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SEC Issues Final Rule on Climate Disclosures

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In an open meeting on Wednesday, March 6, 2024, the Securities and Exchange Commission ("SEC") approved in a 3-2 vote a Final Rule on climate disclosures that will "require registrants to provide certain climate-related information in their registration statements and annual reports."[1] As many expected, the Final Rule, available here, includes significant cutbacks to the requirements contained in the initial proposal, most notably dropping Scope 3 disclosure requirements. Nevertheless, the rule solidifies a standardized disclosure regime under which public companies are to inform investors of their climate-related impacts and risks. Given the breadth of the Final Rule (850+ pages), we will publish a fuller analysis in due course, including how companies should plan for compliance, particularly companies who are also subject to reporting under the EU's Corporate Sustainability Reporting Directive (CSRD).

The Final Rule will be effective 60 days after its publication in the Federal Register. However, issuers will need to comply with the disclosure requirements set forth in the new rules on a gradual basis, depending on the disclosure item itself and the issuer's filer type. In addition, the Final Rule provides smaller reporting companies ("SRCs") and emerging growth companies ("EGCs") an exemption from the Scope 1 and Scope 2 emissions disclosure requirements.

In brief, the Final Rule will require registrants to disclose, among other things:

- material climate-related risks and their impact on the registrant's business;
- activities to mitigate or adapt to such risks and material expenditures incurred for such activities;
- information about the registrant's board of directors' oversight of climate-related risks and management's role in managing material climate-related risks;
- the registrant's processes for identifying, assessing and managing material climate-related risks;
- information on any climate-related targets or goals that are material to the registrant's business, results of operations or financial condition; and
- any costs, expenditures, charges and losses incurred as a result of severe weather events or related to certain carbon offsets and renewable energy credits.

Additionally, larger registrants will be required to disclose certain information related to Scope 1 and/or Scope 2 greenhouse gas ("GHG") emissions, to the extent such emissions are material, and provide varying levels of assurance reports on such disclosure.[2]

The Final Rule repeats the SEC's mantra that investors need "consistent, comparable and reliable" disclosure regarding the climate-related risks an issuer faces in order to make informed investment and voting decisions. The SEC points out that many issuers already provide climate- and GHG emissions-related disclosure outside of their SEC filings, but that the utility of such information is limited since its presentation is inconsistent among issuers or even among an issuer's year-over-year disclosure, making comparisons difficult. Furthermore, these disclosures are often challenging to locate, and are not subject to the stringent standards imposed by the disclosure controls and procedures necessary for SEC filings. In addition, the SEC stated that it "has been and remains agnostic about whether or how registrants consider or manage climate-related risks" and that the Final Rule was adopted and should be read "to advance […] investor protection, market efficiency and capital formation objectives…and not to address climate-related issues more generally."[3]

The SEC's Proposed Climate Disclosure Rules

The SEC's climate disclosure rules were first proposed in March 2022 and were based heavily on the existing disclosure frameworks of the Task Force on Climate-related Financial Disclosures and the Greenhouse Gas Protocol. The proposed rules would have required public companies to disclose two forms of climate-change impacts: physical risks, which refer to climate-related impacts on company operations; and transition risks, which refer to transition plans and costs associated with reducing Scope 1, 2 and 3 GHG emissions.

The originally proposed rules were the subject of significant comment, and the SEC postponed issuance of the Final Rule numerous times. While most climate activists supported additional regulation with some even urging the SEC to enhance their stringency, industry groups lobbied for the SEC to scale back the proposed disclosure requirements.

Industry groups expressed concern about the difficulty of complying with mandatory disclosure requirements for Scope 3 emissions, which would have required companies to report indirect emissions linked with their supply chains. There have also been calls to increase the proposal's 1% impact threshold for triggering a mandatory disclosure of the financial impact of climate-related events. Furthermore, companies requested additional leniency with respect to reporting deadlines, particularly for Scope 1 emissions, which are GHG emissions derived from sources that are owned or controlled by a company, and Scope 2 emissions, which are indirect emissions derived from a company's energy production in its operations.

Important Changes in the Final Rule

After nearly two years of delays and over 22,500 comment letters—including 4,500 unique comment letters—many monitoring the proposed rules believed that the SEC was poised to make significant cutbacks in the final version of the rules. This speculation rings true in the final version adopted as a number of key disclosure requirements contained in the proposed rules have been loosened or eliminated entirely.

The following is a list of some of the important changes incorporated into the Final Rule that companies should note:

- **Scope 3 emission disclosures eliminated:** One of the most high-profile points of contention in the proposed rules, the reporting requirement for Scope 3 GHG emissions and its safe-harbor provision, is eliminated in the Final Rule. Thus, companies are not required to provide any disclosure of emissions originating in their value chains.

- **Reduced Scope 1 and 2 disclosure requirements:** The Final Rule requires only large accelerated filers and accelerated filers (that are not SRCs or EGCs) to report Scope 1 and 2 emissions that they assess would be "material" to a "reasonable investor." The exemption for SRCs and EGCs and the provision for certain materiality assessments did not exist in the proposed rules, which would have imposed blanket requirements on all applicable companies to disclose their Scope 1 and 2 emissions. In addition, the assurance requirement regarding Scope 1 and Scope 2 emissions was relaxed by enabling large accelerated filers additional time to provide reasonable assurance and limiting accelerated filers to limited assurances.

- **Provision for delayed GHG disclosure:** The Final Rule enables registrants to incorporate by reference into their Form 10-K from their second quarter Form 10-Q GHG emissions disclosure related to the prior fiscal year. Foreign private issuers not filing on domestic forms are able to file GHG emissions disclosure in an amendment to their Form 20-F no later than 225 days after the end of the fiscal year to which the GHG metrics disclosure relate.

- **Elimination of material changes updates in Form 10-Q (or Form 6-K for foreign private issuers):** The Final Rule will not require issuers to provide disclosure regarding material changes to the climate-related disclosure set forth in their Form 10-K or registration statement in their Form 10-Qs.

- **Safe harbor from private liability:** The Final Rule provides a safe harbor from private liability for certain climate-related disclosures, other than historic facts, in addition to the existing safe harbors for forward-looking statements available under the Securities Act and the Exchange Act.

- **Extended Phase-in Period:** Compliance dates pursuant to the Final Rule vary based on the filer status of the issuer. The first disclosure items (including most disclosure called for by the new Regulation S-K and Regulation S-X items) will be required from large accelerated filers for annual disclosures related to the fiscal year beginning 2025 (i.e., to be included in a Form 10-K for the fiscal year ended December 31, 2025, filed in 2026) and the last disclosure required (reasonable assurance on GHG emissions for large accelerated filers) will be phased in related to annual disclosure for the fiscal year beginning 2033. Issuers will be required to comply with the new rules in registration statements that are required to include financial information for the full fiscal year in which the annual disclosure is required.

Key Points of Discussion

During the open meeting, the majority of Commissioners who voted in favor of the Final Rule—Commissioners Gensler, Crenshaw and Lizárraga—emphasized the need for a consistent, comparable and reliable means to inform investors of companies' climate-related risks. As Commissioner Crenshaw stated, "[The Final Rule] establishes a floor for [a] disclosure framework that will provide investors with climate risk information, help inform investors' investment decisions, and be subject to the rigor of Commission filings." The proponents of the Final Rule, in advocating for its legality, further noted that the new disclosure requirements are "no different from many of the Commission's existing disclosure

requirements" passed and amended over the SEC's nine-decade history—which the SEC then underscored by a 14 page discussion in the Final Rule.

Meanwhile, Commissioners Peirce and Uyeda, who voted against the rule, characterized it as "climate-related regulations" and an overreach of the SEC's regulatory authority. They also expressed concern about the costs associated with companies' efforts to meet the disclosure requirements and the rule's inclusion of ambiguous materiality metrics.

Next Steps

As noted above, we will publish a fuller discussion of the Final Rule's requirements, as well as its implications for industry and the ESG legal landscape globally.

Meanwhile, litigation over these rules will certainly follow from industry groups that are still dissatisfied with their stringency, as well as potentially from green groups' discontent with the cutbacks to the proposed rules. In fact, the West Virginia Attorney General has already announced a coalition of 10 states planning to file a legal challenge to the SEC's climate disclosure rule.[4]

Nevertheless, thousands of SEC reporting companies will presumptively be subject to enhanced climate disclosure requirements under the new climate disclosure rules. It is critical that companies act quickly to implement the internal mechanisms necessary to comply with these enhanced regulations.

If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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[1] https://www.sec.gov/os/sunshine-act-notices/sunshine-act-notice-open-030624.

[2] https://www.sec.gov/files/33-11275-fact-sheet.pdf.

[3] https://www.sec.gov/files/rules/final/2024/33-11275.pdf (pg. 18-19).

[4] SEC Climate Disclosure Petition for Review.pdf (wv.gov).

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