April 4, 2023

The Honorable Gary Gensler
Chairman
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington, DC 20549-1090

Dear Chairman Gensler,

On behalf of the undersigned organizations, we write to offer observations regarding how private markets contribute to climate-related risks in our financial system. We also write to offer strong support for rulemaking that would help restore the health and vitality of our public markets, and in so doing would limit the ability for companies to shift dirty assets into private markets, thereby hiding them from investors and limiting the effectiveness of the Commission's forthcoming climate-related disclosure rules for public issuers.

**Climate Change-related Disclosure**

As you are well aware, climate change presents significant and increasing financial risks for investors, markets, and our broader economy. Hence, the need for companies to disclose their climate-related risks and impacts is greater than ever. Due to overwhelming investor demand for this information, the Securities and Exchange Commission is set to release a final rule this Spring that will establish a mandatory climate change-related reporting framework for public companies. That rule, as proposed, is consistent with our securities laws' framework, which is based on the notion that only through full and fair disclosure can investors reliably determine the value of a company and make informed investment decisions.[1] Climate risks have profound financial and operational consequences for companies, and investors need accurate and reliable information about those risks in order to properly value their investments and prudently allocate capital.

However, the securities laws' disclosure framework, including the Commission's climate proposal, only applies to public reporting companies, i.e., only companies that register their securities with the Commission. Thus, these rules do not apply to companies that issue securities privately, i.e., companies that sell their securities into the private market through exempt or unregistered offerings. Because issuers of private securities are not required to provide

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[1] *See* John Coates, *Comment Letter Re: The Enhancement and Standardization of Climate-Related Disclosures for Investors* (June 2, 2022), https://bit.ly/3Id9W4x.

information about their activities or risks to the purchasers or holders of these securities, their investors seldom receive the climate risk-related information—or any other disclosures—that are material to investor decision making. Thus, while the Commission's climate proposal would enhance disclosures for approximately 6,220 public issuers,[2] it would not touch an enormous segment of our securities markets.

**Investors Rely on Full and Fair Disclosure**

Our public securities markets provide the gold standard of ensuring the most deserving companies are able to raise capital in a way that protects investors and promotes market integrity. Investors in our public markets receive the essential facts and material information needed to value their investments and make informed investment decisions. This system of full and fair disclosure rewards the best companies and limits the reach and growth of the worst. As the SEC has explained, the disclosure obligations in the Securities Act of 1933 Act and Securities Exchange Act of 1934 Act are based on "a simple and straightforward concept: all investors, whether large institutions or private individuals, should have access to certain basic facts about an investment prior to buying it, and so long as they hold it. Only through the steady flow of timely, comprehensive, and accurate information can people make sound investment decisions."[3] Accordingly, a key result of that transparency "is a far more active, efficient, and transparent capital market that facilitates the capital formation so important to our nation's economy."[4]

The Commission's climate proposal fits squarely within the purview and purpose of these principles. Investors have demonstrated that they need full and fair climate-related information when making decisions about how to manage risk and allocate their capital, i.e., whether to buy, hold or sell a particular security, and how much they should pay for it. This includes information about companies' plans related to climate change and the potential cost of those plans, and investors of all types and sizes have called on the Commission to facilitate accurate, reliable, and decision-useful disclosure of this information.[5] Therefore, it is incumbent upon the Commission to finalize climate-related disclosure requirements for public issuers.

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[2] Proposed Rule, *The Enhancement and Standardization of Climate-Related Disclosures for Investors* at 295 (March 21, 2022), https://bit.ly/3lN7w4M.

[3] U.S. Securities and Exchange Commission, About the Sec, What We Do, http://bit.ly/2MngEXy (last accessed August 16, 2019, quote subsequently removed).

[4] *Id.*

[5] The Commission's Climate Proposal points to numerous investor initiatives that have urged companies to provide better information about the impacts of climate change. *See, e.g.*, *The Enhancement and Standardization of Climate-Related Disclosures for Investors* at 334 ("The 2021 Institutional Investors Survey solicited the views of 42 global institutional investors managing over $29 trillion in assets (more than a quarter of global assets under management (AUM)) and found that climate risk remains the number one investor engagement priority. A significant majority (85%) of surveyed investors cite climate risk as the leading issue driving their engagements with companies. These institutional investors also indicated that they consider climate risk to be material to their investment portfolios and are demanding robust and quantifiable disclosure around its impacts and the plan to transition to net zero." (*citing* Morrow and Sodali, *Institutional Investor Survey* (2021), https://bit.ly/3sWwboy.)); *and id.* at 14 ("[A]s climate-

**Bad Things Happen in the Dark**

In many ways, however, private markets operate differently than our public markets. There is no guarantee that private companies will provide any information about their activities or risks to investors or the market. Because of this lack of transparency, it is extremely difficult to value private companies and price their risk. To the extent private companies do selectively provide information to certain favored investors, that information may not be accurate or reliable. Yet it can be exceedingly difficult for investors to hold private companies accountable for any errors or omissions they make in their disclosures. Under these conditions, private markets present significant and often untenable risks for the overwhelming majority of investors.[6]

Despite these shortcomings, private companies are legally allowed to raise an unlimited amount of money from an unlimited number of investors, which provides little incentive to go public.

Without the need or incentive to go public, private companies can stay private forever and avoid any disclosure obligations. However, their ability to stay dark deprives investors and the market of critical information, including information regarding climate-related risks, as well as other important ESG disclosures, including those relating to corporate board diversity, cybersecurity risks, and human capital management.

**Lack of Private Market Disclosures Can Lead to Regulatory Arbitrage**

Under these circumstances, and especially in the climate disclosure context, it can also create incentives for public companies to move dirty assets off of their balance sheets and into the private markets.[7] While this practice may give the impression that public companies are eliminating climate-related risks, the reality would be they are merely shifting those assets into the dark. At present, neither economic nor regulatory safeguards prevent companies from doing so.[8]

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related impacts have increasingly been well documented and awareness of climate-related risks to businesses and the economy has grown, investors have increased their demand for more detailed information about the effects of the climate on a registrant's business and for more information about how a registrant has addressed climate-related risks and opportunities when conducting its operations and developing its business strategy and financial plans.").

[6] *See* Consumer Federation of America, *Comment Letter Re: Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets* at 32-36 (June 4, 2020), https://bit.ly/3DtGZ2S.

[7] *See* The Economist, *The Truth About Dirty Assets* (February 12, 2022), http://bit.ly/42WkXAN.

[8] This is also true of other important forthcoming rules requiring enhanced disclosures of certain ESG-related risks like, for example, rules for corporate board diversity, cybersecurity risks, and human capital management disclosures.

The ability of private companies to stay dark and of public companies to shift dirty assets into the dark could mean that the overall levels of emissions and climate impacting activities could remain the same, or perhaps even grow.[9] If private markets become a de facto risk repository for the dirtiest assets, then despite the Commission's best efforts to facilitate relevant climate-related information, investors would remain in the dark about these risks, unable to price these risks effectively or ascertain their true exposure to these risks.

In a 2021 op-ed, State Street CEO Cyrus Taraporevala predicted that the path to a net-zero economy would be littered with this type of activity, stating that, "Some companies may simply take the easy path of brown-spinning and sell off their highest emitting assets to the top private bidder who may be less concerned about climate change."[10]

Unsurprisingly, "brown spinning" is already occurring at a rapid clip in the oil and gas sector, where the risk of stranded carbon-intensive assets is greatest. A 2021 Financial Times article highlighted this trend, stating, "Under intense pressure from investors and activists to take more action on climate change, some of the world's biggest oil and gas companies are putting billions of dollars' worth of assets up for sale."[11] According to the article, "The quickest way to shrink emissions as a major company is to shed assets so you can hit climate-related targets . . . But asset sales do nothing for climate change, you're just moving emissions from one hand to another."[12]

At a 2021 Brookings event, BlackRock CEO Larry Fink spoke directly to this issue, stating that, "If regulation is only going to be for public companies, we are going to see a huge arbitrage and that arbitrage is existing right now[.]"[13] Then, referring to the effects of mandatory disclosure for public companies, Fink observed that, "Now once we have that unification of standards and companies reporting it, you can't hide as a public company. Now the beauty is you can hide as a private company. Okay? It gets back to this arbitrage. And that arbitrage is grossly unfair if we think the standard should only apply to public companies. We're going to see more and more public companies going private if we don't solve the problem. And that's where government and government policy has to have an opinion."[14]

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[9] *See* Anjli Raval, *A $140bn Asset Sale: The Investors Cashing in on Big Oil's Push to Net Zero*, Financial Times (July 6, 2021), http://bit.ly/3WS8Tfq.
[10] Cyrus Taraporevala, *The Other Climate Risk Investors Need to Talk About*, Financial Times (May 14, 2021), http://bit.ly/3HMQyfw.
[11] Raval, *A $140bn Asset Sale: The Investors Cashing in on Big Oil's Push to Net Zero*.
[12] *Id.*
[13] The Brookings Institution, *Climate Change and Financial Market Regulation: Insights from BlackRock CEO Larry Fink and Former SEC Chair Mary Schapiro*, Webinar Transcript at 7 (February 2, 2021), https://bit.ly/3S7RPkN.
[14] *Id.* at 9-10.

## Voluntary Disclosure and Private Ordering Is Inadequate

To the extent some argue that external pressure on private companies will cause them to disclose climate-related risks, those arguments ignore the fact that relying on a voluntary disclosure regime in public markets to date has not resulted in public companies providing consistent, reliable, and credible (i.e., decision-useful) information. These arguments also ignore the fact that private companies routinely avoid disclosing critical, decision-useful information to investors.

The absence of decision-useful climate-related information will directly imperil investors in private markets and contribute to the misdirection of capital. The inability to effectively assess climate-related risks can cause investors to assume greater climate risk than they desire, misprice investment risks and misvalue companies, and promote companies that worsen climate outcomes. This leads to a decline in overall market efficiency and stability.[15]

Unpriced climate-related risks also provide fertile ground for "greenwashing," which occurs when an issuer falsely or misleadingly conveys that an investment is environmentally sound or ESG-friendly. Without the ability to assess the climate risk exposure of private securities, investors are susceptible to being sold risky investments under the guise that the investments do not carry these risks. Without the ability to access accurate and reliable information, it would likely be exceedingly difficult for investors in private markets to know whether they are victims of greenwashing. And if they don't know if they've been victimized, it's unlikely they would hold greenwashers accountable. Also, risks that remain unaccounted for have the potential to cause real harm to society writ large, including increasing systemic risk, enabling polluting companies' longevity, and misdirecting capital from the most deserving companies to the least deserving companies, among other negative impacts.[16]

## Reining In Private Markets Can Help Protect from Climate and Other Risks

The Commission can and should take action both to limit private companies' ability to hide the climate-related risks outlined above and to promote the health and vitality of public markets generally.

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[15] *See, e.g.*, State Street Global Advisors, *Boom in Private Markets is No Private Matter* at 16 (October 2019), https://bit.ly/3x2oi2i (Noting that private markets are dependent on healthy public markets and that they get a "free ride on the price discovery mechanisms of public markets, freely taking price signals as reference points for their own valuations and transactions. Leaving this trend unchecked could create bigger imbalances and weaker capital markets in the future.").

[16] *See, e.g.*, Michael Panfil and David Victor, *Climate Change Creates Financial Risks. Investors Need to Know What Those Are*, Brookings (March 29, 2022), http://bit.ly/3x1mlDr.

This can be achieved in part through relatively modest regulatory changes that would help to rebalance the boundaries between public and private markets. This includes updating the Accredited Investor definition, making modest changes to the Regulation D framework, and making long overdue changes to Section 12(g) of the Exchange Act.[17]

Individually and collectively, these updates should be designed to rein in private companies' ability to raise unlimited amounts of money from an unlimited number of investors. In so doing, these updates would stem the growth of private markets and encourage companies to go public, where they would be subject to public disclosure requirements, including disclosure of their climate- and other ESG-related risks.

**Conclusion**

Unless the structural problems outlined above are addressed, the Commission's efforts to improve climate disclosures will, at best, be a partial success, leaving a wide swath of investors and our markets vulnerable to the profound risks of climate change, and compounding the unhealthy imbalance between public and private markets that exists today.

Respectfully,

Americans for Financial Reform Education Fund
As You Sow
Consumer Federation of America
Figure 8 Investment Strategies
Friends Fiduciary
Interfaith Center on Corporate Responsibility (ICCR)
Majority Action
Miller/Howard Investments, Inc.
Public Citizen
School Sisters of Notre Dame Cooperative Investment Fund
SHARE
Sierra Club
Sinsinawa Dominicans, Inc.
The Sunrise Project

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[17] *See* Letter from Dylan Bruce, CFA, to SEC Chair Gary Gensler (November 15, 2022), https://bit.ly/3YV5kHr.