June 17, 2022
Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

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

Dear Ms. Countryman:

The American Council for Capital Formation (ACCF)[1] appreciates the opportunity to provide comment to the Commission's proposed rule to enhance and standardize climate-related disclosures by public companies (the Securities and Exchange Commission ("SEC") on File No. S7-10-22).

The ACCF represents a broad cross-section of the American business community, including a wide range of manufacturing and financial sector interests, Fortune 500 companies and smaller firms, investors, and associations from all sectors of the economy. Our distinguished board of directors includes cabinet members from prior Democratic and Republican administrations, former Members of Congress, prominent business leaders, and public finance and environmental policy experts. The ACCF is celebrating more than four decades of leadership in advocating for sound tax, energy, regulatory, environmental, and trade policies to increase U.S. economic growth and environmental quality.

As the worldwide investor community calls for increased climate-related disclosure, regulatory agencies around the world are looking for ways to respond to these calls. The task is not easy. By nature, public companies are diverse and, with respect to climate issues, each is dealing with different degrees and impacts as they address the best approach to contribute to and achieve net-zero targets. The uncertainties associated with the impact of climate change and how climate impacts cannot be translated into relatively "easy" to prepare and understand financial reporting disclosures and preparing these disclosures under a "one size fits all" system, is a near-impossible task. Further, the difficulty of the task at hand and the complex nature of the suggested solutions can be easily seen in the slew of comments and opinions now in the public domain since the introduction of the SEC's climate disclosure requirements.

Many of the comments submitted will no doubt delve into detailed legal and financial regulatory aspects of the proposal, but sometimes it is important to take a step back and ask some basic questions, namely: What are the goals of these regulations? What is currently being done in the marketplace? And, are these regulations likely to achieve their goals without harming the efficiency of the capital markets?

No doubt the SEC actions are driven by investors, as stated by SEC Chair Gary Gensler during the release of the proposed rules: "Today, investors representing literally tens of trillions of dollars support climate-related disclosures because they recognize that climate risks can pose significant financial risks to

[1] For more information about the Council, please contact the ACCF, 1001 Connecticut Ave, NW, Suite 620 Washington, DC 20036; telephone: 202.293.5811; e-mail: info@accf.org; website: www.accf.org

companies, and investors need reliable information about climate risks to make informed investment decisions."[2]

The SEC needs to chart its course of action under the guidance of its three-part mission: to protect investors, to maintain fair and orderly and efficient markets, and to facilitate capital formation. There are some valid questions on whether the proposed rules follow these guidelines and whether they have been analyzed thoroughly to understand the direct and indirect burden they might impose on the U.S. economy.

Of particular importance to the mission of the ACCF is the proposed rules' impact on the potential regulatory costs for public firms and the resulting adverse impact on capital formation and the overall economy. The ACCF does not dispute the need for SEC guidance in these disclosures, especially as a number of other countries are moving forward with their own rules that could subject U.S. multinationals to different and misaligned rules in multiple jurisdictions. This scenario could multiply the cost of the regulatory burden of climate disclosure. However, the proposed rules as currently formulated are too extensive and prescriptive in nature, creating disclosure requirements "relating to strategy, business model, outlook and risk management, including relating to targets, goals and transition plans,"[3] which could impose significant costs on public companies, and as we will discuss with respect to Scope 3 requirements, many smaller, and private firms in the value chain.

The potential size of the added costs related to new mandatory climate reporting standards is another layer of overall regulatory burden on public companies. According to some experts, increased regulatory costs is one of the reasons for the decrease in the number of U.S. companies traded on major stock exchanges in recent decades. This downward trend in the number of companies has ramifications for capital formation and the U.S. economy. In these comments, the ACCF first highlights a few of the provisions in the proposed rule, as well as the timeline for implementation, which could have a significant impact in terms of raising the regulatory cost faced by public companies if they are finalized as is. These comments then highlight the results of new research commissioned by the ACCF and conducted by EY's Quantitative Economics and Statistics Group (attached to this comment letter).

I. Sample of Issues with Climate Disclosure Rule that Could Raise Regulatory Costs

The comments below highlight some key items in the proposed rules that could have a significant impact on public companies' regulatory costs if they are finalized as is. It is not intended to be a full analysis of the proposal and its costs and benefits, rather it pinpoints how the proposal can introduce significant uncertainty as well as increased costs for public firms.

The Materiality Question, Uncertainty and Costs

SEC rules are guided by the Supreme Court's traditional materiality standard to make sure that reported information is relevant for investors' decisions, based on a 1976 ruling that states that company

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[2] Gary Gensler, "Statement on Proposed Mandatory Climate Risk Disclosures," March 21, 2022. https://www.sec.gov/news/statement/gensler-climate-disclosure-20220321

[3] Michael Littenberg, Marc Rotter, and Hannah Shapiro, "Ten Thoughts on the SEC's Proposed Climate Disclosure Rules," April 20, 2022, Harvard Law School Forum on Corporate Governance. https://corpgov.law.harvard.edu/2022/04/30/ten-thoughts-on-the-secs-proposed-climate-disclosure-rules/

information is material if there is "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 available."[4]

The proposed rule, however, takes a more prescriptive approach, in some cases side stepping the traditional materiality definition. For example, Proposed Items 1502 and 1503 under S-K regulations are very extensive and include much uncertainty, by nature. This could impose significant data collection and analysis costs on firms which, in some cases, would need to gather granular information that is immaterial for investors. For example, Proposed Item 1502 requires registrants to provide a detailed discussion of the particular climate-related risks on:[5]

- Business operations, including the types of risks and locations of potential impacts.
- Products or services.
- Suppliers and other parties in its value chain.
- Activities to mitigate or adapt to climate-related risks, including adoption of new technologies or processes.
- Expenditures for research and development.

The detailed nature of these mandatory disclosures makes it difficult to put a price tag on the effort required to compile such detailed quantitative and qualitative analysis. Again, using Proposed Item 1502 as an example, the proposal would require:[6]

- Disclosing physical and transition risks with a detailed description of the nature of each risk. For example, in the case of physical risk, disclosures would need to include the location and nature of properties that could be impacted, whether risks are acute or chronic and in the case of drought and flooding, additional information about the size and location of the assets at risk would be required. In the case of transition risk, disclosures need to classify whether the risk relates to technological, regulatory, market, liability, reputational or other similar factors.
- Disclosing how such risks would impact business strategy, business model, financial statements and outlook, including the nature and time horizon for each impact and whether they are included in the company's business strategy, financial planning and capital allocation.
- Providing narrative disclosures about the resilience of the business in light of future climate-related risks. This would include a description of mitigation efforts and their cost, effectiveness and impact on financial results and operations. This would also require additional disclosures regarding any analysis of the price and cost per metric ton of carbon dioxide equivalent (CO_2e) and GHG emissions.

[4] Timothy J. Horstmann and Erica M. Wible, "What is Material? The SEC Says You Decide," December 7, 2018, https://www.mcneeslaw.com/what-is-material-the-sec-says-you-decide/
[5] Baker Hostetler, "SEC Proposes Rules for Climate-Related Disclosures and Extends Deadline for Public Comments," May 11, 2022. https://www.mercatus.org/publications/financial-regulation/adopting-secs-proposed-climate-change-disclosure-rules-would-be
[6] Baker Hostetler, 2022.

This Item has been a significant interest to legal scholars. According to Andrew N. Vollmer of Mercatus Center, "The Proposal creates confusion about the standards for disclosure of climate risks and materiality."[7] Mr. Vollmer specifically lists:

- Proposed Item 1502(a) which states that "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," is very broad and covers risks that are not currently material but *could be material* in the future.
- Proposed Item 1502(b) and (d) would require a "description of 'the actual and potential impacts' of the risks identified in response to 1502(a) on the company's strategy, business operations, and suppliers or other parties in the company's 'value chain,'" and "a discussion of any risks described in response to 1502(a) that 'affected or are reasonably likely to affect' the financial statements." Items (b) and (d) would again require companies to discuss costs that are associated with currently immaterial risks.

According to Mr. Vollmer, the uncertainty within the 1502 comes from the fact that first, a company must identify a climate-related risk and then decide whether this risk is "reasonably likely" to impact the company and whether it is material. This decision chain has uncertainties at every stage: "to make a disclosure decision, management must assess a *reasonable* likelihood of a *substantial* likelihood on a *reasonable* investor."[8]

Proposed Item 1503 goes one step further and require the disclosure of any processes that is being used to identify, assess, and manage climate related risks.

The proposed rules also extend Regulations S-X, requiring public companies to analyze each of the line items in their consolidated financial statement for climate-related risks, weather events, and transition activities. As a result of analysis, if the overall impact of these risks is above 1% of the value of a given line item, companies must disclose the impact of each item in a disaggregated manner in their financial statements. Under existing systems, to accomplish such data tracking and analysis would be a herculean task for companies, given the very low threshold for reporting. Given the extensive nature of the language on weather events and transition activities, companies will face significant uncertainty in terms of deciding what risk can be categorized under one of these items versus the risk of doing business in certain locations. Furthermore, since companies must collect, analyze and compile emissions data to see whether they are below the 1% threshold, the 1% threshold does not significantly reduce the burden on companies, even if they ultimately *do not* have to report.

The three new proposed disclosure items described above is just the "tip of the iceberg" in terms of the costs associated with the 500 plus page proposed rules. The rules would also require outside attestation of the disclosures for Scope 1 (direct emissions) and Scope 2 (emissions resulting from the generation of electricity purchased and consumed by the company) emissions, as well as the disclosure of Scope 3 emissions (all other indirect emissions) for certain companies when material. As we will discuss further,

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[7] Andrew N. Vollmer, "Adopting the SEC's Proposed Climate-Change Disclosure Rules Would Be Unwise," May 10, 2022, Mercatus Center, https://www.mercatus.org/publications/financial-regulation/adopting-secs-proposed-climate-change-disclosure-rules-would-be

[8] Vollmer, 2022.

the requirement to disclose Scope 3 emissions could potentially impose costs on companies outside the scope of this rule, including private small and medium size enterprises, further increasing the costs for the overall economy. Some the proposed items also require companies to not only provide current data, but to also evaluate the impact on historical financial statements.

Scope 3 Reporting: Unintended Consequences

Scope 3 emissions include emissions resulting from activities or assets not directly controlled or owned by the registrant, but they are part of the upstream (suppliers) and downstream (clients) value chain of the company. The proposal would require large accelerated filers to report these emissions if they are material or if the company has an emissions reduction target that includes Scope 3 emissions. There are some safe-harbor provisions to protect companies from liability associated with including Scope 3 emissions disclosures in SEC filings. However, the adequacy of these safe harbors with respect to providing robust protection against liability even if company disclosures were undertaken in good faith has been questioned by legal experts. According to John C. Coffee, Jr., "the safe harbor so proposed is a shallow one."[9]

Scope 3 emissions reporting is challenging by definition since it includes extracting data from third parties that the company does not have control over. There are distinct difficulties associated with Scope 3 emissions data tracking and gathering:

- Many businesses have extensive and global supply chain structure, as well as a worldwide customer base, which will make it extremely difficult to gather effective and reliable data that is comparable across industries. Such efforts could be prohibitively costly, especially for industries that have a lot of moving pieces.
- There are also questions regarding whether companies outside the authority of SEC would be willing to furnish such data to the public companies that they are doing business with. This could be simply due to upstream or downstream businesses not having access to, expertise, or even operating systems designed to adequately and reliably gather such data. This could lead required public companies attempt to estimate such data, increasing uncertainty and further diminishing the reliability of the data.
- According to research by Bain & Company and CDP, while 64% of the world's public companies by market capitalization currently report their environmental impact through CDP, the number is less than 1% for private companies.[10] The same research also shows that only 49 percent of the surveyed private companies report Scope 1 and 2 emissions, compared to 88 percent of public companies. In terms of Scope 3 emissions reporting, there is a significant gap between public and private companies. Only 29 percent of private companies report Scope 3 emissions versus 70 percent of the public cohort (See **Figure 1**). As the report indicates "[t]he effective coverage of

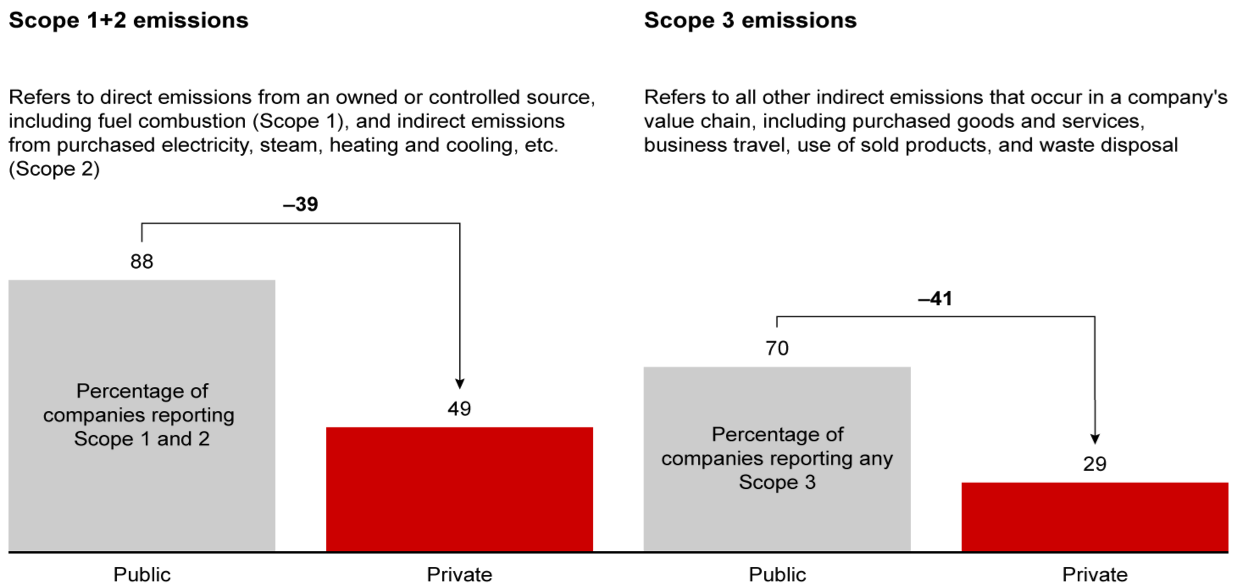
[9] John C. Coffee, Jr., "Unpacking the SEC's Climate-Related Disclosures: A Quick Tour of the Issues," March 29, 2022, Columbia Law School's Blog On Corporations and the Capital Markets, https://clsbluesky.law.columbia.edu/2022/03/29/unpacking-the-secs-climate-related-disclosures-a-quick-tour-of-the-issues/

[10] Bain & Company, "Closing the Public-Private Environmental Transparency Gap," May 19, 2022. https://www.bain.com/insights/closing-the-public-private-environmental-transparency-gap/

Scope 3 emissions reporting is probably much lower, as many public and private companies are not yet reporting comprehensively on all 15 categories of Scope 3 emissions."[11] The reasons for the difference between public and private companies are various, but include: resource constraints, capability gaps, and a lack of urgency from leadership. The SEC's mandatory reporting requirements for Scope 3 might put smaller privately held companies at a disadvantage vis-à-vis their larger counterparts who already track environmental data. Public companies might decide to work with entities that have the capability of tracking the required data to lessen the burden on themselves. This could either result in additional regulatory costs for privately held companies (due to the need to track this data) or alternatively could lead the companies to choose not to do business with public companies (to avoid the need to track such data). In either case, the SEC's rule could have unintentional impacts on private firms, especially smaller private businesses.

- Another inherent problem with Scope 3 reporting is overall "double counting." That is, the Scope 1 emissions of Firm A could be the Scope 3 emissions for multiple firms. For example, the emissions from an oil producer would be included in the Scope 3 emissions for the pipeline company that transports the oil to a refinery, the refinery that processes the oil into fuels, and the separate pipeline company that transports refined products to market. This double (and triple!) counting could result in estimated emissions well in excess of actual emissions and would make it difficult for investors to compare Scope 3 emissions. Many institutions are currently working on improving Scope 3 emissions calculations, but this work is still in its infancy.[12]

Figure 1. Percent of Public Versus Private Companies Reporting Emissions



[11] Bain & Company, 2022.
[12] Gireesh Shrimali, "Scope 3 Emissions: Measurement and Management," April 2021, Stanford University, https://energy.stanford.edu/sites/g/files/sbiybj9971/f/scope_3_emissions_-_measurement_and_management.pdf

Timelines Add to Costs

Once finalized, the proposed rules have an ambitious timeline which will increase the costs for companies for a variety of reasons. **Table 1** outlines these timelines.

Table 1. Phase-in schedule for the proposed rule

Disclosure Requirement	Large Accelerated Filers	Accelerated Filers	Non-Accelerated Filers	Smaller Reporting Companies
All disclosures other than Scope 3	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Same as for Accelerated Filers	Fiscal year 2025 (filed in 2026)
Scope 3 emissions disclosures	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Same as for Accelerated Filers	Exempt
Attestation for Scope 1 & Scope 2 emissions disclosures	Limited Assurance Fiscal year 2024 (filed in 2025) Reasonable Assurance Fiscal year 2026 (filed in 2027)	Limited Assurance Fiscal year 2025 (filed in 2026) Reasonable Assurance Fiscal year 2027 (filed in 2028)	Exempt	Same as for Accelerated Filers or Non-Accelerated Filers (as applicable)

Source: Gibson Dunn, https://www.gibsondunn.com/summary-of-and-considerations-regarding-the-sec-proposed-rules-on-climate-change-disclosure/

The reasons why the timeline could be overly burdensome, especially in the early years after implementation, include:

- Companies need to develop a climate data infrastructure to accurately track, collect, analyze, and report the existing and newly required data. As seen in Table 1, for large accelerated filers, the reporting requirements start as early as in 2024, for the fiscal year 2023. For Scope 3, filing starts in 2025. Many of these timelines are very ambitious, given that some of the public firms will need to start from scratch and will either have to build their own internal infrastructure or hire third parties to fulfill these obligations, or potentially a combination of both approaches.
- Attestation for Scope 1 and Scope 2 emissions could also introduce additional costs. According to Erin Martin and Celia Soehner, "If the Proposal is implemented as currently drafted, third-party attestation providers and/or ESG consulting firms may have limited capacity for new clients, and other external factors could impact a public company's ability to fully assess its climate-relate disclosures and processes."[13]

[13] Erin Martin and Celia Soehner, "How Public Companies Can Prepare for the SEC's Proposed Climate-Related Disclosure Rules," April 2022, https://www.morganlewis.com/pubs/2022/04/how-public-companies-can-prepare-for-the-secs-proposed-climate-related-disclosure-rules?__cf_chl_f_tk=qz.WrtQ1wwA21aAOxBI0w88lYXKNnYS.thnFy144DlY-1655071514-0-gaNycGzNBv0

- Many public companies track and report their Scope 1 and Scope 2 emissions to the Environmental Protection Agency (EPA). This type of data is normally published in Sustainability Reports in the late spring or early summer. However, many companies have much earlier deadlines for 10-K reporting (in March). Due to the differences in the SEC and EPA timelines, the SEC proposes to let companies include reasonable GHG estimates for the fourth quarter of the fiscal year and disclose any material difference between estimated and actual emissions in a subsequent filing. Due to potential liability issues, companies might hesitate to publish and later correct incomplete data. In addition, companies track their GHG emissions on annual basis and converting this tracking to a quarterly basis would be very costly.

II. Increased Reporting Requirements and Public Companies

Why Are Stock Exchanges and Public Companies Important for the Economy?

Well-functioning exchange markets are an integral part of an efficient financial eco-system which bring together businesses that are looking for capital to grow and savers who are looking for a variety of investment options for their resources. Academic research has shown the positive links between well-functioning exchanges and economic development. For example, according to recent research by Caporale and his co-authors "The evidence obtained from a sample of seven countries suggests that a well-developed stock market can foster economic growth in the long run. It also provides support to theories according to which well-functioning stock markets can promote economic development by fueling the engine of growth through faster capital accumulation, and by tuning it through better resource allocation."[14]

There are a variety of reasons why stock markets are attractive options for capital matching. According to a recent report by UNCTAD and the World Federation of Exchanges, these reasons include:[15]

- *Investment horizons*: Stock markets provide investors with easy means of exiting their investment by selling in secondary markets. Investors do not need find a specific buyer or negotiate terms as the rules are set by the market. And even if investors have different time horizon preferences, they can easily put money without a risk in these markets for various stocks.
- *Transparency*: Through listings and ongoing disclosure requirements, important information is readily available for investors' decision process. It also reduces the information asymmetry problem, whereby company insiders might have more information than outsiders.
- *Investor protection*: The rules of the exchange in combination with relevant market regulations mitigate various risks for the investors.

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[14] Guglielmo Maria Caporale, Peter Howells and Alaa M. Soliman, "Stock Market Development and Economic Growth: The causal linkage," January 2004Journal of Economic Development 29(1):33-50. https://www.researchgate.net/publication/227450321_Stock_Market_Development_and_Economic_Growth_The_causal_linkage

[15] UNCTAD and World Federation of Exchanges, "The Role of Stock Exchanges in Fostering Economic Growth and Sustainable Development," 2019. https://sseinitiative.org/wp-content/uploads/2019/12/WFE-UNCTAD-Exchanges-Growth-and-Sustainable-Development.pdf

- *Pooling funds*: A large and diverse set of investors reduces the size of an individual investment (economic exposure with small investment such as buying a single share) and allows investors to manage their risk based on their preference.

According to the report, "These 'risk mitigation', 'risk spreading' and 'risk transformation' features of stock exchanges serve both to reduce the cost of the capital for firms and increase access to financing for larger and/or riskier ventures than they might be able to finance otherwise."[16] At the same time, providing investors with access to diversified investment opportunities could help reduce the risk of income volatility. With positive investment returns, investors' funds available for consumption and/or future investment will be enhanced. This could be used to further accelerate growth and expansion for the overall economy.

Public markets have been driven by "unparalleled wealth creation, opportunities for employees and savers; and stable, low-cost access to capital."[17] The immense success of Apple, Microsoft, and Amazon is partly driven by access to a larger, more liquid pool of capital. For example, for large tech companies, 96 percent of their value was created during their time as public companies. According to research, since the 1970s, 92 percent of corporate job creation has occurred after companies' IPOs.[18]

At the heart of all the success of public markets is a stable supply of IPOs and public companies. However, recent numbers show a decrease in public companies and IPOs in the U.S.

Declining Number of IPOs and Public Companies in the U.S.

The number of US companies traded on major US exchanges has declined significantly in recent decades. After peaking in 1996 at more than 8,000 public companies, the number decreased nearly 50 percent by 2019. The number of IPOs has also gone down sharply during this period. After peaking in 1996 at 700 IPOs, there were barely 100 IPOs in 2017.[19] There are multiple reasons for these trends. According to new a new report by EY's Quantitative Economics and Statistics Group, the reasons include:[20]

- *Declining Business Dynamism* described as the process of new businesses starting, growing, dying, and being replaced with other more productive businesses. A recent paper by Federal Reserve economists highlights multiple reasons for this decline, but they assert that distortions to the diffusion of knowledge across firms in the economy are the likely culprit behind declining U.S. business dynamism.[21]

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[16] UNCTAD and World Federation of Exchanges, pg 9.
[17] Sarah Williamson, "Public Markets for the Long Term: How Successful Listed Companies Thrive," February 2019, Harvard Law School Forum on Corporate Governance. https://corpgov.law.harvard.edu/2019/02/08/public-markets-for-the-long-term-how-successful-listed-companies-thrive/
[18] Sarah Williamson, 2019.
[19] Paul Smith, "Shrinking public markets limit the playing field for the average investors," January 4, 2019, CNBC. https://www.cnbc.com/2019/01/03/shrinking-public-markets-alter-playing-field-for-average-investors.html
[20] EY's Quantitative Economics and Statistics Group, "The declining number of public companies and mandatory reporting requirements," June 2022, Prepared for the ACCF, https://accf.org/2022/06/16/report-the-decli…ing-requirements/
[21] Ufuk Akcigit and Sina T. Ates, "What Happened to U.S. Business Dynamism?," FEDS Notes. Washington: Board of Governors of the Federal Reserve System, February 14, 2020,

- *Increases in the availability of private equity* for start-ups. Access to other types of capital allows companies to scale up without needing to access public markets.
- *Increases in merger and acquisition activity*. The merger of two public companies will reduce the number of listed public companies.
- *Higher regulatory compliance costs* for public companies. Mandatory reporting requirements is part of these higher regulatory costs and they have been increasing significantly since 2000.

The increase in regulatory costs and their impacts on number of public companies and IPOs have taken the center stage in recent years. However, empirical literature on the issue is short and existing research is generally survey based. A recent paper by Michael Ewens, Kairong Xiao and Ting Xu (Ewen et al.), on the other hand, takes a novel approach and finds that various disclosure and internal governance rules lead to a total compliance cost of 4.1% of market capitalization for the median U.S. public firm. According to the same study, regulatory costs have a greater impact on private firms' IPO decisions than on public firms' decision to "go private."[22] These results are, however, conservative. This is because, as noted by Ewens et al., the methodology's reliance on changes in reporting requirements at public float thresholds makes it such that the methodology cannot examine uniform reporting requirements or industry-specific rules.

Based on the Ewens et al. methodology, EY analyzes the impact of mandatory reporting requirements on public firms. The EY study finds that:

- There were at least 800 fewer US companies traded on major US exchanges at the end of 2019 because of mandatory reporting requirements. Note that these companies and the related economic activity do not cease to exist, but rather remain private instead of being public.
- The median US company that would have been public is estimated to have 650 workers. Across the approximately 800 fewer public companies in 2019 this amounts to more than 500,000 workers.
- The median US company that would have been public is estimated to have nearly $300 million in revenue. Across the approximately 800 fewer public companies in 2019 this amounts to upwards of $250 billion in revenue in the public capital markets.
- The median US company that would have been public is estimated to have over $750 million in market capitalization. Across the approximately 800 fewer public companies in 2019 this amounts to nearly $600 billion in market capitalization.

To put these estimates in context, without any mandatory reporting requirements in the 2000-2019 period, the number of public listed companies in 2019 would have been higher by roughly 800, all else equal. That is, there would have been roughly 5,100 publicly listed companies rather than 4,300 in 2019 – a 16% decline – without accounting for the various other factors that may also explain the decline in public listings. Assuming these companies are the size of the median public company in 2019, which tend

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https://www.federalreserve.gov/econres/notes/feds-notes/what-happened-to-us-business-dynamism-20200214.htm

[22] Michael Ewens, Kairong Xiao, and Ting Xu, "Regulatory Costs of Being Public: Evidence From Bunching Estimation," NBER Working Paper 29143, August 2021, https://www.nber.org/system/files/working_papers/w29143/w29143.pdf

to be relatively small, this translates into a smaller 1.7% decline when measured by company market capitalization.

Based on these estimates, the EY study also concludes that *more costly reporting requirements could be expected to reduce the number of public companies*. This analysis estimates that a 10% increase in reporting requirement cost over the 2000-2019 period would have reduced the number of US companies traded on major exchanges further by 80 companies, with a combined 51,000 employees, $60 billion in revenue, and over $23 billion of market capitalization. It stands to reason that higher cost increases would translate into higher estimated impacts on listed companies (e.g., a 20% increase in reporting costs over this period could be expected to be double these estimates). While the EY analysis focuses on reporting requirements during the 2000-2019 period, not the SEC's proposed climate disclosure rules or other reporting requirements, it may be suggestive of the impacts of future reporting requirements

It is hard to estimate what kind of cost increase the SEC's proposed climate disclosure rules will generate. But according to industry experts, they may be costlier than the Sarbanes-Oxley Act of 2002 (SOX) which is still an active concern among public companies. According to the most recent annual survey conducted by Protiviti, "for companies that are beyond their second year of SOX compliance, average annual costs for SOX compliance went up 18% from 2021 to 2022. Thirty percent of surveyed companies beyond their second year of SOX compliance spent more than $2 million in their most recent fiscal year, versus 24% the prior year."[23]

As noted above, this does not mean that companies cease to exist if they do not go public. However, as mentioned before, the trends show that wealth and value creation by public companies is significant. In addition to the overall potential impact of public companies on macro economy, there is another concern regarding the decrease in public companies and IPOs: it could limit the playing field for smaller, less-sophisticated investors and prevent them from putting their money behind big ideas that may create big value for markets and for society.[24] Shutting out the average investor from these potentially lucrative gains could also increase income inequality as private companies become increasingly funded by the wealthiest members of society.

III. How To Make SEC's Climate Disclosure Rules Less Costly

As the world capital markets contemplate some form of climate disclosure regime, the Agency's work in this field is important for the efficiency, productivity and competitiveness of U.S. capital markets. However, the finalized rule should strive to achieve these goals in a cost-effective manner. Given the size and scope of the proposed rules, it is important to get the cost-benefit analysis as accurate as possible. The cost numbers could be dramatically underestimating the overall impact of the rules given the new territory the Agency is moving in. In fact, in their own words, the SEC states that "In many cases, however, we are unable to reliably quantify these potential benefits and costs. For example, existing empirical

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[23] Protivity, "SOX Compliance Amid Rising Costs, Labor Shortages and Other Post-Pandemic Challenges," 2022. https://www.protiviti.com/US-en/insights/sox-compliance-survey?utm_source=ProPress&utm_medium=PressRelease&utm_campaign=survey_webpage&utm_id=2022+SOX+Survey&utm_term=SOX,+Sarbanes-Oxley,+internal+audit

[24] Frank Patnoy, "The Death of the IPO," November 2018, The Atlantic, https://www.theatlantic.com/magazine/archive/2018/11/private-inequity/570808/

evidence does not allow us to reliably estimate how enhancements in climate-related disclosure affect information processing by investors or firm monitoring."[25] As Former OIRA administrator Susan Dudley and former EPA policy official Brian Mannix stated, "In principle, a benefit-cost analysis should be 'complete.' It should include all the significant consequences of a policy decision: direct and indirect, intended and unintended, beneficial and harmful."[26] Unfortunately, the current cost analysis is lacking in many of these aspects. A complete analysis would be key to determine the costliest and least effective items in the proposal that require significant attention.

Another key aspect of the proposed rule that could entail significant cost is Scope 3 reporting. The proposed requirement that most public companies include Scope 3 emissions disclosures in their Form 10-K each year would impose extreme costs and potential for liability on a broad range of issuers. This requirement will drive still unforeseen burdens to companies up and down the value chain, including small and privately held companies, who have limited resources available to address the reporting requirements. As such, the ACCF recommends that the SEC rescind the proposed Scope 3 reporting requirement.

We feel that Scope 1 and Scope 2 emissions disclosures, combined with the new Regulation S-K risk disclosures, are adequate to inform investors of the exposure of publicly held companies to climate risks. Companies are now engaged and will continue to improve their understanding of Scope 3 emissions and will develop and employ new methods to track and report data. Furthermore, companies may even choose (and some do already) to report their Scope 3 emissions in the absence of an SEC mandate.

The SEC proposal document reflects the extreme complexity of the Scope 3 requirement. It is overwhelming and we, along with many others, question how it will be monitored and measured given the diverse range of businesses and investor interest. Furthermore, the data collection requirement to be applied in a consistent and aligned manner will be difficult to attain and may never be able to be fully verified. This will mean the level of investor assurance that the SEC seeks to provide will be lacking value. Analysis and estimates, along with verification processes for Scope 3 reporting will continue to evolve, it will create more work and cost and will constantly result in investors calling into question the reliability and value of Scope 3 reports and disclosures for their investment decision processes.

Should the SEC continue to advance its efforts to mandate Scope 3 emissions disclosure, ACCF does not believe that the materiality threshold and safe harbor are sufficient to protect registrants and their shareholders from the risks associated with the reporting requirements as the SEC has outlined.

The ACCF and its members recognize that the SEC endeavors to develop a workable approach to enhance transparency and understanding of the material impacts of a registrant's GHG emissions on its business and operations. We continue to recommend that the SEC rescind the Scope 3 requirement. However, we

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[25] SEC, "The Enhancement and Standardization of Climate-Related Disclosures for Investors," March 2022, pg. 333. https://www.sec.gov/rules/proposed/2022/33-11042.pdf

[26] Susan E. Dudley & Brian F. Mannix, "Improving Regulatory Benefit-Cost Analysis," 2018, Journal of Law and Politics, pg 12, http://www.lawandpolitics.org/hifi/files/issues/vol-xxxiv-no-1-fall-2018/Dudley_and_Mannix_edited_final10.10.18.pdf

are also confident that if the SEC proceeds, that any final rule will more appropriately balance the significant costs and questionable benefits of Scope 3 emissions disclosure.

Other key recommendations for the SEC to consider are:

- Extend the effective dates for compliance to give enough time to filers to develop the necessary infrastructure, as discussed above.
- Coordinate deadlines with the timelines established in other agencies' climate related actions to lessen the cost
- Reconsider the 1 percent threshold under Regulations S-X; a higher threshold could eliminate the burden on smaller companies to double check to confirm that they are below the reporting threshold.

The ACCF appreciates the chance to comment on SEC's proposed rule and supports the goal of transparency. Nevertheless, we encourage the Agency to reconsider portions of the proposed rule that could significantly impact the regulatory cost of public companies and distort the capital markets overall. We look forward to working with the SEC to ensure that any finalized rule will not distort U.S. capital markets.

Sincerely,

Mark A. Bloomfield
President and CEO
American Council for Capital Formation