OTC Markets

December 22, 2020

Via Electronic Submission

Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
rule-comments@sec.gov

Re: File No. S7-10-22: The Enhancement and Standardization of Climate-Related Disclosures for Investors

OTC Markets Group[1] is pleased to submit this comment letter in response to the Securities and Exchange Commission's (the "SEC" or the "Commission") proposed amendments to its rules under the Securities Act of 1933 and Securities Exchange Act of 1934 that would require registrants to provide certain climate-related information in their registration statements and annual reports (the "Proposal").[2]

We operate the primary over-the-counter ("OTC") electronic trading market in the United States — where regulated broker-dealers trade over 12,000 securities. Our markets are home to a diverse community of public companies: ordinary shares and ADRs of large, global corporations like Adidas, Roche and Heineken; hundreds of U.S. community banks; many venture-stage companies; and over 1,200 active SEC registrants that stand to be impacted by the Proposal.[3]

We are firm believers in the power of public company disclosure. We have seen our own markets transform over the past several decades from a paper-based system to a vibrant, data-driven electronic trading market.

We also understand the desire to focus on climate-related disclosure. However, we believe the framework for that disclosure should be designed to inform not just investors but also *consumers, customers and communities*. Impactful climate disclosure should be "reliable,

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[1] OTC Markets Group Inc. operates the OTCQX® Best Market, the OTCQB® Venture Market and the Pink® Open Market for 12,000 U.S. and global securities. Our OTC Link® Alternative Trading Systems (ATSs) provide critical market infrastructure that broker-dealers rely on to facilitate trading. Our innovative model offers companies more efficient access to the U.S. financial markets. OTC Link ATS, OTC Link ECN and OTC Link NQB are SEC regulated ATSs, operated by OTC Link LLC, member FINRA/SIPC.

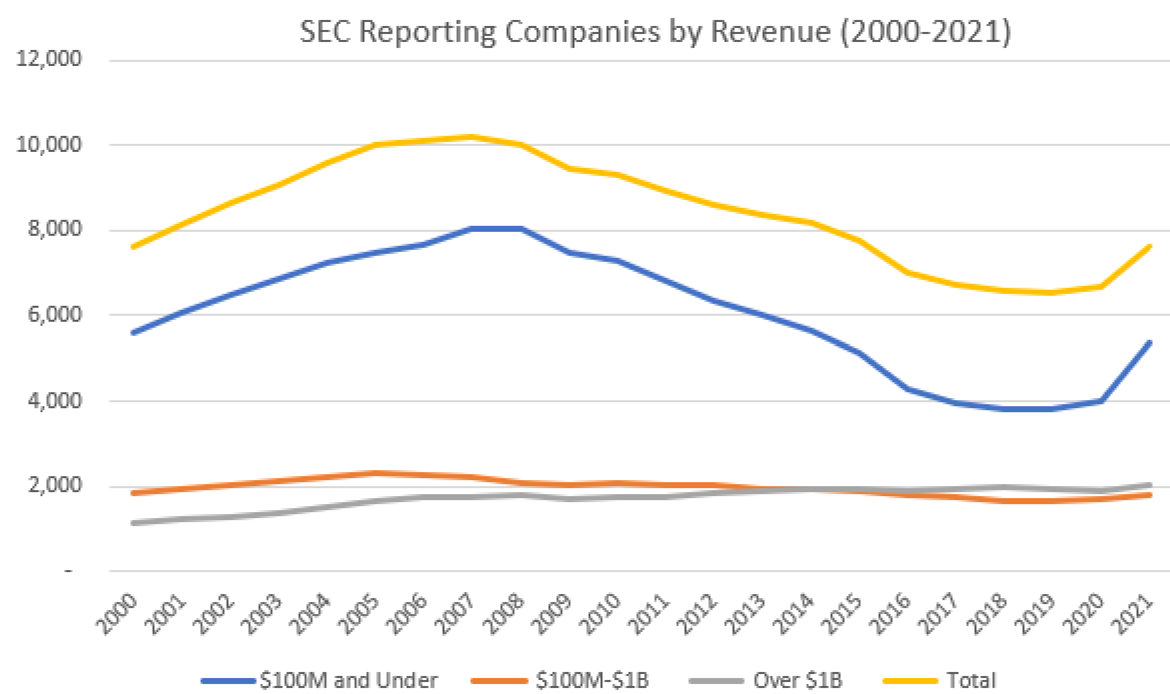
[2] The Enhancement and Standardization of Climate-Related Disclosures for Investors, Release Nos. 33-11042; 34-94478 (March 21, 2022), 87 FR 21334 (April 11, 2022), available at https://www.sec.gov/rules/proposed/2022/33-11042.pdf.

[3] Data is based on the total number of OTC-traded companies (i.e., not listed on a U.S. exchange) that filed annual reports with the SEC in 2021 and are current in their reporting requirements. OTC-traded companies on the Expert or Grey markets that may be delinquent in their SEC reporting requirements are not included. Data referenced herein is provided by EDGAR® Online LLC, a wholly owned subsidiary of OTC Markets Group Inc. EDGAR® is a trademark of the SEC. OTC Market Group's products and services are not affiliated with or approved by the SEC.

comprehensible and globally comparable."[4] In this regard, the Environmental Protection Agency and similar agencies with appropriate subject matter jurisdiction can best regulate climate disclosure.

Notwithstanding broader policy considerations, ***the Proposal fails to address the outsized impact of these enhanced obligations on smaller SEC reporting companies and will further discourage companies from going public***. The Proposal risks widening the divide between our public and private markets by further solidifying a two-tier system where publicly held companies are saddled with additional obligations while large, private companies can continue to operate in the shadows with minimal transparency and a competitive advantage.

The impact of the Proposal will be felt by exchange-listed and OTC-traded companies and is likely to exacerbate the longstanding trend of companies choosing to remain private. The chart below shows the total number of active SEC reporting companies over the past 20 years:[5]



[4] *See* Irene Heemskerk, Nutrition Labels Help Us Make Better Food Choices. Climate Labels Could Do the Same for Sustainability (April 15, 2022), available at: https://time.com/6166192/climate-labels-sustainability/.

[5] The data in this chart represents the total number of exchange-listed and OTC-traded companies that filed annual reports with the SEC for the respective year and were current in their reporting requirements for that year (i.e., does not include delinquent filers). Annual revenue information is based on data reported to the SEC in each of the periods ending on December 31 for the respective years.

What can we learn from this chart?

- **The total number of active SEC registrants has declined significantly,** from a 20-year high of 10,185 in 2007 to a low of 6,534 in 2019.
- **The decline in small companies (<$100M revenue) is the main driver of the overall decline,** dropping nearly 50% from 6,223 in 2007 to 2,927 in 2019 and has just begun to recover in the last two years.
- **The number of mid-sized companies ($100M-$1B revenue) has remained flat.**
- **The number of large companies (>$1B revenue) has grown** at a modest rate of 3% year over year.

Small companies are essential to creating robust public markets and growing the total number of public companies. OTC Markets Group serves as an onramp to the U.S. capital markets, with a tiered market structure designed to encourage public disclosure and facilitate capital formation. Our markets are less complex and costly than an exchange listing, allowing management teams to grow their business as they learn how to be public. As companies provide the required disclosure and make their way to our higher-tier marketplaces, their access to capital and liquidity greatly improves. Over the past five years, an average of 80 OTC companies have graduated to an exchange listing each year (over 400 in total over the past five years), making our markets the most successful venture markets in the world.

Our markets are home to over 1,200 active SEC registrants. Most of these companies would likely fall within the “Smaller Reporting Company” (“SRC”) definition: 91% have revenues under $100 million, 4% have revenues between $100 million and $1 billion and 5% have revenues over $1 billion. The small companies (<$100M revenue) represent a wide array of industries, including manufacturing, technology and natural resources, and are based across 46 U.S. states and 29 countries. They have, on average, 86 employees and annual revenues of $5 million. These small companies have chosen to join our public markets and provide disclosure to U.S. investors and the SEC, despite the costs associated with doing so.

We are concerned that the Proposal’s significant additional disclosure requirements will unduly burden smaller public companies and discourage private companies from joining the public markets. The Proposal’s economic analysis estimates an SRC compliance cost of $490,000 in the first year and $420,000 in subsequent years.[6] Because the SRC definition casts such a wide net, the Proposal would effectively impose the same costs on a company with $100 million in revenue as it would on a company with $5 million in revenue. ***The costs would be prohibitive for a meaningful number of SEC registrants (both exchange-listed and OTC-traded), often surpassing 10% of their annual revenues.***

We are also concerned that the Proposal unfairly shifts cost burdens in a manner that will harm capital formation. There are numerous financial data providers that collect and resell ESG information based on investor demand. Under the proposed regime, the cost of collecting and formatting ESG data would shift to issuers, many of which are not prepared to bear those costs.

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[6] Proposal, supra note 2, at 373.

Such a significant reorganization of the investing data market must consider basic differences among investors. While some investors prefer an ESG strategy or investing passively in only the largest companies through indexes, others choose to focus on individual firm financial performance and internal rate of return on capital (IRR). The Proposal ignores these differences and is overly prescriptive in choosing one model of investing over another, to the detriment of value investors and smaller companies that are not included in major indices.

For the reasons set forth above, we urge the Commission to follow the policy recommendations in its most recent Report on the Annual Small Business Forum, and "[c]onsider the impact of the proposed environmental, social, or governance (ESG) regulations on small and medium-sized companies, including whether such requirements will discourage companies from going public."[7]

We offer three alternatives that would achieve the SEC's climate-related disclosure agenda, while also facilitating capital formation for smaller public companies:

- **Exempt all registrants with under $1 billion in annual revenues.** By beginning with only the largest public companies, the Commission can create a pilot program to study and assess the utility and effectiveness of climate disclosures before applying them to smaller companies.
- **Exempt all OTC-traded registrants.** The role of the OTC market is to provide brokers with a regulated platform to trade securities that are not listed on an exchange. In this sense, our markets serve an essential function within the broader U.S. capital markets landscape, bridging the divide between the private and public markets. Exempting all OTC-traded companies from climate-related disclosure would recognize our markets' important function as an onramp and gateway to a full exchange listing.
- **Adopt a voluntary disclosure regime for all registrants.** The decline in the number of small- and medium-sized public companies over the past two decades is due in part to enhanced regulatory obligations imposed on SEC registrants, such as Sarbanes Oxley controls and XBRL mandates. In particular, the Commission should consider lessons learned from XBRL reporting standards. XBRL reporting was not an industry standard when the Commission's rules became effective. As a result, it shifted costs to issuers that had previously been borne by third-party data providers. Similarly, the Proposal's Scope 3 emissions requirements are "a relatively new type of metric, based largely on third-party data, that [the SEC has] not previously required."[8] We believe that the longstanding "materiality" standard for public company disclosure ensures that investors will receive sufficient climate-related information to make an informed investment decision. A voluntary framework for climate disclosure that incorporates industry best-practices would encourage companies to provide relevant information and shift data collection and processing costs back to third-party data providers.

The suggested approaches above would support smaller company growth and entry into the public market, while ensuring that the largest companies, with the greatest financial wherewithal

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[7] SEC Report on the 41st Annual Small Business Forum, available at: https://www.sec.gov/files/2022-oasb-annual-forum-report.pdf?utm_medium=email&utm_source=govdelivery.
[8] Proposal, supra note 2, at 173.

and often the greatest environmental impact, provide important climate-related disclosure to the public.

Our public markets function best when individuals can own shares in businesses that they work for, that make the products and services they consume, or that operate in their community. The Commission should encourage these companies to be public, bring transparency to their business operations and give the public access a broader range of investing opportunities.

We welcome the opportunity to discuss our comments with the Commission.

Very truly yours,

Cass Sanford
Deputy General Counsel
OTC Markets Group Inc.