# The SEC's Climate Rule*

## *What it Means for Companies and Investors

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**On March 21st, 2022, the United States Securities and Exchange Commission (SEC) released a draft rule for the Enhancement and Standardization of Climate-Related Disclosures for Investors.**

After a protracted rulemaking timeline, the SEC has finally adopted the regulation mandating climate-related financial disclosures for public companies.

The key purpose of this regulation is to collect and make available decision-useful information for investors to assess the climate change risks in their portfolios. Investors will benefit from these standardized disclosures to assess companies' exposure to climate risks and initiate portfolio decarbonization to meet net-zero commitments.

The passing of the SEC climate rule on March 6th, 2024, is a landmark moment in U.S. climate policy, and sets a precedent for future legislation on sustainability-related financial reporting in the U.S.

The SEC's 2024 agenda shows that the financial regulator is betting big on disclosure rulemaking as it hopes to meet evolving investor needs through increased transparency and comparability of information.

# Corporate Climate Disclosure Regulations

Once enforced, the SEC climate rule will require registrants to i) report and attest their Scope 1 and 2 emissions when those emissions are material (specifically larger registrants); ii) assess the impact of severe weather events and transition activities in their financial statements and; iii) provide qualitative information on material climate risks including but not limited to climate-related targets and board oversight and management of climate risks.

So far, federal regulation on climate-related financial reporting has been limited in scope, only covering federal contractors and suppliers. The SEC rule is significant as it extends to all listed issuers.

Federal Acquisition Regulation: Disclosure of Greenhouse Gas Emissions and Climate-Related Financial Risk

Federal Supplier Climate Risks and Resilience Rule, Climate-Related Financial Risk Executive Order

California Climate Package: CA SB 253, CA SB 261

At the state level, California is at the forefront of climate policy action. In 2023, California Governor Gavin Newsom signed two climate disclosure bills – the Climate Corporate Data Accountability Act (CA SB 253) and the Climate-related Financial Risk Act (CA SB 261) – into law.

**CA SB 253**

CA SB 253 will require companies with over $1 billion in annual revenues to report GHG emissions, with mandatory disclosure of Scopes 1 and 2 from 2026 and Scope 3 in 2027 and annually thereafter.

**CA SB 261**

CA SB 261 is designed to help covered companies conduct climate risk assessments in accordance with the Taskforce for Climate-related Financial Disclosure (TCFD) recommendations.

Compared to the SEC climate rule, the California climate laws introduce enhanced GHG disclosure requirements, notably Scope 3 reporting from 2027 on financial year 2026 data.

Despite the SEC scaling back its requirements, the rule will at once incentivize companies to incorporate climate considerations into their business strategy and enable investors to make well-informed decisions based on the sustainability characteristics of their assets.

The test batch of companies subject to the federal rule and/or state legislation will indicate the quality of quantitative data and may form the basis for determining key reporting indicators for climate and ESG reporting.

## SEC Climate Rule: Policy Timeline

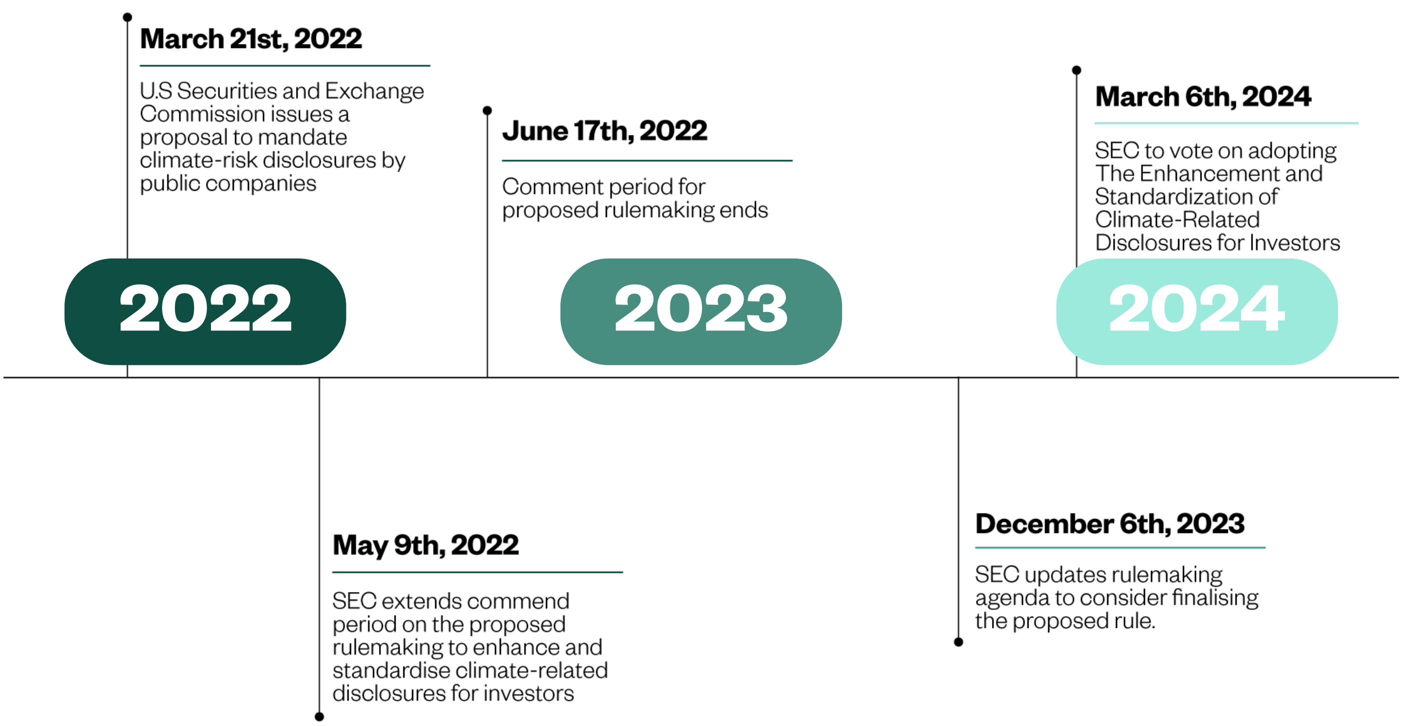
Since its initial release, the SEC climate rule draft has been controversial for including a Scope 3 emissions disclosure requirement. Several groups across the political and financial landscape argued that this would impose an undue compliance burden on companies which would have to allocate significant resources for reporting value chain emissions.

There has been a more fundamental backlash on the grounds that the SEC was overextending its regulatory reach in the first place: expanding beyond securities regulation into climate action.

Politics surrounding the rulemaking led to a considerable delay in its enactment, as seen in Figure 1. On March 6th, 2024, the SEC adopted the final rule, albeit a watered-down version that dropped the original requirement for Scope 3 disclosure.

Climate litigation and politicking may continue to be potential obstacles to the effective enforcement of the SEC climate rule. We are already seeing civil lawsuits coming out of the woodwork in California, blocking the progress made by state legislators and companies that advocated for progressive legislation on climate disclosure.

**Figure 1**



# So, what does the SEC's climate rule mean for companies, and investors?

## Key takeaways

- The SEC's new rule will push U.S. companies to catch up with increasingly global norms around climate disclosure. In Europe, for example, the Corporate Sustainability Reporting Directive (CSRD) requires large companies to prepare environmental, social, and governance information, applying more stringent climate disclosure requirements than the SEC.

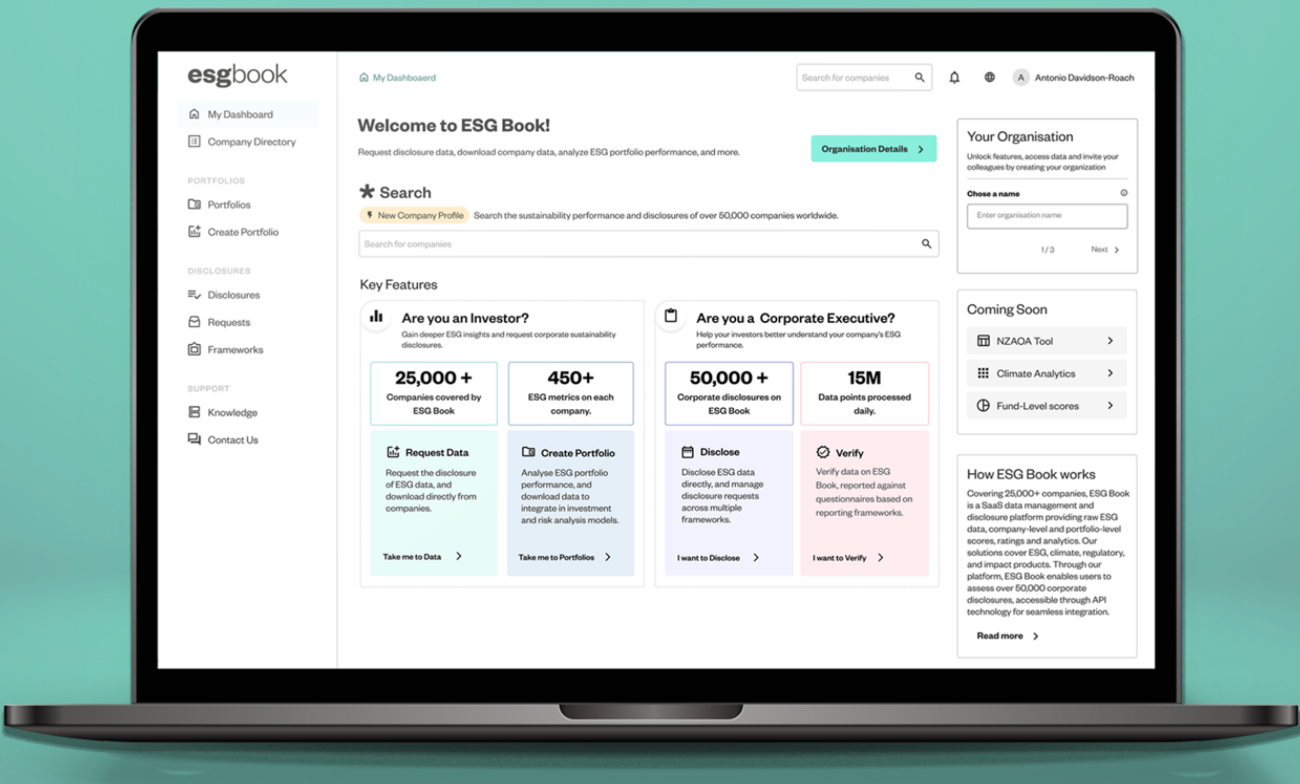
- The reporting of Scope 1 and Scope 2 data will be mandatory for large public companies. However, the final version of the SEC's rule abandons the disclosure requirements for Scope 3 emissions. While this will lessen the reporting burden and compliance costs for large companies compared to the original proposal, investor demand for Scope 3 reporting will only continue to grow, and many U.S. companies will still be required to disclose this data in other jurisdictions.

- The new rule will require companies to include their climate disclosures as part of their annual filings with the SEC, with the largest companies having to start reporting emissions for fiscal year 2026.

- Investors will be the primary audience of the disclosures resulting from the SEC's climate rule. While some have argued that the final ruling does not go far enough in comparison to global standards, it will undoubtedly bring about greater transparency on the climate-related risks for some of the world's largest companies, in turn providing investors with better insights to inform decisions around capital allocation for a net zero future.

**Gain access to one of the market's largest and most comprehensive data sets on estimated Scope 3 emissions through ESG Book. Our Emissions Estimation Model covers the emissions of over 45,000 companies worldwide, including all 15 categories of Scope 3, to provide you with a competitive edge in climate risk management.**

**Contact our team today to learn more.**

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