SEC Proposal: Climate-Related Disclosures

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Wednesday, June 1 | 1-2 p.m. EST

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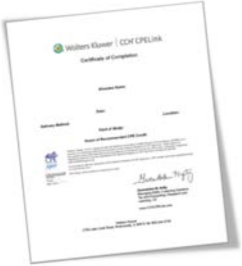

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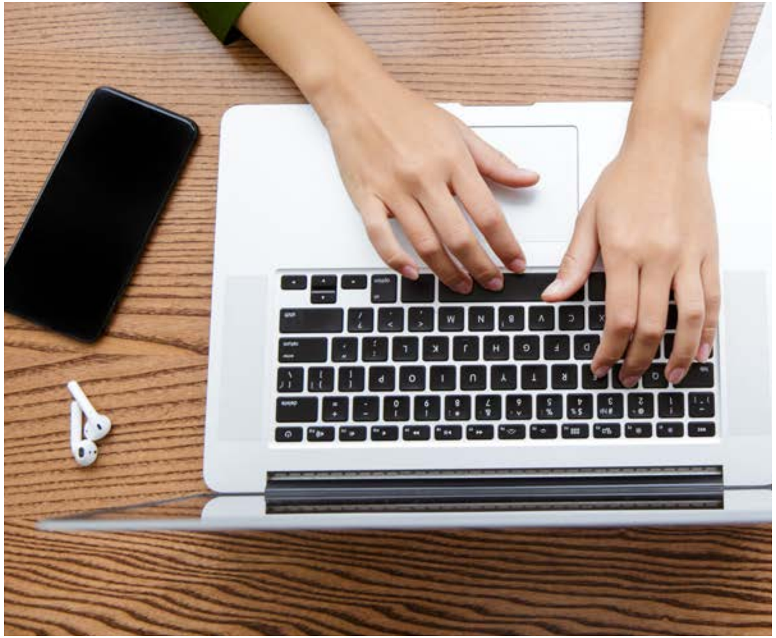
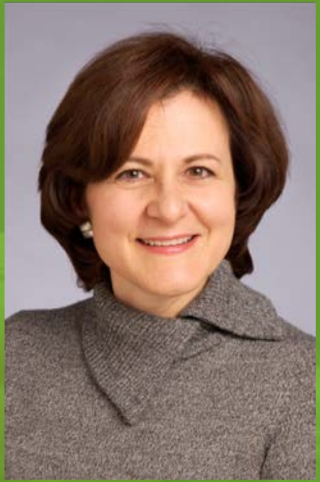


Amy Ripepi



- Managing Director and co-founder, Financial Reporting Advisors, LLC (www.FinRA.com)
- Served as managing partner of Arthur Andersen's national technical group. Also led its SEC Practice group.
- Consults, speaks and writes on a numerous SEC and financial reporting topics.
- Authors the Wolters Kluwer bi-monthly *GAAP Update Service.*

Highlights

SEC Proposal on Climate-Related Disclosures addresses:

- Climate-related risks
- Greenhouse gas (GHG) emission metrics
- Climate-related financial effects
- Attestation requirements

Some Terminology

- **Climate-related risks**
  - Actual or potential negative impacts of climate-related conditions and events on financial statements, business operations or value chains, as a whole. Includes acute and chronic physical risks + transition risks.
- **Greenhouse gas (GHG) emissions**
  - Gases that trap heat in the atmosphere, thus making the earth warmer. Includes carbon dioxide, methane, nitrous oxide, various fluorinated gases.
- **Attestation requirements**
  - Limited assurance ⟶ quarterly review
  - Reasonable assurance ⟶ audit opinion

Agenda

- Why are disclosure rules needed?
- Who would be required to comply with the disclosure rules?
- What disclosures are being proposed?
- Where would the disclosures be presented?
- When would the disclosures be required?
- Additional Resources in CCH® Accounting Research Manager®

POLLING QUESTION

Do you currently subscribe to an accounting research service?

A. Yes, I have a subscription to CCH Accounting Research Manager
B. Yes, I subscribe to another research service
C. No, I do not have a subscription to an accounting research service

Why are disclosure rules needed?

Current Practice → SEC Rules

- SEC disclosure framework: principles + specific rules
- No specific rule on climate-related matters
- Management must assess:
  - Are climate-related matters material?
  - If so, what information should be provided?
- SEC Interpretive Release in 2010
  - Material effects of regulations
  - Risk factors specific to company/industry
  - MD&A and known trends, events, commitments, uncertainties

Current Practice → Disclosures

More disclosures since 2010, but:

- Inconsistent disclosures within and across industries
- Disclosures in 10-Ks are boilerplate
- Information typically provided in separate sustainability reports

Between 2019-2021, 95% of S&P 500 published ESG information*

- Different frameworks for climate-related disclosures
- Separate reports not included in SEC filings
- Different approaches to third party assurance

* *Source: CAQ Study published August 2021 available at https://www.thecaq.org/sp-100-and-esg-reporting/*

SEC Request for Input

More than 6,500 comment letters, including more than 600 unique letters

- Business community
  - Growing investor interest
  - Principle-based rules
  - Existing materiality standards
  - Investor community
  - Strong support for rules
  - Leverage off existing frameworks
  - Principle-based rules with limited number of prescriptive rules

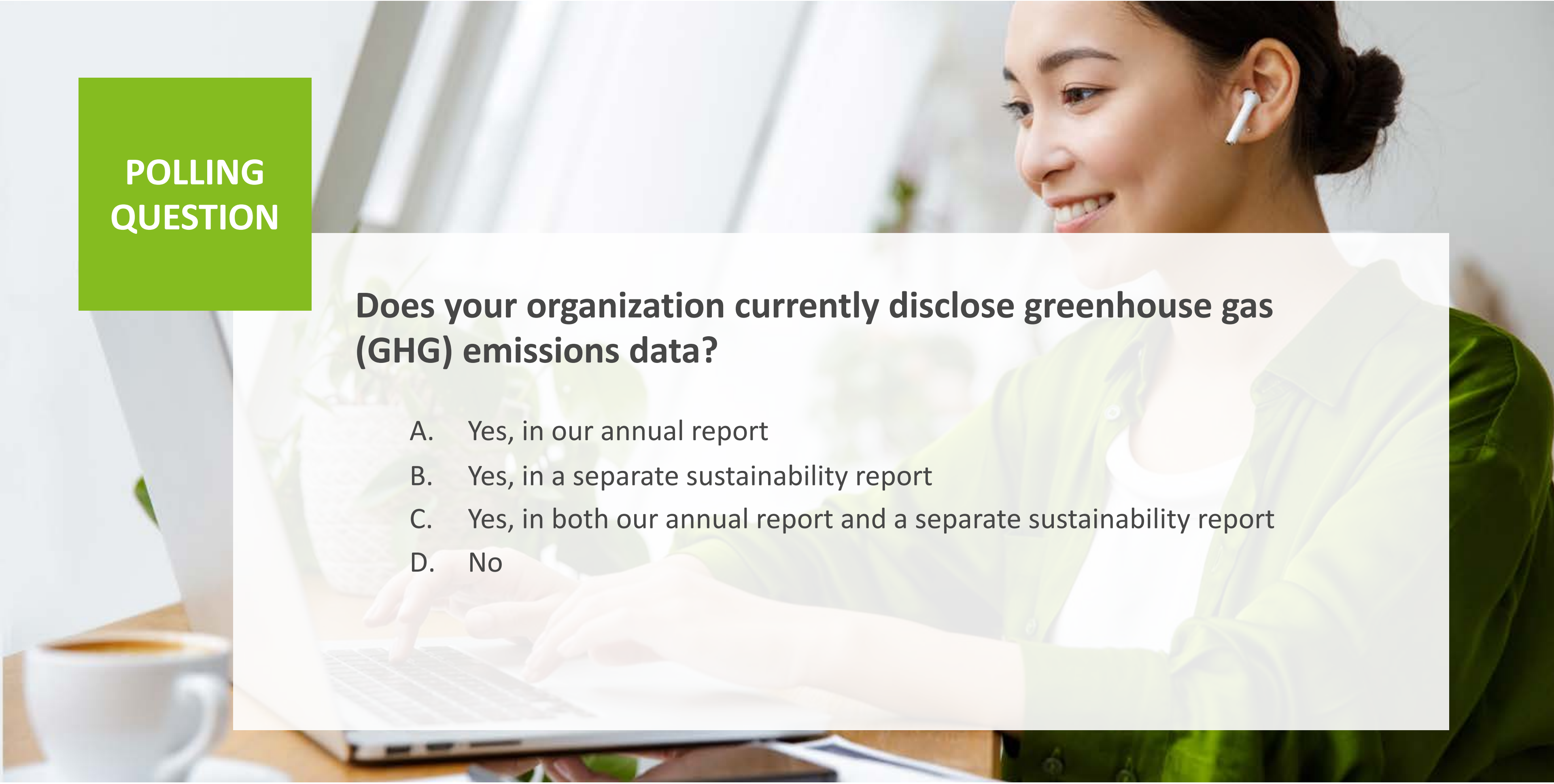
Principles of Materiality

- For SEC disclosure purposes, look to Rule 405 and Supreme Court opinions
- Rule 405:
  - The term material applies to "…those matters to which there is a substantial likelihood that a **reasonable investor** would attach importance in determining whether to purchase the security registered."
- Commonly cited excerpts from Supreme Court opinions:
  - Determinations of materiality require "delicate assessments of the inferences a ***'reasonable shareholder'*** would draw from a given set of facts and the significance of those inferences to" that shareholder.
  - A fact is material if there is "a substantial likelihood that the … fact would have been viewed by the ***reasonable investor*** as having altered the 'total mix' of information available."

Who would be required to comply?

Public companies

- Domestic and foreign registrants
- No exemptions for:
  - Smaller reporting companies
  - Non-accelerated filers
  - Emerging growth companies
  - Initial Public Offerings (IPOs)
  - Private companies merging with public companies (SPACs)
- Asset-backed issuers exempt



POLLING QUESTION

Does your organization currently disclose greenhouse gas (GHG) emissions data?

A. Yes, in our annual report

B. Yes, in a separate sustainability report

C. Yes, in both our annual report and a separate sustainability report

D. No

What disclosures would be required?

Overview of Proposed Disclosures

Four broad areas

- Governance
- Risk Management
- Strategy
- Targets and Metrics

- Qualitative information
- Quantitative information

Qualitative Disclosures — Proposed

- Governance
  - Board oversight
- Risk Management
  - Process to identify risks and plan (if any) to address risks.
- Strategy, business model and outlook
  - Climate-related risks “reasonably likely to have material effect” on business or financial statements
  - Permitted (but not required) to disclose climate-related opportunities
- Targets
  - Applies to (a) targets set voluntarily and (b) targets required by law, treaty, etc.

Quantitative Disclosures — Proposed

- Greenhouse Gas (GHG) emissions and GHG intensity metrics
  - All companies would present certain metrics
  - Presented outside the financial statements
  - Some metrics covered by 3rd party attestation report
- Climate-related financial effects
  - Bright-line materiality threshold
  - Presented in notes to financial statements
  - Covered by audit opinion

Some More Terminology

- Transition Plan
  - Strategy and implementation plan to reduce climate-related risks
- Scope 1 GHG emissions
  - Direct emissions from sources controlled/owned by company
- Scope 2 GHG emissions
  - Indirect emissions from purchase of electricity, heat, cooling; result from company's energy use
- Scope 3 GHG emissions
  - Emissions that are both upstream and downstream of company's activities

GHG Emissions Metrics — Proposed

- Scope 1 and Scope 2 GHG Emissions
  - Disaggregated by each constituent gas and in total
- Scope 3 GHG Emissions
  - Disclose if (a) material OR (b) company has a target that includes Scope 3
  - Smaller reporting companies exempt
- GHG intensity
  - Ratio per unit of revenue and per unit of production
- Methods and assumptions
  - No specific method required. Changes in methods/assumptions permitted.
- Periods presented
- Attestation report covering Scope 1 and Scope 2

Attestation Report — Proposed

- Required for Scope 1 and Scope 2 emissions
  - Non-accelerated filers are exempt
- Third party must (a) be an expert on GHG emissions, (b) be independent and (c) perform engagements as per professional standards
  - Proposal does not prescribe specific professional standards
  - Proposal neither requires nor prohibits hiring the company's independent public accounting firm
- Must also disclose if third party is (a) licensed, (b) subject to inspection program and (c) subject to record-keeping requirements

Climate-Related Financial Effects — Proposed

- Four categories of financial effects
  - Disclose if material using bright-line test
  - Materiality measured for each category
- Some qualitative information
- Include disclosure in annual, audited financial statements
- Disclose amounts for all periods presented in financial statements
- No exemptions, no scaled disclosures

Categories of Climate-Related Financial Effects

Four categories of financial effects

- Nature of event
    - Severe weather or other natural condition
    - Transition activity
- Type of financial effect
    - Impact on financial statements
    - Expenditure

- Disclosures are disaggregated by category and by line item

Climate-Related Financial Effects — Nature

Severe Weather or Other Natural Condition	Transition Activity
Results from flood, drought, wildfire, sea level rise, etc.	Results from actions to reduce GHG emissions or address climate-related risks

Climate-Related Financial Effects — Type

Financial Impact	Impairment? Loss contingency?
Expenditure	Expensed to P/L? Capitalized as an asset?

Climate-Related Financial Effects — Examples

	Severe Weather or Other Natural Condition	Transition Activity
Financial Impact	$5mm impairment charge for asset damaged by severe weather	$400K increase to interest expense driven by climate-linked bond
Expenditure	$750K cost to move asset to less risky location	$1mm asset purchase to reduce GHG emissions

Climate-Related Effects — Materiality

- Broad principle does not apply
- Bright-line threshold: disclosure required if amounts are ≥1% of line item
- Amounts are computed using absolute values of effects
    - Assume inventory is damaged by severe weather. Insurance recovery ($200K credit) and write-off of damaged inventory ($500K debit) = $700K total effect
    - If total is material, negative and positive effects are separately disclosed

Climate-Related Financial Effects — Other

- Disclose how amounts are derived, significant inputs and assumptions, accounting policies related to amounts
- If targets and commitments are disclosed in the narrative section, disclose expenditures and costs to meet those goals
- Disclosures covered by audit opinion and ICFR

POLLING QUESTION

As proposed, which companies would be required to disclose greenhouse gas (GHG) emissions data in their SEC filings?

A. Almost all public companies

B. Only Fortune 100 companies

C. All public and private companies

D. None of the above

Where would the disclosures be presented?

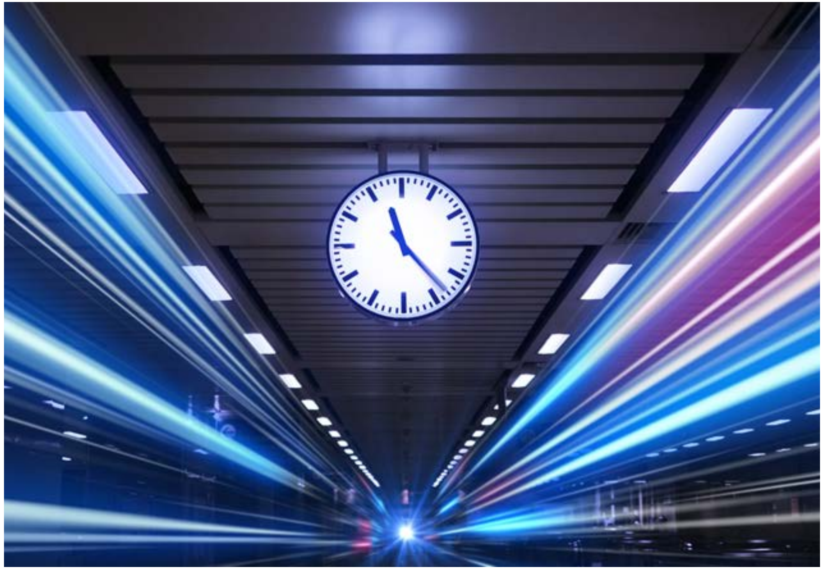
Climate-Related Disclosures in SEC Filings

- Registration statements and annual reports
  - For example, Form S-1 and Form 10-K
- No specific quarterly disclosure requirement
  - However, disclose material changes since annual report
- Qualitative information (governance/risks/strategy/targets) and quantitative GHG emissions metrics in a separately captioned section
- Climate-related financial effects in notes to financial statements

When?

Timing for Implementation

- NO EFFECTIVE DATE PROPOSED!
- Phase-in approach would be used
- As proposed, phase-in would happen over several years
- Separate phase-in timeline for
  - Disclosures
  - Attestation reports on GHG metrics



Phase-in for Disclosures

Table 1

Timeline for a calendar year company *if a final rule became effective December 2022*

Registrant Type	All disclosures except Scope 3 GHG emissions	Scope 3 GHG emissions
Large Accelerated Filer	Year ended 12/31/23	Year ended 12/31/24
Accelerated and Non-Accelerated Filer	Year ended 12/31/24	Year ended 12/31/25
Smaller Reporting Company	Year ended 12/31/25	Exempt

Phase-in for Attestation Reports

Table 2

Timeline for a calendar year company *if a final rule became effective December 2022*

Registrant Type	Attestation Report on Scope 1 and Scope 2 GHG emissions
Large Accelerated Filer	• No assurance – Year ended 12/31/23 • Limited assurance – Year ended 12/31/24 • Reasonable assurance – Year ended 12/31/26
Accelerated Filer	•No disclosure – Year ended 12/31/23 •No assurance – Year ended 12/31/24 •Limited assurance – Year ended 12/31/25 •Reasonable assurance – Year ended 12/31/27
Non-Accelerated Filer and Smaller Reporting Company	Exempt

Final Thoughts

Before You Go…

- SEC projects ongoing costs of $350K- $450K per year
- Comment period ends June 17, 2022
  - No need to comment on all aspects of the proposal
  - SEC website offers simple way to provide input
    - *https://www.sec.gov/cgi-bin/ruling-comments*
- Fully expect significant pushback as well as significant support
- Second webinar will cover more information after comment period ends

Additional Information in CCH® Accounting Research Manager®

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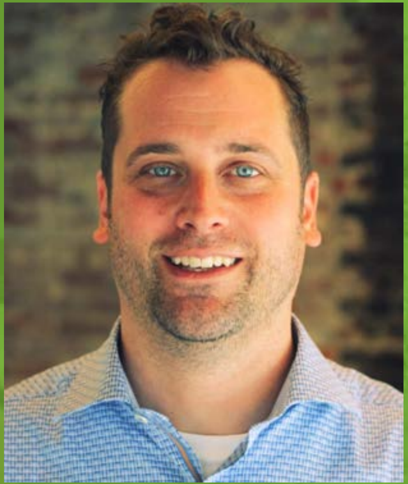

Matt Seegmiller is a Sales and Business Development Manager for CCH® Accounting Research Manager® at Wolters Kluwer. He works with both CPA firms and Corporations sharing best practices to ensure they are utilizing CCH Accounting Research Manager to its fullest.

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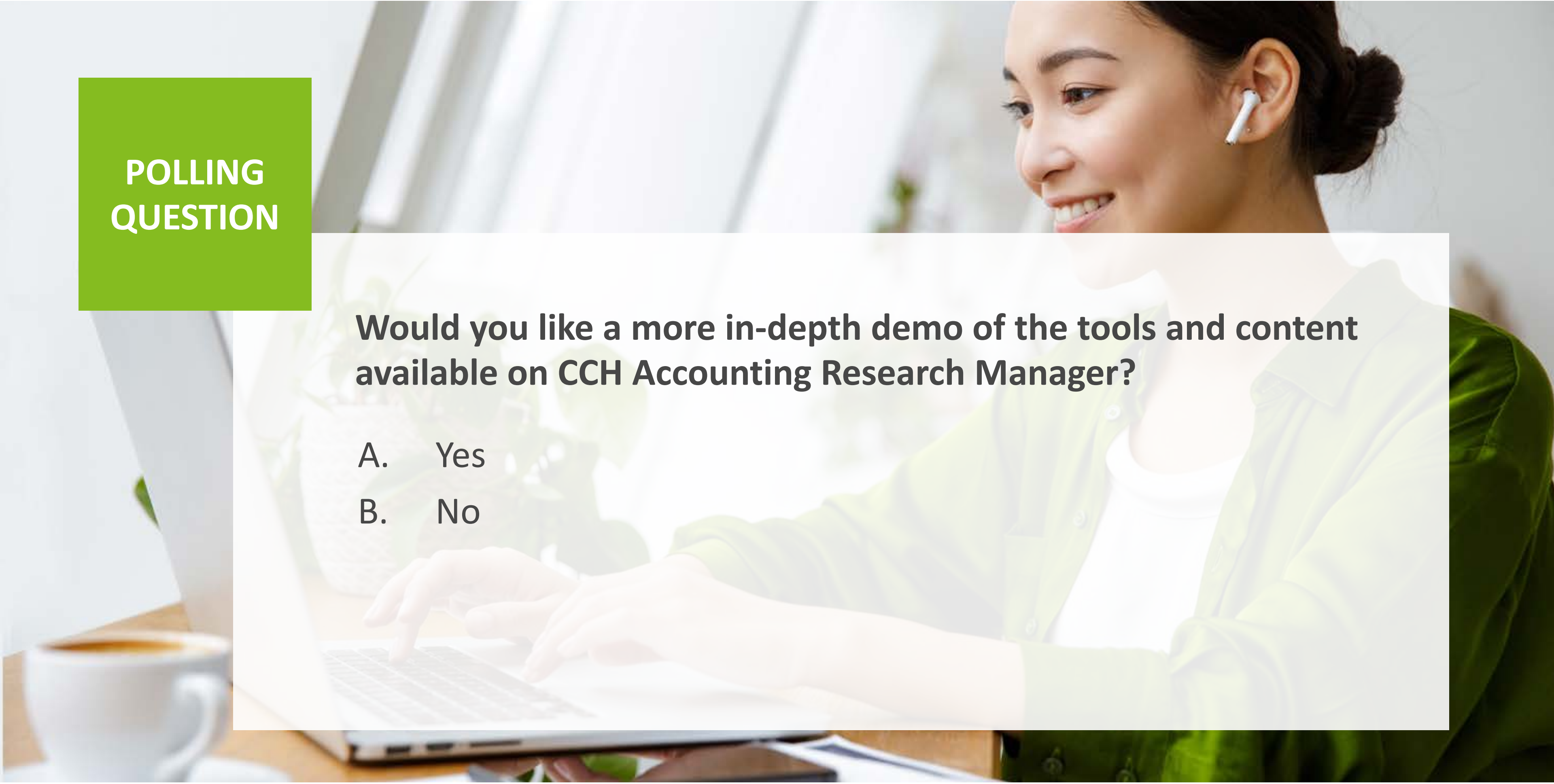

POLLING QUESTION

Would you like a more in-depth demo of the tools and content available on CCH Accounting Research Manager?

A. Yes

B. No

Thank you for attending

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