SEC's Climate Risk Disclosure Proposal Likely to Face Legal Challenges

Posted by Jacqueline M. Vallette and Kathryne M. Gray, Mayer Brown LLP, on Tuesday, May 10, 2022

Editor's note: Jacqueline M. Vallette is partner and Kathryne M. Gray is an associate at Mayer Brown LLP. This post is based on their Mayer Brown memorandum.

On March 21, 2022, the US Securities and Exchange Commission (SEC) voted 3:1 to propose new rules that, if adopted, would require public companies to, among other things, provide audited financial statements containing climate-related financial impact and expenditure metrics, report their greenhouse gas emissions, and disclose details of how climate change is affecting their businesses (the "Proposal"). Though some companies voluntarily report climate-related information, currently there are not any standardized requirements imposed by the SEC. In a statement of support, SEC Chair Gary Gensler said that the Proposal responds to demand from investors and companies given the increased push for information on the risks climate change-related events pose to businesses.

The Proposal signifies a substantial change to existing law and, if adopted, would have wide-ranging implications for companies' disclosure requirements and internal procedures. Given the significant additional expense the proposed rules would impose on public companies, the Proposal will likely face legal challenges. Dissenting and supporting statements from, and in response to, SEC commissioners have previewed the wide range of debate. SEC Commissioner Hester Peirce issued a lengthy dissenting statement sharply rebuking the Proposal, including on the basis that the SEC lacks authority to issue climate-related disclosure rules. As Commissioner Peirce described it, the Proposal "turns the disclosure regime on its head."

Summary of the Proposal

A summary of the Proposal's key disclosure requirements and resulting concerns is necessary for context before examining the potential legal challenges in detail. (A comprehensive description of the Proposal was previously discussed in the March 24 Mayer Brown Legal Update "SEC Proposes Climate Change Disclosure Rules Applicable to Public Companies.") At a high level, the approximately 500-page Proposal would require a public company to disclose the following information in registration statements and periodic reports:

- Climate-related risks and their actual or likely material impacts on the company's business, strategy, and outlook, as well as on the company's business and consolidated financial statements, which may manifest over the short-, medium-, or long-term;
- The company's governance of climate-related risks, including its processes for identifying, assessing, and managing climate-related risks and whether any such

processes are integrated into the company's overall risk management system or processes;

- Certain climate-related financial statement metrics and related disclosures in a note to audited financial statements;
- Information about climate-related targets and goals, and a transition plan, if any; and
- Direct and indirect greenhouse gas (GHG) emissions, which, for accelerated and large accelerated filers and with respect to certain emissions, would require third-party attestation reports. [1]

Publicly Expressed Concerns with the Proposal

While the entirety of the Proposal faces criticism, there are two specific aspects of it that some have strongly opposed: (1) the Scope 3 emissions disclosure requirement and (2) the SEC's elimination or recasting of the materiality qualifier in certain areas of the Proposal.

The Proposal requires the disclosure of three "Scopes" of emissions: (1) "Scope 1" emissions occur from sources directly owned or controlled by the company; (2) "Scope 2" or "indirect" emissions derive from the activities of another party, such as the generation of electricity purchased and consumed by the company; and (3) "Scope 3" emissions are all other indirect emissions generated from sources that are neither owned nor controlled by the company, including emissions occurring from upstream and downstream activities and goods. Compliance with disclosure requirements of Scope 3 emissions may be difficult and could impose considerable costs on issuers. The resources required to collect, quantify, and ensure the accuracy of Scope 3 data may be significant, not just in terms of the volume of required information but also because of the liability risk that companies face for inaccuracies in their disclosures. Indeed, the liability risk could be particularly elevated for Scope 3 emissions disclosures, which must rely on data generated from sources that are neither owned nor controlled by the reporting company. For instance, a company may have to disclose upstream emissions from purchased goods, capital goods, fuel and energy-related activities, transportation and distribution, waste generated in operations, and even business travel, employee commuting, and leased assets. Downstream emissions subject to disclosure could include processing of sold products, end-of-life treatment of sold products, leased assets and franchises, and transportation and distribution activities.

With respect to materiality, certain of the Proposal's disclosure requirements would dispense with materiality entirely (such as disclosure of Scope 1 and Scope 2 emissions). In other areas, it could be difficult to discern material from immaterial environmental impacts. Materiality has been the long-standing standard used to determine whether an investor is entitled to company information. [2] Disclosure is required when information is material, meaning there is a substantial likelihood that a reasonable investor would consider it important in deciding how to vote or make an investment decision. While issuers have generally been tasked with assessing their own disclosure obligations, including what information is material, courts have typically appealed to common sense: investors should get information that is important to consider in their investment

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[1] The Enhancement and Standardization of Climate-Related Disclosures for Investors, Release Nos. 33-11042; 34-94478 (Mar. 21, 2022), https://www.sec.gov/rules/proposed/2022/33-11042.pdf.

[2] *See TSC Industries v. Northway, Inc.*, 426 U.S. 438, 448-49 (1976) (defining the materiality standard in the context of federal securities law); *Basic, Inc. v. Levinson*, 485 U.S. 224, 484-85 (1988) (adopting "the *TSC Industries* standard of materiality" in the context of § 10(b) of the Exchange Act and SEC Rule 10b-5, 17 C.F.R. § 240).

decisions. Given that approach, many are left wondering why companies should be required to disclose *nonmaterial* information, which by definition is not important to investors, and relatedly why the SEC feels the need to mandate disclosure of such information to protect investors. The skepticism extends even further when you consider "the clear link between materiality of information and its relevance to the financial return of an investment" [3] rather than importance from a public policy standpoint.

Trade groups and organizations, state attorneys general, US senators, and other officials have already voiced opposition to mandatory reporting of Scope 3 emissions and its relationship to the materiality standard. For example, the Proposal's materiality qualifier for Scope 3 disclosures has been criticized as presuming materiality determinations that should be made by the reporting company in the first instance, imposing significant deterrents to omitting Scope 3 data, and presenting obscure quantitative and qualitative metrics at which emissions may be material. [4] Sixteen state attorneys general dispute the SEC's authority to require disclosures that are not financially material, arguing that existing SEC rules prohibiting misrepresentation of material information is "not a freestanding source of authority for the Commission to require climate change disclosures—at least without a showing that they are needed to prevent misleading or fraudulent representations." [5] These objections will likely be incorporated into formal comments on the Proposal during the rulemaking process.

Opposition to the Proposal has been swift and strong. [6] If the Proposal is adopted as a final rule in its current or a substantially similar form, affected companies, trade associations, or state officials are likely to challenge the new disclosure rules. There are at least four potential bases on which legal challenges could be made: (1) the SEC lacks statutory authority to adopt mandatory disclosure rules on climate change because such rules are outside the subject matters and purpose prescribed by Congress; (2) the new rules involve major questions of climate change policy that should be decided by duly elected members of the legislature, not a single executive branch agency; (3) the rules compel speech in violation of the First Amendment; and (4) depending on the SEC's explanation for its ultimate decision, the final rule is arbitrary and capricious under the Administrative Procedure Act.

Challenge 1: The SEC Lacks Statutory Authority to Promulgate Rules Requiring Climate-Related Disclosures.

Opponents of the Proposal claim that rules requiring detailed and extensive disclosure of climate-related metrics and similar ESG-related information exceed the SEC's statutory rulemaking authority. As multiple state attorneys general have already argued, the SEC's rulemaking powers must stay within the bounds of the purposes set forth in the SEC's enabling statutes, which "make

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[3] Statement by Commissioner Hester M. Peirce, *We are Not the Securities and Environment Commission—At Least Not Yet* (Mar. 21, 2022), https://www.sec.gov/news/statement/peirce-climate-disclosure-20220321 ("Peirce Statement").

[4] Peirce Statement, *supra* note 3; US Senators' Letter to Chair Gary Gensler and Commissioner Allison Herren Lee (June 13, 2021), https://www.sec.gov/comments/climate-disclosure/cll12-8911330-244285.pdf ("US Senators Letter").

[5] Sixteen State Attorneys General Letter to SEC Chair Gary Gensler (June 14, 2021), https://www.sec.gov/comments/climate-disclosure/cll12-8915606-244835.pdf ("State Attorneys General Letter").

[6] *See, e.g.*, US Senator Joe Manchin III Letter to SEC Chairman Gary Gensler (Apr. 4, 2022), https://www.manchin.senate.gov/imo/media/doc/SEC ClimateDisclosure Letter.pdf?cb; Forty Congressional Members' Letter to SEC Secretary Vanessa A. Countryman (Apr. 11, 2022), https://www.sec.gov/comments/s7-10-22/s71022-20123081-279409.pdf.

clear that legitimate mandatory disclosures are those required to protect investors from inflated prices and fraud, not merely helpful for investors interested in companies with corporate practices consistent with federally encouraged social views." [7]

Detractors could argue that Congress, and not the SEC on its own, must decide whether and how to require mandatory disclosures about climate change in public SEC filings. For agencies charged with administering congressional statutes, both their power to act and how they are to act is authoritatively prescribed by Congress. The SEC derives its rulemaking authority from the Securities Act of 1933 and the Securities Exchange Act of 1934. [8] Specifically, Section 7(a) of the Securities Act and Section 12(b) of the Exchange Act authorize the SEC to promulgate rules or regulations requiring disclosure of information that it believes is "necessary or appropriate in the public interest or for the protection of investors." [9] In determining whether an action is necessary or appropriate in the public interest, Congress has directed the SEC to consider, in addition to the protection of investors, "whether the action will promote efficiency, competition, and capital formation." [10]

While providing the SEC's rulemaking authority, these provisions also operate as limitations on that authority. The Supreme Court has "consistently held that the use of the words 'public interest' in a regulatory statute is not a broad license to promote the general public welfare[; r]ather, the words take meaning from the purposes of the regulatory legislation." [11] Thus, the SEC's authority to regulate "in the public interest" is not a concept without ascertainable criteria, and its authority to issue such rules does not afford it the power to impose disclosure obligations related to securities on *any* subject matter or to use the disclosure framework to achieve objectives that are unaligned with the objectives Congress has required the SEC to pursue. Rather, in order to give content and meaning to the SEC's rulemaking authority, it is necessary to look to the purposes for which the relevant statutory schemes were adopted. As detailed below, there is a reasonable argument that statutory context, legislative history, and other evidence of congressional intent authorize the SEC to require *only* disclosure of information *that is material to the prospect of a company's financial returns*.

First, the Securities Act and the Exchange Act limit the SEC's power to promulgate rules governing disclosure of specific types of information that are closely related to a disclosing company's value and prospects for financial success. Accordingly, Congress, with some exceptions, has restricted the subjects of mandatory disclosures to financial statements, core business information, directors and management, and a description of the securities being sold. Legislative history from the enactment of the Securities Act in 1933 and the Exchange Act in 1934 further suggests that Congress deliberately enumerated these categories of information for company disclosure and did not confer on the SEC unconfined authority to elicit any information whatsoever. Notably, as the SEC itself pointed out, when Congress wished to later expand the subject matter of mandatory disclosures beyond matters that are financial in nature, it specifically

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[7] State Attorneys General Letter, *supra* note 5.

[8] Securities Act of 1933, 15 U.S.C. §§ 77a, *et seq.*; Securities Exchange Act of 1934, 15 U.S.C. §§ 78a, *et seq*.

[9] 15 U.S.C. §§ 77g(a)(1), 78l(b)(1); *see also id.* § 78m(a) ("as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security").

[10] *Id*. §§ 77b(b), 78c(f); *see also id*. § 78w(a)(2). The SEC has interpreted its authority as cabined by its "core mission to promote investor protection, market efficiency and competition, and capital formation." Business and Financial Disclosure Required by Regulation S-K, 81 Fed. Reg. 23,916, 23,917, 23,922 & n.6 & n.55 (Apr. 22, 2016).

[11] *NAACP v. FPC*, 425 U.S. 662, 669 (1976).

did so *by statute*, including for topics such as executive compensation, corporate governance, and conflict minerals.

In addition, Congress has mandated environmental reporting requirements with specificity in other contexts. Congress authorized the Environmental Protection Agency (EPA) to collect reports from emission sources and make them available to the public, and the EPA implemented an annual Greenhouse Gas Reporting Program (GHGRP) that covers thousands of facilities that are large sources of GHG emissions. As part of its GHGRP Program, the EPA mandates public disclosure of GHG emissions. Challengers of the Proposal may seek to use this dichotomy of authority to argue that the SEC lacks, and cannot not act without, equally clear statutory authority.

In 2016, the SEC itself acknowledged that "a specific congressional mandate" would be required before it adopted rules ordering climate change- and ESG-related disclosures. [12] But no such congressional mandate exists. [13] The limitations SEC acknowledged remain.

Challenge 2: The Proposal Exceeds the Limits on Regulation of Major Policy Questions.

The "major questions" doctrine arose from the notion that important choices of social policy should be made by Congress. [14] An agency's exercise of regulatory authority over a major policy question of great economic and political importance requires a clear delegation of authority by Congress. Thus, litigants could invoke this doctrine to argue that, in the absence of a clear congressional command, the regulation of climate disclosures is too significant of a question to rest in the hands of a single Article I regulator like the SEC; instead, setting climate policy is the job of legislators, duly elected by and responsible to the people.

For courts reviewing legal challenges to the SEC's new climate-related disclosure requirements, one key question will be whether the SEC's rules regulate a major policy question of great economic and political importance. Expansive climate-related regulations that have never before been in the province or mandate of the SEC may well fit this criterion. [15] Indeed, the nation's response to climate change and, specifically, the topic of climate change disclosures by public companies, present major and contentious policy questions that are unresolved, including within Congress itself.

Assuming the Proposal does involve a major policy question, it could be difficult for the SEC to argue that Congress has spoken "clearly" to confer on the SEC the authority to promulgate regulations requiring reporting of climate-related information. Congress granted the SEC regulatory authority to protect investors; facilitate capital formation; and maintain fair, orderly, and

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[12] 81 Fed. Reg. at 23,970 & n.663.

[13] In June 2021, the House of Representatives passed a climate risk disclosure bill that would require companies to disclose climate-related risk exposure and risk management strategies. *See* Climate Risk Disclosure Act of 2021, H.R. 1187, 117th Cong. § 402(8) (2021). However, the Senate has not yet passed such a bill.

[14] I*ndus. Union Dep't, AFL-CIO v. Am. Petr. Inst*., 448 U.S. 607, 685 (1980) (Rehnquist, J., concurring) (major policy decisions must be made by Congress and the president in the legislative process, not delegated to agencies); *Nat'l Fed. of Indep. Bus. v. OSHA*, 142 S. Ct. 661 (2022).

[15] The Supreme Court's forthcoming decision in *West Virginia v. EPA*, No. 20-1530, involving the scope of the EPA's authority to regulate greenhouse gases, may inform how a reviewing court would treat a legal challenge to the SEC's climate disclosure rules. Questioning during oral argument, where the major questions doctrine was raised repeatedly, revealed a lack of clear consensus on what the doctrine requires. How the Court ultimately addresses this point could have broader impacts on federal agency regulation, including the legality of the SEC's new disclosure rules.

efficient markets. As Commissioner Peirce pointed out, “Congress, however, did not give [the SEC] plenary authority over the economy and did not authorize [it] to adopt rules that are not consistent with applicable constitutional limitations.” [16]

The Proposal’s opponents can point to recent Supreme Court precedents that invoke the major questions doctrine. Just three months ago, the Supreme Court held that a vaccine mandate issued by the Occupational Safety and Health Administration (OSHA) “significantly expand[ed] OSHA’s regulatory authority without clear congressional authorization” and was thus unlawful. [17] Specifically, the Court concluded: (a) the mandate was “a significant encroachment into the lives—and health—of a vast number of employees” and thus constituted an exercise of agency “power[] of vast economic and political significance” requiring clear congressional delegation; and (b) OSHA’s enabling statute, which empowers OSHA “to set *workplace* safety standards, not broad public health measures,” did not “plainly authorize[]” the mandate. [18] The Court observed that in OSHA’s half century of existence, it “has never before adopted a broad public health regulation of this kind” and, when coupled with the breadth of authority claimed by the agency, that lack of historical precedent signified that the vaccine mandate “extend[ed] beyond the agency’s legitimate reach.” [19] Similar challenges may be leveled against the SEC’s new climate-related disclosure rules, which, if adopted as proposed, arguably expand disclosure requirements beyond the core principle of financial materiality that has animated SEC regulation from inception.

Moreover, legal challenges may be advanced through a related, albeit rarely invoked, constitutional separation-of-powers principle known as the nondelegation doctrine. [20] The Supreme Court has repeatedly held that Congress may authorize an agency to regulate in an area so long as it gives the agency an “intelligible principle” on which to base the regulations. [21] The Supreme Court has not struck down a statute for violating that principle since the New Deal. However, several current justices have suggested that the Constitution places additional limits on Congress’s power to authorize agencies to issue regulations. [22] It is not clear what the additional limits would be. Nonetheless, litigants have invoked those statements to argue that congressional delegations of rulemaking authority are unconstitutional. Proposal challengers likewise could argue that the statutory authority that the SEC invokes to promulgate the rule is an unconstitutional delegation of legislative power by Congress, and the Proposal

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[16] Peirce Statement, *supra* note 3.

[17] *Nat’l Fed. of Indep. Bus. v. OSHA*, 142 S. Ct. 661, 665 (2022) (addressing a vaccine mandate that applied to roughly 84 million US workers, covering virtually all employers with at least 100 employees).

[18] *Id*. (emphasis in original).

[19] *Id.* at 666.

[20] *See OSHA*, 142 S. Ct. at 668-69 (Gorsuch, J. concurring) (“[T]he major questions doctrine is closely related to . . . the nondelegation doctrine . . . . Both are designed to protect the separation of powers and ensure that any new laws governing the lives of Americans are subject to the robust democratic processes the Constitution demands.”).

[21] *See J.W. Hampton v. United States*, 276 U.S. 394 (1928).

[22] *See Gundy v. United States*, 139 S. Ct. 2116 (2019); *Paul*, 140 S. Ct. at 342. In his dissenting opinion in *Gundy*, Justice Gorsuch, joined by Chief Justice Roberts and Justice Thomas, called for the Court to revive the nondelegation doctrine, criticizing current principles that allow for congressional delegation. *Gundy*, 139 S. Ct. at 2136-48. Concurring only in the plurality’s judgment, Justice Alito concluded that, while he did not favor invalidation of the specific statute at issue in *Gundy* given the current legal standards, he would support an effort to reconsider the Court’s approach to congressional delegation if a majority of the Court was so willing. While Justice Kavanaugh did not take part in consideration of *Gundy*, he has since foreshadowed that he would likely join Justices Gorsuch, Thomas, Alito, and Roberts in reviving the nondelegation doctrine. *See Paul*, 140 S. Ct. at 342 (“Justice Gorsuch’s scholarly analysis of the Constitution’s nondelegation doctrine in his *Gundy* dissent may warrant further consideration in future cases.”).

therefore is invalid. Although that argument is unlikely to prevail under the current nondelegation doctrine, this is an area to watch for potential developments in the law.

Challenge 3: The Proposal Unconstitutionally Compels Speech.

Challengers of the new disclosure requirements also may invoke the First Amendment to argue that mandating environmental impact disclosures from publicly traded companies is unconstitutional compelled speech. If public companies are required to comply with the SEC's proposed climate-related disclosure requirements, the argument goes, some companies would be forced to make remarks about their operations that are subjective or disparaging. This is something the First Amendment may protect against.

Some recent precedents suggest a reviewing court may apply an intermediate scrutiny test to the SEC's climate disclosure rules, which would require the SEC to show (1) a substantial government interest that is (2) directly and materially advanced by the rules and (3) that the rules are narrowly tailored. [23] Litigants would have potential arguments for each of these prongs. First, opponents of the Proposal could argue that compelling issuers to speak on information that is not material to financial performance is outside the SEC's core mission and that responding to public demand for increased information about companies' climate measures is not a sufficiently substantial governmental interest to compel such speech. [24] Second, as demonstrated by the SEC's internal disagreements, a great deal of uncertainty exists about the correct values, assumptions, and scenarios for its proposed climate-related disclosure requirements, [25] and, therefore, the resulting disclosures may be inaccurate or controversial, such that they cannot directly and materially advance any government interest that may exist. Finally, litigants could argue that less restrictive means are available because they already exist, namely requirements to disclose *material* climate-related information and to comply with other existing regulations. [26] In addition, peer comparability has led to many companies reporting such information voluntarily or outside the SEC disclosure context in response to requests from investors and other stakeholders. [27]

Litigants may also draw parallels to a recent DC Circuit decision partially vacating a prior SEC rulemaking governing mandatory disclosures of conflict minerals, which was adopted pursuant to an express congressional mandate in the Dodd-Frank Act. In *National Association of Manufacturers v. SEC*, the court of appeals concluded that the First Amendment prevented the SEC from compelling companies to describe their products as not "DRC conflict free" in publicly

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[23] C*entral Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of New York*, 447 U.S. 557, 564-66 (1980); *see also Nat'l Ass'n of Mfrs. v. SEC*, 800 F.3d 518, 521 (D.C. Cir. 2015) (*NAM II*) (applying *Central Hudson*'s intermediate scrutiny to speech compelled by the SEC's prior conflict mineral disclosure rule).

[24] *See*, *e.g.*, State Attorneys General Letter, *supra* note 5.

[25] Commissioner Peirce's dissenting statement highlights the potential confusion created by the Proposal's metrics for materiality in disclosing Scope 3 emissions. *See* Peirce Statement, *supra* note 3. The SEC's unproven methodology is in stark contrast to the uniform, collective judgments of a broad swath of securities professionals with differing views on ESG issues who have determined that statements regarding the quantity of direct or indirect GHG emissions are not material to investors' decisions. As certain opponents have flagged, a review of the 2020 Form 10-K annual reports of the Fortune 150 revealed that none of these reports included quantified metrics regarding the extent of issuer-associated GHG emissions, which is a strong indicator that such information is not necessary to protect investors who are considering securities purchases. *See* State Attorneys General Letter, *supra* note 5.

[26] *See* 40 C.F.R. §§ 98.1, *et al*. (EPA regulations governing "mandatory greenhouse gas (GHG) reporting requirements for owners and operators of certain facilities that directly emit GHG as well as for certain suppliers").

[27] *See* State Attorneys General Letter, *supra* note 5.

filed reports. [28] Applying intermediate scrutiny, [29] the court held that the SEC's purported interest in adopting a forced disclosure regime to ameliorate the humanitarian crisis in the Congo by decreasing revenue of armed groups was unproven and rested on speculation; thus, the SEC could not satisfy its burden of demonstrating that the measure it adopted would "in fact alleviate" the harms it recited "to a material degree." [30] Accordingly, the court partially invalidated the Dodd-Frank Act's conflict minerals disclosure requirement.

Companies may not report climate-related data at a rate that the SEC prefers, or disclose information about matters the SEC deems worthy of regulating, but that does not allow the SEC to circumvent the First Amendment. As the *NAM II* court stated: "[R]equiring a company to publicly condemn itself is undoubtedly a more effective way for the government to stigmatize and shape behavior than for the government to have to convey its views itself, but that makes the requirement more constitutionally offensive, not less so." [31]

Challenge 4: The Final Rule Is Arbitrary and Capricious Under the Administrative Procedure Act.

If the SEC adopts the Proposal as a final rule, another challenge could be that it is arbitrary and capricious in violation of the Administrative Procedure Act (APA). [32] To justify a break with long-standing policy, the SEC's new rules must confront past findings and provide good reasons for departing from them. Depending on the language of the final rule and the SEC's justifications for adopting the rule, challengers may argue that the SEC's underlying rationale or factual assertions are inconsistent, unsupported, unreasonable, or fail to offer sufficient justification for choosing a given proposal over alternatives. [33] If the reasoning in the final rule is similar to that in the Proposal, challengers could argue that the SEC unreasonably concluded that the rule will generate comparable, consistent, and reliable disclosures.

For example, industries may take issue with the SEC's estimates of the costs companies will face to comply with the new disclosure requirements. The Proposal surmises that the cost of increased compliance burdens could be "relatively small" if companies already provide similar information required by the Proposal, [34] but the SEC must proceed cautiously with that assumption. Courts have on multiple occasions vacated other SEC rules under the APA for failure to adequately consider economic consequences, after parsing in fine detail the methods and results of a given rule's cost-benefit analysis. In vacating the SEC's rule expanding proxy ballot access, for instance, the DC Circuit held that the SEC had "inconsistently and

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[28] *Nat'l Ass'n of Mfrs. v. SEC (NAM 1)*, 748 F.3d 359, 371 (D.C. Cir. 2014), overruled in part by *Am. Meat Inst. v. U.S. Dep't of Agr.*, 760 F.3d 18 (D.C. Cir. 2014) (en banc). On rehearing, the *NAM II* panel reaffirmed its initial judgment in *NAM I. See NAM II,* 800 F.3d at 521.

[29] The *NAM* court determined that the relaxed standard of rational basis review did not apply because rational basis review generally applies only to compelled commercial-speech disclosures that serve a governmental interest in preventing consumer deception, and the SEC's rule did not seek to advance such goal. *NAM I*, 748 F.3d at 370-72; *NAM II*, 800 F.3d at 554.

[30] *NAM II,* 800 F.3d at 527.

[31] *Id*. at 530.

[32] *See* 5 U.S.C. § 706(2).

[33] *See Bus. Roundtable v. SEC*, 647 F.3d 1144, 1148–49 (D.C. Cir. 2011) (vacating SEC rule expanding proxy ballot access for shareholder-nominated board candidates for inadequate economic analysis); *Am. Equity Invest. Life Ins. Co. v. SEC,* 613 F.3d 166, 167-68 (D.C. Cir. 2010) (vacating SEC rule regarding fixed index annuities for failure to consider economic effects); *Chamber of Commerce v. SEC*, 412 F.3d 133, 136 (D.C. Cir. 2005) (vacating SEC rule regarding independent directors on investment company boards for failure to consider costs and alternatives).

[34] The Enhancement and Standardization of Climate-Related Disclosures for Investors, *supra* note 1, at p. 305.

opportunistically framed the costs and benefits of the rule; failed adequately to quantify the certain costs or to explain why those costs could not be quantified; neglected to support its predictive judgments; contradicted itself; and failed to respond to substantial problems raised by commenters." [35]

Additionally, pursuant to its statutory rulemaking authority, the SEC must consider "whether the action will *promote* efficiency, competition, and capital formation." [36] Some opponents of the Proposal argue that the SEC has failed to adequately articulate why the current principles-based system of climate-related and other ESG disclosures—in which companies determine on a case-by-case basis whether a reasonable investor would consider the disclosure important—does not already provide sufficient protections to enable investors to make informed decisions. [37] For example, Commissioner Peirce emphasized the lack of any credible rationale for the Proposal's prescriptive framework when existing disclosure requirements already capture material risks relating to climate change. Relatedly, critics have argued that a broad, rigid approach across public companies, including those that are not major emitters of GHG, could alter the SEC's definition of investor demand and fail to take into account what is reasonable under the varying conditions faced by different companies. The SEC's response to public comments in the notice and comment period before a final rule is published will be important when the courts are asked to decide if the SEC's rules are arbitrary and capricious under the APA.

Conclusion

We anticipate a heavy volume of comments on the Proposal. [38] As discussed above, there is already intense interest in, and scrutiny of, the SEC's asserted authority to regulate the new territory of climate change, a subject matter arguably outside its mission and mandate, without any additional congressional grant of authority. Pursuant to standard administrative law principles and procedures, the SEC must consider and respond to any important arguments or data presented by public commenters. By design, the notice and comment process is intended to allow the agency to respond to comments by changing the terms of the Proposal at adoption, but it cannot, without additional notice and comment, make changes to the Proposal that are so significant that the public did not reasonably have the chance to comment on the final rule.

Should the Proposal eventually be adopted in its current form (or in any form without substantial revision), significant litigation challenges will likely follow. It may take years for any facial legal

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[35] *Bus. Roundtable*, 647 F.3d at 1148-49.

[36] 15 U.S.C. § 77b(b) (providing that, for every rulemaking, the SEC "is required to consider or determine whether an action is necessary or appropriate in the public interest, . . . [and] shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation").

[37] *See Am. Equity Invest. Life Ins.*, 613 F.3d at 178 (holding that "the SEC's analysis [was] incomplete because it fail[ed] to determine whether, under the existing regime, sufficient protections existed to enable investors to make informed investment decisions" and that the "failure to analyze the efficiency of the existing state law regime renders arbitrary and capricious the SEC's judgment that applying federal securities law would increase efficiency").

[38] Public comments to the Proposal are due by May 20, 2022 (60 days after issuance). The SEC received approximately 600 unique comments in response to then-Acting Chair Lee's request for public input on climate disclosures. Now, with approximately 500 pages of details crystallized in a formal proposed rule, we expect substantially more engagement. For context, when the Federal Communications Commission (FCC) opened up the public comment period on its proposal to roll back net neutrality rules, it received almost 22 million comments. If the Proposal elicits even a fraction of the comments the FCC's net neutrality rules received, the SEC's notice and comment process could easily take half a year.

challenges to work through the federal courts. Even then, the battle may continue as defendants in SEC enforcement proceedings assert “as applied” challenges to the new rules.