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The SEC's Landmark Climate Disclosure Rules: Considerations for Non-U.S. Public Companies

I. Introduction

On 6 March 2024, the U.S. Securities and Exchange Commission (the "**SEC**" or the "**Commission**") adopted longawaited climate-related disclosure rules for public companies (the "**Final Rules**").[1] The Final Rules, although not as prescriptive as the rules that were proposed almost two years prior (the "**Proposed Rules**"),[2] contain sweeping requirements that significantly expand the climate-related disclosure that public companies will have to make and thus will impose significant burdens on such companies.

The Final Rules apply to both domestic and most foreign private issuers ("**FPIs**"), regardless of industry sector, and to annual reports and registration statements. As explained in Section IV below, compliance obligations are phased in at different times depending on the requirement and the registrant's filer status, with the first filing deadline occurring as early as March 2026 for large accelerated filers ("**LAFs**"), covering fiscal years beginning ("**FYB**") in 2025.

As discussed further in Section X below, litigation challenging the Final Rules was filed immediately in a number of federal courts and was consolidated in the U.S. Court of Appeals for the Eighth Circuit on 21 March 2024. The SEC voluntarily stayed the Final Rules on 4 April 2024 pending completion of the Eighth Circuit litigation, which the staff of the SEC has indicated will likely affect the compliance deadlines.

II. Key Takeaways

- The Final Rules require disclosure about board and management governance of climate-related risks, material impacts of such risks, processes for managing such risks, transition plans used to manage material transition risks and climate-related targets or goals that materially affect the company's business, among other related topics.
- The Final Rules do not require Scope 3 greenhouse gas ("**GHG**") emissions disclosures for any registrants; however, they do require disclosure of Scope 1 and/or 2 GHG emissions metrics, if material, by accelerated filers ("**AFs**") and LAFs on a phased-in basis starting in 2027 for LAFs (covering FYB 2026) and 2029 for AFs (covering FYB 2028).
    - Disclosure of material Scope 1 and/or 2 GHG emissions metrics may be provided in an amendment to registrants' Form 20-F due 225 days after the end of the fiscal year to which such metrics relate.
    - As with many of the disclosures in the Final Rules that are materiality-qualified, registrants should ensure they have appropriate controls, procedures and documentation regarding the materiality determination of their GHG emissions.
    - As described in Section IX below, while the SEC has expressly incorporated the traditional U.S. definition of materiality, there are

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1 *See* Enhancement and Standardization of Climate-Related Disclosures for Investors, 89 Fed. Reg. 21668 (6 March 2024) (the "**Adopting Release**").

2 *See* Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 Fed. Reg. 21334 (21 March 2022) (the "**Original Proposal**").

additional discussions in the Adopting Release that should guide how companies undertake materiality analyses under the Final Rules.

- Attestation reports regarding GHG emissions metrics will be required on a phased-in basis starting in 2030 for LAFs (covering FYB 2029) and 2032 for AFs (covering FYB 2031); the reports must be done at a limited assurance level, with a step up to reasonable assurance for LAFs four years later.
- The Final Rules also require registrants to disclose any climate-related target or goal set by the registrant – whether or not already publicly disclosed – that has materially affected or is reasonably likely to materially affect the registrant's business, results of operations or financial condition, as well as provide annual updates on the progress made towards such target or goal.
  - We expect this disclosure to be closely scrutinized by investors from year to year. Companies may face shareholder engagement with both traditional investors and activists if they are not disclosing sufficient progress towards their goals.
  - There is no provision in the Final Rules that would allow companies to exclude targets or goals framed in terms of Scope 3 GHG emissions, meaning registrants may need to report progress regarding a climate-related goal that includes their Scope 3 emissions such as a net-zero goal (which would in turn require coverage of such Scope 3 emissions in their disclosure controls and procedures maintained in accordance with the Sarbanes-Oxley Act of 2002 ("**DCP**")).
- The Final Rules provide a safe harbor for forward-looking statements, but not "*historical facts*," about transition plans, scenario analyses, use of internal carbon prices and targets and goals made pursuant to the new disclosure requirements.
  - As described further in Section VII.4, companies should avoid putting too much reliance on this safe harbor as significant portions of the required disclosures on these topics will likely constitute historical facts that are outside the scope of the safe harbor.
  - All registrants must disclose in their audited financial statements the aggregate amount of expenditures, losses, capitalized costs and charges incurred as a result of severe weather events and other "*natural conditions*" such as hurricanes, tornadoes, flooding, drought, wildfires, extreme temperatures and sea level rise, subject to certain minimum thresholds.
  - These provisions apply whether the registrant prepares its financial statements pursuant to U.S. generally accepted accounting principles ("**GAAP**") or International Financial Reporting Standards ("**IFRS**").
  - The development and testing of accounting policies and internal control over financial reporting ("**ICFR**") related to these requirements will likely represent one of the most immediate tasks for companies in responding to the Final Rules.
- Notwithstanding any uncertainty about the future of the Final Rules due to the litigation discussed in Section X below or otherwise, companies should not wait to begin preparation, as some of the more time-consuming items will require significant time to implement and companies will not want to be caught unprepared if the Final Rules are upheld. See Section XI below for key next steps.

III. Applicability to FPIs and Certain Other Issuers

FPIs are generally subject to the Final Rules. A new Item 3.E titled "*Climate-related disclosure*" will be added to Form 20F that includes the new subpart 1500 of Regulation S-K. The new Article 14 of Regulation S-X will also apply to FPIs through the general application of Regulation S-X to Form 20-F.

In the Original Proposal, the SEC asked: "*Should we require foreign private issuers that report on Form 20-F to provide the same climate-related disclosures as Form 10-K filers, as proposed?*"[3] In response, the SEC received a number of comments suggesting that the Final Rules should provide for "*substituted compliance*" by permitting companies to comply with the Final Rules by using disclosures provided in response to other climate-related disclosure regimes such as the Recommendations

3 *Id.*, p. 278.

of the Task Force on Climate-Related Financial Disclosures (the "**TCFD Recommendations**") or other international disclosure standards, such as those of the International Sustainability Standards Board.[4]

Although it acknowledged the potential of this approach to reduce costs for registrants, the SEC ultimately decided not to permit substituted compliance "*given the current status of such requirements in other jurisdictions*," saying that instead it would "*observe how reporting under international climate-related reporting requirements and practices develop before making any determination whether such an approach would result in consistent, reliable, and comparable information for investors*."[5] For this reason, registrants may be subject to both the requirements of the Final Rules as well as related but distinct regimes, including the Corporate Sustainability Reporting Directive ("**CSRD**") in the European Union ("**EU**").

The Final Rules will not apply to Canadian registrants that use the Multijurisdictional Disclosure System and file their Securities Exchange Act registration statements and annual reports on Form 40-F.

As explained in Section VII below, most of the Final Rules will apply to smaller reporting companies ("**SRCs**") and emerging growth companies ("**EGCs**"). These filers are exempt, however, from the requirements to disclose material Scope 1 and 2 GHG emissions and file attestation reports.

IV. Compliance Dates

Per the Adopting Release, the Final Rules are subject to delayed and staggered compliance dates as shown below.

Filer Type	Disclosure and Financial Statement Effects		GHG Emissions / Assurance			Electronic Tagging
	All Reg. SK and S-X disclosures other than as otherwise noted	Item 1502(d)(2), Item 1502(e)(2) and Item 1504(c)(2)	Item 1505 – Scopes 1 and 2 GHG emissions	Item 1506 – limited assurance	Item 1506 – reasonable assurance	Item 1508 – Inline XBRL tagging for subpart 1500
LAFs	FYB 2025	FYB 2026	FYB 2026	FYB 2029	FYB 2033	FYB 2026
AFs (other than SRCs and EGCs)	FYB 2026	FYB 2027	FYB 2028	FYB 2031	N/A	FYB 2026
SRCs, EGCs and non-accelerated filers	FYB 2027	FYB 2028	N/A	N/A	N/A	FYB 2027

Notably, these dates are likely to be pushed back at least to some extent given the stay of the Final Rules by the SEC in the litigation challenge (see Section X below). At the time of this writing, it is unclear whether the compliance deadlines will be tolled on a day-for-day basis for as long as the effectiveness of the litigation stay or whether the SEC will elect a different timeline.

V. Background

While it may seem as if the SEC has focused on environmental or climate-related disclosure only in the past few years, it has considered this area periodically over its 90-year history.[6] Disclosure regarding climate change has been the subject of particular SEC attention starting in 2010, when the SEC issued Commission-level guidance relating to climaterelated disclosure (the "**2010 Guidance**"). The 2010 Guidance reminded companies that they needed to disclose *material* climate-related risks under the SEC's existing principles-based disclosure requirements. The 2010 Guidance did not introduce novel climate-related disclosure requirements, but rather explained how then-existing SEC rules may require public companies to disclose climate-related matters in their filings.

Shortly after the Biden administration began in 2021, Acting Chair Allison Herren Lee requested public input on climaterelated disclosure from investors, registrants and other stakeholders. The request began: "*[i]n light of demand for climate change information and questions about whether current disclosures adequately inform investors, public input is requested from investors, registrants, and other market participants on climate change*

4 *See* Adopting Release, p. 805 (n. 3176) (citing comment letters from firms that raised arguments in favor of substituted compliance, including based on cost savings).

5 *Id.*, p. 805.

6 *See*, *e. g.*, Disclosure Pertaining to Matters Involving the Environment and Civil Rights, 36 Fed. Reg. 13989 (19 July 1971).

disclosure."[7] The request elicited significant feedback from commenters, both supportive and critical of the idea that the SEC should propose new substantive rules regarding climate-related disclosures, and contributed to the expectation that the SEC might initiate new rulemaking on the subject.

One year later, in March 2022, the SEC issued the Proposed Rules. The Proposed Rules generated an historic number of comments – over 24,000 (including both unique and form letters) from a broad spectrum of stakeholders – and were widely considered one of the most, if not the most, controversial proposed rulemakings in SEC history. The SEC emphasized a number of different factors it said formed the basis for the Proposed Rules, including that: (i) there was significant investor demand for climate-related disclosures; (ii) climate-related information may be material to investors as they make investment decisions; (iii) registrants had been taking a wide range of approaches to such disclosure, resulting in inconsistent, incomplete and/or difficult-to-compare disclosures (with some registrants providing little or no such disclosure); and (iv) because disclosures made outside of SEC filings are not subject to the same DCP or legal liability as disclosures filed with the SEC, existing climate-related disclosure was likely insufficiently reliable.[8]

The Commission echoed these sentiments in the Adopting Release, stating that "*the current state of climate-related disclosure has resulted in inconsistent, difficult to compare, and frequently boilerplate disclosures, and has therefore proven inadequate to meet the growing needs of investors for more detailed, consistent, reliable, and comparable information about climate-related effects on a registrant's business and financial condition to use in making their investment and voting decisions*."[9] Nonetheless, as noted below, the Final Rules differ from the Proposed Rules in a variety of significant ways.

VI. General Scope

The Final Rules introduce a new subpart 1500 of Regulation S-K and Article 14 of Regulation S-X and, like the Proposed Rules, are generally aligned with the disclosure framework laid out in the TCFD Recommendations. As discussed in Section III above, the SEC declined to permit substituted compliance for FPIs, meaning they are generally subject to these new requirements.

The requirements of the Final Rules can generally be grouped into five categories, which are discussed in Section VII below: (i) governance, strategy and risk management disclosures; (ii) targets and goals; (iii) Scope 1 and 2 GHG emissions metrics (including attestation requirements); (iv) safe harbor; and (v) financial statement disclosures.

VII. Required Disclosures 1. Governance, Strategy and Risk Management Disclosures

a. Governance – Item 1501

The Final Rules require descriptions of climate-related governance at both the board and management levels.

Board Disclosures – Item 1501(a) requires registrants to describe their boards' oversight of climate-related risks. Companies must identify any board committee(s) or subcommittee(s) responsible for oversight of climate-related risks and describe the processes by which the board or such committee(s) or subcommittee(s) are informed of such risks. If a registrant has climate-related targets or goals or a transition plan (as defined in Section VIII below) required to be disclosed under other sections of subpart 1500, it must also describe whether and how the board oversees progress with respect thereto. Pursuant to Instruction 1 to Item 1501, for FPIs with a two-tier board, the term "board of directors" means the supervisory or non-management board.

The Final Rules do not call for information regarding whether and how the board sets climate-related targets or goals, which was required under the Proposed Rules.[10] Nevertheless, boards should carefully consider what, if any, targets their companies set or may set and generally be involved in any significant decision-making with respect thereto, as further explained in Section XI below.

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7 *Allison Herren Lee*, Public Input Welcomed on Climate Change Disclosures, U. S. Securities and Exchange Commission Statement (15 March 2021), https://www.sec.gov/news/public-statement/lee-climatechange-disclosures.

8 *See* p. Original Proposal, pp. 7, 22.

9 Adopting Release, pp. 22-23.

10 *See id.*, p. 169.

Management Disclosures – Item 1501(b) requires a description of management's role in assessing and managing **material** climate-related risks. Registrants should address whether and which positions or committees are responsible for assessing and managing material climate-related risks and the relevant expertise of each, among other topics. Relevant experience may include prior work experience in climaterelated matters, any relevant degrees or certifications and any knowledge, skills or other background in climate-related matters. These disclosure requirements closely track the recently adopted Item 106(c) of Regulation S-K, which requires disclosure about board and management governance of cybersecurity matters.

b. Strategy – Material Climate-Related Risks – Item 1502(a)

The Final Rules require disclosure of any climate-related risks that have materially impacted or are reasonably likely to have a material impact on the registrant, including on its strategy, results of operations or financial condition. Registrants must disclose whether such risks are reasonably likely to manifest in the short term (meaning within the next 12 months) or long term (beyond the next 12 months), whether they are physical or transition risks, information necessary to understand the nature of such risks and the extent of the registrant's exposure thereto.

Physical Risks – Companies must disclose whether the disclosed physical risks are acute or chronic risks (as defined in Section VIII below), as well as the "*geographic location*" and nature of the properties, processes or operations subject to the physical risks. The concept of "*geographic location*" is undefined in the Final Rules and we expect to see a wide range of approaches to this disclosure.

Transition Risks – Companies must disclose whether their transition risks relate to regulatory, technological, market (including changing consumer, business counterparty and investor preferences) or other transition-related factors, and how those factors impact the registrant. Under Item 1502(a), if a registrant has "*significant operations*" in a jurisdiction that has made a GHG emissions reduction commitment, it should consider whether it may be exposed to material transition risk related to the implementation of such commitment.

c. Strategy – Impacts of Climate-Related Risks – Items 1502(b), (c), (d), (e), (f) and (g)

Material Impacts from Climate Risk – Item 1502(b) requires registrants to describe actual or potential material impacts of risks identified in response to Item 1502(a) on their strategy, business model and outlook, including their business operations and related matters. In contrast to the Proposed Rules, the Final Rules clarify that only material impacts need to be disclosed in response to this item.[11]

Consideration of Material Impacts – Item 1502(c) requires registrants to discuss "*whether and how*" they consider any impacts described in Item 1502(b) as part of their strategy, financial planning and capital allocation, including whether impacts have been integrated into their business model or strategy and whether and how resources are being used to mitigate climate-related risks.

Discussion of Material Impacts – Item 1502(d) requires registrants to discuss *how* any climate-related risks described in Item 1502(a) have materially impacted or are reasonably likely to materially impact their business, results of operations or financial condition. Registrants also must describe "*quantitatively and qualitatively*" the material expenditures incurred and material impacts on financial estimates and assumptions that, in management's assessment, "*directly result*" from activities disclosed under Item 1502(b)(4) (*i.e.*, activities to mitigate or adapt to climate-related risks, including adoption of new technologies or processes). The phrase "*directly result*" is not defined in the Final Rules.

Transition Plans – Item 1502(e) provides that, if a registrant has adopted a transition plan to manage material transition risks, it must describe such plan, as well as provide annual updates about such plan, including any actions taken during the year under the plan and how such actions have impacted its business, results of operations or financial condition. Consistent with Item 1502(d), companies must also include quantitative and qualitative disclosure of material expenditures incurred and material impacts on financial estimates and assumptions as a direct result of the transition plan. Notably, Item 1502(e) requires disclosure of transition plans that

11 *See id.*, p. 115; Original Proposal, p. 464.

relate to a material transition risk, regardless of whether the plan itself is deemed material.

Scenario Analyses – Item 1502(f) requires registrants that use scenario analysis to assess potential impacts of climate-related risks on their business, results of operations or financial condition and that determine, based on such analysis, that climate-related risk is reasonably likely to have a material impact on the registrants to describe each scenario, including brief descriptions of assumptions used in such analysis, as well as the expected material impacts on the registrants under each scenario.

Internal Carbon Price – Lastly, Item 1502(g) requires that, if a registrant's use of an internal carbon price is material to how it evaluates and manages climate-related risks identified in Item 1502(a), it must disclose the price per metric ton of CO2e and the total price, including how the price is estimated to change in the short term and long term, among other matters.

d. Risk Management – Item 1503

Item 1503(a) requires registrants to describe any processes they have in place for identifying, assessing and managing material climate-related risks and address certain related matters, including how the registrant identifies whether it has incurred or is reasonably likely to incur material physical or transition risk.

Item 1503(b) provides that, if a registrant manages a material climate-related risk, it must disclose whether and how any processes described in Item 1503(a) have been integrated into its overall risk management system.

2. Targets and Goals – Item 1504

Disclosure of Targets or Goals – Item 1504(a) requires registrants to disclose any climate-related target or goal that has materially affected or is reasonably likely to materially affect the registrant's business, results of operations or financial condition. Importantly, this requirement is not limited to targets or goals that have otherwise been publicly disclosed.

Additional Information on Targets or Goals – Item 1504(b) provides that any additional information necessary to understand the material impact or reasonably likely material impact of the target or goal must be disclosed, including a description of the scope of activities included in the target or goal, the defined time horizon for achieving the target or goal and a qualitative description of how the registrant intends to meet the target or goal.

Annual Progress – Item 1504(c) requires registrants to annually disclose progress towards any target or goal disclosed under Item 1504(a) and how such progress was achieved. Registrants must update such progress each fiscal year by describing actions taken during the year, and include discussion of any material impacts to their business as a direct result of the target or goal or actions taken to make progress towards the target or goal. They must also include quantitative and qualitative disclosure of material expenditures and material impacts on financial estimates and assumptions as a direct result of the target or goal or actions taken to make progress towards the target or goal.

Use of Carbon Offsets – Item 1504(d) requires that, if a registrant has used carbon offsets or renewable energy credits or certificates ("**RECs**") as a "*material component*" of its plan to achieve a climate-related target or goal, it must separately disclose the amount of carbon avoidance, reduction or removal represented by the offsets or the amount of generated renewable energy represented by RECs and certain other information, including the nature and source of the offsets or RECs and the costs thereof. "*Material component*" is not defined in the Final Rules.

3. GHG Emissions – Items 1505 and 1506

a. Scope 1 and 2 GHG Emissions Metrics – Item 1505

Scope 1 and 2 GHG Emissions Metrics – Item 1505(a) requires AFs and LAFs (but no other types of registrants) to disclose their Scope 1 and/or 2 GHG emissions, if such emissions are material (as further discussed in Section IX below), for their most recently completed fiscal year and, "*to the extent previously disclosed in a Commission filing*," for historical fiscal years included in the consolidated financial statements in such filing. Registrants must disclose Scope 1 and 2 GHG emissions data separately and express such data in terms of CO_2e. Registrants must disclose their emissions in gross terms, excluding the impact of any purchased or generated emissions offsets.

In a very significant departure from the Proposed Rules, the Commission completely eliminated disclosure requirements related to Scope 3 GHG emissions from the Final Rules, which was a major sticking point for many commenters.

GHG Emissions Methodology – Item 1505(b) requires registrants to disclose any methodology, significant inputs and assumptions used to calculate their Scope 1 and 2 GHG emissions. Registrants must disclose the organizational boundaries they utilize in calculating their GHG emissions, as well as the method used to determine those boundaries. Registrants must also describe the protocol or standard used to report their GHG emissions. Registrants may use reasonable estimates when calculating and disclosing their GHG emissions, provided the underlying assumptions and reasons for using estimates are disclosed.

Delayed Reporting – Item 1505(c) provides that FPIs may include their required GHG emissions metrics in an amendment to their Form 20-F filed no later than 225 days after the end of the fiscal year to which the GHG emissions metrics relate.

b. Attestation Reports – Item 1506

Attestation Requirements – The Final Rules include attestation requirements with respect to GHG emissions metrics. Pursuant to Item 1506(a), if a registrant is required to disclose Scope 1 and/or 2 GHG emissions pursuant to Item 1505, it must include an attestation report covering that information in the relevant filing.

Assurance Levels and Dates – For AFs, beginning in 2032 (covering FYB 2031) and thereafter, attestation must (at a minimum) be provided at a limited assurance level. LAFs must obtain at least limited assurance beginning in 2030 (covering FYB 2029) and, beginning in 2034 (covering FYB 2033) and thereafter, must obtain attestation at the reasonable assurance level. In both cases, the attestation requirements are phased in after the underlying GHG emissions requirements.

Assurance Standards – The attestation reports required by Item 1506 must be made pursuant to standards that are established by a body that has followed "*due process procedures*," including broad distribution of such standards for public comment, and are either publicly available at no cost or are widely used for GHG emissions assurance.

Attestation Providers – Item 1506(b) contains an extensive set of requirements applicable to attestation providers. For example, any such provider must be an "*expert*" in GHG emissions through "*significant experience*" measuring, analyzing, reporting or attesting to GHG emissions. The provider must also be independent of the registrant during the attestation and professional engagement period, and the Commission has provided in Item 1506(b)(2) a substantial list of considerations relevant to determining the provider's independence.

Disagreements with Attestation Providers – Item 1506(d) requires, among other things, that registrants disclose whether any provider that was previously engaged to provide attestation over a registrant's emissions disclosure for the fiscal year covered by the report resigned, declined to stand for reappointment after engagement or was dismissed (and if so, the registrant must provide additional details of the circumstances such as the nature of any disagreement between the registrant and the provider).

Delayed Reporting – Item 1506(f) requires the inclusion of the attestation report and related disclosure in the filing that contains the GHG emissions disclosure to which the attestation report relates, which may include the Form 20-F amendment filed within 225 days following the end of the fiscal year under the delayed reporting provision of Item 1505(c).

4. Safe Harbor – Item 1507

Under Item 1507, there is a safe harbor for climate-related disclosures pertaining to transition plans, scenario analyses, use of internal carbon prices and targets and goals, as disclosed pursuant to Items 1502(e), (f), (g) and Item 1504, respectively. The safe harbor provides that all information required by those items, *except for historical facts*, is considered a forward-looking statement for purposes of the Private Securities Litigation Reform Act safe harbors for forwardlooking statements.

Given the limitation of the safe harbor to forward-looking statements, it is unlikely to be helpful to companies when making certain disclosures required by Items 1502 and 1504 that are inherently historical in nature – for example, when describing annual progress and associated impacts under a transition plan pursuant to Item 1502(e). Such historical statements are likely to make up a significant portion of the disclosures related to transition plans, scenario analyses, internal carbon prices and targets and goals.

5. Financial Statement Disclosures – Article 14

Article 14 of Regulation S-X, which contains the financial statement disclosure requirements, comprises two primary components: disclosure related to severe weather events and "*other natural conditions*," and disclosure related to the use of carbon offsets and RECs. These provisions apply whether the registrant prepares its financial statements pursuant to U.S. GAAP or IFRS.

a. Severe Weather Events and Other Natural Conditions

Financial Statement Impacts – Rules 14-02(c) and (d) require registrants to disclose in the notes to the financial statements, subject to certain thresholds described below, the aggregate amount of expenditures expensed as incurred, losses, capitalized costs and charges, excluding recoveries (that is, generally, insurance recoveries), incurred during the fiscal year **as a result of** "*severe weather events and other natural conditions*," such as hurricanes, tornadoes, flooding, drought, wildfires, extreme temperatures and sea level rise. The term "*natural conditions*" is not defined in the Final Rules. Importantly, severe weather events and natural conditions do not need to have any nexus to climate change in order to trigger the disclosure requirements.[12] This means that a wide range of events will need to be monitored on an ongoing basis, not just weather events caused by climate change or even events related to weather.

Examples of potentially required disclosures include the amount of expense, loss, capitalized costs or charges, as applicable, to restore operations, relocate assets or operations affected by the event or natural condition or replace or repair affected assets.

Minimum Thresholds – Rule 14-02(b) sets minimum thresholds for the foregoing disclosures. Rule 14-02(b) requires disclosure if the aggregate amount of expenditures and losses equals or exceeds one percent of the absolute value of income or loss before income tax expense or benefit for the relevant fiscal year, provided that disclosure is not required if the aggregate amount is less than $100,000 for the relevant fiscal year. Similarly, Rule 14-02(b) requires disclosure if the aggregate amount of the absolute value of capitalized costs and charges equals or exceeds one percent of the absolute value of stockholders' equity or deficit at the end of the relevant fiscal year, but disclosure is not required if the aggregate amount is less than $500,000 for the relevant fiscal year.

Attribution – Under Rule 14-02(g), companies must attribute a capitalized cost, expenditure, charge, loss or recovery to a severe weather event or other natural condition if such event or condition is a "*significant contributing factor*" in incurring such cost, expenditure, charge, loss or recovery. We expect it may be difficult for accountants and auditors to identify when a severe weather event or other natural condition is a significant contributing factor as opposed to, for example, general repairs or other weatherproofing activities.

b. Carbon Offsets and RECs

Rule 14-02(e) provides that, if carbon offsets or RECs have been used as a "*material component*" of a registrant's plans to achieve disclosed climate-related targets or goals, the registrant must disclose the aggregate amount of carbon offsets and RECs expensed, aggregate amount of capitalized carbon offsets and RECs recognized and aggregate amount of losses incurred on capitalized carbon offsets and RECs during the fiscal year, among other information. Unlike the financial statement disclosures regarding severe weather events and other natural conditions, there is no one percent or *de minimis* dollar threshold for disclosures regarding carbon offsets or RECs.

c. Financial Estimates and Assumptions

Rule 14-02(h) requires registrants to disclose whether the estimates and assumptions used to prepare the consolidated financial statements were materially impacted by exposures to risks and uncertainties associated with, or known impacts from, severe weather events and other natural conditions, or any climate-related targets or transition plans disclosed by the registrant.

d. Contextual Information

Rule 14-02(a) requires registrants to provide contextual information describing how each specified financial statement effect disclosed pursuant to the above requirements was derived, including a description of significant inputs and assumptions used, significant judgments made and, if applicable, policy decisions made by the registrant to calculate the specified disclosure. Rules 14-02(e) and (f) call for additional contextual information with respect to the use of carbon

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12 *See* Adopting Release, p. 485 (n. 2091).

offsets or RECs and the impact of severe weather events and other natural conditions, respectively.

VIII. Definitions – Item 1500

The Final Rules contain over a dozen important definitions in Item 1500, a few of which are particularly consequential.

"*Physical risks*" are defined as both "*acute*" and "*chronic*" risks to the registrant's business operations.

"*Acute*" risks are event-driven and may relate to shorterterm severe weather events such as hurricanes, floods, tornadoes and wildfires, among other events.

"*Chronic*" risks relate to longer-term weather patterns such as sustained higher temperatures, sea level rise and drought, as well as related effects such as decreased usability of land or decreased availability of fresh water.

"*Transition risks*" are actual or potential negative impacts on a registrant's business, results of operations or financial condition from regulatory, technological and market changes to address the mitigation of, or adaptation to, climate-related risks, including, but not limited to, increased costs attributable to changes in law or policy, reduced market demand for carbon-intensive products, devaluation or abandonment of assets, risk of legal liability and litigation defense costs, competitive pressures associated with the adoption of new technologies and reputational impacts (including those stemming from customers or business counterparties) that might change market, consumer or registrant behavior.[13] Interestingly, based on this definition, transition risks may be tied to political processes such as the passage of a new law.[14] The concept of transition risks may prove generally difficult to pin down with certainty and we expect to see registrants frequently refer to the above list of examples provided in the Adopting Release.

"*Transition plan*" is defined broadly to mean a registrant's strategy and implementation plan to reduce climate-related risks, which may include a plan to reduce its GHG emissions in line with its own commitments or commitments of jurisdictions within which it has significant operations. The reference to "*jurisdictions within which [a company] has significant operations*" is notable because it applies to situations where a relevant governmental entity – rather than the company itself – has made a commitment to reduce GHG emissions. For example, as noted in the Adopting Release, 195 parties, including the U.S., the EU and the United Kingdom, had signed the Paris Agreement as of December 2023;[15] any countries that have implemented domestic laws in response to the Paris Agreement would likely constitute such jurisdictions.

IX. Materiality

As illustrated above, the Final Rules are heavily qualified by the concept of materiality, reflecting a key change relative to the Proposed Rules. New subpart 1500 alone contains nearly 40 references to materiality (and the Adopting Release contains over 1,000 such references).

The Commission has made clear that the applicable definition of materiality is the traditional one developed and utilized in U.S. federal securities law: "*[a]s defined by the Commission and consistent with Supreme Court precedent, a matter is material if there is a substantial likelihood that a reasonable investor would consider it important when determining whether to buy or sell securities or how to vote or such a reasonable investor would view omission of the disclosure as having significantly altered the total mix of information made available*."[16] As noted in the Adopting Release, "*the materiality determination is fact specific and one that requires both quantitative and qualitative considerations*."[17]

FPIs who are also subject to the CSRD will face additional complexity given that the CSRD uses a so-called "double materiality" standard – which includes an assessment of companies' impact on people and the environment – rather than the traditional U.S. concept of materiality. Such companies will need to be very clear about what concept is being used in a given disclosure and should be aware of the possibility of SEC comments inquiring about the distinction (including why a particular matter may have been captured in their

13 *See id.*, p. 93.

14 *See id.* (n. 329).

15 *See id.*, p. 635

16 *Id.*, p. 105.

17 *Id.* (n. 382).

double materiality analysis but omitted from their SEC filings).

Materiality of GHG Emissions – The Adopting Release provides several specific examples of the materiality of GHG emissions of which AFs and LAFs should be aware. First, "*where a registrant faces a material transition risk that has manifested as a result of a requirement to report its GHG emissions metrics under foreign or state law*," such as the CSRD, "*because such emissions are currently or are reasonably likely to be subject to additional regulatory burdens through increased taxes or financial penalties, the registrant should consider whether such emissions metrics are material*."[18]

Second, a "*registrant's GHG emissions may also be material if their calculation and disclosure are necessary to enable investors to understand whether the registrant has made progress towards achieving a target or goal or a transition plan that the registrant is required to disclose*" under the Final Rules.[19] Thus, if a company is required to disclose its GHG emissions targets under Item 1504 and/or a transition plan under Item 1502, it should weigh this factor in determining the materiality of the GHG emissions themselves.

The Commission also strongly suggests in the Adopting Release that AFs and LAFs need to measure and assess their Scope 1 and 2 GHG emissions in order to make the necessary materiality determinations.[20]

X. Litigation

As anticipated, litigation challenging the validity of the Final Rules was initiated immediately upon their adoption. Attorneys general from over a dozen states filed petitions for review in the U.S. Courts of Appeals for the Fifth, Eighth and Eleventh Circuits challenging the Final Rules, and the U.S. Chamber of Commerce, companies and trade organizations filed petitions in the Fifth Circuit as well. These petitions generally advance arguments against the Final Rules in three key areas: (1) the "major questions" doctrine (essentially arguing that the SEC exceeded its authority in propounding climate-related rules without a clear Congressional mandate); (2) the Administrative Procedure Act (with arguments focusing on the relative costs and benefits of the Final Rules, the economic analysis of the impact of the Final Rules and the extent to which the Final Rules differ substantially from the Proposed Rules in violation of due process requirements); and (3) First Amendment grounds (with challenges focusing on the fact that the Final Rules lead to compelled speech and, accordingly, require a compelling justification).

On 21 March 2024, the federal petitions were consolidated in the Eighth Circuit, which was selected randomly by the Judicial Panel on Multidistrict Litigation (the "**JPML**"). The lottery system of the JPML was used because separate but closely related litigation was filed in various federal courts. The Eighth Circuit covers much of the upper Midwest of the U.S., stretching from North Dakota through Minnesota and Iowa and down to Arkansas.

On 4 April 2024, the SEC voluntarily stayed the Final Rules pending the completion of judicial review in the Eighth Circuit, while noting that it would "*continue vigorously defending the Final Rules' validity*."[21] In a subsequent court filing, the SEC stated it would provide a new effective date at the conclusion of the stay, but it is unclear what impact that may have on the compliance deadlines included in the Adopting Release.[22] Moreover, it is difficult to predict how long the litigation will take; some expect an initial decision by the end of this year or early 2025 while others expect it to take longer. Given the magnitude of the Final Rules and complex legal issues involved, it is also likely that any decision by the Eighth Circuit will be appealed to, and reviewed by, the U.S. Supreme Court, which would extend the litigation timeline further.

Notwithstanding any uncertainty about the future of the Final Rules as a result of such litigation or the change in the U.S. presidential administration

18 *Id.*, pp. 246-47.

19 *Id.*, p. 247.

20 "We acknowledge, however, that registrants could incur **costs to assess and monitor the materiality of their emissions, even in situations in which they ultimately determine that they do not need to provide disclosure**, and that for some registrants these costs could be significant, especially if firms are not already tracking this information for internal purposes." *Id.*, p. 248 (emphasis added).

21 In the Matter of the Enhancement and Standardization of Climate-Related Disclosures for Investors, Securities Act Release No. 11280, Exchange Act Release No. 99908 (4 April 2024).

22 *See* Omnibus Opp. to Petitioners' Mot. for Stay Pending Disposition of Petitions for Review at 5 (n. 2), *Iowa v. SEC*, No. 24-1522 (8th Cir. 5 April 2024).

later this year, companies and their advisors should begin preparing for compliance as soon as possible in light of the many new requirements imposed by the Final Rules and to avoid being caught unprepared if the Final Rules are upheld. We believe this is the best approach even for FPIs located in the EU who might otherwise be inclined to wait for the outcome of the litigation or presidential election, in part because many are already subject to the CSRD and therefore need to build out much of the same basic infrastructure (including GHG emissions measurement, materiality and risk analysis, board and management oversight, etc.) required to comply with the Final Rules in any event.

XI. Next Steps

With rules as dense and transformative as the Final Rules, we expect registrants will need to act quickly to be in a position to comply. Below we identify five areas requiring the most immediate attention.

Internal Controls and Procedures for Article 14 Requirements – First, compliance with Article 14 of Regulation S-X will require promptly setting up internal controls and procedures to record and properly categorize the financial statement impacts of severe weather events and other natural conditions beginning as early as 1 January 2025 for LAFs. The financial statement impacts of such weather events and conditions – which will be subject to companies' ICFR and audit – need to be recorded and evaluated on an ongoing basis in order to comply with Rules 14-02(c) and (d). Moreover, **all** registrants will need to monitor such financial statement impacts in order to determine whether the amounts, if any, exceed the prescribed thresholds. Since disclosures are triggered by aggregate amounts and it is impossible to predict when a catastrophic event resulting in significant expenses, losses or costs may occur, the amounts will need to be tracked from the first dollar. Companies should work with their independent auditors and internal audit and compliance departments to ensure appropriate processes are put in place in a timely manner. Testing of ICFR should also be done before the accounting books are closed for the relevant period; for LAFs, this would entail starting testing as early as 1 October 2025. We also expect the Public Company Accounting Oversight Board to issue auditing standards or guidance for purposes of applying the new Article 14 requirements and companies should track these developments.

Measuring Scope 1 and 2 GHG Emissions (AFs and LAFs) – Second, if they have not already done so, AFs and LAFs should begin the process of measuring their Scope 1 and 2 GHG emissions. The SEC made clear in the Adopting Release that in order to determine whether Scope 1 and/or 2 GHG emissions are material, such emissions must be measured and assessed. LAFs in particular should feel a sense of urgency, as they will need to disclose Scope 1 and 2 GHG emissions, if material, beginning as soon as 2027 (covering FYB 2026).

Assessing Materiality of Climate-Related Matters – Third, companies should develop a plan to assess materiality for climate-related matters. As discussed above, the Final Rules are heavily qualified by the traditional U.S. securities law concept of materiality. In order to comply with many of the new requirements, companies will need to have well-defined frameworks for making materiality determinations both initially and on an ongoing basis. Management should take steps to apply materiality frameworks in a rigorous manner, including consulting with outside advisors as appropriate. Boards should also take an active oversight role in ensuring management are taking these steps. The necessary materiality frameworks and determination procedures should be integrated with companies' DCP, given that the determinations will flow into their SEC filings. As noted above, FPIs who are subject to the CSRD will need to be particularly careful in applying U.S. materiality principles along with the double materiality framework of the CSRD.

Considering Interplay with Other Climate-Related Reporting Obligations – Fourth, companies should consider the interplay of the Final Rules with other applicable climaterelated reporting obligations. The Final Rules differ in notable ways from climate-related reporting obligations in other jurisdictions, such as the CSRD. As applicable, companies should assess differences in such requirements (as well as any potential liability exposure) as they relate to companies' operations, existing or planned disclosure and materiality assessments under such requirements.

Reviewing Climate-Related Targets and Goals – Fifth, companies should scrutinize their climate-related targets and goals, whether they have already set such targets or goals or are considering doing so. As explained above, targets and goals feature prominently in the Final Rules and use of them may have unintended consequences for companies. For example, if a company sets a Scope 3 GHG emissions target that is reasonably likely to materially affect its business, it will be required to disclose "*any progress made toward meeting the target*" even though quantified Scope 3 emissions are not required to be disclosed under the Final Rules.

Moreover, board involvement in evaluating, setting and managing climate-related targets and goals is critical. Climate-related targets by their nature directly relate to the long-term strategy and direction of the company and can result in the commitment of significant resources over a number of years. Accordingly, as stewards of the company for the long term, directors should have a key role in the setting and review of climate-related targets. Further, yearover-year progress disclosures related to such targets will likely be closely scrutinized by investors and could result in shareholder pressures on directors. Given these dynamics, boards and companies may even consider withdrawing already-set goals to avoid the potential application of Item 1504, though they should carefully consider the risks, including potential strong pushback from stakeholders.