



April 30, 2021

Via Electronic Mail

The Honorable Gary Gensler
Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: March 15, 2021 Statement Welcoming Public Input on Climate Change Disclosures

Dear Chair Gensler:

The University of Miami School of Law Investor Rights Clinic (“IRC”) appreciates the opportunity to offer input on the U.S. Securities and Exchange Commission’s (“SEC”) evaluation of the current rules and requirements regarding issuer disclosure of climate change-related information. The IRC supports the SEC’s efforts¹ to review and update disclosure requirements to better facilitate issuer disclosure of climate change-related information. Writing on behalf of our clients—unsophisticated, and often senior, investors who are untrained in deciphering opaque securities filings—the IRC advocates that any update to disclosure requirements include the reporting or provision of issuer-specific climate performance information which unsophisticated investors can easily comprehend and compare, ideally reduced to a standardized metric or rating promulgated by government agencies.

American investors’ increasing focus on climate-related issues in making investment decisions has significantly outpaced the development of disclosure standards regarding climate-related information for far too long. A comprehensive update to these disclosure standards would effectuate not only better climate performance but more efficient capital markets: the best tool in accelerating corporations’ shift to investing in green assets might well be investors discounting their securities’ valuations after learning more about those corporations’ climate risks. And while top-performing companies will be excited to advertise their greenness, those behind the lead pack will probably need mandated requirements to force such material information into public view. Although unpopular to implement, the increased transparency created by continuous mandated disclosures² will incentivize all issuers to improve their climate performance, preventing the race to the bottom currently under way.

¹ Commissioner Lee, Statement on the Review of Climate-Related Disclosure, Public Statement (Feb. 24, 2021).

² Cf. SEC Asset Management Advisory Committee, Potential Recommendations of the ESG Subcommittee (Dec. 1, 2020) [hereinafter ESG Recommendations] (“The impact of the current approach could be poor transparency with the potential to mislead investors in investment products, as well as poor disclosure of material risks to investors.”).

Increased transparency is generally good news for investors; increased disclosure of consistent, comparable, and reliable information regarding climate change generally appears good for the investing public as well. Yet at present day, many public companies' climate-related disclosures would appear not to "adequately inform investors" of "known material risks, uncertainties, impacts, and opportunities"³ stemming from the unabating warming of our environment and resulting increase in extreme weather events. While mitigating this inadequacy will require some extensively detailed disclosure requirements, the IRC remains steadfast that any disclosure framework or update must also feature the provision of consistent, comparable and reliable climate information that is easily comprehensible to unsophisticated investors.

I. Overview

As the only *pro bono* organization in Florida assisting investors of modest means, the IRC consistently encounters situations where unsophisticated investors struggled to decipher complex disclosure materials necessary to making informed investment decisions. The result is often a loss which might have been avoided had the investor received verbal explanation in plain language. This dynamic of unsophisticated investors lacking reliable, yet comprehensible information exists well beyond the IRC's securities arbitration work, extending across financial markets.

As the SEC considers updating disclosure requirements regarding climate information, the IRC would like to express its view that any update must include disclosure information that is simple and comparable enough for unsophisticated climate-minded investors to actually use in investment decisions. Further, the IRC believes that government development of a simple, standardized metric or rating communicating an issuer's climate performance would most effectively enable unsophisticated investors to incorporate climate criteria in investment decisions. Increased capital inflows to truly sustainable assets are integral to both the continued maintenance of fair, orderly, and efficient markets and the protection of investors from undisclosed climate risks; the SEC ought to do everything possible in helping unsophisticated investors join this inflow.

First, the IRC will highlight its concern that unsophisticated investors will be harmed by a climate change disclosure framework that produces only highly technical securities filing disclosures without simple, comparable, and reliable performance information. It is in the interest of those looking to achieve climate objectives—in addition to fair and efficient markets, more broadly—for any disclosure update to require the disclosure of both simple and technical metrics.

Second, the IRC will outline its support for the development of a standardized metric or rating that communicates a simple evaluation of each issuer's climate risk and response as an operating business. This discussion considers similar classification systems used in other contexts, all of which communicate technical analysis through a simple outcome, although administered through a range of public and private structures. These systems communicate an outcome that is simple to understand, allowing for easy comparison and reliability over time. Regardless of how a standardized climate performance metric or rating might be administered in

³ See Commissioner Lee, *supra* note 1.

practice, the examples mentioned demonstrate how increased government involvement in the assessment of a standardized rating can create optimal protection for consumers.

II. Climate Change Disclosure Reform Must Not Disadvantage Unsophisticated Investors

Over the years, unsophisticated investors have largely been denied opportunities to capture the early price appreciation pervasive in fast-growing markets featuring nascent technologies. As innovative tech companies, including but not limited to green tech companies, begin entering public markets relatively earlier,⁴ an improved focus on unsophisticated investor accessibility to public disclosures becomes increasingly effective for the purpose of facilitating the entire investing public's participation in such early-stage opportunities. While dense disclosures are generally a necessary evil of publicly offered securities, too much complexity without a practicable alternative inhibits much of the investing public's participation in the evaluative process. Any regulatory update involving climate change disclosures thus presents an inviting opportunity to provide access for unsophisticated investors who want to take their opportunity to make informed investments in this fast-growing yet under-developed sector of the public markets before technological development further drives price appreciation.⁵

Updating issuer reporting requirements regarding climate change disclosures will be a difficult and complex process with many stakeholders. The level of detail necessary to create a comprehensive reporting framework will likely result in technical standards packed with legal terms of art which communicate implied meanings not clear to the everyday investor. Accordingly, most investors will need some assistance decoding disclosure corporate-speak to discern greenwashing from genuine climate-related performance.⁶ Rules aimed to facilitate market participants' inclusion of climate information as a material investment factor will leave potentially enthusiastic participants (i.e., investors not trained in reading technical disclosure filings) behind if consistent, easy-to-comprehend climate disclosures are not required.⁷ Conversely, enabling those investors to begin utilizing climate performance as a primary investment criterion would help accelerate the shift to sustainable assets by further lowering the cost of capital for greener issuers. If the SEC hopes to maximize capital formation for green assets, facilitating unsophisticated climate-minded investors' participation by requiring clear and comparable climate information is necessary.

Moreover, without access to easy-to-understand climate performance data to inform personal investment decisions, many unsophisticated investors seeking exposure to the most

⁴ Yuliya Chernova, *Tech Startups Drop Stay-Private Mantra as Wall Street Beckons*, WALL ST. J. (Nov. 2, 2020), <https://www.wsj.com/articles/tech-startups-drop-stay-private-mantra-as-wall-street-beckons-11604313000>.

⁵ Claire Ballentine, *'Green tidal wave' lifts clean energy stocks with Biden plan*, BLOOMBERG NEWS (Apr. 8, 2021), <https://www.bloomberg.com/professional/blog/green-tidal-wave-lifts-clean-energy-stocks-with-biden-plan/>.

⁶ See generally ESG Recommendations, *supra* note 2, at 3 ("How [to] avoid 'greenwashing'" identified as area of concern by the ESG Subcommittee).

⁷ See Kenneth Pucker, *Overselling Sustainability Reporting*, HARV. BUS. REV., May 2021 <https://hbr.org/2021/05/overselling-sustainability-reporting> ("Even for consumers who care about sustainability issues and are dogged in their pursuit of sustainability information, CSR reports are often bewildering . . . Unlike with temperature or calories, consumers have no intuitive reference point that helps them understand many measures of environmental impact.").

climate-friendly and climate risk-responsive issuers may instead invest in managed products that employ subjective allocation criteria. These unsophisticated investors are then forced to pay the price for passing on the role of evaluating issuers' climate performance through the relatively higher fees charged across most climate-focused funds.⁸ Additionally, by helping individual climate-minded investors assume the evaluative role through the provision of digestible disclosure information, the portion of capital previously earmarked for fund management fees is instead directly invested in the sustainable assets themselves.

III. Government Development of a Reliable, Easy-to-Comprehend Metrics or Ratings Communicating Public Issuers' Climate Performance Would Most Effectively Enable Unsophisticated Investors to Participate in the Shift to Green Assets

The IRC supports either the SEC or another government entity creating a standardized metric or rating which categorizes an issuer's climate risk and corresponding response for all public issuers. Although nuance is lost with simplistic classification, the consistency and convenience of one assessment outcome regarding an issuer's climate performance would most effectively empower unsophisticated investors to incorporate climate criteria in their own investment decisions.

a. Key Characteristics of a Standard Climate Performance Metric or Rating

First and foremost, a standard climate performance metric needs to be *simple*. Simplicity includes both clearly observable denotations and a logical scale that makes intuitive sense to the investing public. A standardized metric would also need to be easily *comparable* to best facilitate individual investment decisions. Using a single metric allows for straightforward apples-to-apples comparisons, but at the expense of a more nuanced analysis that more sophisticated investors would likely seek out. Finally, a standard climate metric would have to be *reliable*. Government development and administration could help to quickly establish a uniform metric's pre-eminence, but those assessing the metric would likely need to demonstrate exceptional competency and thoroughness for an extended period of time to be considered truly reliable by market participants. The metric should also incorporate a diverse range of factors to ensure that it produces useful outcomes when applied to all different sorts of industries, in addition to limiting companies' ability to manipulate scores.

b. Comparing Analogous Ratings Systems and Public/Private Involvement

One example of a comparable sort of ratings system is the public and private mix currently in place for communicating car safety and performance evaluation. The National Highway Traffic Safety Administration sets standards on vehicle safety and administers crash safety tests, awarding five-point scores for both an overall rating and sub-categories,⁹ while the Environmental Protection Agency ensures the accuracy of manufacturers' fuel performance claims.¹⁰ Companies can be federally reprimanded for misrepresentations, yet there is still a role

⁸ Michael Wursthorn, *Tidal Wave of ESG Funds Brings Profit to Wall Street*, WALL ST. J. (Mar. 16, 2021), <https://www.wsj.com/articles/tidal-wave-of-esg-funds-brings-profit-to-wall-street-11615887004>.

⁹ NAT'L HIGHWAY TRAFFIC SAFETY ADMIN., <https://www.nhtsa.gov/ratings> (last visited Apr. 19, 2021).

¹⁰ U.S. DEP'T OF ENERGY, https://www.fueleconomy.gov/feg/how_tested.shtml (last visited Apr. 19, 2021).

for some private entities to issue supplemental performance and aesthetic ratings that many customers use to guide their vehicle purchase decisions.

Comparatively, bond markets offer a look at what can happen when the private sector is left to allocate an investment product's rating function itself: three primary market leaders developed, promulgating two unique letter-based rating systems applied to largely the same products (i.e. Moody's Aaa, Aa3, A3, Baa1, B3, and Caa2 ratings correspond to Fitch or Standard & Poor's AAA, AA-, A-, BBB+, B-, and CCC ratings).¹¹ Although bond market investors have learned to translate corresponding ratings over time, similar competition in the nascent climate performance ratings market could cause significant confusion, specifically among unsophisticated investors struggling to compare inconsistent metrics.

A final example of a comparable ratings system is the New York City Health Department's restaurant inspection program, where government officials conduct inspections to calculate a compliance score that is translated into an A, B, or C letter grade.¹² New York City's system produces a simple scaled outcome, allowing customers to make informed decisions regarding an important personal concern. Enough information is communicated that uninformed passersby can effectively incorporate it in their decision of where to eat. Increased transparency also encourages compliance on behalf of the restaurants too; customers will notice if a sign is not clearly displayed because they know to seek it out. The effectiveness of this general concept appears to result, at least in part, from proactive government involvement in its administration.

c. Increased Transparency for Unsophisticated Investors Will Accelerate Capital Flow Towards Green Assets

Much of the public input offered in response to Commissioner Lee's recent request¹³ will rightly be focused on developing an increasing amount of nuanced disclosure requirements related to climate information. Yet the promulgation of exclusively nuanced disclosure requirements may only benefit sophisticated investors able to understand both the technical statistics and dense securities law language involved. Imagine, for example, that issuers were required to disclose the exact amount of carbon they were responsible for emitting, along with the portion of next year's research and development budget that is allocated towards sustainable projects. Such specific data, while useful for professionals performing complex comparisons, would be too granular for an unsophisticated climate-minded investor to actually consider¹⁴ – a standardized metric or rating could instead take a variety of disclosed data points into account before arriving at an easy to see and easy to compare outcome. Most importantly, a single metric or rating that reliably encompassed several factors would be useful enough for unsophisticated investors to widely adopt, allowing the entire investing public to feel confident about incorporating climate performance in their investment decisions.

¹¹ *Bond ratings*, FIDELITY, <https://www.fidelity.com/learning-center/investment-products/fixed-income-bonds/bond-ratings> (last visited Apr. 19, 2021).

¹² *Food Establishment Inspections*, N.Y.C. HEALTH DEP'T, <https://www1.nyc.gov/site/doh/services/restaurant-grades.page> (last visited Apr. 19, 2021).

¹³ Commissioner Lee, Public Input Welcomed on Climate Change Disclosures, Public Statement (Mar. 15, 2021).

¹⁴ See Pucker, *supra* note 7 ("Even metrics that seem easy to grasp may cause confusion.").

d. Private Market Solutions are Developing, Often with Inadequate Protections for Unsophisticated Climate-Minded Investors

Private ratings services, such as MSCI,¹⁵ reflect the investing public's demand for accessible climate information not yet provided by federal regulators. Although these private market solutions can provide regulators a proof-of-concept highlighting the sort of functionality useful for just about all investors, they are often plagued by issues a government-promulgated system could effectively resolve. These include outlier outcomes and limited correlation between leading private ratings providers,¹⁶ resulting in complexity for market participants. Another common problem are measurements conflating climate risk and performance with other evaluative factors, such as the governance and social criteria commonly seen packaged together in popular Environmental, Social, and Governance funds and ratings. While increasingly demanded by all sorts of investors, climate-minded retail investors' sole reliance on ESG ratings can work to limit capital flows to more climate friendly issuers by misleading those investors into thinking a higher ESG rating ensures top climate performance. In total, although the private sector can certainly develop some useful solutions to help assess and communicate issuer climate performance, it cannot be counted on to always protect unsophisticated investors while doing so.

IV. Conclusion

The IRC is committed to assisting unsophisticated investors vulnerable to complex, inconsistent, and opaque disclosure practices. While we recognize that the SEC is primarily focused on reviewing and updating technical disclosure requirements regarding climate information, we urge the SEC to provide or require the disclosure of simple, consistent information which unsophisticated investors can easily compare and rely on. We further believe such information would be most effectively communicated in the form of a single government-developed metric or rating. Overall, facilitating the inclusion of unsophisticated investors in the shift to sustainable assets is both consistent with the SEC's mission and in the best interest of the market's overall health. Again, we thank the SEC for the opportunity to comment on its review of issuer requirements regarding disclosure of climate change information.

Respectfully submitted,

/s/ Zachary Tayler

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¹⁵ *ESG Ratings*, MSCI, <https://www.msci.com/our-solutions/esg-investing/esg-ratings> (last visited Apr. 19, 2021).

¹⁶ Florian Berg, Julian Koelbel, & Roberto Rigobon, *Aggregate Confusion: The Divergence of ESG Ratings* 2 (MIT Sloan Sch. Working Paper No. 5822-19, 2020) ("ESG ratings from different providers disagree substantially . . . This means that the information that decision-makers receive from ESG ratings agencies is relatively noisy.").