June 15, 2022

Vanessa A. Countryman,
Secretary,
Securities and Exchange Commission
100 F St., NE
Washington, D.C. 20549

Re: The Enhancement and Standardization of Climate-Related Disclosures for Investors, RIN 3235—AM87, File Number S7-10-22

Dear Ms. Countryman:

The Club for Growth Foundation's ("Foundation") core mission is to inform the general public about the many benefits of economic freedom and limited government, which benefits include prosperity and opportunity. We write out of concern that the proposed rule would depart from the statutory mission Congress has given the Commission and displace the workings of the free market, along the way engaging in arbitrary rulemaking in violation of the Administrative Procedure Act and irrationally imposing massive costs on the American economy, businesses, and workers.

The Foundation warmly supports the freedom of American investors to invest where and for whatever reason they wish, including to advance social and political causes in which investors believe. Such investment strategies are a time-honored practice that do credit to the generosity and public-spiritedness of American investors. But this proposal goes far beyond enabling such investment strategies.

To make any intelligent investment decision, a potential investor needs information about the enterprise in which he or she is considering an investment. Ordinarily, such an investor would acquire this information in the same way he or she would acquire any information from a potential contractual counterparty: by demanding the information as a condition of transacting. Just as an employer demands certain information from an employee before entering an employment contract, and just as a home buyer demands certain information from the seller

before entering a purchase agreement, investors can and do demand the disclosure of information relevant to their investment decision from companies in which they are considering investments. The remarkable growth of environmental, social, and governance ("ESG") disclosures in recent years is a case in point: many public companies have undertaken disclosures far above those required by law in response to growing demand from some investors, particularly institutional investors.

Of course, the making of disclosures is not cost-free; it can require considerable expenditures by the disclosing company, expenditures which may be passed on to the company's customers, investors, or both. Further, as the Supreme Court has recognized, too-extensive disclosures may overwhelm investors in information that most of them do not need or want and that may impede their evaluation of other vital information.[1] When potential investors seek information as a condition of investment, companies must weigh these and other considerations against the desirability of the funding that the potential investors offer. Just as in the context of employment or real estate transactions, a company will disclose information to a potential investor when the benefit of doing so outweighs the costs to the company (and thus to the company's shareholders, customers, and other stakeholders). The default position that investors must rely on free-market forces to obtain information thus prompts companies to make decisions about disclosures that promote the net benefit of society.

In the Securities and Exchange Acts (the "Acts"), Congress decided to compel the disclosure of information material to financial risks and returns as a condition of entering the public capital markets. It is easy to see why: unlike other sorts of information, which may be of interest only to some investors, information necessary to evaluate the risks and returns of an investment is *always* relevant to *all* investors. That is because no matter what their other reasons for investing may be, all investors care about the value of their investments. Moreover, inaccurate information about risks and returns can lead to systemic instability of the sort that roiled U.S. financial markets in 1929 and precipitated the Great Depression, the prevention of which was one of the principal goals of the Acts.[2] The Acts do not displace the free market; rather, by preventing manipulation of the prices of securities, the Acts establish important preconditions for the workings of the market; they aid rather than displace it.

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[1] *TSC Indus. v. Northway, Inc.*, 426 U.S. 438, 448-49 (1976).

[2] *See generally Stock Exchange Practices: Report of the Committee on Banking and Currency* (June 16, 1934).

The Supreme Court has long interpreted the Acts in light of Congress's objective of guaranteeing disclosure of financially material information, while allowing investors to seek other information through the normal processes of the free market. The Court has explained that the Acts embody "a legislative philosophy … of full disclosure."[3] Writing in the Rule 10b-5 context, the Court explained that the standard for such disclosure is whether there is "a substantial likelihood that the disclosure ... would … [be] viewed by the *reasonable investor* as having significantly altered the 'total mix' of information made available."[4] The question of whether information would be material to a reasonable investor "is an objective one."[5] That is to say, it does not turn on the subjective desires of particular investors for particular information. Rather, the question is whether an investor abstracted from his or her subjective, particular preferences would find the information at issue relevant. The only information that fits that description is information relevant to risks and returns, for that is the only thing that all investors care about.

Any other position would leave the Commission with unbounded discretion to select the information that companies must disclose. When guided by the polestar of financial materiality, the Commission's regulations can play an important role in carrying out Congress's objective of ensuring honest and efficient capital markets. But without this guidance, the Commission would lack a statutory "intelligible principle" for its disclosure mandates and would thus find itself in the unconstitutional position of legislating rather than implementing Congress's legislation.[6]

The Commission's proposal departs from the mission given it by Congress in the Acts and the intelligible principle that renders its rulemaking constitutional. It is clear that much of the information that the proposal deems material is not material at all, but we need not rely on that fact, for the proposal by its terms *decouples its disclosure mandates from the materiality standard*. We can see this most easily with respect to the proposal's demand for disclosure of GHG emissions. The proposal demands that registrants disclose scopes 1 and 2 emission information; it also demands scope 3 information, but only if that information is material.[7] Thus

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[3] *Basic v. Levinson*, 485 U.S. 224, 230 (1988).

[4] *Id.* at 231-32 (emphasis added; internal quotation mark omitted).

[5] *TSC Indus.*, 426 U.S. at 445.

[6] *Whitman v. Am. Trucking Ass'ns., Inc.*, 531 U.S. 457, 472 (2001).

[7] 87 Fed. Reg. 21334, 21374 (2022).

it is clear that the materiality limitation of scope 3 does not apply to scopes 1 and 2; registrants must disclose scopes 1 and 2 information regardless of whether it is material.[8]

As its justification for departing from the foundational principle of the Acts, the Commission cites the subjective interests of some investors in obtaining the information that the proposal would require to be disclosed.[9] In the first place, the Commission has no business considering such demands rather than the objective needs of a reasonable investor per the Supreme Court's longstanding case law; the Commission's reliance on irrelevant subjective investor demands would render a finalized version of the proposal arbitrary and capricious.[10]

Even if the Commission were right to consider subjective investor demands, it fails to show that the proposal is necessary to meet those demands. As we explained above, the free market *already* provides investors with the ability to demand the information they seek from potential recipients of their investments. And many investors, especially institutional investors, have taken advantage of the leverage that market forces provide to demand some of the information that the proposal would mandate. The proposal fails to explain why this free-market solution is inadequate. To be sure, the free market may not give every investor all the climate-related information he or she wants. But that leaves him or her no worse off than every other investor who seeks information that is not financially material. A rule that fails to demonstrate a problem to which it is a needed response is arbitrary and capricious.[11]

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[8] If any doubt remained, it would be removed by the proposal's Question 98, which asks whether the materiality limitation for scope 3 emissions disclosures is appropriate, or if the Commission should "instead require the disclosure of Scope 3 emissions for all registrants, regardless of materiality." *Id.* at 21381. The Commission thus reveals that it does not believe itself bound by the materiality limitation and also that the absence of any materiality limitation with respect to the disclosure of scopes 1 and 2 information means that such information must be disclosed "regardless of materiality." *Id.*

[9] *See, e.g.*, 87 Fed. Reg. at 21337.

[10] *See, e.g.*, *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) ("an agency rule would be arbitrary and capricious if the agency has relied on factors which Congress has not intended it to consider").

[11] *See, e.g.*, *Alltel Corp. v. FCC*, 838 F.2d 551, 561 (D.C. Cir. 1988).

The proposal thus chooses to privilege investor demand for non-material climate-related information over demand for other sorts of non-material information—but it never gives a reason for that choice. Investors may desire all sorts of information about a company in which they are considering investment. For instance, religious investors may wish for assurance that the company does not engage in any practices or offer any goods or services that the investors would consider immoral. Other investors may wish to know that the company does not do business with regimes that they consider wicked. The proposal does not conclude that, or even ask whether, more investors wish for non-material climate-related information than would welcome non-material information of other sorts. Absent such a conclusion, the proposal's singling out of climate-related information for special treatment is irrational and therefore arbitrary and capricious.[12]

Similarly, even assuming that some of the information the proposal would demand is material, the scope and detail of its disclosures far exceed the requirements for other material information. As one among many possible examples, consider information about the COVID-19 pandemic. The pandemic has profoundly affected every economy of the world and millions of businesses, but the proposal does not create a special disclosure regime for information about it notwithstanding its proven materiality. The Commission nowhere asserts that climate-related information is likely to be more material, or material to more registrants, than information about the COVID-19 pandemic or other events of obvious materiality, such as wars or inflation. This irrationally preferential treatment for climate-related information is arbitrary and capricious.

The proposal illustrates the wisdom of leaving the disclosure of non-material information to the workings of the free market, for it would impose just the type of undue costs that the free market is meant to prevent. Even the Commission admits that the proposal would be fantastically costly. It would *more than double* the cost of complying with the SEC disclosure requirements it would amend, in terms of both expenditure and employee hours.[13] These costs would be passed on to customers, investors, or both; they would in effect amount to a subsidization of investors who wish for additional climate-related disclosures by investors who are not interested in such information and by the customers of registered companies. Yet extraordinarily, the Commission never finds that the benefits it asserts the proposal would

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[12] If the Commission finalizes the proposal, it must explain its preferential treatment of climate-related information or accord similar treatment to all other similarly-situated information.

[13] *See* 87 Fed. Reg. at 21461.

achieve are worth these massive costs. Indeed, the Commission never even asks if the proposal's costs are worth its benefits—that is to say, never asks whether its proposal will do more good than harm. The failure to ask and answer that basic question is textbook arbitrariness.[14]

This arbitrariness is compounded by the proposal's failure to account for the most important costs it would impose: costs to the operations of businesses in every economic sector and on the workers, families, and communities who depend on these businesses. By increasing the prevalence and salience of climate-related information, the proposal would drive up the cost of capital for certain businesses that investors may deem "climate-exposed" or less environmentally conscious than competitors. This increased cost would likely have profound effects across the economy, as would the efforts of companies to keep down their cost of capital by undertaking new "greener" business strategies. The proposal admits its potential to change the way businesses operate.[15] Yet, it never seeks to measure its effects on these businesses or on their workers. The Administrative Procedure Act squarely forbids the proposal's attempt to disregard its most important effects.

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For the foregoing reasons, the Club for Growth Foundation urges the Commission to decline to finalize the proposal and instead to publish a notice withdrawing the proposal from consideration.

Sincerely,

David McIntosh
President
Club for Growth Foundation

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[14] *See Michigan v. EPA*, 576 U.S. 743 (2015).

[15] *See* 87 Fed. Reg. at 21447-48.