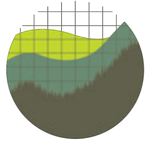

Institute *for*
Policy Integrity
NEW YORK UNIVERSITY SCHOOL OF LAW

August 16, 2022

VIA ELECTRONIC SUBMISSION

Attn: Secretary Vanessa Countryman

Re: Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices (File No. S7-17-22)

The Institute for Policy Integrity (Policy Integrity) at New York University School of Law respectfully submits the following comments to the Securities and Exchange Commission (SEC) regarding its proposal to add disclosures regarding Environmental, Social, and Governance (ESG) investment practices (Proposed Rule).[1] Policy Integrity is a non-partisan think tank dedicated to improving the quality of government decisionmaking through advocacy and scholarship in the fields of administrative law, economics, and public policy.[2]

Our comments focus on the Economic Analysis for the Proposed Rule. We commend the SEC for conducting a preliminary analysis that is consistent with relevant case law, and we suggest additions and minor revisions that would strengthen the final version. The Commission should consider:

- including any **relevant compliance cost data** from its PRA Analysis in its Economic Analysis and **explaining** whether the PRA estimates represent the incremental costs of the Proposed Rule;
- **expressly concluding** that benefits justify the costs;
- **contextualizing** the Proposed Rule's costs, either by comparing them to the costs of already existing disclosure requirements or by conducting a breakeven analysis;
- incorporating the **relevant economic baseline** more directly into its assessment of costs and benefits; and
- **providing additional support** for certain estimates.

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[1] *See* Sec. & Exch. Comm'n, Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices, 87 Fed. Reg. 36,654 (June 17, 2022) [hereinafter "Proposed Rule"].

[2] These comments do not purport to represent the views, if any, of New York University School of Law.

I. The SEC should consider including any relevant compliance cost data from its PRA Analysis in its Economic Analysis and explaining whether the PRA estimates represent the incremental costs of the Proposed Rule.

The SEC's Paperwork Reduction Act (PRA) Analysis contains quantified cost estimates of paperwork burdens. However, this analysis may be both too broad and too narrow. The SEC should consider integrating any relevant compliance cost data from its PRA Analysis into the body of its Economic Analysis and explaining, for each item, whether the PRA totals underestimate or overestimate the full incremental costs of the Proposed Rule.

Under the PRA, the burden of information collection is the "total time, effort or financial resources" associated with "generat[ing], maintain[ing], disclos[ing] or provid[ing] information to or for a Federal agency."[3] Costs that persons incur "in the normal course of their activities" may be excluded from these estimated burdens only if the agency can show that the activities required for compliance are "usual and customary."[4] As a result, the PRA Analysis might overestimate the incremental cost of the Proposed Rule because it does not take into account the status quo costs that certain funds and asset managers already incur to comply with voluntary ESG frameworks.[5]

At the same time, the PRA Analysis may also underestimate costs because it covers only the direct costs of information collection and not other compliance costs.[6] For this reason, the Commission should consider systematically integrating the PRA Analysis figures into its Economic Analysis and explaining their relationship to the incremental costs of the Proposed Rule.

II. For each element of the Proposed Rule, the Commission should consider expressly concluding that benefits justify the costs.

In general, we suggest that the Commission supplement its analysis with a side-by-side comparison of the costs and benefits associated with each element of the Proposed Rule, with reference to the economic baseline. Although a simple numerical comparison of the Proposed Rule's costs and benefits is not practicable given that many important effects are unquantifiable, there are other ways the Commission could enhance the clarity and accessibility of its analysis. For each proposed disclosure, the Commission should consider aggregating in a single place—such as a two-column table—all the available information on the expected costs and benefits, including unquantified investor protection, efficiency, competition, and capital formation-related benefits, and expressly concluding that each disclosure is net beneficial. This would help the

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[3] 5 CFR § 1320.3(b)(1).

[4] *Id.* § 1320.3(b)(2).

[5] *See infra* Section IV.

[6] The SEC discusses this when assessing potential effects of the Proposed Rule on small entities. *See* Proposed Rule, *supra* note 1, at 36,741–42 at n.486–89, n.492 ("Cost estimates only refer to the paperwork collection costs estimated in connection with the PRA, not all possible costs associated with compliance.").

public understand why the Commission believes that the benefits of each disclosure, and the overall benefits of the Proposed Rule, justify the associated costs.

III. The SEC should consider contextualizing the Proposed Rule's costs, either by comparing them to the costs of already existing disclosure requirements or by conducting a breakeven analysis.

The SEC could strengthen its Economic Analysis by contextualizing the compliance burden. This could be achieved by comparing the costs to other disclosure requirements—after accounting for the economic baseline—or by conducting a breakeven analysis.

The costs of the Proposed Rule may seem large in isolation but may be easier to understand in the context of funds' other compliance costs or overall revenues. Expenses that seem significant to an individual may be insignificant to a fund or advisor. The SEC could help the public contextualize the cost of the Proposed Rule by comparing it to funds' overall expenditures on disclosure, or by projecting how the costs could affect a fund's overall valuation. For example, in the context of the SEC's climate risk disclosure proposal, Professor Shivaram Rajgopal, an expert in corporate accounting and auditing, contextualized compliance costs by estimating their effects on a typical public company's market capitalization. He concluded that "the loss in market capitalization, if any, from compliance costs is too tiny for any outsider to detect."[7] If possible, a similar analysis could be useful here.

The SEC could also consider conducting a breakeven analysis. A breakeven analysis addresses the question "How large would the value of the non-quantified benefits have to be for the rule to have positive net benefits?" and can "provide insights when quantification is speculative or impossible."[8] For example, the SEC could analyze how much time or money each investor would need to save in order to justify the costs of the Proposed Rule. This would lend context to the magnitude of positive effects that would be necessary in order for benefits to outweigh costs.

Lending additional context to the anticipated costs of the Proposed Rule would strengthen the SEC's Economic Analysis.

IV. The SEC should consider incorporating its economic baseline more directly into its assessments of costs and benefits.

The baseline in an economic analysis lays out "how the world would look in the absence of the proposed action."[9] This includes, for example, "the existing regulatory structure" and "economic attributes" of the market.[10] Throughout the preamble, the SEC describes existing regulatory and

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[7] Shivaram Rajgopal, Comment Letter on Proposed Rule on the Enhancement and Standardization of Climate-Related Disclosures for Investors 3 (June 12, 2022), https://perma.cc/DJ72-25TH.

[8] OFF. OF MGMT. & BUDGET, CIRCULAR A–4, REGULATORY IMPACT ANALYSIS 13 (2003), https://perma.cc/M9LD-C4TM.

[9] Memorandum from RSFI and OGC to Staff of the Rulewriting Divisions and Offices on Current Guidance on Economic Analysis in SEC Rulemakings at 6 (March 16, 2012), https://perma.cc/S35K-QQ7V.

[10] *Id.* at 6–7.

voluntary ESG disclosure frameworks and discusses how certain funds may already be engaging in market practices consistent with the requirements in the Proposed Rule.[11] In addition to this overview, the SEC should consider providing additional information on funds' current expenditures on voluntary ESG disclosures, as well as the amount of time that investors currently spend sorting through incomparable or unavailable ESG data. The Commission should consider incorporating these elements directly into its considerations of costs and benefits in the Economic Analysis.

A. Existing expenditures on voluntary ESG disclosures

As the SEC notes, there already exist several third-party ESG reporting frameworks, many of which have begun consolidating and aligning their standards.[12] The SEC could improve its analysis by explaining, more clearly, how the incremental compliance costs are decreased by this existing market behavior. While the SEC acknowledges that compliance costs may be lower "to the extent that some funds . . . may already disclose some form of ESG-related information,"[13] a more in-depth analysis would be useful, particularly given that the numerical estimates used in the PRA Analysis do not reflect this economic baseline.

In particular, the SEC estimates that, in 2021, 10% of asset managers provided climate-related disclosures under the disclosure framework of the UN Principles for Responsible Investment (UN PRI), of which 12% disclosed greenhouse gas emissions.[14] This would imply that 1.2% of asset managers, overall, already report greenhouse gas emissions. While this number may seem low, recall that the SEC estimates that only 2.4% of funds reporting to Form N-PORT had names containing words like, "Sustainable, Responsible, ESG, Climate, Carbon, or Green."[15] Therefore, it is possible that half of the funds that would be affected by the greenhouse gas emissions disclosures for ESG-focused funds are already collecting and reporting that information. The SEC should consider examining the appropriate baseline for greenhouse gas reporting—and for other types of disclosures—and incorporating quantified estimates into its consideration of costs.

B. Time savings for investors

In considering the economic baseline, the SEC provides survey evidence of high investor interest in ESG funds, and also provides evidence that this interest has resulted in an increased number of ESG-related funds on the market.[16] Under the status quo, the information asymmetry between investors and funds likely causes investors to spend time and money attempting to identify the types of funds that align with their interests. While the SEC does discuss improved market

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[11] Proposed Rule, *supra* note 1, at 36,702–06.

[12] *Id.* at 36,703.

[13] *Id.* at 36,704.

[14] *Id.*

[15] *Id.* at 36,657 (internal quotations omitted).

[16] *Id.* at 36,700–02.

alignment and how mandatory reporting results in more comparable and accurate information,[17] it could strengthen its analysis by providing a thorough treatment of the time and money investors spend trying to identify ESG funds.

V. The SEC should consider adding additional support for certain estimates.

There are a handful of places where the SEC's estimates could benefit from further discussion and support.

First, the SEC uses a survey from the Partnership for Carbon Accounting Financials (PCAF) to support its estimates for compliance costs related to emissions accounting.[18] The survey provides helpful information about the range of costs that various institutions have faced, including banks and asset managers. If possible, the SEC's analysis would be stronger if the Commission were able to isolate the average compliance costs of asset managers within this survey, as costs may vary between banks and asset managers. If additional data on average costs exists, outside of this survey, that data would also be useful to incorporate.

Second, in discussing the costs of assessing greenhouse gas emissions, the SEC provides data from compliance costs with the European Union Taxonomy.[19] These costs could be more directly integrated into the reasoning of the costs section to provide an upper bound on anticipated compliance costs.

Third, the SEC notes that funds may share costs at the institutional and fund family level, which would lead to reduced compliance costs in assessing greenhouse gas emissions, due to economies of scale.[20] Both in estimating compliance costs for environmental ESG-focused funds, and in other areas where economies of scale could reduce costs, the SEC should consider identifying how many unique institutions may be affected by the rule and by what amount pooling these fixed costs would reduce overall compliance burdens.

Respectfully,

Jack Lienke
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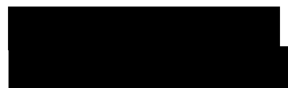

[17] *See, e.g.*, *id.* at 36,707.

[18] *Id.* at 36,714.

[19] *Id.*

[20] *Id.*