The SEC's Climate Disclosure Rule: Critiquing the Critics

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Climate change is an existential phenomenon, which entails a wide variety of physical risks as well as sizeable but underappreciated economic risks. In March 2022, the U.S. Securities and Exchange Commission (SEC) moved to address some of the information gaps related to the effects of climate change on firms by proposing a rule that requires public companies to report detailed and standardized information about important climate-related matters for the benefit of investors and markets. Though the rule proposal was welcomed by many market participants, it was also met with a level of opposition that was unusual in both its intensity and consistency. Instead of following standard practice and engaging with the specific policy judgments made by the SEC in an effort to improve the final rule through constructive notice-and-comment rulemaking, many critics chose to attack every aspect of the rule proposal and the SEC's very decision to pursue a climate disclosure rule. The critics disputed the SEC's statutory authority and motivations, questioned the materiality of information about the economic impacts of climate change, and advanced certain novel administrative and constitutional law theories that had gained traction in other, unrelated contexts. Unless the SEC yields to pressure and abandons the climate disclosure project, these same arguments will serve as the basis for the widely predicted litigation against the final rule.

This Article presents an original analysis of some of the principal challenges to the SEC's climate disclosure rule and, ultimately, finds them unpersuasive. A close review of the features of the traditional disclosure regime, many of them long forgotten, and of the features of the SEC's rule, many of them distorted by the critics, suggests that the rule is in keeping with longstanding regulatory practice. In short, the SEC has the statutory authority to act, its motivations are neither improper nor novel, materiality, when properly understood, does not present an obstacle, and theories pertaining to "major questions" and "compelled speech" are misplaced in this context.

The Article contributes to the debate on climate-related disclosure in two ways. First, it draws attention to the flawed legal and policy arguments against the SEC's climate disclosure initiative and the distracting rhetoric that has accompanied them. And, second, it highlights the rule's core function, which is to put in place an information-generating framework to help capital markets and capital market participants—the primary intended beneficiaries of SEC regulation—with the climate-related economic challenges that lie ahead.

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* Associate Professor, Emory University School of Law. Some of the ideas contained in this Article were previewed in an essay I published in the Oxford Business Law Blog in March 2022, in my commentary on aspects of the SEC's proposal in various media outlets between March and September 2022, and in a comment letter to the SEC, which I co-authored with Jill Fisch, Donna Nagy, and Cynthia Williams in June 2022 on behalf of 30 corporate and securities law scholars. I am grateful to my comment letter co-authors and to the other scholars who engaged with these ideas, including John Coates, John Coffee, James Cox, Joe Grundfest, Sarah Haan, Joan Heminway, Rob Jackson, and Don Langevoort. I am also grateful to participants in presentations at UCLA School of Law and the 2022 National Business Law Scholars Conference. The views expressed herein are mine alone and should not be attributed to any of the individuals named above. I would like to thank the editors of the *Rutgers Law Record* for so graciously agreeing to publish this Article on an expedited schedule in light of the time-sensitive nature of the subject matter.

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INTRODUCTION

Climate change is a multi-faceted problem that, first and foremost, threatens human and natural habitats in existential ways. Quite apart from its effects on the physical environment, climate change is also an economic problem that requires extensive adaptation by firms across the economy.[1] The transition that lies ahead has been described aptly as "the biggest economic transformation since the Industrial Revolution."[2] Estimates suggest that without action, a significant portion of global GDP will be lost due to climate change by 2050.[3] Despite their paramount importance, however, the economic effects of climate change and the required adaptive responses remain poorly understood due to inadequate information at the level of individual firms.[4] And, importantly, these economic effects and the need for economic adaptation do not depend on matters that may still be subject to debate in some quarters, including whether the environmental effects of climate change can be slowed or reversed, or the extent to which climate change is due to human activity.[5]

The Securities and Exchange Commission (SEC), which oversees U.S. capital markets, moved to address some of the climate information gaps in March 2022 by issuing a rule proposal (the "Proposal" or "rule") that would require public companies to report detailed and standardized information about various climate-related matters.[6] These matters include: climate-related risks and their actual or likely material impacts on a firm's business, strategy, and outlook; governance of climate-related risks and relevant risk management processes; greenhouse gas (GHG) emissions; certain climate-

[1] *See, e.g.*, Renee Cho, *How Climate Change Impacts the Economy*, COLUM. UNIV.: STATE OF THE PLANET (June 20, 2019), https://bit.ly/3BJISr3. In addition to its physical and economic effects, climate change also has implications for national security, foreign policy, global food security and migration patterns, and various other areas. *See, e.g.*, White House, Fact Sheet: Prioritizing Climate in Foreign Policy and National Security (Oct. 21, 2021), https://bit.ly/3Wi377m.

[2] *See* Ben Geman & Andrew Freedman, *Climate Spending is a Story of the Century*, AXIOS (Apr. 9, 2021), https://bit.ly/3PArEC6 (quoting U.S. government climate envoy John Kerry).

[3] *See* SWISS RE INST., THE ECONOMICS OF CLIMATE CHANGE (2021), https://bit.ly/3v1EYpI (suggesting an 18% drop in worldwide GDP if no mitigating actions are taken).

[4] *See, e.g.*, Emma Cox, *See Your Climate Blind Spots*, WORLD ECON. F. (May 25, 2022), https://bit.ly/3hGDD4N (highlighting relevant evidence).

[5] *See, e.g.*, Kevin Anderson & Jessica Jewell, *Debating the Bedrock of Climate-Change Mitigation Scenarios*, NATURE (Sept. 16, 2019), https://bit.ly/3BWxh80 (providing an overview of some of the debates and associated relevance). There is no legitimate disagreement on the basic facts, however, including that the earth's climate is warming. *See, e.g.*, NASA, SCIENTIFIC CONSENSUS: EARTH CLIMATE IS WARMING, https://climate.nasa.gov/scientific-consensus (last updated Dec. 16, 2022) ("[S]cientists always focus on the evidence, not on opinions. Scientific evidence continues to show that human activities (primarily the human burning of fossil fuels) have warmed Earth's surface and its ocean basins, which in turn have continued to impact Earth's climate.").

[6] *See* Press Release, U.S. Sec. & Exch. Comm'n, SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors (Mar. 21, 2022), https://bit.ly/3PMXpb4.

related financial statement metrics, and information about climate-related targets and goals, and transition plans, if any.[7]

Many market participants welcomed the rule and many were eager to engage with some of its technical details, which, like with any initial regulatory release, could stand to be finetuned during notice-and-comment rulemaking. Surprisingly, however, there were also a number of critics who chose to attack the SEC's very decision to pursue a climate disclosure rule. Their goal was not to improve the rule but to persuade the SEC, directly or through public pressure, to abandon it. Many of these critical arguments had first started appearing soon after the SEC kicked off the climate disclosure project in 2021.[8] They were refined and advanced more forcefully in response to the March 2022 Proposal. And, when the SEC finalizes the proposed rule, as it is expected to do, these same arguments will be deployed in the widely predicted court challenges. Given their implications and recurrence, it is important to assess whether these arguments have any merit.

A careful and dispassionate review of the SEC's Proposal suggests that it is firmly grounded within the traditional SEC disclosure framework, which was established in 1933 and which has been in place ever since. The SEC has the statutory authority to act on climate-related disclosure, its motivations are neither improper nor novel, materiality, when properly understood, does not present an obstacle, and theories pertaining to "major questions" and "compelled speech" are misplaced in this context. The 2022 Proposal is certainly ambitious (and, many would submit, overdue), but, viewed in the appropriate historical context, it is by no means extraordinary. To support this view, the Article highlights features of the nine-decade-old disclosure regime, many of them long forgotten, as well as certain features of the 2022 Proposal that have been distorted by the critics. In examining the attacks against the Proposal, the Article also draws attention to their internal contradictions and the ways in which they use rhetoric and superficially intuitive arguments to misrepresent the applicable legal framework.

The Article proceeds as follows. Part I outlines the sources of opposition to the SEC's climate-related disclosure project. Part II examines the often-misleading dichotomy between disclosure serving shareholders and disclosure that may be useful to stakeholders and then considers the role of climate expertise and constructive industry engagement in formulating new disclosure requirements. Part III offers a historical perspective on statutory authority and regulatory practice. Part IV focuses on the complex concept of materiality as it applies to the SEC's Proposal and dispels several myths about materiality that have been advanced in an effort to straightjacket the SEC's ability to promulgate relevant disclosure rules. Part V briefly discusses objections to the Proposal based on novel and untested theories such as "major questions" (stemming from recent Supreme Court cases in other areas) and "compelled speech" under the First Amendment.

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[7] *See* U.S. Sec. & Exch. Comm'n, The Enhancement and Standardization of Climate-Related Disclosures for Investors, Release Nos. 33-11042, 34-94478, 87 Fed. Reg. 21,334 (Apr. 11, 2022).

[8] *See, e.g.*, Jonathan D. Brightbill, *Evaluating Challenges to the SEC's ESG Disclosure Proposal*, WINSTON & STRAWN LLP (Aug. 25, 2021), https://bit.ly/3HI05VC (discussing anticipated challenges to the SEC's proposal seven months before the actual proposal was released).

Because this Article is aimed at a broader audience, it is deliberately more conversational in tone and more targeted in scope.[9] The debate on the SEC's climate-related disclosure project is likely to continue for some time and the goal here is to steer it in a more constructive direction rather than to settle it.

I. THE VANGUARD OPPOSITION TO CLIMATE-RELATED DISCLOSURE

The SEC's Proposal was portrayed as unprecedented (and, hence, illegitimate) even before it was unveiled on March 21, 2022. A well-coordinated campaign to oppose any SEC action on climate-related disclosure had launched in March 2021, immediately after Acting SEC Chair Allison Herren Lee invited public input on climate disclosure,[10] and it quickly gained momentum. As a result, the arguments against the Proposal were ready even before the Proposal was finalized. An op-ed in the *Wall Street Journal*, published the day before details of the actual Proposal became available, criticized the SEC for taking an "activist approach to climate policy—an area far outside the SEC's authority, jurisdiction and expertise [which] will deservedly draw legal challenges," for, among other reasons, going against the SEC's "time-tested approach to capital allocation."[11] By December 2022, the *Wall Street Journal* had published more than a dozen additional opinion pieces that criticized the SEC's Proposal on climate-related disclosure.[12]

The most visible and vocal early critic of the SEC Proposal came from within the agency. In casting the sole dissenting vote against the Proposal, SEC Commissioner Hester Peirce issued a 9,000-word statement titled "We are NOT the Securities and Environment Commission – At Least Not Yet."[13] This statement set out the legal and rhetorical blueprint for opposing the Proposal, and it was subsequently quoted in the

[9] For the most part, the Article does not discuss the specific justifications for climate-related disclosure since it broadly agrees with the analysis presented in the SEC's Proposal. For excellent academic commentary, see Jill E. Fisch, *Making Sustainability Disclosure Sustainable*, 107 GEO. L. J. 923 (2019); Cynthia A. Williams & Donna M. Nagy, *ESG and Climate Change Blind Spots: Turning the Corner on SEC Disclosure*, 99 TEX. L. REV. 1453 (2021); Madison Condon, *Market Myopia's Market Bubble*, 2022 UTAH L. REV. 63 (2022); Virginia Harper Ho, *Modernizing ESG Disclosure*, 2022 U. ILL. L. REV. 277 (2022); and other works.

[10] *See* Allison Lee, Comm'r, U.S. Sec. & Exch. Comm'n, Public Input Welcomed on Climate Change Disclosures (Mar. 15, 2021), https://bit.ly/3Vofm0T. The March 2021 request for input generated over 700 substantive comment letters, over 5,000 form letters, and resulted in over 50 meetings between SEC officials and interested parties. Despite the opposition of groups such as the U.S. Chamber of Commerce, the National Association of Manufacturers, and some Republican attorneys general, the vast majority of comments, including comments by mainstream investor constituencies, were supportive of SEC action. *See* U.S. Sec. & Exch. Comm'n, Comments on Climate Change Disclosures (last modified July 28, 2022), https://bit.ly/3YMvX1q.

[11] *See* Jay Clayton & Patrick McHenry, *The SEC's Climate-Change Overreach*, WALL ST. J. (Mar. 20, 2022), https://bit.ly/3Yzd8i3.

[12] Author's survey of *Wall Street Journal* opinion pieces as of Dec. 22, 2022.

[13] Hester Peirce, Comm'r, U.S. Sec. & Exch. Comm'n, *We are NOT the Securities and Environment Commission – At Least Not Yet* (Mar. 21, 2022), https://bit.ly/3viMw7r (internal quotation marks omitted).

majority of comment letters critical of the Proposal.[14] Commissioner Peirce admonished that the Proposal "turns the disclosure regime on its head" and erects "a hulking green structure" that will "trumpet" a "revised mission" for the SEC: "protection of stakeholders, facilitating the growth of the climate-industrial complex, and fostering unfair, disorderly, and inefficient markets."[15] This certainly sounds both problematic and dramatic, but once we set aside the rhetorical flourishes, we see that many of the arguments against the Proposal misstate the applicable legal constraints and mischaracterize important aspects of the Proposal. Moreover, even though Commissioner Peirce went out of her way to praise "the existing regulatory framework that for many decades has undergirded consistent, comparable, and reliable company disclosures,"[16] her lengthy dissenting statement revealed that she actually opposes many important and established elements of the very framework she says she wants to conserve. These include, for example, congressionally-mandated auditor attestation provisions stemming from the 2002 Sarbanes-Oxley Act,[17] as well as long-settled SEC disclosure mandates on executive compensation, related party transactions, and environmental litigation.[18]

In the subsequent months, industry lobbyists,[19] national politicians,[20] and state officials[21] picked up the critical mantle. Many of the arguments opposing the Proposal, however, stemmed not from specific flaws in the Proposal but from a general opposition to any governmental action on climate change—a point further confirmed by a *New York Times* expose examining the policy networks that were involved in opposing the SEC Proposal and other climate-related initiatives.[22] Unfortunately, some of the critical

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[14] Author's survey of comments submitted and posted on the SEC's website as of Dec. 22, 2022. *See* U.S. Sec. & Exch. Comm'n, Comments for "The Enhancement and Standardization of Climate-Related Disclosures for Investors" (last visited Dec. 22, 2022) [hereinafter SEC Comment File], https://bit.ly/3jolDfY.

[15] *See* Peirce, *supra* note 13.

[16] *Id*.

[17] *See id* (opposing the Proposal's attestation mandate because it "could be a new sinecure for the biggest audit firms, reminiscent of the one given them by Section 404(b) of the Sarbanes-Oxley Act.").

[18] *Id.* at n.15.

[19] *See, e.g.*, Letters from U.S. Chamber of Commerce (June 17, 2022), National Association of Manufacturers (June 6, 2022), and American Petroleum Institute (June 17, 2022), among others, in SEC Comment File, *supra* note 14.

[20] *See, e.g.*, Letter from Republican Members of the U.S. House of Representatives (June 15, 2022); Letter from Senators Kevin Cramer, Shelly Moore Capito & Other Members of the U.S. Senate (Apr. 5, 2022); Letter from Representatives Ted Budd, Ralph Norman & Other Members of the U.S. House of Representatives (Apr. 11, 2022), in SEC Comment File, *supra* note 14.

[21] *See, e.g.*, Letter from State Attorneys General (June 15, 2022); Letter from State Attorneys General (June 17, 2022); Letter from State Attorneys General (July 13, 2022); Letter of Scott Fitzpatrick, State Treasurer of Missouri (June 17, 2022), in SEC Comment File, *supra* note 14.

[22] Among other evidence, the *New York Times* report discussed the State Financial Officers Foundation, which, according to a quoted expert "is a key node in a network of political groups waging a coordinated attack on climate policy" and is working "to weaponize state treasurers' offices against federal appointees, regulations, and corporate policies that address climate change."

arguments showed a lack of awareness of longstanding and technical aspects of U.S. securities law and were built on the erroneous but oft-repeated premise that the Proposal seeks to advance environmental goals. (These matters are the subject of Parts II–IV.) In effect, the SEC Proposal—and the SEC itself—became part of a much larger battle about climate change, which distracted from the debate about the merits of the actual Proposal.[23]

While this debate was unfolding in 2022, Congress passed two pieces of legislation that provided extensive funding for climate-related programs: the bipartisan CHIPS and Science Act (CHIPS) and the Inflation Reduction Act (IRA).[24] These bills were not related to climate disclosure, but they further bolstered the case for such disclosure because of the massive federal spending involved (over $500 billion by 2030).[25] The bills advance two primary goals: (1) reducing GHG emissions through tax and other incentives; and (2) supporting research on clean energy and promoting the growth of zero-carbon industries.[26] The new federal spending will impact the financial and operational prospects of all firms across the economy in different ways and over the course of many years; investors need to understand these effects as they make investment decisions and allocate capital. For example, firms that can reduce their GHG emissions stand to benefit under the IRA, while those that cannot reduce emissions will fare relatively worse. And, as green energy becomes cheaper due to new R&D funded by CHIPS, firms with strong plans for decarbonization will benefit, while those reliant on fossil fuels will likely fare worse. The effects cannot be predicted but information supplied under the SEC rule will help investors distinguish among firms, take advantage of relevant investment opportunities, and mitigate new risks.[27]

II. THE SEC'S MOTIVES AND EXPERTISE

Arguments against the Proposal that question the SEC's motives and expertise are misplaced but they have gained some traction because of their superficially intuitive nature: Why is the SEC, a capital markets regulator, proposing a rule that seems to address issues that had been championed by environmental NGOs? Can an SEC

See David Gelles, *How Republicans Are 'Weaponizing' Public Office Against Climate Action*, N.Y. TIMES (Aug. 5, 2022), https://bit.ly/3GhwH7k.

[23] The SEC received many supportive comment letters, including supportive letters from significant market participants (such as issuers, institutional investors, asset managers, and various gatekeepers), former SEC officials, experts in securities law, experts on the First Amendment, and others. The focus here is on the critics of the Proposal and I do not attempt to analyze the entire comment file, which contained more than 4,000 substantive comment letters and more than 10,000 form letters. *See* SEC Comment File, *supra* note 14.

[24] *See* Robinson Meyer, *Congress Just Passed a Big Climate Bill. No, Not That One.*, THE ATLANTIC (Aug. 10, 2022), https://bit.ly/3WmhuaF.

[25] *Id*.

[26] *Id*.

[27] *See* Letter from Americans for Financial Reform Education Fund (Dec. 1, 2022) in SEC Comment File, *supra* note 14.

disclosure rule do anything to mitigate climate change? And is the SEC equipped to adopt a rule that deals with technical scientific matters? Upon closer examination, however, none of these arguments survives scrutiny: the rule serves traditional investor audiences and there is no evidence that the SEC has been captured by special interests; the rule does not aim to mitigate climate change and, hence, should not be judged by such a standard; and rule is about disclosure regulation, not command-and-control regulation, and the SEC has ample experience with developing disclosure rules in technical areas.

A. *Is the SEC Advancing Investor Interests or Special Interests?*

The SEC's Proposal for climate-related disclosure prompts a question that has often been asked about new disclosure rules: Is the disclosure intended for shareholders or for stakeholders?[28] But this is not a binary choice, and posing it as such automatically shifts the terms of the debate in favor of opponents of climate-related disclosure, regardless of the actual content of the Proposal. Since climate change has society-wide implications, information about it will inevitably resonate beyond the boundaries of the disclosing firm and the capital markets, even when the focus is on financially-material disclosure relying on investor- and issuer-generated disclosure frameworks (as is the case here). The social resonance of climate-related disclosure can drown out its clear-cut financial relevance, render any proposed disclosure rule suspect, and lead to a situation that, when we stop and think about it, is quite illogical: A subject matter's relevance to one audience (stakeholders) is used as an argument to cancel out the well-established relevance of that same subject matter to another audience (investors). This is a general vulnerability that applies not just to climate-related disclosure, but to other ESG disclosure as well. It is important to understand it and de-bias policymaking accordingly.

In her dissenting statement, Commissioner Peirce deftly zeroed in on this vulnerability by asserting that the Proposal "tells corporate managers how regulators, doing the bidding of an array of non-investor stakeholders, expect them to run their companies" and "forces investors to view companies through the eyes of a vocal set of stakeholders, for whom a company's climate reputation is of equal or greater importance than a company's financial performance."[29] Reading this, one would think that the Proposal was written by the Sierra Club or the Natural Resources Defense Council—or by a Washington D.C. bureaucrat, who is either clueless or captured, or both. Yet, the Proposal did not originate with environmental groups, nor is there any

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[28] *See, e.g.*, Ann Lipton, *Not Everything Is About Investors: The Case for Mandatory Stakeholder Disclosure*, 37 YALE. J. ON REG. 499 (2020) (criticizing the use of the investor-focused disclosure regime as a means of supplying important information to non-investor audiences); *see also* Steven A. Bank & George S. Georgiev, *Securities Disclosure As Soundbite: The Case of CEO Pay Ratios*, 60 B.C. L. REV. 1123 (2019) (discussing the debate on the investor- and stakeholder-focused justifications for the pay ratio disclosure mandate during the rulemaking process).

[29] Peirce, *supra* note 13.

evidence that the SEC has been captured by environmental groups.[30] Moreover, a rule from an agency that is hypothetically captured would look very different from the actual rule proposed by the actual SEC.[31]

At most, the SEC can be faulted for citing environmental organizations more than it cited investors in parts of the proposing release.[32] Even this can be explained by the context because environmental organizations have studied the economic impacts of climate change on firms, and, moreover, it is the SEC's standard practice to mention all relevant comments when discussing a particular point. But since mainstream investor groups have made many of the same points as those environmental organizations, the SEC can and should fix this issue in the final release.

The Proposal's actual disclosure requirements draw on technical frameworks for financially-material disclosure developed by expert groups such as the Task Force on Climate-Related Financial Disclosures (TCFD) and the Greenhouse Gas Protocol.[33] Take the TCFD, for example: Its members include representatives of mainstream investors (including BlackRock and UBS Asset Management), banks (JP Morgan, Citibanamex), insurance companies (Aviva, Swiss Re, Axa), giant industrial firms (BHP, Eni, Tata Steel, Unilever), rating agencies (Moody's, S&P), accounting firms (Deloitte, E&Y), and others.[34] The TCFD's secretariat is headed not by a professional

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[30] In addition to the absence of evidence of capture here, the extensive literature analyzing the SEC as an administrative agency contains no suggestion that the SEC has been captured, or is susceptible to capture, by special interest groups representing stakeholders. *See, e.g.*, Stephen J. Choi & A.C. Pritchard, *Behavioral Economics and the SEC*, 56 STAN. L. REV. 1 (2003); James D. Cox & Randall S. Thomas, *Revolving Elites: The Unexplored Risk of Capturing the SEC*, 107 GEO. L.J. 845 (2019).

[31] *See* Letter from John Coates IV, John F. Cogan Professor of Law and Economics, Harvard Law School (June 1, 2022), https://bit.ly/3PPpVck (noting that the SEC rule is likely to disappoint environmental advocates in various ways because of its investor and public-company focus). From an environmental perspective, there may be a strong interest in generating information about the biggest polluters. Increasingly, the biggest polluters are private firms, but those firms are not covered by the SEC rule proposal. *See* George S. Georgiev, *The Breakdown of the Public–Private Divide in Securities Law: Causes, Consequences, and Reforms*, 18 N.Y.U. J. L. & BUS. 221, 284-86 (2021); *see also* George S. Georgiev, *Is "Public Company" Still a Viable Regulatory Category?*, 13 HARV. BUS. L. REV. 1 (2023).

[32] *See* Letter from Lawrence A. Cunningham, Professor of Law, George Washington University, Corresponding Author, on Behalf of Twenty-Two Professors of Law and Finance (Apr. 25, 2022), https://bit.ly/3WGj8nx (noting the Proposal's citation patterns).

[33] The TCFD is an independent organization comprised exclusively of capital market participants and their professional advisors and created at the behest of the Financial Stability Board (FSB). The FSB was established in 2009 to, inter alia, "assess vulnerabilities affecting the global financial system," and includes among its members the SEC, the Board of Governors of the Federal Reserve System, and the U.S. Department of the Treasury. *See* FINANCIAL STABILITY BOARD, MEMBERS OF THE FSB, https://bit.ly/3sY8U5x. The Greenhouse Gas Protocol accounting standards for disclosing greenhouse gas (GHG) emissions have been developed for over 20 years with input from industry associations, civil society experts, the World Business Council for Sustainable Development, and the World Resources Institute. *See* Greenhouse Gas Protocol, www.ghgprotocol.org (stating that 92% of Fortune 500 companies that report on their GHG emissions to voluntary data repository CDP do so according to the GHG Protocol).

[34] *See* TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES: STATUS REPORT 76-77 (2021), https://bit.ly/3jrUAAt.*Id*.

environmental advocate, but by a leader in the financial industry and capital markets, Mary Schapiro, who holds the unique distinction of having served as an SEC Commissioner, Chair of the SEC, Chair of the CFTC, and CEO of FINRA.[35] And, for better or worse, no environmental NGOs or stakeholder organizations are represented on the TCFD. As its name suggests, the TCFD's focus is on *financial disclosures* of the kind that investors require and use. The TCFD has generated an impressive roster of supporters and official adopters in just over six years,[36] and, importantly, each of the "big three" (BlackRock, State Street, and Vanguard) has endorsed the TCFD framework.[37]

Zooming out, it is worth recalling a basic postulate of financial economics: Information released pursuant to mandatory securities disclosure requirements is non-rivalrous and non-excludable in character.[38] In practice, this means that the information can be used both by its target audience (investors) and by other audiences, but, importantly, that the use of disclosure by other audiences does not diminish its utility to the target audience. Given the economic, social, and political salience of climate-related information, it is inevitable that at least some of the information released pursuant to any new SEC disclosure requirements will be of interest to non-investor constituencies. Indeed, such constituencies may elect to become involved in the rulemaking process by submitting comment letters to the SEC, which the SEC may then cite in its rulemaking releases. Nevertheless, a subject matter's relevance to one audience (stakeholders) does not negate the relevance of that same subject matter to another audience (investors). This is not a contested proposition: At the start of the Covid-19 crisis in 2020, for example, the Republican-appointed leadership of the SEC spoke approvingly of the collateral benefits of investor-facing disclosure for society as it required new specialized disclosure.[39] So long as the SEC continues to be focused on and guided by the informational needs of mainstream investors, it is on solid footing regardless of the collateral effects of its disclosure rules with respect to other audiences.[40]

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[35] *Id.*, at 77.

[36] *Id.*, at 26-54.

[37] See *id.*; *see also* Jason Halper et al., *Asset Management Industry Confronts the Challenges Presented by Climate Change Transition*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 28, 2022), https://bit.ly/3PAeepR.

[38] *See, e.g.*, ONNIG H. DOMBALAGIAN, CHASING THE TAPE: INFORMATION LAW AND POLICY IN CAPITAL MARKETS 27-28 (2015).

[39] *See* Jay Clayton, Chairman & William Hinman, Dir., Div. of Corp. Fin., U.S. Sec. & Exch. Comm'n, *The Importance of Disclosure—For Investors, Markets and Our Fight Against COVID-19* (Apr. 8, 2020), https://bit.ly/3z9smjx ("High quality disclosure will not only provide benefits to investors and companies, it also will enhance valuable communication and coordination across our economy—including between the public and private sectors—as together we pursue the fight against COVID-19. This transparency can foster confidence in countless specific instances, for example, between a supplier and a manufacturer as well as between an investor and a company, which in combination will benefit all.").

[40] A number of other important disclosure categories implicate non-investor constituencies: cybersecurity information is of potential interest to customers (in addition to investors), information about human capital management matters is of potential interest to employees (in addition to

B. *What is the Rule's Purpose and How Should It Be Judged?*

The confusion about the SEC's motives also lends itself to rhetorical arguments that question the Proposal's legitimacy and effectiveness. As mentioned in Part I, the title of Commissioner Peirce's dissenting statement suggested that the SEC is acting as an environmental regulator—a "Securities and *Environment* Commission."[41] Despite the lack of evidence that the Proposal seeks to mitigate firms' impact on climate change, some commenters simply accepted this premise and then alleged that the Proposal is unwarranted because environmental goals lie outside the SEC's authority (plausible and likely true),[42] and because the Proposal cannot possibly succeed in achieving those goals (also true—because the proposal is aimed at investor protection goals).

The submission of the American Securities Association ("ASA"), an organization that "exclusively represents the wealth management and capital markets interests of regional financial services firms,"[43] illustrates this dangerous sleight of hand. The ASA alleged that "the Proposed Rule has nothing to do with the Commission's purpose or mission [but] is an environmental regulation, designed to force companies to adopt practices that will decrease their greenhouse gas emissions."[44] The ASA then proceeded to warn that "the Commission's attempt to rewrite its own authority is alarming [because] [a] central principle of administrative law is that, when an agency decides to depart from decades-long past practices and official policies, the agency must at a minimum acknowledge the change and offer a reasoned explanation for it."[45] The warning would be apt were it not for the basic fact that the Proposal is not an environmental regulation but, rather, an investor-focused one.

The erroneous premise that the Proposal has environmental goals also served as the basis for an attack on the Proposal's expected effectiveness. The ASA stated that "the Commission has failed to tell the American public exactly how it plans to empirically prove its disclosures under the Proposed Rule will impact global temperatures, America's reliance on foreign sources of energy, or the cost of food, gas,

investors), and so on. As noted above, the non-excludable nature of securities disclosure suggests that this is to be expected, while its non-rivalrous nature suggests that it is not a problem.

41 Peirce *supra* note 13 (emphasis added).

42 A textualist case can be made that the recurring references to "public interest" in the SEC statutes (usually as part of the phrase "as necessary or appropriate in the *public interest* and for the protection of investors") cover environmental goals. In addition, the National Environmental Policy Act of 1969 (42 U.S.C. § 4332) contains a clear congressional directive that "to the fullest extent possible . . . the policies, regulations, and public laws of the United States shall be interpreted and administered in accordance with" the broad environmental protection policies set forth in the statute. Notwithstanding these statutory provisions, the SEC's longstanding practice on disclosure rulemaking, discussed in Part III, does not support such an expansive interpretation.

43 AMERICAN SECURITIES ASSOCIATION, *About*, https://www.americansecurities.org/about.

44 Letter from American Securities Association to Vanessa Countryman, Sec'y, U.S. Sec. & Exch. Comm'n (June 13, 2022), https://bit.ly/3WqwV1E.

45 *Id*. (internal quotation marks omitted).

heat, and other goods and services American citizens need to live."[46] Again, if the Proposal had environmental (or consumer protection) goals, this critique would be apt, but this is not the case: both on its face and functionally, the Proposal is about investors and capital markets. Any inquiry into its expected effectiveness should focus only on these goals.

C. *Expertise Critiques vs. Constructive Engagement*

Critics of the SEC's Proposal, including Commissioner Peirce, have also pointed out that the SEC does not have the depth of expertise on climate-related matters that other, specialized regulators have.[47] And while this is true, such expertise is not necessary here since the SEC is not setting GHG emission limits, calculating carbon trading prices, drawing up climate transition plans, or setting climate resilience standards for businesses. The SEC's Proposal is limited to disclosure—and only disclosure—on a technical topic, and the SEC has decades-long experience handling disclosures on technical topics. For example, during the 1930s the Commission, rather than developing a set of internal metrics for financial disclosure, drew upon the technical framework established by FASB's predecessors. In the 1970s, the SEC drew up a specialized disclosure framework for oil and gas extraction activities (with help from expert groups, much like it has done here),[48] and it has administered this framework successfully since then.[49] As the composition of the economy has changed, the SEC has had to develop some expertise in cybersecurity disclosure, tech disclosure, human capital disclosure, and disclosure in other specialized areas.[50] The Proposal does not veer away from this time-tested approach; the only difference is that it concerns a hot-button topic—climate change. Moreover, a version of the expertise critique can be applied to any other governmental body, except the EPA and perhaps NOAA, that is responding to climate change issues in its administrative domain.[51]

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[46] *Id*.

[47] Peirce, *supra* note 13.

[48] These disclosure requirements were introduced pursuant to a directive in the Energy Policy and Conservation Act of 1975 (EPCA), which directed the SEC to "take such steps as may be necessary to assure the development and observance of accounting practices to be followed in the preparation of accounts by persons engaged, in whole or in part, in the production of crude oil or natural gas in the United States." *See* 42 U.S.C. §§ 6201-6422.

[49] *See* Modernization of Oil and Gas Reporting, Securities Act Release No. 33-8995, Exchange Act Release No. 59192, 74 Fed. Reg. 2158, 2159 (Jan. 14, 2009) (discussing the history of the oil and gas disclosure framework).

[50] *See, e.g.*, U.S. Sec. & Exch. Comm'n, Commission Statement and Guidance on Public Company Cybersecurity Disclosures (Feb. 21, 2018), https://bit.ly/3vvrDX7.

[51] To use just one example, the Department of Defense ("DoD") has identified climate change as "a critical national security issue and threat multiplier" and "a top management challenge" and is taking various steps to adapt, mitigate, and develop resilience. *See* DEPARTMENT OF DEFENSE, CLIMATE ADAPTATION PLAN (2021), https://bit.ly/3vmxbCR. Talking about the impact of climate change on its activities does not turn the DoD into an environmental regulator and the same is true for the SEC.

To be sure, the first version of any regulatory proposal is hardly ever perfect, and the SEC's Proposal on climate-related disclosure was no exception. There were many aspects of the Proposal that could have benefitted from more constructive debate and engagement. In this vein, a particularly frustrating feature of the opposition to the SEC's Proposal is that the campaign to scrap the rule likely resulted in wasted opportunities for the notice-and-comment rulemaking process to unfold as it should. Instead of following the common practice of engaging with the specific policy judgments made by the SEC in an effort to improve the substance of the rule through the rulemaking process set out in the Administrative Procedures Act, many critics simply challenged the SEC's decision to pursue rulemaking on climate-related disclosure. These challenges distracted from the Proposal's more technical (but, also, more difficult and more important) aspects, and consumed considerable bandwidth. The technical aspects relate to rule effectiveness periods, liability safe harbors, downstream/upstream reporting, and various similar matters that go directly to the corporate bottom line—compliance costs and litigation risk. As a result, by underwriting the well-orchestrated campaign against the rule, industry associations such as the U.S. Chamber of Commerce and the National Association of Manufacturers may well have done a significant disservice to their members who paid the cost of the campaign and who in the future may need to comply with a final rule that is costlier than it would have been had the industry associations engaged more constructively. There were plenty of business-friendly solutions mooted by commenters, including creative solutions from academics sympathetic to the need for climate-related disclosure.[52]

On a final note, the campaign to quash the SEC's Proposal may be particularly quixotic in light of the fact that many U.S. firms are already providing at least some of the disclosure required by the Proposal and that many others are gearing up to do so in response to ongoing demand from significant shareholders and from regulators in other jurisdictions. For example, U.S. firms with business in the European Union would have to report at least some, and possibly most, of the information in question pursuant to the EU's Corporate Sustainability Reporting Directive.[53] Other major capital market jurisdictions outside the United States are also looking at requiring disclosure either directly from issuers or indirectly, by imposing an information gathering and reporting mandate on asset managers.[54]

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[52] *See, e.g.*, Letter of Joseph A. Grundfest, William A. Franke Professor of Law and Business, Stanford Law School (June 15, 2022) (distinguishing between disclosure of climate-related information issuers already possess and the generation of new climate-related information); Letter of Scott Hirst, Associate Professor of Law, Boston University (June 17, 2022) (advocating for an "investor-optional" approach), in SEC Comment File, *supra* note 14.

[53] *See* Directive of the European Parliament and the Council As Regards Corporate Sustainability Reporting (CSRD) (adopted Nov. 2022), https://bit.ly/3vd8YPG.

[54] *See, e.g.*, Frédéric Louis, WilmerHale, *ESG: The EU's Agenda for 2022 – What You Need to Know* (Feb. 10, 2022), https://bit.ly/3aioeTU. The EU's highly visible leadership on climate disclosure issues should not eclipse the fact that all other major developed markets are making swift progress. *See* Joanna Treacy et al., K&L Gates, *ESG Regulatory Developments in the UK, Japan, and Hong Kong* (Jan. 14, 2022), https://bit.ly/3PQjlSk ("Regulators in the United Kingdom and Hong Kong are

III. STATUTORY AUTHORITY AND REGULATORY PRACTICE

Another prominent line of attack against the Proposal is that it goes beyond the authority given to the SEC by Congress because the rules are too prescriptive, not rooted in materiality, and because Congress has not directed the SEC to pursue rulemaking on this particular topic. As a result, a fair amount of debate has focused on what it means for the SEC to act as "necessary or appropriate in the public interest or for the protection of investors"—language that appears in various places in the underlying statutes and that has been part of the securities laws since they were passed in the 1930s.[55] To address these issues, we need to look to the statutory text, including Schedule A in the original Securities Act, to judicial interpretations of the SEC's disclosure authority, and to the SEC's extensive rulemaking practice since the 1930s.

A. *The SEC Statutes, the "Schedule A" Template, and the Courts*

So how should the SEC interpret the statutory language when engaging in rulemaking? In the case of disclosure rulemaking, the answer is clear. Though this is often forgotten, Congress supplied the SEC with a detailed initial template: Schedule A of the Securities Act.[56] Schedule A prescribes 32 categories of information, both general and highly specific, that are required to be included in SEC-filed registration statements. At the same time, Congress also delegated power to the SEC to waive some of the requirements of Schedule A, and, importantly, to mandate disclosure of "such other information, and . . . such other documents, as the Commission may by rules or regulations require as being necessary or appropriate in the public interest or for the protection of investors."[57] The SEC has continuously mandated such disclosures on a wide variety of topics over the course of its 88-year history, without challenge to its authority.[58] This process has been driven by the evolution of the economy and financial markets and has included both additions and subtractions from the initial topics Congress put forward in 1933. Regulation S-K as it exists today can be traced back directly to Schedule A (which has never been amended or repealed by Congress).

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sending a clear message that compliance with ESG disclosure requirements is important, and that greenwashing will not be tolerated. Asset managers have been warned and now need to take action. The Japanese regulator also seems not far behind.").

[55] For a list of statutory references containing this language, see Comment Letter of Professors Jill E. Fisch, George S. Georgiev, Donna M. Nagy & Cynthia A. Williams on Behalf of Thirty Securities Law Scholars (June 6, 2022), https://bit.ly/3zQg4ve. The securities laws contain a number of other relevant sources of authority (*see id.*); by design, this Article is limited to the statutory language quoted above. For an expanded discussion, including discussion of the "efficiency, competition, and capital formation" mandate, see George S. Georgiev, *The Market-Essential Role of Corporate Climate Disclosure*, 56 U.C. DAVIS L. REV. (forthcoming 2023) [hereinafter Georgiev, *The Market-Essential Role of Corporate Climate Disclosure*].

[56] Securities Act of 1933, Schedule A, 48 Stat. 88 (1933).

[57] Securities Act §7(a)(1).

[58] *See infra* notes 76-89 and accompanying text.

It is worth taking a close look at what Congress did (and did not do) through Schedule A in 1933:

First, Congress did not impose a materiality requirement—either for Schedule A as a whole, or for the type of "other information" the SEC is expressly authorized to require. Congress was clearly aware of the concept of materiality, since a few of the particular items it included in Schedule A are qualified by materiality (e.g., "material contract").[59] But most other items are not, and neither is Schedule A as a whole. The provisions of the securities laws pertaining to SEC disclosure rulemaking simply do not contain a materiality constraint. (As discussed in Part IV, this does not mean that materiality is entirely irrelevant.)

Second, Congress deemed it appropriate to require disclosure of information that many today may find financially insignificant. For example, Schedule A requires the disclosure of any contract with a public utility company that provides for the "giving or receiving of technical or financial advice or service (if such contract may involve a charge to any party thereto at a rate in excess of $2,500 per year)."[60] This threshold amount translates to only $52,500 today,[61] but the SEC has used its discretion to drop the entire disclosure provision. Schedule A also requires disclosure of "the remuneration, paid or estimated to be paid, by the issuer . . . to . . . its officers *and other persons*, naming them whenever such remuneration exceeded $25,000 during any such year."[62] This threshold amount translates to $525,000 today. Even though Schedule A is still on the books, the SEC has, once again, exercised its discretion and does not require public companies to name all employees earning more than half a million dollars. The SEC has, however, developed an extensive executive compensation disclosure framework to which Congress has not objected over the three decades it has been in place.[63]

Third, Congress calibrated Schedule A to the particular risks of the time, with abuse by public utility holding companies being one.[64] Based on the delegation of authority and the Schedule A template, the SEC today should, similarly, develop disclosure requirements that take into account contemporary realities. Incidentally, public utilities during the 1930s employed pyramid structures and various business practices that harmed *both* investors and the broader economy.[65] The fact that a particular problem was not *exclusively* an investor protection problem did not preclude Congress from imposing disclosure regulation. Similarly, the fact that today's climate

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[59] *See* Schedule A, Item 24 (requiring disclosure of "dates of and parties to, and the general effect concisely stated of every material contract made, not in the ordinary course of business").

[60] *Id*.

[61] Calculations performed using the CPI Inflation Calculator. *See* CPI Inflation Calculator, U.S. BUREAU OF LABOR STATISTICS, https://data.bls.gov/cgi-bin/cpicalc.pl.

[62] Schedule A, Item 14.

[63] *See* Regulation S-K, Item 402 (Executive Compensation), 17 CFR § 229.402.

[64] *See supra* note 60 and accompanying text.

[65] *See* William M. Emmons III, *Franklin D. Roosevelt, Electric Utilities, and the Power of Competition*, 53(4) J. OF ECON. HIST. 881 (1993).

issues affect non-investor constituencies as well as investors should not be used as an argument against the Proposal.[66]

Judicial pronouncements support this interpretation. Courts have always interpreted Congress' authorization to the SEC to act as "necessary or appropriate in the public interest or for the protection of investors" as granting the SEC broad rulemaking authority. As summarized by the D.C. Circuit Court of Appeals in 1979, "the Commission has been vested by Congress with broad discretionary powers to promulgate (or not to promulgate) rules requiring disclosure of information beyond that specifically required by statute."[67] In related proceedings, the D.C. District Court stated unequivocally: "These statutes grant the SEC broad rulemaking authority. The language of the acts suggests that the SEC is empowered to exercise its informed discretion about which information will be required to be disclosed in the various corporate filings."[68] No court has invalidated an SEC rule for overstepping the SEC's disclosure authority despite the SEC's active rulemaking spanning close to nine decades and despite the fact that, as is often the case with economic regulation, many of the SEC's rules were initially resisted by the regulated entities and other interested parties.

Even a narrow reading of the legislative history of the original securities laws supports the SEC's authority to pursue the Proposal. Climate-related matters impact the most important aspect of any securities transaction—the price at which investors buy or sell—and Congress was focused on valuation matters, among others, when it adopted the Securities Act in 1933. Congress' intent was to create an information-generating regime "designed to reach items of distribution profits, watered values, and hidden interests . . . [of] indispensable importance in appraising the soundness of a security," which contains "items indispensable to any accurate judgment upon the value of the security."[69]

It should be emphasized that if Congress had objected to the SEC's approach, it could have easily intervened. Congress has amended the Securities Act and the Exchange Act on multiple occasions since the 1930s,[70] so it has had ample opportunity to reconsider the broad authority it delegated for disclosure-based rules, or to constrain the SEC's power to require disclosures about new topics. It has not found it necessary to do so. To the contrary, Congress has emphasized the importance of agency delegation with respect to disclosure matters. In the 2002 Sarbanes-Oxley Act, for example, in addition to prescribing specific items, Congress also mandated that public companies should disclose "on a rapid and current basis" such information about "material changes in [their] financial condition or operations" as the SEC determines "necessary or useful for the protection of investors and in the public interest."[71] Further back, in hearings

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[66] *See* discussion *supra* Part II.A.

[67] Nat. Res. Def. Council, Inc. v. SEC, 606 F.2d 1031, 1045 (1979).

[68] Nat. Res. Def. Council, Inc. v. SEC, 389 F. Supp. 689, 695 (D.D.C. 1974).

[69] House Report on Securities Act, H.R. Rep. No. 85, 73d Cong., 1st Sess. 3 (1933).

[70] *See, e.g.*, JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET: A HISTORY OF THE SECURITIES AND EXCHANGE COMMISSION AND MODERN CORPORATE FINANCE (2003).

[71] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 409, 116 Stat. 745, 791.

during the 1970s that followed the collapse of the Penn Central railway, Congress criticized the Interstate Commerce Commission (ICC), which had authority over the securities of common carriers pursuant to an exemption in the original Securities Act, for failing to promulgate appropriate disclosure requirements.[72] Congress repealed the relevant exemption in 1976 and placed common carriers under the SEC's disclosure jurisdiction.[73]

The D.C. Circuit has explained the historical interaction between Congress and the SEC as follows: "Rather than casting disclosure rules in stone, [the 1933] Congress opted to rely on the discretion and expertise of the SEC for a determination of what types of additional disclosure would be desirable."[74] The court further noted that "[t]he Commission's task [is] a peculiarly difficult one, requiring it to find a path between the views of the parties to the rulemaking polarized in support of the broadest disclosure or in opposition to any disclosure, to interpret novel statutory commands, and to make decisions against the background of rapidly changing conditions."[75] Indeed, Congress delegated the task of keeping up with the rapid evolution of financial markets and of regulating those markets to a specialized agency—the SEC—precisely because the task at hand is a "difficult one."

B. *The SEC's Rulemaking Practice Since the 1930s*

Relying on the power granted to it by Congress in 1933, the SEC has, decade after decade, built out a detailed disclosure regime aimed at protecting investors, which covers a number of matters that are not mandated by Schedule A or subsequent acts of Congress. These matters include executive compensation, related-party transactions, asset-backed securities, and various technical industry-specific items.[76] Since 1940, the form and content of financial statements and notes thereto (which contain a substantial amount of prescribed disclosure) have fallen into the same category.[77] As recently as 2020, during the tenure of Chairman Jay Clayton, the SEC recognized that economic changes warrant a specific disclosure requirement in the area of human capital management (HCM), and it adopted this new disclosure provision without a

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[72] The Report on the hearings noted: "More than thirty-seven years later, the ICC has continued to ignore the Congressional mandate of Schedule A and has negligently failed to promulgate one single informational requirement for inclusion in a prospectus covering securities of rail and motor carriers." *See* House of Representatives, Special Subcommittee on Investigations, Inadequacies of Protections for Investors in Penn Central and Other ICC Regulated Companies (July 27, 1971).

[73] *See* Section 308, Railroad Revitalization and Regulatory Reform Act of 1976, 90 Stat. 31 (Feb. 5, 1976) (amending Section 3(a)(6) of the Securities Act).

[74] Nat. Res. Def. Council, Inc. v. SEC, 606 F.2d 1031, 1045 (1979).

[75] *Id.*, at 1057. As part of the same proceedings, the D.C. District Court urged the Commission to "develop a [factual] record" and "imaginatively exercise its authority and expertise." *See* Nat. Res. Def. Council, Inc. v. SEC, 389 F. Supp. 689, 695 (D.D.C. 1974).

[76] *See* George S. Georgiev, *The Human Capital Management Movement in U.S. Corporate Law*, 95 TUL. L. REV. 639, 718-22 (2021) [hereinafter Georgiev, *Human Capital Management*].

[77] *See* U.S. Sec. & Exch. Comm'n, Regulation S-X: Form and Content of Financial Statements, 17 C.F.R. § 210.1-01 *et seq*.

Congressional mandate.[78] It is worth noting that both the House and the Senate had been contemplating HCM disclosure mandates since early 2019,[79] but no one argued that the SEC was required to await congressional authorization before proceeding with or finalizing its own rulemaking; such an argument is similarly misplaced in the context of the current Proposal.[80]

The SEC also has a long history of requiring environmental disclosures. In a 1971 release, it "called attention to the requirements" under the Securities Act and the Exchange Act "for disclosure of legal proceedings and a description of the registrant's business as these requirements relate to material matters involving the environment and civil rights."[81] In 1973, the SEC mandated disclosure of *all* environmental proceedings by a governmental authority, and of environmental proceedings not involving a governmental authority that meet certain specified conditions, and in 1976 it required disclosure about capital expenditures relating to environmental compliance.[82] In parallel, the SEC and accounting standard-setters developed detailed rules on the treatment of contingent environmental liabilities,[83] as well as rules about disclosure and

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[78] *See* Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Modernizing the Framework for Business, Legal Proceedings and Risk Factor Disclosures (Aug. 26, 2020), https://bit.ly/3GS8YJD ("From a modernization standpoint, today, human capital accounts for and drives long-term business value in many companies much more so than it did 30 years ago. Today's [new] rules reflect that important and multifaceted shift in our domestic and global economy."); *see also* Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Remarks at Meeting of Investor Advisory Committee (Mar 28, 2019), https://bit.ly/3t51w8x (noting that "the historical approach of disclosing only the costs of compensation and benefits often is not enough to fully understand the value and impact of human capital on the performance and future prospects of an organization"). All five commissioners agreed on the materiality of human capital matters and supported enhanced disclosure in this area, despite some disagreement about the format of the new disclosure requirement, which resulted in a split vote. *See* Georgiev, *Human Capital Management*, *supra* note 76, at 682, 714 (discussing objections of Commissioners Lee and Crenshaw).

[79] *Id.*, at 683-85.

[80] Given the difficulty in advancing legislation and the flaws in many recently-adopted Congressional mandates, waiting for Congress to act is neither feasible nor desirable, particularly when the SEC has the requisite rulemaking authority and expertise. *See, e.g.*, Steven A. Bank & George S. Georgiev, *Paying High for Low Performance*, 100 MINN. L. REV. 14 (2015) (discussing the flaws in the highly-prescriptive Congressional mandates on executive compensation disclosure imposed by the Dodd-Frank Act).

[81] Disclosures Pertaining to Matters Involving the Environment and Civil Rights, Release Nos. 33-5170, 34-9252, 36 Fed. Reg. 13,989, 13989 (July 29, 1971).

[82] *See* Notice of Commission Conclusions and Rulemaking Proposals in the Public Proceeding Announced in Securities Act Release No. 5569, Release No. 5627 (Oct. 14, 1975), 40 Fed. Reg. 51659, 51663 (Nov. 6, 1975) (summarizing disclosure provisions adopted in 1973); Conclusions and Final Action on Rulemaking Proposals Relating to Environmental Disclosure, Release No. 33-5704 (May 6, 1976), 41 Fed. Reg. 21632 (May 27, 1976).

[83] Financial Accounting Standards Board, Statement of Financial Standards No. 5: Accounting for Contingencies (1975); Statement of Position 96-1: Environmental Remediation Liabilities (American Institute of Certified Public Accountants, 1996); SEC Staff Accounting Bulletin, Release, No. 92, 58 Fed. Reg. 32,843 (June 14, 1993).

accrual of environmental obligations upon future asset retirement.[84] The SEC's MD&A releases have also made reference to environmental matters.[85] Of particular note, in 1993 the Commission issued Staff Accounting Bulletin 92, which addressed accounting and disclosures relating to environmental loss contingencies.[86] The existence of these extensive financial disclosure rules and guidance related to environmental matters has been overlooked as part of efforts to portray the SEC's Proposal as unprecedented.

In addition to formal disclosure rules, the SEC has also developed a practice of providing real-time disclosure guidance for the benefit of investors and firms, which in most cases results in substantially enhanced disclosure. For example, the SEC has provided guidance on disclosure relating to "Year 2000" (Y2K) risks,[87] the impact of the Eurozone crisis and Brexit,[88] and, most recently, the Covid-19 pandemic and Russia's war on Ukraine.[89] Importantly, in 2010, the SEC provided additional guidance on climate-change developments that could be required to be disclosed under the existing rules. Noting that legislation, regulation, international accords, business trends, and physical impacts of climate change could all affect a registrant's operations or results, the guidance "remind[ed] companies of their obligations under existing federal securities laws" and of the need "to consider climate change and its consequences" when preparing disclosure reports.[90]

While the subject matter of the SEC's Proposal—climate change—implicates existential threats to businesses, the economy, and human habitats, from the vantage

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[84] Financial Accounting Standards Board, Statement of Financial Standards No. 143: Accounting for Asset Retirement Obligations (June 2001); Financial Accounting Standards Board Interpretation No. 47: Accounting for Conditional Asset Retirement Obligations – An Interpretation of FASB Statement No. 143 (March 2005).

[85] *See, e.g.*, Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, Securities Act Release No. 6835, Exchange Act Release No. 26831, Investment Company Act Release No. 16,961, 54 Fed. Reg. 22,427, 22,430 (May 24, 1989).

[86] SEC Staff Accounting Bulletin, Release, No. 92, 58 Fed. Reg. 32,843 (June 14, 1993).

[87] *See* U.S. Sec. & Exch. Comm'n, Statement of the Commission Regarding Disclosure of Year 2000 Issues and Consequences by Public Companies, Investment Advisers, Investment Companies, and Municipal Securities Issuers, 63 Fed. Reg. 41,394 (Aug. 4, 1998).

[88] *See* U.S. Sec. & Exch. Comm'n, Div. of Corp. Fin, CF Disclosure Guidance: Topic No. 4: European Sovereign Debt Exposure (Jan. 6, 2012), https://bit.ly/3FPlR7o (providing extensive guidance on disclosure of Eurozone crisis impacts); Tatyana Shumsky, *SEC Calls For More Detailed Disclosure on Brexit Impact*, WALL ST. J. (Nov. 12, 2018), https://on.wsj.com/3PLs4W3 (reporting that "[the SEC] is sharpening its focus on corporate disclosures about the risks associated with the U.K.'s exit from the European Union" and quoting Chairman Jay Clayton's opinion that "the potential impact of Brexit has been understated" and that "companies [should] be looking at this closely and sharing their views with the investment community").

[89] *See* U.S. SEC. & EXCH. COMM'N, COVID-19 (last modified: Jan. 8, 2021), https://bit.ly/3VkrpfC (listing 15 guidance documents, statements, and interpretations by the Commission in connection with the Covid-19 crisis); U.S. Sec. & Exch. Comm'n, Div. of Corp. Fin, Sample Letter to Companies Regarding Disclosures Pertaining to Russia's Invasion of Ukraine and Related Supply Chain Issues (May 3, 2022), https://bit.ly/3VicmmL.

[90] Commission Guidance Regarding Disclosure Related to Climate Change, Release Nos. 33-9106, 34-61469, FR-82 (Feb. 8, 2010).

point of securities regulation, the Proposal is simply part of a tradition spanning nine decades. The SEC has been cognizant of the appropriate role of disclosure as a regulatory tool; accordingly, the SEC is not aiming to address climate change any more than it was trying to solve a geopolitical crisis (Russia's war on Ukraine) or a global health crisis (the Covid-19 pandemic) when it required public companies, for the benefit of investors and markets, to disclose the risks and operational and financial impacts of these critical events.

In conclusion, it is worth quoting a statement by Republican-appointed SEC Chairman Jay Clayton, which provides a good summary of the SEC's rulemaking practice and the importance of the iterative modernization of disclosure requirements. Speaking in 2018, then-Chairman Clayton described the SEC's disclosure system as "powerful, far reaching, dynamic and ever evolving" and noted that "[a]s stewards of this . . . system, a key responsibility of the SEC is to ensure that the mix of information companies provide to investors facilitates well-informed decision making."[91]

IV. MATERIALITY, MISUNDERSTOOD AND WEAPONIZED

The complex concept of materiality has in recent years come to be used as a "killer switch" for new SEC disclosure requirements because of its superficial objectivity.[92] Unfortunately, many of the arguments against disclosure that refer to materiality are based on a distortion of the actual legal framework. In the context of climate-related disclosure, it is important to understand the appropriate role of Supreme Court precedent and to tackle head-on several misconceptions that, if allowed to become entrenched, can seriously damage the SEC's ability to promulgate any new disclosure rules, including climate-related disclosure rules, as well as its ability to maintain the existing disclosure regime.

A. TSC Industries *and* Basic *Do Not Impose a Constraint*

As we saw from Part III, the original federal securities statutes do not impose a materiality constraint on SEC disclosure rulemaking. Contrary to oft-repeated assertions, neither do the two leading Supreme Court cases on materiality, *TSC Industries* and *Basic*.[93] The *TSC Industries* court noted that information is material if

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[91] Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Remarks at Meeting of the Investor Advisory Committee (Dec. 13, 2018), https://bit.ly/3wV4UnB.

[92] The U.S. Chamber of Commerce was one of the original architects of using materiality against ESG disclosure. *See* U.S. CHAMBER OF COMMERCE, CTR. FOR CAP. MKTS. COMPETITIVENESS, ESSENTIAL INFORMATION: MODERNIZING OUR CORPORATE DISCLOSURE SYSTEM (2017), https://bit.ly/3hKl7IN (asserting that "groups advocating an ESG agenda seek to reconceptualize materiality to advance their own objectives" and that "[a]n investor that bases its voting and investment decisions on promoting social or political goals is not a 'reasonable' investor when it comes to what materiality means under the federal securities laws"). *See also infra* note 96 and accompanying text.

[93] *See* TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976) (defining materiality in the context of a proxy fraud action under Rule 14a-9); Basic Inc. v. Levinson, 485 U.S. 224, 231–32

there is a "substantial likelihood that a reasonable [investor] would consider it important" in making an investment or voting decision, or, as the court explained, "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."[94] A crucial first step in understanding this and other cases is that they deal with whether or not an issuer, at some specified point in the past, had *a legal duty to disclose* particular information, under a particular set of circumstances and in light of the applicable regulatory framework. In other words, the Supreme Court's materiality test applies to an *ex post* liability determination, not to an *ex ante* policy choice by a regulator. When it engages in disclosure rulemaking, the SEC inevitably has to make *ex ante* policy choices. Unsurprisingly, then, neither *TSC Industries*, nor *Basic*, nor any other Supreme Court case touches on or limits the types of information the SEC is empowered to require when it promulgates disclosure rules.[95] This is further evidenced by the fact that in late 2022 members of the House of Representatives introduced a bill seeking to impose a materiality requirement on SEC-promulgated disclosure rules;[96] no bill would be necessary if a materiality requirement were already in place.

These principles extend beyond Supreme Court jurisprudence. When the D.C. Circuit has struck down SEC rules, it has been for failure to carry out adequate cost-benefit analysis,[97] and never due to a finding that the challenged rule lacked materiality. It is instructive that none of the hundreds of disclosure rules the SEC has promulgated since the 1930s has been challenged in court on materiality grounds; this corpus includes many rules adopted pursuant to the SEC's broad delegated authority (rather than prescriptive SEC mandates),[98] as well as various rules on environmental and

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(1988) (adopting the *TSC Industries* materiality formulation in the context of securities fraud actions under Rule 10b-5). *See also* George S. Georgiev, *Too Big to Disclose: Firm Size and Materiality Blindspots in Securities Regulation*, 64 UCLA L. REV. 602, 620-25 (2017) (examining the content of the materiality standard, various approaches to applying it, and the associated challenges).

[94] *See* TSC Indus., Inc. v. Northway, Inc., *supra* note 93, at 439.

[95] Of course, when courts are tasked with adjudicating ex post liability for non-disclosure under Rule 10b-5, they will inquire into materiality by applying the Supreme Court's test. It is perfectly normal for a complex concept such as materiality to operate differently depending on the context.

[96] *See* Brian Croce, *House Republicans Float Bill to Block SEC Climate Disclosure Proposal*, PENSIONS & INVESTMENTS (Dec. 5, 2022), https://bit.ly/3jiVM8Y (discussing the proposed Mandatory Materiality Requirement Act of 2022, which would write a materiality requirement into the securities laws).

[97] *See* Bus. Roundtable v. SEC, 647 F.3d 1144, 1148–49 (D.C. Cir. 2011) (invaliding SEC proxy access rule mandated by the Dodd-Frank Act); *see also* Am. Equity Inv. Life Ins. Co. v. SEC, 613 F.3d 166, 177–79 (D.C. Cir. 2009) (invalidating SEC rule on fixed index annuities); Chamber of Commerce v. SEC, 412 F.3d 133, 142–44 (D.C. Cir. 2005) (invaliding SEC rule imposing director independence requirements on mutual funds).

[98] *See, e.g.*, Asset-Backed Securities Disclosure and Registration, Securities Act Release No. 33-9638, Exchange Act Release No. 72982, 79 Fed. Reg. 57,184, 57,186 (Sept. 24, 2014) (adopting new rules because "the financial crisis highlighted that investors and other participants in the securitization market did not have the necessary information and time to be able to fully assess the risks underlying asset-backed securities and did not value asset-backed securities properly or

climate matters.[99] Importantly, the D.C. Circuit has not ruled that cost-benefit analysis requires an assessment of materiality.[100] The closest the D.C. Circuit has come to considering materiality in the context of SEC disclosure rulemaking has been to find that the SEC is entitled to deference in its determination on the materiality (or lack thereof) of particular topics: During the 1970s, the Natural Resources Defense Council challenged the SEC's refusal to pursue disclosure rulemaking in response to its petition, which the SEC had justified on the grounds that the non-disclosed information was not material; the D.C. Circuit sided with the SEC.[101]

The existing confusion on this point is understandable, at least to a certain degree. The SEC has referenced the Supreme Court's succinct articulation of materiality with some frequency for the sake of consistency. Many, though certainly not all, existing disclosure requirements are qualified by materiality (e.g., material risks).[102] In these cases, however, the SEC has not left firms to struggle with the Supreme Court's elegant-yet-economical articulation of materiality; instead, the SEC has supplemented it by developing extensive guidance on how firms are to go about making the often-difficult materiality judgments. Over the years, some of this guidance has been general in character,[103] and some of it has been more topic-specific.[104]

The other reasons for the confusion are more unfortunate: Over the past decade, SEC commissioners, speaking in their individual capacities, have implied[105] or

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accurately"); Executive Compensation and Related Person Disclosure, Exchange Act Release No. 54302A (Aug. 29, 2006), 71 Fed. Reg. 53,158 (Sept. 8, 2006).

[99] *See supra* Part III.B.

[100] *See id*. This argument has been made in the academic context but has failed to gain traction. *See, e.g.*, J.W. Verret, *The Securities Exchange Act Is a Material Girl, Living in a Material World*, 3 HARV. BUS. L. REV. 453 (2013) (suggesting that cost-benefit analysis should incorporate a formal assessment of materiality).

[101] *See* Nat. Res. Def. Council, Inc., v. SEC, 606 F.2d 1031 (D.C. Cir. 1979). Note, of course, that the SEC is not bound by a policy judgment it made during the 1970s, and that the economy, market fundamentals, investor preferences, and other factors have changed since then.

[102] 17 C.F.R. § 229.105(a) ("Where appropriate, provide under the caption "Risk Factors" a discussion of the material factors that make an investment in the registrant or offering speculative or risky."). Other examples of rules qualified by materiality include Item 103 of Regulation S-K (requiring disclosure of "material pending legal proceedings") and Item 303 of Regulation S-K (requiring disclosure of matters that have had a "material impact" on reported operations or are reasonably likely to have such an impact on future operations).

[103] For example, Staff Accounting Bulletin 99 provides extensive guidance on "qualitative materiality." SEC Staff Accounting Bulletin No. 99, 64 Fed. Reg. 45,150 (Aug. 19, 1999).

[104] *See, e.g.*, Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, Securities Act Release No. 6835, Exchange Act Release No. 26831, Investment Company Act Release No. 16,961, 54 Fed. Reg. 22,427, 22,430 (May 24, 1989) (providing guidance on materiality judgments for forward-looking financial information under Item 303 of Regulation S-K); Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations, Securities Act Release No. 8350, Exchange Act Release No. 48960, 68 Fed. Reg. 75,056 (Dec. 29, 2003) (providing supplemental guidance on key topics and summarizing prior guidance since 1980).

[105] *See* Elad L. Roisman, Comm'r, U.S. Sec. & Exch. Comm'n, Keynote Speech at the Society for Corporate Governance National Conference (July 7, 2020), https://bit.ly/3vaauSs.

asserted[106] that *TSC Industries* imposes a limit on the SEC's power to promulgate disclosure rules, and that the already-existing framework "requires disclosure of *all material information*"[107] (which, conveniently, would make it unnecessary to promulgate any additional disclosure rules). The law is clear, however, that there is no general requirement to disclose "all material information"; issuers have to disclose information only when a particular SEC rule requires it, including "as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading."[108] In addition, a subset of existing disclosure items are not qualified by materiality,[109] reflecting a policy judgment that particularized materiality testing at the disclosure stage is unwarranted because, for example, it may be impractical or costly for registrants, because it may be susceptible to abuse, or because the underlying information is basic in nature.

B. *Materiality as an Appropriate Background Principle*

To say that *TSC Industries* and *Basic* do not impose *a formal constraint* on SEC rulemaking is not to say that they are *irrelevant* to SEC rulemaking. The SEC should be (and has been) guided by the general materiality of a given subject matter when deciding whether to adopt new disclosure rules. And once the SEC identifies a general subject area that is material to investors, it usually comes up with detailed guidance and/or an information-generating framework that ensures the consistency, comparability, and reliability of public companies' disclosures in that area.

Even though the specific language of *TSC Industries* and *Basic* cannot serve as a self-executing disclosure criterion—securities markets are too complicated for that—it can help illuminate aspects of the SEC's policy analysis. On this score, too, the Proposal on climate-related disclosure appears both justified and consistent with established practices. Consider the application of three key elements of materiality doctrine, the "reasonable investor" concept, the probability-magnitude test, and the notion of the "total mix of information."

The "Reasonable Investor": Materiality is always viewed through the eyes of the "reasonable investor," but the particular attributes of this construct are so amorphous

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[106] *See* Jay Clayton, Chairman, Remarks on Telephone Call with Investor Advisory Committee Members (Feb. 6, 2019), https://bit.ly/3hN8cFP.

[107] Roisman, *supra* note 105.

[108] *See* Exchange Act Rule 12b-20, 17 C.F.R. § 240.12b-20 (2020); *see also* Securities Act Rule 408, 17 C.F.R. § 230.408 (2020) (providing for a similar obligation in registration statements under the Securities Act).

[109] Examples of rules not qualified by materiality include, among others, Item 401 of Regulation S-K (requiring disclosure of specified information about directors, executive officers, promoters, and control persons) and Item 402(c)(1) of Regulation S-K (requiring disclosure of the salary, bonus, stock awards, stock option awards, and other specified elements of executive compensation without subjecting the elements or the amounts involved to a materiality test).

as to generate an entire sub-genre of securities law scholarship.[110] Commissioner Peirce and other opponents of ESG disclosure have used this ambiguity to dismiss evidence of significant investor demand for climate-related disclosure by implying that this demand does not come from reasonable, financially-motivated investors.[111] But as the SEC points out in the Proposal, the investors demanding climate-related disclosure include BlackRock, State Street, Vanguard, Calpers, and others who, in the aggregate, invest the bulk of Americans' savings.[112] These investors have expressly endorsed the TCFD framework upon which the SEC Proposal is based and have indicated how they use climate-related information in their investment decisions.[113] The SEC is right to take these mainstream investors at their word and not second-guess their motivations. To do otherwise would be to imply that U.S. capital markets are dominated by investors who are not "reasonable"—a conclusion that would raise troubling questions about the price efficiency and overall health of these same markets. And, as between BlackRock (an actual investor) and the Chamber of Commerce (a lobbying group that is an always-reliable detractor to disclosure regulation),[114] it would appear that BlackRock is much better positioned to speak about the disclosure needs of the "reasonable investor."

The "Probability-Magnitude Test": In *Basic*, the Supreme Court stated that materiality determinations should be made by considering *both* the probability and the magnitude of an event or effect.[115] A highly-consequential event may be material even if the probability of it occurring is relatively low. Applying this rationale to climate-related risk militates in favor of mandating disclosure. The magnitude of the adverse effects from climate change is extremely high both for individual firms and across the economy. And, in most cases, the probability of adverse events occurring is not low, but, rather, difficult to estimate.[116] Such uncertainty and estimation difficulties are also being

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[110] *See, e.g.*, David A. Hoffman, *The "Duty" to Be a Rational Shareholder*, 90 MINN. L. REV. 537, 543 (2006); Tom C.W. Lin, *Reasonable Investor(s)*, 95 B.U. L. Rev. 461 (2015); Amanda M. Rose, *The "Reasonable Investor" of Federal Securities Law: Insights from Tort Law's "Reasonable Person" & Suggested Reforms*, 43 J. CORP. L. 77 (2017); Margaret V. Sachs, *Materiality and Social Change: The Case for Replacing "the Reasonable Investor" with "the Least Sophisticated Investor" in Inefficient Markets*, 81 TUL. L. REV. 473 (2006).

[111] *See* Juliet Chung & Dave Michaels, *ESG Funds Draw SEC Scrutiny*, WALL ST. J. (Dec. 16, 2019), https://bit.ly/3GeG5ZG; *see also supra* note 92 and accompanying text.

[112] *See, e.g.*, GRAHAM STEELE, THE NEW MONEY TRUST: HOW LARGE MONEY MANAGERS CONTROL OUR ECONOMY AND WHAT WE CAN DO ABOUT IT (2020), https://bit.ly/3jrPyDR.

[113] *See* Halper et al., *supra* note 37.

[114] *Compare* Letter from Sandra Boss et al., Senior Managing Dir., BlackRock, to Vanessa Countryman, Secretary, U.S. Sec. & Exch. Comm'n (June 11, 2021), https://bit.ly/3jrGzT2 (emphasizing importance of climate-related disclosure to asset allocation and voting decisions), *with* Letter from Tom Quaadman, Exec. Vice President, U.S. Chamber Ctr. for Cap. Mkts. Competitiveness, to Vanessa Countryman, Secretary, U.S. Sec. & Exch. Comm'n (June 11, 2021), https://bit.ly/3hREPlB (stating opposition to climate-related disclosure based on speculative evidence).

[115] Basic Inc. v. Levinson, 485 U.S. 224 (1988) (setting out the probability-magnitude framework).

[116] *See, e.g.*, Jane Sillman et al., *Understanding, Modeling and Predicting Weather and Climate Extremes: Challenges and Opportunities*, 18 WEATHER & CLIMATE EXTREMES 65 (2017).

used to brand the Proposal as outside the mainstream. We should remember, however, that the disclosure regime already incorporates provisions where firms have to weigh risks and estimate probabilities (e.g., ASC 450 loss contingencies).[117] Providing investors with the underlying information will enable better investor modeling and, ultimately, promote the informational efficiency of securities prices.

The "Total Mix of Information": Recall that *TSC Industries* applies materiality in the context of an ex post inquiry into securities fraud liability. Notably, the case uses the concept of "the total mix of information made available" as the baseline against which courts are to test the materiality of any misstatement or omission in order to determine whether it can support a finding of liability. As such, the case pre-supposes the existence of a "total mix" of relevant information; without a total mix, there is no baseline against which to test—and the materiality test itself does not work. To be sure, part of the total mix comes from voluntary disclosure, but voluntary disclosure alone cannot produce a balanced picture of the underlying reality that would serve as a baseline for determining liability. Implicitly, then, it is the SEC's job to design an information-generating framework that produces the appropriate total mix. Seen this way, *TSC Industries* does not prohibit the SEC from mandating disclosure items that eschew the *TSC Industries* test for materiality; instead, *TSC Industries* practically requires the SEC, as the regulator in charge of securities markets, to use its expertise and mandate appropriate disclosure items.[118] The Proposal is an important part of the SEC's effort to generate the total mix. And while it is possible to argue that the total mix itself should only contain material information (which, for present purposes, would mean sticking to the 2010 Guidance), this would mean that the *TSC Industries* liability test would suffer from an endogeneity problem: On a conceptual level, materiality is both contextual and relative—significant information takes on the property of materiality by comparison to information that is less significant and hence not material. The total mix therefore should contain information of various levels of significance in order to enable such comparative judgments for purposes of imposing liability.[119]

C. *The "Universal Materiality" Trap*

The notion of "universal materiality" is another novel, creative, and seemingly intuitive tool for opposing new disclosure rules. "Universal materiality" does not appear in any statute or judicial decision, but seems to have originated with Commissioner Peirce and has since resurfaced in some of the comment letters submitted to the SEC.

At the end of Commissioner Peirce's dissenting statement on the Proposal, she promised to keep an open mind about the final rule and asked commenters to identify

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[117] *See* FINANCIAL ACCOUNTING STANDARDS BOARD, CONTINGENCIES (TOPIC 450): DISCLOSURE OF CERTAIN LOSS CONTINGENCIES (2010).

[118] The statement by SEC Chairman Jay Clayton noted in Part III also supports this view: "a key responsibility of the SEC is to ensure that the mix of information companies provide to investors facilitates well-informed decision making." *See supra* note 78 and accompanying text.

[119] *See* Georgiev, *Human Capital Management*, *supra* note 76, at 720-22.

for her "types of *universally material* climate information that are not being disclosed under [the] existing rules."[120] Though its provenance cannot be ascertained, the notion of "universal materiality" implies that for a category to be *universally* material, it should be material for all public companies at all points in time. This is an incredibly high bar that few, if any, of the SEC's existing disclosure rules would meet. Consequently, it cannot be the proper standard for evaluating new disclosure rules. Given that materiality is by its nature both contextual and relative, few, if any, categories of information could be relevant for *all companies*, *all the time.* How would we identify those categories and how could we be confident of their universal materiality? These questions go to the design and administrability of the entire securities disclosure regime. Even though Commissioner Peirce does not offer answers, she points out in a footnote that long-settled rules on executive compensation, related-party transactions, and environmental litigation do not meet the materiality standard (as she understands it) and do not belong in the disclosure regime.[121]

In a quest to operationalize "universal materiality," we might stipulate that basic information about a company, such as the number of employees, is "universally material"; after all, one cannot understand a company—any company—without it. But according to Commissioner Peirce, even this basic data point does not meet the standard of "universal materiality" that would qualify the information for unconditional disclosure. In 2020, she expressed support for eliminating the requirement to disclose the number of employees because it "might be material for some companies under some circumstances, but not for others."[122] An impossibly high bar, indeed. It is safe to assume, then, that those commenting on the Proposal would be unable to identify climate-related information that meets Commissioner Peirce's standard of "universal materiality." A disclosure regime built on this standard would likely be one where all of Regulation S-K and Regulation S-X fit on a single page.

"Universal materiality" may well be a category error and stem from its mirror image, universal *immateriality*. Because questions of materiality require "delicate assessments of the inferences a 'reasonable [investor]' would draw from a given set of facts and the significance of those inferences to him,"[123] these questions are usually for a jury to decide. As an exception to this principle, when matters "are so obviously unimportant to an investor that reasonable minds cannot differ on the question of materiality, the court may rule them immaterial as a matter of law."[124] The universal *immateriality* of a matter, in other words, bars liability for misleading disclosure or non-disclosure. But this principle does not mean that universal *materiality* is required for the SEC to impose a disclosure duty. Furthermore, to suggest that materiality bars the SEC

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[120] Peirce, *supra* note 13.

[121] *Id*. at n.15.

[122] Hester M. Peirce, Comm'r, U.S. Sec. & Exch. Comm'n, Statement at Open Meeting on Modernization of Regulation S-K 101, 103, and 105 (Aug. 26, 2020), https://bit.ly/3YHOjAG.

[123] TSC Indus., 426 U.S. at 450.

[124] *See* Recupito v. Prudential Sec., Inc., 112 F. Supp. 2d 449, 454 (D. Md. 2000) (quoting Klein v. Gen. Nutrition Cos., 186 F.3d 338, 342 (3d Cir. 1999)).

from adopting climate-related disclosure rules would be to suggest that climate-related information is "so obviously unimportant to an investor that reasonable minds cannot differ on the question of materiality." Notwithstanding the range of views about the desirability of climate-related disclosure, the available factual record does not support such a categorical conclusion.

D. *The "Double Materiality" Trap*

Another part of the campaign against ESG disclosure involves setting up a sharp dichotomy between so-called "American materiality" and "double materiality" (or "dynamic materiality"). "American materiality" is shorthand for the *TSC Industries* approach discussed above.[125] The explanation of American materiality starts off by accurately stating the language of *TSC Industries*, but then quickly proceeds to misstate the actual legal constraints that apply to SEC rulemaking.[126] "Double materiality" or "dynamic materiality," on the other hand, is shorthand for an approach whereby materiality has two alternative prongs, a financial one and a social one. In the words of the EU Non-Financial Reporting Directive (emphasis on "non-financial"), this means that "companies should disclose not only how sustainability issues may affect the company, but also how the company affects society and the environment."[127]

"Double" or "dynamic materiality" is a EU-generated and EU-centric approach. (Indeed, "double materiality" means something entirely different to U.S. transactional lawyers.[128]) Regardless of its merits and demerits, the EU's "double" or "dynamic materiality" approach is not the issue here. Based on a close reading of the 510 pages comprising the SEC's actual Proposal, there is nothing in the Proposal that reflects a "double materiality" or "dynamic materiality" approach. And if there is something that reflects such an approach, commenters will be sure to point it out as part of the notice-and-comment rulemaking process. It is easy to see why the EU's push for double materiality or dynamic materiality is a powerful tool in the U.S.-centric materiality debates, but we ought to be careful not to conflate the two. Materiality has different meanings based on *both context and geography*.

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[125] *See* David Katz & Laura Mcintosh, *Corporate Governance Update: "Materiality" in America and Abroad*, HARV. L. SCH. F. ON CORP. GOVERNANCE (May 1, 2021), https://bit.ly/3PPtkbd.

[126] *Id*. As explained in Part IV.A, materiality, as defined by *TSC Industries* and *Basic* for the purposes of adjudicating liability, is not a constraint on SEC disclosure rulemaking.

[127] *See* EUR. COMM'N, CONSULTATION DOCUMENT: REVIEW OF THE NON-FINANCIAL REPORTING DIRECTIVE (JUNE 8, 2020), https://bit.ly/3VnQ973; *see also* Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 Amending Directive 2013/34/EU as regards Disclosure of Non-financial and Diversity Information by Certain Large Undertakings and Groups, 2014 O.J. (L 330) 1, https://bit.ly/3uYXKhl.

[128] *See, e.g.*, Broc Romanek, *Understanding "Double Materiality,"* DEAL LAWYERS BLOG (Feb. 14, 2011), https://bit.ly/3hN8ixb.

V. UNTESTED THEORIES: "MAJOR QUESTIONS" AND "COMPELLED SPEECH"

There are two additional lines of attack which made an appearance in the dissenting statement by Commissioner Peirce and that have since been amplified by commenters; those are based on novel and untested theories such as "major questions" and compelled speech under the First Amendment. It is beyond the scope of this Article to address these arguments in a comprehensive manner,[129] but it is nevertheless useful to highlight how the analysis presented in the preceding parts undermines these arguments.

A. *"Major Questions" after* West Virginia v. EPA

The dissenting statement by Commissioner Peirce previewed a line of attack that has since become much more explicit in light of the Supreme Court's June 2022 ruling in *West Virginia v. EPA*.[130] This case continued the resurgence of the so-called "major questions doctrine." As the court explained, the doctrine applies when an agency "claims to discover in a long-extant statute an unheralded power . . . representing a transformative expansion in [its] regulatory authority."[131] The court concluded that the EPA's regulatory approach in that case "effected a 'fundamental revision of the statute, changing it from [one sort of] scheme of . . . regulation' into an entirely different kind."[132]

Given the power of the major questions doctrine, it is understandable why opponents of the Proposal would seek to portray it as a break with tradition. The factual record discussed in Part III, however, does not support this view. The Securities Act of 1933 is, indeed, a "long-extant statute," but, far from being "unheralded," the regulatory power at issue has been exercised consistently since the 1930s without any objection from Congress. Moreover, while the Proposal touches various economic actors, it can hardly be said to "regulate" the economy in the command-and-control sense in which the Supreme Court has spoken about regulation.[133]

B. *The First Amendment and "Compelled Speech"*

The argument that SEC disclosure regulation on climate-related matters may fall foul of the First Amendment's limitations on compelled commercial speech is a fairly new line of attack first advanced by the West Virginia Attorney General in March

[129] I discuss these issues in more detail in forthcoming work. *See* Georgiev, *The Market-Essential Role of Corporate Climate Disclosure*, *supra* note 55.

[130] 142 S. Ct. 2587 (2022).

[131] *Id.* at 2610.

[132] *Id*. at 2612. *See also* Util. Air Regulatory Group v. EPA, 134 S. Ct. 2427, 2444 (2014) (stating that "[w]hen an agency claims to discover in a long-extant statute an unheralded power to regulate a significant portion of the American economy, we typically greet its announcement with a measure of skepticism").

[133] *Id*.

2021[134] (subsequently joined by a group of Republican state attorneys general),[135] which has since been taken up by others as well.[136] The relevant questions appear to be whether a disclosure mandate focuses on "purely factual and uncontroversial information" and whether it is "unjustified or unduly burdensome."[137] Even though opponents of the SEC's climate disclosure initiative made it controversial well before the contours of the Proposal became known, this does not mean that the actual information required by the actual Proposal is controversial, burdensome, or unjustified. In her statement, Commissioner Peirce asserts that the subject matter of climate-related risk may not be "uncontroversial" because it is not "consistent with the language and objectives of the statute authorizing the mandate."[138] But, just like the major questions arguments, this assertion too is called into question by the analysis in Part III of the disclosure template established by Congress in 1933 (Schedule A), the contemporaneous delegation of authority to update and build upon that template, and almost nine decades of subsequent regulatory practice.

CONCLUSION

Properly understood, the SEC's rule is about market capitalism, not about environmentalism, and this neatly encapsulates why it ought to be adopted and withstand legal challenge. Nothing in the SEC's rule is aimed at mitigating or reversing the physical effects of climate change; the rule itself is also neutral with respect to the allocation of capital toward or away from certain types of businesses.[139] It is often said that information is the lifeblood of the capital markets; capital markets, in turn, are a central institution of a capitalist economy. This means that for capitalism to work, market participants need accurate, standardized, and comparable information about the major risks and opportunities faced by firms, which, in today's world, include climate-related risks and opportunities.[140] The reality on the ground is that firms are impacted

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[134] *See* Letter from Patrick Morrisey, Attorney Gen., W. Va., to Allison Herren Lee, Acting Chair, U.S. Sec. & Exch. Comm'n (Mar. 25, 2021), https://bit.ly/3vd9eOE.

[135] *See* Letter from Patrick Morrisey et al., Attorney Gen., W. Va., to Gary Gensler, Chair, U.S. Sec. & Exch. Comm'n (June 14, 2021), https://bit.ly/3BWvKia.

[136] *See* Letter from Ryan Morrison, Attorney, Institute for Free Speech, to Gary Gensler, Chair, U.S. Sec. & Exch. Comm'n (June 10, 2021), https://bit.ly/3vcvJ65.

[137] Nat'l Inst. of Family & Life Advocates v. Becerra, 138 S. Ct. 2361, 2372 (2018).

[138] Peirce, *supra* note 13; *see also* Sean Griffith, *What's "Controversial" About ESG? A Theory of Compelled Commercial Speech under the First Amendment*, HARV. L. SCH. F. ON CORP. GOVERNANCE (June 17, 2022), https://bit.ly/3Wm7NJr.

[139] To be sure, investors may direct capital away from certain assets and firms in response to the information provided under the rule. But this process is no different than any other capital allocation decision stemming from information investors deem relevant based on their risk, liquidity, and other preferences.

[140] The SEC has also proposed rules that would increase the transparency obligations of funds and asset managers with respect to the climate-related risks of their products. *See* Investment Company Names, Release No. IC-34593 (May 25, 2022), https://bit.ly/3FRBDi1; Enhanced Disclosures by

by climate change and are taking measures in response—whether because they have decided to do so as a matter of sound business strategy, because U.S. policies require them, or, alternatively, incentivize them to do so,[141] or simply because of mandates adopted by independent foreign regulators.[142]

The SEC's rule seeks to elicit relevant information about these developments, risks, and opportunities. It will bring to light the effects of climate change on firm valuations in the real economy and, in turn, enable markets and market participants to adjust those valuations accordingly. Price is the most important term of any transaction, including a transaction in securities, and ensuring accurate asset and firm valuations is an essential element of investor protection. Another such element is making sure that investors can exercise their well-established voting rights under corporate law; these rights comprise "the procedures of corporate democracy" whose importance has been recently reinforced by the Supreme Court.[143] While there are many difficult policy decisions on the road to the economic transformation necessitated by climate change, the decision to advance longstanding goals such as investor protection and capital market efficiency through the SEC's well-calibrated Proposal on climate-related disclosure should not be one of those difficult policy choices.

Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, Release No. IA-6034; IC-34594 (May 25, 2022), https://bit.ly/3jkjaTw.

[141] *See* White House, Building a Clean Energy Economy: A Guidebook to the Inflation Reduction Act's Investments in Clean Energy and Climate Action (2022), https://bit.ly/3jnbAHR (describing the various economic incentives and programs in support of firms' transition to a clean energy economy). *See supra* notes 24-27 and accompanying text.

[142] *See supra* note 54 and accompanying text.

[143] Citizens United v. FEC, 558 U.S. 310, 361-362 (2010).