The Evolution of Sustainability Disclosure

Comparing the 2022 SEC, ESRS, and ISSB Proposals

The SustainAbility Institute by ERM

PERSEFONI

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1. New Developments in Corporate Climate Disclosure

A Rapidly Evolving Context

The corporate climate disclosure landscape is rapidly evolving. Investor demand for information concerning companies' climate-related financial risks has grown at an accelerating pace over the last decade. In the absence of regulatory disclosure mandates, a number of voluntary reporting regimes have emerged. While helpful in focusing companies on climate change as a business concern, this proliferation of standards quickly became confusing as both investors and issuers complained about the "alphabet soup" of guidelines and called for convergence and harmonization of reporting standards.

The year 2021 saw important progress toward such harmonization, prompted by leaders in the international reporting community. In June 2021, the International Organization of Securities Commissions (IOSCO) published a report finding that investor demand for consistent and comparable sustainability disclosures was not being met. The IOSCO report concluded "there is an urgent need to work towards improving the completeness, consistency, comparability, reliability and auditability of sustainability reporting." It identified three priorities to improve sustainability reporting: (1) encouraging globally consistent standards, (2) promoting comparable metrics and narratives, and (3) coordinating across approaches. IOSCO endorsed efforts by the IFRS Foundation to form an International Sustainability Standards Board (ISSB) to develop a global baseline of sustainability standards to help harmonize sustainability disclosure requirements around the world.[1]

Consistent with IOSCO's recommendation, the IFRS Foundation established the ISSB in November 2021. Over the past three months, the US Securities and Exchange Commission (SEC) and the EU's European Financial Reporting Advisory Group (EFRAG) have published proposed sustainability disclosure rules, and the International Financial Reporting Standards (IFRS) organization has published proposed sustainability disclosure standards. Each of these proposals is undergoing public consultation before final rules or standards are adopted.

> **"There is an urgent need to work towards improving the completeness, consistency, comparability, reliability and auditability of sustainability reporting."**
> **- IOSCO Report on Sustainability-related Issuer Disclosures**

While the SEC, EFRAG, and ISSB proposals deal with similar material, they differ in certain respects, including their enforceability, jurisdictional scope, substantive scope of coverage, and detailed requirements. The following proposal analysis seeks to help companies make sense of the three by comparing them on their alignment to primary international climate disclosure frameworks, details of disclosure, and timelines for implementation. It is jointly authored by the SustainAbility Institute by ERM ('ERM'), ERM's primary platform for thought leadership on sustainability, and Persefoni, the leading carbon management and accounting platform.

Box 1: Overview of the Proposals

- In the United States, the Securities and Exchange Commission (SEC) in March 2022 issued a proposed climate disclosure rule that would require nearly all companies filing with the SEC to report on their climate-related risks, including greenhouse gas emissions.*
    - For the purposes of this report, the SEC's *Enhancement and Standardization of Climate-Related Disclosures* for Investors proposal will be referred to as the 'SEC proposal'.

- In Europe, EFRAG, a private organization that provides technical assistance to the European Commission (EC), released guidance on a broad range of sustainability-related disclosure requirements in April 2022 to the EC as it finalizes its proposed sustainability directive, the EU Corporate Sustainability Reporting Directive (CSRD).
    - For the purposes of this report, EFRAG's *European Sustainability Reporting Standards* exposure drafts will be referred to as the 'ESRS proposal'.

- And on an international level, the IFRS Foundation's recently-formed International Sustainability Standards Board (ISSB) released exposure drafts in April 2022 presenting detailed standards for climate-related disclosures.
    - For the purposes of this report, the IFRS's International Sustainability Standards Board *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information* and *IFRS S2 Climate-related Disclosures* will be referred to collectively as the 'ISSB proposal'.

Jurisdictional Authority and Scope

The SEC, EFRAG, and the ISSB each occupy very different spaces in the global regulatory landscape.

The SEC's focus is first and foremost on the protection of investors in publicly traded companies in the USA. It is authorized to promulgate and enforce rules to implement securities laws. Because its focus is on investor protection, its rules are framed around ensuring investors have the information they need to make informed investment decisions. In this context, the SEC's new proposed climate rules focus on the financial impact of climate change on reporting companies and their financial condition. The SEC's jurisdiction is limited to publicly reporting companies and requires a material connection to financial impacts disclosed in the 10-K.

EFRAG's proposed sustainability reporting standards will provide the basis for implementation of the mandatory sustainability disclosures required under the CSRD. Unlike the SEC's focus, which is strictly directed to investor protection, EFRAG's proposals are based on the principle of double materiality. This means that EFRAG's proposed standards focus both on how sustainability matters impact reporting companies and also how reporting companies impact the environment and society. Moreover, the EFRAG proposal has a wider remit than the SEC's proposed rule, with the scope of the CSRD applying to a broader range of environmental, social, and governance issues and extending beyond the SEC's strict focus on climate.

* The SEC Proposal would apply to all but a limited group of issuers, namely issuers of asset-backed securities, and filers on Form 40-F.

Finally, among the three, the ISSB is the body without any authority to compel disclosures. Rather, as a standard setter, its role is to craft sustainability standards that individual jurisdictions and regulators can adopt or otherwise use in their rulemaking.

Box 2: Scope of Coverage - ESRS and SEC

EFRAG's ESRS proposal, which will inform the EU CSRD disclosure rules, will eventually apply to all large companies in the European Union, meaning any company operating in the EU that fits two of the three following conditions:

- 40 million Euros in net annual turnover
- 20 million Euros in assets
- 250+ employees

An estimated 49,000 companies will be covered by the EU CSRD reporting requirements, compared to just 11,000 companies covered under the EU's current sustainability disclosure rule, the Non-Financial Reporting Directive (NFRD).[6]

The SEC's proposal applies to all SEC registrants including foreign private issuers, even those with no publicly listed equities.[7] Around 1,000 of these companies are smaller reporting companies, or SRCs, which have limited reporting requirements under the current proposal's structure.[8] See the 'SEC Phase-In Period' table in the *Timeline to Implementation section* for further details.

Note: Where sources are unspecified, information was sourced from each proposal's respective draft documents.

- SEC: The Enhancement and Standardization of Climate-Related Disclosures for Investors[2]
- ESRS: Draft European Sustainability Reporting Standards[3]
- ISSB: IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information4 and IFRS S2 Climate-related Disclosures[5]

Eight Key Takeaways for The Private Sector

1. **Companies should focus on the TCFD framework to guide current reporting (see detail in Box 3):** All three proposals draw heavily on the disclosure framework introduced by the Task Force on Climate-related Financial Disclosures (TCFD). The SEC focused on the four main pillars of TCFD to frame its proposal, while, in addition to the pillars, the ESRS and ISSB proposals integrate the underlying 11 disclosure recommendations of the framework. Both ESRS and ISSB introduce additional requirements and call for different disclosure definitions or locations for certain components, but otherwise fully align with TCFD guidance.*
2. **More companies will disclose Scope 3 emissions:** The ESRS and ISSB proposals directly call for disclosure of Scope 3 emissions (indirect emissions from an issuer's upstream and downstream value chains) and companies should be ready to calculate emissions to disclose for the FY23 reporting year. Because IFRS cannot mandate ISSB standards across jurisdictions, it leaves materiality to interpretation by users and regulators, whereas ESRS requires Scope 3 disclosure regardless of materiality. The SEC proposes disclosure "where considered material" or when the company has already issued a Scope 3 GHG reduction target.** The bottom line is that companies should begin to evaluate their Scope 3 emissions to determine whether they are material or not and, if they are, to prepare to report them.
3. **Third party assurance will become more common:** Companies should prepare for limited assurance requirements soon, with a longer-term transition to reasonable assurance likely under both the SEC and ESRS disclosure regimes. Though ISSB proposal provides guidance, whether disclosures made pursuant to the ISSB standards are subject to assurance will be left to adopting jurisdictions and regulatory agencies.
4. **It is not yet clear whether jurisdictions will recognize disclosures made pursuant to other jurisdictions' rules:** The SEC proposal does not include a provision for alternative or substituted compliance with another jurisdiction's reporting requirements. However, it does solicit public comment on whether it should accept alternative compliance. The ESRS indicates that other reporting standards can be used in addition to the ESRS, but there is uncertainty as to whether ISSB standards will satisfy ESRS requirements. To align these standards, and others around the world, the ISSB initiated a cross-jurisdictional working group to facilitate the creation of a global baseline standard while the SEC, ESRS, and ISSB proposals all have open consultations.
5. **The proposals differ in their levels of prescriptiveness and scope:** Of the three proposals, ESRS disclosure requirements appear to be the most prescriptive of the three as they stand right now. They include detailed examples of disclosure requirements, sample metrics, line-item disclosures and impacts, and sample formats for entities to use in disclosure. The SEC's disclosure proposals use a combination of principles-based disclosure requirements, which leave significant discretion to the registrant to determine what information to disclose, and prescriptive rules-based disclosure requirements, which tell issuers specifically what must be disclosed. The scope of the proposals also differs significantly. The SEC proposal is limited to climate change. The ISSB proposal currently includes general requirements and climate disclosure provisions, but intends to expand to more ESG topics. The ESRS proposal covers the full range of environmental, social, and governance topics.

* For example, the ESRS directs companies to disclose climate-related financial risks and opportunities, as framed by the TCFD, and also requires companies to disclose their impacts on the environment and society, consistent with its double materiality mandate.

**The SEC proposal would exempt smaller reporting companies from the Scope 3 disclosure requirements.

6. **Potential future expansion:** While the SEC's climate-related disclosure proposal is limited to climate, the SEC's regulatory agenda signals that the agency is likely to propose disclosure regulations on additional ESG-related topics such as board diversity, human capital, and cybersecurity. The ISSB's proposal focuses only on climate and other environmental disclosure items, though its scope is likely to expand with future exposure drafts, which are expected to eventually cover the entire ESG landscape.* The ESRS already includes E, S, and G components in its proposal and is designed as an all-encompassing ESG disclosure rule.
7. **Timeline for compliance is pushing pace for 2023/4:** For all three frameworks, large companies should collect data beginning at least with their Fiscal Year 2023 and prepare to file by the following year.
8. **Commenting on the proposals.** Companies, investors, and other interested parties are strongly encouraged to share their comments with the SEC, ESRS, and ISSB on the current exposure drafts. The deadlines for submission of comments are:
   - SEC: Comments are due June 17, 2022.
   - ISSB: Comments are due July 29, 2022.
   - ESRS: Comments are due by August 8, 2022.

Box 3: The Devil in the Detail: Observations on TCFD Alignment

Key takeaways with relation to TCFD alignment are as follows:

- The SEC's climate-related disclosure proposal uses TCFD as a guide in developing disclosure requirements, but uses its own approach for disclosure related to metrics and targets disclosure and climate-related opportunities.
- ISSB's exposure draft aligns with TCFD guidance, with additional requirements and components to make the proposal more granular and detailed.
- The ESRS proposal is the most prescriptive and detailed of the three, not only aligning with TCFD guidelines but significantly adding detail to TCFD's recommended disclosures, most notably to incorporate the EU double materiality framework into the rules.
- The proposals closely adhere to TCFD guidance with respect to emissions disclosures, with some addition or variation:
  - Each proposal uses the greenhouse gas accounting standards defined in the Greenhouse Gas Protocol's Corporate Accounting and Reporting Standard, including their concept of scopes and related methodology.
  - All of the proposals require all companies to disclose Scopes 1 & 2 greenhouse gas emissions measured in metric tons of CO2 equivalent as prescribed by the GHG Protocol.
  - Scope 3 emissions are required by the ISSB and ESRS proposals and are required by the SEC if Scope 3 emissions are material or if the company has set reduction targets that include Scope 3.

* The ISSB's 'S1' proposes that companies should provide material information on all significant sustainability-related risks and opportunities necessary to assess enterprise value. Where those risks and opportunities relate to climate, 'S2' provides specific requirements for doing so – including the requirement to disclose physical and transition risks, as well as climate-related opportunities. The ISSB is expected to consult on its future agenda during H2/2022.

Conclusions

The entities responsible for developing the proposals profiled in this report each occupy significantly different positions in the global regulatory landscape. Even so, their recent proposals demonstrate increasing alignment in the development of climate-related risk and opportunity disclosure frameworks. This alignment is important in developing global consistency across reporting requirements, and may also impact the overall quality of climate- and ESG-related data, ultimately resulting in improved insights and outcomes. However, there is still room for improvement: the variations between the SEC, ESRS, and ISSB proposals described in this report should be further addressed within the comment period and beyond to drive momentum towards a global baseline for climate- and sustainability-related disclosure requirements.

The development of existing and new climate- and sustainability-related disclosure is expected to have the benefits of improved disclosure. As companies are required to collect and manage relevant data, they may be more likely to develop a more comprehensive understanding of their risk profile. Reporting entities will be able to use the data and insights gathered to help their identification of climate-related risks and opportunities, mitigating their exposure to climate impacts while capitalizing on the potential benefits presented by the transition to a low carbon economy. In short, investment in effective reporting and disclosure processes to comply with relevant regulations is likely to pay off.

While investment required for effective reporting and disclosure may not be inconsequential, it may have real benefits for issuers. As highlighted in a recent ERM study on the cost of climate-related disclosure for corporate issuers and institutional investors, the SEC has noted that “more consistent, comparable, and reliable disclosures could lead to capital market benefits in the form of improved liquidity, lower costs of capital, and higher asset prices (or firm valuations).”[9] These benefits are likely to be further magnified by improved data and information alignment brought on by disclosure requirements, such as those seen in the SEC, ESRS, and ISSB proposals.

And with SEC, ESRS, and ISSB proposals driving a reduction in information asymmetries, there is also likely to be a fundamental change in the relationship and dialogue between investors and companies. Through a more congruent understanding of climate-related risks and opportunities and the ability to build a strategy to address them, investors may push more capital towards those companies driving the transition to a low carbon economy. Ultimately, this should reduce the systemic risk that is presented by climate change.

Alignment of disclosure requirements is clearly more consequential than simple regulatory compliance. Investors, companies, and consumers alike will benefit from consistent and comprehensive climate and sustainability disclosure. But regulators and standard-setters need to know what works and what needs improvement in order to effectively craft these requirements. ERM and Persefoni encourage corporate issuers, investors, and other relevant stakeholders to participate in the open comment periods for each of these proposals to help drive momentum towards a consistent global reporting baseline.

2. Detailed Analysis of the Three Proposals

Comparison Matrices

Proposal Comparison Matrix			
Comparison Matrix	**SEC Climate Disclosure**	**EFRAG ESRS**	**ISSB Proposal**
Jurisdiction	All publicly reporting companies under the SEC's jurisdiction in the United States except for Canadian issuers filing annual reports on Form 40-F, and asset-backed issuers.	All large companies in the EU subject to CSRD; listed companies on EU regulated markets except listed micro-enterprises.	ISSB Standards will be considered for adoption on a voluntary basis by individual jurisdictions.
Comment period	Comment period open until June 17, 2022	Comment period open until Aug. 8, 2022	Comment period open until July 29, 2022
Phase-in / time to implementation	Phase-in period from 2023-2026. Assumes adoption of rules by end of 2022.	Anticipated phase-in period from 2023-2026; Multiple advisory bodies have suggested to postpone implementation by at least a year.	Expected release of guidelines by EOY 2022 for implementation by G20 countries in the following year.
Likely date of first report	Initial reports expected 2024	First reports expected by 2024	N/A - guidelines for usage by jurisdictions
Assurance requirements	Accelerated Filers and Large Accelerated Filers required to include attestation report for Scopes 1 and 2 emissions, phased in with limited assurance in the second and third years after the initial compliance. Beginning in the fourth year, attestation must be at a reasonable assurance level.	Limited assurance requirements are expected within three years after implementation and reasonable assurance after six years.	Guidelines include audit and oversight of disclosures from third party.
Acceptance of alternative or substituted reporting	Does not include guidance in the Proposed Rule, but the release asks for public comment on whether substituted or alternative compliance provisions should apply.	Other frameworks can be used in addition to the ESRS.	ISSB standards are not mandatory unless adopted by regulatory authorities with enforcement power. However, ISSB seeks to align frameworks to be acceptable compliance across jurisdictions. ISSB has intention to internationalize SASB metrics and add financed emissions disclosures. Additionally, an MOU was announced with GRI.

Proposal Comparison Matrix			
Comparison Matrix	**SEC Climate Disclosure**	**EFRAG ESRS**	**ISSB Proposal**
Level of prescriptiveness	Combination of principles-based and prescriptive disclosure requirements. Certain disclosure items also required at detailed level if company has taken certain actions (e.g., if company has set targets or goals, or if company does scenario analysis, then detailed disclosure is required related to those goals and scenario analysis).	The most prescriptive of the three. Very detailed framework with KPIs that are both sector-agnostic and sector-specific. EFRAG's disclosure requirements include detailed examples of line item disclosures, metrics, impacts, and sample formats. EFRAG requires scenario analysis.	Final level of prescriptiveness is unclear as of now, but more can be expected post-exposure drafts.

TCFD Reconciliation Matrix

<table>
<tr><th colspan="4">Governance</th></tr>
<tr><th></th><th>SEC Climate Disclosure</th><th>EFRAG ESRS</th><th>ISSB Proposal</th></tr>
<tr><td>Describe the board's oversight of climate-related risks and opportunities</td><td rowspan="2">Oversight and governance of climate-related risks by board and management.</td><td>How governance bodies are informed about sustainability matters.</td><td rowspan="2">Management oversight of climate-related risks and opportunities.</td></tr>
<tr><td>Describe management's role in assessing and managing climate-related risks and opportunities</td><td>How sustainability matters are addressed by administrative / management bodies.</td></tr>
<tr><th colspan="4">Strategy</th></tr>
<tr><td>Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term</td><td rowspan="2">How any identified climate-related risks have had or are likely to have a material impact, affect business model / strategy, impact financial statements.</td><td>Material sustainability impacts, risks and opportunities: sector-agnostic, sector-specific, and in some cases entity-specific.</td><td>Impacts of climate-related risks and opportunities on business model, strategy, cash flow, financing / cost of capital; short-, medium-, and long-term risks; physical vs. transition risks.</td></tr>
<tr><td>Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario</td><td>Potential financial effects from material transition and physical risks and opportunities.</td><td>Effects of significant climate-related risks and opportunities on business model & value chain, strategy & decision making, and financial position / performance.</td></tr>
<tr><td>Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario</td><td>Scenario analysis is not required by the SEC, but it is discussed as a reasonable alternative that could could inform investors of the resilience of registrant's business strategies and operations.</td><td>Use of scenario analysis to identify and assess risks and opportunities over the short, medium, and long term.</td><td>Use scenario analysis to describe climate resilience of its strategy, including business model, significant physical risks and transition risks; results of the climate-related scenario analysis, how the analysis was conducted, and which scenarios were considered.</td></tr>
</table>

Highlight key:
- Proposal deviates from TFCD recommendations
- Proposal fully aligns or adds to TCFD recommendations

Risk Management

	SEC Climate Disclosure	EFRAG	ISSB Proposal
Describe the organization's processes for identifying and assessing climate-related risks	The registrant's processes for identifying, assessing, and managing climate-related risks and whether any such processes are integrated into the registrant's overall risk management system or process.	Processes to identify sustainability impacts, risks, and opportunities, and assess which ones are material. Double materiality: material impacts on climate change as well as material impacts of climate risks on business & value chain.	Processes used to identify climate-related risks and opportunities, such as how likelihood and effects are analyzed, how risks are prioritized, input parameters used.
Describe the organization's processes for managing climate-related risks			Processes used to assess, monitor, and manage risks.
Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organization's overall risk management		No discussion of inclusion in entity's overall risk management process.	Integration into entity's overall risk management process.

Metrics & Targets

Disclose the metrics used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process	GHG emissions metrics for Scope 1, 2, and 3 (if applicable); other metrics used to assess risks and opportunities are optional.	Expanded details on metrics and targets required, such as energy consumption and mix, timetables for targets, and detailed emissions information.	Metrics an entity uses to measure, monitor, and manage climate-related risks and opportunities.
Disclose Scope 1, Scope 2, and Scope 3 GHG emissions, and the related risks	Scopes 1 and 2 GHG emissions metrics, separately disclosed, expressed as disaggregated and aggregate constituent greenhouse gasses, and in absolute and intensity terms.	Gross Scope 1, Scope 2 emissions in metric tons of CO2 equivalent.	Information on transition / physical risks, opportunities, capital deployment, internal carbon prices; cross-industry metrics for Scope 1 and 2 greenhouse gas emissions, separately disclosed for consolidated accounting group, associates, joint ventures, and subsidiaries / affiliates.

Highlight key:
- Proposal deviates from TFCD recommendations
- Proposal fully aligns or adds to TCFD recommendations

Metrics & Targets			
	SEC Climate Disclosure	**EFRAG**	**ISSB Proposal**
Disclose Scope 3 GHG emissions and the related risks	Scope 3, if material or if have set reduction targets that include Scope 3; If reporting Scope 3, separately break out significant categories as well as reporting total. Excludes SRCs.	Scope 3 Emissions required to be disclosed in metric tons of CO2 equivalent, categorized from (i) upstream purchasing, (ii) downstream sold products, (iii) goods transportation, (iv) travel, and (v) financial investments.	Scope 3 Emissions including upstream and downstream emissions as well as value chain emissions.
Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets	The registrant's climate-related targets or goals, and transition plan, if any.	Policies, measurable targets, and action plans / resources related to climate change mitigation and adaptation.	Climate-related targets including metrics used to assess progress, absolute vs. intensity, objective of target, comparison to last int'l climate agreement, timeframe / base period, and whether derived using sectoral decarbonization approach.

Highlight key:
- Proposal deviates from TFCD recommendations
- Proposal fully aligns or adds to TCFD recommendations

Integration of TCFD

The Task Force on Climate-related Financial Disclosures (TCFD) is a set of disclosure recommendations that are structured around four thematic areas representing the core operating components of a company: Governance, Strategy, Risk Management, and Metrics & Targets. Further supported by 11 recommended disclosures, these components build out a framework that is intended to help investors and other stakeholders understand how an organization is assessing, incorporating, and addressing climate-related risks and opportunities.[10]

In developing their respective disclosure guidelines, the SEC, EFRAG, and IFRS each used elements of TCFD's disclosure framework to inform their climate reporting requirements. Components of the framework are incorporated at varying degrees of magnitude in each entity's proposal, but each utilizes TCFD as at least a foundational template in deciding what companies may be required to report.

Establishing a common framework to be used in developing regulation is important when considering future sustainability disclosure requirements. By aligning the methods and requirements, regulators can promote commonality across jurisdictions and ease the reporting burden on those companies that may be required to report to multiple regulatory entities. TCFD is already one of the most commonly used disclosure frameworks, with countries such as the UK and New Zealand among the first countries to require certain entities to include climate-related risks and opportunities in their annual reporting utilizing TCFD guidance (the UK requirements will be phased in starting in 2022, while New Zealand's will become mandatory commencing 2023).[11] With many multinational corporations either based in or operating in the UK, it is likely that these requirements will have considerable reporting implications across geographies. As such, TCFD-alignment within existing and future regulatory updates should be considered to continue movement towards a global reporting standard.

By aligning the methods and requirements, regulators can promote commonality across jurisdictions and ease the reporting burden on those companies that may be required to report to multiple regulatory entities.

Here we compare how each proposal maps onto TCFD's four pillars: Governance, Strategy, Risk Management, and Metrics & Targets.

Alignment with TCFD

With TCFD as a foundational component of each entity's proposed reporting structures, those organizations voluntarily reporting in line with TCFD guidance may find parts of these disclosures to be familiar and already have structures and processes in place to gather and report data. However, there are additional components to each proposal that go above and beyond the pillars and recommendations laid out by TCFD, adding more specificity and granularity to their desired outputs.

Both the ESRS and ISSB exposure drafts strongly align with TCFD guidance. Their differences, both from TCFD and each other, arise primarily from two dimensions: different wording that is intended to capture the same information as TCFD, and additional requirements for additional information to provide a more granular level of detail (which this report will focus on). Both proposals add to the aforementioned pillars of Governance, Strategy, Risk Management, and Metrics & Targets, though the majority of additions and classification differences arise in the Strategy and Metrics & Targets pillars, as further explored in the following sections.

Consistency across regulatory frameworks and geographies will be important to not only improve the quality of data being reported, but also to ease the reporting burden on corporate issuers. As that burden eases, corporate issuers will be able to devote more resources to address the climate crisis.

In comparison, the SEC's climate disclosure proposal varies from TCFD guidance more than both the ESRS and ISSB exposure drafts. The proposal does broadly align with the four pillars and 11 recommended disclosures, and in some circumstances requires additional disclosure on top of TCFD guidance. However, there are components that either vary significantly or are not required, diverging from other proposals and impacting global alignment. For certain metrics, only those entities which have publicly released related targets or strategies would be required to disclose. For example, an entity that has defined Scope 3 emissions as material or has set an emissions target including Scope 3 emissions would be required to disclose said emissions (with a safe harbor provision), while a company that has not set a relevant emissions goal or determined Scope 3 to be material would not have to disclose this information under the current proposal.

Differences notwithstanding, the near-simultaneous emergence of three highly-visible disclosure proposals, all utilizing TCFD guidance, marks a significant step towards developing a harmonized global baseline in climate-related reporting and disclosure. Consistency across regulatory frameworks and geographies will be important to not only improve the quality of data being reported, but also to ease the reporting burden on corporate issuers. As that burden eases, corporate issuers will be able to devote more resources to address the climate crisis.

Governance

Each of the three proposals fully aligns with the Governance guidance outlined by TCFD, and additional components are minimal. Where each proposal distinctively builds on TCFD guidance is on disclosure of qualifications and experience of those responsible for climate oversight. Specifically, the SEC's proposal would require disclosure of the climate-related expertise of those management and board members responsible for climate oversight. Similarly, the ISSB's proposal would require reporters to provide additional detailed information describing the body or individual responsible for the oversight of climate-related risks and opportunities. The ESRS takes a wider approach with broad additions, requiring reporting entities to describe more of the processes and strategies used to inform sustainability matters.

The alignment with TCFD's governance guidance across the three proposals is an encouraging step towards consistency between nations and across markets. Though each is tailored specifically to its respective market, companies that already report along the TCFD guidance should be able to successfully utilize existing methods and strategies when reporting along any of the three highlighted proposals.

Strategy

Scenario analysis

Climate scenario analysis is an analytical tool that helps companies develop climate plans and assess their resilience to climate-related risks by charting out business implications and potential consequences in a number of different climate scenarios (e.g., at different levels of temperature increases). This process should uncover market transition risks that a company may face in the world's transition to a low-carbon economy (e.g., markets shrinking or growing) as well as physical risks associated with climate change, like temperature increases, droughts, and floods.

Consistent with the TCFD's inclusion of scenario analysis in its framework, all three policies include scenario analysis as a tool to help companies develop a climate strategy. Scenario analysis is not required by the SEC, but it is discussed as a "reasonable alternative" that "could inform investors with respect to the resilience of registrants' business strategies and operations across a range of plausible future climate scenarios". The SEC notes that the analytical tools required to do exhaustive scenario analysis are still in their developmental stages and that the data necessary to complete scenario analysis may be costly to obtain. By contrast, both the ISSB and ESRS proposals require all entities to disclose how they used scenario analysis to evaluate climate-related risks and opportunities in a high level of detail.

Additional requirements and insights

Many of the components that diverge from TCFD guidance can be found within the Strategy pillar in each proposal. As with all other pillars, both ESRS and ISSB are fully consistent with all recommended disclosures and guidance of the Strategy pillar. However, both have requirements for additional, more granular information surrounding strategy disclosure. In the ESRS proposal, the strategy pillar is complemented with additions focusing on additional risk disclosures and connection to financial position and associated statements. This section also integrates components of the EU Taxonomy Regulation, requiring the use of "Taxonomy-alignment ratios and consistency of resources and financial opportunities from Taxonomy Regulation." [12] Additional information required in the ISSB proposal leans more towards impacts on strategy and planning: this exposure draft references transition plans as a part of an entity's strategy, and thus these plans are subject to disclosure requirements, unlike the TCFD guidelines which do not expressly require disclosure.

Connecting the risks and opportunities to financial impacts is important in advancing both global regulation and wider corporate sustainability action, acting as a clearer link between planet and profits in a company's triple bottom line.

One of the most important differences to highlight is the SEC's requirements on disclosure related to the entity's finances and the impact of climate-related risks and opportunities on financial performance. The SEC's mode of effecting change is through regulation tied to investment activities and is inherently biased toward the needs of investor communities, hence their focus on the 10-K as the vehicle for disclosure requirements. Entities are required to report how any identified climate-related risks have had or are likely to have a material impact on the line items of their consolidated financial statements and related expenditures, which investors often consider in their decision making processes. Specifically, the proposal sets a threshold for financial impact and expenditure metrics, requiring that any impact greater than 1 percent of the total line item value must be disclosed. This varies from TCFD guidance in that the SEC's proposal describes the connection to financial performance more clearly. There is speculation that this requirement may be challenging for some reporting entities, as it requires a different definition of materiality than TCFD guidance and would require a more quantitative assessment on financial impacts.

The additions to the Strategy pillar demonstrate a clear need to align strategy disclosure with tangible and quantifiable financial impacts of climate-related risks and opportunities. These are particularly highlighted by the SEC and ESRS proposals given their positions as regulators, while those entities adopting ISSB practices may choose to incorporate more financial focus in their eventual regulations. Connecting the risks and opportunities to financial impacts is important in advancing both global regulation and wider corporate sustainability action, acting as a clearer link between planet and profits in a company's triple bottom line.

Risk Management

Each proposal largely aligns with the Risk Management pillar in the TCFD guidance. The ESRS proposal requires additional impacts be taken into consideration in the disclosure of top risks and opportunities, along with more detailed application guidance for both physical and transition risks identification and assessment. Furthermore, the ESRS proposal includes the concept of double materiality as the union of impact and financial materiality, or how sustainability matters affect the company's position along with how the entity itself impacts the environment and society at large. Double materiality requires companies to manage the external risk on their own operations, along with how their operations impact risk management on external factors.

Climate-related reporting should not only provide a historical view of the entity's performance, but also present a future-oriented view of how the company will address the risks and opportunities presented by the climate crisis.

ISSB's proposal similarly highlights priority opportunities and fine-tunes reporting on input parameters for risk identification, along with including an update requirement if the entity has changed their processes compared to the prior reporting period. Outside of these additions, entities following TCFD guidelines may already be prepared for risk management disclosure in the ESRS and ISSB proposals.

A major change in Risk Management stems from the SEC's proposal. Under the current structure, those under the SEC's jurisdiction would only be required to disclose climate-related risks, while climate-related opportunities are optional and can be described if applicable. Where described, financial information connected to climate-related opportunities should be included. With TCFD requiring disclosure on both climate-related risks and opportunities, this represents a significant deviation from the framework and its capabilities.

Alignment on risk management will be important, as it will allow for a more accurate forward-looking view on a firm's climate strategy and activity, rather than just those risks that the firm has identified or already experienced. Climate-related reporting should not only provide a historical view of the entity's performance, but also present a future-oriented view of how the company will address the risks and opportunities presented by the climate crisis. Without the disclosure of potential climate-related opportunities, disclosure may paint an incomplete picture of a reporting company's climate strategy and activity: although in the case of the SEC in particular, the risk with mandating disclosure of opportunities is that the SEC might foster greenwashing and create a defense because companies would say they were required to disclose opportunities.

Metrics & Targets

Scope 1 & 2

The SEC's Proposed Rule requires Scopes 1 and 2 GHG emissions disclosures, by constituent greenhouse gasses and in the aggregate, in absolute terms and in terms of intensity.

The ESRS exposure draft requires the gross Scope 1 and 2 emissions. Additionally, ESRS requires the share of Scope 1 GHG emissions under regulated emission trading schemes. For Scope 2, both market-based and location-based Scope 2 emissions disclosures are required.

ISSB proposes disclosures of Scope 1 and 2 GHG emissions on an absolute basis and on an intensity basis. Separately, the ISSB requires Scope 1 and 2 disclosures for the consolidated accounting group (parent and its subsidiaries) and the associates, joint ventures, unconsolidated subsidiaries, or affiliates not included in the consolidated accounting group.

Scope 3

The SEC's proposed rule only requires Scope 3 disclosures where material or where a company has already set Scope 3 reduction targets. Smaller Reporting Companies (SRCs) are exempt from Scope 3 requirements. Where a company is disclosing Scope 3 emissions, the SEC would required emissions calculations to be broken out into significant categories in addition to total Scope 3 emissions. In order to ensure that reporting companies are shielded from undue liability originating from third parties within the value chain, a safe harbor provision was included with respect to Scope 3 emissions in the SEC's proposal. This provision is hoped to address the many challenges associated with reporting Scope 3 emissions and encourage companies to track and disclose associated information.

ESRS Scope 3 emissions disclosures will be mandatory for all companies disclosing. Specifically, the GHG emissions in metric tons of CO_2 equivalent that occur in the company's value chain beyond Scope 1 and 2 emissions. It also includes GHG emissions from:
a) upstream purchasing, b) downstream sold products, c) goods transportation, d) travel, and e) financial investments.

ISSB's exposure drafts propose that companies' Scope 3 emissions should include a) both upstream and downstream emissions, b) an explanation of the activities included within Scope 3 calculations, and c) an explanation of whether or not the company has included emissions information for entities in its value chain. If the company is not disclosing Scope 3 emissions, ISSB includes a provision to explain why they are omitted. For example, if a U.S.-based SRC would like to use the ISSB standards as a basis for their disclosures, they are not required to to include Scope 3 under the SEC, and would therefore explain reasons for omission instead.

Alignment along these disclosures are particularly important as the data disclosed here will inform analysis by other entities like ESG data providers and ratings agencies.

Additional requirements and insights

As seen with other TCFD guidance pillars, the ESRS and ISSB proposals fully align with TCFD guidance on Metrics & Targets, and further add on to the requirements to ensure a more granular view of the reporting entity. Specifically, the ESRS is much more prescriptive in this section compared to both TCFD and the other regulations, as is the case throughout the entirety of the highly prescriptive proposed regulation. The ESRS would require additional disclosure on components like a target's potential effects on financial metrics, integration of Taxonomy regulations, and a distinction of three levels of targets including general climate-related targets, GHG emission reduction targets, and net zero targets / other neutrality claims. The level of specificity seen here in the ESRS (and elsewhere in the proposal) may provide a more clear direction for future regulatory agencies in developing a highly-prescriptive disclosure framework.

The SEC's proposal aligns with TCFD in certain circumstances: for companies that have publicly communicated climate-related goals and targets, the proposal would require disclosure on the scope and structure of said goal or target. For example, if a company has committed to net zero emissions by 2030 or alignment with the Paris Agreement, it would be required to disclose the scope and structure along with any progress toward meeting the target. Alternatively, those companies that have not committed to any such goal or target would not be required to report these metrics. This may result in a variety of scenarios: it may discourage companies from setting more ambitious net zero goals with the knowledge that they would then be required to commit resources toward identifying and reporting their Scope 3 emissions and other related information. On the other hand, the inclusion of a regulatory requirement may incentivize the creation of stronger and more effective net zero commitments.

From zero disclosure required for some entities under the SEC's proposal to a long list of additional disclosure requirements seen with the ESRS proposal, the Metrics & Targets pillar demonstrates the greatest variation to TCFD guidance. Alignment along these disclosures are particularly important as the data disclosed here will inform analysis by other entities like ESG data providers and ratings agencies. Future regulatory entities developing sustainability disclosure requirements should consider the Metrics & Targets pillar to be a core component of their reporting structure, and should follow in ESRS and ISSB's footsteps to fully incorporate (and expand upon) TCFD guidance and recommendations.

The inclusion of a regulatory requirement may incentivize the creation of stronger and more effective net zero commitments.

TCFD recommends the disclosure of Scopes 1, 2, and 3 emissions in their guidelines. The ESRS and ISSB proposals both adhere to this guidance, while the SEC varies in Scope 3 requirements depending on materiality. Emissions disclosures are a major component covered in the Metrics and Targets pillars of the TCFD guidance, and will be further expanded upon in subsequent sections.

Note: In addition to each respective proposal's full draft documents (see New Developments in Corporate Climate Disclosure section), sources for the TCFD Alignment section are as follows:

- SEC: ERM Market Update - SEC Proposed Climate Rule [13]
- ESRS: Appendix IV - TCFD Recommendations and ESRS reconciliation table[14]
- ISSB: IFRS S2 Climate-related Disclosures with the TCFD Recommendations[15]

3. Additional Components

Assurance Requirements

Assurance requirements denote the level of third-party auditing needed for companies to comply with emissions disclosure requirements. Assurances need to be completed by professionals with requisite expertise to perform the review (typically accountants and specialized assurance providers with deep expertise in ESG topic areas), to ensure the accuracy of the sustainability information that is being disclosed. There are two main kinds of assurance mentioned in the three proposals: limited and reasonable assurance. Limited assurance is the less stringent form of assurance, and the conclusions of a limited assurance engagement can be framed as 'no material misstatements appeared to be found during the engagement.' In contrast, reasonable assurance requires more effort and entails that the assurance provider can positively conclude, 'the information provided is accurate.'

Both the SEC and ESRS will require assurances on varying timeframes, with the SEC phasing in assurance beginning with limited assurance and then moving up to reasonable assurance for Scope 1 and 2 Emissions. Importantly, this only applies to large accelerated filers, accelerated filers, and non-accelerated filers for Scope 1 and 2 Emissions; there are no assurance requirements for Scope 3 Emissions, or for Smaller Reporting Companies under SEC guidelines. The proposed rule specifies an audit of the climate-related financial data, consistent with the disclosure of that information in the financial statements, while separately requiring assurance of GHG emissions. In the EU, the ESRS proposal is considering mandating limited assurance, with a long-term plan of moving to reasonable assurance requirements.

Though audit requirements are not included within the ISSB's scope, guidelines for audit and oversight of disclosures from third parties are given. Regulators that choose to implement the ISSB proposals will be able to specify their own assurance requirements, but regardless of specific regulator requirements, companies will still need to adhere to the strict processes and controls needed to fully disclose sustainability-related information.

Acceptance of Alternative Reporting

The ISSB is working to develop a global baseline standard for sustainability reporting. This is demonstrated by the merging of the Value Reporting Foundation (VRF) and the Climate Disclosure Standards Board (CDSB) to form the ISSB, with the intention to incorporate industry-specific SASB metrics at an international level.[16] The ISSB also issued a Memorandum of Understanding (MoU) with the Global Reporting Initiative (GRI) in March of 2022 with the hopes of creating a 'building blocks approach' in which the ISSB creates the global baseline standard.[17] This partnership allows disclosure of information that meets the needs of investors, and then builds onto that baseline to include information from the GRI that meets the needs of a broader stakeholder group.

The SEC proposal does not include the acceptance of other reporting standards, but the proposed release solicits public comment on whether it should accept alternative reporting. It does mention, however, that it intends to be in harmony with requirements from other regulatory agencies such as the Environmental Protection Agency (EPA) and intends to accept data prepared in compliance with relevant regulations from other agencies to reduce reporting burdens on companies.

The ESRS proposal allows other frameworks to be used in addition to the ESRS, however, there are few clear references to ISSB in the exposure drafts. This has left companies and business coalitions concerned that reporting in line with ISSB will not satisfy the ESRS requirements. One key area of divergence is that the ESRS definition of impact materiality does not encompass enterprise value creation like the ISSB's does.

In April 2022, the IFRS convened a working group for enhanced cross-jurisdictional compatibility to align sustainability reporting initiatives around the world. The Chinese Ministry of Finance, the European Commission, the European Financial Reporting Advisory Group, the Japanese Financial Services Authority, the Sustainability Standards Board of Japan Preparation Committee, the United Kingdom Financial Conduct Authority, and the US Securities and Exchange Commission are all involved in hopes of fostering dialogue and bringing the current proposals together for alignment on a global baseline of climate disclosures while public consultation periods are still open.[18]

Level of Prescriptiveness

The ESRS disclosure requirements are the most prescriptive when compared to SEC and ISSB at this time. ESRS's framework is quite detailed, as it outlines KPIs that are both sector-specific and agnostic. The ESRS includes detailed examples of line item disclosures, metrics, impacts of climate-related information, and sample formats for inclusion in reporting. One specific example of increased prescriptiveness between the ESRS and SEC proposals is in the inclusion of scenario analysis. Whereas the SEC only requires disclosure of scenario analysis if a company is already undertaking such activity, ESRS requires scenario analysis from all companies.

Potential Expansion of Scope

This report was developed specifically focusing on the climate-related disclosures of each proposal. However, as the regulatory landscape continues to expand and other considerations are taken into account, it is expected that regulators such as the SEC will introduce additional ESG-related disclosure requirements or standards boards like the IFRS will expand the reach of their proposed frameworks.

The urgency of the climate crisis has helped drive momentum in developing these three proposals. But their introduction also demonstrates the need for deeper disclosure across a wider range of metrics and issues.

The ESRS has been developed to include all aspects of ESG. On top of general principles and requirements, there are unique exposure draft documents relating to ESG-specific topics including pollution, workforces, consumers, and business conduct. Through this proposed regulation, ESRS is intended to be an all encompassing ESG and sustainability reporting and disclosure requirement rather than piecemeal implementation across an extended timeframe.

In the spring of 2022, the IFRS released two ISSB standards: the General Requirements Standard and the Climate Standard. For the time being, these exposure drafts only cover a limited amount of ESG-related topics, chiefly the climate-related consideration highlighted in this report. Using feedback from this consultation period, they plan on developing further standards across a variety of sustainability-related topics to "form a comprehensive global baseline of sustainability disclosures designed to meet the information needs of investors in assessing enterprise value."[19]

It is not expected that other ESG components will be added into the SEC's proposal. Instead, the SEC is likely to introduce proposals similar to the climate-related disclosure proposal focused on other ESG-related issues. In March 2022, the SEC proposed a rule on cybersecurity risk management, strategy, governance, and incident exposure.[20] Further, it is expected that they will update rules on issues like human capital management and board diversity in the near future.[21]

The urgency of the climate crisis has helped drive momentum in developing these three proposals. But their introduction also demonstrates the need for deeper disclosure across a wider range of metrics and issues. As the climate-related disclosures take off, companies across geographies can expect disclosure on ESG-related considerations to follow in step.

Timeline to Implementation

All three policies are in the middle of public comment periods, with the SEC's deadline recently extended to June 17 to allow more comments. After comments are collected, each proposal will revert to a finalization phase, with anticipated phase-in periods varying between the three.

The SEC currently plans to phase in its disclosure rules beginning in FY 2023, with large accelerated filers first due to disclose their Scope 1 and 2 Emissions for FY23 in 2024 and then Scope 3 Emissions a year later. Accelerated filers and small reporting companies are then phased into the rules as in the table below.

Timeline to implementation*

SEC Phase-In Period	Large, accelerated filers	Accelerated filers, non-accelerated filers	Small reporting companies
Scope 1 and 2 Emissions	First disclosure year FY23, filed in 2024	First disclosure year FY24, filed in 2025	First disclosure year FY25, filed in 2026
Scope 3 Emissions	First disclosure year FY24, filed in 2025	First disclosure year FY25, filed in 2026	N/A

** Assumes adoption of rules during 2022 and timing applies to companies with a 12/31 FYE.*

The EU has not released an official phase-in timeline yet, but current communication states that FY 2023 will be the first disclosure year for large companies, with SMEs to report beginning only in 2026. Other key dates in the EU's timeline include:

- October 2022: Adoption of first set of standards via delegated Act by the European Commission
- October 2023: Adoption second set of Standards, incl. SMEs and sector-specific standards.

Additional Resources

How to Comment

The SEC's Enhancement and Standardization of Climate-Related Disclosures for Investors

- Find the link to the comment page here
- For guidance on how to submit a comment, visit the SEC's How to Submit Comments page

EFRAG European Sustainability Reporting Standards

- See page 12 of the Cover Note for Public Consultation for instructions here
- Find the Sections 1 and 2 survey here
- Find the Section 3 survey here

IFRS International Sustainability Standards Board Disclosure Exposure Drafts

- General Sustainability-related Disclosures survey found here, or submit a comment letter
- Climate-related Disclosures survey found here, or submit a comment letter

Resource Documents

Climate Disclosure Convergence: TCFD, SEC, and ISSB: TCFD-hosted one-hour webinar in conjunction with representatives from the SEC and ISSB to highlight the proposals' integration of TCFD guidance.

Connecting ESG, Capital Markets, and CFOs: Explores the evolving relationship between ESG, capital markets, and corporate finance. It argues the importance of ESG reporting and disclosure, and its growing impact on corporate performance.

Costs and Benefits of Climate-Related Disclosure Activities by Corporate Issuers and Institutional Investors: Survey of corporate issuers and institutional investors to understand what U.S. private sector organizations currently spend measuring and managing climate-related disclosure activities.

Market Update: SEC Proposed Climate Rule: Overview of the SEC's proposed climate rule, highlighting the proposal's impacts on business strategy and what it means for companies under the SEC's jurisdiction.

Understanding the cost implications of the SEC's proposed climate-related disclosure rule: Webinar featuring representatives from Ceres, ERM, and Persefoni speaking on the cost of climate change related disclosure.

Endnotes

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About the SustainAbility Institute by ERM

The SustainAbility Institute is ERM's primary platform for thought leadership on sustainability. The purpose of the Institute is to define, accelerate, and scale sustainability performance by developing actionable insight for business. We provide an independent and authoritative voice to decode complexities. The institute identifies innovative solutions to global sustainability challenges built on ERM's experience, expertise, and commitment to transformational change.

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About Persefoni

Persefoni, Inc., is the leading Climate Management & Accounting Platform (CMAP). The company's Software-as-a-Service solutions enable enterprises and financial institutions to meet stakeholder and regulatory climate disclosure requirements with the highest degree of trust, transparency, and ease. As the ERP of Carbon, the Persefoni platform provides users a single source of carbon truth across their organization, enabling them to manage their carbon transactions and inventory with the same rigor and confidence as their financial transactions.

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