U.S. SMALL BUSINESS ADMINISTRATION
OFFICE OF ADVOCACY
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June 17, 2022

VIA ELECTRONIC SUBMISSION

Vanessa A. Countryman, Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: The Enhancement and Standardization of Climate-Related Disclosures for Investors – File Number S7-10-22

Dear Ms. Countryman:

On April 11, 2022, the Securities and Exchange Commission (SEC or Commission) published proposed rules that would require public companies to provide detailed disclosures about climate-related risks and climate-related financial metrics in their registration statements and annual reports, including greenhouse gas (GHG) emissions.[1] This letter constitutes the Office of Advocacy's (Advocacy) public comments on the proposed climate disclosure rules.

Advocacy supports the Commission's commitment to ensure that investors have consistent and reliable information, including information about companies' climate-related risks and metrics. The ability to assess climate risks is important to the future of the U.S. economy. Nevertheless, Advocacy encourages the Commission to take a holistic approach to its regulatory agenda with a focus on small business impacts. The climate disclosure rules impose fixed costs that will fall disproportionately on small entities. These costs do not occur in isolation and must be viewed in conjunction with other SEC regulations. Advocacy urges the Commission to focus on the cumulative impacts its regulations have on small entities. This would ease the heightened burden of its regulations on the small business community.

As detailed in this letter, Advocacy is concerned about the widespread economic impacts of the proposed climate disclosure rules on both public and privately owned small businesses. First, Advocacy is concerned that the Initial Regulatory Flexibility Analysis (IRFA) in the proposed

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[1] 87 Fed. Reg. 21334.

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rules lacks essential information required under the Regulatory Flexibility Act (RFA).[2] Specifically, the IRFA does not adequately describe the costs of the proposed disclosure requirements on the small entities that would be directly regulated. Nor does the IRFA set forth significant alternatives which accomplish the stated objectives, and which minimize the significant economic impact of the proposal on regulated small entities beyond accommodations that are already included in the rulemaking. Second, the proposal does not consider indirect impacts to privately owned businesses that are not generally subject to SEC regulation. Based upon feedback received by Advocacy from multiple industries, the costs of the proposal to small private businesses could be extensive.

For these reasons, Advocacy recommends the SEC publish a Supplemental IRFA for public comment before proceeding with this rulemaking. Advocacy further recommends that the SEC reconsider its requirements for the Scope 3 GHG emissions disclosure when considering the impacts these rules could have on the small business community.

I. Background

A. The Office of Advocacy

Congress established the Office of Advocacy under Pub. L. 94-305 to represent the views of small entities before Federal agencies and Congress. Advocacy is an independent office within the U.S. Small Business Administration (SBA). As such the views expressed by Advocacy do not necessarily reflect the views of the SBA or the Administration. The RFA, as amended by the Small Business Regulatory Enforcement Fairness Act (SBREFA),[3] gives small entities a voice in the rulemaking process. For all rules that are expected to have a significant economic impact on a substantial number of small entities, the RFA requires federal agencies to assess the impact of the proposed rule on small entities and to consider less burdensome alternatives.

The Small Business Jobs Act of 2010 requires agencies to give every appropriate consideration to comments provided by Advocacy.[4] The agency must include a response to these written comments in any explanation or discussion accompanying the final rule's publication in the *Federal Register*, unless the agency certifies that the public interest is not served by doing so.[5]

Advocacy's comments are consistent with Congressional intent underlying the RFA, that "[w]hen adopting regulations to protect the health, safety, and economic welfare of the nation, federal agencies should seek to achieve statutory goals as effectively and efficiently as possible without imposing unnecessary burdens on the public."[6]

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[2] 5 U.S.C. § 601 et seq.
[3] Pub. L. 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C. §601 et seq.).
[4] Small Business Jobs Act of 2010 (PL. 111-240) §1601.
[5] *Id*.
[6] *Id*.

B. The Proposed Rules

On April 11, 2022, the SEC published a notice of proposed rulemaking on *The Enhancement and Standardization of Climate-Related Disclosures for Investors*.[7] The proposal would amend the Commission's rules under the Securities Act of 1933[8] and Securities Exchange Act of 1934[9] to require public companies to provide certain climate-related information in their registration statements and annual and periodic reports.

The proposed provisions under Regulation S-K would require disclosure of a registrant's governance of climate-related risks, any material climate-related impacts on its strategy, business model and outlook, and its climate-related risk management.[10] Registrants would be required to disclose GHG emissions metrics and any climate-related targets and goals.[11] Proposed provisions under Regulation S-X would require a registrant to disclose in a note to its financial statements three categories of climate-related financial statement metrics: financial impact metrics, expenditure metrics, and financial estimates and assumptions.[12]

A key component of the proposal is the requirement that registrants disclose GHG emissions. The SEC has based its proposed emissions disclosure rules on the Greenhouse Gas Protocol (GHG Protocol).[13] Following the GHG Protocol, the proposal uses the concept of "scopes" of emissions "to help delineate those emissions that are directly attributable to the reporting entity and those that are indirectly attributable to the company's activities."[14] Under the proposed rules:

- Scope 1 emissions are direct GHG emissions from operations that are owned or controlled by a registrant;
- Scope 2 emissions are indirect GHG emissions from the generation of purchased or acquired electricity, steam, heat, or cooling that is consumed by operations owned or controlled by a registrant; and
- Scope 3 emissions are all indirect GHG emissions not otherwise included in a registrant's Scope 2 emissions, i.e., emissions which occur upstream and downstream in the value chain.[15]

Upstream emissions include emissions attributable to goods and services that the registrant acquires, the transportation of goods, and employee business travel and commuting. Downstream emissions include the use of the registrant's products, transportation of products (for example, to the registrant's customers), end of life treatment of sold products, and investments made by the

[7] 87 Fed. Reg. 21334.
[8] 15 U.S.C. § 77a et seq.
[9] 15 U.S.C. § 78a et seq.
[10] 87 Fed. Reg. 21334 at 21347.
[11] *Id*.
[12] *Id.*
[13] *Id*. at 21373-21374.
[14] *Id*. at 21344.
[15] *Id.* at 21374.

registrant.[16] Registrants would be required to disclose Scope 3 emissions if "material" or if the registrant set a GHG emissions reduction target or goal that includes its Scope 3 emissions.[17]

The SEC included an IRFA in the proposed climate disclosure rules.[18] In the IRFA, the SEC estimates 1,004 registrants that are small entities would be subject to the proposed amendments.[19] All of these directly regulated small entities are classified by the SEC as small reporting companies (SRCs).[20] As with larger registrants, the proposed amendments would require SRCs to disclose climate-related information when filing registration statements or annual or other periodic reports.[21] SRCs would also be required to report Scopes 1 and 2 emissions.[22] However, SRCs would be exempt from the rules requiring additional disclosure of Scope 3 emissions from upstream and downstream activities in their value chain.[23]

The proposed rules would include a phase-in for all registrants, with the compliance date dependent on the registrant's filer status.[24] Assuming an effective date of December 2022, the rules would require "large accelerated filers" to comply by fiscal year 2023, "accelerated filers" and "non-accelerated filers" to comply by fiscal year 2024, and SRCs to comply by fiscal year 2025.[25] The proposed rules include an additional one-year phase-in period for Scope 3 emissions disclosure and a safe harbor for Scope 3 emissions disclosure.[26]

The exemption from Scope 3 emissions disclosure for SRCs and the longer compliance transition period for SRCs were discussed in the IRFA as accommodations that would reduce the proposed rules' compliance burden for small entities.[27] The IRFA did not discuss other specific alternatives to the proposed rules considered by the SEC but did discuss the suitability of broad categories of alternatives.[28]

II. Advocacy's Small Business Concerns

A. The IRFA Included in the Proposed Rules is Insufficient

Advocacy has two principal concerns with the IRFA in the proposed rules. Under the RFA, an IRFA must contain:

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[16] *Id.*
[17] *Id.* at 21468.
[18] *Id.* at 21462-21463.
[19] *Id.* at 21462.
[20] *Id.*
[21] *Id.*
[22] *Id.* at 21463.
[23] *Id.*
[24] *Id.* at 21346, 21463.
[25] *Id.* at 21411-21412.
[26] *Id.* at 21346.
[27] *Id.* at 21463.
[28] *Id.*

1) A description of the reasons why the regulatory action is being taken.
2) The objectives and legal basis for the proposed regulation.
3) A description and estimated number of regulated small entities.
4) A description and estimate of compliance requirements, including any differential for different categories of small entities.
5) Identification of duplication, overlap, and conflict with other rules and regulations.
6) A description of significant alternatives to the rule.[29]

First, Advocacy is concerned that the IRFA does not adequately describe the regulated small entities and potential impacts on those entities. Second, Advocacy believes the IRFA does not adequately discuss specific alternatives that might reduce the impacts on small entities.

1. The Proposed Rules Do Not Adequately Describe and Estimate Small Entities or Impacts to Those Entities

The IRFA included in the proposed rules does not adequately describe the regulated small entities. The IRFA estimates that the proposed rules would apply to 1,004 small entities.[30] However, it does not provide additional information such as the North American Industry Classification System classifications of the affected entities. Additionally, the IRFA does not break down the affected entities into smaller size groups (e.g., based on total assets). Advocacy recommends that the SEC revise its IRFA and provide such information to better identify and describe the distribution of all regulated small entities.

Furthermore, the IRFA does not adequately analyze the relative impact of costs to small entities. The SEC expects the costs associated with the proposed amendments to be similar for large and small entities.[31] Small entities will need to allocate larger shares of their technological, financial, and staff resources to comply with the proposed rules. Representatives from the biotechnology, plastics, and equipment manufacturing industries have reported to Advocacy that small businesses in their industries have not traditionally tracked GHG emissions or other climate-related metrics. These businesses would either need to develop modeling software to track climate metrics in-house or hire third-party consultants to do so. A representative of the Plastics Industry Association noted that one of their small business members reported spending from 20 to 40 hours compiling information for CDP (formerly the Carbon Disclosure Project), a voluntary climate-related reporting framework.[32]

Additionally, small business representatives have expressed concern that certain financial metrics in the proposed rules would require small companies to report more information than larger companies, despite the difficulty that small companies may have in gathering the necessary information. For instance, the rules on "financial impact metrics" would require registrants to disclose the financial impacts of severe weather events and other climate-related

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[29] 5 U.S.C. § 603.
[30] 87 Fed. Reg. 21334 at 21462.
[31] *Id*.
[32] *See* CDP, *About Us*, https://www.cdp.net/en/info/about-us (last visited June 13, 2022).

risks on their consolidated financial statements unless the aggregated impact of those risks is less than 1% of the total line item for the relevant fiscal year.[33] Although the SEC states that the 1% threshold could "promote comparability and consistency" among different registrants, it is more likely that small companies' risks will exceed the 1% threshold than larger companies which are able to distribute their climate risks.[34] However, small business representatives have expressed concern that they will have difficulty assessing climate risks in the detail required by this metric.

Finally, small business trade representatives have stated that the data, information, and metrics required by the proposed rules are unclear and that the rules do not provide sufficient guidance to reporting companies. There will be additional costs to small entities if they are required to update their systems and processes in response to clarifying guidance from the SEC in the future.

For these reasons, Advocacy recommends that the SEC revise its IRFA using the information described above to analyze costs based on entity size and industry characteristics, including whether the entities are likely capable of tracking the information internally. This would help the SEC to understand the cost burden faced by the smallest regulated entities. In addition, Advocacy recommends that the SEC extend safe harbors found in the regulations to account for the release of future guidance related to the proposed disclosure rules.

2. The Proposed Rules Do Not Adequately Consider Alternatives

Advocacy commends the SEC for its efforts to lower costs of the proposed rules to small entities through measures such as the exemption from Scope 3 emissions disclosure requirements and the longer compliance transition period for SRCs.[35] Nevertheless, the IRFA does not contain a description of any additional regulatory alternatives which accomplish the SEC's stated objectives, and which would further minimize the significant economic impact of the proposal on small entities.

The RFA requires that an IRFA provide significant, feasible alternatives that accomplish an agency's objectives. In this case, the IRFA lists broad categories of potential alternatives to the proposed rules but does not analyze specific alternatives that were considered by the SEC.[36] Instead, the IRFA supplies the SEC's reasoning in rejecting broad categories of potential alternatives. For example, the IRFA states that "[a] key objective of the proposed amendments is to elicit consistent, comparable, and reliable information about climate-related risks across registrants. Alternative compliance requirements for small entities could undermine that goal."[37] Rejecting a category of alternatives because it does not meet the goals of the regulation is not an analysis of a regulatory alternative. Any alternatives considered in the IRFA should be feasible and achieve the objectives of the proposal.

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[33] 87 Fed. Reg. 21334 at 21363-21365.
[34] *Id.* at 21366.
[35] *Id.* at 21463.
[36] *Id.* at 21463.
[37] *Id*.

Advocacy recommends that the SEC revise its IRFA to include alternatives which accomplish its objectives for the rulemaking. Advocacy further encourages the SEC to provide a detailed analysis of each potential alternative and to discuss how that alternative may reduce the economic burden on small entities.

B. The Proposed Rules Do Not Address Foreseeable, Significant Impacts to Small Privately-owned Businesses

Advocacy is concerned that the SEC has not considered the impacts of the proposal to indirectly regulated small entities. The proposed rules appear to require certain public companies to collect Scope 3 emissions data from parties in their value chains.[38] Many of these upstream and downstream parties will be small, privately-owned companies that do not have public reporting requirements. Advocacy has heard from trade representatives and small business owners across industries regarding the proposed Scope 3 disclosure rules. These stakeholders include retailers, home builders, scrap recyclers, and equipment manufacturers, among others. Their concerns shared a common refrain: small businesses are unsure what information they would be expected to provide to public companies, how to collect the necessary information, and whether their businesses would be able to absorb the associated costs.

The owners of small, privately-owned companies have expressed that they do not understand what kind of data they may be required to supply to public companies in their value chains. These businesses are also concerned that they may be required to provide different emissions data to each reporting company that they partner with. Small businesses have already incurred and will continue to incur costs in trying to understand what kinds of data they may be asked to provide to public reporting companies. Providing different data to companies that may have distinct methodologies for calculating emissions would increase the costs of data collection and analysis to small businesses.

Small private companies have also voiced that the costs of collecting and analyzing GHG emissions data could be prohibitive. Because they have not historically been required to report emissions data and generally do not have the capacity to collect it themselves, these companies will likely need to contract with third-party consultants. Multiple small businesses and trade representatives stated that they were unaware of third-party consultants who would be available to perform the services in their respective industries. The lack of consultants currently available to perform these services will likely increase the cost of their services.

Business owners worry that there may be significant impacts if they are not able to provide the emissions data requested by upstream and downstream partners. Financial institutions and other public companies may no longer work with them if they cannot provide data in the time or manner requested. This could potentially lower the value of certain small businesses while others may be forced to cease operations.

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[38] *Id.* at 21374.

Small business owners in the retail fuel industry have expressed concern about the effect the proposed rules would have on their businesses. Sixty percent of retail fuel businesses are owned by single-store operators, while more own 10 or fewer stores.[39] On June 2, 2022, Advocacy met with small operator members of the National Association of Convenience Stores, including 8 small retailers. At that meeting, retail fuel operators stated that single-store and other small operators may have no way of gathering emissions data to provide to the public oil companies that they contract with because they do not have the necessary resources in an industry with small profit margins (2 to 3% of retail sales). These operators worry that the entire industry may shift towards larger operations because the public companies will not want to work with small operators who cannot provide the required information. Other industries expressed similar concerns that their inability to report this information or the high costs they will need to incur (and pass through to the public companies) will make working with smaller companies less appealing and create a market-wide shift toward larger businesses with greater reporting capabilities.

Finally, small businesses have expressed concerns regarding historical GHG emissions disclosure requirements. The proposed rules would not require emissions disclosure for historical fiscal years if the registrant has not been required to and has not previously presented such data, and the historical information necessary to calculate or estimate such metric is not available to the registrant without unreasonable effort or expense.[40] However, the proposal does not outline what the SEC considers to be an "unreasonable effort" or an "unreasonable expense." The lack of guidance on these matters is a concern for small private businesses. Small business owners have told Advocacy that public companies may not wish to purchase a business that cannot provide historical emissions data. If this occurs, it will immediately lower the value of the company in question due to a limited buyer pool.

Based upon the feedback of the small business community, Advocacy recommends that the SEC reconsider the breadth of the Scope 3 emissions requirements. As written, the proposed rules impose indirect reporting requirements that many small businesses will be unable to satisfy. The SEC should clarify the proposed rules to ensure that public reporting companies do not request GHG emissions data directly from small, private entities. Advocacy further recommends that the SEC revise its IRFA to include analysis of impacts to indirectly regulated small businesses, including the relative impact of costs based on entity size. This would help the SEC to understand the total cost of the regulation to small businesses and the broader economy.

III. Conclusion

Advocacy is concerned that the proposed rulemaking and IRFA lack essential information. That information could help inform the SEC's decision making and would supply useful data to small entities that wish to comment on the proposed rules. Advocacy is also concerned that the proposed rulemaking does not analyze foreseeable, widespread impacts to indirectly regulated small entities. We urge the SEC to further analyze the impact of the proposed rules on all impacted small entities and explore additional regulatory alternatives before proceeding to a final

[39] This data was provided to Advocacy by the National Association of Convenience Stores.
[40] 87 Fed. Reg. 21334 at 21362-21363.

rule. This analysis should be published in a supplemental IRFA to provide small entities an opportunity to comment. Additionally, Advocacy recommends that the SEC reconsider the breadth of its Scope 3 emissions disclosure to ease the burden of the proposed rules on small, private businesses. We are available to assist the SEC in its outreach to small entities and in its consideration of the impact upon them.

If you have any questions or require additional information, please contact me or Assistant Chief Counsel Meagan Singer at (202) 921-4843 or by email at meagan.singer@sba.gov.

Sincerely,

/s/
Major L. Clark, III
Deputy Chief Counsel
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/s/
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Copy to: Dominic Mancini, Deputy Administrator
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