Boyden Gray PLLC
801 17th Street NW, Suite 350
Washington, DC 20006
(202) 955-0620

October 30, 2023

The Honorable Gary Gensler
Chair
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: RIN 3235–AM87, The Enhancement and Standardization of Climate-Related Disclosures for Investors

Dear Chair Gensler,

This letter is written as a supplement to our prior comments on the SEC's Proposed Rule on "The Enhancement and Standardization of Climate-Related Disclosures for Investors" ("the proposed rule"), published in the Federal Register on April 11, 2022, at 87 Fed. Reg. at 21,334 through 21,473.

We write to discuss three recent developments concerning the proposed rule. *First*, California Governor Gavin Newsom recently signed into law SB 253 and SB 261, which will collectively require businesses generating more than $1 billion in revenue to publicly disclose their scope 1, 2, and 3 emissions, and businesses with revenue surpassing $500 million to identify climate-related financial risks. *Second*, investor demand for ESG investment products has collapsed in 2023, with more ESG funds closing than in the previous three years combined. *Third*, and related to the collapsing demand for ESG investment products, at least one market leader has ceased to provide ESG ratings products and further evidence indicates the market for such products is rapidly shrinking.

I. California's SB 253 and SB 261 Provide No Justification for the Costs of the Proposed Rule.

We are concerned that the SEC may try to improperly bake California's recently enacted disclosure laws into its own climate-related disclosure rule as a regulatory "baseline" in an attempt to justify the requirements or the costs of this rule. This would be unlawful for two reasons.

First, the SEC cannot use collaboration with states to exercise powers that the Securities Act and Exchange Act do not provide. One such limit, as our June 17, 2022 comment highlighted, is the SEC's limitation to require the disclosure of only "material" information. Comment of Boyden Gray at 20–23 (June 17, 2022), https://www.sec.gov/comments/s7-10-22/s71022-20132160-302652.pdf. The relevant

statutes limit the SEC to mandating disclosures only when "necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 77g(a)(1); § 77j(c) (same); § 78*l*(b)(1) (same); § 78o(d) (same); *see also* § 78m(a) ("necessary or appropriate for the proper protection of investors and to insure fair dealing."). And the Supreme Court has recognized that the "public interest" is not furthered by requiring companies "simply to bury the shareholders in an avalanche of trivial information," which "is hardly conducive to informed decisionmaking" and thus would "accomplish more harm than good." *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 448-49 (1976). Because material climate-related risks must already be disclosed, any requirement to disclose information *beyond* what is already required would necessarily require companies to disclose non-material information. The SEC lacks that statutory power.

Reliance on actions done by another entity—like California's climate disclosure laws or the E.U.'s climate disclosure rules—does not remove this limitation. The SEC cannot attempt to bring in through the backdoor what the Supreme Court has said they cannot bring through the front. "[A]gencies, as mere creatures of statute, must point to explicit Congressional authority justifying their decisions." *Clean Water Action v. EPA*, 936 F.3d 308, 313 (5th Cir. 2019). "[A]n agency literally has no power to act … unless and until Congress confers power upon it." *La. Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374 (1986). Congress "confer[ed]" no power to require new climate-related disclosures, and so the SEC cannot obtain such disclosures either on its own, or by incorporating a state disclosure scheme.

Second, it would be unlawful for the SEC to incorporate California's laws into its own rules because the California laws are themselves unlawful. There are several problems with California's laws that make their challenge and defeat a near certainty. California's laws violate the First Amendment, the Dormant Commerce Clause, and are preempted by several federal laws including, as you recently noted, the National Securities Market Improvement Act, *see* Jessica Corso, *SEC's Gensler Cautions Against Climate Rule Lawsuit*, Law360 (Oct. 26, 2023), https://www.law360.com/articles/1737081/sec-s-gensler-cautions-against-climate-rule-lawsuit. The SEC cannot expect corporations to comply with these unconstitutional laws because, as the Supreme Court explained more than a century ago: "An unconstitutional act is not a law; it confers no rights; it imposes no duties; it affords no protection; it creates no office; it is, in legal contemplation, as inoperative as though it had never been passed." *Norton v. Shelby Cnty.*, 118 U.S. 425, 442 (1886).

Of course, the SEC would not be the first agency in this administration to try to incorporate an unlawful Californian analog into its own rulemaking. The National

Highway Traffic Safety Administration's (NHTSA) included electric cars made to comply with California's Advanced Clean Cars program as part of a "baseline" in its "Corporate Average Fuel Economy Standards for Model Years 2024–2026." This baseline was intended to serve as a sort of regulatory insurance policy that would ensure the continued survival of those state laws even if they were struck down. Ironically, NHTSA's insurance policy created more trouble for itself, as challengers in *Natural Resources Defense Council v. NHTSA*, 22-1080 (D.C. Cir.) pointed specifically to the unlawful incorporation of California's laws as a reason NHTSA's standards should be vacated. The SEC should avoid making the same mistake.

II. Collapsing Demand for ESG Investment Products Further Undercuts the SEC's "Investor-Demand" Rationale.

Our first comment described how the SEC's "investor-demand" rationale for the proposed rule is not in the public interest because the demand for climate information the SEC cites is not from investors, but *asset managers*. Comment of Boyden Gray, *supra*, at 32–35. But in the time since the proposed rule was published, even that purported demand has also collapsed. Today, the very asset managers the SEC cited in the proposed rule are sharply pulling back from the ESG investment products that require climate-related information. On the SEC's own rationale, the "investor demand" the proposed rule discusses no longer exists.

The SEC claimed in the proposed rule that there was "significant investor demand for information about how climate conditions may impact their investment." 87 Fed. Reg. at 21,340. For this "investor demand" rationale, the SEC cited the amount of assets under management collectively controlled by, among others, the asset managers BlackRock, State Street, and Vanguard. 87 Fed. Reg. at 21,3378 n.38. The SEC also cited the membership of several asset managers In the Net Zero Asset Managers Initiative. 87 Fed. Reg. at 21,340.

Our first comment explained that the primary drivers of this "demand" are asset managers, who are not investors. Comment of Boyden Gray, *supra*, at 32–35. But even if the SEC could validly consider asset managers to be "investors," its own rationale has since been undercut.

Since the SEC's publication of the proposed rule, BlackRock and State Street have begun "abandoning" so-called "sustainable" funds amidst collapsing demand for ESG investment products in the market—*i.e.*, demand by *actual* investors. *See* Silla Brush, *BlackRock, State Street Among Money Managers Closing ESG Funds*, Bloomberg (Sept. 21, 2023), https://www.bloomberg.com/news/articles/2023-09-21/blackrock-state-street-among-money-managers-closing-esg-funds. According to

Morningstar, more ESG funds have closed in 2023 than in the prior three years combined. *Id.* As of July 2023, investors had pulled more money out of ESG funds than they put into them. *Id.* Further, Vanguard left the Net Zero Asset Managers Initiative, which its CEO justified by stating "[o]ur research indicates that ESG investing does not have any advantage over broad-based investing." Chris Flood et al., *Vanguard chief defends decision to pull asset manager out of climate alliance*, Fin. Times (Feb. 21, 2023), https://www.ft.com/content/9dab65dd-64c8-40c0-ae6e-fac4689dcc77.

Asset manager demand for climate-related information—among the very asset managers the SEC cites—is not "increasing," 87 Fed. Reg. at 21,340, but, in fact, *declining*. It would be arbitrary for the SEC to conclude that investor demand supports the proposed rule, even along its own rationale that asset managers are "investors."

III. The Termination of ESG Ratings Products in the Market Undercuts the Proposed Rule's Purported Benefit of Reducing Reliance on Private ESG Ratings.

The SEC cited as a benefit of the proposed rule that "direct disclosures [of climate-related information] would reduce reliance on ESG ratings" provided by private ratings companies. 87 Fed. Reg. at 21,429. This benefit is either highly diminished or no longer available, as leading private ratings companies are increasingly abandoning the ESG ratings market.

As investor demand for ESG investment products has cratered, private ratings companies have diminished or dropped their ESG ratings altogether. In August 2023, S&P Global (a leading ratings company) ceased providing alphanumeric ESG scores to companies in "an about-turn that comes amid a backlash against environmental, social, and governance investing." Lauren Foster & Evie Liu, *S&P Drops ESG Scores for Credit Ratings Amid Backlash*, Barron's (Aug. 9, 2023), https://www.barrons.com/articles/sp-esg-credit-scores-5290338f. Further, in September 2023, Morningstar's ESG ratings unit Sustainalytics, another leading ratings company, announced it would lay off over 200 employees, further suggesting declining investor demand for ESG ratings. *Morningstar to cut up to 12% of staff at ESG unit Sustainalytics*, Reuters (Sept. 13, 2023), https://www.reuters.com/sustainability/morningstar-cut-up-12-staff-esg-unit-sustainalytics-2023-09-13/. Adding further pressure against suppliers of ESG ratings, attorneys general in 19 states have launched an investigation into potential violations of state consumer protection laws by Sustainalytics over its ESG ratings.

Ross Kerber, *Eighteen U.S. states join Missouri probe into Morningstar ESG*, Reuters (Aug. 17, 2023), https://www.reuters.com/world/us/eighteen-us-states-join-missouri-probe-into-morningstar-esg-2022-08-17/.

As a result of the ongoing decline of private ESG ratings offerings, the proposed rule cannot provide its described benefit of reducing reliance on ESG ratings.

Sincerely,

Boyden Gray PLLC