EXECUTIVE SUMMARY

Overall, we support the spirit of the Securities and Exchange Commission's Proposed Rule: The Enhancement and Standardization of Climate-Related Disclosures for Investors.

Investors want more information on climate-related risks and opportunities for value-relevant investment decision making. We know from 60-plus years of advocating on behalf of investors that what gets disclosed gets monitored, measured, and managed—not only by investors but also by management. This Proposal rightly brings climate-related risks into the sphere of improved information for investment decision making, the perspective from which we respond to the Proposal.

The Summary of Positions section which follows provides a bullet point summary of our views on the 200+ questions in the Proposal that are described in more detail in the Appendix. Several overarching or cross-cutting issues emerged as we reviewed the Proposal, which we address in the Overarching Considerations section. We note there, and below, that we believe additional industry-based disclosures consistent with the SASB, soon to be ISSB, standards are needed to make the disclosures the SEC is proposing, both outside and inside the financial statements, most decision-useful for investors. We also make several recommendations related to the disclosures being proposed by the SEC in the Release which we describe in the Summary of Positions and the Appendix. Given our view on the most important disclosures and the potentially challenging proposed implementation dates, we propose an alternative path forward in the Proposed Path Forward section.

Support Climate-Related Risk Management & GHG Emission Disclosures Outside of Financial Statements

We support most of the disclosure provisions outside the financial statements—including the disclosure of greenhouse gas emissions (GHG) and the disclosure of climate-related risks, the governance and management of such risks and their impact on the strategy, business, and outlook of the organization—and their inclusion in a separate section.

- ***Disclosures of Climate-Related Risks, Their Management and Governance, and Impact on Strategy of the Business Likely Mostly Qualitative: Enforcement will Be Important***— Though the climate-related risk disclosures outside the financial statements are more specific than those for other risks (i.e., we would seek similar improvements for many other risks as well), if history repeats itself, the disclosures proposed will likely be highly qualitative and SEC enforcement will be a key ingredient in making these disclosures useful to investors over time. The new definitions included with the Proposed Rule are likely to create significant interpretive issues given their inclusion in disclosures inside as well as outside of the financial statements. We are supportive of the SEC's new requirement that registrants describe how they assessed the materiality, considering time horizons, of climate-risk and believe this could be useful in other disclosure contexts as well (e.g., Scope 3 GHG emission materiality decisions).

  We agree with the need to make location disclosures, with several suggested improvements, regarding a registrant's physical assets, but these location disclosures and other disclosures raise a question regarding the relative prioritization and ability to make improvements in

climate-related disclosures while not making improvements in other areas of financial reporting (e.g., income taxes, segment reporting, cash flows).

We note the SEC's option to allow registrants to also discuss climate-related opportunities. Though we expect such disclosures will be minimal, we believe the SEC should require, not simply allow, such disclosures if such opportunities are described in other publications and venues by the registrant.

- ***Support Disclosure of Scope 1, 2 and 3 Emissions (Recognize Challenges in Gathering Scope 3 Emissions, But Likely the Most Material)***—The disclosure of GHG emissions is important as a barometer of progress (financially and non-financially) in reducing emissions and addressing climate risks, and we support the inclusion of this non-financial metric in the forepart, not the financial statements, of registrants' SEC filings.

  All climate-related risk and GHG emission disclosures (i.e., consistent with our long-held views on the topic of filed versus furnished information) should be included in documents filed, as opposed to furnished, with the SEC. Our view is that at implementation, current period disclosures are sufficient as comparative period information can be built going forward. Disaggregation of GHG emissions by scope, type of GHG, location, geography, segment, and upstream and downstream category—preferably visually—are essential to understanding the risks by industry, region, and supply chain. We are concerned, as we describe later in this summary, that the Actual Proposed Rule lacks sufficient specificity—because it is based off of, but does not directly reference, the GHG Protocol—regarding the emission methodology, assumptions, and certain definitions (e.g., organizational vs. operational boundaries).

  We support disclosure of all three scopes of emissions and GHG intensity metrics—recognizing the many challenges, and high degree of estimation, associated with gathering Scope 3 emissions and with the understanding that assessing the materiality of Scope 3 emissions requires they be collected. Our support is informed by investors advising us that Scope 3 emissions will likely be the most significant emission category (See **Exhibit A-2** in the **Appendix**). As such, excluding them will not appropriately convey the transition risk faced by a registrant. For similar reasons, we do not support voluntary disclosure of Scope 3 emissions. We not only support, but recommend, the SEC require disclosure of Scope 3 emissions *as a range* as this will highlight the measurement uncertainty. The safe harbor protections over Scope 3 emissions are essential (i.e., even in an initial public offering context). Our view is that the relevance, and likely significance, of Scope 3 emissions supersedes them being perfectly reliable. We are supportive of a disclosure transition for Scope 3 emissions that considers the industry and size of registrant, with the most significant emitters providing information first.

  Without some mechanism to require disclosing Scope 3 emissions, the challenges in their estimation and collection will not improve over time (i.e., this will always be a stated hurdle to disclosure). Our view is also informed by an understanding that Scope 3 emission disclosures will have on private and public companies globally (i.e., they will need to gather and report their Scope 1 and 2 emissions) that does business with a US registrant. We believe

these disclosures will be a matter of course in jurisdictions globally and believe many large private companies may already be required to make such disclosures.

For many registrants, there is a high probability that a materiality threshold will be reached when considering Scope 3 emissions—if materiality is assessed, at least in part, as Scope 3 emissions as a percentage of total emissions. Thus, the SEC should require a description by registrants of how they made such materiality assessments (i.e., like for climate-related risks) given the need to make such assessments absent any required disclosures on the cost of reducing emissions (i.e., and therefore the impact of reducing them on the enterprise value).

- ***Support Disclosure of Emission Reduction Commitments and Targets and Goals as They Facilitate More Meaningful Analysis of Transition Plans and Impacts***—We strongly support the requirement for registrants to make disclosures of any GHG emission reduction commitments; targets or goals; or transition plans. Such commitments or objectives are clarifying to investors in (1) understanding transition risks as well as management's intent and strategy in reducing GHG emissions, (2) the cost of doing so, and (3) making the impacts of progress toward achieving these milestones more measurable. While the disclosures may make establishing commitments, targets, or goals less frequent, they are likely not true commitments if that is the effect.

- ***Attestation of GHG Emissions: Support Same Professional Standards and Reporting Requirements for All Attestation Providers***—While our investor members have told us they desire assurance over sustainability disclosures, they also have told us in previous surveys that the verification can be done by professional services firms with ESG expertise as well as more traditional professional services firms providing assurance. They were nearly split on whether verification should be done at the same level as an audit. We have not specifically asked our investor members whether the Scope 1 and Scope 2 emissions should be attested to—or to what level (limited or reasonable) of assurance. This is a particularly challenging question when contextualizing the location of the disclosures. Specifically, when you remind investors that GHG emissions will be subject to attestation while other non-financial information (i.e., really any information not derived from financial statements) included in an SEC filing has no similar assurance, they may not support such different treatment. The question naturally arises: are GHG emission disclosures relatively more important than other disclosures in the same location?

  Whether a public company auditor or other attestation provider, we believe the standards for appointment, independence, execution, and inspection of any attestation engagement on Scope 1 and Scope 2 emissions (i.e., we do not support attestation over Scope 3 emissions) should be the same irrespective of the organization providing assurance. We believe they should be of the same standard, quality, and expectation of those providing attestation and subject to PCAOB requirements. Differing levels of standards and requirements will only add confusion for investors. It is our view that all attestation providers must also meet a financial wherewithal test.

  We understand the need for a delay in providing attestation, and the staggering of assurance levels, after making initial disclosures, given our focus on relevance over reliability.

Attestation by management and audits of internal controls over financial reporting appears premature.

- ***Cost of Reducing GHG Emissions: Sophisticated Investors Will Need to Estimate***—While an important barometer, GHG emissions will be a non-financial metric providing those who seek impact-related metrics something they desire with possibly a higher degree of precision and comparability. That said, there is no requirement in the Proposed Rule that enables investors—particularly if there is no transition goal or target—to quantify the impact to enterprise value of the registrant reducing the disclosed GHG emissions and the timing of those cash flows. While we may have a more precise barometer (i.e., GHG emissions) investors will likely have to make their own estimates of the cost of reducing such emissions—which may be imprecise, and which is work likely only ably done by sophisticated investors.

- ***Use of Other Frameworks and Standards May Require Additional Consideration***—In the Overarching Considerations section we address the Proposed Rule's use of the Task Force on Climate-Related Financial Disclosures (TCFD) and GHG Protocol frameworks/standards, but without reference to them in the Actual Proposed Rule. There we highlight for the SEC questions for consideration regarding whether such frameworks/standards have met best practices for independent standard-setting and how they will be maintained going forward given the point in time snapshot of such standards incorporated into the Actual Proposed Rule. We consider also whether there is sufficient specificity in the Actual Proposed Rule related to the compilation and estimation of GHG emissions.

- ***Materiality Decisions Within Proposal Should Be Assessed Against Commissioner Lee's Statement on Materiality Myths and Misconceptions***—Many observers have commented on the various materiality decisions made by the Commission throughout the Proposed Rule noting that in some instances no materiality threshold has been applied in establishing the Proposal's requirements and that materiality assessments made by the SEC—and to be made by management—are uneven. In the Overarching Considerations section, we assess these materiality observations across various aspects of the Proposal. We then consider them in light of Commissioner Lee's 2021 statement on materiality myths and misconceptions and find that opinions held by stakeholders regarding the uneven application of materiality may be rooted in these myths and misconceptions.

Support Climate-Related Disclosures Inside Financial Statements: Prefer More Decision-Useful Cash-Based Metrics

- ***Support SEC Requirement to Anchor Disclosures in Financial Statements***—We support the SEC's efforts to anchor disclosures outside of the financial statements with those inside the financial statements and we support their inclusion in a separate footnote to the financial statements, noting significant interpretive issues associated with the inclusion of new definitions used to identify, capture, record, and report climate-related events and transactions. Inclusion within financial statements will bring a focusing effect to the definitions and disclosures—given the legal liability attaching to management and auditors for information contained within financial statements. This focusing effect may well yield benefits not only in the US market but globally where there will be no similar disclosure

requirement of climate-related impacts within financial statements. The US will be unique in this regard.

- ***Prefer Cash-Based Metrics and Disclosure of Quantitative Impacts of Changes in Estimates and Assumptions***—In light of our view above, here we address a variety of concerns with respect to whether the financial impact metrics are really metrics or simply financial statement elements, and we raise the point that expenditure metrics may be mistakenly considered cash metrics. Both metrics will be on an accrual basis with the financial impact metrics being disclosed by financial statement caption and the expenditure metrics being expressed in the aggregate, which may challenge investors' understanding of the metrics and their relationship to one another. We note that most of the metrics are backward-looking, and investors seek forward-looking information when assessing enterprise value. We do not believe presentation of metrics should be required for historical periods at implementation as comparative periods can be developed going forward. Metrics and disclosures should be provided by segment and geography.

  We suggest an alternative approach proposing disclosure of climate-related cash-flow metrics, akin to a direct cash flow for climate-related cash flows, with an indication of which cash flows have been capitalized and for what expected useful life. We note that the SEC's proposed disclosure related to financial estimates and assumptions are likely only to be qualitative, and investors need quantitative information about climate-relate events, transactions, and risks. As such, we propose material changes in such assumptions and estimates be provided on a quantitative basis by financial statement caption as such information is useful in showing the variability of key estimates and assumptions going forward and their future impact on cash flows.

  Together, the cash-based metrics can be more directly linked, and concisely articulated relative to the climate-related risk disclosures within the forepart – making them more useful on a confirmatory basis – and the quantitative estimates and assumptions information is instructive in understanding the variability of future cash flows.

  We also note we would support the inclusion of such metrics outside the financial statements first with transition to inclusion in the financial statements as definitions, methodologies, best practices, and controls mature. In our proposed path forward, we also highlight that a deferral of their implementation date may make them more useful in assessing management's previous disclosures of climate-related risks in previous periods—enhancing their confirmatory effect.

- ***1% Disaggregation Threshold: Investors Seek Disaggregation of Many Financial Statement Elements***—We note that the 1% disaggregation threshold in the Proposed Rule may actually have the unintended consequence of creating greater disaggregation in the financial statements such that the registrants do not strike the 1% threshold. Further, the disaggregation threshold creates a paradox for investors who would like this level of disaggregation for many other financial statement elements.

CFA Institute

- ***SEC Must Balance Climate Reporting and Other Financial Reporting Priorities***—The disaggregation threshold highlights another concern for investors—the need to address many important financial reporting priorities and the relative balance of those priorities with climate reporting priorities. We ask the SEC to consider the implications of the climate reporting priorities relative to other needed financial reporting improvements as we discussion in the Overarching Considerations section.

Industry-Based Forward-Looking Metrics Are a Needed to Link Disclosures Inside and Outside Financial Statements and to Achieve Global Convergence

We note the requirement in the Proposal for a registrant to discuss in the forepart to the financial statements the GHG emissions as well as, and alongside, the financial impact and expenditure metrics being derived from the financial statements. This connection and discussion may be challenging, and likely only qualitative, for registrants to prepare as the GHG emissions are a non-financial metric with no cost associated with reducing them provided to investors, while the financial statement metrics are accrual-based financial metrics and likely are more backward-looking than forward-looking.

We have suggested the aforementioned alternative set of cash-based metrics for inclusion in the financial statements to improve the linkage of the discussion of climate-related risks disclosed outside the financial statements and their financial statement impacts. We have also suggested that industry-based metrics which illustrate drivers of future performance—developed by the SASB and being incorporated into the ISSB standards—be included in the Proposed Rule if they cannot be legally referenced in the Actual Proposed Rule. We believe these industry-based, more forward-looking metrics are an important missing link for investors seeking to discover the financially value-relevant impact of climate-related risks in the financial statements.

We also believe the aforementioned industry-based disclosures are essential to achieving global comparability as they will be disclosures that other companies will make globally, not the metrics included within the financial statements of US public registrants. See Overarching Considerations and **Exhibit 1**.

The Path Forward

In sum, we laud the SEC for its timely consideration of these issues. Its efforts have forced focus on climate-related disclosures and advanced the conversation. We have proposed a path forward including our recommendations and an adjusted timetable in the Proposed Path Forward. Irrespective of the final outcome of the Proposed Rule, the Commission has unequivocally advanced understanding of these issues among all stakeholders and how such disclosures can be useful to investment decision making.