June 13, 2022

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549


Dear Ms. Countryman:

The American Securities Association\(^1\) submits this comment to raise our concerns with the above-referenced notice of proposed rulemaking (Proposed Rule).

The Commission has long required companies to disclose “material” information. Under this principles-based standard, companies disclose information that a reasonable investor would find important when deciding whether to purchase or sell a stock or how to vote as a shareholder. This standard protects investors by ensuring that they are not inundated with irrelevant information, and it helps companies and promotes capital formation by limiting the reach of burdensome, expensive disclosure requirements.

The Proposed Rule represents a dramatic and unwarranted turn away from this regime. The Commission is proposing to adopt a prescriptive approach to disclosures—one that mandates numerous disclosures the Commission alleges will protect the environment, not investors.

As described in more detail below, the rule (1) exceeds the Commission’s statutory authority, (2) is arbitrary and capricious, and (3) raises serious First Amendment concerns. As a result, the ASA urges the Commission to drop this rule and refrain from fundamentally transforming the securities laws in this way without express Congressional authorization.

I. The Commission Has No Statutory Authority to Adopt the Proposed Rule

As a federal agency, the Commission has “no power to act . . . unless and until Congress confers power upon it.”\(^2\) Because the Commission is a “creature of statute,” it has “no constitutional or

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1 The ASA is a trade association that represents the retail and institutional capital markets interests of regional financial services firms who provide Main Street businesses with access to capital and advise hardworking Americans how to create and preserve wealth. The ASA’s mission is to promote trust and confidence among investors, facilitate capital formation, and support efficient and competitively balanced capital markets. This mission advances financial independence, stimulates job creation, and increases prosperity. The ASA has a geographically diverse membership of almost one hundred members that spans every region of the United States.

common law existence or authority, but only those authorities conferred upon it by Congress.”

The Commission’s statutory authority “may not be lightly presumed.”

The Commission has no statutory authority to adopt the Proposed Rule. As an initial matter, nothing in the Exchange Act explicitly empowers the Commission to require climate-related disclosures. As important, the Commission has not adequately explained why current market practices regarding disclosure of climate-related risks are insufficient and warrant such intrusive regulatory action.

The Commission relies on its general power to impose disclosure requirements that are “necessary or appropriate in the public interest or for the protection of investors.” But it is “a fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme.” The Act’s disclosure provisions are not nearly as capacious as the Commission believes.

To begin, the use of the phrase “public interest” in a regulatory statute “is not a broad license to promote the general public welfare.” Instead, the phrase “take[s] meaning from the purposes of the regulatory legislation.” As a result, the Commission, in this instance, also has no freewheeling power to define and promote the “public interest.”

Nor will a court “presume that an agency’s promulgation of a rule is permissible because Congress did not expressly foreclose the possibility.” “Regardless of how serious the problem an administrative agency seeks to address . . . it may not exercise its authority in a manner that is inconsistent with the administrative structure that Congress enacted into law.” In other words, the Commission’s power to promulgate disclosure requirements is constrained by the “subject matter [of] the agency’s jurisdiction.”

Here, the Commission’s jurisdiction is well known. Congress “created the Securities and Exchange Commission as a special agency charged with the function of protecting the investing public.” In particular, the Exchange Act “was designed to provide investors with full disclosure of material information concerning public offerings of securities in commerce, to protect investors against fraud and, through the imposition of specified civil liabilities, to promote ethical standards of

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8 Id.; see, e.g., id. at 670 (“The use of the words ‘public interest’ in the Gas and Power Acts is not a directive to the Commission to seek to eradicate discrimination, but, rather, is a charge to promote the orderly production of plentiful supplies of electric energy and natural gas at just and reasonable rates.”).
9 New York Stock Exch. LLC v. Sec. & Exch. Comm’n, 962 F.3d 541, 546 (D.C. Cir. 2020) (citation omitted).
honesty and fair dealing.” To survive judicial review, then, the Proposed Rule must “protect[] investors” and “promote efficiency, competition, and capital formation.”

Unfortunately, the Proposed Rule has nothing to do with the Commission’s purpose or mission. Instead, the Proposed Rule is an environmental regulation, designed to force companies to adopt practices that will decrease their greenhouse gas emissions. While that may or may not be good policy, it is far afield from Congress’s charge to the Securities and Exchange Commission.

Even if the Exchange Act could be read to authorize certain environmental disclosures, it is inconceivable that Congress gave the Commission the type of sweeping power envisioned by the Proposed Rule. Courts “expect Congress to speak clearly if it wishes to assign to an agency decisions of vast economic and political significance.” There is a “clear statement” rule for major questions—Congress must clearly and expressly declare that the agency has rulemaking authority to address those questions, or the agency does not have that authority. As the court noted, Congress “does not . . . hide elephants in mouseholes.”

The Proposed Rule is no “‘everyday exercise of federal power.’” It is perhaps the most significant and sweeping change to corporate disclosure the Commission has ever proposed. It touches the lives of nearly every American and a vast array of regulated and unregulated companies.

The Proposed Rule “requires disclosure of: climate-related risks; climate-related effects on strategy, business model, and outlook; board and management oversight of climate-related issues; processes for identifying, assessing, and managing climate risks; plans for transition; financial statement metrics related to climate; greenhouse gas (“GHG”) emissions; and climate targets and goals.” These are monumental changes that will impose enormous financial costs on companies of all sizes, including private businesses that the Commission has no authority to regulate.

Nor would Congress ever have empowered the Commission to demand disclosures on a topic as politically sensitive as climate change. Under the Commission’s theory, it has near limitless authority to require disclosures on hot-button political issues—such as abortion, guns, immigration, and racial justice—if the Commission thinks doing so will be in the “public interest” or if politically favored investors with a certain amount of assets under management request such information.

And it is “especially unlikely that Congress would have delegated this decision to the [Securities and Exchange Commission], which has no expertise in” regulating greenhouse gas emissions. Indeed, a more logical federal agency—the Environmental Protection Agency (EPA)—is already regulating in this space through its Greenhouse Gas Reporting Program, which requires certain

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17 Id.
entities to disclose their greenhouse gas emissions. Yet, it appears the Commission has failed to recognize the EPA’s role on this topic or consult with the EPA in any manner.21

The Proposed Rule pushes the limits of federal power, which also casts doubt on its legality. Laws regulating ethical corporate behavior have long been the province of the States, and Congress has not sought to federalize this area of traditional State regulation. Without “a clear indication of congressional intent,” courts are extremely “reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities.”22 Because “Congress’ intent” must be “certain” before “federal law overrides the usual constitutional balance of federal and state powers,”23 the Commission cannot lawfully create a prescriptive climate regime until and unless Congress explicitly directs it to do so.

The Proposed Rule is a classic example of agency overreach. The Commission is proposing to aggressively push the boundaries of its authority to override the legislature’s failure or, in this case, refusal to act.

Agencies have no constitutional power to fill this space. Our constitution creates this separation of powers for a reason. As James Madison wrote in Federalist 47, “[t]here can be no liberty where the legislative and executive powers are united in the same person.” The Proposed Rule intentionally subverts the Constitution’s vesting of legislative power in Congress.

II. The Proposed Rule Is Arbitrary and Capricious

Under the Administrative Procedure Act (APA), “[f]ederal administrative agencies are required to engage in reasoned decisionmaking.”24 An agency rule is “arbitrary and capricious” if, among other things, the agency “fail[s] to consider an important aspect of the problem” or “offer[s] an explanation for its decision that runs counter to the evidence before the agency.”25 The Commission cannot satisfy these basic requirements of the APA.

A. The Proposed Rule Improperly Abandons the Commission’s Longstanding Principles-Based Approach to Disclosures

The Commission cannot show why its “existing regime” fails to provide “sufficient protections to investors.”26 Under Rule 10b–5(b), the Commission has long focused on the disclosure of “material” facts. The Commission defines “material” as limited to “those matters to which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to purchase the security registered.”27 This definition reflects the Supreme Court’s interpretation of “material” in TSC Industries v. Northway: “[T]here must be a substantial likelihood that the

22 Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 479 (1977).
26 Am. Equity Inv. Life Ins. Co. v. S.E.C., 613 F.3d 166, 179 (D.C. Cir. 2010).
27 17 C.F.R. §230.405.
disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information made available.”28 Under this principles-based approach, regulated entities determine on a case-by-case basis whether a “reasonable investor” would consider the disclosure relevant and important.

The Proposed Rule’s prescriptive approach, however, shifts the focus from what a “reasonable investor” would view as material under the specific circumstances to a standardized requirement, where the Commission (not public companies) determine what is important.

With good reason, the Commission has long rejected calls to create mandatory prescriptive disclosure standards. As opposed to prescriptive standards, which employ a one size fits all approach to disclosure, the Commission’s longstanding principles-based approach “provide[s] registrants with the flexibility to determine (i) whether certain information is material, and (ii) how to disclose such information.”29 As a result, the principles-based approach filters out immaterial information that would dilute material disclosures and make it more difficult for investors to make decisions.30

Additionally, the principles-based system “elicit[s] disclosure that is more in line with the way the registrant’s management and its board of directors monitor and assess the business” and therefore is “easier for registrants to prepare” and “provide[s] investors better insight into the decision-making process, current status, and prospects of the registrant.”31 This approach is particularly fitted to climate-related information because “the relevant information tends to vary greatly across companies” and “the more standardized prescriptive requirements are less likely to elicit information that is tailored to a specific company.”32 There is no legal basis that supports carving out the issue of climate for a prescriptive disclosure approach.

The Proposed Rule’s one-size-fits-all approach would also prevent the organic development of materiality standards to fit changing circumstances and market preferences. This is exactly why the Commission has refused to issue prescriptive standards. It is simply “impossible to provide every item of information that might be of interest to some investor in making investment and voting decisions.”33 Indeed, there have been more than “100 times” that the Commission has refused “to include societal issues as material.”34

30 Id.; see also Am. Securities Ass’n, Comment, File No. S7-11-19 (Oct. 25, 2019) (noting principles-based approach “rightly emphasizes that the quality—rather than volume—of disclosure is what ultimately matters to investors”).
32 Id. at 63,749; see also William Hinman, Dir. Corporation Finance, SEC, *Applying a Principles Based Approach to Disclosing Complex, Uncertain, and Evolving Risks* (Mar. 19, 2019), https://bit.ly/3IXTjPq (“As we approach [ESG] or other disclosure topics, I am always cognizant that imposing specific bright-line requirements can increase the costs associated with being a public company and yet not deliver the relevant and material information that market participants are seeking.”).
34 Id.
The Commission’s reliance on third-party standard setters for corporate disclosure is also a departure from historical practice and is plainly inconsistent with the Commission’s authority. Under the Proposed Rule, the Commission has effectively outsourced its responsibilities to organizations such as the Task Force on Climate-Related Financial Disclosures (TCFD), GHG Protocol, and the Sustainability Accounting Standards Board (SASB). These are privately funded non-governmental organizations with no legal or regulatory authority to set standards. Notably, the members of these organizations stand to profit handsomely if they are able to circumvent Congress and get the Commission to rubber stamp their agenda. There is simply no authority for the Commission to delegate the statutory mission it received from Congress to these self-interested partisan political organizations.

The Commission’s attempt to rewrite its own authority is alarming. “A central principle of administrative law is that, when an agency decides to depart from decades-long past practices and official policies, the agency must at a minimum acknowledge the change and offer a reasoned explanation for it.” The Commission cannot evade this responsibility by unilaterally deciding to “whistle past the factual graveyard” of its principles-based materiality disclosure standard.

For decades, companies have relied on the Commission’s principles-based approach. Yet the Proposed Rule never meaningfully considers this reliance. The Commission cannot ignore these serious reliance interests.

Simply put, the Commission’s principles-based approach already accomplishes much of what the Proposed Rule purports to seek. Rules cannot be “adopted in search of regulatory problems to solve; they are adopted to correct problems with existing regulatory requirements that an agency has delegated authority to address.” Climate-related financial risk that is “material” must already be disclosed. The Commission has not articulated why this current principles-based system is insufficient. The Proposed Rule is precisely the sort of solution in search of a problem that is incompatible with reasoned decision making.

B. The Commission’s Cost-Benefit Analysis Is Flawed

The Commission has a “unique obligation” under the Exchange Act to “consider the effect of a new rule upon efficiency, competition and capital formation.” Just last year, the Commission conducted a full cost-benefit analysis and determined that a principles-based approach had greater

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36 Am. Wild Horse Pers. Campaign v. Perdue, 873 F.3d 914, 923, 927 (D.C. Cir. 2017); see id. ("While the agency tries to whistle past that factual graveyard, the established pattern of agency conduct and formalized positions cannot be evaded."); see also Northwest Envtl. Def. Ctr. v. Bonneville Power Admin., 477 F.3d 668, 687, 690 (9th Cir. 2007) (invalidating an agency action because the agency “departed from its long-standing practice” and “two-decade-old precedent without supplying a reasoned analysis for its change of course”).
37 Id.
38 See Encino Motorcars, LLC v. Navarro, 579 U.S. 211, 222 (2016) (“A summary discussion may suffice in other circumstances, but here—in particular because of decades of industry reliance on the Department’s prior policy—the explanation fell short of the agency’s duty to explain why it deemed it necessary to overrule its previous position.”).
net benefits than a prescriptive approach. Because its recent reaffirmation of the principles-based approach rested on robust factual findings, the Commission must provide an even more robust analysis to explain its abrupt change in course. Specifically, when an agency’s “new policy rests upon factual findings that contradict those which underlay its prior policy,” it must “provide a more detailed justification than what would suffice for a new policy created on a blank slate.” As it relates to the Proposed Rule, the Commission has failed to do so.

The Proposed Rule also vastly underestimates the financial costs that will be borne by registrants. The Commission estimates that the direct costs will be between $490,000 and $640,000 for the first year of compliance and between $420,000 and $530,000 for subsequent years. These figures are almost certainly huge underestimates given the outside consulting and professional assistance from the ESG-Industrial Complex that the Commission admits companies will need.

The Commission also ignores the Proposed Rule’s impact on small business capital formation, which will bear a disproportionate brunt of the Proposed Rule. Imposing additional costs on small businesses will further entrench large companies in markets and create less competition and innovation. The Commission has a blind spot for this important distributional impact.

Given these high costs, the Proposed Rule would have to achieve outsized benefits to be justified. But it doesn’t come close. The Proposed Rule is driven by the idea that climate disclosures will “ultimately change the cost of capital for companies, rewarding outperformers, punishing laggards and creating a strong financial incentive for all to improve against ESG metrics.” But even those in charge of “responsible investments” know that there is “no compelling evidence” that such disclosures will achieve these benefits or have any impact on global temperatures.

C. The Proposed Rule Improperly Favors Asset Managers Over Investors

Under the Exchange Act, the Commission is charged with protecting investors, which are distinct from custodial asset managers. But the Proposed Rule plainly favors the input of the large asset managers, not to mention environmental groups and other activists. As Commissioner Peirce explains, “many calls for enhanced climate disclosure are motivated not by an interest in financial returns from an investment in a particular company, but by deep concerns about the climate or,
sometimes, superficial concerns expressed to garner goodwill.”⁴⁹ Elevating the interests of the Wall Street professional class over retail investors—who include retirees and working families—contradicts the entire spirit and purpose of the Exchange Act.

**D. The Proposed Rule Will Increase Liability Risks by Forcing the Use of Suspect Data**

The Proposed Rule ignores the serious liability that companies will face if the Commission forces it to do the impossible—namely, to accurately quantify Scope 3 emissions. Thus, the Proposed Rule will not actually lead to a disclosure regime that investors can rely on. Instead, it will lead to a regime in which some entities are shielded from liability if they can afford sophisticated Scope 3 emissions analyses and the remainder will be left with the impossible task of accurately reporting Scope 3 emissions. This is a litigation nightmare waiting to happen.

**E. The Commission’s Public-Interest Analysis Is Flawed**

The Commission’s public-interest analysis is flawed because it ignores broader concerns such as national security, the price of goods, and inflation. Specifically, the Commission has failed to tell the American public exactly how it plans to empirically prove its disclosures under the Proposed Rule will impact global temperatures, America’s reliance on foreign sources of energy, or the cost of food, gas, heat, and other goods and services American citizens need to live.

Additionally, the Commission never considers the impact of China, which is the world’s largest emitter of greenhouse gases. China and Chinese companies are an “important aspect of the problem” stemming from climate change, yet the Commission ignores them entirely.⁵⁰ Perversely, the Proposed Rule will advantage heavily emitting Chinese entities by making American companies less competitive.

**F. The Proposed Rule Creates New Burdens for Private Businesses that the Commission Has No Authority to Regulate**

The Proposed Rule would require that most issuers disclose information regarding Scope 3 emissions if that information is material to the company or the company has established an emissions reduction target. Mandating Scope 3 disclosure would in many instances require that private businesses who are customers, vendors, or part of a supply chain for public companies to collect, analyze, and report their emissions data in a standardized format to public filers.

This will result in thousands of privately owned businesses, including small businesses that have limited resources, having to comply with an enormously costly Commission mandate. However, the Proposed Rule and accompanying economic analysis make little mention of these costs and how they would affect businesses that the Commission has no authority to regulate. This is a fatal flaw of the Proposed Rule, and again, it highlights how the Commission has overstepped its authority.

⁴⁹ Peirce Statement.
III. The Proposed Rule Raises Serious First Amendment Concerns

The First Amendment protects the right to speak freely and, equally important, the right not to speak.\textsuperscript{51} Indeed, “[s]ome of the [Supreme] Court’s leading First Amendment precedents have established the principle that freedom of speech prohibits the government from telling people what they must say.”\textsuperscript{52} “Commercial speech is no exception.”\textsuperscript{53} While the Court has applied a lower level of scrutiny to laws that compel certain disclosures, this more lenient standard applies only to laws that explicitly require the disclosure of “purely factual and uncontroversial information.”\textsuperscript{54}

The type of disclosures required by the Proposed Rule are not “purely factual and uncontroversial information.” To the contrary, the rule is “directed at achieving overall social benefits” rather than “generat[ing] measurable, direct economic benefits to investors or issuers.”\textsuperscript{55} As a result, this is not the type of regulation than can escape First Amendment scrutiny.

By “compelling an issuer to confess blood on its hands,” the Proposed Rule “interferes with the exercise of freedom of speech under the First Amendment.”\textsuperscript{56} To be sure, “[r]quiring a company to publicly condemn itself is undoubtedly a more ‘effective’ way for the government to stigmatize and shape behavior than for the government to have to convey the views itself.”\textsuperscript{57} But that motivation “makes the requirement more constitutionally offensive, not less so.”\textsuperscript{58} The Commission should avoid adopting any rule that would raise such serious First Amendment concerns.

IV. Conclusion

For all of the reasons outline above, ASA opposes the Proposed Rule, and urges the Commissioners to carefully consider the consequences of using the securities laws in this way without express Congressional authorization.

Sincerely,

Christopher A. Iacovella

Christopher A. Iacovella
Chief Executive Officer
American Securities Association

\textsuperscript{53} Sorrell v. IMS Health Inc., 564 U.S. 552, 566 (2011).
\textsuperscript{55} NAM v. SEC, 800 F.3d 518, 522 (D.C. Cir. 2015).
\textsuperscript{56} Id. at 530.
\textsuperscript{57} Id.
\textsuperscript{58} Id. (emphasis added).