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Too Soon?

An Analysis of Major Investor Comments on the SEC's Proposed Climate Disclosure Rule

July 2022

The comment period for the U.S. SEC's proposed rule on climate-related disclosure ended on June 20th.

Thousands of comments were submitted by companies, investors, trade associations and individuals. To help companies plan for their future climate disclosures and shareholder engagement, we have provided a summary of the six (6) issues most frequently commented on by ten (10) of the largest institutional investors in the world, totaling approximately $36 trillion in assets under management: *BlackRock, Vanguard, Fidelity Investments, SSGA, Capital Group, T. Rowe Price, Wellington, Legal & General, Franklin Templeton, and Alliance Bernstein.*

In general, most institutional investors expressed strong support for the SEC's initiative to establish climate disclosure standards for companies. However, many institutional investors also expressed concerns relating to specific implantation issues, such as Scope 3 GHG emissions, external assurance requirements, legal liability, climate governance, financial disclosures and alignment with the Task Force on Climate-related Financial Disclosure (TCFD). The requirement to disclose Scope 3 GHG emissions seemed to be the most polarizing issue among investors, with some strongly supporting Scope 3 GHG emissions disclosure for all companies and others calling for a delay or removal of the requirement. We provide a more detailed analysis of major institutional investor views on these issues below.

Background: In March of this year, the SEC proposed its climate-related disclosure rule. In short, the SEC proposed mandatory quantitative and qualitative climate-related disclosures by companies, including (i) board & management risk oversight; (ii) scenario planning & transition risk; (iii) financial impact of climate events and other related expenditures; (iv) Scopes 1, 2 & 3 GHG emissions data; and (v) external assurance. Please see our summary here for more details about the proposed SEC rule.

1. Should Scope 3 GHG emissions be in scope? Investors express conflicting views

The SEC's proposed rule requires disclosure of Scope 3 GHG emissions if they are deemed "material" or if the company has set any targets or goals. Many investors expressed concerns about the mandatory disclosure requirement of Scope 3 GHG emissions. While BlackRock's comment letter expressed support for mandatory Scopes 1 & 2 GHG emissions, it encouraged a "comply or explain" model for Scope 3 wherein companies had the option of either disclosing material category Scope 3 GHG emissions or explaining why it is unable to provide such data (e.g. the data was not readily available). Similarly, SSGA and Fidelity conveyed a view that disclosing company Scope 3 GHG emissions data should be voluntary until there is a more accurate framework for Scope 3 GHG data calculation. These investor views are somewhat surprising, as Scope 3 generally accounts for a majority of a company's total GHG emissions. However, some investors believe that the potential costs of such disclosure outweigh the potential benefits at this time.

Capital Group, Wellington, Legal & General and Alliance Bernstein all expressed the more progressive view that all large companies should be required to disclose Scope 3 GHG emissions (if material) because it is a necessary supplement to Scopes 1 & 2 GHG data. Vanguard articulated the slightly nuanced view that Scope 3 GHG disclosures should also be required if material to the company, but only for certain categories of Scope 3 GHG emissions. T. Rowe Price stated that it supported mandatory Scope 3 GHG emissions disclosure only for companies in *industries* where it was material, rather than on a company basis.

2. Are we sure? Investors express skepticism of external assurance

For large, accelerated filers, the proposed SEC rule required "limited" external assurance of Scopes 1 & 2 GHG emissions by 2024, and "reasonable" external assurance by 2026. Many investors voiced concerns that companies may need more time to comply with the contemplated external assurance requirement. BlackRock and T. Rowe Price suggested further engagement with the industry be conducted before any external assurance requirement is included in the final SEC rule. SSGA noted that it does not believe external assurance is necessary or appropriate at this time given "evolving data, methodologies and disclosure capabilities." Capital Group also stated it does not believe that any external assurance should be required. On the contrary, Legal & General, Alliance Bernstein and Franklin Templeton endorsed the SEC's external assurance requirement, noting that having reliable GHG emissions data is critical to the marketplace.

3. Unchartered waters: Investors endorse expanded legal safe harbor

The SEC proposed rule contemplated a legal "safe harbor" for company Scope 3 GHG emissions data to help limit legal liability. Most investors, including Wellington, Alliance Bernstein and Franklin Templeton, were generally supportive of this provision. Some investors even requested that the SEC expand the legal safe harbor for companies. Vanguard and Capital Group endorsed the view that the safe harbor should be expanded and closely track forward-looking statements under federal securities laws. BlackRock, SSGA and T. Rowe Price not only endorsed a more robust legal safe harbor for companies, but also advocated that Scope 1, 2 and 3 GHG emissions data be *furnished* rather than *filed* with the SEC – thereby further limiting company liability. Like externally assured data, *filed* information generally inspires greater confidence in the data than *furnished* data. However, some investors believe that it is just too soon to expect GHG emissions data to be that definitively provided, so further legal protections from liability are necessary.

4. There is no "I" in ESG: Investors view climate governance as a team sport

The SEC's proposed rule requires companies to disclose how boards and management oversee climate risk and to identify which individuals have relevant expertise. Investors generally supported the disclosure requirement of how boards and management oversee climate risks. However, many investors expressed concern about the individual "expert" labeling requirement contemplated in the proposal rule. BlackRock noted that the identification of "specialist" directors "is not conducive to a holistic undertaking by the board." SSGA notes that individual requirements could "imply that boards without directors with specific expertise are deficient, which we believe is inaccurate." Fidelity conveyed a similar concern and added that "there is no justification for singling out climate-related risks for requiring such a heightened level of board disclosure." Wellington cited the need to focus on board/management education rather than qualifications. These views are generally aligned with investors' recent push for more disclosure regarding the board oversight of ESG risks, without being overly prescriptive as to how boards implement such oversight.

5. Can we put a number on it? Investors push back on financial impact disclosure

The SEC's proposed rule requires companies to disclose the financial impact of transition activities and severe weather events, as well as expenditures related to either, if such financial impact is 1% or greater (collectively under Regulation S-X). BlackRock suggested removing all contemplated requirements under Regulation S-X, noting that such disclosure was unduly burdensome and complex. SSGA and Fidelity expressed similar views, also noting that the 1% threshold was arbitrary. T. Rowe Price and Alliance Bernstein voiced support for the financial disclosure requirements, but expressed concern about the 1% threshold and suggested a "materiality" threshold in line with other financial reporting. Legal & General also encouraged the SEC to "consider various inputs on the topic." Again, investors are expressing a "too soon" type of sentiment towards this type of climate disclosure.

6. Don't break protocol: Investors seek greater alignment with current frameworks

The TCFD and GHG Protocol has gained tremendous market support from both investors and issuers across the world. While the SEC acknowledged that its proposed rule is largely based on the TCFD and GHG Protocol, there are some notable differences (e.g. Regulation S-X noted above). Many investors articulated concerns about these differences and suggested that the SEC's final rule be more closely aligned to the TCFD and GHG Protocol. Both BlackRock and SSGA noted the importance of the TCFD framework and its embedded flexibility that allows for the evolution of climate disclosures. Capital Group also pushed back on certain provisions within the contemplated SEC rule by stating the requirements go beyond the TCFD framework. Investors seemed to be in agreement that the SEC should align its final rule more closely with the TCFD and GHG Protocol frameworks, furthering the goal of creating a singular, global ESG disclosure framework.

What’s Next?

The SEC’s forward agenda notes that it intends to finalize the climate-related disclosure rule by October, 2022. It is likely that the final rule will look very different than the proposed rule. There are also likely to be legal challenges that may have an impact on the rule’s implementation. Regardless, companies should understand what their large investors expect of them regarding the climate disclosure issues contemplated by the SEC. Investors are likely to embed many of these views into their engagement and proxy voting policies in 2023 and beyond. Our summary of investor views can help companies plan for their future climate disclosure and investor engagement.

Requirement	BlackRock	Vanguard	SSGA	Fidelity	Capital Group	T. Rowe Price	Wellington	Franklin Templeton	Legal & General	Alliance Bernstein
Scope 3 GHG Emissions	Comply or explain basis	If “material” to company	Voluntary	Voluntary	If “material” to company	If “material” to industry	If “material” to company	N/A	If “material” to company	If “material” to company
Legal Safe Harbor	Expand	Expand	Supports	N/A	Expand	Expand	Supports	Supports	N/A	Supports
External Assurance	Delay all	N/A	Delay all	N/A	Eliminate all	Delay all	Delay Scope 3	Supports	Supports	Supports
Financial Impact Disclosure	Remove all	N/A	Remove all	Remove all	N/A	Remove 1% threshold	N/A	N/A	Revisit 1% threshold	Remove 1% threshold
Climate Governance	Collective oversight	N/A	Collective oversight	Collective oversight	Collective oversight	Collective oversight	Collective oversight	N/A	N/A	N/A
TCFD Alignment	Yes	N/A	Yes	Yes	Yes	Yes	N/A	Yes	Yes	Yes

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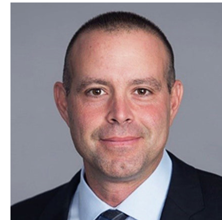

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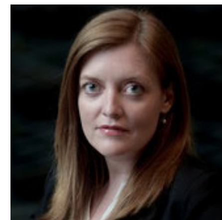

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