MORTGAGE BANKERS ASSOCIATION

Summary of SEC Proposed Rules on Climate-Related Disclosures

On March 21, 2022, the U.S. Securities and Exchange Commission (SEC) issued a notice of proposed rulemaking (NPRM) proposing new climate-related disclosure rules.[1] The comment period on the proposal will run until at least May 20, 2022.

The new regulations would apply to domestic and foreign companies that file periodic reports with the SEC, for example 10-Ks and 10-Qs. These disclosure requirements are modeled generally on recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD),[2] and some companies are already making voluntary disclosure that are similarly modeled after the TCFD recommendations.

The new disclosure requirements fall into three general categories:

- **Disclosures related to climate-related risk.** These disclosure include, as applicable, disclosure of::
    - Governance of climate-related risks and opportunities;
    - The company's strategy, business model, and outlook; and
    - How a company integrates climate-related risk and transition plans, as applicable, into its risk management systems and processes.
- **Disclosures of greenhouse gas (GHG) emissions**. This includes –
    - Mandatory disclosure of:
        - Direct emissions (Scope 1); and
        - Purchase emissions (Scope 2).
    - Mandatory disclosure of indirect emission (Scope 3). only if—
        - It is material; or
        - The company has set goals or targets that include Scope 3 emissions.
        - Except that smaller registered companies are exempt from Scope 3 reporting requirements.

[1] The pre-*Federal Register* publication version of the NPRM is available here and an SEC fact sheet is available here. If the NPRM is published in the *Federal Register* later than April 20, 2022, the comment period will run into 30 days after the date of publication.

[2] The TCFD was established by Financial Stability Board to develop recommendations for more effective climate-related disclosures. See TCFD, *Final Report; Recommendations of the Task Force on Climate-related Financial Disclosures* (June 2017); available here.

- **Disclosures of climate-related impacts on financial reporting.** This includes disclosure of:
    - Impacts of severe weather events on financial statement line items (e.g., revenues);
    - Impacts of severe weather events on expenditures; and
    - Impacts of severe weather events or climate-related assumptions on financial statements.

MBA has prepared the following summary of selected elements of the rule for our members. This includes an implementation timeline at section IV.

I. DISCLOSURE OF COMPANY APPROACH TO CLIMATE RISK

These disclosure requirements apply across the categories of **governance; strategy, business model, and outlook; and risk management.**

A. Governance. The proposal requires disclosure of board and senior management governance of climate-related risk and opportunities, as applicable. § 229.1501.

- **Board oversight of climate-related risks.** § 229.1501(a).
    - The identity of any board members or board committee responsible for the oversight of climate-related risks**.** § 229.1501(a)(1)(i).
    - Whether any member of the board of directors has expertise in climate-related risks, with disclosure in such detail as necessary to fully describe the nature of the expertise.
    - The processes by which the board of directors or board committee discusses climate-related risks, including how the board is informed about climate-related risks, and the frequency of such discussion.
    - Whether and how the board of directors or board committee considers climate-related risks as part of its business strategy, risk management, and financial oversight.
    - Whether and how the board of directors sets climate-related targets or goals, and how it oversees progress against those targets or goals, including the establishment of any interim targets or goals.
    - If applicable, a registrant may also describe the board of director's oversight of climate-related opportunities.

- **Management's role in assessing and managing climate-related risks.** § 229.1501(a).
  - Whether certain management positions or committees are responsible for assessing and managing climate-related risks and, if so, the identity of such positions or committees and the relevant expertise of the position holders or members in such detail as necessary to fully describe the nature of the expertise.
  - The processes by which such positions or committees are informed about and monitor climate-related risks.
  - Whether and how frequently such positions or committees report to the board or a committee of the board on climate-related risks.
  - If applicable, a registrant may also describe management's role in assessing and managing climate-related opportunities.
  - identifying responsible positions or committees, expertise of individuals in those positions or on those committees, management processes for reporting on and monitoring climate-related risks, the frequency of such reporting, and, as applicable, management's role in assessing and managing climate-related opportunities. § 229.1501(b).

B. **Strategy, business model, and outlook.** The proposal requires various disclosures on impacts of climate-related risk on the registrant's business. § 229.1502.

- Describe any climate-related risks reasonably likely to have a material impact on the registrant, including on its business or consolidated financial statements, which may manifest over the short, medium, and long term. § 229.1502(a).
  - Discuss such climate-related risks, specifying whether they are physical or transition risks and the nature of the risks presented, and describe the nature of those risks in specified detail. § 229.1502(a)(1).
  - Describe how the registrant defines short-, medium-, and long-term time horizons, including how it takes into account or reassesses the expected useful life of the registrant's assets and the time horizons for the registrant's climate-related planning processes and goals. § 229.1502(a)(2).
- *Strategy, business model, and outlook*. Describe the actual and potential impacts of any identified climate-related risks on the registrant's strategy, business model, and outlook, in specified detail. § 229.1502(b).

- Discuss whether and how any identified impacts are considered as part of the registrant's business strategy, financial planning, and capital allocation, including current and forward-looking disclosures. § 229.1502(c).

- Provide a narrative discussion of whether and how any identified climate-related risks have affected or are reasonably likely to affect the registrant's consolidated financial statements. § 229.1502(d).

- Disclose the registrant's use of an internal carbon price, in specified detail, if applicable. § 229.1502(e).

- Describe the resilience of the registrant's business strategy in light of potential future changes in climate-related risks. § 229.1502(f).

C. **Risk management.** The proposal requires disclosure of how the company integrates climate risk, and transition plans as applicable, into its risk management systems and processes. § 229.1503.

- Describe any processes the registrant has for identifying, assessing, and managing climate-related risks. If applicable, a registrant may also describe any processes for identifying, assessing, and managing climate-related opportunities, and describe in specified. § 229.1503(a).

- Disclose whether and how any risk management processes the registrant describes are integrated into the registrant's overall risk management system or processes. § 229.1503(b).

- If the registrant has adopted a transition plan as part of its climate-related risk management strategy, describe the plan, including the relevant metrics and targets used to identify and manage any physical and transition risks, and describe in specified detail. § 229.1503(c).

II. DISCLOSURE OF GREENHOUSE GAS (GHG) EMISSIONS

The proposal includes a set of requirements for disclosing GHG emissions, including Scope 1, Scope 2, and Scope 3 emissions.

A. Scope 1, Scope 2, and Scope 3 emissions

- **Scope 1** emissions are direct GHG emissions that occur from sources owned or controlled by the registrant. § 229.1500(p).
    - ***Scope 1 and real estate investments.*** Direct emissions resulting from the operation of the buildings on the property would be considered Scope 1 to the property owner. Scope 1 includes emissions from combustion of fuels in stationary sources that are located on the property, e.g., boilers, furnaces, turbines.

- **Scope 2** emissions are indirect GHG emissions attributable to the generation of purchased or acquired electricity, steam, heat, or cooling that is generated offsite and consumed by operation of real property owned or controlled by a registrant. § 229.1500(q).
    - ***Scope 2 and real estate investments.*** Emissions attributable to electricity purchased and consumed to operate commercial or multifamily buildings that the registrant owns and controls would be considered Scope 2 for the property owner.
- **Scope 3** emissions are all indirect GHG emissions not otherwise included in a registrant's Scope 2 emissions. Scope 3 emissions occur in the upstream and downstream activities of a registrant's value chain, including investments by a registrant. § 229.1500(r).
    - ***Scope 3 and mortgages.*** For a reporting company that holds mortgages, Scope 3 emissions may include a portion of emissions from real estate that secures the mortgages on its balance sheet. Specifically, the GHG Partnership for Carbon Accounting and Reporting Standard (PCAF)[3] methodology (which the SEC cites as an acceptable approach for calculating Scope 3 emissions) presents a model in which a lender is responsible for the GHG emissions tied to loans held on their balance sheets and in proportion to the LTV ratio.
    - ***Scope 3 and real estate investments.*** Depending on the lease structure, emissions attributed electricity purchased by tenants may be considered Scope 3 for the property owner, but methodologies and approaches vary across the industry.
    - ***Scope 3 and mortgage-backed securities***. Accounting for Scope 3 emissions on real property securing mortgages that secure an asset-backed security is less clear. To date, the PCAF has not identified a methodology for GHG accounting for asset-backed securities and, under the GHG Protocol methodology that the PCAF applies, GHG accounting is not required for securitized products. Also, there appears to be no identified methodology for accounting for Scope 3 GHG emissions across holders of different interests of the security (e.g., holders of the AAA tranche vs. the B piece).

[3] Partnership for Carbon Accounting Financials (PCAF), *The Global GHG Accounting & Reporting Standard for the Financial Industry* (Nov. 18, 2020); available here.

B. Disclosure rules for Scope 1, Scope 2, and Scope 3 GHG emissions

1. Mandatory disclosure of Scope 1 and Scope 2 emissions

- *Generally*. Disclosure of Scope 1 and Scope 2 GHG emissions is mandatory (and Scope 1 and Scope 2 emissions must be disclosed separately). § 229.1504(b).
    - *By making disclosure of Scope 1 and Scope 2 emissions mandatory, the ESEC has, in effect concluded that information about Scope 1 and Scope 2 emissions is material information for all reporting companies.*
- *Calculation methodology*. The proposal requires the reporting company to describe its methodology, significant inputs, and significant assumptions used for calculating Scope 1 and Scope 2 emissions but does not specify a methodology for computing Scope 1 and Scope 2 emissions. The SEC cites the GHG Protocol as an acceptable methodology, but the rule permits reporting companies to use other approaches. § 229.1504(e)
- *Intensity*. A registrant also must report "intensity" of GHG emissions, in terms of metric tons of CO2e per unit of total revenue (using the registrant's reporting currency) and per unit of production. May also disclose other measures of GHG density. § 229.1504(d).
- *Attestation*. If the registrant is an accelerated or large accelerated filer, it must obtain an attestation report from an independent attestation service provider covering, at a minimum, Scopes 1 and 2 emissions disclosure. § 229.1505.
- *Safe harbor*. There is no safe harbor from liability for Scope 1 and Scope 2 disclosures.

2. Limited mandatory disclosure of Scope 3 emissions

- *Generally*. Scope 3 emission must be disclosed only if they are "material" or if the registrant has set a GHG emissions target or goal that includes Scope 3 emissions. However, smaller registered companies are fully exempt from mandatory disclosure of Scope 3 emissions. § 229.1504(c).
- *Calculation methodology*. The proposal requires the reporting company to describe its methodology, significant inputs, and significant assumptions used for calculating Scope 3 emissions but does not specify a methodology for computing Scope 3 emissions. § 229.1504(e). The NPRM description of the proposal identifies the GHG Partnership for Carbon Accounting and

Reporting Standard (PCAF)[4] as an acceptable methodology for measuring emissions, but it also permits the use of other approaches.[6] PCAF is a global industry-led initiative to measure and disclose the greenhouse gas emissions financed by loans and investments.

- *Intensity*. A registrant that discloses Scope 3 must also disclose "intensity." § 229.1504(d)(2).
- *Attestation*. There is no attestation requirement for Scope 3 disclosures.
- *Safe harbor*. A Scope 3 disclosure is deemed not a fraudulent statement unless it is shown that a statement regarding Scope 3 disclosures was made or reaffirmed without a reasonable basis or was disclosed other than in good faith. § 229.1504(f)(1).

3. Disclosure where registrant has set climate-related targets or goals

- *Generally*. The proposal requires a registrant to provide disclosure if it has set any targets or goals related to the reduction of GHG emissions – or any other climate-related target or goal (e.g., regarding energy usage, water usage, conservation or ecosystem restoration, or revenues from low-carbon products) such as actual or anticipated regulatory requirements, market constraints, or other goals established by a climate-related treaty, law, regulation, policy, or organization.
- *Specific disclosures*. If the registrant has set climate-related targets or goals, disclose the targets or goals, including a description of:
- The scope of activities and emissions included in the target;
- The unit of measurement, including whether the target is absolute or intensity based;
- The defined time horizon by which the garget is intended to be achieved, and whether the time horizon is consistent with one or more goals established by a climate-related treaty, law, regulation or policy;
- The defined baseline time period and baseline emissions against the tracked progress; and
- Interim targets set by the registrant and how the registrant intends to meet its climate target or goals.

[4] Partnership for Carbon Accounting Financials (PCAF), *The Global GHG Accounting & Reporting Standard for the Financial Industry* (Nov. 18, 2020); available here.

[6] See NPRM at p. 206 (pre-publication version).

III. DISCLOSURE OF CLIMATE RELATED METRICS RELATED TO FINANCIAL REPORTING

The proposal also requires various disclosures on climate-risk factors that could have an impact on the company's financial performance or its financial reporting.

A. General requirement. The proposal requires reporting companies to report how each reported climate-related metric was derived, including significant inputs and assumptions**.** § 210.14-02(a).

B. **Line-item disclosures.** The proposal requires disclosures of the following impacts at the line-item level (e.g., financial statement line for Revenues) if the absolute value of the positive and negative impacts is at least 1% of the line item.

- Financial impacts of severe weather events and other natural conditions. § 210.14-02(c).
- Financial impacts related to mitigating transition risks. § 210.14-02(d).
- Note: Not applicable if the absolute value of the positive and negative impacts is less than 1% of the line item. § 210.14-02(b)(1).

C. Separate disclosures. The proposal requires disclosures of the following expenditures if they are 1% or more of total expenditures expensed or total capitalized costs:

- Expenditure to mitigate risks of severe weather events and other natural conditions. § 210.14-02(e).
- Expenditure related to transition activities. § 210.14-02(f).

D. Financial statement impact disclosures. The proposal required companies to disclose certain impacts on their financial statements:

- Financial estimates and assumptions impacted by severe weather events and other natural conditions. § 210.14-02(g).
- Financial estimates and assumptions impacted by transition activities. § 210.14-02(h).
- Impact of identified climate-related risks. § 210.14-02(i).

E. **Optional disclosure of climate-related opportunities.** The proposal includes an optional disclosure of climate-related opportunities, subject to a requirement to continue the disclosure on a consistent basis if the company elects to make such a disclosure. § 210.14-02(j).

IV. IMPLEMENTATION TIMELINE

In the NPRM, the SEC projects an effective date of December 2022. Based on that projected effective date, the SEC projects implementation timeline shown in the tables below.

Registrant Type	**Disclosure Compliance Date**	
	All proposed disclosures, including GHG emissions metrics: Scope 1, Scope 2, and associated intensity metric, but excluding Scope 3	**GHG emissions metrics: Scope 3 and associated intensity metric**
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)
Accelerated Filer and Non-Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)
Small reporting company	Fiscal year 2025 (filed in 2026)	Exempted

Filer Type	**Scopes 1 and 2 GHG Disclosure Compliance Date**	**Limited Assurance**	**Reasonable Assurance**
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Fiscal year 2026 (filed in 2027)
Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Fiscal year 2027 (filed in 2028)

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