Blogs
April 04, 2022
Public Chatter

The SEC's Climate Proposal: Disclosing Carbon Offsets

Digging further into the **SEC's proposing release for climate disclosure**, the SEC's proposal would elicit disclosure about carbon offsets – for those companies that engage in that sort of thing. For some companies, carbon offsets and renewable energy credits or certificates (known as "RECs" and defined by the SEC consistent with how the EPA defines it) play a role in their climate-related business strategy.

The Difference Between Carbon Offsets and RECs Most securities lawyers don't know the difference between a "carbon offset" and a "REC." The SEC provides an explanation in footnote 237 on page 77 as: - A company may purchase carbon offsets to address its direct and indirect GHG emissions (i.e., its Scopes 1, 2, and 3 emissions) by verifying global emissions reductions at additional, external projects. The reduction in GHG emissions from one place ("offset project") can be used to "offset" the emissions taking place somewhere else (at the company's operations). - A company may purchase a REC in renewable electricity markets solely to address its indirect GHG emissions associated with purchased electricity (i.e., Scope 2 emissions) by verifying the use of zero- or low-emissions renewable sources of electricity. Each REC provides its owner exclusive rights to the attributes of one megawatt-hour of renewable electricity whether that renewable electricity has been installed on the company's facilities or produced elsewhere.

The Disclosure Requirements As noted on page 77 of the proposing release, companies would be required to disclose, under proposed Item 1502(c) of Regulation S-K, the role that carbon offsets or RECs play in the company's climate-related business strategy. Given the sensitivity of how much carbon offsets and RECs cost over time, the SEC believes those companies using them should address the risk of higher costs over time in their disclosures. The SEC also notes that the value of an offset may decrease substantially and suddenly – and provides the example of an offset representing protected forest land that burns in a wildfire and no longer represents a reduction in GHG emissions and the company needs to replace that offset with something that now costs more. That's another type of disclosable risk. There also are regulatory risks in addition to market risks when it comes to carbon offsets and RECs. A change in a regulation could impact the cost – or even the availability – of certain types of carbon offsets and RECs. In addition to risk disclosure, under the proposal, companies would make disclosures about their carbon offsets and RECs when they address their targets and goals disclosures. That disclosure would cover the extent to which a company relies on offsets and RECs to meet target and goal commitments and their progress over time in meeting those commitments. This type of disclosure would also include a description of the carbon offset or REC, including any registries or authentication of the offset or RECs, and the cost. We will cover this more in detail in our blog about setting climate goals, targets and pledges. Carbon offsets and RECs are addressed in the proposed rules in other contexts too. For example, for each type of Scope – 1, 2, 3 – companies would be required to disclose the emissions disaggregated by each constituent greenhouse gas, and in the aggregate. This greenhouse gas emissions data would be disclosed in gross terms, *excluding* any use of carbon offsets.

What Will Sunlight Do to the Future of Carbon Offsets? Some investors increasingly are vocal that they don't believe carbon offsets should be considered a valid climate strategy. It is possible that this is another area – like internal carbon pricing (see **this blog**) where sunlight on a company's practices might be a disincentive to continue engaging in those practices.

Here are our other blogs about the SEC's climate proposal so far: 1. **SEC Proposes Climate Disclosure Rules: 9 Things to Know** 2. **"How Much Is This Gonna Cost Us?" The SEC's Climate Economic Analysis** 3. **The**

SEC's Climate Proposal: Where Did We Wind Up With "Materiality"? 4. **The SEC's Climate Proposal: When Should Scope 3 Emissions Be Considered "Material"?** 5. **The SEC's Climate Proposal: Assessing "Physical Risks"** 6. **The SEC's Climate Proposal: Assessing "Transition Risks"** 7. **In-House Corner: Climate Disclosure Bracketology"**

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