Comments on the Request for the "Rules to Enhance and Standardize Climate Related Disclosures for Investors" by the SEC

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Global Strategy Task Force on ESG Disclosure
Committee on Financial and Capital Markets
Keidanren

To: The U.S. Securities and Exchange Commission (SEC)

Keidanren welcomes the opportunity to submit comments on the Request for the "Rules to Enhance and Standardize Climate-Related Disclosures for Investors" by the SEC.

General Comments

Keidanren (Japan Business Federation) is Japan's largest comprehensive economic organization with a membership comprised of more than 1,400 representative companies in Japan across all sectors including manufacturing, financial services, the service industry, distribution, construction and transportation. Many of Keidanren's members are raising and managing funds in both domestic and global markets. There are now more than 10 Japanese companies listed on the U.S. stock exchange and registered with the SEC, most of which are leading companies in the manufacturing and financial industries.

Taking action to combat climate change is an urgent task here in Japan, similar to the rest of the world. As part of this effort, both Japanese public and private sectors are working together to achieve the country's commitment to being carbon neutral by 2050. There is an increasing demand from investors and capital markets for the disclosure of sustainability information centered on climate change issues. To fulfill the demand, the International Financial Reporting Standards (IFRS) Foundation established the International Sustainability Standards Board (ISSB) and published a draft version of climate-related disclosure standards at the end of March 2022.

Japan also sees an increasing number of corporations that are actively engaged in the disclosure of their sustainability information centered on climate change issues. As of May 17, 2022, the country has 843 companies and institutions that have announced their support to the Task Force on Climate-related Financial Disclosures (TCFD), which is the largest number in the world. In addition, all businesses listed on Japan's Prime Market are required, under the Corporate Governance Code, to disclose information based on a framework equivalent to that of the TCFD. Japan's Financial Services Agency (FSA) is considering institutionalizing the practices of sustainability (including climate change) disclosure in securities reports. The country's public and private sectors are both active in disclosing information related to climate change issues.

Under these circumstances, we consider that it is a timely opportunity for the U.S. Securities and Exchange Commission (SEC), where a number of global enterprises are listed on stock exchanges and the world's largest capital markets are located, to propose "Rules to Enhance and Standardize Climate-Related Disclosures for Investors" (hereinafter the "Rules"). We hope that the SEC will utilize the insights received through the comment period to contribute to the development of standards that can serve as a global, high-quality baseline for the ISSB. Keidanren looks forward to sharing its views regarding the development of ISSB standards in the future.

Keidanren is pleased with the SEC's proposed Rules related to the following points: 1) They were developed based on the TCFD recommendations; 2) They take into consideration the disclosure of corporate business models; and 3) They do not require industry-based disclosures in order to reduce the burden on registrants. On the other hand, in order to ensure the effectiveness of disclosures according to the Rules, it is critical that the SEC define the disclosure requirements by fully considering the embedding of disclosure practices into the registrants' business environment.

In view of this, we would particularly like to request the matters described in the Detailed Comments below.

Detailed Comments

1. Information to Be Disclosed

(A) Disclosure of Scenario Analysis [Questions 19, 21, 28, 30, 31, 32, and others]

- The proposed Rules require that a company provide specific scenario analysis disclosure if it uses such analytical tools. However, in that case, the company should be allowed to use a scenario model that aligns with a company's individual situation, and should not be forced to apply a specific scenario model designated by the Rules.
- In view of the fact that a scenario analysis involves a large amount of forward-looking information and many uncertainties, businesses are concerned about the disclosure in statutory disclosure documents that could potentially result in a penalty. Accordingly, if the Rules require scenario analysis disclosure, it should be covered by a safe harbor.
- Furthermore, references to other disclosure documents should be allowed[1] since scenario analysis disclosure is meant to include professional and technical information.

[1] In order to reduce burden on registrants, they should be widely allowed to incorporate scenario analysis and other disclosures by reference from other parts of voluntary disclosure documents and annual reports. Registrants should also be kept free from the need to follow additional procedures when making a reference from voluntary disclosure documents or other relevant documentation.

(B) Notes on Financial Impacts of Climate Change [Questions 53, 59, 60, 66, 68, 77, 87, and others]

- Under the proposed Rules, a registrant is required to calculate the impact of climate change (impact of climate-related risks on its financial statements' line items and related expenditures, and disclosure of financial estimates and assumptions) on a consolidated basis for the fiscal year presented and disclose the impact in notes to the financial statements.
- Considering the following, it would be premature to require registrants to include financial impacts of climate change in notes to financial statements as part of statutory disclosures:
  - Climate-related risks change over an extended period of time, and therefore, it is difficult to identify their direct and indirect impacts. Even if the impacts are calculated, the results may differ significantly when only a slight change is made to the assumptions. It would be a challenging task to make a comparison with a competitor using the same conditions as those of the competitor.
  - Financial impacts often involve multiple factors, and in most cases, it is difficult to quantify the impacts that are caused solely by climate change.
  - It is difficult for an auditor, whose expertise is in accounting, to assess the impact of a potential natural disaster on a business.
  - A threshold of one percent of a line item for disclosing a financial impact will impose a significant burden on companies, as they need to aggregate the impacts on the whole of consolidated financial statements.
  - The proposed Rules require a consistent scope of consolidation for disclosure between financial statements and financial impacts from climate change. This is not readily feasible due to data constraints and other factors as well.

(C) Disclosure of GHG Emissions (Scope3) [Questions 98, 100, 125, 133, 136, and others]

- The proposed Rules require disclosure of Scope 3 GHG emissions data if it is material or if the registrant has made a GHG emissions reduction commitment.
- However, we consider that a significant amount of time and labor will be needed to require all registrants to establish a mechanism to measure and collect data necessary for the Scope 3 disclosure and disclose information ensuring reliability and completeness. The significance of disclosure (usefulness for and ways of use by investors) must be made perfectly clear, as some have pointed out that the Scope 3 GHG emissions disclosure could obscure the ownership of responsibilities for GHG emissions when a company ("Company A") is operating in various corporations' value chains. Emissions from Company A will be counted by those various corporations in their volume of Scope 3 GHG emissions.
- Therefore, we would recommend that Scope 3 emissions disclosure not be mandatory but be voluntary for the time being. When Scope 3 emissions disclosure practices become more sophisticated, a decision should be made on whether to implement the statutory disclosure mandate based on an analysis of the costs and benefits of disclosure.

- If the statutory disclosure mandate needs to be implemented, a safe harbor rule should apply to Scope 3 disclosures. At the same time, we believe that the requirement to disclose Scope 3 emissions "if material" should be maintained.

(D) Disclosure of GHG Emissions (Scope 1, 2, and 3) [Questions 94, 105, 107, 114, and 116]

- If GHG emissions disclosure is required, we request that the following five points be considered to ensure a strong balance of the costs and benefits with the feasibility of disclosure practices by registrants:
    - While the proposed Rules require disclosure of emissions by the type of GHG, the GHG emissions should be disclosed in terms of aggregate carbon dioxide equivalent (CO2e). [Question 94]
    - Most companies have not yet established a mechanism to measure and collect consolidated GHG emission information. Considering the fact that they need to collect data from multiple locations at home and abroad, companies should be allowed to use data for the preceding fiscal year rather than data for the same fiscal year as financial statements. [Question 105]
    - There is still no readily available way to use so-called location data in a manner that would be useful to investors in making their investment decisions. [Question 107]
    - Reporting of historical GHG emissions data for fiscal years preceding the enforcement of the "Rules" should not be required, as it would pose a certain level of challenge to registrants. [Question 114]
    - Under the proposed Rules, a registrant is required to include all of the emissions from a consolidated subsidiary. For an equity method investee, the registrant is required to include its share of emissions based on its percentage ownership of such investee. We suggest that, because of the difficulties to ask all equity-method investees to submit GHG emission data in a timely manner, registrants be permitted to exclude some investees from the scope of the emission calculation according to a materiality threshold. [Question 116]

(E) Disclosure of Goals and Targets [Questions 168, 169, 174, and others]

- In order to reduce the burden on registrants while ensuring comparability, the range of goals and targets subject to the mandatory disclosure should be restricted to the minimum. We recommend that the Commission require registrants disclose a minimum range of goals and targets after articulating disclosure objectives and allow registrants to select other disclosure items on their own.
- With regard to the goals and targets subject to disclosure, the scope of information for mandatory disclosure should be limited to a certain range. We recommend that no detailed rules be set on the disclosure of "measures to meet a registrant's goals or targets," so that registrants have a certain level of freedom in making their disclosures.

- Disclosed goals and targets may include forward-looking information and therefore should be covered by a safe harbor rule.

2. Attestation [Questions 135, 136, 144, and others]

- The proposed Rules require an attestation report (in a phased manner from limited assurance to reasonable assurance) on Scope 1 and 2 disclosures. However, we consider that this would impose a significant burden on registrants, and it is premature to require them to include an attestation report at this point in time since attestation practices for Scopes 1 and 2 emissions have not yet been developed fully. For the purpose of providing useful information to investors, it is most important to establish the practices of measuring and disclosing GHG emissions, which we consider would help meet investor demand to a satisfactory degree.
- For similar reasons, an attestation report should not be required for Scope 3 disclosures.
- Measures to ensure data accuracy should be explored widely, without limiting to attestation.

3. Compliance Date [Questions 198, 199, and others]

- Under the proposed Rules, the compliance date for the disclosures is set in fiscal year 2023 for large accelerated filers. Unfortunately, this timeline is not realistic. A significant amount of time is necessary to prepare for the statutory disclosures, and at least one year should be afforded from finalization of the "Rules". Therefore, we request that the Commission reconsider the compliance date.
- While, as mentioned above, we consider that it is premature to request registrants provide Scope 3 emission disclosure requirements and an attestation report covering Scope 1 and 2 emissions, if these are included in the proposed Rules, we support establishing a date for compliance that is later than the date for other disclosure items.