New SEC Climate Disclosure Rules – prospective impact on Canadian issuers

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Canadian issuers who are U.S. registrants will have to comply with the SEC's new climate-related disclosure rules unless they report through the multijurisdictional disclosure system.

Takeaways

- The U.S. Securities and Exchange Commission (**SEC**) has published its final rules for climate-related disclosure, entitled, "*The Enhancement and Standardization of Climate-Related Disclosures for Investors*" (the **Final Rules**).
- Dual-listed Canadian issuers, including "foreign private issuers" and "domestic issuers", will have to comply with the new disclosure requirements unless they report through the multijurisdictional disclosure system (**MJDS**).
- Initial compliance deadlines are based upon the issuer's size with the earliest deadline falling in early 2026.
- On April 4, 2024, the SEC voluntarily stayed implementation of the Final Rules, pending completion of judicial review of consolidated challenges to the rules by the Court of Appeals for the Eighth Circuit. In its stay order, the SEC noted that it intends to "vigorously defend the validity" of the Final Rules.

Background

On Wednesday, March 6, 2023, the SEC released its much-awaited Final Rules on climate disclosure. A draft of the Final Rules was originally published on March 21, 2022.

The Final Rules present an opportunity for SEC registrants to reassess and adjust their processes for data collection, controls, governance, and disclosure practices as it pertains to climate-change related disclosure. At a high level, the Final Rules will require SEC registrants to provide certain climate-related information in their registration statements and annual reports, including information about an SEC registrant's climate-related risks that have materially impacted, or are reasonably likely to have a material impact on, its business strategy, results of operations, or financial condition. In addition,

under the Final Rules, certain disclosures related to severe weather events and other natural conditions will be required in an SEC registrant's audited financial statements.

The Final Rules are being phased in for issuers based on their size/classification with the earliest timeline for disclosure applying to "large accelerated filers" who must satisfy certain disclosure requirements for any fiscal year beginning in 2025 (*i.e.*, due in early 2026).

Why should Canadian issuers pay attention?

Importantly, the Final Rules will apply to Canadian issuers that are considered to be "foreign private issuers" as well as Canadian issuers that have become "domestic issuers" in the U.S. The Final Rules will *not* apply to Canadian registrants that use the MJDS and file their *Securities Exchange Act of 1934* (**Exchange Act**) registration statements and annual reports on Form 40-F. As has been noted by many commentators, excluding MJDS filers from the Final Rules is consistent with the purpose of the MJDS and will continue to allow MJDS registrants to follow their home jurisdiction laws and rules when registering securities in the U.S. and satisfying their reporting obligations under the Exchange Act.

In the absence of a specific Canadian climate-related disclosure rule, the SEC's Final Rules may serve to expedite climate-related disclosure by Canadian issuers. While the CSA published a proposed climate-disclosure rule in October 2021 (the **Proposed CSA Rules**) (we wrote about Proposed National Instrument 51-107 – *Reporting of Climate Change-related Risks* here), following the International Sustainability Standards Board's (ISSB) publication of ISSB S1 and S2 in July 2023 (discussed here), the CSA announced that it intended to conduct further consultations to adopt disclosure standards based on the ISSB standards, with modifications considered necessary and appropriate in the Canadian context. More recently, the Canadian Sustainability Standards Board (**CSSB**) published its Canadian Sustainability Disclosure Standards (the **CSDS**) for public feedback with responses due in June 2024. The CSA welcomed the CSDS and expressed its intention to incorporate the CSDS and related public feedback into the next iteration of a proposed CSA climate-disclosure rule. The CSA will likely only adopt the aspects of the CSDS deemed essential for climate-related disclosures.

Given the CSA's stated intention to draw on both domestic and international developments when finalizing its Canadian climate-related disclosure rule, Canadian issuers should ensure they review and understand the disclosure criteria and sustainability standards outlined in the SEC's Final Rules, ISSB standards, and CSDS. By taking a proactive approach now to reviewing their internal controls and procedures for climate-related disclosures, Canadian issuers will be well positioned to adapt to the CSA's final climate-related disclosure rules (more on the CSA's rules below).

Comparison of the Final Rules to the Proposed CSA Rules

While both sets of rules are substantially informed by the TCFD framework, the Proposed CSA Rules placed a particular emphasis on the importance of ensuring

Canadian disclosure standards align with expectations of international investors and the stated aim of reducing the costs associated with navigating multiple disclosure frameworks. This additional objective helps contextualize the CSA's reluctance to finalize the Proposed CSA Rules prior to the SEC releasing the Final Rules. Notably, given the substantial scaling back of the Final Rules compared to their draft version by the SEC, it's reasonable to anticipate that the CSA's final rule set will reflect significant revisions from the proposed rules, potentially placing greater emphasis on alignment with the ISSB standards and the CSDS.

One area of notable contrast between the two jurisdictions is with respect to GHG emissions – the Final Rules provide for a relatively enhanced level of disclosure compared to the Proposed CSA Rules. Specifically, the Final Rules provide for mandatory or dependant disclosure in relation to scope 1 and scope 2 emissions, internal carbon pricing, and emissions offsets, whereas the Proposed CSA Rules only provide for a "comply or explain" standard for scope 1 and 2 emissions and are silent with respect to carbon pricing and emissions offsets. Further, the Final Rules provide for a "safe harbour" provision for scope 3 emissions to alleviate concerns about liability for information derived from third parties, which was not included in the Proposed CSA Rules.

The two sets of rules generally align as they pertain to transition management and risk exposure & impacts, with both providing for either mandatory or dependant disclosure for climate risks, impact of climate on strategy and targets. As for financial statement disclosure, the Proposed CSA Rules do not require issuers to disclose financial statements impacts at any stated threshold which contrasts with the Final Rules, as previously discussed. Lastly, both sets of rules provide for materiality qualifiers, however the standard for materiality slightly differs between Canada and the U.S. which could impact the materiality analysis and in turn, the level of disclosure required.

As stated above, the CSA has expressly indicated that international developments, such as the release of the Final Rules, will impact and inform the final CSA rules. Accordingly, we can expect that the final CSA rules will be adjusted from the Proposed CSA Rules to account for any major discrepancies vis-à-vis the Final Rules.

Key disclosures under the Final Rules

The Final Rules require, among other things, disclosure of the following information by US registrants:

- how they identify, manage and oversee climate-related risks (similar to the TCFD framework);
- material expenditures for activities to mitigate or adapt to climate-related risk, disclosed transition plans, and disclosed targets and goals;
- financial information regarding severe weather events and natural conditions (such as hurricanes, flooding, wildfires, extreme temperatures and sea level rise), subject to applicable 1% and de minimis disclosure thresholds;
- scope 1 and 2 emissions (subject to a materiality assessment); and
- attestation (auditing) for GHG emissions.

Notably, the Final Rules do not require disclosure with respect to how much registrants are spending on decarbonization or Scope 3 emissions, both of which were in the SEC's original proposal.

Materiality qualifiers have been incorporated into various sections of the Final Rules, restricting the discussion of management oversight to only material climate-related risks, confining climate-related risk disclosure to material physical or transition risks, and limiting the discourse on targets or goals to those considered material. The obligation to disclose any "climate expert" on the Board has been eliminated under the Final Rules. However, SEC registrants are still obligated to disclose information regarding the expertise of the management. The Final Rules do not require the disclosure of interim targets. Nevertheless, annual disclosure of progress toward targets and goals within each fiscal year is included in the Final Rules.

Next steps

With Canadian issuers facing a significant increase in ESG related disclosure, we recommend that issuers consider the opportunities increased disclosure may present. While there may be crucial efforts needed to comply with the Final Rules, enhanced disclosure also provides issuers with an opportunity to signal to the market some of the positive impacts they have had on society at large, including with respect to climate and environment. Canadian issuers that must comply with the Final Rules may also get a head start on compiling information and preparing disclosure that will be responsive to requirements expected to be adopted by the CSA in the near term.

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