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June 17, 2022

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: File Number S7-10-22 Proposed Rule - The Enhancement and Standardization of Climate-Related Disclosures for Investors

Dear Office of the Secretary,

The Center for Audit Quality (CAQ) is a nonpartisan public policy organization serving as the voice of U.S. public company auditors and matters related to the audits of public companies. The CAQ promotes high-quality performance by U.S. public company auditors; convenes capital market stakeholders to advance the discussion of critical issues affecting audit quality, U.S. public company reporting, and investor trust in the capital markets; and using independent research and analyses, champions policies and standards that bolster and support the effectiveness and responsiveness of U.S. public company auditors and audits to dynamic market conditions. Based in Washington, DC, the CAQ is affiliated with the American Institute of CPAs. This letter represents the observations of the CAQ based upon feedback and discussions with certain of our member firms, but not necessarily the views of any specific firm, individual, or CAQ Governing Board member.

The CAQ appreciates the opportunity to share our views related to the Securities and Exchange Commission (SEC), *Proposed Rule: The Enhancement and Standardization of Climate-Related Disclosures for Investors* (proposed rule or release).

CENTER FOR AUDIT QUALITY
555 13th Street NW, Ste 425 E
Washington, DC 20004

(202) 609-8120
www.thecaq.org

The key points of our letter, which are described in more detail below, are as follows:

- **Organizational boundaries for GHG emissions disclosures:** While we appreciate the intent of the SEC aligning the organizational boundaries for GHG emissions disclosures with the boundaries of the consolidated financial statements, we think it's important to acknowledge that many companies are voluntarily reporting under different organizational boundaries than proposed. As a result, companies could encounter reporting challenges and burdens as they move toward reporting under a different boundary.

- **GHG emissions methodology:** The proposed rule concerning the presentation, methodology, including underlying assumptions, and organizational and operational boundaries applicable to the determination of Scopes 1 and 2 emissions does not specify a framework such as the GHG Protocol. We understand the SEC did not specify a framework so that registrants would have flexibility to adapt to new approaches and GHG emissions methodologies as they emerge. However, we believe specifying in the final rule that a widely used framework, such as the GHG Protocol, should be used will help support GHG emissions disclosures being more comparable from company to company and limit companies from opting to use bespoke methods.

- **Attestation requirements:** We are supportive of the proposed rule requiring certain registrants to subject GHG emissions disclosures to attestation as this will enhance the reliability and quality of GHG emissions disclosures. Research shows that assurance over climate related reporting offers increased investor protection, in particular when performed by a public company auditor. There is an opportunity for the SEC to promote consistent, comparable, high-quality attestation over GHG emissions by further enhancing some of the attestation requirements in the proposed rule.

- **Regulation S-X proposed amendments:** Climate-related risks, like any other risk, will vary from company to company. The time horizon for when those risks become material to the financial statements and are reflected in the underlying financial statement accounts also can vary from company to company. At the same time, investors continue to call for greater insight into how climate-related risks are affecting the financial statements. We are supportive of the SEC's efforts to provide more clarity on what climate-related matters a company must disclose in their financial statements. However, we believe the proposed financial statement metrics requirements as written will not achieve the intended objectives and will result in various practical implementation challenges. We ask that the SEC consider alternatives that could help

focus registrants on preparing more meaningful cost-effective climate-related disclosures that are comparable from company to company.

- **Convergence with international standards:** The CAQ is supportive of a globally accepted ESG reporting system that is built from existing standards and frameworks that can be adapted to the needs of investors in different jurisdictions. Accordingly, we are supportive of an alternative provision structured to enable reporting pursuant to criteria developed by the International Sustainability Standards Board (ISSB).[1]

- **Compliance dates:** To implement the requirements of the proposed rule in a way that will support the disclosure of high-quality information that is decision useful will take time for registrants, auditors, and others to prepare. We are supportive of the SEC's phased in approach to the proposed rule's requirements. However, we provide an alternative phased in approach by both disclosure area and registrant type that would provide registrants more time to prepare for the GHG emissions and financial statement metrics disclosure requirements.

Our comments below are arranged by the various topics noted within the proposed rules.

<u>Regulation S-K proposed amendments</u>

Organizational boundaries for GHG emissions disclosures
We believe that there will be certain reporting challenges without certain clarifications related to the organizational boundaries of GHG emissions disclosures. As mentioned above, many issuers report voluntarily using the GHG Protocol under either the equity share or the operational control approach and have developed targets and milestones based on those calculations. Some observations associated with aligning the organizational boundaries for GHG emissions disclosures with the boundaries of the consolidated financial statements include:

- For companies accounting for an investment using the equity method, the proposed rule would effectively result in the company consolidating Scope 1 and Scope 2 emissions of equity method investees into Scope 1 and Scope 2 emissions of the registrant, respectively, despite the financial results of the equity method investee being collapsed into one line item in the consolidated financial statements.

[1] We acknowledge that the ISSB standards are not yet finalized and as such this recommendation is contingent upon the final standards being approved and the SEC's assessment of the final standards.

- Certain industries that account for their investments using investment company accounting and account for their investments at the fair value irrespective of ownership percentage even if an investment is controlled (i.e., they do not apply full consolidation). A key interpretive question would be whether the emissions from those investments would be classified in Scope 3 as they are not consolidated, accounted for under the equity method, or proportionately consolidated. For an equity method investee or an operation that is proportionally consolidated, the registrant would be required to include its share of emissions based on its percentage ownership of such investee or operation. That would mean that two investors (80% and 20%) in a single entity could together account for 120% of that entity's emissions which we believe would not be appropriate because it leads to the double counting of emissions.

The release states that applying existing GAAP would help limit the compliance burden for registrants as they would be able to use familiar concepts from financial reporting when preparing their required GHG emissions disclosures. For companies voluntarily reporting using the GHG Protocol under the equity share approach or operational control approach, modifying the boundaries used for these calculations at this time could place a burden on registrants preparing this information.

GHG emissions methodology

Proposed Item 1504(a), Item 1504(b), and Item 1504(e)'s instructions concerning the presentation, methodology, including underlying assumptions, and organizational and operational boundaries applicable to the determination of Scopes 1 and 2 emissions do not specify a framework such as the GHG Protocol. Thus, a company would need to reference the GHG Protocol (assuming they choose to use it) as modified by the SEC (e.g., the boundaries set by the Commission) when describing the methodology, significant inputs, and significant assumptions used to calculate GHG emissions. Without requiring a framework or adding specificity to Proposed item 1504(e)'s instructions, registrants may seek to use bespoke methods as long as they comply with the general definitions in the proposed rule. We recommend that the SEC state in the final rule that a known framework that meets specified minimum criteria be used by registrants when determining their GHG emissions. We note that the GHG Protocol is a widely used framework for emissions measurement and would expect many companies to look to their guidance when determining their GHG emissions. The SEC states in the release that the proposed rule does not require the use of the GHG Protocol in order to allow for some flexibility in the choice of GHG emissions methodologies that would permit registrants to adapt to new approaches as they emerge. We believe that specifying in the rule that a known framework that meets specified minimum criteria be used will establish a baseline for determining a registrant's GHG emissions while still allowing for flexibility that will enable registrants to adapt to new approaches as they emerge. Further, specifying a known framework be used could minimize the risk that companies use bespoke

methods for calculating their GHG emissions which would make the disclosures less comparable from company to company.

Attestation requirements

Benefits of assurance

The proposed rule would require certain registrants to subject their Scope 1 and 2 GHG emissions metrics to third party assurance. Investors continue to demand high-quality, reliable information on climate and other ESG initiatives, and other jurisdictions are responding to those demands by requiring, among other things, assurance (e.g., the Corporate Sustainability Reporting Directive Proposal (CSRD) in Europe). Accordingly, we believe the proposed requirement for certain registrants to subject certain GHG emissions metrics to attestation will help enhance the reliability and quality of that information and align assurance requirements in the U.S. with those developing globally.

A review of peer-reviewed academic studies provides additional insight and evidence on the benefits of assurance of ESG information. From an economic perspective, García-Sánchez et al. (2019) found that external assurance of corporate social responsibility (CSR) disclosure improves the positive effect of CSR disclosure on the access to financial resources for reporting companies. According to the authors, external assurance increases the credibility of CSR information and favors access to financing with lower capital constraints.[2] Further, Del Giudice et al. (2020) found that ESG rating agencies provide more accurate measures of companies' sustainability when the underlying non-financial information is subject to assurance. According to the authors, third-party assurance about the quality of ESG reporting is thus valuable to investors and other stakeholders who rely on the ESG rating for their decision making.[3]

Obtaining any level of assurance by a public company auditor involves the understanding of processes, systems, and data, as appropriate, considering the risks of material misstatement of the subject matters, and then developing an appropriate approach to obtaining evidence in order to support an opinion based on an examination or conclusion based on a review.

Research suggests that assurance over climate-related reporting, specifically when performed by a public company auditor, offers increased investor protection compared with other forms of third-party assurance or verification. There is also evidence that companies see the value of auditors applying

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[2] García-Sánchez, Isabel-María, Nazim Hussain, Jennifer Martínez-Ferrero, and Emiliano Ruiz-Barbadillo. "Impact of disclosure and assurance quality of corporate sustainability reports on access to finance." *Corporate Social Responsibility and Environmental Management* Vol. 26 (4) (2019). 832-848

[3] Del Giudice, Alfonso and Silvia Rigamonti. "Does Audit Improve the Quality of ESG Scores? Evidence from Corporate Misconduct." *Sustainability* Vol. 12 (2020). 5670

independence and objectivity to enhance the reliability of the company's ESG disclosures. Martínez-Ferrero et al. (2018) found that the probability of detecting material errors and omissions in a sustainability report is higher if it is assured by an auditing firm. It states that the propensity to detect any errors, omissions, or misrepresentations in a sustainability report is greater if the assurance is entrusted to an audit firm than to an engineering or consultancy firm. According to the authors, this arises from their greater experience in audit services, their stringent education and training, the strict ethical requirements and control mechanisms they must follow, and their stronger reputational capital.[4]

Independence and quality control

We previously shared with the SEC our view that the independence, ethical and quality control requirements with which public company auditors are required to comply are among the factors that contribute to the high-quality attestation engagements performed by public company auditors. This is consistent with the research described above. Accordingly:

- We believe the proposed rule requiring a registrant to obtain a GHG emissions attestation report that is provided by a GHG emissions attestation provider that meets the specified requirements, as proposed in 17 CFR 229.1505(b)(1), will enhance the reliability of the GHG disclosures.

- The proposed rule's requirement for the GHG emissions attestation provider to be independent with respect to the registrant, and any of its affiliates, for whom it is providing the attestation report, as proposed in 17 CFR 229.1505(b)(2), will enhance the quality and reliability of the attestation report.

Attestation standards

We support the proposed rule's requirement that the attestation engagement and related attestation report be provided pursuant to standards that are publicly available at no cost and are established by a body or group that has followed due process procedures, including the broad distribution of the framework for public comment. We agree that this approach would help to make sure that the standards upon which the attestation engagement and report are based are the result of a transparent, public, and reasoned process taking into account the public interest. This requirement should also help to protect investors who may rely on the attestation report by limiting the standards to those that have been sufficiently developed.

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[4] Martínez-Ferrero, Jennifer and Isabel-María García-Sánchez. "The Level of Sustainability Assurance: The Effects of Brand Reputation and Industry Specialisation of Assurance Providers." *Journal of Business Ethics* Vol. 150 (4) (2018). 971-990

The attestation standards of the AICPA and IAASB meet this requirement given that they follow due process, are subject to public comment and are freely available. Additionally, both the AICPA and IAASB attestation standards are principles-based and have been supplemented with guidance specifically for sustainability attestation engagements that helps support consistent application of the standards to promote the performance of quality attestation engagements. While we agree that the attestation standards of the PCAOB meet this due process requirement, we note that they are the attestation standards of the AICPA from 2003. Since 2003, the AICPA attestation standards have evolved and are the standards that are currently used by U.S. public company auditors when reporting on ESG subject matters.[5] According to an analysis that we performed of ESG reporting and assurance data for S&P 500 companies as of June 18, 2021, all U.S. public company auditors that had provided assurance over ESG-related metrics had performed those services in accordance with the AICPA attestation standards. We note that one of the strategic objectives of the AICPA's Auditing Standards Board is to converge its standards (which include the AICPA attestation standards) with those of the IAASB which will drive continued alignment and transparency on differences.[6]

To promote the quality and comparability of the attestation provided over GHG emissions from company to company, we recommend the SEC consider limiting the attestation standards that can be used by attestation providers to standards established by the following standard setters: AICPA, IAASB, and PCAOB (if updated).[7] Usage of these standards by assurance providers would be governed by their terms and regulatory requirements (e.g., non-CPA firms are not eligible to use the AICPA standards). Further, application of these professional standards will include additional requirements around engagement acceptance and continuance, quality control, independence, and ethical standards, all of which will work in concert with other professional standards and regulatory requirements to provide greater consistency over the quality of service provided by GHG emissions attestation providers.

In our analysis referred to above, we noted that some providers indicated that the attestation standard they had used was their own methodology based on the IAASB's ISAE 3000 (Revised). Accordingly, it was unclear to what extent the assurance provider had applied the ISAE 3000 standard, including its independence and quality control provisions. Given the potential differences in practice, it will be

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[5] Please note that attestation should be for assertion-based engagements (i.e., AT-C 205).

[6] See the "Strategic Initiatives of the Auditing Standards Board" within the American Institute of Certified Public Accountants, Auditing Standards Board – Auditing, Attestation, and Quality Control Standards Setting Activities - Operating Policies: https://us.aicpa.org/content/dam/aicpa/research/standards/auditattest/asb/downloadabledocuments/asb-operating-policies.pdf

[7] On May 4, 2022, the PCAOB updated their Standard-Setting and Research Projects which includes a project to consider *Attestation Standards Update*.

important for the SEC to consider limiting the standards used (as described in the previous paragraph) and also monitoring those standards referenced by the provider in their attestation report or relying upon other monitoring processes that relate to quality control.

Definition of limited and reasonable assurance
If, as suggested above, the attestation standards were limited to those issued by the AICPA, IAASB, and PCAOB, we do not believe that it would be necessary for the terms limited and reasonable assurance to be defined given that they are already defined in those standards. However, if the attestation standards were not limited to those of the AICPA, IAASB and the PCAOB, we believe the SEC should define the terms by reference to the attestation standards of the AICPA and the IAASB, rather than developing alternative definitions of the terms.

Support the progression from limited assurance to reasonable assurance
While review engagements (which result in obtaining limited assurance) help to enhance the reliability of information, they are substantially less in scope than examination engagements (reasonable assurance). The SEC states in the release that the evolving and unique nature of GHG emissions reporting involves and, in some cases, warrants varying methodologies, differing assumptions, and a substantial amount of estimation. Certain aspects of GHG emissions disclosure also involve reliance on third party data. We are supportive of the rationale described in the SEC release and agree that requiring a third party's attestation over these disclosures would provide investors with an additional degree of reliability regarding not only the figures disclosed, but the key assumptions, methodologies and data sources used by the registrant to arrive at those figures. We believe it will be important for this information to ultimately be subject to a requirement for examination engagements (which result in reasonable assurance) and as such are supportive of the proposed rule's progression from limited to reasonable assurance.

Characteristics of the GHG emissions attestation provider
17 CFR 229.1505 (b)(1) indicates that a GHG emissions attestation provider is an expert in GHG emissions by virtue of having significant experience in measuring, analyzing, reporting, or attesting to GHG emissions. In order to perform attestation engagements, it is essential that the provider have experience attesting to GHG emissions. Third-party assurance is the hallmark of investor confidence in financial reporting. We do not believe investors will be instilled with such confidence if the attest provider only has experience with, for example, reporting on its own measurements of GHG emissions. Performing competent GHG attestation engagements requires competence in assurance skills and techniques developed through extensive training and practical application and sufficient competence in the quantification and reporting of emissions. We recommend that the SEC require prior experience in issuing attest reports as one of the characteristics of the GHG emissions attestation provider.

Requirements for GHG emissions attestation reports
We believe the proposed rule to require the GHG emissions attestation report to meet certain minimum requirements in addition to any form and content requirements set forth by the attestation standard or standards used by the GHG emissions attestation provider, as proposed in 17 CFR 229.1505(c), will provide investors with increased trust and confidence in the GHG emissions data and as such are supportive of these aforementioned requirements. This is particularly important if standards beyond those of the AICPA, IAASB, and PCAOB are permitted.

Disclosure by the registrant about the attestation provider
In situations where the registrant makes use of a PCAOB-registered accounting firm for the GHG emissions attestation engagement, we believe the registrant should not be required to make the additional disclosures proposed by 17 CFR 229.1505(d)(1)-(3)). Given that a PCAOB-registered accounting firm is already complying with stringent requirements for things such as licensure, oversight, and record-keeping and this is well understood by investors, the issuer disclosure would seem unnecessary.

As part of the audit of the financial statements, the audit committee is responsible for selecting and overseeing the auditor and providing a description of their approach to overseeing the auditor in the audit committee report of the proxy statement. We believe it would be appropriate, regardless of whether the attestation provider is a PCAOB registered accounting firm, for the board of directors (or a Board committee) as part of their overall governance responsibilities, to be responsible for selecting and overseeing the GHG emissions attestation provider, akin to the responsibilities of the audit committee in the context of the financial statement and ICFR audits. As this oversight likely would be important to investors and others, we recommend that the SEC consider having registrants disclose these activities as part of their overall governance disclosures.

Regulation S-X proposed amendments

Financial Statement Metrics
We recognize that investors are looking for greater insight into how and where climate-related risks are impacting financial statements, including climate-related estimates and assumptions used to prepare the financial statements and capital expenditures incurred due to climate-related risks. However, we believe the proposed financial statement metric requirement as written could result in numerous practical implementation challenges for issuers and unintended consequences that are described below. Further, we believe the proposed financial statement metrics as written will risk investors not receiving consistent, comparable, decision-useful information and could ultimately detract from the information investors are most interested in. In our experience, investors seem most interested in knowing what underlying estimates and assumptions in the financial statements have been materially impacted by

climate-related matters and what material physical impacts of climate related matters have been accounted for in the financial statements.

Impact and expenditure measurement
While the SEC provided examples, there is still uncertainty in how an issuer would identify certain impacts or measurements (e.g., lost revenue or impacts or expenditures that may include multiple components including climate risk). Consider the following fact patterns:

- A software provider needs to add a new data center to meet customer demand. The cost of a new center is relatively consistent regardless of location chosen. In assessing possible options to locate the center, one factor considered is the physical risk of the geography but that factor alone is not determinative of the ultimate chosen location. Would some or all of the amounts expended for this facility be included in the disclosure? What if the choice was significantly influenced by the physical risk factors? Or if the cost was slightly or significantly different between locations deemed higher/same/lower physical risk? The disclosures recommended may result in significant inconsistency among issuers which may impact its decision usefulness.

- A company is constructing an "environmentally friendly" facility. Certain costs associated with the construction could be the same as those related to constructing a "brown" facility. To comply with the proposed requirements, would the entire cost be assessed against the 1% threshold, or specific items like solar panels and electric vehicle chargers in the parking lot, or a hypothetical difference between the cost of the "environmentally friendly" facility and a "brown" one? How would the hypothetical difference be determined? The proposed rule is essentially requiring "what if" scenarios, which do not have a foundation in financial reporting.

- It may be particularly difficult to determine whether a one percent change in certain line items (e.g., goodwill, deferred taxes) is due exclusively to climate-related matters. If the carrying value of goodwill is reduced because an impairment is recorded, it is because the fair value of the reporting unit is less than the carrying value. It may be difficult to determine which aspects of the decrease in fair value are directly related to climate related risks. Investors may find it more useful to understand how climate related risks were considered in determining the fair value (when applicable) versus the one percent change in that balance that is attributed to a climate related event.

- An oil and gas company has a drilling rig that was damaged in a hurricane. The proposed rules suggest that the lost revenue from the extraction interruption would need to be considered in the 1% analysis. What would actual revenue need to be compared with to determine lost revenue? How would the impact be measured? Would it involve comparison to hypothetical amounts? The proposed rule is essentially requiring "what if" scenarios, which do not have a foundation in financial reporting.

Given the challenges of bifurcating the climate-related impacts and expenditures, a company could unintentionally overstate these metrics or its efforts to mitigate exposure to transition risk.

Disclosure threshold
The CAQ supports the SEC's efforts to promote the disclosure of consistent, comparable, and reliable – and therefore decision-useful – climate-related information to investors. Financial Accounting Concepts No. 8 indicates that in order for financial information to be useful, it must be relevant and faithfully represent what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely, and understandable. Robust disclosure about items of relatively insignificant value in the context of the financial statements taken as a whole could distract from the financial statement impact of other business risks. Consider the following:

- Classifying, characterizing, and presenting information clearly and concisely makes it understandable. The use of a one percent threshold (in relation to the levels of materiality used for the rest of the financial statements, including the statement of cash flows) would place disproportionate prominence on these climate-related financial statement metrics relative to other, perhaps more significant matters presented in the financial statements.

- Further, we note that the one percent is lower than the thresholds typically used in financial reporting today. The one percent thresholds that the rule proposal points to are generally based on larger line items in the financial statements (see footnote 347 of the rule proposal – revenues, total assets, net asset value). Further, as it relates to the financial impact metrics, in certain situations, it will result in disclosure of amounts that are less than one percent of the line item, given the use of absolute values to determine the disclosures.

- Applying any percentage threshold will result in some events or activities being disclosed for a small line item and omitted for a larger line item, and this could ultimately result in disclosures by registrants that are inconsistent and not comparable solely because the value of the various line items within their financial statements differ. Information about a reporting entity is more

useful if it can be compared with similar information about other entities and with similar information about the same entity for another period or another date.

- The one percent threshold, or any percentage threshold could result in the unintended consequence of discouraging disaggregation of financial statement line items. Anecdotally, many registrants disaggregate the face of the financial statements further than what Regulation S-X would mandate in an effort to be transparent for investors and other users.

ICFR considerations
The lower materiality threshold could result in additional information and systems being deemed financially significant for a registrant's internal control over financial reporting. Additionally, the one percent threshold would also require the controls over the financial impact metrics, expenditure metrics and financial estimates and assumptions related to climate-related disclosures to have a level of precision that is different from controls over other accounts and disclosures in the financial statements. Since effective organizational ICFR is based on the entire system functioning, this could be costly to issuers without a corresponding benefit to the quality of financial reporting.

Audit-related considerations
We note that under the proposed rules, PCAOB auditing standards would be applicable to the financial statement metrics that are included in the audited financial statements to the same extent as any other amounts or disclosures. The auditing standards include provisions for establishing materiality lower for certain items that may warrant special attention (which Staff Practice Alert No. 9 indicates could include such items as the impact on meeting a regulatory requirement). As such, there could be a situation where the climate-related metrics are in scope for the audit, but the underlying financial statement line item ordinarily would not because of risk assessment judgements (both qualitative and quantitative) made by the auditor related to the potential likelihood of material misstatement. Auditors may decide to scope in these lower risk accounts, which could create significant inefficiencies and increased audit costs with minimal additional benefits for investors. Additionally, the challenge with the one percent threshold being proposed for disclosure (or potentially any percentage threshold) is that this may likely be at levels well below the materiality for the financial statements as a whole, making the determination of materiality for these items more complex. Under the proposal, most of the items that would be subject to the one percent threshold for disclosure are included within general ledger accounts and financial statement line items subject to materiality for the financial statements as a whole.

Transition considerations
We note that the SEC expects to finalize the requirements in December 2022, less than a month later on January 1, large-accelerated filers would need to have made significant progress in designing and

implementing internal controls around tracking the financial statement line items at an unprecedented level of precision. In addition, assessing operating effectiveness through management testing would likely need to happen almost in parallel with design to enable a company to identify and remediate any deficiencies identified before year end. We are concerned about the practical challenges of establishing effective ICFR in such a short timeframe. Further, the timing also raises questions about the implications for management who is having to prepare the climate-related financial impacts information for comparative periods when no controls were in place. We would recommend that the SEC require the proposed climate-related financial impacts disclosures to be adopted prospectively only. For example, if the first year that disclosure is required is a company's fiscal year 2023 filed in 2024, they would not apply the new requirements to the comparative periods disclosed.

An alternative approach to financial statement disclosure about climate-related risks
Given the various challenges noted above, we do not believe that the proposed changes to Regulation S-X Part 210 are practicable, as written. We offer an alternative approach that, in our view, balances the demand for this information with the costs and consequences of providing it, in a manner that is more consistent with US GAAP and other SEC disclosure requirements.

We believe that it is important for materiality decisions related to the financial statement climate metrics to be made by management, similar to the existing guidance and standards related to the materiality in relation to the financial statements taken as a whole. As discussed in Statement of Financial Accounting Concepts No. 8, "materiality is an entity-specific aspect of relevance based on the nature or magnitude or both of the items to which the information relates in the context of an individual entity's financial report." We believe these same considerations which are mature and well understood by investors should apply to financial statement climate disclosures.

We note that investors have expressed significant interest in understanding the quantitative financial statement impact of climate-related estimates and assumptions, and capital expenditures. We believe the SEC could take an approach more in line with the existing focus on critical accounting policies and practices and critical accounting estimates. In our view, providing additional guidance on climate-related risks and opportunities in the context of these well-understood disclosures and encouraging greater transparency when such estimates (including their inputs and significant assumptions) are materially affected by climate-related risks would provide decision-useful information to investors. In addition, controls and processes around these disclosures are well established, and could more easily be tailored to collect information and monitor the impact of climate on these critical areas of financial reporting. Further, it would encourage companies to take a more holistic approach to the disclosure of climate impact – identifying key disclosures in the Form 10-K and financial statements using the existing

framework of critical accounting policies and practices and critical accounting estimates, complemented by the proposed requirements to enhance Regulation S-K with respect to climate.

Convergence with international standards

The proposed rule seeks comment on whether the SEC should allow all issuers, including FPIs to use disclosure pursuant to the ISSB's standard on climate disclosure once finalized as alternative reporting under the SEC's proposed rule. We encourage the Commission to continue to actively engage in dialogue about convergence of ESG standards, including in its role as co-chair of the International Organization of Securities Commissions Technical Expert Group. International coordination on disclosure standards will be especially important as disclosure regimes develop around the globe, which could result in companies with global operations being required to follow local requirements in several different jurisdictions.

The CAQ has long been of the view that a globally accepted ESG reporting system should be built from existing standards and frameworks that can be adapted to the needs of investors in different jurisdictions. Accordingly, we believe allowing the use of IFRS Sustainability Disclosure Standards as alternative reporting to satisfy SEC issuer climate reporting obligations could be a mechanism for enhancing global comparability for investors. Allowing the use of ISSB standards could help reduce the need to report in accordance with multiple standards or requirements. Since the ISSB standards are currently in development, it will be important for the SEC to monitor and evaluate the final ISSB standards to determine whether they are appropriate for use in context of the SEC requirements. If they are deemed appropriate, the SEC could issue guidance similar to what exists for FPIs using IFRS, to identify which parts of the proposed rule would be satisfied through application of the ISSB standards.

Compliance Date

Phased in effective dates

The preparation for and implementation of the requirements in the proposed rule will take time for registrants, auditors, and others to prepare in a way that will support the disclosure of high-quality information that is decision useful. Certain aspects of the disclosure requirements will take more time than others, and as such we are supportive of a phased in approach to the effective dates. When regulation of this magnitude has previously been issued, such as that required by the Sarbanes Oxley Act, as well as major accounting standards like Revenue Recognition, Leases and Credit Losses, registrant readiness has been evaluated and where necessary extensions to compliance dates have been

provided after adoption of the final rules.[8] It will be very important for the SEC to monitor progress by registrants to evaluate whether they will be ready in time to meet the proposed compliance dates and take action as necessary.

We have observed a modest increase in climate-related disclosure by companies in their Forms 10-K.[9] However, there are still very few companies that include GHG emissions in their Forms 10-K.[10] For those companies that do disclose GHG emissions outside of their Forms 10-K, the timing of that disclosure is typically a few months after the 10-K has been filed. As a result, we recommend that the Commission consider additional potential phase in approaches, including that requirements be phased in by both disclosure area and registrant type, with certain disclosure areas such as the proposed GHG emissions and proposed Regulation S-X disclosures having a longer phase in period. For example, subject to input the SEC receives directly from preparers, the Commission could consider whether to make the proposed S-K requirements (excluding GHG emissions and related attestation) effective in the first phase, followed by the proposed GHG emissions disclosures and related limited assurance and S-X requirements in the second phase, and reasonable assurance requirements for GHG emissions disclosures in the third phase. The base year would be the first year that certain of the requirements would be effective. The table below illustrates an alternative approach that would further phase in the requirements by disclosure area and registrant type:

Disclosure Requirement	**Filer Type**	**Compliance Date**
Proposed S-K disclosures (**excluding GHG emissions**)	Large-accelerated filers	Base year
Proposed GHG emissions disclosures and related limited assurance (as applicable)	Large-accelerated filers	Base year plus one year
Proposed S-X disclosures	Large-accelerated filers	Base year plus one year

[8] For example: Revenue Recognition was released in 2014 with an original effective date in 2016 for all public companies that was later delayed by one year (see ASU 2014-09, ASU 2015-14, ASU 202-05). Leases was released in 2016 with an original effective date in 2018 for public companies that was later delayed twice for private companies (See ASU 2016-02, ASU 2019-10, and ASU 2020-05). CECL was released in 2016 with an original effective date in 2019 for public companies and 2020 for private companies and was later delayed for smaller reporting companies and private companies (see ASU 2016-13, ASU 2019-10, and ASU 2020-02).

[9] According to an analysis conducted by the CAQ, approximately 91% of S&P 500 companies mentioned climate-change in their 2021 form 10-K, compared to approximately 76% of S&P 500 companies in their 2020 form 10-Ks.

[10] According to an analysis conducted by the CAQ, we observed roughly 102 of S&P 500 companies mention scope 1, scope 2, and/or scope 3 GHG emissions status, objectives and/or targets in their 2021 form 10-K.

Disclosure Requirement	Filer Type	Compliance Date
Reasonable assurance on GHG emissions (as applicable)	Large-accelerated filers	Base year plus three years
Proposed S-K disclosures (**excluding GHG emissions**)	Accelerated filers and non-accelerated filers	Base year plus one year
Proposed GHG emissions disclosures and related limited assurance (as applicable)	Accelerated filers	Base year plus two years
Proposed S-X disclosures	Accelerated filers, non-accelerated filers, and smaller reporting companies	Base year plus two years
Reasonable assurance on GHG emissions (as applicable)	Accelerated filers	Base year plus four years
Proposed S-K disclosures (**excluding GHG emissions**)	Smaller reporting companies	Base year plus two years
Proposed GHG emissions disclosures	Non-accelerated filers and smaller reporting companies	Base year plus two years

Prospective adoption of the requirements

The proposed rule would require the climate-related regulation S-X disclosures be provided for the registrant's most recently completed fiscal year, and for the historical years included in the consolidated financial statements in the filing. The release states a registrant, however, would not need to provide a corresponding historical metric for a fiscal year preceding its current reporting fiscal year if it is eligible to take advantage of the accommodation in 17 CFR 230.409 ("Rule 409") or 17 CFR 240.12b-21 ("Rule 12b-21"). For example, if a registrant has not previously presented a metric for a fiscal year and the historical information necessary to calculate or estimate the metric is not reasonably available to the registrant without unreasonable effort or expense, the registrant may be able to rely on Rule 409 or Rule 12b-21 to exclude a corresponding historical metric. We believe that it is not clear when a registrant could take advantage of the accommodation, and instead recommend the S-X requirements in the proposed rule be applied prospectively (i.e., in the year of adoption a registrant would not be required to provide disclosures for the historical periods included in the filing).

The proposed rule would require GHG emissions disclosures for a registrant's most recent fiscal year and for the historical years included in its consolidated financial statements in the filing, to the extent such historical GHG emissions data is reasonably available. We do not believe that it is sufficiently clear when a registrant could conclude that historical GHG emissions data is not reasonably available. As such, we recommend that the proposed GHG emissions disclosure requirements be adopted prospectively (i.e., in

the year of adoption a registrant would not be required to provide disclosures for the historical periods included in the filing).

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The CAQ appreciates the opportunity to comment on the proposed rule and would be pleased to discuss our comments or answer any questions that the Staff or the SEC may have regarding the views expressed in this letter. Please address questions to Dennis McGowan ([redacted]) or Desiré Carroll ([redacted]).

Sincerely,

Dennis J. McGowan
Vice President, Professional Practice
Center for Audit Quality

cc:

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Honorable Gary Gensler, Chair
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