The Future of
Environmental Solutions

# Answers to Your Questions on Climate-Related Disclosures

**In case you missed it, in mid-June 2024, Montrose led a webinar discussing the rapidly changing world of climate-related disclosures. You can access that webinar here.**

Over the course of the webinar, and in discussion with Montrose clients, many questions have been raised about the various climate-related disclosure rules, including:

- The US Securities and Exchange Commission's (SEC's) climate rules,
- The State of California's Senate Bill (SB) 253 and SB 261, and
- The EU's Corporate Sustainability Reporting Directive (CSRD) and the underlying European Sustainability Reporting Standard (ESRS) E1: Climate Change.

In order to help organizations better navigate these requirements, we created this document that compiles both frequently asked questions as well as specific questions asked during the webinar. Have a question that is not answered in this document? Please reach out to us directly here.

## QUESTIONS & ANSWERS

### My company is small and our greenhouse gas (GHG) emissions are insignificant. Do these rules still apply to us?

Yes. These rules are unique in that the triggers for applicability are not based on the amount of expected emissions. Specifically:

- The SEC rules apply to all public companies subject to SEC financial disclosure requirements. The requirements vary based on filing status, and some filers are exempt from some requirements. For example, non-accelerated filers (NAFs), smaller reporting companies (SRCs) and emerging growth companies (EGCs) are not required to disclose GHG emissions; these filers are only required to make the climate-related risk and financial disclosures. You can find more information about the requirements by filing status in our blog, here.
- The California rules apply to companies that do business in California and meet certain revenue thresholds: $1 billion for SB 253 and $500 million for SB 261. You can find more information about the California rules in our blog, here.
- The EU CSRD triggers are based on listing status (i.e., being listed on an EU-regulated market), net turnover (revenue), balance sheet, and employee count. You can find more information about the various phases and triggers for CSRD in our blog, here.

## We are a privately held company. These rules only apply to publicly traded companies, right?

Wrong. While the SEC climate rules only apply to companies publicly traded in the US, the California rules apply to public and private companies alike. A privately held company that generates revenue in the EU may also be subject to CSRD, depending on the amount of revenue and other factors as described in our blog, here.

## What if my company is private but we plan on becoming a publicly traded company in the near future. How does our requirement timeline change?

As the rules currently stand, private companies must comply with California's SB 253 and SB 261, and the reporting requirements would not change when you shift from private to public.

For the SEC rules, you will be subject to the rules once you become public and will need to include climate-related information in your SEC disclosures according to the rule schedule (see summary table in our blog, here). It is strongly recommended that companies get started on GHG emissions calculations and climate risk assessments now; these processes take time, and – in this case – waiting until you go public is not likely to allow enough time for compliance (at least according to the current rule schedule, depending on your filing status).

## Do these reporting standards also specify the decarbonization progress a company will make? Are decarbonization performance requirements specified in these standards?

No. These rules and requirements are focused on disclosure, not performance. In other words, they do not require a certain reduction in GHG emissions or even that you set GHG emissions reduction targets. There are no performance standards.

However, the SEC climate rule notes that if certain things are in place, they must be disclosed. In this case, if a company had set GHG reduction targets, it would have to disclose those targets and their progress towards meeting them.

## My company does not have any offices or other assets in California. Does that mean that SB 253/SB 261 will not apply to us?

It does not. Companies can fall under the scope of the California rules simply by doing business in California, even if they do not have offices, plants, or people based in the state. For example, a company based only in New York that sells into the California market can be considered to be doing business in California.

### What is the definition of 'doing business in California'? Are there certain thresholds that apply?

At the moment, there are no 'official' thresholds for defining what doing business in California means as it relates to these rules. We anticipate that the implementing regulations that the California Air Resources Board (CARB) develops will provide a more clear definition.

That said, across the State of California, different state agencies currently define 'doing business in California' slightly differently.

- Some definitions are very broad. For example, the California Corporations Code notes that a company does business in California by 'entering into repeated and successive transactions of its business in the state, other than interstate or foreign commerce'.
- A more restrictive definition comes from the California Franchise Tax Board, which provides thresholds for California sales ($711,538), California property ($71,154) and California payroll ($71,154), and you only need to exceed one of these to be considered as doing business in the state.

While we must wait for CARB's implementing regulations before we know for sure how 'doing business in California' will be defined, companies can look to these existing definitions to start to understand whether they will be subject to the requirements of SB 253/SB 261.

### What is the extent of Scope 3 emissions disclosures by California's SB 253?

California's SB 253 requires that companies subject to the bill report Scope 3 emissions in accordance with the GHG Protocol's accounting and reporting standards. Specifically:

> A reporting entity shall, beginning in 2026, measure and report its emissions of greenhouse gases in conformance with the Greenhouse Gas Protocol standards and guidance, including the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard and the Greenhouse Gas Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard developed by the World Resources Institute (WRI) and the World Business Council for Sustainable Development (WBCSD), including guidance for scope 3 emissions calculations that detail acceptable use of both primary and secondary data sources, including the use of industry average data, proxy data, and other generic data in its scope 3 emissions calculations.

Categories of Scope 3 emissions that must be reported will depend on the materiality of those emissions sources to an individual reporter/company.

### Is measuring Scope 3 emissions double counting? Are my Scope 3 emissions my customers' Scope 1 emissions?

Yes and no. It is true, your Scope 3 emissions may include, for example, the Scope 1 emissions of your suppliers and other parties along your value chain. However, that is by design. Furthermore, that is already the case with Scope 2 emissions – that is, your Scope 2 emissions are the Scope 1 emissions of your utility provider.

It is important to understand, the intent is not for Scope 1 + Scope 2 + Scope 3 = global emissions. If it was, then yes – this would be double counting.

Instead, the intent is to understand how each company **influences** emissions outside of its direct emissions. So, think of your Scope 2 and Scope 3 emissions as **indicators** of how your company is driving the emissions of others (through your electricity demand, your need for raw materials, the transport of your products to the market, etc.). By taking actions to reduce your Scope 2 and Scope 3 emissions, you are playing your part in helping drive down the Scope 1 emissions of others (i.e., by reducing demand).

### There are some requirements that require all stages of the supply chain to disclose emissions in accordance with the GHG Protocol's standards and guidance. What happens in this case, given that there are usually several parties along the supply chain?

This is correct – the State of California bills and EU CSRD require disclosure of Scope 3 emissions, which include emissions from a company's supply chain. This can seem daunting, but it is important to keep in mind that this is an iterative process. In calculating your Scope 3 emissions, you can start with the data that you have and then gradually increase the quality of that data over time.

For example, related to Category 1 – Purchased goods and services: to start, a company might identify its most significant suppliers (e.g., by spend) and then use publicly available information to estimate GHG emissions based on spend. Over time, a company can begin to work directly with its most significant suppliers to help them calculate their Scope 1 emissions, and then leverage that data in place of spend data.

### How can I make sure I'm following the requirements for all standards? Should I focus on CSRD requirements since the rules are so stringent?

It is true, the EU's CSRD is the most stringent set of requirements (noting that it covers not only climate, but also other ESG factors). The ESRS E1 (still in draft) spells out the climate-related reporting requirements, largely aligned with the International Sustainability Standards Board's (ISSB's) International Financial Reporting Standard (IFRS) S2. Recall from Part 3 of our blog series that the Taskforce on Climate-Related Financial Disclosures (TCFD) has been disbanded, ISSB is now overseeing the TCFD final recommendations, and these recommendations have been rolled into IFRS S2. Therefore, using ESRS E1 as your set of requirements (that is, the 'what' that you need to disclose) is the best place to start if you are subject to CSRD.

The current versions of the SEC and California rules are also based on TCFD, so again – ESRS E1 should get you close to compliance with the US-based requirements as well. However, there will be some nuances to be aware of – most notably in regards to the 'how' around your disclosures. The SEC rule requires information to be disclosed as part of financial reporting, the California rules require information to be disclosed on your website (SB 261) and via a yet-to-be-developed digital platform (SB 253).

And finally, for all of the schemes noted above, the GHG Protocol establishes the methodology for the GHG emissions calculations.

### How many companies have you worked with are not monitoring their Scope 1 and 2 data? What advice do you give these clients to help them start?

The companies that my team have supported run the full spectrum. At this very moment, we are working with clients on their very first Scope 1 and 2 GHG inventory as well as with clients who have been disclosing Scope 1, Scope 2, and Scope 3 for years. On average, the majority of the clients we work with have disclosed at least Scope 1 emissions.

Our advice to those who have not started yet: calculating your Scope 1 and Scope 2 GHG emissions for your most recently completed calendar year is a great first step. This process helps companies get their arms around their assets and their emissions sources, identify and engage with key data owners, and build climate awareness and literacy in the organization. The methodology is standardized (via the GHG Protocol's standards and guidance), and even in the unlikely situation that none of these rules come to pass (or apply to you), this emissions data can still provide value to your key stakeholders. (They may not be asking for it now, but it is likely that those expectations are coming.)

It is worth noting - many companies also find additional business value in the Scope 1 and Scope 2 GHG inventory process. For some, it is the first time a company has compiled a comprehensive list of all of its assets (buildings, vehicles, etc.); for others, this process uncovers financial savings opportunities (e.g., one client recently discovered they were still paying for electricity at a building it no longer owned or occupied).

There is not much to lose in undertaking your first Scope 1 and Scope 2 inventory – and remember, just because you do the inventory does not mean that you have to report it publicly...in particular while the SEC and California rules have not yet been implemented. Now is your chance to prepare and get started.

## How can we effectively calculate emissions for our employees who work remotely?

While currently there are no definitive 'rules', companies may account for the amount of energy used (e.g., kWh of gas, electricity consumed) from remote working (or 'teleworking') in their calculations of Scope 3, Category 7 (Employee Commuting) emissions. As noted in the current version of the GHG Protocol's Corporate Value Chain (Scope 3) Accounting and Reporting Standard:

> Companies may *optionally* calculate the emissions of teleworking from home. To calculate these emissions, a baseline emissions scenario should first be established. Baseline emissions occur regardless of whether or not the employee was at home (e.g., energy consumed by the refrigerator). The reporting company should only account for the additional emissions resulting from working from home, for example the electricity usage as a result of running the air conditioner to stay cool.

This white paper is also often referred to, which complements the GHG Protocol's guidance. This methodology is used by the UK government, and most businesses calculating homeworking emissions use a version of this.

For the US, this involves assigning each full-time equivalent (FTE) employee to a specific subregion to estimate the amount of energy consumed and applying a subregion-specific emission factor. At this point, my understanding is that we only have FTE, and do not have those employees tied to specific regions, potentially making this a substantial undertaking.

## How difficult is it for companies to calculate their process and/or fugitive emissions when building a GHG inventory for the first time?

As always, the answer is it depends. However, most companies approach this as a mass balance equation. For example, the amount of refrigerant added to HVAC systems over the course of the year is equal to the amount of refrigerant emitted.

When it comes to process emissions, this approach may not always work. In some cases, companies may choose to directly measure GHG emissions. For example, we are seeing a move towards this direct measurement in the oil and gas industry; you can read more about that in our blog series on the Oil and Gas Methane Partnership (OGMP) 2.0.

### We have to report some emissions due to the BERDO ordinance in Boston but I'd love to hear recommendations for reporting and sharing our emissions with the public.

For those companies who are already calculating and reporting greenhouse gas (GHG) emissions due to local or other requirements, there are a few options for reporting those emissions to the public.

1. Companies may consider directly posting their regulatory reporting submissions on their website for public consumption. While this route requires the least amount of effort, these regulatory reporting mechanisms do not include much context setting and therefore may be of little value to your stakeholders. Without this context, there is also risk that your emissions profile will be misinterpreted.
2. For those companies that already publish a sustainability or ESG report, this is a great place to include GHG emissions data (as well as climate risk information). Beyond disclosing the data, companies should be transparent about the 'context' in which that data sits – what are the emissions sources, are emissions increasing or decreasing, what is the company's plan to address emissions (e.g., set targets? decarbonization plan?), etc. If your company does not already publish a sustainability report and has no near-term plans to do so, you can also consider publishing a brief, standalone climate report to post on your website.
3. Reporting GHG emissions via CDP is also an option to consider. Data reported via CDP feeds several other schemes. Not responding to CDP is an option, but in doing so you lose the chance to tell your own story. Companies often provide a link to their CDP submission on their website (or take steps to ensure it is publicly available via the CDP website).

It is not recommended that GHG emissions data only be published on a webpage (e.g., the sustainability page of a company website). Web pages are continually undergoing updates and changes, and therefore it is difficult to preserve the integrity of the data set if not established via a separate, controlled document. It IS recommended that any public disclosure be reviewed by your legal counsel prior to publishing.

Lastly, specific to BERDO, keep in mind that this only captures building-related emissions and excludes some Scope 1 emissions categories (e.g., emissions from vehicle fleets and refrigerants).

### Where do corporate buyers report their environmental claims when they purchase from carbon offsets on the VCM market? Is this publicly available what projects buyers/investors support?

The Biden administration has a policy statement, [Voluntary Carbon Markets Joint Policy Statement and Principles (whitehouse.gov)](), that addresses these questions. Some key highlights:

- Activities that generate credits and the credits themselves should be certified to a robust standard for activity design and measurement, monitoring, reporting and verification (MMRV) of emission reductions or removals, applying procedures that deliver on core integrity principles.
- Disclosure of purchased, cancelled, or retired credits should be made on at least an annual basis and include details that enable outside observers and relevant stakeholders to assess whether purchased and retired credits are of high integrity and avoid negative environmental and social impacts.
- Credit users should determine the optimal format in which to publish information about purchased and retired credits in light of evolving practices while seeking to disclose information in a standardized manner that enables comparability across credit users. Regardless of format, such information should be made easily accessible to stakeholders, such as in a regular publication. Credit users should consider reporting to resources that aggregate and publicly disseminate this information.

It is important to note, the SEC also requires filers to disclose the use of carbon offsets or Renewable Energy Certificates (RECs) if they are a material component of a filer's plan to achieve its climate targets. In these cases, filers must disclose the aggregate amount expensed, the aggregate amount of capitalized carbon offsets and RECs recognized, and the aggregate losses incurred on the capitalized carbon offsets and RECs. These disclosures are to be included in the footnotes of financial statements.

### What is your take on the status of the SEC and State of California regulations vs. the legal challenges that are rising against these regulations?

Of course, no one has a crystal ball to see into the future and know what will happen with these rules. However, there are a few things that we know to be true:

- The SEC has vowed to keep pressing to implement their climate rules. Currently, the SEC has until August 5, 2024, to respond to the climate rule challengers' briefs in court.
- The State of California bills have already passed; they are only waiting for implementation. They are not on hold the way that the SEC climate rules are. And while it appears that CARB will not start the rulemaking process until 2025, this likely only means a delay in the requirements – we do not anticipate that the requirements will go away.
- Looking more broadly across the globe, the writing is on the wall – increased requirements to publicly disclose climate-related impacts and risks are on the rise. It is only a matter of time before these requirements come to US companies (and of course, the EU CSRD already applies to many US companies).
- Regulations aside, pressure for more transparency on climate impact and risk – from investors, customers, consumers, and other stakeholders – is also on the rise and is likely to drive action even without regulations underpinning their expectations.

TL;DR: Climate disclosure expectations and requirements are coming; now is the time to get prepared.

### Are there any updates expected on these disclosure requirements? If so, what is the best way to stay informed regarding any upcoming updates?

As for how to stay informed of future updates, this might sound simple but…keep an eye out on LinkedIn. These are hot topics, and whenever any action is taken there is sure to be a flurry of posts about it. (Feel free to reach out and connect with me, as I am planning to post re: any updates that I come across.) Your legal department is also likely keeping tabs on this, and may even subscribe to digital platforms that provide alerts and summaries when new rules and regulations are published.

Montrose will also keep our climate-related disclosures webpage up-to-date as we learn more. And of course, if you have questions in the meantime, you can reach out to us here.

If you have any additional questions, reach out to speak to a trusted advisor. We pride ourselves on meeting our clients where they are and on teaching our clients along the way, rather than simply doing.

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