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Issuers On Notice For Climate Risks.

Municipal issuers who've yet to make a habit of disclosing material climate-related risks may be at risk of violating the Securities and Exchange Commission's antifraud provisions, following the rollout of its newly updated climate rule last week.

The SEC's new climate rules, reviled by many on both sides of the aisle for either doing too much or not doing enough, represent a compromise from the original 2022 proposal and drops that initial provision requiring corporate issuers to disclose emissions from supply chains. Now, registered companies are on the hook for reporting emissions from their operations and energy purchases, or Stage 1 and Stage 2, respectively.

The rule does not directly touch the municipal bond market but some have long feared that this model will eventually be applied to the muni market, either directly or through enforcement and could eventually see Rule 15c2-12 (which lays out specific material events that need to be disclosed) include climate risk events.

"The regulation assumes that investors want more robust and consistent information to assess climate-related risks to make informed investment decisions and price securities," wrote Lisa Washburn, chief credit officer at Municipal Market Analytics. "This may render such climate-related information 'material' under its definition for purposes of the antifraud law."

"Municipal participants should expect that, over time, many of the disclosures outlined in the new rule will be expected from municipal issuers too," Washburn added, expecting that climate related enforcement will follow in the footsteps of issues such as the disclosure of bank loans and enforcement related to MCDC as the Commission's new enforcement strategy du jour.

"Given the keen interest in addressing climate-related disclosure gaps and the rising effects of both acute and chronic climate perils, MMA expects that one of the enforcement approaches is likely to be its first course of action," Washburn wrote.

The disclosures the SEC generally expects from corporate issuers can generally be put into such buckets as the disclosure of climate-related risks and impact on business strategy, financial condition and outlook; governance and risk management of climate-related risks, mitigation and adaptation strategies; scope 1 and scope 2 greenhouse gas emissions; climate goals or targets and the related impact on expenditures; financial impacts from severe weather events or the use of carbon offsets.

The rule also states that the Commission will provide a safe harbor that all information, except for historical fact, will be treated as forward looking.

MMA recommends that municipal issuers begin disclosing information on climate-related risks that have a material impact on finance or operations, a discussion of mitigation or adaptation efforts and related material costs, as well as if and how climate-related risks are identified, assessed and managed.

But there is a chance that the final rules will never be rolled out as proposed. A coalition of states including West Virginia, Georgia, Alabama, Alaska, Indiana, New Hampshire, Oklahoma, South Carolina, Wyoming and Virginia have already sued the Commission, in hopes of showing that the final rule “exceeds the agency’s statutory authority and otherwise is arbitrary, capricious, an abuse of discretion and not in accordance with the law,” the lawsuit said.

“Although not directly applicable, it is an exemplar potentially in our sector,” said Chuck Samuels, member at Mintz Levin and counsel to the National Association of Health & Educational Facilities Finance Authorities. “It’s considerably less burdensome than as proposed. But, there is a substantial possibility this will never be effective between court challenges, the Congressional Review Act, and possible change in Administrations.”

The rule will become effective sixty days after publication in the federal register and compliance dates differ depending on the size of the firm, with the earliest date for large accelerated filers beginning in 2025.

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