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SEC Adopts Climate-Related Disclosure Rules for Public Companies

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On March 6, 2024, the U.S. Securities and Exchange Commission (SEC), by a 3 to 2 vote, adopted new climate-related disclosure rules for public companies. The adopting release is titled "The Enhancement and Standardization of Climate-Related Disclosures for Investors," SEC Release Nos. 33-11275, 34-99678 (Adopting Release).

To implement these new rules, the SEC created a new subpart 1500 of Regulation S-K and Article 14 of Regulation S-X. The new subpart 1500 governs the general climate-related disclosures that companies must make while Article 14 of Regulations S-X governs the climate-related disclosures companies must make in their financial statements.

Required Disclosures

Under the new rules, a public company must disclose the following:

- **Climate-Related Risks.** Any climate-related risks that have materially impacted or are reasonably likely to have a material impact on the company, including on its strategy, results of operations and financial condition.
- **Impacts of Climate-Related Risks.** The actual or potential material impacts of the material climate-related risks on the company's strategy, business model and outlook.
- **Financial Statement Effects.** A quantitative and qualitative description of material expenditures incurred and material impacts on financial estimates and assumptions that directly result from material climate-related risk mitigation or adaptation activities.
- **Risk Mitigation Activities.** A company's activities, if any, to mitigate or adapt to a material climate-related risk or use of transition plans, scenario analysis or internal carbon prices to manage a material climate-related risk.
- **Governance and Management.** Information regarding any oversight by the company's board of directors of climate-related risks and any role by management in assessing and managing material climate-related risks.

- **Risk Management.** A description of any processes the registrant uses to assess or manage material climate related risks and, if the company is managing those risks, whether and how any such processes are integrated into the registrant's overall risk management system or processes.

- **Targets and Goals.** Information regarding a 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 (examples include material expenditures, material impacts on financial estimates and assumptions as a direct result of the target or goal or actions taken to make progress toward meeting such target or goal).

Article 14 to Regulation S-X will require a public company to disclose certain climate-related matters in the notes to the company's financial statements, including:

- The capitalized costs, expenditures expensed, charges and losses incurred as a result of severe weather events and other natural conditions, like hurricanes, tornadoes, flooding, drought, wildfires, extreme temperatures and sea level rise.

- The capitalized costs, expenditures expensed and losses related to carbon offsets and renewable energy credits or certificates if used as a material component of a company's plans to achieve its disclosed climate-related targets or goals.

- If the estimates and assumptions a 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, a qualitative description of how the development of such estimates and assumptions were impacted.

Large accelerated filers (LAF) and accelerated filers (AF) will also have to disclose information regarding their material Scope 1 and Scope 2 greenhouse gas (GHG) emissions. In tandem with Scope 1 and Scope 2 disclosures, the disclosing company must provide an attestation report covering these emissions as described in more detail below. The SEC decided to exempt all smaller reporting companies (SRC), emerging growth companies (EGC) and non-accelerated filers (NAF) from disclosing Scope 1 and Scope 2 emissions and the related attestation requirement. The final rule differs from the proposed rule whereby the SEC would have required reporting companies to disclose Scope 3 emissions (*i.e.*, the emissions generated by its supply chain).

Importantly, the SEC clarified in the Adopting Release that the materiality threshold for these new rules remains the same as other SEC materiality reporting thresholds. Therefore, companies are not to consider the importance of the climate-related issues, but instead, companies must consider the importance of the information as it is related to investment and voting decisions of the company. In this regard, "material" has previously been defined as a "substantial likelihood that a reasonable investor would consider it important when determining whether to buy or sell securities or how to vote or [how] such a reasonable investor would view omission of the disclosure as having significantly altered the total mix of information made available."

Compliance Timeline

The final rules will be effective 60 days following publication of the Adopting Release in the Federal Register. Even then, the SEC has adopted a "phase-in" compliance approach whereby the date in which a company must comply varies depending on the type of registrant the company is. Accordingly, an LAF must include climate related disclosures in its filing for its fiscal year beginning during calendar year 2025 and an AF will have to make climate-related disclosures in its filing for its fiscal year beginning during calendar year 2026. An SRC, EGC or NAF does not have to include these disclosures filings until its filing for its fiscal year beginning during calendar year 2027. The SEC has noted this phased-in compliance approach will allow companies to create and implement processes and methods to track and gather the relevant information necessary for disclosure.

The SEC is also requiring all companies, no matter the registrant type, to comply with electronic tagging. This requirement is consistent with other financial filings companies must file with the SEC. Like the disclosure requirements, compliance with electronic tagging of these climate related disclosures will be phased in. LAFs and AFs must comply with electronic tagging in their 2027 filings while SRCs, EGCs and NAFs must comply with this requirement in their 2028 filings.

Attestation Reports

By 2030, LAFs reporting their Scope 1 and 2 emissions must obtain an attestation report at the "limited assurance" level and by 2034, LAFs must also obtain attestation reports at the "reasonable assurance level." AFs reporting their Scope

1 and 2 emissions must obtain attestation reports at the "limited assurance" level in 2032. Because the SEC is not yet requiring SRCs, EGCs and NAFs to report their Scope 1 and 2 emissions, these companies will not have to submit an attestation report. These assurance levels are only the minimum assurance levels required at the relevant time period, however, at any time the companies may voluntarily obtain a higher level of assurance. The SEC noted that limited assurance requires the company to "express a conclusion about whether it is aware of any material modifications that should be made to the subject matter in order for it to be fairly stated in accordance with the relevant criteria." Moreover, reasonable assurance "provides positive assurance that the subject matter is free from material misstatement."

The attestation report must be provided pursuant to standards that are publicly available at no cost or that are widely used for GHG emissions assurance, and established by a body or group that has followed due process procedures, including the broad distribution of the framework for public comment. In the Adopting Release, the SEC observed that attestation standards of the Public Company Accounting Oversight Board (PCAOB), the American Institute of Certified Public Accountants (AICPA), the International Auditing and Assurance Standards Board (IAASB) and the International Organization for Standardization (ISO) would meet these requirements.

The final rules set forth the required criteria for an attestation report provider. The attestation report provider must be (1) an expert in GHG emissions by virtue of having significant experience in measuring, analyzing, reporting or attesting to GHG emissions; and (2) independent with respect to the registrant, and any of its affiliates, for whom it is providing the attestation report, during the attestation and professional engagement period.

The attestation report would not be considered "expert" disclosure within the meaning of Sections 7 and 11 of the Securities Act of 1933 (the Securities Act). However, an acknowledgment letter from the attestation report provider will need to be filed as an exhibit to registration statements or periodic reports incorporated into registration statements as with auditor consents.

Treatment for Purposes of the Exchange Act and Securities Act

Because these disclosures will be included in SEC filings, and therefore will be treated as "filed," reporting companies will be subject to enhanced liability under Section 18 of the Securities Exchange Act of 1934 (the Exchange Act). The disclosures will also be subject to potential liability under Section 11 of the Securities Act if including in or incorporated by reference into a registration statement under the Securities Act. Therefore, companies should diligently and carefully disclose this information to avoid SEC enforcement actions.

How to Disclose

The new climate-related disclosures will be required in Annual Reports on Form 10-K. In addition, the disclosure must appear in Registration Statements on Form S-1, including for IPOs, and is incorporated by reference into Registration Statements on Form S-3. The SEC left it up to the companies for the exact placement of the disclosures within the relevant reporting forms. Companies may create a new section entitled "Climate-Related Disclosure" or to simply include these new disclosures in already existing parts of the registration statement or annual report such as Risk Factors, Description of Business, or Management's Discussion and Analysis of Financial Condition and Results of Operations.

Moving Forward

The SEC's new climate-related disclosure rules raise various complex issues that public companies should closely monitor, including:

- **Keep track of litigation challenging the new rules.** The SEC's climate-related disclosure rules are already being challenged in multiple federal courts across the country, including by Republican-led states, energy companies and other plaintiffs who are challenging the rules for going too far and, by the Sierra Club, that claims the rules do not go far enough. With multiple lawsuits filed in various circuit courts, there will likely be a procedural fight to determine the court that will handle the litigation. Depending on the court, a stay of enforcement of the new rules is possible. Ultimately the case could end up at the Supreme Court of the United States after a prolonged legal battle that could delay implementation.

- **SEC's 2010 climate guidance is still in effect**. Until the new disclosure rules take effect and pending any legal challenges to them, the SEC's 2010 guidance will continue to be relevant as it expresses the SEC's view of the application of existing SEC rules such as those relating to disclosure regarding environmental laws and regulations.

- **Prepare for alignment with other related disclosure requirements**. Many public companies may also be subject to other climate-related disclosure requirements in addition to the SEC rules. For instance, California recently enacted two similar laws requiring both private and public companies to report and disclose climate related information to the state and provide climate related information on the company's website. California's Climate Redacted Financial Risk Act requires private and public U.S. companies that "do business in California" and have more than $500 million in annual revenue to disclose their climate-related financial risk and measures on the company's website no later than January 2026. Also, California's Climate Corporate Data Accountability Act requires certain public and private U.S. companies that "do business in California" and have more than $1 billion in annual revenues, to disclose their GHG emissions by 2026. These California laws are also subject to pending litigation. In addition, U.S. companies with subsidiaries or other operations in the European Union may also be subject to its Corporate Sustainability Reporting Directive which takes effect beginning in 2026. The United Kingdom has also adopted disclosure requirements.

- **Begin evaluating how the final rules will affect your future disclosure, operations and climate-related goals.** Public companies should begin assessing the actions they will need to comply with the various reporting requirements which may be applicable. While LAFs and other larger companies typically have some form of disclosure and risk evaluation program in place, they will have less time to comply with the new rules and have the added burden of disclosure and attestation requirements for Scope 1 and Scope 2 emissions. Smaller companies have more time but may have little to no existing programs in place.
- **Consider liability risks**. As noted, the new disclosure requirements are subject to liability under the Exchange Act and Securities Act for material misstatements. Any climate-related disclosures should be subject to controls and procedures consistent with other reporting requirements. Litigation and other challenges are becoming more common when there is a disconnect with corporate disclosures such as sustainability statements and actual practices. New disclosure rules can be expected to increase the litigation risk.

If you have any questions about the new rules, changes to your policies and procedures or other securities law matters, please contact Benjamin Lombard, another member of the Reinhart Securities Team or your Reinhart attorney.

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