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June 16, 2022

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: The Enhancement and Standardization of Climate-Related Disclosures for Investors (File No. S7-10-22)

Dear Ms. Countryman:

Americans for Tax Reform (ATR) appreciates the opportunity to comment on the Securities and Exchange Commission's (SEC) proposed rule entitled, *The Enhancement and Standardization of Climate-Related Disclosures for Investors* (Proposal).

ATR is a 501(c)(4) nonprofit, taxpayer advocacy organization that opposes all tax increases and supports limited government regulation.

As drafted, ATR strongly opposes the provisions outlined in the Proposal. If the SEC adopts the Proposal as a final rule, future litigation will likely determine that it is arbitrary and capricious under the Administrative Procedure Act.

Initial Thoughts

Congress has not directed the SEC to pursue the provisions outlined in the Proposal. Climate-related risks and disclosure of greenhouse gas (GHG) emissions are overly prescriptive and deviate from the SEC's traditional principles-based disclosure regime. To move forward with the Proposal without proper statutory authorization from Congress would violate the provisions of the Administrative Procedure Act.

The Proposal's amendments to rules under the Securities Act of 1933 and the Securities Exchange Act of 1934 would drastically degrade federal securities regulation in the United States. Most notably, the requirement for disclosure of Scope 3 emissions will force public companies, including financial institutions, to reallocate capital to companies that are favored by the current administration, or limit exposure to companies disfavored by the current administration. This behavior is eerily similar to Operation Choke Point, an example of government intervention at its worst.

The Proposal signals a disturbing degradation of the independent nature of the SEC. The SEC is bowing to the political preferences of the White House and activist and institutional investors. Instead of drafting rules as required by Congressional authorization, the SEC is acting unilaterally and circumventing the rule of law. The SEC's decision to move forward with the Proposal epitomizes the burgeoning power of the administrative state.

The gargantuan compliance costs to carry out the requirements in the Proposal will undoubtedly limit services provided to consumers and raise costs for any services that are maintained. Although some companies have decided to voluntarily report information that outlines their exposure to "climate-related risks" that does not mean the SEC should mandate that **all** public companies compile information that may or may not improve an investors' decision-making. Moreover, disclosure of Scope 3 emissions will go beyond public companies and require small businesses and farmers who conduct business with public companies to compile and disclose information that they will not have readily accessible.

Blanket disclosure requirements will entrench market power with larger companies while smaller companies without the resources to comply with the new disclosure and reporting requirements will struggle to maintain solvency. The Proposal's onerous intervention will exacerbate anticompetitive behavior, thus reducing options and quality of services for consumers. Instead of drafting this in the "public interest" or for "protection of investors" the cost of the Proposal's provisions would, if adopted, produce a capital markets sector that is costly, reduces returns for investors, and limits investment options and services for consumers.

Instead of focusing on investors' pecuniary interest, public companies would be regulated to focus less on returns and more on criteria that promotes a political or social agenda at the behest of special interest groups and activists. Free market enterprise would be slowly chipped away because the SEC's prerogative is to inculcate a larger focus on ancillary environmental, social, and governance (ESG) factors.

SEC's Statutory Authority

The SEC does not possess the statutory authority to pursue the provisions outlined in the Proposal. Congress has not directed the SEC to draft the Proposal. Instead, the SEC claims that it has "considered this statutory standard and determined that disclosure of information about climate-related risks and metrics would be in the public interest and would protect investors." The SEC justifies the rulemaking by stating that it is appropriate "to consider such investor demand in exercising our authority and responsibility to design an effective and efficient disclosure regime under the federal securities laws." In fact, the provisions of the Proposal are arbitrary and capricious and "in excess" of statutory authority.

Court precedent has made it clear that the SEC cannot act without explicit Congressional authorization. Accordingly, a federal agency "is owed no deference if it has no delegated authority from Congress to act." Moreover, agencies "literally have no power to act" without Congress conferring "power upon" them.

Additionally, the Proposal is at odds with the "major questions" doctrine. The Proposal is formulating environmental policy that will impose "vast economic and political significance" on all public companies in the U.S. Accordingly, Supreme Court precedent will likely influence future litigation and determine that only Congress may establish significant environmental policy.

Investor demand by itself is not enough for a federal agency to pursue a legally binding rulemaking. The SEC states that since "2010 and earlier, there has been significant investor demand for information about how climate conditions may impact their investments." Only Congress has the power to authorize a federal agency to pursue certain rulemakings. To date, Congress has not passed any legislation to authorize the drafting and publication of the Proposal.

The SEC is circumventing the duly elected representatives in Congress, to follow the recommendations of an organization led by Michael Bloomberg. The Proposal states that "Each of these initiatives has advocated for mandatory climate risk disclosure requirements aligned with the recommendations of the Task Force on Climate-Related Financial Disclosures ("TCFD") so that disclosures are consistent, comparable, and reliable." The TCFD was founded by the Financial Stability Board (FSB), an international organization established by bureaucrats instead of elected representatives. The recommendations made by the TCFD do not represent Congressional intent, and by extension, the intent of the American people.

Congress has authorized the disclosure of material information that closely affects the financial performance of an issuer. Issuers of securities are already required to disclose material information that is listed under Schedule A. The information required for registration of publicly-traded securities is also specifically outlined in 15 USC §77aa. The detailed list directly pertains to the financial performance of a public company, unlike climate-related disclosure information. According to the House report for the Securities Act of 1933, "The items required to be disclosed, set forth in detailed form, are items indispensable to any accurate judgement upon the value of the security." The report also explicitly states that in order to "assure the necessary knowledge for judgement, the bill requires enumerated definite statements." Additionally, the statute does not grant the SEC "general power to require such information" as it sees fit. In fact, the report feared that too much regulatory flexibility "would lead to evasions, laxities, and powerful demands for administrative discriminations." If Congress wanted climate-related disclosures, it would have passed legislation authorizing it. Thus far, this has not happened. Nevertheless, the SEC is marching forward with policy-specific disclosures that will force public companies to mitigate their exposure to traditional energy sources.

Climate-related disclosures are ambiguous and unnecessary for determining the value of a security. Quantifying climate-related risks is difficult and costly to quantify. According to a report published by the Bank for International Settlements, as a practical matter, "the range of impact uncertainties, time horizon inconsistencies, and limitations in the availability of historical data on the relationship of climate to traditional financial risks, in addition to a limited ability of the past to act as a guide for future developments, render climate risk measurement complex and its outputs less reliable as risk estimators."

Materiality

The SEC has already issued rules that would require public companies to disclose climate-related risk information if it is deemed material. SEC guidance from 2010 shows how Regulation S-K requires under Item 503(c) to provide "a discussion of the most significant factors that make an investment in the registrant speculative or risky." Additional climate-related disclosures are

redundant and will only serve to increase costs for public companies and reduce returns for investors.

It can be argued that the "reasonable investor" would not benefit from "speculative" climate-related disclosure information and GHG emissions. The Proposal's claim that Scope 3 emissions only need to be reported if it is "material" stretches the limit of what constitutes material information. The SEC is dipping into the concept of "double materiality" and "dynamic materiality," which would likely not survive litigation because of Supreme Court precedent. *Basic V. Levinson* highlights the importance of "balancing probability and magnitude" of the information applied to varying industries. Scenario analysis of climate-related events and calculating transition risk is highly speculative and do not provide investors with useful information to make important investment decisions.

Regarding double materiality, in *TSC v. Northway*, Justice Marshall pointed out the clear impediments of "over-inclusive disclosure." In fact, Justice Marshall stated that mandated disclosures of certain information "may accomplish more harm than good." If materiality is too broad, "not only may the corporation and its management be subjected to liability for insignificant omissions or misstatements, but also management's fear of exposing itself to substantial liability may cause it to bury the shareholders in an avalanche of trivial information—a result that is hardly conducive to informed decision-making." This fear of liability is exactly what will push companies to limit or eliminate their exposure to traditional energy sources. Instead of market forces instituting a transition, a singular government agency is shaping U.S. energy policy. The SEC is wandering into rulemaking that is unlawful and beyond the scope of their expertise and authority. Not to mention, investors will be inundated with information that is unhelpful and likely immaterial.

Unwarranted deviation from the traditional materiality standard also negatively impacts management of companies and subsequently returns to investors. One registered investment adviser noted in a comment letter to the SEC, that forcing a company to disclose "external impacts of the company on the environment, when it does not affect the company itself, could compel corporate leaders to spend a disproportionate amount of time managing the disclosure of climate change risk at the expense of other activities that could add value for the company and its shareholders, as well as lead to the disclosure of information that, while not material from an investment standpoint, may be misconstrued as such by investors." The cost of stakeholder governance and focus on nonpecuniary matters that have a negligible effect on the financial performance of a company could put the company in jeopardy and hurt returns to investors.

Investor demand for certain disclosure information does not warrant the mandatory disclosures outlined in the Proposal. The SEC claims that investors "need information about climate-related risks—and it is squarely within the Commission's authority to require such disclosure in the public interest and for the protection of investors—because climate-related risks have present financial consequences that investors in public companies consider in making investment and voting decisions." This is contrary to a previous statement made by former SEC Commissioner Roberta Karmel. In 1978, Commissioner Karmel believed in exercising "caution in applying a non-economic standard of materiality to disclosure requirements." Commissioner Karmel stated that just because "some investors may want certain information in order to make an investment or

voting decision does not mean that mandatory disclosure of such information would be necessary or appropriate in the public interest or for the protection of investors." In the case of the Proposal, the SEC is pandering to the requests of large institutional investors and ignoring the opinions of retail investors.

Third Parties

The Proposal wrongly expands the traditional understanding of "materiality" to include disclosures promoted by largely European-based third-party organizations. The Proposal outlines the breadth of current climate-related disclosures produced by companies voluntarily. Some companies already follow reporting frameworks by the Sustainability Accounting Standards Board (SASB), Climate Disclosure Standards Board (CDSB), the International Integrated Reporting Council (IIRC), TCFD, Global Reporting Initiative (GRI), and CDP (formerly the Carbon Disclosure Project). However, the SEC admits the disclosures outlined in the Proposal are based on ideas perpetuated by foreign organizations that have no accountability to U.S. citizens.

Additionally, recent academic research has shown that adopting more extensive disclosure requirements harms innovation. A study of European countries found that "more-extensive financial-reporting mandates were negatively associated with innovation inputs such as personnel working in research and development, and with outputs such as new processes and products." The SEC's attempt to copy European climate disclosures will harm innovation, not improve it.

Companies may willingly decide to align their reporting with sustainability frameworks because they feel it is in the best interests of investors. However, that should remain a voluntary action—not subject to government mandate. As Chair Gary Gensler stated recently, "The core bargain from the 1930s is that investors get to decide which risks to take, as long as public companies provide full and fair disclosure and are truthful in those disclosures." The time-tested disclosure-based regime must remain in place. Unfortunately, the Proposal aims to divert the SEC's agenda to that of a merit-based regime that rewards companies for prioritizing politically convenient investment exposure (e.g., solar and wind power) as opposed to traditional energy exposure (e.g., oil and natural gas). Contrary to the SEC's belief, this is not in the best interest of investors.

Institutional investors are being prioritized over retail investors. The Proposal indicates that 85 percent of surveyed institutional investors referenced climate risk as "the leading issue driving their engagements with companies." Specifically, the Proposal mentions State Street and BlackRock expect their portfolio companies to decarbonize. The SEC should be prioritizing the needs of retail investors, not pandering to multi-trillion-dollar asset managers that have the wherewithal to perform precise due diligence and analysis. Additionally, State Street and BlackRock wield enormous power when voting on shareholder resolutions. According to a policy brief published by Caleb Griffin, investment stewardship teams "will be consciously or unconsciously biased toward their own preferences rather than those of their investors. Alternatively, such teams could be influenced by pressure from special-interest groups that, while more organized or more vocal than the majority, may not represent the interests of the majority." Index funds that are influenced by political or activist forces are now influencing the SEC to finalize a rulemaking that will allow institutional investors to reallocate capital to politically favored energy sources. In fact, this collusion is already being investigated as a potential violation of

antitrust law. This is likely subverting the economic interests of retail investors and index fund investors to promote a political agenda.

First Amendment Violation

By requiring climate-related disclosures, the SEC is violating the First Amendment. Court precedent clearly prohibits government agencies, including the SEC, to compel companies to disclose information on politically-charged topics such as climate change. This unconstitutional compelled speech parallels *National Association of Manufacturers v. SEC*, in which the court of appeals "concluded that the First Amendment prevented the SEC from compelling companies to describe their products" as to whether they came from "conflict mineral" zones. Similarly, the required climate disclosures, including GHG emissions, in the Proposal are subjective as to the importance to all investors. At the same time, "some companies would be forced to make remarks about their operations that are subjective or disparaging."

GHG Emissions

The Proposal provides no substantive justification for the requirements to disclose GHG emissions. The proposed disclosures deviate from the original purpose of revealing to investors "indispensable" information so that investors can assess the "soundness of a security." GHG emissions, whether directly or indirectly emitted, provide no clarity for the investor into the granular financial performance of a company. Only information that closely parallels the financial metrics as outlined in Schedule A can be determined to fit the bill and not supersede Congress's warning against "administrative discriminations."

Scope 3

One of the most egregious requirements in the Proposal is the disclosure of "Scope 3 GHG" emissions and their "intensity, if material." For fear of enforcement actions, companies will likely decide to disclose Scope 3 exposure whether it is material or not. This superfluous disclosure provides no relevant information that would inform investors on the elements of a security, and the immense cost of the collecting this information could negatively impact investors equity or debt positions in registered companies. Scope 3 disclosures are unfeasible for a company of any size.

Disclosure of Scope 3 emissions would require financial institutions to collect and distribute emissions information on the companies in which they have invested—this includes debt and equity financing. Collection of emissions information from counterparties would be costly and time consuming. It also runs the risk of providing duplicative information to the SEC. The companies that have received investment may already be required to disclose their own Scope 1 and 2 emissions under the Proposal. Accordingly, the disclosure of the Scope 3 investment emissions would be redundant and unnecessary.

Recent research has found no consistent relationship between GHG emissions and the performance of stocks and bonds. One study conducted by Dimensional Fund Advisors did "not detect a reliable empirical relation between these emission metrics" and returns for stocks and bonds. The lack of a relationship "suggests that the impact of climate change on the expected

returns of high-emissions firms, for example, is already captured by prices and proxies for expected future cash flows." Climate risk, including GHG emissions, are already accounted for in pricing securities. Additional risk disclosures will provide negligible benefits, but significant costs.

The Proposal admits that the economic effects of the GHG emissions disclosures could force a firm "to change some suppliers or disengage with certain clients due to the effect that they may have on the firm's Scope 3 emissions." Additionally, "These financial institutions may be less willing to extend credit to firms for which it is difficult to measure climate risk exposure information, potentially increasing the cost of capital for these firms."

The mandated disclosure of GHG emissions data politicizes securities regulation. If the Proposal could force financial institutions to divest from certain energy companies, the SEC could issue future proposals to require disclosure on other heated social topics. The SEC could publish rules requiring companies to disclose their exposure to firearm manufacturing, boardroom diversity, or a company's policy on unionization. This represents a strong deviation from traditional securities law and the original intent of the Securities Act of 1933 and the Securities Exchange Act of 1934. It also subverts the role of Congress and the rule of law.

Compliance Costs

The compliance costs that the Proposal will impose on companies will be greater than expected. The Scope 3 emissions reporting will force small, private companies that conduct business with public companies to collect and collate emissions data to comply with the SEC's proposed mandates. For example, a large bipartisan group of House members submitted a letter to the SEC that discusses how small farmers may have to disclose emissions data in order to conduct business with public companies. The letter states that, "these additional reporting requirements could disqualify small, family-owned farms from doing business with companies which could lead to more consolidation in the agriculture industry."

One comment to the Proposal specifically outlines the detrimental affects that Scope 3 reporting would have on family-owned egg farms. The commenter states that "If an egg farmer is not able to provide the necessary data and information required by the SEC registrant who now must disclose their Scope 3 emissions, this registrant could be forced to look elsewhere to purchase its raw inputs from an entity that has that information. This search for supply could push small and medium-sized farmers out of business." Compliance costs associated with the required disclosures will increase expenses and eat into small farmers' bottom lines. Increased costs will assuredly exacerbate the already grossly high cost of food at grocery stores as the U.S. continues to grapple with historic rates of inflation.

According to one media report, "For companies that are starting from scratch in reporting climate data, complying with the rules could be more expensive than the SEC estimates." Some companies will have to hire additional employees to comply with new disclosures. This increases payroll expenses and significantly reduces a business' bottom line.

Some investment advisers agree that the compliance costs will harm investors. One commenter highlighted that the costs for disclosures will be high for companies. Specifically, the "costs will be

borne by each company's investors, who may be harmed by a decrease in the company's stock price, and by the company's customers, who may have to pay higher prices for the company's goods and services."

Economic Analysis

The SEC's cost-benefit analysis leaves much to be desired. The Proposal admits that "In many cases, however, we are unable to reliably quantify these potential benefits and costs. For example, existing empirical evidence does not allow us to reliably estimate how enhancements in climate-related disclosure affect information processing by investors or firm monitoring." Moreover, the SEC claims that it describes the factors that could affect disclosure costs, but it is "unable to accurately quantify these costs." The SEC's poor attempt to provide an excuse for the inadequate cost-benefit analysis should by itself be grounds for failing to follow the stringent rulemaking process and be deemed arbitrary and capricious.

Concluding Thoughts

The Proposal is a significant deviation from the traditional implementation of U.S. federal securities law. The SEC is distorting the foundation of more than 80 years of principles-based disclosures by prioritizing merit-based disclosures that focus on achieving public policy goals by circumventing Congress.

There is no directive from the elected representatives in Congress—and by extension the American people—to pursue the arbitrary disclosure requirements in the Proposal. This blatant circumvention of the rule of law, whereby federal agencies will carry out directives required by Congress, is subjective and lacks clear authorization from elected representatives. Instead, the Proposal exemplifies "administrative discriminations" as described in the original House report for the Securities Act of 1933. Under the Proposal unelected bureaucrats are determining the direction of regulation of public companies, and creating their own version of environmental public policy.

If the SEC adopts the Proposal as a final rule, future litigation will likely determine that it is arbitrary and capricious under the Administrative Procedure Act.

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ATR appreciates the opportunity to comment on the Proposal. If you have any questions or need any additional information, please contact Bryan Bashur at [redacted].

Sincerely,

Americans for Tax Reform