PROBLEMS WITH THE SEC'S CLIMATE DISCLOSURE PROPOSAL

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Subcommittee on Oversight and Investigations
"Oversight of the SEC's Proposed Climate Disclosure Rule: A Future of Legal Hurdles"

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Chair Huizenga, Ranking Member Green, Members of the Subcommittee, thank you for hearing my testimony. It addresses a March 2022 proposal of the Securities and Exchange Commission (the "SEC") prescribing disclosure of greenhouse gas emissions information and related governance practices (the "Proposal"). I am Special Counsel with Mayer Brown LLP, Emeritus Professor at The George Washington University, and Founder of Quality Shareholders Group.[1] I have spent my 35-year career in corporate and securities law and investing, writing extensively in these areas,[2] including comment letters and other writings on the Proposal.[3]

As a threshold matter, climate and climate change are significant matters of social and economic policy. That is one reason Congress authorized the Environmental Protection Agency (the "EPA") to protect the climate. Climate risks that are material to companies would be of interest to reasonable investors. That is why SEC guidance, in place for more than a decade, has required companies to disclose all climate risks that are material to their businesses.[4] The Proposal is therefore both unnecessary and outside the SEC's policy lane as well as problematic in other ways that my testimony will detail.

To summarize some primary problems, the Proposal:

- disregards evidence that most individual investors buy stocks primarily to save, not to influence climate policy;
- does not address the millions of individual American investors who need the SEC's protection as they save for education, homes, retirement, and philanthropy; and
- ignores conflicts of interest between large asset managers and their beneficiaries—ordinary Americans—who have different preferences and goals.

In addition, the Proposal mandates irrelevant and burdensome disclosures that would harm investors by:

- forcing companies to disclose information about the greenhouse gas emissions of their suppliers, employees, and customers, which is useless to investors;

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[1] This testimony is my own and does not necessarily reflect the views of Mayer Brown LLP or any of its clients.

[2] My resume is posted at the following link: www.law.gwu.edu/sites/g/files/zaxdzs5421/files/2023-06/cunningham-prof-cv-may-2023-full.pdf.

[3] *E.g.*, Comment Letter (April 25, 2022), https://perma.cc/7YR9-QJPT.

[4] SEC, Commission Guidance Regarding Disclosure Related to Climate Change (February 2010).

- making companies report climate impact, not just climate risk, which investors do not need;
- imposing millions of dollars in annual costs on companies with no clear benefit for investors (or the climate);
- compelling the disclosure of information that is inherently speculative and uncertain, as likely to mislead investors as to inform them;
- spurring lawsuits over disclosure adequacy, which wastes resources even when baseless;
- discouraging companies from being publicly traded, which deprives ordinary investors of opportunities and frustrates capital formation; and
- usurping state corporate law and company business judgment, which undermines investor rights and interests.

Furthermore, the Proposal faces legal challenges under:

- the major questions doctrine, as it lacks clear Congressional authorization for its significant policy reach, as suggested in cases since the Proposal was issued, especially *West Virginia v. EPA;*[5]
- the First Amendment, for compelling company speech on controversial matters; and
- the Administrative Procedure Act, as it solves no problem within the SEC's mandate, and includes no proper cost-benefit analysis, perils that led another SEC rule to be vacated last month.[6]

Given these problems, developments since the Proposal was issued, and the extensive comments submitted expressing concern about the Proposal, a final question is whether the SEC should reopen a new comment period for the Proposal, or any revision.[7]

1. Shortchanging Individual Investors

The SEC relies heavily on "investor demand" to invoke authority based on investor protection. But while the Proposal copiously documents large global institutional interests making such demands, including large asset managers and especially climate activists, the Proposal scarcely mentions individual investors. Yet the views of the executives of large asset managers and climate-focused organizations may not represent the best interests of retail investors, including individual direct owners, mutual fund investors, and beneficiaries of pension plans.

Institutional Demand. The Proposal refers to "investor demand" 54 times, with citations to one segment of the universe. The Proposal introduces what it calls "growing investor demand" by listing six consortia of large global institutions along with reported assets under management.[8] The list includes groups of such institutions that have signed policy advocacy documents from the United Nations urging countries to reduce climate risks: Net Zero Asset Managers Initiative, Climate Action 100+, and Glasgow Financial Alliance for Net Zero. Count the Proposal's citations, presented on the next page, and you will see that the SEC relies overwhelmingly on prominent environmentalists, not prominent investors nor ordinary ones:

[5] 142 S. Ct. 2587 (2022).

[6] *Chamber of Commerce v. SEC,* 88 F.4th 1115 (5th Cir. 2023).

[7] The final footnote in this testimony summarizes potential lines of oversight inquiry that these problems suggest.

[8] Proposal, pp. 25-29 (repeated at pp. 332-333).

The Proposal's citations skew heavily toward organizations that are prominent environmentalists, not prominent investors. The following are the seven organizations the Proposal cites most frequently (each cited in 14 to 28 different footnotes):

MOST CITED OVERALL	Footnotes
Environmental Protection Agency (EPA)	28
Carbon Disclosure Project (CDP)	27
Natural Resources Defense Council	22
American Institute of Certified Public Accountants (AICPA)	22
Coalition for Environmentally Responsible EconomieS (CERES)	21
Sustainability Accounting Standards Board (SASB)	19
United Nations Principles for Responsible Investment Corp. (PRI)	14

The investors the Proposal cites most frequently skew toward those focused on social and political investing and many are non-U.S. entities. The following are the seven investors the Proposal cites most frequently (each cited in 9 to 14 different footnotes; a majority are non-U.S.):

MOST CITED INVESTORS	Footnotes
New York State Comptroller	14
BNP Paribas (French)	12
BlackRock	11
Impax Asset Management (English)	9
Baillie Gifford (Scottish)	9
Trillium: Socially Responsible Investing	9
Northwest & Ethical Investments (NEI) (Canadian)	9

Of the 36 other organizations the Proposal cites heavily (at least 5 footnotes), 12 are climate advocacy groups.

OTHER MOST CITED	Footnotes
Climate Governance Initiative	12
Interfaith Center on Corporate Responsibility	9
Carbon Tracker Initiative	8
Regenerative Crisis Response Committee	7
Friends of the Earth	7
Amazon Watch	6
Partnership for Carbon Accounting Financials (PCAF)	5
As You Sow	5
Center for Climate and Energy Solutions	5
Institute for Governance and Sustainable Development	5
World Benchmarking Alliance	5
World Resources Institute	5

What About Individual Investors? The investor group most needing the SEC's protection is not the multi-trillion-dollar funds the Proposal repeatedly emphasizes, but the 160 million individual American investors who cannot fend for themselves. Yet, inexplicably, while the Proposal repeatedly cites the interests of such powerful institutions, it mentions individual investors only once in 508 pages. This occurs when it says that if institutional analysts digest the detailed climate disclosure using certain advanced software:

> this would likely benefit retail investors, who have generally been observed to rely on analysts' interpretation of financial disclosures rather than directly analyzing those disclosures themselves.[9]

The SEC should not give America's individual investors such short shrift. To the contrary, the SEC should directly attempt to gauge the level of investor demand—and especially protection—among individuals for the Proposal's controversial and expensive disclosures.

Research and Survey Data. Relevant research raises serious doubts about whether individual investors share the SEC's enthusiasm for such disclosure and the SEC should take these views into consideration. For instance, when scholars explicitly distinguish institutional from individual investor "demand," they find that "ESG disclosures are irrelevant to retail investors' portfolio allocation decisions."[10]

Survey findings support this point.

- *Barron's* highlighted a survey of individual investors co-sponsored by FINRA indicating that most do not share institutional investor enthusiasm for "ESG investing," many are unfamiliar with it, and one-fourth think the acronym stands for "earnings stock growth."[11]
- The survey co-sponsored by FINRA finds that individual investors prioritize financial results and return on investment more than any other factor and view environmental aspects of a potential investment as the *least important consideration* compared to financial, governance, and social factors.[12]
- Another recent FINRA survey of investors of color confirms that they, like all individual investors, overwhelmingly prioritize financial returns compared to other reasons for investing.[13]

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[9] Proposal, p. 384.

[10] *See* Austin Moss*, et al*., The Irrelevance of ESG Disclosure to Retail Investors: Evidence from Robinhood (2020), https://papers.ssrn.com/abstract_id=3604847.

[11] *See* Lauren Foster, Investors Know Little About ESG, a New Study Finds, *Barron's* (April 12, 2022).

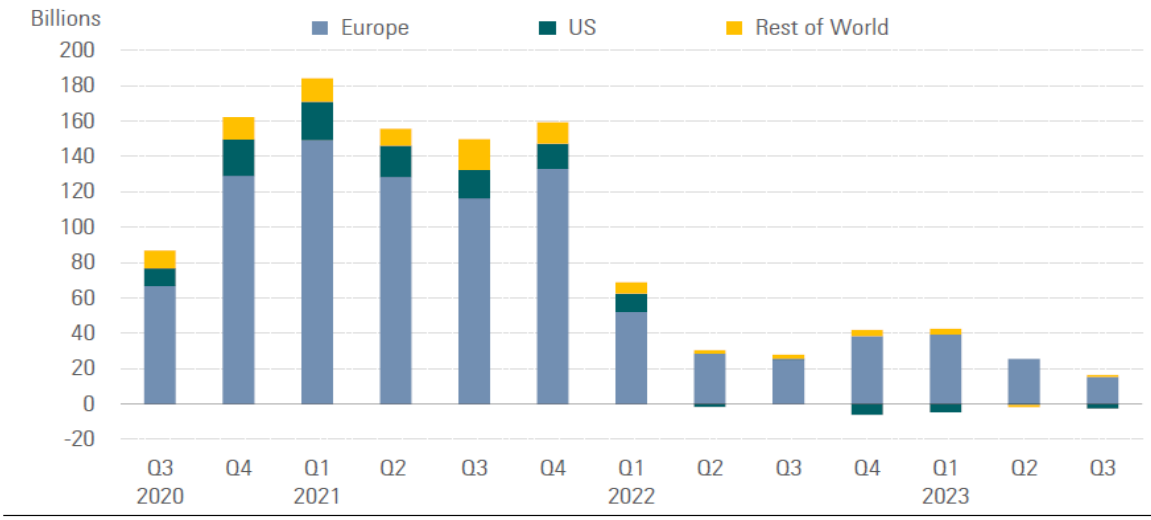
[12] FINRA Investor Education Foundation & NORC at the University of Chicago, Investors say they can change the world, if they only knew how: Six things to know about ESG and retail investors (March 2022).

[13] FINRA Investor Education Foundation, Investors of Color in the United States (January 2024) (concerning "reasons for investing," at least 95% of respondents in all racial categories chose "to make money in the long-term" and at least 69% in all racial categories (and 91% of Blacks surveyed) chose "to make money in the short term" compared with lower levels, from 39% to 66%, choosing "to make a difference in the world/support values I care about/be socially responsible."). Another reason chosen by a majority of those surveyed in all racial categories was "to learn about investing." *Id*. *See also* Oyin Ardoyin & Sanaa Rowser, Stocks' Fastest-Growing Sector: Black Investors, *Wall St. J*. (January 16, 2024) (reporting survey data showing that among individuals under 40, nearly 70% of Black respondents are investing).

- A Gallup poll of individual investors finds that most prioritized the expected rate of return and risk for potential losses over environmental and other issues.[14]

Market and Funds Flow Data. Markets reflect such preferences. Since the date of the Proposal, in the first quarter of 2022 through the third quarter of 2023, investors have withdrawn from sustainable funds, as seen in the following chart of fund flows from *Morningstar*.[15]

Exhibit 2 Quarterly Global Sustainable Fund Flows (USD Billion)



Source: Morningstar Direct, Manager Research. Data as of September 2023.

Shareholder Proposal Trends. The fate of recent shareholder proposals on climate-related matters reflects similar appetites. While the Proposal cites a rise in the number of climate-related shareholder proposals as evidence of its "investor demand," the rise is measured in a misleading manner and the data since the Proposal undermine the claim.

First, the SEC Staff in late 2021 changed its approach to vetting shareholder proposals, and since then has been requiring companies to include any that "relate to a significant social policy issue" even if unrelated to a company's ordinary business operations.[16] This change explains much of the recent rise in the frequency of climate-related shareholder proposals. In the year before the SEC staff's reversal, the staff agreed with company requests to exclude proposals 40% of the time, but the next year that figure dropped to 23%.[17] The SEC staff's new approach correlates with increases in shareholder proposal submissions and ensuing votes.[18]

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[14] *See* Gallup, Where U.S. Investors Stand on ESG Investing (February 23, 2022).

[15] Alyssa Stankiewicz, Sustainable Funds Hit by Weaker Demand in Q3 2023: Investors Pulled $2.7 Billion From U.S. Sustainable Funds, For Fourth Consecutive Quarter of Outflows, Amid Rising Energy Prices and Political Backlash, *Morningstar* (Oct. 23, 2023).

[16] SEC, Division of Corporation Finance, Staff Legal Bulletin No. 14L (Nov. 3, 2021).

[17] Mark T. Uyeda, Remarks at the Society for Corporate Governance 2023 National Conference (June 21, 2013).

[18] *See, e.g.*, James Nani & Lydia Beyoud, Shareholders Up Climate, Social Demands After SEC Policy Shift, *Bloomberg L.* (April 4, 2022); Paul Verney, SEC Allows Firms to Block Just 15% of E&S Proposals this Year,

Second, most such proposals are submitted by organizations whose websites unambiguously indicate that their objective is to pursue political values, not investment returns, including many of the authorities the SEC cites most often in the Proposal, particularly CERES and As You Sow.[19] Many proponents acknowledge following the strategy of hijacking the shareholder proposal rule, stressing that they buy minimal stakes in big companies to advance their missions regardless of the effects on a company's performance or shareholder value—an approach that is largely denounced[20] but sometimes encouraged.[21]

Third, not coincidentally, support for shareholder proposals has declined sharply in the two years since the Proposal was issued, after rising for several years before that.[22] Comparing 2021 to 2023 among all proposals, the average percentage of shares voting in favor fell from 36% to 24% and the portion of proposals attracting majority support dove from 19% to 5%.[23] For social and environmental proposals, the average percentage of shares voting in favor dropped from 37% to 20% and the portion attracting a majority plummeted from 23% to 3%.[24]

Declining support is unsurprising, since proposals are increasingly unfocused on shareholder value, address topics not material to shareholders, and risk decreasing value as they distract managerial attention from running the business. In short, the evidence from shareholder proposal practices does not support the case that "investor demand" justifies invoking the SEC's "investor protection" authority to pass the Proposal.

SEC Bears the Burden of Producing Evidence. The foregoing data points concerning surveys, funds flows, and shareholder proposals may not be conclusive evidence concerning whether individual investors are "demanding" what the Proposal offers. But as a matter of the Subcommittee's oversight, it bears emphasizing that SEC should both take account of the evidence that exists, including such surveys, and fill in the gaps in the administrative record. For instance, it is well-known that institutional investors vote for environmental shareholder proposals at about twice the rate of individual investors.[25] Recent empirical research, moreover, indicates that less than 2% of mutual fund money is invested in ESG funds.[26]

Responsible Investor (April 12, 2022); Suzanne McGee, Shareholders Push an Array of ESG Proposals, *Wall St. J.* (April 28, 2022). The number of proposals submitted to companies in 2023 increased 18% over 2021, rising to almost 1000, while the portion put to a vote increased 40%, exceeding 600 in 2023. Uyeda, *supra*. Social and environmental topics led the increases, up 52% in submissions and 125% in those put to a vote. *Id.*

[19] *See* Jeff Green & Saijel Kishan, Guns, Abortion and Race Heat Up Company Annual Meetings, *L.A. Times* (June 8, 2022).

[20] *E.g.,* John H. Matheson & Vilena Nicolet, Shareholder Democracy and Special Interest Governance, 103 *Minn. L. Rev.* 1649 (2019).

[21] *See* Lisa M. Fairfax, Social Activism through Shareholder Activism, 76 *Wash. & Lee L. Rev*. 1129 (2019); David Webber, The Rise of the Working Class-Shareholder: Labor's Last Best Weapon 45-151 (2018).

[22] Kate Hilder, Mark Standen & Siobhan Doherty, Institutional Investors Have Changed Their Tune on Supporting ESG Shareholder Proposals, Minter Ellison (May 26, 2021); Jackie Cook, How Fund Families Support ESG-Related Shareholder Proposals, *Morningstar* (Feb. 12, 2020).

[23] Uyeda, *supra*.

[24] *Id*.

[25] *See*, *e.g*., PwC/Broadridge, Proxy Pulse: 2022 Proxy Season Preview 8 (Feb. 2022).

[26] Jonathan Berk & Jules H. Van Binsbergen, The Impact of Impact Investing (June 10, 2022).

The SEC, not commentators or the public, bears the burden of demonstrating that a proposed rule promotes efficiency, competition, and capital formation as required by its organic statutes.[27] If the SEC has chosen to put forth meeting investor demand as a rationale for the Proposal, it is reasonable to expect it to have evidence indicating such demand emanating not only from an institutional subset of investors and social activists, but from the large base of individual investors. While generating requisite quantitative data can be difficult, evidence-based rulemaking remains both desirable and feasible.[28] Again, this would be a fruitful area to exercise the Subcommittee's oversight.

Institutional Asset Managers and Individual Investors. Another area of fruitful Subcommittee oversight would focus on how the institutional investors "demanding" climate-related information are overwhelmingly asset managers who are managing other people's money, not their own. This raises the obvious question whether their advocacy is prompted by concern for their beneficiaries' returns or their own profitability. Two of the SEC's recent major rulemaking proposals relating to private fund advisors each contained dozens of references to potential conflicts of interest between private advisors and their sophisticated clients.[29] Yet the Proposal makes not a single reference to potential conflicts of interest between retail asset managers and their less-sophisticated clients, instead taking it as given that what is good for the asset manager is good for the beneficiary. The Subcommittee should consider asking the SEC to explain why.

After all, to determine whether adopting the Proposal will protect investors, the SEC must explicitly consider the conflicts that arise between large asset managers and their beneficiaries and whether climate disclosure mandates will exacerbate them.[30] There is no indication that the SEC has attempted to assess, much less quantify, the potential losses to individual investors from self-interested voting or engagement by the asset managers to whom 160 million Americans entrust their savings.

The Subcomittee would also do well to investigate whether the SEC has asked the institutions "demanding" such information whether they have polled their individual clients, the ultimate investors, to determine whether they agree on the desirability or need for such information. That would provide a more meaningful measure of "investor demand" than the Proposal presents. It would also help assure that such institutions are meeting their fiduciary duties when managing assets for others.[31] The empirical evidence also raises doubts about whether

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[27] *See*, *e.g*., *Timpinaro v. SEC*, 2 F.3d 453, 455 (D.C. Cir. 1993)*; Chamber of Commerce v. SEC*, 412 F.3d 133 (D.C. Cir. 2005)*; Chamber of Commerce v. SEC*, 443 F.3d 890, 893-94, 909 (D.C. Cir. 2006); *American Equity Investment Life Insurance Co. v. SEC*, 613 F.3d 166, 168 (D.C. Cir. 2010); *Business Roundtable v. SEC,* 647 F.3d 1144 (D.C. Cir. 2011).

[28] *See* John C. Coates IV, Cost-Benefit Analysis of Financial Regulation: Case Studies and Implications, 124 *Yale L.J.* 882, 892-893 (2015); Bruce Kraus & Connor Raso, Rational Boundaries for SEC Cost-Benefit Analysis, 30 *Yale J. Reg*. 289, 298-99 (2013); Richard L. Revesz, Cost-Benefit Analysis and the Structure of the Administrative State: The Case of Financial Services Regulation, 34 *Yale J. Reg*. 545, 565-570 (2017).

[29] SEC, Release No. IA-5950; File No. S7-01-22, and SEC, Release Nos. IA-5955; File No. S7-03-22.

[30] *See* Paul G. Mahoney & Julia D. Mahoney, The New Separation of Ownership and Control: Institutional Investors and ESG, 2021 *Colum. Bus. L. Rev*. 840.

[31] *See* Max M. Schanzenbach & Robert H. Sitkoff, Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee, 72 *Stan. L. Rev.* 381 (2020).

institutional investors, such as public pension funds, are doing so.[32] In its oversight role, the Subcomittee might ask the SEC to assess the evidence.

2. Why Climate? Why Not Materiality?

The Proposal does not explain why climate risk information warrants compelled disclosure, rather than relying on voluntary disclosure, compared to information about all the other risks a company faces. After all, companies must manage many risks that government could in principle require specific disclosure on. With that disclosure, investors would have more information, which, in theory, should lead to better decision making. If there were no costs, government could require disclosure of all of them.

But there are costs, in both the production of information by companies and the prospect that overproduction of immaterial information can overwhelm and distract investors from what is important.[33] So a line must be drawn. The SEC's original disclosure regime focused on an audited set of financial statements that investors would find useful. Related accounting rules, ultimately generally accepted accounting principles (GAAP), provided the anchor. Expected future events, to be disclosed, had to pose a material risk on ensuing financial statements. Most SEC disclosure rules remain anchored to such principles.[34]

The Proposal, however, is not anchored to any principles. It is unmoored and does not offer any limiting principle to what the SEC can compel companies and their managers to disclose. The SEC must articulate a reasoned—non-arbitrary and non-capricious[35]—basis to distinguish climate change not only from financial reporting but also from myriad other risks businesses face. Examples: war, pandemic, monetary policy, or social issues such as equality or free speech, and geopolitical concerns, such as transacting with companies in China or Russia.

Since disclosure is costly—to companies and investors—requiring disclosure must also confer benefits greater than their costs. For investors, such costs must provide benefits tied to the information required to be disclosed. But consider two facts: (1) numerous climate models exist and none of them agree with each other and (2) take any climate model and feed in the conditions of the past, and they are unable to predict the present.[36] In a setting so imprecise, it is hard to see how investors will benefit from such disclosure.

The extent of a company's greenhouse gas (GHG) emissions would be directly relevant to the costs of a company's operations had Congress enacted a tax on such emissions. It has not. It would be relevant to a company's costs had Congress created a cap-and-trade system for such

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[32] *See* Jean-Pierre Aubry, *et al.,* ESG Investing and Public Pensions: An Update, Boston College Center for Retirement Research (2020) ("The evidence suggests, however, that social investing: (1) yields lower returns; and (2) is not effective at achieving social goals. Hence, *any form of social investing is not appropriate for public pension funds*.") (emphasis and punctuation added); Ulrich Atz, *et al.,* Does Sustainability Generate Better Financial Performance?, 13 *J. Sustainable Fin.* 1 (2022) (meta review of ~1400 empirical studies 2015-2020 finding "the financial performance of ESG investing has on average been indistinguishable from conventional investing").

[33] *See* Mark T. Uyeda: Remarks at the Going Public in 2020s Conference (May 3, 2023); Troy A. Paredes, Blinded by the Light: Information Overload and Its Consequences for Securities Regulation, 81 *Wash. U. L. Q*. 417 (2003).

[34] *E.g*., Items 101, 103, 105, 303, and 503(c) of Regulation S-K.

[35] Administrative Procedure Act, 5 U.S.C. 706(2); *Chamber of Commerce v. SEC,* 85 F.4th 760, 777 (5th Cir. 2023); *Chamber of Commerce v. SEC,* 88 F.4th 1115 (5th Cir. 2023). *Business Roundtable v. SEC*, 647 F.3d 1144, 1150 (D.C. Cir. 2011).

[36] *See* Steven E. Koonin, Unsettled: What Climate Science Tells Us, What It Doesn't, and Why It Matters (2021).

emissions. It has not. It would be relevant to a company's costs had Congress adopted binding nationwide GHG emission targets with an enforcement mechanism. It has not.

Note also that the lack of a materiality qualification for some of the proposed disclosures is relevant to whether these disclosures serve the interests of investors as opposed to other stakeholders. The Proposal would compel reporting three sources of emissions, called scope 1, 2 and 3. These are not only (1) the GHG emissions a company controls but those it does not control, but also (2) the suppliers of its energy and (3) its employees and customers. Ordinary investors could well consider scope 1 important (material in securities law parlance), but not scope 2 nor 3. Marketers of so-called "green" funds could well consider scope 2 and 3 important to design a fund, but Congress has not authorized the SEC to protect the interests of such marketers.

While it is difficult to see how GHG emissions of third parties would be material to a company's shareholders, the Proposal would make it extremely difficult for a company to choose to omit such information for that reason. For instance, the Proposal offers without explicitly endorsing a possible quantitative metric for the materiality of scope 3 emissions—40% of a company's total GHG emissions—but then sweeps them all in as presumptively material if they present a significant risk or are subject to significant regulatory focus.[37] Moreover, the Proposal admonishes that companies determining that some or all their scope 3 emissions are not material to explain why that is the case—effectively compelling the disclosure of all type 3 emissions whether material or not.

A related issue is the definition of "climate risk." Climate evolves over decades and centuries. A report by the Basel Committee on Banking Supervision highlights the practical difficulties and inherent unreliability of calculating climate risk information:

> 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.[38]

How will SEC reporting companies declare risk exposure to such long-term change? Even if it were feasible to do so, despite the limits of climate models, how will companies characterize the risk itself? To calculate exposure, they would need, at the very least, a distribution of the risk. Where will that come from?

On the other hand, the risk could be that companies are exposed in the shorter term to changing attitudes to products thought to harm the environment. Clearly that will affect businesses and will expose them to risks. But how is that different from any risk firms face with changing preferences? It would be preposterously outside its mandate for the SEC to require disclosure modeling the risks of shifting consumer preferences.[39]

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[37] *See* Hester M. Peirce, Commissioner, SEC, We are Not the Securities and Environment Commission—At Least Not Yet (Mar. 21, 2022).

[38] Basel Committee on Banking Supervision, Climate-Related Financial Risks—Measurement Methodologies (April 2021) p. 17 https://www.bis.org/bcbs/publ/d518.pdf.

[39] The SEC would do well to recall the advice given in 1978 by then-Commissioner Roberta Karmel (since then a distinguished law professor):

3. Huge Known Costs v. Illusory Benefit

The Proposal follows the form of cost-benefit analysis expected of U.S. federal agencies. The substance, however, leaves a great deal to be desired. There is ample precedent of courts abrogating SEC rules for failure to conduct an adequate cost-benefit analysis,[40] including a case from just last month,[41] and there are good reasons to question the merits of the cost-benefit analysis contained in the Proposal.[42] The Subcommittee might ask the SEC about the lessons it has learned from the recent case, overall and for purposes of the Proposal.

As a threshold matter, courts will insist that the SEC demonstrate that there is a problem to be solved, as its own internal policies contemplate.[43] If voluntary disclosure suffices to inform investors of material climate related risks, the SEC would be unable to provide the required rational basis for the Proposal rule. In the recent case, *Chamber of Commerce v. SEC*, the SEC failed to support its proposed share buyback disclosure rule for that reason: it did not identify the problem its mandatory disclosure was going to solve.[44]

In *Chamber of Commerce v. SEC*, the SEC's attempted statement of the benefits, moreover, failed to substantiate them because they were wrapped in a contradiction: the SEC both said the disclosure would be valuable to investors but not costly to companies. The court observed that the SEC "cannot have it both ways."[45]

Is there a problem facing investors that the Proposal can redress or a benefit it will provide to investors? The Proposal and its supporters talk of promoting comparability and consistency to enable markets to improve stock pricing accuracy. They suggest the specific disclosures called for by the Proposal will contribute meaningfully to the market's ability to value companies. The Proposal is equivocal, however, referring repeatedly to benefits that "could," "may" or "might" arise.

> [D]espite the legitimate concerns of ethical investors, I believe we should exercise caution in applying a non-economic standard of materiality to disclosure requirements. . . . 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.

Commissioner Roberta S. Karmel, Changing Concepts of Materiality, Speech before the National Investor Relations Institute (April 12, 1978), www.sec.gov/news/speech/1978/041278karmel.pdf.

[40] *E.g.*, *Timpinaro v. SEC*, 2 F.3d 453, 455 (D.C. Cir. 1993)*; Chamber of Commerce v. SEC*, 412 F.3d 133 (D.C. Cir. 2005); *Chamber of Commerce v. SEC*, 443 F.3d 890, 893-94, 909 (D.C. Cir. 2006); *American Equity Investment Life Insurance Co. v. SEC*, 613 F.3d 166, 168 (D.C. Cir. 2010).

[41] *Chamber of Commerce v. SEC*, 85 F.4th 760 (5th Cir. 2023) (holding that the SEC acted arbitrarily and capriciously in violation of the Administrative Procedure Act by failing to conduct a proper cost-benefit analysis of share buyback rule it adopted); *Chamber of Commerce v. SEC*, 88 F.4th 1115 (5th Cir. 2023) (vacating that rule due to SEC's failure to remedy the violations).

[42] *Business Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011) (vacating a rule in part because the SEC "inconsistently and opportunistically framed the costs and benefits of the rule").

[43] *See* Memorandum from the Division of Risk, Strategy, and Financial Innovation (RSFI) and the Office of the General Counsel to Staff of the Rulewriting Divisions and Offices (Mar. 16, 2012).

[44] *Chamber of Commerce v. SEC*, 85 F.4th 760 (5th Cir. 2023); *Chamber of Commerce v. SEC*, 88 F.4th 1115 (5th Cir. 2023).

[45] *Id*.

But there does not appear to be any evidence of persistent climate-related pricing anomalies (profitable trading opportunities) under the current disclosure system that additional disclosure would eliminate. Indeed, given the enormous quantity of existing mandated and voluntary disclosure about climate risk, it would be surprising to discover significant mis-pricings that the new disclosures could correct.

Put another way, it is generally accepted that all material information is incorporated into stock prices, but that does not imply that all climate information affects stock prices. Only material climate information not already available to the market will affect stock prices. The fact that empirical research has not been able to find a relation should ring an alarm bell, since a possible reason is that much climate information is not material.

Yet, despite such uncertain or illusory benefits, even the SEC acknowledges that the Proposal's costs will be very large and borne entirely by SEC registrants, mostly U.S.-listed companies and their shareholders. The Proposal estimates costs approaching an average of $1 million per company per year—and these estimates are low.

For example, the SEC recognizes that a major cost of the Proposal concerns litigation risk. But the Proposal suggests that costly lawsuits would be the result only for companies who fail to comply. In fact, however, detailed prescriptive disclosure rules like those proposed are magnets for lawsuits, including those that are frivolous or borderline. Such suits can cost $10 million or more each and produce scant or no benefits for either companies or society.

Worse, the Proposal ignores many other obvious and substantial costs altogether, including, including the costs of company certification and increased director compensation necessitated by the expanded personal liability and reputational risks; the costs of shrinking the pool of director candidates willing to serve under the greater risks; the costs of higher D&O insurance premiums, which are very likely given increased liability risks; and the opportunity costs of directors and officers meeting the prescribed managerial and procedural functions rather than performing value-added services such as business development, constituent relations, or networking and stewardship.

Given its high costs and scant benefits, the Proposal will continue to drive some companies into private equity rather than public markets. That impairs capital formation through public markets, contrary to the SEC's mandate and mission.[46] It also narrows the investment universe available to everyday American investors. Indeed, such a high cost for illusory benefit returns to the question which investors are demanding this information that the SEC is seeking to protect.

As the Proposal expressly acknowledges, the focus of large index funds is on the average market return, not on the profitability of specific companies, whereas individual investors care

[46] Securities Act § 2(b); Exchange Act § 23(a)(2); *see* Mark T. Uyeda: Remarks at the Going Public in 2020s Conference (May 3, 2023):

> To the extent that disclosures that are not financially material are added at the whims of the Commission, companies, over time, will face a collection of immaterial topics that will need to be disclosed and that will be subject to litigation. The costs to prepare such disclosure and defend any litigation will likely be passed on to the companies' investors in the form of lower investment returns or to their customers in the form of higher prices. Such costs may also disincentive private companies from going public. Moreover, the mere possibility that new, burdensome and immaterial disclosure requirements may be imposed in the future could similarly cause private companies to think twice about going public.

deeply about the profitability of each business they invest in. Passive index funds are largely indifferent to company-specific disclosure and immune to the danger of the SEC requiring excessive information overload; meanwhile, Main Street investors suffer an avalanche of information. The Proposal ignores differences between the interests of powerful institutional investors and everyday American investors and fails to delineate the different costs and benefits for each. This is another potential area for Subcommittee oversight.

4. Major Questions for Congress, Not SEC[47]

The Proposal is vulnerable to legal challenge under the major questions doctrine, as outlined by the Supreme Court in a pivotal opinion handed down during the quarter after the Proposal was released. In *West Virginia v. EPA*, the Court held that the Environmental Protection Agency (EPA) lacks authority under the Clean Air Act to limit GHG emissions from power plants through "generation shifting," *i.e.*, increasing the use of cleaner energy sources such as wind and solar and reducing the use of dirtier ones like coal.[48]

Although the case centered on the interpretation of the EPA's authority under the Clean Air Act, the Court's reasoning applies equally to other federal agency efforts to adopt significant new regulations, including possibly the Proposal. As a matter of oversight, the Subcommittee might ask the SEC about the lessons it has learned from the recent case, overall and for purposes of the Proposal.

The major questions doctrine is the principle that there are "extraordinary cases" where the "history and breadth" of the authority asserted and the "economic and political significance" of the assertion means that courts should hesitate before concluding that Congress meant to confer such authority.

In *West Virginia v. EPA*, the contours were elaborated in an instructive concurring opinion by Justice Gorsuch, joined by Justice Alito, making it clear that the Constitution vests Congress—not executive agencies—with "all legislative powers." Therefore, only Congress can make major policy decisions. Allowing federal agencies to interpret their authorizing statutes to assume broad powers by which to implement major policies of national significance undermines the separation of powers, the concurrence explained, by transferring legislative power from Congress to federal agencies.

Further, where Congress has chosen not to enact legislation providing an agency with explicit authority to adopt a new regulatory scheme, the major questions doctrine prevents agencies from bypassing Congress and simply adopting a broad, new reading of their authorities to enforce that policy on their own. In *West Virginia v. EPA*, for example, the Court noted that Congress had declined several times to pass carbon dioxide cap-and-trade legislation.

Applying the major questions doctrine to the Proposal reveals further doubt about the SEC's statutory authority. First, the Proposal is almost certainly one of "economic and political

[47] This section draws upon the Mayer Brown Legal Update, Supreme Court Decision in *West Virginia v. EPA* Casts Doubt on SEC's Climate Proposal and Other Regulatory Initiatives (July 7, 2022).

[48] For a summary of the case, see Mayer Brown, Supreme Court Limits EPA's Power to Regulate Greenhouse Gas Emissions from Power Plants (July 5, 2022). For other recent Supreme Court cases applying the major questions doctrine, see *Nat'l Fed. of Indep. Bus. v. OSHA*, 595 U.S. 109 (2022) (COVID vaccine mandate); *Biden v. Nebraska*, 143 S. Ct. 2355 (2023) (student loan forgiveness).

significance," as it would seek to change company behavior to focus more on GHG emissions and climate risk oversight.[49] In addition, Congress has repeatedly declined to enact legislation granting the SEC authority to require climate-related disclosures.[50]

Second, the SEC seeks not only to establish a new regulatory scheme requiring extensive disclosure by companies on a subject matter that the agency does not typically regulate, but in a divergence from historical practice, it is also proposing to require information to be provided that is not "material" to an average investor.

As a result, the courts should conclude that the SEC's policy objective is to impose environmental regulation through the guise of corporate disclosure. In doing so, the SEC would be acting (as the EPA did) by seeking a "fundamental revision of the statute, changing it from [one sort of] scheme of . . . regulation" into an entirely different kind than intended by Congress. The SEC would be circumventing the democratic process by assuming authorities that Congress has not voted to confer upon the agency.

5. Usurping State Corporate Law

Supporters of the Proposal say investors increasingly use climate information in their investment processes, that companies that fail to provide this information deprive investors of this capability, and that the SEC is therefore authorized to compel disclosure of such information for investor protection. They say investors take such an approach to evaluate the long-term viability of a company's business model, its adaptability to potential future regulation, and its susceptibility to reputational harm. Many say that investors perceive a connection between a company's climate practices and its economic performance.

However, it is beyond the SEC's authority to compel the creation and disclosure of any information for the purpose of inducing companies to modify their operational decision making in any way. That is the province of state corporation law, and not within the SEC's jurisdiction, as explained further below. Indeed, the SEC has never questioned the basic decision of the Congress that, insofar as investing is concerned, the primary interest of investors is economic.[51] Departures from this principle would require explicit Congressional authorization.[52]

Many advocacy groups the SEC cites for action make it clear that their passion on climate change leads them to want significant changes in behavior. Many champions of ESG generally are equally clear in their passion that corporations should not prioritize shareholder interests but treat

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[49] *Compare Alliance for Fair Board Recruitment et. al. v. SEC*, No. 21-60626 (5th Cir. Oct. 18, 2023) (putting outside the major questions doctrine an SEC-approved stock exchange disclosure rule concerning board diversity as not of requisite "economic and political significance").

[50] *See*, *e.g.*, H.R. 2570, The Climate Disclosure Act of 2021; H.R. 3623, The Climate Disclosure Risk Act of 2019; and S. 3481, The Climate Disclosure Act of 2018).

[51] *See* Securities Act of 1933 Release No. 5569 (February 11, 1975) & Securities Exchange Act of 1934 Release No. 5627 (Oct. 14, 1975):

> The SEC's experience over the years in proposing and framing disclosure requirements has not led it to question the basic decision of the Congress that, insofar as investing is concerned, the primary interest of investors is economic. After all, the principal, if not the only, reason why people invest their money in securities is to obtain a return.

[52] *National Association of Manufacturers v. SEC,* 800 F.3d 518 (D.C. Cir. 2015).

all stakeholders equally.[53] The Proposal provides a mechanism for implementing those advocacy groups' desired outcomes that they have not been able to accomplish through legislative changes.

The Proposal, a radical departure from current law, would require companies to disclose extensive climate-related risks that have little to do with firms' current financial outlook but serve an ulterior political purpose.[54] For instance, the Proposal prescribes a wide range of detailed disclosure requirements. These start with emissions and extend to a company's governance, strategy, business model and outlook, risk management targets and goals and climate-related financial statement metrics.[55] All such matters, while far afield from the information shareholders need for investment decision making, are extremely useful for advocacy groups' aims at influencing the behavior of corporations in which they have little, if any, economic stake.

But the SEC's mission does not include adopting positions intended to promote particular conceptions of acceptable corporate behavior. By law and tradition, that is the province of state corporation law, not federal securities law.[56] While a minority of critics have long sought to federalize corporate law by preempting state law, they have failed.[57] Those laws repose the power and duty to formulate corporate strategy in the board, not shareholders, and make boards accountable to shareholders above all other stakeholders. Courts defer to the business judgements that a board makes, including on matters of climate and their relationship to business.

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[53] *See* Ann M. Lipton, Not Everything Is About Investors: The Case for Mandatory Stakeholder Disclosure, 37 *Yale J. Reg*. 499, 532 (2020).

[54] *See* Ruth Jebe, The Convergence of Financial and ESG Materiality: Taking Sustainability Mainstream, 56 *Am. Bus. L. J.* 645, 669 (2019).

[55] The Proposal would require granular disclosure of governance and management practices, obviously intended to determine the substance of corporate behavior, which Congress has not authorized the SEC to undertake. Examples include disclosure of:

- "the processes and frequency by which the board or board committee discusses climate-related risks"
- "how the board is informed about climate related risks"
- "how frequently the board considers such risks"
- "whether and how the board or board committee considers climate-related risks as part of its business strategy, risk management, and financial oversight"
- "whether and how the board sets climate-related targets or goals and how it oversees progress against those targets or goals, including the establishment of any interim targets or goals"
- "whether certain management positions or committees are responsible for assessing and managing climate-related risks and, if so, to identify such positions or committees and disclose the relevant expertise of the position holders or members in such detail as necessary to fully describe the nature of the expertise"
- "the processes by which the responsible managers or management committees are informed about and monitor climate-related risks"
- "whether the responsible positions or committees report to the board or board committee on climate-related risks and how frequently this occurs"

Proposal at pp. 95-97. The Proposal says such disclosure would help:

> "an investor to understand whether and how the board or board committee considers climate-related risks when reviewing and guiding business strategy and major plans of action, when setting and monitoring implementation of risk management policies and performance objectives, when reviewing and approving annual budgets, and when overseeing major expenditures, acquisitions, and divestitures."

[56] *E.g., Santa Fe Industries, Inc. v. Green*, 430 U.S. 462 (1977).

[57] *See* Roberto Romano, The Genius of American Corporate Law (1993).

The Proposal reflects a different vision, one in which a subset of shareholders dictate corporate policy, corporate mission is geared to all stakeholders not primarily shareholders, and boards no longer enjoy deference to their business judgment. But the SEC has generally respected these longstanding boundaries and has been repudiated when it failed to do so.[58]

Supporters of the Proposal argue that concerns about SEC overreach are misplaced because the Proposal requires only disclosures. As one commentator expresses this point, the Proposal will not cap emissions, impose a cap-and-trade system, or force any company to shut down GHG-emitting factories.[59] Another letter notes that the Proposal does not require "particular governance structures to oversee climate risk, . . . carbon goals, [or] . . . a climate transition plan."[60]

All true. Nevertheless, the clear purpose (and certain effect) of these disclosures is to give third parties information for use in their campaigns to reduce corporate emissions, regardless of the effect on investors. The SEC itself discusses the efforts of non-profit climate change advocacy organizations as part of the background for the Proposal.[61] Those organizations:

- aim to prevent or alleviate climate change, not to protect investors;[62]
- use disclosures about transition plans, scenario analyses, internal carbon prices, and climate-related targets and goals to identify companies that aren't doing enough, in their opinion, to combat climate change; and
- pressure those companies to change operations in ways not required by existing U.S. environmental laws while pressuring institutional investors to support such changes.[63]

Imposing substantial costs on all public companies to prepare for a "potential transition to a lower carbon economy"[64] that Congress has not mandated—and may never mandate—will harm investors who prioritize financial returns over social goals. To be sure, the Proposal only facilitates, rather than requires, this result. As Commissioner Peirce's dissenting statement aptly concluded, the Proposal will put the SEC's weight behind "an array of non-investor stakeholders" demanding changes in company operations.[65] However, the SEC can and should—and the courts almost certainly will—consider predictable consequences when evaluating the Proposal's legality.

For a current analogy, consider the SEC's recently vacated rule compelling disclosures concerning share buybacks.[66] State law permits corporations to repurchase their shares[67] and

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[58] *Business Roundtable v. SEC*, 905 F.2d 406 (D.C. Cir. 1990) (dual class capital structures).

[59] Letter of John Coates p. 11 (June 2, 2022).

[60] Letter of Thirty Law Professors' Letter, p. 3 (June 6, 2022).

[61] Proposal, pp. 29-31.

[62] Besides the EPA, the most-cited entity in the Proposal is the Carbon Disclosure Project, as noted on page 3 above. Its website declares that the organization's purpose is "to act urgently to prevent dangerous climate change and environmental damage."

[63] Some have prescribed rules such as are contemplated by the Proposal precisely to influence corporate behavior. *See* Cynthia A. Williams, Fiduciary Duties and Corporate Climate Responsibility, 74 *Vand. L. Rev.* 1875, 1912 (2021).

[64] Proposed Rule 14-02(h) of Regulation S-X, Proposal, p. 471.

[65] Commissioner Hester M. Peirce, SEC, We are Not the Securities and Environment Commission—At Least Not Yet (March 21, 2022).

[66] *Chamber of Commerce v. SEC,* 85 F.4th 760 (5th Cir. 2023); *Chamber of Commerce v. SEC,* 88 F.4th 1115 (5th Cir. 2023).

[67] *E.g.*, 8 Del. C. §160(a); Mod. Bus. Corp. Act § 6.40.

leading investors have long explained how such buybacks can be a rational shareholder-friendly capital allocation decision.[68] Proponents of the stakeholder model of the corporation, however, criticize buybacks as harmful to workers or social equality and President Biden has made this a political priority.[69]

The SEC waded into this area with a rule to require companies to disclose the reasoning behind their repurchases. The Fifth Circuit Court of Appeals vacated the rule because the SEC failed to identify a problem within its jurisdiction to solve. As a matter of oversight, the Subcommittee might ask the SEC about the lessons it has learned from this case in terms of stating a proper purpose and measuring expected benefits, as well as responding to the public's comment letters, which the case also rebuked the SEC for failing to do.

6. First Amendment Problems

Governments in the United States may compel the disclosure of a wide variety of information, but there are limits under the First Amendment's "freedom of speech" clause. Long-settled precedent forbids regulatory agencies such as the SEC from compelling citizens, including officers and directors and corporate entities, from expressing views, other than those that are "purely factual and uncontroversial" and not otherwise "unduly burdensome."[70]

The SEC lost such a case about a decade ago after it adopted a rule requiring companies to disclose whether any minerals necessary to their products or those of third parties were sourced in the Democratic Republic of the Congo or an adjoining country.[71] If so, the companies had to inform the SEC of measures taken to assure that such minerals were untainted by the ongoing regional war—that they were "DRC conflict free."

In some ways, that "conflict minerals" rule is factual and non-controversial, because the minerals were or were not conflict free. But the Court held that the rule violated the First Amendment because the "conflict free" label conveyed a moral judgment implicated by the issues in the Congo war. The Court noted that the required speech was not related to preventing deception, which can provide a substantial government interest, but rather to advancing a humanitarian and foreign policy goal of the government. Therefore, the rule violated the First Amendment.

How the Proposal would fare under such a test is uncertain. In some ways, requiring emissions data is also factual and non-controversial, because the data are the data (assuming they can be reliably measured). But a court could easily hold that the Proposal violates the First Amendment because climate disclosure, particularly of third parties but even a company's own when not financially material to it, convey a moral or political judgment and that reducing emissions are a policy goal of the government. The court could likewise note the Proposal is not aimed at preventing deception either. Therefore, the Proposal could readily be held to violate the First Amendment.

A counterargument might be that it's not merely moral or political or controversial, because there is a scientific or professional consensus on the economic and social importance of climate

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[68] *See* Warren E. Buffett & Lawrence A. Cunningham, The Essays of Warren Buffett 133-139 (8th ed. 2023).

[69] *See* John Rekenthaler, President Biden's Stock-Buyback Tax Proposal, Morningstar (May 11, 2023).

[70] *See* Sean J. Griffith, What's "Controversial" About ESG? A Theory of Compelled Commercial Speech under the First Amendment, 101 *Neb. L. Rev*. 876 (2023).

[71] *National Association of Manufacturers v. SEC,* 800 F.3d 518 (D.C. Cir. 2015).

data and abundant investor demand for it. The rejoinder is this: the Proposal compels a political viewpoint that's controversial because the requirements are not based on a recognized or objective standard of materiality but on a novel and subjective view of what certain large institutional asset managers—and climate activists—say it's important for investors to know.

The rest of the mandatory securities law disclosure system hinges on some nexus between the information and what a reasonable investor would consider important. Fundamentals such as GAAP financial statements, MD&A and other content required in current and periodic reports and proxy statements are "purely factual and uncontroversial." Indeed, another federal circuit court recently rejected a First Amendment challenge to an SEC rule requiring a company to explain its share buyback rationales.[72] It is certainly reasonable to opine that such disclosure is akin more akin to GAAP financials than GHG emissions and the rest of the disclosure to be compelled under the Proposal.[73] While this vulnerability of the Proposal may not be as acute as others outlined in this testimony, it is a legitimate concern.

Conclusion

The comment letter other professors and I wrote on the Proposal in April 2022 had a considerable impact on the debate, shaping the arguments in many other comment letters.[74] The responses inspired our group to submit a second comment letter in June 2022 presenting areas of agreement and disagreement with certain other professors who had submitted responsive comment letters.[75] There we explained that proponents and opponents of the Proposal seem to agree on three things.

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[72] *Chamber of Commerce v. SEC*, 85 F.4th 760 (5th Cir. 2023); *Chamber of Commerce v. SEC*, 88 F.4th 1115 (5th Cir. 2023).

[73] Professor Griffith explains:

> Rules compelling commercial speech receive deferential judicial review, provided they are purely factual and uncontroversial. . . . Applied to securities regulation, the compelled commercial speech paradigm requires the SEC to justify disclosure mandates as a form of investor protection. . . . Disclosure mandates that are uncontroversially motivated to protect investors are eligible for deferential judicial review. Disclosure mandates failing this test must survive a form of heightened scrutiny. . . . The [Proposal] fail[s] to satisfy these requirements. Instead, the [Proposal] create[s] controversy by imposing a political viewpoint, by advancing an interest group agenda at the expense of investors generally, and by redefining concepts at the core of securities regulation. Having created controversy, the [Proposal is] ineligible for deferential judicial review. Instead, a form of heightened scrutiny applies, under which [the Proposal] will likely be invalidated.

Griffith, What's "Controversial" About ESG? 101 *Neb. L. Rev*. 876, 876-77.

[74] *E.g*., Harvey L. Pitt, *et al*. (June 17, 2022) (five former SEC officials, reprinted in *Harvard Law School Forum on Corporate Governance* July 1, 2022); Working Group on Securities Disclosure Authority (June 16, 2022) (32 professors and former SEC officials, reprinted in *Columbia Law School Blue Sky Blog*); Society for Corporate Governance (June 17, 2022). Some of these letters supported our letter and others challenged it; notably, a distinguished former SEC Chair, the late Harvey Pitt, signed one letter of each type (the first two cited above).

[75] Lawrence A. Cunningham, *et al*., Comment Letter of Law and Finance Professors on the Proposal on Climate-Related Disclosures for Investors (June 17, 2022), https://www.sec.gov/comments/s7-10-22/s71022-20132133-302619.pdf (engaging with comment letter from 30 law professors, on letterhead of Jill E. Fisch & George S. Georgiev, dated June 6, 2022, and comment letter from John Coates, dated June 2, 2022).

First, the SEC has broad statutory authority to require disclosures it believes are necessary for investor protection. Second, the relevant inquiry is whether a proposed disclosure requirement will protect investors, not whether it is material, although the two inquiries generally overlap. Third, the relevance of a disclosure requirement to a social issue or to non-shareholder constituents does not demonstrate, in and of itself, that it exceeds the SEC's authority.

Indeed, all seem agreed that the SEC's 2010 guidance regarding climate change disclosures (the "2010 Guidance") was a valid exercise of the SEC's statutory authority.[76] The 2010 Guidance reminded issuers that several elements of the existing disclosure framework, including disclosure of the material effects of compliance with laws and regulations,[77] material pending legal proceedings,[78] and material risk factors,[79] may require disclosures relating to climate change.

An analysis of the SEC's authority to adopt the Proposal must grapple with the substantial differences between it and the 2010 Guidance. A helpful framework is set out by one of the Proposal's supporters, Professor John Coates, a former Acting General Counsel of the SEC. The Coates framework distinguishes disclosures about the impact of *climate on a company* with disclosures about the impact of *a company on climate*.[80] This is a simple rubric for separating disclosures focused on investor protection from those focused on social goals.

The Proposal manifestly requires the second type of disclosure. A core element of the Proposal, one highlighted in the SEC's *Fact Sheet* accompanying the Proposal, is disclosure of GHG emissions.[81] This is a quintessential measure of a company's contribution to climate change. It is not a measure of the impact of climate change on the company, its results of operations, financial condition, or trends that may affect shareholders. The Proposal would require information about a company's impact on the environment, but not vice versa.

In sum, the Proposal is within the SEC's authority only if it will protect investors, as opposed to society, the environment, or other potentially worthy third parties. The SEC bases its affirmative conclusion largely on the advocacy of large institutional asset managers, government agencies, and non-governmental organizations seeking more climate-related information. To so shortchange everyday American investors is not within the SEC's statutory investor protection mandate.[82]

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[76] SEC, Commission Guidance Regarding Disclosure Related to Climate Change (February 2010).

[77] Regulation S-K, Item 101(c)(2)(i).

[78] *Id*. Item 103.

[79] *Id*. Item 105

[80] Coates, *supra*, p. 2 ("The focus of the [Proposal] is the impact *of climate change on companies, and not vice versa*") (emphasis in original).

[81] *See* Proposed Item 1504 of Regulation S-K, Proposal at 484-490.

[82] The following are some topics that this testimony would indicate are fruitful for potential Subcommittee oversight. The overall focus would be to evaluate the effects of these topics on the SEC's stated rationales for the Proposal, particularly its concept of "investor demand" and the statutory mandate of "investor protection." Consider whether the SEC has:

- conducted research into the preferences of individual investors, including their reasons for investing;
- reviewed survey data on such individual investor preferences or conducted its own;
- examined the flow of funds out of sustainable investment vehicles since the Proposal was issued;

- reassessed developments concerning shareholder proposals since the Proposal was issued, including the identities and purposes of those submitting them and the voting outcomes;
- probed conflicts of interest between large asset managers and their beneficiaries and assessed the potential losses to individual investors from self-interested voting or engagement by the asset managers;
- considered the different costs and benefits between individual investors versus other investor types, especially passive index funds, including their different needs and uses of mandatory disclosure information;
- reevaluated the Proposal given West Virginia v. EPA, the major questions case, which will require the SEC to show either that the Proposal does not raise a matter of significant policy or has been explicitly authorized by Congress;
- reevaluated the Proposal and its approach in response to Chamber of Commerce v. SEC, the case vacating a recent SEC rule for failing to identify a problem within its jurisdiction to solve, failing to analyze expected benefits properly, and failing to respond to public comments; and
- whether the SEC plans to open a new comment period for the Proposal, or any revision, given such developments, the passage of time, and/or comments received and considered on the Proposal.