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BRIAN TOMLINSON

MANAGING DIRECTOR, ENVIRONMENTAL, SOCIAL AND GOVERNANCE (ESG), ERNST & YOUNG LLP

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SEC Climate Change Proposal

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Building a better working world

Overview of the SEC proposal

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SEC proposal on climate change disclosures

Why is the SEC proposing the disclosures, and why now?

Why is the SEC proposing the new disclosure rules?

- Investors are seeking more information about the effects of climate-related risks on a company’s business to inform their investment decision-making.
  - more consistent, comparable and reliable information
  - how registrant has addressed climate-related risks in operations, business strategy and financial plan.
- Several investor initiatives on climate, for example:
  - Climate Action 100+,
  - Net Zero Asset Managers Initiative.
- A little history:
  - Interpretive guidance (2010)
  - Request for comment on climate disclosure (2021)
  - SEC Comment Letters (2021-22)

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Highlights of the proposed rules

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Proposal on climate-related disclosures
Components of the new rules

Disclosures outside the audited financial statements

- Narrative disclosures about climate-related risks, their impact and how the company manages them
- Quantitative disclosures about greenhouse gas (GHG) emissions

Disclosures in the audited financial statements

- Climate-related impacts of events and transition activities on each financial statement line item
- Aggregate amount of climate-related costs both expensed and capitalized
- Climate-related impacts on estimates and assumptions used to prepare financial statements

Disclosure location considerations

- All information would be subject to disclosure controls and procedures (DCPs)
- Financial statement disclosures would be subject to internal control over financial reporting (ICFR)

Assurance

- Scope 1 and 2 emissions, first subject to limited assurance and later reasonable assurance for all but non-accelerated filers and SRCs

Timeline of transition for all issuers

- Dependent on a registrant's filer status and would be phased in, beginning with fiscal year 2023

Narrative disclosures

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SEC proposal and the Task Force on Climate-related Financial Disclosures (TFCD)

- The SEC's proposal is modeled in part on the **TCFD's recommendations** (and **the GHG-Protocol**).
- The TCFD recommendations approach climate-related financial disclosure through the **lens of financial materiality** and focus on the financial impact of climate-related risks and opportunities on an organization, rather than the impact of an organization on the environment.
- The recommendations center on four thematic areas of how organizations operate. These thematic areas interlink and inform one another.

1 **Governance:** The organization's governance around climate-related risks and opportunities

2 **Strategy:** The actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy and financial planning

3 **Risk management:** The processes used by the organization to identify, assess and manage climate-related risks

4 **Metrics and targets:** The metrics and targets used by the organization to assess and manage relevant climate-related risks and opportunities

Source: "Final Report: Recommendations of the TCFD on Climate-related Financial Disclosures," TCFD, June 2017.

Governance

- The oversight and governance by the board and management of climate-related risks, the risk management process and the registrant’s response
- Describe the board of director’s oversight of climate-related risks and opportunities, **as applicable**, including disclosing the following:
  - Which board members or committees are responsible for managing-climate-related risks and their expertise
  - The frequency and manner of board discussions and whether climate-related risks are part of the entity’s business strategy, risk management and financial oversight
  - Whether and how the board sets climate-related targets or goals, including how it oversees progress against those targets or goals
- Describe management’s role in assessing and managing climate-related risks and opportunities, **as applicable**, including the following:
  - Whether certain management positions or committees are responsible, and if so, their identity and relevant expertise
  - The process by which management is informed about and monitors climate-related risks
  - Whether and how frequently such positions or committees report to the board

Strategy, business model and outlook

- How climate-related risks **identified by the registrant** have had or are reasonably likely to have a material impact on its business and consolidated financial statements over the **short, medium or long term**.
  - The SEC did not define a specific range of years for the time horizons to allow flexibility for a registrant to select the time horizons that are most appropriate, but the registrant would be required to describe how it defines these time horizons.
  - Both current and forward-looking disclosures are required, including how any resources are being used to mitigate climate-related risks.
- **If** the registrant uses **scenario analysis** to assess the resilience of its business strategy to climate-related risks, disclosure would have to include:
  - a description of the scenarios used;
  - the parameters, assumptions, analytical choices, and projected principal financial impacts.
- **If** a registrant uses an **internal carbon price**, disclosure must include information about the price and how it is set.

Risk management

- The registrant's processes for:
  - identifying, assessing, and managing climate-related risks;
  - whether any such processes are integrated into the registrant's enterprise risk management system or processes

- **If** the registrant has adopted a **transition plan** as part of its climate-related risk management strategy:
  - a description of the plan, including the relevant metrics and targets used to identify and manage any physical and transition risks

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Quantitative disclosures outside audited financial statements

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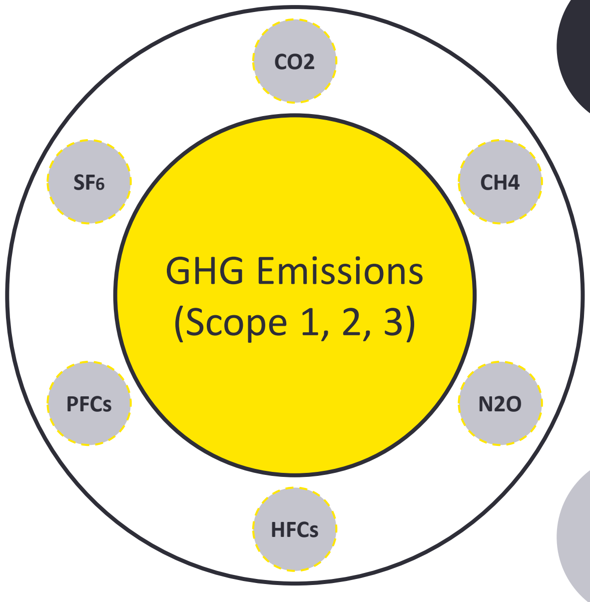
GHG emissions (Scope 1, 2, 3)

GHG emissions[1] means direct and indirect emissions of greenhouse gases expressed in metric tons of carbon dioxide equivalent (CO_2e).



Scope 1

Scope 1 emissions are **direct** GHG emissions from operations that are owned or controlled by a registrant.

Scope 2

Scope 2 emissions are **indirect** GHG emissions from the generation of purchased or acquired electricity, steam, heat or cooling that is consumed by operations owned or controlled by a registrant.

Scope 3

Scope 3 emissions are all **indirect** GHG emissions not otherwise included in a registrant's Scope 2 emissions, which occur in the upstream and downstream activities of a registrant's value chain.

[1] Greenhouse gases means carbon dioxide (CO_2), methane (CH_4), nitrous oxide (N_2O), nitrogen trifluoride (NF_3), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs) and sulfur hexafluoride (SF_6).

Quantitative disclosures outside financial statements

- GHG disclosures:
  - The registrant’s Scope 1 and Scope 2 GHG emissions, separately disclosed:
    - disaggregated & aggregated (CO_2e)
    - absolute & intensity (per unit of economic value or production)
    - excluding offsets
  - Scope 3, **if** material, or **if** the registrant has Scope 3 GHG emissions target / goal:
    - Materiality assessed using the Supreme Court’s reasonable investor standard (quantitative and qualitative);
    - Proposal provides examples to consider regarding materiality determination.
    - Scope 3 accommodations: new safe harbor, longer phase-in, no assurance
  - Required to be presented for **all years reported in the financial statements** (ie inc. look-back)
  - Aligns reporting boundary: Disclosure for all entities that it consolidates in the financial statements (variation from GHG-Protocol approach).
  - Additional disclosure: if the registrant has **publicly set climate-related targets or goals**, including progress toward those targets or goals and how the registrant intends to meet them.

Quantitative disclosures in audited financial statements

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Financial impact metrics

- Financial impact metrics:
  - Proposal would amend Regulation S-X to require a registrant to include disaggregated information about the impact of climate-related conditions and events, and transition activities, on the consolidated financial statements included in the relevant filing, unless the aggregate impact on an absolute basis is less than 1% of the total line item for the relevant fiscal year.

Financial statement line-item	Financial statement balance (from consolidated financial statements)	Impact of Events A and B	Impact of Event C	Impact of Transition Activity D	Absolute value of impacts	Percentage impact
Cost of revenue	$10,000,000	-$300,000	+$70,000	+$90,000	$460,000	4.6%

Expenditure metrics

- Expenditure metrics:
  - Registrants would be required to disclose the aggregate amount of climate-related costs incurred that are both expensed and capitalized, unless the aggregate is less than 1%.

Expenditure category	Current fiscal year balances (from consolidated financial statements)*	Event D	Activity E	Event F	Percentage impact
Capitalized costs (total expenditure incurred during the year that was capitalized)	$8,000,000	$200,000	$100,000		3.85%
Expense (total expenditure incurred during the year that was expensed)	$3,000,000			$25,000	0.8%

Climate impacts on financial estimates and assumptions

- Financial estimates and assumptions:
  - The proposed rules would require a registrant to disclose whether the estimates and assumptions used to produce the consolidated financial statements were impacted by exposures to risks and uncertainties associated with, or known impacts from, climate-related events.
    - Including identified physical risks and severe weather events and other natural conditions
  - A qualitative description of how the estimates and assumptions were impacted by a potential transition or the registrant’s disclosed climate-related targets would also be required.

Disclosure location considerations

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Disclosure location implications

- All disclosures would be included in registration statements and annual reports:
  - need to have appropriate DCPs over the information.
- Disclosures inside the audited financial statements:
  - subject to audit as part of the financial statement audit
  - within the scope of the registrant's ICFR.
- All proposed disclosures would be subject to Sarbanes-Oxley Sections 302 and 906 certifications.
- Liability would be the same as other annual report disclosures:
  - new safe harbor for Scope 3 emissions disclosures, plus;
  - PSLRA safe harbor on Forward-Looking Information applies (subject to conditions).
- Both narrative and quantitative climate-related disclosures would be electronically tagged in Inline XBRL.

ESG Reporting: what the SEC proposal on climate change disclosures means for business

Proposal on climate-related disclosures

Assurance

- Scope 1 and Scope 2 emissions would first be subject to limited assurance and later reasonable assurance - No assurance of Scope 3
- Assurance providers would need to be independent and have significant experience in measuring, analyzing, reporting or attesting to GHG emissions.
- Registrant would make disclosures about whether:
  - The provider has a license from a licensing or accreditation body
  - The engagement is subject to an oversight inspection program
  - The provider is subject to record-keeping requirements for the engagement
- SEC did not specify attestation standards that would need to be used but did provide criteria for standards that would be acceptable.
- Obtaining voluntary assurance on GHG emissions also would trigger disclosure about the provider, the engagement and any relationships that might impair independence.

Next steps for the SEC and organizations

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Phase-in periods and accommodations for proposed disclosures

Registrant type	Compliance date		
	All disclosures, except for Scope 3	**Scope 3 GHG emission disclosures**	**Assurance on Scope 1 and 2 emission disclosures**
Large accelerated filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Limited Assurance – 2024 Reasonable assurance - 2026
Accelerated filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Limited Assurance – 2025 Reasonable assurance - 2027
Non-accelerated filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Exempt
Smaller reporting company	Fiscal year 2025 (filed in 2026	Exempt	Exempt

Source: 33-11042-fact-sheet.pdf (sec.gov)

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Q&A

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