Securities Law Tackles Impact of a Changing Climate on Bottom Line

Bethany A. Davis Noll is executive director at NYU Law's State Energy & Environmental Impact Center: bethany.davisnoll@nyu.edu.

With its recent climate risk rule, the Securities and Exchange Commission has begun to create a regime where investors will receive reliable disclosures about climate problems that they can compare across companies. This is something that has been needed for quite some time, as many companies have trumpeted their emissions reduction pledges, with very little holding them accountable to implement plans to meet those reductions. The new rule faces a slew of lawsuits. Despite the SEC's contention it is on solid ground, with the focus on material risks and a robust supporting analysis, the commission temporarily halted the rule as this issue went to press.

The SEC finalized the rule in early March. It requires public companies to make disclosures about their material climate-related risks. It also requires them to disclose material greenhouse gas emissions associated with operations that the company owns or controls (known as "scope 1" emissions) as well as the emissions associated with the energy it consumes (known as "scope 2"). These emissions are often considered material because they might relate to the company's exposure to changing regulations targeted at those emissions (known as "transition risk"), and they could be relevant to the company's own progress toward meeting their public emissions-reduction goals.

The rule faces suits, but SEC is on solid ground with focus on material risks

Trade associations, states, and the U.S. Chamber of Commerce have all filed lawsuits challenging the rule as unlawful. The many petitioners still need to lay out their arguments, but their comments on the proposed rule provide a good indication of what their lawsuits are about: they have argued that the agency is stepping outside of its statutory authority to finalize a rule related to climate, that these disclosures violate the First Amendment, and that the case fails to pass muster under the "major questions doctrine" adopted by the Court recently in *West Virginia v. EPA.* On the other side, Earthjustice and the Natural Resources Defense Council have also challenged the agency's decision not to include even more emissions in the disclosure requirements.

Petitioners filed their challenges across six different courts of appeal. All the cases are now consolidated in the Eighth Circuit, by operation of a randomized lottery. The Eighth Circuit has only one Democratic-appointed judge.

The SEC has faced a few other challenges recently to other rules, and the decisions in those cases may become relevant to the new climate risk case. For example, in a recent case in the Fifth Circuit, decided by a panel with a majority of Republican-appointed judges, the court addressed a rule that requires companies to disclose more information about their decisions to repurchase stocks.

Companies sometimes do that to increase the value of shares, but they sometimes do it for reasons that are less good and more about boosting executive compensation. The agency thinks that investors need to know more about company motivations in order to be able to assess the firm's financial health. In that case, the court held that the SEC's rule did not violate the First Amendment—likely a helpful persuasive precedent for the new climate risk case. But the court ultimately vacated the rule for failure to "substantiate the rule's benefits and costs" through a "proper cost-benefit analysis," which the court held should have included an analysis of data that petitioners had offered. It is yet to be seen how much the cost-benefit analysis will factor into petitioners' challenges of the climate risk rule.

In another case also in the Fifth Circuit, the SEC prevailed in a challenge to a rule about how much information companies should disclose about their boards; the court also rejected a major questions doctrine argument against the rule. But that decision did not remain on the books for long. It was issued by the usual panel of three judges, chosen at random and all by happenstance appointed by Democratic presidents. Recently, the full Fifth Circuit vacated that panel decision and announced that it would hear the case again en banc. Republican presidents appointed the majority of the judges on that court.

Recently, the New York attorney general sued a meat conglomerate for misleading investors in its claims that it would be emitting zero greenhouse gas emissions by 2040, on net. As the case alleges, the company actually has no plan for reaching that goal but instead has plans to increase beef production—which will cause it to emit even more greenhouse gases, not less. In an environment where companies are greenwashing in this way about their plans for emissions cuts, more clarity about those claims would certainly seem beneficial. So it will be interesting to see how challenges to the SEC's new rule play out in court.