Scope 3 Emissions Disclosure

US SEC Proposed Rule – Scenarios Expected in 2023

Supply Chain
Background

Under the Paris Agreement, countries across the world agreed to limit global warming to around 1.5 degrees C. The latest science suggests that limiting warming to 1.5 degrees C depends on CO₂ emissions reaching net-zero levels by 2050. Considering the urgency, an increasing number of national and local governments and business leaders are committing to reach net-zero emissions within their jurisdictions or businesses by 2050.

In line with this agreement, on March 21, 2022, the US Securities and Exchange Commission (SEC) proposed a rule to improve and standardize climate-related disclosures from public companies. The rule would require companies to disclose information about their greenhouse gas (GHG) emissions, specific financial statements, and qualitative and governance details in their registration statements and annual reports.

The SEC requested comments on the proposed rule and received mixed reactions from industries. While a few companies have supported the rule, many businesses have strongly opposed it. Currently, the SEC has been going through the comments and has not disclosed the date of releasing the final rule yet.

While the US is progressing toward making things formal, Europe is leading the race to make climate disclosures mandatory, starting 2025. The discussions on making sustainability reporting mandatory in APAC have also begun.

Increased focus on decarbonization encouraged SEC to suggest strong measures related to Scope 3 emissions reporting

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If earlier compliance dates are to be believed, then the mandatory compliance date for the adoption of the rule for a registrant would begin as early as 2023-24. However, it would further depend on the timing of the final release.

While responses received by SEC have been positive overall, associations have highlighted industry-specific challenges

Due to high public interest, the SEC extended the comment period for the proposal until June 17, 2022. The general public has submitted more than 3,400 individual and over 10,000 standard letters. Commenters comprise various entities (such as corporations, trade and industry associations, non-governmental organizations, and investors), asset managers, and private citizens.

Associations that support the commission’s efforts to harmonize GHG reporting requirements, some of them are already participating in market-based efforts voluntarily, through GHG Protocol and the Task Force on Climate-Related Disclosure (TCFD). While industries agree that investors should have access to climate risk information when making investment decisions, however, emphasized expanding the safe harbor for reporting Scope 3 emissions, reducing the compliance cost of companies with the rule and the potential drawbacks of requiring additional reporting on climate targets. Other challenges highlighted are the availability, consistency, and authenticity of data and know-how related to sustainability, guidelines, and reporting frameworks.

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The associations supporting the intenders behind the proposed rule argued that only publicly traded registrants will be affected by the proposed rule. If a registrant must obtain data on emissions from its supply chain partners to comply with the Scope 3 disclosure requirement, it will naturally come under the purview. It may require those non-registrant entities to undertake time, manpower, and costs to track and calculate their emissions to share them with the appropriate registrants.

Industries have also argued that SEC should require registrants to disclose climate matters publicly rather than filing them to limit excessive liability exposure, while some have questioned SEC’s authority to make rules.

What other regions/countries are doing?

On January 5, 2023, the Corporate Sustainability Reporting Directive (CSRD), approved by the EU Council, entered into force. CSRD requires all large European companies or companies with operations in Europe or companies listed on regulated markets that currently report according to the Non-Financial Reporting Directive (NFRD) to report and publish more detailed information on sustainability matters, including all direct and indirect emissions.

While there is no single rule mandating climate-related disclosures in APAC, GRI, SDG, and TCFD recommendations are gaining widespread recognition in APAC, as many countries are adopting the framework as the basis for ESG reporting regulations.

In Hong Kong and Singapore, similar ESG reporting requirements are coming into effect, which will have implications for companies across APAC.

SEC Proposed rule – Potential scenarios

It is speculated that the SEC may disclose it by late 2023. Based on the criticality of the climate disclosure and the feedback given to the SEC by various entities, there could be three possible scenarios:

1. Disclose in 2023-24; Mandatory filing would be pushed to next year
2. Disclose & File in 2023-24
3. No Mandatory Disclosure in 2023-24

Probability: Most Likely

Expectations: Introduced with minor amendments, requiring companies to disclose Scope 3 emissions but need not file them

Implications: Companies: The ones who have not started scope 3 estimations need to act fast

Probability: Less Likely

Expectations: Introduced with major changes; requiring companies to disclose and file Scope 3 emissions in financial statements

Implications: For SEC: Legal action by organizations questioning SEC’s authority.

Probability: Least Likely

Expectations: Disclosure and filing pushed to subsequent years

Implications: For Companies: Plan for estimation and auditing (too short timeline)


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The bottom line

The draft SEC rule was expected to get finalized by December 2022. However, it may be delayed until the end of 2023. Sooner or later, the SEC will publish the final rule requiring companies to at least begin disclosing Scope 3 emissions and related disclosures, and then start filling climate-related matters. Disclosing Scope 3 emissions will likely become mandatory in most scenarios. Hence, companies are suggested to take initial steps toward decarbonization and proactively embark on the Scope 3 journey to set high benchmarks for peers.

The road to net-zero emissions is not a one-time project. It is a journey that every company has to travel along with its employees and customers. As regular updates/amendments keep coming, companies should collaborate with an intelligence partner who can steer it through the journey, starting from analyzing timely updates related to Scope 3 rules, guidelines, and frameworks to preparing an implementation plan for Scope 3 estimation, ensuring data readiness, sharing stakeholder knowledge, identifying emission hotspots, setting reduction targets, and tracking progress.

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