U.S. Securities and Exchange Commission (SEC)

Proposed Rule on Mandatory Climate-related Financial Disclosure

March 21, 2022

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What Is It?

The SEC has released a long-awaited proposed rule on mandatory climate-related financial disclosures. If adopted, this rule will require public companies to disclose greenhouse gas emissions and material financial risks facing the business related to climate change, including how severe weather could disrupt operations. Specifically, the proposal calls for disclosures on scopes 1 and 2 emissions for all companies and scope 3 emissions under certain circumstances, such as whether the company has set targets for reducing emissions. It also requires companies to explain how they plan to achieve stated goals related to environmental impact and manage identified risks associated with climate change.

What is climate disclosure?

Climate disclosure is when companies publicly report the risks they face from both the physical impacts of climate change and the transition to a low-carbon economy.

The goal is to help companies prepare for the impacts of climate change, and help investors understand risks so that they can make more informed investment decisions.

Source: London School of Economics

Why Does it Matter?

Companies must prepare for complete, credible, transparent qualitative and quantitative disclosures tied to climate change risks and their climate commitments.

This shouldn't be news. Countries and jurisdictions around the world are already calling for transparent, reliable information to underpin the transition to a low-carbon economy—without a view on how well companies are managing climate change effects or portfolio net zero alignment, capital markets cannot accurately price the financial impacts of a warming planet.

In the past several years, climate-related financial disclosure requirements have been rapidly developed around the world. Attention is increasingly being paid to such rules across the financial system and in civil society. Integral to global rules and regulations are the recommendations of the **Task Force on Climate-related Financial Disclosures (TCFD)**.

This will be the first time U.S. listed companies will have a designated mandated framework for climate-related financial disclosure. While companies have an existing requirement to disclose material financial risks, the disclosures vary and can be challenging for investors to compare. SEC Chair Gary Gensler has long discussed the need for a single standard for "clear rules of the road" to benefit both companies and investors in their climate disclosures.

Companies should expect greater investor engagement on climate change, as common mandated disclosures make it easier for investors to engage on the issue. Companies are already facing scrutiny from both stakeholders and investors on their commitments and operational plans to reduce emissions.

What is the TCFD?

The TCFD is a voluntary, industry-led framework designed to encourage consistent, reliable disclosure of climate-related financial data to ensure more informed capital allocation decisions.

Currently, more than 3,000 organizations globally support the TCFD, spanning 89 countries and jurisdictions and nearly all sectors of the economy, with a market capitalization of over $28 trillion.

The G7 and G20 have announced support for the TCFD recommendations along with more than 120 regulators and government entities. In 2021, eight jurisdictions, including Brazil, the European Union, Japan, Singapore, and the United Kingdom, referenced the TCFD in announcements to require climate-related reporting.

What's Next?

How Companies Can Prepare for Mandatory Climate Disclosure

Based on our experience in jurisdictions where mandatory disclosure has already been implemented, we advise clients that **preparation is key**.

Sustainability teams should be preparing their data-collection, iterating on transition plans, and working to ensure they live up to the increasingly intense regulatory and stakeholder scrutiny. Companies that are first movers can capture investor and consumer goodwill, better prepare their operations for a volatile future, and boost their bottom line in the long run.

We propose the following guidance.

1.

Identify gaps in current reporting against new requirements.

For many companies, mandated climate reporting will require additional disclosures. Of the more than 1,600 public companies that the TCFD reviewed at the end of 2020, companies on average shared less than a quarter of the total information the TCFD calls for. For example, only 13% of organizations disclosed information on the resilience of their strategy, which is a critical factor when it comes to implementation plans to mitigate risk exposure. Currently, several industries lead on TCFD-aligned disclosure, including materials and buildings, banking, and energy, while others lag—transportation, consumer goods, and technology and media. Companies and industries need to continue ramping up disclosure while at the same time preparing strategies that can address future scrutiny.

2.

Assess alignment of your positioning with business and industry associations.

Companies must tread carefully if they are associated with any business organizations actively opposing the climate disclosure rule—especially if they have been vocal in supporting the climate transition. Media and civil society will be looking for this dissonance. Preparing will require internal coordination within a company as well as a mitigation plan for potential media stories looking to identify these gaps, possibly exposing major pitfalls in companies' climate action commitments and trust and transparency around those commitments.

3.

Develop and articulate your climate narrative.

Mandatory climate reporting will result in greater scrutiny by not only investors, but also a broader range of stakeholders looking for companies to improve their climate resilience and deliver shareholder value in a low-carbon economy. Stakeholders will be seeking to understand at what pace companies intend to reduce emissions over medium- and long-term time horizons, as well as their strategy for achieving these reductions. Moreover, they will be asking: how this is integrated within the business through remuneration, governance, and internal processes? And how are companies engaging with policymakers and throughout the value chain to drive impact?

Companies will therefore need to not only disclose—but will need a clear and comprehensive narrative to accompany disclosure and communicate how the business will be transitioned. Brunswick's *Net Zero Stakeholder Benchmark* provides a comprehensive view of stakeholder expectations regarding transition plans and can help ensure engagement is credible and robust. Brunswick's Climate Hub is happy to connect further to discuss the *Net Zero Stakeholder Benchmark* and how you can best prepare for this new proposed rule.

From Announcement to Implementation

After the 60-day comment period ends, the SEC will review the public's recommendations and make any adjustments to the proposed rule before approving a final rule. While it's possible to overturn or amend a final rule once it has been approved, regulatory rulemakings are traditionally difficult to overturn, even with a new administration.

While the final rule is expected to be adopted in the next few months, it won't happen without political and industry pushback. Strong opposition is expected from Republicans and some moderate Democrats in Congress as well as major trade associations. There may also be lawsuits against the SEC to end the disclosure mandate.

Regardless of procedural challenges to the ruling, investors are increasingly expecting TCFD-aligned climate disclosure, and shareholder proposals on climate change will continue to increase. We therefore advise clients to prepare accordingly.

2021

February 24

SEC Acting Chair Allison Herren Lee directs SEC staff to enhance its focus on climate-related disclosure in public company filings

March 3

SEC Division of Examinations announces it will enhance focus on climate-related risks

July 21

SEC Chair Gary Gensler says he has asked staff to draft a proposed rule

2022

March 21

SEC votes to propose a rule on standardization of climate-related disclosures and requests public comment for a period no shorter than 60 days

60+ days after the rule is proposed

SEC Commissioners and staff review comment letters and can amend the proposed rule based on public feedback before voting on a final rule

2024+

2024 and later

If the final rule is adopted, there will be a phase-in period for issuers to begin filing disclosures beginning in 2024

Brunswick is advising clients on the rapidly evolving developments relating to climate-related financial disclosure and how to engage on climate in a way that is recognized as credible, robust, and distinct by critical stakeholders. Brunswick has been at the center of the stakeholder universe on climate by advising organizations such as the Task Force on Climate-related Financial Disclosures, Glasgow Financial Alliance for Net Zero, and U.N. Race to Zero campaign.

Brunswick's Climate Hub brings together senior expertise from across the connected worlds of finance, policy, and society, to help companies engage meaningfully with the full range of stakeholders on climate change.

For more information, please email:
ClimateHub@brunswickgroup.com

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