What Companies Need to Know About New ESG Disclosure Requirements

Environmental, Social and Governance (ESG) reporting requirements are now being standardized as government bodies in the U.S. and Europe have begun to implement a range of requirements for both private and public companies.

The Securities and Exchange Commission (SEC) recently adopted a new rule requiring greater standardization in ESG reporting for SEC registered foreign and domestic entities. California passed the California Climate Accountability Package, which will require all public and private entities doing business in the state with revenues in excess of $1 billion to adhere to new reporting requirements for Scope 1 (direct greenhouse emissions) and Scope 2 (indirect greenhouse emissions) emissions starting in 2026 and Scope 3 (indirect upstream and downstream greenhouse emissions) emissions starting in 2027. Part of that effort will also require companies with $500 million-plus in annual revenues to submit climate-related financial risk reports to the state every other year. The European Union (EU) adopted its own Corporate Sustainability Reporting Directive last summer that will require ESG reporting as early as this year.

Comparison of Recent ESG Disclosure Requirements

SEC	California		EU
Climate-Related Disclosures Requires SEC-registered entities to assess climate-related risks and include corresponding disclosures within their registration statements.	**California Climate Accountability Package** Requires companies doing business in California to disclose their greenhouse gas emissions and climate-related financial risks.		**Corporate Sustainability Reporting Directive (CSRD)** Requires EU businesses to publish regular reports on the social and environmental risks they face, and on how their activities impact people and the environment.
	SB 253 Climate Corporate Data Accountability Act	**SB 261** Greenhouse Gasses: Climate-Change Related Financial Risk	
Requirements Disclosure of climate-related information in registration statements, including material climate-related risks, activities to mitigate or adapt to such risk, oversight of these risks and Scope 1 and Scope 2 greenhouse gas emissions.	**Requirements** Disclosure of greenhouse gas emission data, as well as obtaining third-party assurance of disclosures.	**Requirements** Disclosure of climate-related financial risks and measures adopted to reduce and adapt to those risks. Reports must follow the Task force on Climate-related Financial Disclosures (TCFD) framework.	**Requirements** Disclosure of applicable information for each of the 12 European Sustainability Reporting Standards (ESRS). Reporting must be conducted utilizing a "double materiality" approach assessing both Impact and Financial materiality.
Who's Affected All SEC registered companies.	**Who's Affected** All public and private business entities with annual revenues greater than $1B that do business in CA.	**Who's Affected** All public and private businesses entities with annual revenues greater than $500M that do business in CA.	**Who's Affected** All companies listed on an EU-regulated market and additional large*, non-listed companies, subsidiaries of listed parents and additional non-EU companies if any entity within the organization falls within the scope of requirements.
Timeline Reporting will begin in 2026 for FY2025.	**Timeline** Annual reporting of Scope 1 emissions and Scope 2 emissions will begin in 2026. Reporting of Scope 3 emissions will start in 2027.	**Timeline** Reporting will begin on or before January 1, 2026 and biennially thereafter.	**Timeline** Reporting will be phased in, beginning in 2025 for FY2024. The timeline for reporting will vary based on the individual company.
Learn More SEC Final Rule: The Enhancement and Standardization of Climate-Related Disclosures for Investors	Learn More CA Senate Bill No. 253	Learn More CA Senate Bill No. 261	Learn More EU Corporate Sustainability Reporting

* Large defined as meeting at least two of the following: (1) asset balance greater than 20 million euros, (2) net revenue balance greater than 40 million euros, or (3) average number employees above 250.

Before these latest standards were adopted, ESG reporting was entirely voluntary. The real estate industry has been proactive on this front, with the National Association of Real Estate Investment Trusts (Nareit) reporting that nearly all U.S. REITs reported ESG metrics as of 2022 and 83% also reported overall sustainability goals.

However, until now, metrics collected varied from company to company and have done little to illuminate the true impact that ESG has across industries.

For instance, Nareit groups its reporting frameworks into two categories: Voluntary Disclosures, which provide mechanisms for ESG disclosures that are applicable to organizations across different industry sectors and regions, and Guidance Frameworks, which provide specific topics, methodologies and metrics for companies to use in reporting on their ESG performance.

Many REITs rely on the same Voluntary Disclosure Framework, the Global Real Estate Sustainability Benchmark, which provides some standardization among reporting. Other industries have similar frameworks in place.

These new rules could have significant financial implications for the companies affected, with the SEC update impacting the most companies in the REIT universe. According to a recent study conducted by Environmental Resource Management's SustainAbility Institute, the average corporation currently spends about $677,000 every year on reporting on sustainability and other ESG-related concerns.

> *"These final rules build on past requirements by mandating material climate risk disclosures by public companies and in public offerings," SEC Chair Gary Gensler said in a statement. "The rules will provide investors with consistent, comparable, and decision-useful information, and issuers with clear reporting requirements."*

poor execution against their stated goals, contradicting previous reporting.

Efforts like switching to energy efficient LED lighting, establishing emissions reduction goals and enforcing good corporate governance are all valuable, but these alone will not be enough to eliminate risk under the new reporting requirements. Given the challenges in implementation, the loose reporting structure that has been in place could potentially drive some material litigation across industries in the years ahead.

New Risks to Consider

These new rules from the SEC and others will have a direct impact on a wide range of companies, with risks that trickle down to their Directors and Officers (D&O) liability insurance coverage.

First, consider the alignment between the disclosures that were being reported under the voluntary framework and those that will be reported with new, required standards. In some cases, this new oversight could expose potential errors and omissions in data being reported up until this point. The same holds true for companies reporting

Next Steps to Take

The focus for companies that want to avoid potential litigation should be on understanding the timeline for implementation of these new rules and the metrics that now need to be reported. From there, it is a matter of collecting data and verifying reliability and accuracy for the purpose of ESG reporting.

Take the first step now. Consult with your underwriter, broker and external advisors to determine which of these new disclosure rules will impact you and learn more about what you can do to best prepare you and your company.

Arch is the endorsed primary carrier for the National Association of Real Estate Investment Trusts' (Nareit) Directors and Officers Liability (D&O) program, which offers Nareit members market-leading, broad REIT-specific coverage. The Nareit D&O program is anchored by Arch's expertise and extensive resources, Nareit, and Alliant Insurance Services, which serves as the exclusive program administrator.

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