, private companies seeking to make themselves attractive acquisition targets for public companies should be cognizant of the new rules and disclosure standards.

- **Equity Investees.** In presenting emissions data, the Proposed Rules would require companies to include in their calculation emissions data from equity method investees, calculated on a proportionate basis. As part of their disclosure controls and procedures, companies will need to assess what contractual and other rights they have to obtain the information necessary to comply with this requirement. As part of the planning process, companies will also need to assess the ability of their existing non-wholly owned consolidated entities and equity method investees to provide the required information. With respect to new joint venture and other equity investments, companies should consider including covenants requiring that this information be provided, similar to covenants that may be included around financial reporting.
- **Foreign Private Issuers.** The Proposed Rules subject foreign private issuers (other than Canadian issuers filing on Form 40-F) to the obligations that apply to U.S. domestic companies, which include the novel financial statement requirements for issuers whose financials are prepared under IFRS-IASB. Although the SEC has partly based its proposals on TCFD and the GHG Protocol (under which many foreign private issuers already report on a voluntary or “comply or explain” basis), as detailed above and in [Appendix A](#), the SEC’s proposed implementation goes far beyond the present scope of disclosure of many such issuers. Furthermore, home country regulation may require foreign private issuers to undertake scenario analysis, or specify climate-related plans, goals or targets, which effectively would make certain optional aspects of the Proposed Rules mandatory. The SEC has asked for feedback on whether it should permit foreign private issuers subject to an alternative reporting regime that the SEC deems substantially similar to the Proposed Rules to satisfy their obligations under the SEC’s rules by complying instead with the requirements of the alternative reporting regime.

**Liability.** The Proposed Rules significantly expand the scope of both historical and forward-looking disclosures that companies will be required to include, on a “filed” basis, in their periodic reports and registration statements. However, the Proposed Rules provide only narrowly targeted safe harbors that are in many respects more limited than the safe harbors that currently exist with respect to information that can be calculated on a much more reliable basis.<sup>32</sup> As one of many examples, the SEC notes that the proposed

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transition periods for assurance over GHG emission disclosures are intended to provide companies with time to familiarize themselves with the GHG emissions disclosure requirements and develop the relevant DCP but the Proposed Rules do not provide a safe harbor for corrections that may result over time as a result of this transition. Furthermore, any adoption of the Proposed Rules would be against the backdrop of the SEC's creation of the Climate and ESG Task Force in the Division of Enforcement in March 2021, which the SEC announced will play a role in "[p]roactively addressing emerging disclosure gaps that threaten investors and the market."

***Timing, Legal Challenges and Comment.*** The Proposed Rules include an aggressive implementation schedule, with reporting for large accelerated filers (with a December 31 fiscal year-end) applying with respect to fiscal year 2023 if the Proposed Rules become effective before the end of this year. However, it is unclear whether the Proposed Rules will be adopted in the form currently proposed. The Proposed Rules will likely elicit vigorous comments and are widely expected to be subject to legal challenges, including on the basis that they exceed the SEC's statutory authority and violate First Amendment rights. Parties that anticipate being affected by the Proposed Rules are encouraged to submit comments as part of the public comment processes. Sullivan & Cromwell intends to comment and is actively consulting with clients and other interested stakeholders about the potential effects of the Proposed Rules.

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## ENDNOTES

- 1 See Press Release, SEC, SEC Extends Comment Period for Proposed Rules on Climate-Related Disclosures, Reopens Comment Periods for Proposed Rules Regarding Private Fund Advisers and Regulation ATS (May 9, 2022), available at <https://www.sec.gov/news/press-release/2022-82>.
- 2 See the proposing release at pp. 16-29, available at <https://www.sec.gov/rules/proposed/2022/33-11042.pdf>.
- 3 See Audit Analytics, The SEC Focuses on Climate Change in Latest Round of Comment Letters (Feb. 24, 2022), available at <https://blog.auditanalytics.com/the-sec-focuses-on-climate-change-in-latest-round-of-comment-letters/>.
- 4 European Commission Press Release IP/21/1804, Sustainable Finance and EU Taxonomy: Commission takes further steps to channel money towards sustainable activities (April 21, 2021), available at [https://ec.europa.eu/commission/presscorner/detail/en/ip\\_21\\_1804](https://ec.europa.eu/commission/presscorner/detail/en/ip_21_1804).
- 5 Press Release, UK Dept. for Business, Energy & Industrial Strategy, UK to Enshrine Mandatory Climate Disclosures for Largest Companies in Law (Oct. 29, 2021) available at <https://www.gov.uk/government/news/uk-to-enshrine-mandatory-climate-disclosures-for-largest-companies-in-law>.
- 6 The Companies (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018 No. 1155 (UK), available at <https://www.legislation.gov.uk/ukdsi/2018/9780111171356/contents>.
- 7 See Sullivan & Cromwell, Biden Administration Announces New Climate Change Initiatives (Feb. 28, 2022), available at <https://www.sullcrom.com/files/upload/sc-publication-biden-administration-announces-new-climate-change-initiatives.pdf>.
- 8 CFTC, Climate-Related Market Risk Subcommittee, *Managing Climate Risk in the U.S. Financial System* (Oct. 2020), available at <https://www.cftc.gov/sites/default/files/2020-09/9-9-20%20Report%20of%20the%20Subcommittee%20on%20Climate-Related%20Market%20Risk%20-%20Managing%20Climate%20Risk%20in%20the%20U.S.%20Financial%20System%20for%20posting.pdf>.
- 9 Board of Governors of the Federal Reserve System, *Financial Stability Report* (Nov. 2020) at 59, available at <https://www.federalreserve.gov/publications/files/financial-stability-report-20201109.pdf>.
- 10 See Sullivan & Cromwell, Financial Stability Oversight Council Report on Climate-Related Financial Risk (Nov. 2, 2021), available at <https://www.sullcrom.com/sc-publication-financial-stability-oversight-council-report-on-climate-related-financial-risk>.
- 11 See Sullivan & Cromwell, OCC Seeks Public Feedback on Principles for Climate-Related Financial Risk Management for Large Banks (Dec. 21, 2021) available at <https://www.sullcrom.com/files/upload/sc-publication-occ-release-and-seeks-feedback-on-principles-for-climate-related-financial-risks-management-for-large-banks.pdf>.
- 12 See News Release, Department of Labor, U.S. Department of Labor Proposes Rule to Remove Barriers to Considering Environmental, Social, Governance Factors in Plan Management (Oct. 13, 2021), available at <https://www.dol.gov/newsroom/releases/ebsa/ebsa20211013>.
- 13 See Sullivan & Cromwell, SEC Adopts Final Rules to Implement the "Conflicts Minerals" Disclosure Requirements of the Dodd-Frank Act (Aug. 31, 2012), available at [https://www.sullcrom.com/siteFiles/Publications/SC\\_Publication\\_SEC\\_Adopts\\_Final\\_Rules\\_to\\_Implement\\_the\\_Conflict\\_Minerals\\_Disclosure\\_Requirements\\_of\\_t.pdf](https://www.sullcrom.com/siteFiles/Publications/SC_Publication_SEC_Adopts_Final_Rules_to_Implement_the_Conflict_Minerals_Disclosure_Requirements_of_t.pdf); Sullivan & Cromwell, Court Vacates SEC Resource Payment Disclosure Rule (July 2, 2013), available at [https://www.sullcrom.com/siteFiles/Publications/SC\\_Publication\\_Court\\_Vacates\\_SEC\\_Resource\\_Payments\\_Disclosure\\_Rule.pdf](https://www.sullcrom.com/siteFiles/Publications/SC_Publication_Court_Vacates_SEC_Resource_Payments_Disclosure_Rule.pdf).
- 14 The TCFD Framework is organized around four core pillars: governance, strategy, risk management, and metrics and targets.
- 15 Similarly, based on a TCFD study in 2021 (available at <https://www.fsb.org/wp-content/uploads/P141021-1.pdf>), companies that are reporting under the framework are not

## ENDNOTES (CONTINUED)

- implementing fully all of the TCFD recommendations, including recommended board and management disclosures.
- 16 “Scope 3 emissions” is defined as “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.” Upstream emissions include emissions attributable to goods and services that the company acquires, the transportation of goods (for example, to the company), and employee business travel and commuting. Downstream emissions include the use of the company’s products, transportation of products (for example, to the company’s customers), end of life treatment of sold products, and investments made by the company.
- 17 The Proposed Rules would require inclusion of GHG emissions from outsourced activities that previously were conducted as part of a company’s own operations when determining whether its Scope 3 emissions are material and when disclosing those emissions.
- 18 Some U.S. public (and private) companies are required to report certain GHG emissions data to the U.S. Environmental Protection Agency (USEPA), which also refers to the GHG Protocol in its reporting program. Companies that provide GHG emissions data under the USEPA’s program may be able to leverage some of their reported data to partially satisfy the disclosures contemplated by the Proposed Rules.
- 19 For companies that use carbon offsets or renewable energy credits as part of their plans to achieve climate-related targets or goals, the Proposed Rules would require disclosure of the amount of carbon reduction, description and location of projects, any authentication and cost.
- 20 The Proposed Rules noted that a financial institution’s Scope 3 emissions disclosures would likely include the so-called “financed emissions” (i.e., emissions from companies to which the financial institution provides debt or equity financing). Although the Proposed Rules would permit financial institutions to use any appropriate methodology to calculate its Scope 3 emissions, the SEC notes that the Partnership for Carbon Accounting Financials’ Global GHG Accounting & Reporting Standard provides one methodology that complements the GHG Protocol and could assist financial institutions in calculating their financed emissions.
- 21 Although the Proposed Rules generally would apply to foreign private issuers, they are not proposed to extend to Canadian issuers reporting under the Multijurisdictional Disclosure System.
- 22 The proposed EU Corporate Sustainability Reporting Directive also includes an attestation requirement that contemplates limited assurance pursuant to standards to be adopted by the European Commission, with the potential for the European Commission to require reasonable assurance in the future.
- 23 Examples of such line items include revenue, cost of revenue, selling, general and administrative expenses, sale of property, plant and equipment (in statement of cash flows), inventories, intangible assets, long-term debt and contingent liabilities.
- 24 See Sullivan & Cromwell, SEC Proposes New Cybersecurity Disclosure Rules for Public Companies (Mar. 11, 2022), *available at* <https://www.sullcrom.com/files/upload/sc-publication-sec-proposes-new-cybersecurity-disclosure-rules-for-public-companies.pdf>.
- 25 See Press Release, SEC Reopens Comment Period for Listing Standards for Recovery of Erroneously Awarded Compensation (Oct. 2021), *available at* <https://www.sec.gov/news/press-release/2021-210>.
- 26 See Sullivan & Cromwell, European Commission Proposes Mandatory Corporate Sustainability Due Diligence and Climate Change Plans (Mar. 7, 2022), *available at* <https://www.sullcrom.com/sc-publication-eu-proposes-mandatory-corporate-sustainability-due-diligence-and-climate-change-plans?msclid=d65da294ad2f11ecb38a03a5e185fde3>.
- 27 Financial regulators have identified scenario analysis as a key emerging tool in the study of climate-related financial risks. In particular, in the Principles for Climate-Related Financial Risk Management for Large Banks, the OCC noted that management should develop and implement climate-related scenario analysis frameworks in a manner commensurate to the bank’s size, complexity, business activity and risk profile. See *supra* Note 11.
- 28 See *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976).
- 29 See SEC Staff Accounting Bulletin No. 99, 17 Fed. Reg. 211 (Aug. 12, 1999).
- 30 See European Commission Press Release, *supra* Note 4.

ENDNOTES (CONTINUED)

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- <sup>31</sup> In December 2009, the USEPA issued an “endangerment and cause or contribute finding” for GHG emissions under the Clean Air Act, which enabled the USEPA to craft rules to directly regulate GHG emissions, and, on January 1, 2010, the USEPA began requiring large emitters of GHG to collect and report data with respect to their GHG emissions. *West Virginia v. Environmental Protection Agency*, currently pending in the United States Supreme Court, challenges the ability of USEPA to regulate carbon dioxide emissions related to climate change and could significantly impact the agency's future ability to regulate GHG emissions.
- <sup>32</sup> Although certain climate-related information will be protected by the forward-looking statement safe harbors under the Private Securities Litigation Reform Act (“PSLRA”), these safe harbors are not available for registration statements. Moreover, the SEC specifically notes in the proposing release that the PSLRA also does not limit the SEC’s ability to bring enforcement actions.

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Appendix A

**Comparison with TCFD**

TCFD Recommendation	SEC Proposed Rules
<p><i>Governance:</i> Describe the board’s oversight of climate-related risks and opportunities.</p>	<p>Describe the board of directors’ oversight of climate-related risks, including, as applicable, the identity of any board member with climate-related expertise and other details summarized in “Summary of the Proposed Rules” above.</p> <p>If applicable, discuss the board’s oversight of climate-related opportunities, but such discussion is not required.</p>
<p><i>Governance:</i> Describe management’s role in assessing and managing climate-related risks and opportunities.</p>	<p>Describe management’s role in assessing and managing climate-related risks, including, as applicable, the identity of any members of management with climate-related expertise and other details summarized in “Summary of the Proposed Rules” above.</p> <p>If applicable, discuss management’s oversight of climate-related opportunities, but such discussion is not required.</p>
<p><i>Strategy:</i> Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term.</p>	<p>Describe any climate-related risks reasonably likely to have a material impact on the company, including on its business or consolidated financial statements, over the short, medium and long term. This discussion should specify whether such risks are physical or transition risks and the nature of the risks presented (including the location of properties subject to material physical risk by ZIP or similar postal code). In addition, the company must describe how it defines short, medium and long term horizons.</p> <p>If applicable, disclose the actual and potential impact of any climate-related opportunities, but such discussion is not required.</p>
<p><i>Strategy:</i> Describe the impact of climate-related risks and opportunities on the organization’s businesses, strategy, and financial planning.</p>	<p>Describe the actual and potential impact of any climate-related risks identified on the company’s strategy, business model and outlook.</p> <p>In addition, discuss whether and how any impacts are considered as part of the company’s business strategy, financial planning and capital allocation, as well as whether and how any such risks have affected or are reasonably likely to affect the company’s consolidated financial statements.</p> <p>Discuss how any of the new climate-related financial statement metrics or any of the company’s own climate-related goals and targets are used in the company’s strategy and analysis, and whether it maintains an internal carbon price.</p>

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TCFD Recommendation	SEC Proposed Rules
<p><i>Strategy:</i> Describe the resilience of the organization’s strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.</p>	<p>Describe the resilience of the company’s business strategy in light of potential future change in climate-related risks. Describe any analytical tools, such as scenario analysis, that the company uses to assess the impact of climate-related risks on its business and consolidated financial statements.</p> <p>While the Proposed Rules do not require scenario analysis, if the company uses scenario analysis to assess the resilience of its business strategy, it must disclose the scenarios considered, including parameters, assumptions and analytical choices, as well as the projected principal financial impacts on the company’s business strategy under each scenario.</p>
<p><i>Risk Management:</i> Describe the organization’s processes for identifying and assessing climate-related risks.</p>	<p>Describe any processes the company has for identifying, assessing and managing climate-related risks.</p> <p>If applicable, describe any processes for identifying, assessing and managing climate-related opportunities, but such description is not required.</p>
<p><i>Risk Management:</i> Describe the organization’s processes for managing climate-related risks.</p>	<p>Same as above.</p>
<p><i>Risk Management:</i> Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organization’s overall risk management.</p>	<p>Describe how any climate-related risk identification and management processes are integrated into the company’s overall risk management system or process. If a separate board or management committee is responsible for managing climate-related risks, disclose how such committee interacts with the committee governing general risks.</p> <p>If the company has adopted a transition plan as part of its climate-related risk management strategy, describe the plan, including relevant metrics and targets.</p>
<p><i>Metrics and Targets:</i> Disclose the metrics used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process.</p>	<p>Financial statement disclosure under three categories of financial statement metrics: (i) financial impact metrics, (ii) expenditure metrics and (iii) financial estimates and assumptions.</p> <p>For each type of financial statement metric used, provide contextual information, describing how each specified metric was derived, including a description of significant inputs and assumptions used, and if applicable, policy decisions made by the company to calculate such metrics.</p>

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TCFD Recommendation	SEC Proposed Rules
<p><i>Metrics and Targets:</i> Disclose Scope 1, Scope 2 and, if appropriate, Scope 3 greenhouse gas (GHG) emissions and the related risks.</p>	<p>Disclose total Scope 1 emissions and total Scope 2 emissions separately after calculating them from all sources that are included in the company's organizational and operational boundaries.</p> <p>Accelerated filers and larger accelerated filers must provide an attestation report covering their Scope 1 and 2 emissions disclosure in the relevant filing.</p> <p>The Proposed Rules would phase in the requirements for such attestation over the second, third and fourth years after the rule's compliance date.</p> <p>Disclose Scope 3 emissions if (i) such emissions are material or (ii) the company has set a GHG emissions reduction target or goal that includes its Scope 3 emissions. If required, such disclosure should identify the categories of upstream and downstream activities included in the calculation and if a category of Scope 3 emissions is significant to the company it must identify such category and separately provide emissions data for such category. In addition, describe the data sources used to calculate its Scope 3 emissions.</p> <p>Smaller reporting companies are exempt from reporting Scope 3 emissions.</p>
<p><i>Metrics and Targets:</i> Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets.</p>	<p>Disclose any targets or goals related to the reduction of GHG emissions, or any other climate-related target or goal, including, as applicable, a description of the scope of activities and emissions included in the target, the unit of measurement, the defined time horizon by which the target is intended to be achieved, the defined baseline period and emissions against how progress will be tracked, any interim targets and how the company intends to meet its target of goals.</p> <p>In addition, if the company sets targets or goals, disclose the relevant data to indicate whether the company is making progress toward meeting its targets and goals and how such progress has been achieved. Companies must report if they used carbon offsets to achieve their climate-related targets or goals.</p>

Appendix B<sup>(a)</sup>

1. Disclosure Compliance Dates

Filer Type	Disclosure Compliance Date		Statement Metrics Audit Compliance Date
	All proposed disclosures, other than Scope 3 GHG emissions metrics	Scope 3 GHG emissions metrics	
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Same as Disclosure Compliance Date
Accelerated Filer and Non-Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	
Smaller Reporting Company	Fiscal year 2025 (filed in 2026)	Exempted	

2. Attestation Compliance Dates

Filer Type	Disclosure Compliance Date (No Assurance)	Limited Assurance <sup>(b)</sup>	Reasonable Assurance <sup>(c)</sup>
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Fiscal year 2026 (filed in 2027)
Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Fiscal year 2027 (filed in 2028)

<sup>(a)</sup> Assumes a fiscal year end of December 31. The SEC indicated a company with a different fiscal year-end date that results in its fiscal year 2023 commencing before the effective date of the rules would not be required to comply until the following fiscal year.

<sup>(b)</sup> Reasonable assurance is equivalent to the level of assurance provided in an audit of a company's consolidated financial statements included in a Form 10-K or Form 20-F annual report.

<sup>(c)</sup> Limited assurance is equivalent to the level of assurance (commonly referred to as a "review") provided over a company's interim financial statements included in a Form 10-Q.