Davis Polk

Davis Polk & Wardwell LLP
450 Lexington Avenue
New York, NY 10017
davispolk.com

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Re: *The Enhancement and Standardization of Climate-Related Disclosures for Investors*
Release Nos. 33-11042; 34-94478
File No. S7-10-22

Ms. Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington D.C. 20549-1090

Dear Ms. Countryman:

We are submitting this letter in response to the Commission's request for comment on its proposal, *The Enhancement and Standardization of Climate-Related Disclosures for Investors*.

Climate change is a defining issue facing the country and addressing it requires concerted action from both the public and private sectors. For this reason, numerous companies have made commitments to their shareholders, employees, customers, business partners and communities to conduct their activities in ways that reduce or offset their carbon footprint, and to voluntarily report on their greenhouse gas ("GHG") mitigation efforts.

Climate change affects the capital markets as part of the broader financial system and national economy. But the significance of climate change risk does not mean that each federal regulatory agency has plenary authority to mitigate or require information about the impact of climate change. The Federal Trade Commission does not, for example, have authority to block mergers when the parties fail to commit to GHG reduction targets that the agency considers warranted. The Food and Drug Administration does not have authority to withhold approval for a new therapeutic on grounds that its manufacturer has not quantified the CO_2 emissions impact of production and distribution. And the Commission does not have authority to impose costly and complex disclosure burdens on public companies that are untethered from the concept of meaningfulness to investors, or what is embodied in the basic principle of materiality.

A fundamental Constitutional premise is that each Executive Branch agency must work within the bounds of authority that Congress has provided to it. And of course there is an agency to whom Congress has delegated authority for protecting the environment: the Environmental Protection Agency.[1]

Mandatory Greenhouse Gas Reporting, 40 CFR Part 98, commonly referred to as the Greenhouse Gas Reporting Rule, requires reporting by large GHG emission sources, fossil fuel suppliers, industrial gas suppliers and facilities that inject CO_2 underground for sequestration, enhanced oil and gas recovery or other purposes. The EPA promulgated the Greenhouse Gas Reporting Rule pursuant to a 2008

[1] *See* Env't Prot. Agency, *The Clean Air Act in a Nutshell: How It Works,* 19 (2013), https://www.epa.gov/sites/default/files/2015-05/documents/caa_nutshell.pdf.

Congressional mandate to "develop and publish a . . . rule . . . to require mandatory reporting of greenhouse gas emissions above appropriate thresholds *in all sectors of the economy*."[2]

The Commission does not have comparable unbounded authority from Congress to impose uniform climate change disclosure obligations on all companies who have sought, or are seeking, access to the public capital markets. Its authority must instead be found in the Securities Act of 1933 (as amended, the "Securities Act") and the Securities Exchange Act of 1934 (as amended, the "Exchange Act")—laws that, as the Commission explains on its website, "require that investors receive financial and other significant information concerning securities being offered for public sale" and require the "disclosure of important financial information through the registration of securities," and which therefore "enable[] investors, not the government, to make informed judgments about whether to purchase a company's securities."[3]

While the Commission's proposal cites multiple well-publicized examples of investor requests for climate risk disclosure, nowhere does it explain that a *reasonable investor* in *each* publicly traded company in the United States needs information with the granular level of detail called for by the proposal to make informed investment decisions. The proposing release elides this basic problem by focusing on the needs of institutional investors managing portfolios of investments:

> Further, we understand investors often employ diversified strategies, and therefore do not necessarily consider risk and return of a particular security in isolation but also in terms of the security's effect on the portfolio as a whole, *which requires comparable data across registrants*.[4]

This is a remarkable departure from the approach that has until now governed required public company disclosures. We are not aware of a prior mandate to disclose information that is concededly irrelevant to an investment in a particular company's securities on the basis that some investors would like comparable data across all companies in their portfolio. If this were accepted grounds for rulemaking, the Commission could long ago have required companies to provide any information that any investor requests, regardless of burden.

That is not, and has never been, the law. "The mission of the SEC is to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation."[5] Capital formation cannot be facilitated without regard to regulatory costs, and when information is not material to an investment in a particular company's securities, requiring the company to bear anything more than a *de minimis* burden to produce it is difficult if not impossible to justify.

Yet, unlike the Greenhouse Gas Reporting Rule promulgated by an agency empowered with an express Congressional mandate, the Commission would require each publicly traded company, regardless of industry or business model, to disclose:

- the company's total Scope 1 and total Scope 2 emissions, *regardless of materiality*, after calculating them from "all sources" that are included in the company's "organizational and

[2] Consolidated Appropriations Act, 2008, Pub. L. No. 110–161 (2007) (emphasis added).

[3] SEC, *The Laws That Govern the Securities Industry*, Investor.gov, https://www.investor.gov/introduction-investing/investing-basics/role-sec/laws-govern-securities-industry.

[4] *The Enhancement and Standardization of Climate-Related Disclosures for Investors*, 17 CFR §§ 210, 229, 232, 239, and 249 at 9 (proposed Mar. 21, 2022) (emphasis added) ("Proposing Release").

[5] SEC, *About the SEC*, https://www.sec.gov/about.shtml.

operational boundaries"—a vague and confusing construct without precedent in the federal securities laws,

- the company's[6] total Scope 3 emissions, *regardless of materiality*, if the company "has set a GHG emissions reduction target or goal that includes its Scope 3 emissions"—an objective that need not be publicly announced in order to trigger mandatory immaterial Scope 3 emissions disclosures, but that could be as simple and laudable as a company's decision to look for ways to reduce its carbon footprint,

- a *1% impact on each line item* in the company's audited consolidated financial statements from "severe weather events and other natural conditions," such as flooding, drought, wildfires, extreme temperatures, and sea level rise—a disclosure threshold divorced from generally accepted materiality standards that conflates climate change with all weather-related events, and which would require categorizing and measuring information that most companies' internal controls are not configured to identify, and

- any climate-related risks reasonably likely to have a material impact on the company that "may manifest" over the "long term"—which the proposal does not define but suggests could be *as long as 30 to 50 years*—categorizing such risks as "physical" or "transition," and "acute" or "chronic," and listing, among other things, the ZIP codes and square footage of the affected "properties, processes, or operations"—a Domesday Book of corporate assets and operations that could not be remotely useful to the shareholders of many, if not most, public companies.

With a Congressional directive to develop GHG reporting standards for *all sectors of the economy*, the EPA nevertheless focused its regulatory burden on carbon-intensive activities. Here, the proposal's refusal to distinguish between industries and business models, its multiple obligations to provide information that the proposal itself concedes is immaterial to investment decisionmaking, and its undifferentiated approach to mandating this disclosure from all public companies, all but ensures—

- years of litigation challenging the Commission's authority to promulgate the proposed suite of rules under the Securities Act and the Exchange Act,

- years of litigation questioning the Commission's cost-benefit justifications undertaken pursuant to the Exchange Act, the Administrative Procedure Act of 1946 (as amended, the "APA"), the Regulatory Flexibility Act of 1980, the Paperwork Reduction Act of 1995 and the Small Business Regulatory Enforcement Fairness Act of 1996, and

- years of litigation objecting to disclosures compelled by the rules in the absence of express Congressional authority as both violating the free speech guarantees of the First Amendment[7] and implicating the major questions doctrine.[8]

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[6] This obligation would not apply to a smaller reporting company. *See* Proposing Release at 210.

[7] *See Nat'l Ass'n of Mfrs. v. SEC*, 748 F.3d 359 (D.C. Cir. 2014) (vacating in part an SEC rule compelling commercial speech upon the Court's application of elevated First Amendment scrutiny).

[8] *See Nat'l Fed'n of Indep. Bus. v. OSHA*, No. 21A244, slip op., at 3 (U.S. 2022) (Gorsuch, J., concurring) ("The federal government's powers, however, are not general but limited and divided." (quoting *McCulloch v. Maryland*, 4 Wheat. 316, 405 (1819))) ("Not only must the federal government properly invoke a constitutionally enumerated source of

The variety and weightiness of potential legal objections to the proposal raises the significant possibility that, in the end, the Commission's long-awaited rulemaking on the topic of climate change will be invalidated by the federal courts. In the meanwhile, we expect that many of the requirements outlined in the proposal, if adopted and not stayed pending final judicial resolution—

- will impose heavy costs on all public companies as they rush to hire staff and outside consulting firms whose highly specialized expertise will be required to gather newly reportable data and build processes for compliance—an extraordinary implication of the proposal to which the Commission nods only in passing,[9]

- will discourage new entrants from accessing the U.S. public capital markets because of the significant increase in regulatory compliance costs, and

- will cause some currently public companies, for the same reasons, to withdraw from these markets entirely.

This predictable set of outcomes is not one we believe will serve the interests of U.S. investors, our economy or the country more generally.

We believe the better course would be for the Commission to withdraw the proposal and instead formulate climate risk disclosure requirements that are tailored to investor decisionmaking and would therefore be more squarely located within its statutory authority.

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The Commission has general authority to require public companies to disclose information that is "necessary or appropriate in the public interest or for the protection of investors."[10] In doing so it must consider whether a disclosure mandate will "promote efficiency, competition, and capital formation."[11] While the Commission's remit from Congress is therefore broad, it is not legislative in character.

Because the Commission has been entrusted by Congress to safeguard investors and our national market system but not to serve as a general-purpose referee of what information should be in the public domain, the touchstone for public company disclosure requirements not specifically mandated by Congress is

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authority to regulate in this area or any other. It must also act consistently with the Constitution's separation of powers. And when it comes to that obligation, this Court has established at least one firm rule: 'We expect Congress to speak clearly' if it wishes to assign to an executive agency decisions 'of vast economic and political significance.'" (quoting *Alabama Assn. of Realtors v. Dep't of Health & Hum. Servs.*, No. 20A169, slip op., at 6 (U.S. 2021) (per curiam))) ("We sometimes call this the major questions doctrine." (quoting *Gundy v. United States*, No. 17-6086, slip op., at 20 (U.S. 2019) (Gorsuch, J., dissenting))).

[9] The Commission "recognize[s] that determining the likely future impacts on a registrant's business may be difficult for some registrants. Commenters have noted that the science of climate modelling has progressed in recent years and enabled the development of various software tools and that climate consulting firms are available to assist registrants in making this determination." *See* Proposing Release, *supra* note 4, § II.B.2 (citing letters from AIR Worldwide (June 11, 2021); Coastal Risk Consulting (May 3, 2021); CoreLogic (June 12, 2021); Datamaran (June 14, 2021); Dynamhex, Inc. (June 15, 2021); EC-Map (June 12, 2021); FutureProof Technologies, Inc. (June 7, 2021); and right.based on science GmbH (June 12, 2021)).

[10] *See, e.g.*, Securities Act, 15 U.S.C. § 77g; Exchange Act, 15 U.S.C. §§ 78l, 78m, 78o.

[11] Securities Act, 15 U.S.C. §§ 77b(b), 78c(f), 80a-2(c).

investment materiality.[12] This is, of course, consistent with the fact that disclosure liability under the Securities Act and the Exchange Act is limited to *material* misstatements and omissions of information.[13] It is also consistent with a regulatory approach designed to encourage companies not to "bury the shareholders in an avalanche of trivial information."[14]

We believe the proposal, if adopted, would depart from longstanding principles of materiality while imposing heavy compliance costs, and therefore likely exceed the Commission's authority from Congress under the Securities Act and the Exchange Act.

The Supreme Court has explained that information is "material" if "there is a substantial likelihood that a reasonable shareholder would consider it important" in making an investment decision. Put another way, "there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[15] A "reasonable investor" is someone whose interest is in a financial return on their investment in the company making the disclosure,[16] and not a citizen concerned, however validly, with how individual actors in the national and global economies are confronting the challenges posed by anthropogenic climate change.

Therefore, if information is not "significant to the reasonable investor's trading decision,"[17] the Commission's authority to require its public disclosure is on a weak footing, particularly where the costs of such disclosure may adversely impact efficiency, competition and capital formation by diverting a company's scarce managerial and financial resources to production of the immaterial but mandatory disclosure.

In a May 2021 speech, a commissioner stated that it is a "myth" that "SEC disclosure requirements must be strictly limited to material information."[18] It is correct that the Commission's statutory rulemaking basis does not on its face reference the concept of materiality. But it is equally the case that companies do not have liability under Sections 11, 12 or 17(a)(2) of the Securities Act or Rule 10b-5 under the Exchange Act for misstatements or omissions that are not material, even if the misstated or omitted information is required by SEC rules.[19] Likewise, Section 23(a)(2) of the Exchange Act prohibits the Commission from adopting any rule that would impose a burden on competition not necessary or appropriate *in furtherance of the purposes of the Exchange Act*[20]—not, it must be emphasized, in furtherance of every goal that the Commission or the Executive Branch determines to be in the national interest.

[12] *See* David A. Katz & Laura A. McIntosh, *Corporate Governance Update: "Materiality" in America and Abroad*, N.Y.L.J., Apr. 28, 2021 (asserting that "the concept of materiality is a bedrock feature of American securities law and regulation" and investors who are interested in obtaining information that is not generally "decision-useful" to "the average prudent investor" have "other ways" to obtain it.).

[13] *See* Securities Act, 15 U.S.C. §§ 77k, 77l; 17 CFR § 240.10b-5 (2022).

[14] *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 448–49 (1976).

[15] *Basic, Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988) (quoting *TSC Industries*, 426 U.S. at 449).

[16] *Id.*

[17] *Basic*, 485 U.S. at 231–32, 240; *see also* Exchange Act, 17 CFR § 240.12b-2 (providing definition of "material").

[18] *See* Commissioner Allison Herren Lee, Keynote Remarks at the 2021 ESG Priorities Event, Living in a Material World: Myths and Misconceptions about "Materiality" (May 24, 2021) (transcript available at https://www.sec.gov/news/speech/lee-living-material-world-052421).

[19] *See* Securities Act, 15 U.S.C. § 77k, § 77l; Exchange Act, 17 CFR § 240.10b-5.

[20] *See* 15 U.S.C. 78w(a)(2).

And so a balance must be struck—while materiality may not be an express textual requirement for the Commission's rulemaking, the proposition that the Commission possesses unlimited authority to require the production and disclosure of information immaterial to an investment decision regarding a company's securities, regardless of cost to the company and the resulting impact on efficiency, competition and capital formation, would be equally mythical.

Although there are examples of bright-line disclosure requirements that do not have express materiality qualifiers,[21] these are fairly simple and inexpensive for companies to track and report, and are thus exceptions that prove the rule. By contrast, the proposal re-conceptualizes the traditional understanding of what companies are obligated to disclose in significant respects, including those we discuss below.

- ***Disclosure of "climate-related risks" would be required even when such risks are not material to current investment decisionmaking***. Under the proposal, climate-related risks are defined as "the actual or *potential* negative impacts of climate-related conditions and events on a registrant's consolidated financial statements, business operations, or value chains, as a whole" and narrative disclosure is required for "*any* climate-related risks reasonably likely to have a material impact on the registrant, including on its business or consolidated financial statements, which may manifest over the short, medium, and long term."[22]

  Traditional concepts of materiality require a "balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event."[23] In contrast, the proposal specifically directs companies to assess the impact of any climate-related risk over the short, medium and long term—with the suggestion that this time horizon may extend up to 50 years.[24] The proposed disclosure requirement thus departs from traditional materiality by introducing a novel temporal dimension not tied to a reasonable investor's investment decision, which focuses on the present discounted value of any particular risk.

  Indeed, it is difficult to see how a company would be able to rule out the possibility of a material impact from climate change on *any* of its properties, processes and operations over a time horizon as long as 50 years, meaning that the proposal seems to call for precise geographical disclosures about all of a company's physical operations—exactly the opposite of the kind of laundry-list disclosure that the Commission otherwise explicitly warns companies not to disclose in SEC filings.[25] Similarly, the requirement conflicts directly with the *Commission Guidance Regarding Disclosure Related to Climate Change*, published in 2010, cautioning that companies "should focus on material information and eliminate immaterial information that does not promote understanding

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[21] *See* Herren Lee, *supra* note 18.

[22] *See* Proposing Release, *supra* note 4, § II.B.1; § VIII (emphasis added).

[23] *Basic*, 485 U.S. at 238 (citing *SEC v. Texas Gulf Sulphur Co*., 401 F.2d 833, 849 (2d Cir. 1968). *See also Commission Guidance Regarding Disclosure Related to Climate Change*, Release Nos. 33-9106; 34-61469; FR-82, 18, available at: https://www.sec.gov/rules/interp/2010/33-9106.pdf ("2010 Guidance").

[24] For example, the proposal suggests that if a registrant determines that rising sea levels are a climate-related risk that are reasonably likely to have a material impact on its business in the long-term (which the registrant must itself define), disclosure may be required even if the registrant believes that such impacts is only likely to manifest in the very distant future.

[25] *See* Item 102 of Regulation S-K, 17 CFR § 229.102 (2022): "[D]etailed descriptions of the physical characteristics of individual properties . . . . are not required *and shall not be given*." (emphasis added).

of registrants' financial condition, liquidity and capital resources, changes in financial condition and results of operations."[26]

- ***GHG emissions would be required to be disclosed, even if not material, despite the obvious complexity and cost***. Under the proposal, Scope 1 and Scope 2, and in many cases, Scope 3 emissions disclosures would be required on a disaggregated and aggregated basis, regardless of materiality.

  Each public company would be required to calculate its Scope 1 and Scope 2 emissions, whether or not relevant to investment decisionmaking, from "all sources" that are included in the company's "organizational and operational boundaries." The precise scope of a company's "organizational and operational boundaries" takes public companies into uncharted territory—the "boundaries" that "determine" the "direct and indirect emissions associated with the business operations owned or controlled by a registrant" and that "determine" the "operations owned or controlled by a registrant for the purpose of calculating its GHG emissions."

  Companies are well-accustomed to providing disclosure of material information about their business and operations, but a requirement to provide immaterial information that exists "directly or indirectly" within their "boundaries"—and on top of that to obtain third-party assurance that the information is accurate[27]—will on its face require many companies to dedicate expensive resources to fulfilling compliance obligations that are difficult to comprehend but that have little to do with the informational needs and financial goals of their shareholders.

  All but smaller reporting companies would be required to provide Scope 3 emissions data, *regardless of materiality*, if the company "has set a GHG emissions reduction target or goal that includes its Scope 3 emissions." Presumably the Commission is counting on the proposed requirement in Regulation S-K Item 1501(a) to disclose "[w]hether and how the board of directors sets climate-related targets or goals" in order to ensure that few if any companies are able to escape responsibility for disclosing Scope 3 emissions, despite their immateriality.

  Even if a company forewarned by a Regulation S-K disclosure requirement withdraws or declines to set a target or goal, the proposal contains language that would significantly expand what it means for Scope 3 emissions to be "material." The proposal disclaims that it is "proposing a quantitative threshold for determining materiality," but observes "that some companies rely on, or support reliance on, a quantitative threshold such as 40 percent" of total emissions falling into Scope 3 as being the line for determining that its Scope 3 emissions are material.[28] But materiality focuses on the importance of information *to the reasonable investor*, not the relative size of different dimensions of a particular activity or impact. If a company's total Scope 1, Scope 2 and Scope 3 emissions are immaterial to a reasonable investor, it is of no moment that more than 40% of those emissions may be Scope 3.

- ***Proposed financial statement disclosure rules are based on an insignificant 1% per line item threshold.*** Instead of a materiality threshold, the proposal mandates disclosure in companies' audited financial statements, using a 1% threshold, of the positive and negative impacts on

[26] *See* 2010 Guidance, *supra* note 23, at 18.

[27] *See* Proposing Release, *supra* note 4, at § II(G)(2).

[28] *Id.* at 165.

individual financial statement line items of severe weather events and other natural conditions (such as flooding, drought, wildfires, extreme temperatures, and sea level rise), transition activities and identified climate-related risks. As the proposal acknowledges:

> Although we agree that registrants are currently required to disclose material financial impacts on the financial statements, the proposed climate-related financial statement metrics should provide additional transparency into the impact of climate-related events on information reported in the financial statements that would be relevant to investors when making investment or voting decisions.[29]

The proposal would thus inaugurate a new standard for comprehensive financial statement disclosure mandates: no longer is it sufficient for companies to disclose all material financial information needed by reasonable investors for investment decisionmaking—which after all is the standard that today governs the financial statements themselves, where audit opinions are *always* caveated by materiality.

Instead, under the new standard for financial statement disclosures in the realm of climate impact, companies would be required to go further and provide "additional transparency" that may be "relevant" to investment decisionmaking. Why should this new standard be limited to climate disclosure? Certainly the Securities Act and the Exchange Act draw no distinctions on the basis of climate.

Companies are not required today to maintain internal control over financial reporting or disclosure controls and procedures that facilitate the gathering, reporting and auditing of costs associated with severe weather events and other natural conditions at the level of a 1% impact on each financial statement line item, and indeed it is far from clear that many companies would even be able to design and implement controls and procedures enabling them to capture and report such highly specific information about phenomena as vaguely defined as "natural conditions."

But even if companies could, with enough time and consulting fees, design and implement accounting and disclosure controls capable of measuring climate-change impacts at this minute level on financial statement line items such as revenues, cost of goods sold, selling, general and administrative expenses, depreciation and amortization, inventory, property, plant & equipment, and cash flows from operating activities, the proposal does not attempt to explain why a reasonable investor would find this information necessary to proper investment decisionmaking. Needless to say, a 1% impact on any of these particular financial statement line items could easily equate to far less than 1% of a company's total assets, shareholders' equity, revenues, operating income, net income or market capitalization—in other words, an impact that is far below what any reasonable investor might need for decisionmaking purposes, as the Commission has recognized in other contexts.[30]

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[29] *See id. at* § II.F.2; *see also id.* at 138, 145 (asking in questions 68 and 77, "Alternatively, should we just use a materiality standard?"*)*.

[30] *See* 17 CFR Part 211, Release No. SAB 99. ("The use of a percentage as a numerical threshold, such as 5%, may provide the basis for a preliminary assumption that—without considering all relevant circumstances—a deviation of less than the specified percentage with respect to a particular item on the registrant's financial statements is unlikely to be material.").

- ***Proposed board disclosure requirements would result in immaterial disclosure while appearing intended to impose substantive corporate governance requirements.*** We believe proposed new Regulation S-K Item 1501(a), covering the board's role in the management of climate-related risk, is overly prescriptive and unnecessary, because any material information that could be captured by the proposed rule is already addressed by Item 407(h) of Regulation S-K, which obligates companies to disclose the extent of the board's role in the company's risk oversight and how the board administers this oversight function.

  We are also concerned about the cumulative impact of using disclosure mandates to nudge companies into appointing directors specialized in climate, cybersecurity and accounting. At a time when board skill sets need to be carefully balanced with other important objectives such as diversity, independence and board refreshment, a proliferation of specialty director quasi-mandates makes it more difficult to assemble an effective board. This is especially true in an area like climate change, where field knowledge is rapidly evolving and today's expertise will quickly become outdated.

  Climate change is one of myriad risks faced by public companies and, despite what may be an animating assumption of the proposal, it is not the primary risk or even among the primary risks faced by many companies in our highly competitive, dynamic and rapidly changing economy. Lacking general-purpose regulatory authority from Congress over public company governance, the highly prescriptive nature of proposed Item 1501(a)'s disclosure requirements, far beyond any board risk-management disclosure obligations currently in Regulation S-K, appear designed to require that climate-risk management take center stage as a boardroom concern—or at least to make it visibly uncomfortable for any company whose board, in the exercise of its state-law fiduciary duties of loyalty and care, concludes that micromanagement of the company's climate-change preparedness is not the optimal use of its time.

  But micromanaging these issues seems to be what the Commission has decided all public company boards should do, with its proposed requirements to disclose:

  - the names of any directors or board committee responsible for the oversight of climate-related risks,
  - whether any director is a climate-risk expert, and what qualifies them as such,
  - the processes by which the board discusses climate-related risks,
  - the processes for how the board is informed about climate-related risks,
  - the frequency of board discussions of climate-related risks,
  - whether and how the board 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 whether they include interim targets or goals, and
  - how the board oversees progress against these targets or goals.

In *Business Roundtable v. SEC*,[31] the U.S. Court of Appeals for the D.C. Circuit held that "the Exchange Act cannot be understood to include regulation of an issue that is so far beyond matters of disclosure . . . and that is concededly a part of corporate governance traditionally left to the states." To the extent the Commission's purpose in prescribing detailed corporate governance disclosures around climate risk management is to impact board behavior for all public companies above and beyond obligating companies to provide information that is needed for investment decisionmaking, we believe the proposal, if adopted, would be vulnerable to challenge on the same grounds.

* * *

Although we believe the better course would be for the Commission to withdraw the proposal and instead put forth a set of proposed disclosure requirements that is more likely to survive inevitable judicial challenges, if the Commission proceeds with the current rulemaking project we believe the final rules should provide a number of accommodations in order to mitigate the proposal's adverse impact on competition and capital formation. Our comments in response to certain specific questions raised in the proposal follow.

Overview of the Climate-Related Disclosure Framework

> 4. *Do our current reporting requirements yield adequate and sufficient information regarding climate-related risks to allow investors to make informed decisions? In lieu of, or in addition to the proposed amendments, should we provide updated guidance on how our existing rules may elicit better disclosure about climate-related risks?*

Please refer to our introductory comments above.

Disclosure of Climate-Related Risks

> 8. *Should we require a registrant to disclose any climate-related risks that are reasonably likely to have a material impact on the registrant, including on its business or consolidated financial statements, which may manifest over the short, medium, and long term, as proposed? If so, should we specify a particular time period, or minimum or maximum range of years, for "short," "medium," and "long term?" For example, should we define short term as 1 year, 1-3 years, or 1-5 years? Should we define medium term as 5-10 years, 5-15 years, or 5-20 years? Should we define long-term as 10-20 years, 20-30 years, or 30-50 years? Are there other possible years or ranges of years that we should consider as the definitions of short, medium, and long term? What, if any, are the benefits to leaving those terms undefined? What, if any, are the concerns to leaving those terms undefined? Would the proposed provision requiring a registrant to specify what it means by the short, medium, and long term mitigate any such concerns?*

Please refer to our introductory comments above.

> 9. *Should we define "climate-related risks" to mean the actual or potential negative impacts of climate-related conditions and events on a registrant's consolidated financial statements, business operations, or value chains, as proposed? Should we define climate-related risks to include both physical and transition risks, as proposed? Should we define physical risks*

[31] 905 F.2d 406 (D.C. Cir. 1990).

to include both acute and chronic risks and define each of those risks, as proposed? Should we define transition risks, as proposed? Are there any aspects of the definitions of climate-related risks, physical risks, acute risks, chronic risks, and transition risks that we should revise? Are there other distinctions among types of climate-related risks that we should use in our definitions? Are there any risks that we should add to the definition of transition risk? How should we address risks that may involve both physical and transition risks?

We believe the Commission needs to clearly define "climate-related risks" as none of these risks have been defined in a way that supports an understanding of the required disclosure. Transition risk is particularly challenging and requires a deep knowledge that would, for most registrants, require hiring outside consultants, and even then would result in intense speculation. For example, under the TCFD framework, the components of transition risk are: regulatory, technology, stakeholder and legal. Companies would need to rely on consultants to continuously assess the types and forms of technologies that could displace existing technologies currently being used, far off into the future (given the proposal's focus on long-term risks), and then evaluate whether those future technologies pose potential risks. Companies would also need to attempt to gauge customer preferences in the same speculative manner. The only way to fulfill an obligation to consider medium- and long-term risks is to construct an analysis based on varying layers of speculation built on top of one another. It would be entirely plausible that two companies in the same industry would view these risks differently. As a result, most companies would likely be conservative in providing a laundry-list of possible events that could eventually become material. Such an outcome hardly seems likely to produce decision-useful information for investors. At minimum these risks should be limited to known material risks, using traditional conceptions of materiality.

12. *For the location of its business operations, properties or processes subject to an identified material physical risk, should we require a registrant to provide the ZIP code of the location or, if located in a jurisdiction that does not use ZIP codes, a similar subnational postal zone or geographic location, as proposed? Is there another location identifier that we should use for all registrants, such as the county, province, municipality or other subnational jurisdiction? Would requiring granular location information, such as ZIP codes, present concerns about competitive harm or the physical security of assets? If so, how can we mitigate those concerns? Are there exceptions or exemptions to a granular location disclosure requirement that we should consider?*

We understand that some commenters have stated that granular location information is useful for an overall assessment of portfolio climate risk. The professional investors who engage in this level of portfolio analysis would certainly benefit from shifting the costs of producing this data onto the shareholders of individual companies, even when the financial, competitive and physical security costs of doing so cannot be justified on a company-by-company basis. As we noted in our introductory comments, we believe this would improperly move the U.S. disclosure regime closer to a model where companies are simply required to provide whatever information investors request.

13. *If a registrant determines that the flooding of its buildings, plants, or properties is a material risk, should we require it to disclose the percentage of those assets that are in flood hazard areas in addition to their location, as proposed? Would such disclosure help investors evaluate the registrant's exposure to physical risks related to floods? Should we require this disclosure from all registrants, including those that do not currently consider exposure to flooding to be a material physical risk? Should we require this disclosure from all*

> *registrants operating in certain industrial sectors and, if so, which sectors? Should we define "flood hazard area" or provide examples of such areas? If we should define the term, should we define it similar to a related definition by the Federal Emergency Management Agency ("FEMA") as an area having flood, mudflow or flood-related erosion hazards, as depicted on a flood hazard boundary map or a flood insurance rate map? Should we require a registrant to disclose how it has defined "flood hazard area" or whether it has used particular maps or software tools when determining whether its buildings, plants, or properties are located in flood hazard areas? Should we recommend that certain maps be used to promote comparability? Should we require disclosure of whether a registrant's assets are located in zones that are subject to other physical risks, such as in locations subject to wildfire risk?*

As with our response to Question 12, we have no doubt that there are professional investment analysts who would be able to make profitable use of data from each U.S. public company, whether or not flooding or wildfire risk is remotely relevant to the particular company's business and operations, that shows:

- the percentage of the company's assets that are in flood hazard areas or zones that are subject to wildfire or other physical risks,
- how the company has defined "flood hazard area" or the boundaries of another hazard zone, and
- whether the company has used particular maps or software tools when determining whether its buildings, plants or properties are located in flood hazard areas or other hazard zones.

And of course these analysts would prefer that specifically prescribed maps be used, in order to promote comparability. But because facilitating capital formation is one part of the Commission's three-part mission, we think any mandate to describe physical risks in the level of detail contemplated by this question must be limited to companies for whom these risks, and this specific data about these risks, are in fact material to a reasonable investor's investment decision in such companies' securities.

Disclosure Regarding Climate-Related Impacts on Strategy, Business Model, and Outlook

> *19. Should we require a registrant to describe the actual and potential impacts of its material climate-related risks on its strategy, business model, and outlook, as proposed? Should we require a registrant to disclose impacts from climate-related risks on, or any resulting significant changes made to, its business operations, including the types and locations of its operations, as proposed?*

Please refer to our introductory comments above.

> *29. Should we require all registrants to disclose an internal carbon price and prescribe a methodology for determining that price? If so, what corresponding disclosure requirements should we include in connection with such mandated carbon price? What methodology, if any, should we prescribe for calculating a mandatory internal or shadow carbon price? Would a different metric better elicit disclosure that would monetize emissions?*

It is not clear what authority the Commission would have under the Securities Act or the Exchange Act to require all public companies to formulate and disclose an internal carbon price, in order to "monetize emissions" or otherwise.

Governance Disclosure

34. Should we require a registrant to describe, as applicable, the board's oversight of climate-related risks, as proposed? Should the required disclosure include whether any board member has expertise in climate-related risks and, if so, a description of the nature of the expertise, as proposed? Should we also require a registrant to identify the board members or board committee responsible for the oversight of climate-related risks, as proposed? Do our current rules, which require a registrant to provide the business experience of its board members, elicit adequate disclosure about a board member's or executive officer's expertise relevant to the oversight of climate-related risks?

Please refer to our introductory comments above.

Risk Management Disclosure

42. Should we require a registrant to describe its processes for identifying, assessing, and managing climate-related risks, as proposed?

Please refer to our introductory comments above.

Financial Statement Metrics

53. The proposed rules would specify the basis of calculation for the climate-related financial statement metrics. Is it clear how to apply these accounting principles when calculating the proposed climate-related financial statement metrics, or should we provide additional guidance? Should we require a registrant to report these metrics with reference to its consolidated financial statements, as proposed? If not, how should registrants report these metrics? If we were to establish accounting principles (e.g., the basis for reporting these metrics) in a manner that differs from the principles applicable to the rest of the consolidated financial statements, would the application of those principles to the proposed metrics make climate-related disclosures less clear, helpful, or comparable for investors?

In addition to the substantive concerns discussed in our introductory comments, we believe it would be more appropriate to formulate the new accounting disclosure requirements contemplated by the proposal through the Financial Accounting Standards Board's standard-setting process,[32] which includes a thorough cost-benefit analysis[33] and significantly more public deliberation and input than the APA's notice-and-comment model. The FASB Rules of Procedure set forth an extensive review, drafting and discussion process for any new standard, including board deliberation at one or more public meetings, the issuance of an exposure draft soliciting stakeholder input, and public roundtable meetings in order to refine the standard in response to public feedback. This process typically takes months if not years to complete, unlike here, where the Commission has provided the public a mere 88 days to review and comment upon a 506 page proposal with far-reaching consequences. The complexity of accounting and auditing standard setting, and

[32] FASB, Standard-Setting Process, https://www.fasb.org/Page/PageContent?PageId=/about-us/standardsettingprocess.html&isstaticpage=true&bcpath=tff.

[33] FASB, Cost-Benefit Analysis, https://www.fasb.org/Page/PageContent?PageId=/about-us/standardsettingprocess/cba.html&bcpath=tff.

an awareness of the need to avoid adverse unintended consequences, is why the FASB has historically been delegated responsibility for these matters in the first place.

> 55. *The proposed rules would require disclosure for the registrant's most recently completed fiscal year and for the corresponding historical fiscal years included in the registrant's consolidated financial statements in the filing. Should disclosure of the climate-related financial statement metrics be required for the fiscal years presented in the registrant's financial statements, as proposed? Instead, should we require the financial statement metrics to be calculated only for the most recently completed fiscal year presented in the relevant filing? Would requiring historical disclosure provide important or material information to investors, such as information allowing them to analyze trends? Are there other approaches we should consider?*

We do not believe disclosure of the climate-related financial statement metrics should be required for each of the fiscal years presented in the financial statements for the substantive reasons discussed in our introductory comments in this letter. Regardless of whether historical disclosure may provide important information to investors, including allowing them to analyze trends, it will be impossible for many companies to produce reliable disclosure for prior periods because data collection systems would not have been in place for the relevant periods to conduct the line-item analysis that is required.

> 59. *Should we require registrants to disclose the financial impact metrics, as proposed? Would presenting climate-specific financial information on a separate basis based on climate-related events (severe weather events and other natural conditions and identified physical risks) and transition activities (including identified transition risks) elicit decision-useful or material information for investors? Are there different metrics that would result in disclosure of more useful information about the impact of climate-related risks and climate-related opportunities on the registrant's financial performance and position?*

Since "climate-related" is not defined, it is not clear how any company would be able to discern if a particular weather event is "climate-related" or constitutes a "severe weather event" or is merely a summer thunderstorm. Companies may need to account for any weather event in their financial statements in order to avoid being under inclusive. For example, if temperatures are somewhat higher than the prior period and the cost of air conditioning increases, it will likely be unclear whether that is "climate-related" and therefore needs to be part of the financial statement analysis, or whether it might be a normal fluctuation.

> 63. *Is it clear which climate-related events would be covered by "severe weather events and other natural conditions"? If not, should we provide additional guidance or examples about what events would be covered? Should we clarify that what is considered "severe weather" in one region may differ from another region? For example, high levels of rainfall may be considered "severe weather" in a typically arid region.*

As discussed in our response to Question 59, we expect that it will not be clear which climate-related events would be covered by "severe weather events and other natural conditions" as the proposal fails to define what is considered a "severe weather event" and whether the proposal is asking for disclosure regarding the full impact of a weather event, or, instead, the portion attributable specifically to climate change.

> 68. *Instead of including a quantitative threshold, as proposed, should we require disaggregated disclosure of any impact of climate-related risks on a particular line item of the registrant's consolidated financial statements? Alternatively, should we just use a materiality standard?*

Please refer to our introductory comments above.

GHG Emissions Metrics Disclosure

> 98. *Should we require a registrant to disclose its Scope 3 emissions for the fiscal year if material, as proposed? Should we instead require the disclosure of Scope 3 emissions for all registrants, regardless of materiality? Should we use a quantitative threshold, such as a percentage of total GHG emissions (e.g., 25%, 40%, 50%) to require the disclosure of Scope 3 emissions? If so, is there any data supporting the use of a particular percentage threshold? Should we require registrants in particular industries, for which Scope 3 emissions are a high percentage of total GHG emissions, to disclose Scope 3 emissions?*

Please refer to our introductory comments above.

> 100. *Should Scope 3 emissions disclosure be voluntary? Should we require Scope 3 emissions disclosure in stages, e.g., requiring qualitative disclosure of a registrant's significant categories of upstream and downstream activities that generate Scope 3 emissions upon effectiveness of the proposed rules, and requiring quantitative disclosure of a registrant's Scope 3 emissions at a later date? If so, when should we require quantitative disclosure of a registrant's Scope 3 emissions?*

Please refer to our introductory comments above.

> 109. *Should we require a registrant to disclose the intensity of its GHG emissions for the fiscal year, with separate calculations for (i) the sum of Scope 1 and Scope 2 emissions and, if applicable (ii) its Scope 3 emissions (separately from Scopes 1 and 2), as proposed? Should we define GHG intensity, as proposed? Is there a different definition we should use for this purpose?*

Please refer to our introductory comments above.

> 133. *Should we provide a safe harbor for Scope 3 emissions disclosure, as proposed? Is the scope of the proposed safe harbor clear and appropriate? For example, should the safe harbor apply to any registrant that provides Scope 3 disclosure pursuant to the proposed rules, as proposed? Should we limit the use of the safe harbor to certain classes of registrants or to registrants meeting certain conditions and, if so, which classes or conditions? For example, should we require the use of a particular methodology for calculating and reporting Scope 3 emissions, such as the PCAF Standard if the registrant is a financial institution, or the GHG Protocol Scope 3 Accounting and Reporting Standard for other types of registrants? Should we clarify the scope of persons covered by the language "by or on behalf of a registrant" by including language about outside reviewers retained by the registrant or others? Should we define a "fraudulent statement," as proposed? Is the level of diligence required for the proposed safe harbor (i.e., that the statement was made or reaffirmed with a reasonable basis and disclosed in good faith) the appropriate standard? Should the safe harbor apply to other climate-related disclosures, such as*

Scopes 1 and 2 emissions disclosures, any targets and goals disclosures in response to proposed Item 1505 (discussed below), or the financial statement metrics disclosures required pursuant to Proposed Article 14 of Regulation S-X? Should the safe harbor apply indefinitely, or should we include a sunset provision that would eliminate the safe harbor some number of years, (e.g., five years) after the effective date or applicable compliance date of the rules? Should the safe harbor sunset after certain conditions are satisfied? If so, what types of conditions should we consider? What other approaches should we consider?

We agree that a safe harbor for Scope 3 emissions disclosures is necessary given that companies will need to rely on estimates, assumptions and third-party data outside of their control to compile this data. That said, the safe harbor is subject to the condition that the company's disclosure must not have been "made or reaffirmed without a reasonable basis" or been "disclosed other than in good faith." The proposal is silent on what the "reasonable basis" and "good faith" thresholds are, and we believe the benefit of the safe harbor is minimal if not useless if conditioned upon a showing the company acted reasonably and in good faith, which will be difficult when hindsight has already shown that the company's disclosures were materially incorrect. We believe a better approach would be the one taken in Rule 144 and Regulation D, where the availability of a safe harbor is forfeited through use of a plan or scheme to evade federal securities law requirements.[34]

134. Should we provide an exemption from Scope 3 emissions disclosure for SRCs, as proposed? Should the exemption not apply to a SRC that has set a target or goal or otherwise made a commitment to reduce its Scope 3 emissions? Are there other classes of registrants we should exempt from the Scope 3 emissions disclosure requirement? For example, should we exempt EGCs, foreign private issuers, or a registrant that is filing or has filed a registration statement for its initial public offering during its most recently completed fiscal year from the Scope 3 disclosure requirement? Instead of an exemption, should we provide a longer phase in for the Scope 3 disclosure requirements for SRCs than for other registrants?

Please refer to our introductory comments above and our responses to Questions 175 and 176.

Attestation of Scope 1 and Scope 2 Emissions Disclosure

135. Should we require accelerated filers and large accelerated filers to obtain an attestation report covering their Scope 1 and Scope 2 emissions disclosure, as proposed? Should we require accelerated filers and large accelerated filers to obtain an attestation report covering other aspects of their climate-related disclosures beyond Scope 1 and 2 emissions? For example, should we also require the attestation of GHG intensity metrics, or of Scope 3 emissions, if disclosed? Conversely, should we require accelerated filers and large accelerated filers to obtain assurance covering only Scope 1 emissions disclosure?

[34] *See* 17 CFR § 230.144 ("The Rule 144 safe harbor is not available to any person with respect to any transaction or series of transactions that, although in technical compliance with Rule 144, is part of a plan or scheme to evade the registration requirements of the Act."). *See also* 17 CFR § 230.500(f) ("In view of the objectives of Regulation D and the policies underlying the Act, Regulation D is not available to any issuer for any transaction or chain of transactions that, although in technical compliance with Regulation D, is part of a plan or scheme to evade the registration provisions of the Act. In such cases, registration under the Act is required.").

Should any voluntary assurance obtained by these filers after limited assurance is required be required to follow the same attestation requirements of Item 1505(b)-(d), as proposed?

The Commission should not require third-party attestation reports for Scope 1 and Scope 2 emissions, at least not until it is has concrete data on the costs of such a mandate. The types of data that require expertization today include financial statements, internal control over financial reporting and natural resources reserves—in other words, data that is plainly relevant to investor decisionmaking. By contrast, the Commission's proposed Scope 1 and Scope 2 emissions disclosure requirements are unconstrained by materiality considerations. Before significantly increasing the burden of immaterial disclosures by adding a third-party attestation requirement, the Commission should wait to see whether third-party attestation is actually needed to ensure the availability of information for investment decisionmaking purposes and is obtainable at a cost that is outweighed by the benefits to investors.

137. Should the attestation requirement be limited to accelerated filers and large accelerated filers, as proposed? Alternatively, should the attestation requirement be limited to a subset of accelerated filers and large accelerated filers? If so, what conditions should apply? Should the attestation requirement only apply to well-known seasoned issuers? Should the attestation requirement also apply to other types of registrants? Should we create a new test for determining whether the attestation requirements apply to a registrant that would take into account the resources of the registrant and also apply to initial public offerings? For example, should we create a test similar to the SRC definition, which includes a separate determination for initial registration statements, but using higher public float and annual revenue amounts?

If the Commission proceeds with a third-party attestation requirement, it should apply only to those companies for whom Scope 1 and Scope 2 emissions data is material to the investment decision of a reasonable investor.

Registrants Subject to the Climate-Related Disclosure Rules and Affected Forms

175. Should the proposed climate-related disclosures be required in Exchange Act reports and registration statements, as proposed? Should we exempt SRCs from all of the proposed climate-related disclosure rules instead of exempting them solely from Scope 3 emissions disclosure requirements, as proposed? Should we exempt SRCs from certain other proposed climate-related disclosure requirements and, if so, which requirements? For example, in addition to the proposed exemption from Scope 3 emissions disclosure, should we exempt SRCs from the proposed requirement to disclose Scopes 1 and 2 emissions? Are there certain types of other registrants, such as EGCs or business development companies ("BDCs"), that should be excluded from all or some of the proposed climate-related disclosure rules?

We believe EGCs, non-accelerated filers and, for a specified period of time, companies pursuing an initial public offering ("IPO") or who have recently completed an IPO (and are not otherwise exempted) should be exempted from the proposed rules. Even if the benefits of requiring climate-related disclosure for these types of companies is the same as for other registrants, the costs must be considered in the appropriate light. While implementation of the proposal would dramatically increase compliance costs for all companies, the negative impact on capital formation would be particularly acute among EGCs, non-accelerated filers and companies pursuing an IPO. Based on our experience advising clients seeking to become publicly listed in the United States, we believe that the proposal would act as a meaningful deterrent for companies who are considering going public. For those companies that nonetheless pursue a listing, we believe that proposed Article 14 of Regulation S-X would cause substantial delays associated with initial PCAOB audits, which are often the most time-consuming and mission-critical step in the IPO process. Requiring significant climate-related disclosure in the financial statements thereby increasing the information subject to audit review would impose a heavy burden on companies pursuing an IPO who are least able to bear such a burden, and is certain to lead to fewer private companies going public. Similarly, the attestation requirements included in proposed Item 1500 of Regulation S-K are likely to cause significant delays for companies seeking to go public. As such, we believe that if the proposal is adopted, EGCs, non-accelerated filers and, for a specified period of time, companies pursuing an IPO and recently public companies should be exempted from the requirements of both proposed Item 1500 of Regulation S-K and proposed Article 14 of Regulation S-X in order to mitigate the negative impacts of the proposal on capital formation.

> *176. Should we require foreign private issuers that report on Form 20-F to provide the same climate-related disclosures as Form 10-K filers, as proposed? Should we require climate-related disclosures in the registration statements available for foreign private issuers, as proposed? If not, how should the climate-related disclosures provided by foreign private issuer registrants differ from the disclosures provided by domestic registrants?*

We believe foreign private issuers should be permitted to follow home country practice. Similar to EGCs, the negative impact on capital formation for foreign private issuers should be considered in the light of their particular circumstances. Foreign private issuers elect to list in the United States due to the expected benefits of having access to U.S. capital markets. However, they are permitted to follow home country practice in many cases. We believe that it would impair capital formation in the United States if foreign private issuers were subject to proposed Item 1500 of Regulation S-K and proposed Article 14 of Regulation S-X and the attendant increased compliance costs and potential for liability, as it would add substantial costs that many foreign private issuers are likely to view as a deterrent to listing in the United States. Moreover, proposed Article 14 of Regulation S-X may lead a number of foreign private issuers to withdraw their Exchange Act registrations when possible, especially since to our knowledge similar financial statement requirements do not exist, and are not generally contemplated, in other countries.

> *180. Should we require climate-related disclosure in Forms S-4 and F-4, as proposed? Should we provide transitional relief for recently acquired companies? For example, should we provide that a registrant would not be required to provide the proposed climate-related disclosures for a company that is a target of a proposed acquisition under Form S-4 or F-4 until the fiscal year following the year of the acquisition if the target company is not an Exchange Act reporting company and is not the subject of foreign climate-related disclosure requirements that are substantially similar to the Commission's proposed requirements? Should such transitional relief in this instance be for a longer period than one year and, if so, for how long should such transitional relief extend?*

We believe the Commission should provide transitional relief for recently acquired companies in both registration statements and periodic reports for at least one year following the consummation of the acquisition. As the Commission has recognized in the context of internal controls, "it might not always be possible to conduct an assessment of an acquired business's internal control over financial reporting in the period between the consummation date and the date of management's assessment."[35] If it is not possible for management to assess an acquired company's internal control environment prior to a reporting date (whether triggered by a registration statement or periodic report filing), it would be equally impractical for an issuer to include detailed climate-related disclosures that are based in part on the same internal control environment.

* * *

We appreciate the opportunity to participate in the Commission's rulemaking process, and would be pleased to discuss our comments or any questions that the Commission or its staff may have, which may be directed to Margaret E. Tahyar, Joseph A. Hall, Michael Kaplan, Shane Tintle, Ning Chiu, Loyti Cheng, Stephen A. Byeff, David A. Zilberberg or Jonathan I. Stempel of this firm at 212-450-4000.

Very truly yours,

Davis Polk & Wardwell LLP

[35] SEC, *Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports*, https://www.sec.gov/info/accountants/controlfaq.htm.