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Twenty-Two Professors[1]*

The following article adapts and consolidates two comment letters submitted last spring by a group of twenty-two professors of finance and law on the SEC's proposed climate change disclosure rules. The professors reiterate their recommendation that the SEC withdraw its proposal as legally misguided, while outlining some of the issues that the proposal will face when challenged in court.

The enthusiasm of many Commissioners and Staff of the Securities and Exchange Commission (the SEC) to participate in the global debate about climate change is understandable. After all, protecting the earth's sustainability is perhaps the most compelling issue of our time. It's an issue all must take seriously and everyone must do their part. But each of us, and particularly governmental authorities, must always act in accordance with law and fairness.

A group of 22 professors of law and finance (the "Twenty-Two Professors") are concerned that the SEC's recent proposal to impose extensive mandatory climate-related disclosure rules on public companies (the "Proposal") exceeds the SEC's authority. In addition, rather than provide "investor protection," the Proposal seems to be heavily influenced by a small but powerful cohort of environmental activists and institutional investors, mostly index funds and asset managers, promoting climate consciousness as part of their business models.

The Twenty-Two Professors submitted a comment letter dated April 25, 2022, detailing their principal concerns,[2] starting with the question of the SEC's authority, which are a function of federal statutes and other federal laws.[3] The analysis raised concerns that the Proposal is neither necessary nor appropriate for either investor protection or the public interest. The letter recommended that the SEC withdraw the Proposal and revisit the subject with a fresh approach focused on the interests of all investors rather than an elite global subset.

In June 2022, two other comment letters from other professors joined the issue, one from a group of thirty law professors (the "Thirty Professors' Letter")[4] and another by Professor John Coates (the "Coates Letter").[5] Because those letters reflected sharply divergent understandings of the nature and factual background of the Proposal compared to that presented in our letter, the Twenty-Two Professors submitted a response to them dated June 17, 2022.[6] As the SEC has given no indication that it is considering withdrawing the Proposal as we recommended, we believe that an eventual legal challenge is forthcoming and that the divergent understandings will influence the course of that litigation.

Areas of Agreement

We agree with the Thirty Professors' Letter and the Coates Letter that the SEC has broad statutory authority to require disclosures for the protection of investors. We further agree that the relevant inquiry is whether a proposed disclosure requirement will protect investors, not whether it is material, although the two inquiries will generally overlap.[7] Finally, we agree that the relevance of a disclosure requirement to a social issue or to non-shareholder constituents does not demonstrate, in and of itself, that it exceeds the SEC's authority.

Indeed, the two letters make a strong case that the SEC's 2010 guidance regarding climate change disclosures (the "2010 Guidance") was a valid exercise of the SEC's statutory authority.[8] The 2010 Guidance reminded issuers that several elements of the existing disclosure framework, including disclosure of the material effects of compliance with laws and regulations,[9] material pending legal proceedings,[10] and material risk factors,[11] may require disclosures relating to climate change.

Coates Framework Affirms Proposal's Invalidity

An analysis of the SEC's authority to adopt the Proposal must grapple with the substantial differences between it and the 2010 Guidance. Here we find helpful a framework set out in the Coates Letter, which distinguishes disclosures about the impact of climate on a company with disclosures about the impact of a company on the climate.[12] This is a simple rubric for separating disclosures focused on investor protection from those focused on social goals.

The Proposal manifestly requires the second type of disclosure. A core element of the Proposal, one highlighted in the SEC's Fact Sheet accompanying the Proposal, is a disclosure of greenhouse gas (GHG) emissions.[13] This is a quintessential measure of a company's contribution to climate change. It is not a measure of the impact of climate change on the company.

The extent of a company's GHG emissions would be directly relevant to the costs of a company's operations had Congress enacted a tax on such emissions. It has not. It would be relevant to a company's costs had Congress created a cap-and-trade system for such emissions. It has not. It would be relevant to a company's costs had Congress adopted binding nationwide GHG targets and an enforcement mechanism to achieve them. It has not. The GHG emissions disclosures, in the context of existing US law, would require information about the company's impact on the environment, but not vice versa.[14]

We also note that the lack of a materiality qualification for some of the proposed disclosures is relevant to whether these disclosures serve the interests of investors as opposed to other stakeholders. While data about immaterial Scope 1 or Scope 2 emissions might be useful to non-shareholder constituencies, it is more difficult to see how it will be useful to investors.

Not "Business as Usual" or "Disclosure Only"

Both the Thirty Professors' Letter and the Coates Letter also argue that concerns about SEC overreach are misplaced because the Proposal requires only disclosures. As the Coates Letter expresses this point, the Proposal will not cap emissions, impose a cap-and-trade system, or force any company to shut down GHG-emitting factories.[15] The Thirty Professors' Letter notes that the Proposal does not require "particular governance structures to oversee climate risk, … carbon goals, [or] … a climate transition plan."[16]

All true. Nevertheless, the clear purpose (and certain effect) of these disclosures is to give third parties information for use in their campaigns to reduce corporate emissions, regardless of the effect on investors. The SEC itself discusses the efforts of non-profit climate change advocacy organizations as part of the background for the Proposal.[17] As detailed further later this in this article, those organizations aim to prevent or alleviate climate change, not to protect investors.[18] They use disclosures about transition plans, scenario analyses, internal carbon prices, and climate-related targets and goals to identify companies that aren't doing enough, in their opinion, to combat climate change. They then pressure those companies to change their operations in ways not required by existing US environmental laws while pressuring institutional investors to support such changes.

Imposing substantial costs on some companies to prepare for a "potential transition to a lower carbon economy"[19] that Congress has not and may never mandate will harm investors who prioritize financial returns over social goals. To be sure, the Proposal only facilitates, rather than requires, this result. As Commissioner Peirce's dissenting statement put it, the Proposal will put the SEC's weight behind "an array of non-investor stakeholders" demanding changes in company operations.[20]

We believe, however, that the SEC and the courts can and should consider predictable consequences when deciding whether the Proposal will protect investors and whether it involves a "major question" that Congress should decide. Supporting the view that the proposed disclosure is not "business as usual" and is not focused on protecting investors, there is no substantial evidence suggesting causation between climate practices and superior economic performance, nor that ESG investing outperforms conventional investing.[21]

Only by ignoring the long and contentious history of debates over the appropriate policy response to climate change could one conclude that the Proposal is a mere "business as usual" tweak to the disclosure system.[22] We also note that investors are ill-served by rules whose costs exceed their benefits. If disclosure were free, the SEC could require disclosure of all possible risks, regardless of magnitude or probability. The SEC does not do so because it is too costly and difficult to assess all possible risks a company faces. Climate risk is especially hard to assess, creating a real danger that the

Proposal's new disclosures will impose costs (including litigation costs) greater than their benefits to investors.

Asset Pricing

We agree with the Thirty Professors' Letter and the Coates Letter on the importance of information to the market pricing of risk but disagree about the likelihood that the specific disclosures called for by the Proposal will contribute meaningfully to the market's ability to value companies. The Coates Letter cites studies showing that prices currently reflect climate risks only imperfectly.[23] The Thirty Professors' Letter asserts that "climate-related matters impact the most important aspect of any securities transaction—the price at which investors buy or sell."[24]

We are unaware of evidence that there are persistent climate-related pricing anomalies (profitable trading opportunities) under the current disclosure system that additional disclosure would eliminate. Indeed, given the enormous quantity of existing mandated and voluntary disclosure about climate risk, it would be surprising to discover significant mis-pricings that the new disclosures could correct.[25]

Put another way, it is generally accepted that all material information is incorporated into stock prices, but that does not imply that all climate information affects stock prices. Only material climate information not already available to the market will affect stock prices. The fact that empirical research has not been able to find a relation should give the SEC pause, since a possible reason is that much climate information is not material.

Individual Investor Demand

We do not read the Thirty Professors' Letter or the Coates Letter as taking issue with a central concern of our April 25 letter—that the publicly expressed views of the executives of large asset managers and climate-focused organizations may not represent the best interests of retail investors, including individual direct owners, mutual fund investors, and beneficiaries of pension plans.[26] Because we draw a sharper distinction between institutional investor demand and investor protection, however, we believe the SEC should put more effort into determining whether retail investors would benefit from additional climate-related disclosures before proceeding further.

We criticized the Proposal for mentioning individual investors only once, in passing. The Coates Letter counters that the Proposal cites letters from some individual investors.[27] The Coates Letter also mentions a survey conducted by an institutional investor claiming that individuals prioritize climate information.[28] Finally, it argues that "critics have offered no robust evidence of their own showing that individual investors generally oppose disclosure about climate-related risks."[29]

The SEC, however, should both take account of the evidence that exists and fill in the gaps in the administrative record. It is well-known that institutional investors vote for environmental shareholder proposals at about twice the rate of individual investors.[30] Recent empirical research, moreover, indicates that less than 2 percent of mutual fund money is invested in ESG funds.[31]

There are also two relevant surveys of individual investors conducted by non-partisan institutions shortly before the Proposal was issued. The first is a survey of 1,228 retail investors conducted by NORC at the University of Chicago, an independent, non-partisan research institution, and the FINRA Investor Education Foundation. It found that individual investors prioritize return on investment and other financial factors in their investment decisionmaking more than any other factor.[32] Individual investors identified environmental aspects of a potential investment as the *least important consideration* compared to financial, governance, and social factors.[33] The second is a Gallup poll of 953 US adult individual investors finding that most prioritized the expected rate of return and risk for potential losses over environmental and other issues.[34]

By contrast, Public Citizen, a consumer advocacy group, recently conducted its own poll, apparently in response to and in support of the Proposal, finding substantial individual investor demand for climate-related information.[35] Other commentators have criticized the methodology and phrasing of the Public Citizen poll's questions as biased and failing to reflect the specific rules contemplated by the Proposal. In particular, the questions asked whether investors would want this information if it were *free*—ignoring the substantial costs the Proposal estimates will be incurred.[36]

We note, moreover, that it is the SEC, and not commentators, that bears the burden of demonstrating that a proposed rule promotes efficiency, competition, and capital formation as required by its organic statutes.[37] If the SEC has chosen to put forth meeting investor demand as a rationale for the Proposal, it is reasonable to expect it to have evidence indicating such demand emanating from the large base of individual investors. While we appreciate that generating requisite quantitative data can be difficult, evidence-based rulemaking remains both desirable and feasible.[38]

Institutional Asset Manager Demand

It is simply a fact that large index fund managers have less to lose than their investors should the managers' environmentally motivated votes and engagement reduce the return on publicly traded equities as an asset class. There is also substantial evidence that these managers believe that cultivating an ESG-friendly image is privately beneficial. We therefore believe that it is essential that the SEC do more work to determine whether the specific disclosures called for in the Proposal would benefit retail investors.

The investors demanding climate-related information are overwhelmingly institutional asset managers who are managing other people's money, not their own. This raises an obvious question: whether their advocacy is prompted by concern for their beneficiaries' returns or their own profitability. Two of the SEC's recent major rulemaking proposals relating to private fund advisors each contain dozens of references to potential conflicts of interest between private advisors and their sophisticated clients.[39] Yet this Proposal makes not a single reference to potential conflicts of interest between retail asset managers and their less-sophisticated clients, instead taking it as given that what is good for the asset manager is good for the beneficiary.

To determine whether adopting the Proposal will protect investors, the SEC must explicitly consider the conflicts that arise between large asset managers and their beneficiaries and whether climate disclosure mandates will exacerbate them.[40] There is no indication that the SEC has attempted to assess, much less quantify, the potential losses to individual investors from self-interested voting or engagement by the asset managers to whom 160 million Americans entrust their savings. That fact alone is a fatal flaw of the Proposal.

Special Interest Group Demand

The Proposal refers to "investor demand" 54 times, with copious citations tied to one segment of the investment industry. The Proposal devotes five pages to introduce what it calls "growing investor demand," mainly by listing six consortia of large global institutions along with reported assets under management.[41] The list starts with three groups of such institutions that have signed the United Nations' policy advocacy documents urging countries to reduce climate risks.

The United Nations is neither a business nor an investor and lacks any relevant expertise in either domain. It is a political institution coordinating international policies on contentious topics, including as an incubator of the concept of "ESG" and climate management that provide the backdrop for the Proposal.[42] The other three groups are avowed climate activists, reflected in their names: Net Zero Asset Managers Initiative, Climate Action 100+ and Glasgow Financial Alliance for Net Zero. The Proposal does not identify these investors nor indicate the portion of the reported assets invested in SEC registrants as compared to other investments around the world.

The Proposal's citations skew heavily toward organizations that are prominent environmentalists, not prominent investors. The following are the seven organizations the Proposal cites most frequently (each cited in 14 to 28 different footnotes):

MOST CITED OVERALL	Footnotes
Environmental Protection Agency (EPA)	28
Carbon Disclosure Project (CDP)	27
Natural Resources Defense Council	22
American Institute of Certified Public Accountants (AICPA)	22
Coalition for Environmentally Responsible EconomieS (CERES)	21
Sustainability Accounting Standards Board (SASB)	19
United Nations Principles for Responsible Investment Corp. (PRI)	14

The investors the Proposal cites most frequently skew toward those focused on social and political investing and many are non-US entities. Of the seven investors the Proposal relies upon most, four are non-US entities, organized in Canada, England, France, and Scotland.

The following are the seven investors the Proposal cites most frequently (each cited in 9 to 14 different footnotes):

MOST CITED INVESTORS	Footnotes
New York State Comptroller	14
BNP Paribas (French)	12
BlackRock	11
Impax Asset Management (English)	9
Baillie Gifford (Scottish)	9
Trillium: Socially Responsible Investing	9
Northwest & Ethical Investments (NEI) (Canadian)	9

Of the 36 other organizations the Proposal cites heavily (at least 5 footnotes), 12 are climate advocacy groups.

OTHER MOST CITED	Footnotes
Climate Governance Initiative	12
Interfaith Center on Corporate Responsibility	9
Carbon Tracker Initiative	8
Regenerative Crisis Response Committee	7
Friends of the Earth	7
Amazon Watch	6
Partnership for Carbon Accounting Financials (PCAF)	5
As You Sow	5
Center for Climate and Energy Solutions	5
Institute for Governance and Sustainable Development	5
World Benchmarking Alliance	5
World Resources Institute	5

Despite the sweeping phrase "investor demand," the Proposal never discloses any meaningful information about the investors it has in mind. For instance, it does not disclose the proportion of their assets under management invested in SEC registrants that are actively managed versus passively managed. It does not delineate important matters of investment style, particularly whether these investors follow traditional fundamental valuation analysis, conventional diversification based on modern portfolio theory, or fashionable indexing based on rankings of companies according to their climate-related practices. It does not disclose which of these investors invest for their own account or on behalf of clients or the breakdown of such clients between institutions or individuals.

Such investor demographics and styles are essential predicates to determining whether there is a need for rulemaking along the lines stated in the Proposal.[43] Such an understanding of which institutions are expressing such demand is particularly important for SEC disclosure regulations because these investor types demand different kinds of information and utilize it differently.[44] For instance, traditional index funds do not select stocks by parsing SEC disclosure but rather formulaically buy and sell based on fluctuations in an index, without regard to such disclosure.[45] Traditional stock pickers scrutinize such information carefully to ascertain business value, economic advantages, and investment trajectory.[46]

BlackRock, State Street, and other large index fund providers face a challenging competitive environment. Fees for index funds have been driven nearly to zero. Profitability therefore depends on spreading the managers' fixed costs over a larger pool of managed assets. In attempting to attract investment inflows, large index funds compete against one another and with active managers. The latter has a built-in advantage in attracting socially conscious investors because they can offer non-indexed products specifically catering to ESG-focused investors.

For the manager of an index fund that must invest in all or substantially all companies in the index, public statements that climate is a top priority across the entire portfolio can be an important competitive marketing tool. A recent academic article makes the point cogently: "With fee competition exhausted and returns irrelevant for index investors, signaling a commitment to social issues is one of the few dimensions on which index funds can differentiate themselves and avoid commoditization."[47]

While index funds may be interested in using climate-friendly voting and engagement as a marketing device, they cannot afford to incur substantial new costs to do so. A mandatory climate disclosure regime requiring publicly traded companies to bear the cost of producing and standardizing the climate-related information would save such funds costs while advancing their agendas.

The Proposal creates an obvious conflict: the Proposal provides a special financial benefit to ESG funds, by reducing their costs for identifying ESG investments. As most investors are not in those funds, that indicates that the SEC's Proposal would impose a disproportionate bearing of the costs on them. Yet the SEC never considers how the Proposal would affect different segments of the investment industry differently. Equally defective, it also fails to consider alternative approaches that would avoid favoring some sectors at the expense of others.[48]

Another subgroup of investors the Proposal unfairly favors are those who, unlike traditional investors, are not focused on the economic gain from their investments. For instance, the boards of public employee pension funds, such as CalPERS, include government appointees and elected officials, all of whom respond to politics, including the politics of climate change.[49] Less overtly, the Proposal benefits fund managers promoting goals other than investor protection, such as the pension funds of the AFL-CIO, which advocate shareholder proposals pushing a labor agenda.[50]

Another powerful force in certain segments of the investment industry is proxy advisors, such as Institutional Shareholder Services (ISS). These organizations invest heavily in non-financial products such as climate ratings. For instance, ISS's ESG ratings unit assigns sustainability ratings to companies. Then ISS's Corporate Solutions unit turns around and sells a separate set of services to those companies to improve their ratings. Pushing companies to disclose more and more of the information contemplated by the Proposal, and to reset behavioral baselines around such services, may well be good for ISS's business. But the SEC's assessment of "investor demand" should adjust for these powerful forces.

The Proposal makes much of the assertion that large institutional money managers say that climate policy is the number one thing they like to discuss with companies during their engagements with them.[51] In doing so, the Proposal overlooks two critical features of such shareholder engagement.

First, the practice of shareholder engagement is relatively new and is evolving.[52] At present, most institutional investors continue to prioritize engagement with those companies and on those topics of special interest for particular reasons, not recurring matters of business life. If they are prioritizing climate, that may not reflect pervasive investor demand as much as it does specific issues at certain companies or specific priorities for certain investors and their business models.

Second, the SEC overlooks that while institutional investors may have the power and influence to get engagement meetings with companies, individual investors do not. Individual investors must be content with annual shareholder meetings and periodic investor Q&As. To elevate the priorities and practices of such privileged institutions over those of individual shareholders is perverse for an agency whose historical raison-d'etre and current website emphasize protecting individual investors.[53]

Major Question of Public Interest

In theory, the SEC could claim the authority to promulgate the Proposal under the "public interest" prong of its statutory power. Weak as the grounding in investor protection is, however, a public interest rationale is even more problematic.

Climate change is perhaps the most important public policy question of our time, as the SEC's leadership's repeated assertions attest.[54] Commissioners and other officials have stressed in speeches and other forums that climate poses enormous economic and political consequences. The large and diverse number of comment letters submitted on the Proposal illustrates this fact.[55] Congress is aware of these and has long been active on the topic.[56] Congress has passed important legislation in this area, most dramatically the Clean Air Act of 1974, which expressly delegates climate disclosure regulation, particularly greenhouse gas emissions, to the Environmental Protection Agency (EPA). The EPA exercises that authority through its Greenhouse Gas Reporting Program, which currently measures and reports on almost all such emissions in the United States from all sources. A general principle of federal law holds that more recent and specific laws addressing a subject matter supersede earlier and more general laws on that subject.

Accordingly, the EPA's empowerment over this topic probably preempts any statutory authority the SEC might claim. For another apt analogy, the SEC should consider the landmark Supreme Court ruling that the

ERISA statute, under the jurisdiction of the Department of Labor, abrogates the jurisdiction of the federal securities laws and the SEC's regulation.[57]

Concerning major questions such as climate change, moreover, federal law also recognizes that Congress can be expected to speak explicitly, thereby narrowing the scope for inferences of authority such as the SEC necessarily relies upon. Indeed, this was the rationale for the Supreme Court's recent repudiation of an agency rule imposing national COVID vaccination requirements[58] and EPA's overzealous environmental regulations.[59] In each case, Congress had not clearly authorized the agency to do so as is expected concerning matters of "vast economic and political significance."

The SEC should take heed of such Supreme Court guidance. Since the latter case was handed down after the Proposal was released, it is difficult to fathom how the SEC has not rethought its position in light of it.

Conclusion

In sum, the Proposal is within the SEC's authority only if it will protect investors, as opposed to society, the environment, or other potentially worthy third parties. The SEC bases its affirmative conclusion on the advocacy of large institutional asset managers, government agencies, and non-governmental organizations seeking more climate-related information. These arguments remain unpersuasive. The SEC would better serve its constituents by starting over.[60]

Notes

1. Stephen M. Bainbridge (UCLA), Jonathan B. Berk (Stanford), Sanjai Bhagat (Colorado), Bernard S. Black (Northwestern), William J. Carney (Emory), Lawrence A. Cunningham (GW) (corresponding author), David J. Denis (Pittsburgh), Diane Denis (Pittsburgh), Charles M. Elson (Delaware), Jesse M. Fried (Harvard), Sean J. Griffith (Fordham), Jonathan M. Karpoff (Washington), F. Scott Kieff (GW), Edmund W. Kitch (Virginia), Katherine Litvak (Northwestern), Julia D. Mahoney (Virginia), Paul G. Mahoney (Virginia), Adam C. Pritchard (Michigan), Dale A. Oesterle (Ohio State), Roberta Romano (Yale), Christina P. Skinner (Pennsylvania), Todd J. Zywicki (George Mason).
2. Letter to SEC from Twenty-Two Law and Finance Professors (corresponding author Lawrence A. Cunningham) (April 25, 2022), *https://www.sec.gov/comments/s7-10-22/s71022-20126528-287180.pdf*.
3. The statutes that created the SEC in the 1930s authorize the SEC to promulgate disclosure regulations that are "necessary or appropriate in the public interest or for the protection of investors." Securities Act Sections 7, 10, 19(a); Exchange Act, Sections 3(b), 12, 13, 14, 15(d), and 23(a). Amendments to those statutes in the late 1990s instructed the SEC to report on whether a proposed regulation will promote efficiency, competition, and capital formation. Securities Act §2(b); Exchange Act §23(a)(2); *see American Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166 (D.C. Cir. 2010).
4. Letter to SEC from Thirty Law Professors (on letterhead of Jill E. Fisch & George S. Georgiev) (June 6, 2022).
5. Letter to SEC from John Coates (June 2, 2022).
6. Letter to SEC from Twenty-Two Law and Finance Professors (corresponding author Lawrence A. Cunningham) (June 17, 2022), *https://www.sec.gov/comments/s7-10-22/s71022-20132133-302619.pdf*.
7. The SEC is required to consider whether a proposed rule "will promote efficiency, competition, and capital formation" in addition to, and not in substitution for, investor protection. Securities Act §2(b), Exchange Act §3(f).
8. SEC, Commission Guidance Regarding Disclosure Related to Climate Change (February 2010).
9. Regulation S-K, Item 101(c)(2)(i).
10. Id. Item 103.
11. Id. Item 105
12. Coates Letter at p.2 ("The focus of the [Proposal] is the impact *of climate change on companies, and not vice versa*") (emphasis in original).
13. See Proposed Item 1504 of Regulation S-K, Proposal at pp.484–490.
14. We recognize that other countries in which a registrant operates may have adopted more stringent climate-related regulations than the United States. We see nothing in the Proposal that limits the scope of the required disclosure to information regarding the registrant's compliance with the laws of the countries in which it does business and the associated costs. Such a limitation would bring the Proposal more closely into line with the SEC's usual approach to compliance-related disclosures.
15. Coates Letter at p.11.
16. Thirty Professors' Letter at p.3.
17. Proposal at pp.29–31.
18. Besides the EPA, the most-cited entity in the Proposal is the Carbon Disclosure Project (see charts below). Its website declares that the organization's purpose is "to act urgently to prevent dangerous climate change and environmental damage."
19. Proposed Rule 14-02(h) of Regulation S-X, Proposal at p.471.
20. Commissioner Hester M. Peirce, *We are Not the Securities and Environment Commission—At Least Not Yet* (March 21, 2022).
21. *See* Jitendra Aswani et al., Are Carbon Emissions Associated With Stock Returns? (manuscript 2022) (documenting the *lack* of a relationship between carbon emissions of companies and their stock returns, and company carbon emissions and company operating performance), *https://papers.ssrn.com/abstract_id=3800193*; Ulrich Atz et al., Does Sustainability Generate Better Financial Performance? Review, Meta-Analysis and Propositions (2022), available at: *https://ssrn.com/abstract=3708495* (meta-analysis of studies indicating ESG investing does not outperform non-ESG investing.).
22. *See* Coates Letter at p.1 (characterizing the Proposal as "not a 'transformative' surprising regulatory departure" that "would

have modest effects on the economy"); Thirty Law Professors Letter at p.4 ("The Proposal's requirements are thus properly understood as core capital markets disclosure"). In contrast, a law firm analysis referred to the Proposal as "the most far-reaching company disclosure *and governance* mandate to be introduced in decades" (emphasis added). See Joseph A Hall, Margaret E. Tahyar & Ning Chiu, SEC Proposes Climate Disclosure Regime, Harvard Law School Forum on Corporate Governance (April 9, 2022), *https://corpgov.law.harvard.edu/2022/04/09/sec-proposes-climate-disclosure-regime* (Davis Polk & Wardwell LLP).

23. Coates Letter at p.16.
24. Thirty Professors' Letter at p.3.
25. See Jitendra Aswani et al., Are Carbon Emissions Associated With Stock Returns? (manuscript 2022) *https://papers.ssrn.com/abstract_id=3800193*.
26. *https://www.sec.gov/comments/s7-10-22/s71022-20126528-287180.pdf*.
27. Coates Letter at p.15 (referring to the Proposal at p.18 and ns.154 and 412).
28. Coates Letter at n.60.
29. Coates Letter at n.58.
30. *See, e.g.,* PwC/Broadridge, Proxy Pulse: 2022 Proxy Season Preview 8 (February 2022) ("institutional investors were more than twice as likely as retail investors to support environmental and social proposals. Only 18 percent of votes by retail shareholders were cast in favor of environmental and social proposals.").
31. Jonathan Berk and Jules H. Van Binsbergen, The Impact of Impact Investing (June 10, 2022), available at *https://papers.ssrn.com/abstract_id=3909166*.
32. FINRA Investor Education Foundation & NORC at the University of Chicago, Investors say they can change the world, if they only knew how: Six things to know about ESG and retail investors (March 2022).
33. Id.
34. *See* Gallup, Where US Investors Stand on ESG Investing (February 23, 2022).
35. Public Citizen, Survey Reveals Retail Investors Want SEC to Require Climate Disclosure (April 29, 2022); Public Citizen, Results of a Nationwide Survey: Retail Investors' Support for the SEC Mandating Climate-Related Financial Disclosures from Public Companies (April 28, 2022).
36. The Society for Corporate Governance submitted a comment letter on the Proposal that details the shortcomings of the Public Citizen poll. *https://www.sec.gov/comments/s7-10-22/s71022-20132044-302525.pdf*
37. *See e.g., Timpinaro v. SEC*, 2 F.3d 453, 455 (D.C. Cir. 1993) (remanding for further cost-benefit analysis); US Chamber of Commerce v. SEC, 412 F.3d 133 (D.C. Cir. 2005) (same); *US Chamber of Commerce v. SEC*, 443 F.3d 890, 893-94, 909 (D.C. Cir. 2006) (vacating rule on those grounds); American Equity Investment Life Insurance Co. v. SEC, 613 F.3d 166, 168 (D.C. Cir. 2010) (vacating a rule because the SEC "failed to properly consider the effect of the rule upon efficiency, competition, and capital formation"); *Business Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011) (vacating a rule because, among other things, the SEC "inconsistently and opportunistically framed the costs and benefits of the rule … and failed to respond to substantial problems raised by commenters").
38. See John C. Coates IV, Cost-Benefit Analysis of Financial Regulation: Case Studies and Implications, 124 Yale L. J. 882, at pp.892–893 (2015); see also Bruce Kraus & Connor Raso, Rational Boundaries for SEC Cost-Benefit Analysis, 30 Yale J. Regul. 289, at pp.298–99 (2013); Richard L. Revesz, Cost-Benefit Analysis and the Structure of the Administrative State: The Case of Financial Services Regulation, 34 Yale J. Regul. 545, at pp.565–570 (2017).
39. SEC, Release No. IA-5950; File No. S7-01-22, *https://www.sec.gov/rules/proposed/2022/ia-5950.pdf* and SEC, Release Nos. IA-5955; File No. S7-03-22, *https://www.sec.gov/rules/proposed/2022/ia-5955.pdf*.
40. *See* Paul G. Mahoney and Julia D. Mahoney, The New Separation of Ownership and Control: Institutional Investors and ESG, 2021 Columbia Bus. Law Rev. 840.
41. Proposal, pp.25–29 (repeated at pp.332–333).
42. ESG refers to "environmental, social and governance" principles that the United Nations believes should guide all management and investment decisions worldwide. *See* U.N. Principles for Responsible Investment, *https://www.unpri.org*.
43. See SEC Office of Inspector General, Follow-Up Review of Cost-Benefit Analyses in Selected SEC Dodd-Frank Act Rulemakings, Report No. 499 (January 27, 2012) at 31–36.
44. *E.g.*, Amir Amel-Zadeh & George Serafeim, Why and How Investors Use ESG Information: Evidence from a Global Survey, 74 Financial Anal. J. 87 (2018).
45. *See* John C. Bogle, *The Little Book of Common-Sense Investing: The Only Way to Guarantee Your Fair Share of Stock Market Returns* (2017); Burton G. Malkiel, *A Random Walk Down Wall Street* (12th ed. 2019).
46. See Benjamin Graham & Jason Zweig, *The Intelligent Investor: The Definitive Book on Value Investing* (rev. ed. 2009); Warren E. Buffett & Lawrence A. Cunningham, *The Essays of Warren Buffett: Lessons for Corporate America* (5th ed. 2019).
47. Michal Barzuza, Quinn Curtis & David H. Webber, Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance, 93 USC L. Rev. 1243, 1244 (2020).
48. *See Business Roundtable v. SEC*, 647 F.3d 1144, 1150 (D.C. Cir. 2011).
49. *See* David Webber, *The Rise of the Working-Class Shareholder: Labor's Last Best Weapon* (2018).
50. *See* Ashwini K. Agrawal, Corporate Governance Objectives of Labor Union Shareholders: Evidence from Proxy Voting, 25 Rev. Finan. Stud. 187 (2012).
51. Proposal, pp.330–331 (citing survey of 42 large institutions managing $29 trillion in assets indicating that climate risk is "the number one investor engagement priority" or the "leading issue driving their engagement with companies").
52. *See* Shareholder Engagement: An Evolving Landscape, Drexel University *https://www.lebow.drexel.edu/news/shareholder-engagement-evolving-landscape*.
53. See Lawrence A. Cunningham, SEC's Climate Change Proposal Gives Main Street Investors No Voice: Here's How to Make Yourself Heard, *MarketWatch* (April 9, 2022).
54. See Joseph P. Grundfest, *The SEC is Heading Toward a Climate Train Wreck*, Bloomberg (April 5, 2022).

55. See Lawrence A. Cunningham, What the Volume and Diversity of Comment Letters to the SEC Say About its Climate Proposal (July 3, 2022), *https://corpgov.law.harvard.edu/2022/07/03/*; Ropes & Gray, The SEC's Proposed Climate Disclosure Rules (Comment Letter Stats) (August 1, 2022), *https://www.ropesgray.com/-/media/Files/alerts/2022/08/20220802_ESG_Alert.pdf*.
56. As an indicator of that awareness, as well as a measure of the highly political nature of the Proposal, it prompted letters from 19 Senators and 40 House Members challenging the SEC's power and urging it to withdraw the Proposal.
57. *International Brotherhood of Teamsters v. Daniel*, 439 U.S. 551 (1979).
58. See *National Federation of Independent Business v. Department of Labor*, 595 U.S. ___ (2022).
59. *West Virginia v. Environmental Protection Agency*, 597 U.S. ___ (2022).
60. Our April 25 letter identified other shortcomings of the Proposal, including as to shareholder proposals, the supply of climate disclosure, the relevance of the EPA's statutory jurisdiction, the risk of encroachment on state corporate law prerogatives, the risk of violation of the First Amendment, the certain high costs versus highly speculative benefits, the impairment of investment industry competition and how compliance burdens discourage public company registrations. We continue to believe that these objections are important and provide additional reasons for the SEC to withdraw the Proposal.

THE MONITOR

The Monitor is an agenda of matters of interest to the financial services industry. The Monitor includes: (1) regulatory and related matters on which comment periods are open; (2) important regulatory initiatives that are still pending and under active consideration; (3) recent regulatory matters of continued urgency to the financial services community; and (4) cases pending before the US Supreme Court and other federal and state courts. All cases are listed by subject. Unless otherwise noted, this issue of The Monitor covers developments during the period August 20, 2022, through September 20, 2022.

BANK REGULATION

Bureau's Interpretive Rule Addresses Digital Marketing

An interpretive rule issued by the Consumer Financial Protection Bureau explains when digital marketing providers for financial firms must comply with federal consumer protection law. According to the rule, digital marketers involved in the identification or selection of prospective customers or the selection or placement of content to affect consumer behavior are service providers under the law and may be held liable by the CFPB or other law enforcers for unfair, deceptive, or abusive acts or practices.

Modernization of advertising. In a press release, the CFPB states that digital marketing providers have transformed advertising, seeking to maximize individuals' interaction with ads and harvesting personal data to feed behavioral analytics models targeting individuals and groups they predict are more likely to interact with an ad or sign up for a product or service. Digital marketers also obtain data from third-party data brokers and "second-party" partnerships with other companies to develop insights about consumers' behavior more broadly—for example, whether individual consumers are "concert goers," etc. Digital marketers also target advertisements at specific times based on context, for example, the content the user is currently viewing. When digital marketers go beyond traditional advertising, they are typically covered by the CFPB as service providers. While the Consumer Financial Protection Act creates an exception for companies solely providing time or space for an advertisement for a consumer financial product or service through print, newspaper, or electronic media, the exception does not cover firms materially involved in the development of content strategy.

Liability for digital marketing providers. The interpretive rule explains that digital marketers provide material services to financial firms when they identify or select prospective customers or select or place content to encourage consumer engagement with advertising. This type of ad targeting and delivery are not merely providing ad space and time and do not qualify under the time or space exception. Because of this, the CFPB and other consumer protection enforcers can sue digital marketers to stop violations of consumer financial protection law and are liable for unfair, deceptive, or abusive acts or practices.

Fed Issues Final Guidelines on Reserve Bank Account Access

The Federal Reserve Board has issued final guidelines intended to assist Federal Reserve Banks in evaluating requests for access to accounts and payment services (Account Access Guidelines). According to the Fed, the guidelines establish a "transparent, risk-based, and consistent set of factors" for FR Banks to use in reviewing these requests. The final guidelines are substantially similar to those proposed in May 2021, and March 2022.

The Fed noted that the payments landscape is changing rapidly as technological progress and other factors are leading both to the introduction of new financial products and services and to different ways of providing traditional banking services. Many of these "novel charter" organizations have requested access to Fed accounts and payment services. "The new guidelines provide a consistent and transparent process to evaluate requests for Federal Reserve accounts and access to payment services in order to support a safe, inclusive, and innovative payment system," said Lael Brainard, Fed Vice Chair.

The guidelines include a tiered review framework to provide clarity on the level of due diligence that FR Banks will apply to different types of institutions with varying degrees of risk. For example, organizations with federal deposit insurance are subject to a more streamlined review, while novel charter institutions will undergo a more extensive review. The Fed noted that the tiered review framework was refined in the final guidelines due to comments that requested comparable treatment between non-federally-insured institutions chartered under state and federal law.

"Entities making application to the Federal Reserve should be able to clearly understand the expectations and standards of review that will apply when they seek access to Reserve Bank accounts and services," said Fed Governor Michelle Bowman. "However, these guidelines are only the first step in providing a transparent process. More work remains to be completed before a process is established to fully implement the guidelines. There is a risk that this publication could set the expectation that reviews will now be completed on an accelerated timeline."

The American Bankers Association expressed approval of the Account Access Guidelines, stating, "We welcome the Federal Reserve's new Account Access Guidelines, which we hope will provide much-needed clarity and consistency to master account eligibility and approval. As we indicated in our comment letters, we embrace financial innovation, but we should not do anything to undermine the strength and resiliency of our banking system. Allowing new financial players to access the Federal Reserve system without requiring them to meet the same high standards as banks poses real risks."

FHFA Releases "Severely Adverse" Stress Test Results

The Federal Housing Finance Agency has announced the release of the results of the "severely adverse scenario" of the Dodd-Frank Act stress test for Fannie Mae and Freddie Mac, the Government Sponsored Enterprises. The FHFA—the primary federal financial regulator of Fannie Mae and Freddie Mac (the Enterprises) and the 12 Federal Home Loan Banks—issued a report, Dodd-Frank Act Stress Tests—Severely Adverse Scenario, providing updated information on possible ranges of future financial results of the Enterprises under severely adverse economic conditions.

Stress tests, required by the Dodd-Frank Act, as amended by the Economic Growth, Regulatory Relief, and Consumer Protection Act, are designed to determine whether the regulated entities have the capital necessary to absorb losses as a result of adverse economic conditions. Under the Dodd-Frank Act, certain financial companies with total consolidated assets of more than $250 billion, and which are regulated by a primary federal financial regulatory agency, are required to conduct periodic stress tests to determine whether the companies have the capital necessary to absorb losses as a result of severely adverse economic conditions.

The stress testing applies to the Enterprises on an annual basis because each Enterprise has total consolidated assets of more than $250 billion. Because the FHLBanks do not meet the total consolidated asset threshold, they are not subject to the stress test requirements of the rule.

The Federal Housing Finance Agency published a notice in the *Federal Register* on March 16, 2022, concerning orders issued to Fannie Mae, Freddie Mac, and the 12 Federal Home Loan Banks requiring reporting of annual stress testing results, including the stress test scenarios

Fannie Mae stated it conducted a stress test in 2022 reflecting two hypothetical economic scenarios. According to the Enterprise, its projected performance in the hypothetical severely adverse scenario has improved significantly since the implementation of the regulatory stress testing requirement nine years ago. Freddie Mac also posted the results of its 2022 stress test for the severely adverse scenario. The FHFA will review each Enterprise's assumptions for reasonableness and consistency with the assumptions used by the other Enterprise. The agency may require an Enterprise to adjust its assumptions or resubmit its results where the FHFA deems the stress test results, assumptions, or processes are unacceptable.

CFPB, CMS tackle illegal nursing home debt practices

The Consumer Financial Protection Bureau and the US Department of Health and Human Services' Centers for Medicare & Medicaid Services (CMS) have issued detailed joint warnings to nursing homes and their debt collectors in connection with illegal and unenforceable "Responsible Party" contract tactics. The agencies similarly warned debt collectors not to bring "information and belief" accusations against third parties about fraudulent transfers that lack any basis in evidence. The CFPB provided parallel legal guidance to federal enforcement agencies in connection with the agencies' observations about illegal nursing home debt collection behaviors.

The CFPB and CMS issued a joint letter reminding nursing care facilities that they cannot legally require third-party caregivers to personally guarantee payment of a nursing home resident's bills as a condition of the resident's admission to a nursing facility. Recent survey findings by CFPB and CMS, as summarized in a joint Issue Spotlight report, prompted the agencies to issue this reminder. The agencies said that conditioning nursing home admission on a guarantee of a third-party caregiver payment violates the Nursing Home Reform Act (NHRA). The agencies likewise warned that attempts to collect debts from third parties based on illegal Responsible Party contract clauses may violate the Fair Debt Collection Practices Act (FDCPA) and the Fair Credit Reporting Act (FCRA).

Findings. The joint Issue Spotlight report, "Nursing Home Debt Collection," explored questionable nursing home contract provisions and debt collection tactics and related effects on the families and friends of nursing home residents. The agencies said that some third-party caregivers have even lost their homes as a result of illegal debt-collection tactics. The agencies say they found that "many facilities" include illegal Responsible Party clauses in resident admission contracts. While clauses vary, the agencies observed that "many bear similarities." The agencies said that consumers should watch particularly for joint and several liability languages and internal contradictions. A contract may say, for example, that third parties do not guarantee costs, but the same contract may later state provisions that suggest the opposite.

The agencies said that many third parties are "unaware that the law imposes restrictions on nursing home contracts." They may also be insufficiently prepared to defend unenforceable claims in court. They often permit default judgments against them which then gives collection firms access to forceful wage garnishment and foreclosure tools.

The Issue Spotlight also drew attention to potentially specious claims that third parties engage in financial wrongdoing, like fraudulent asset transfers. Medicaid rules address fraudulent transfers, and they do happen, but the agencies found that a "majority" of collection suits against third parties alleged fraudulent dealing without reciting any real support for the allegations. The agencies said this raised the possibility that such claims were simply used as an empty "technique of coercion." The agencies drew attention to their perception of suspicious "boilerplate" "information and belief" pleading language in New York and Ohio in particular.

The Issue Spotlight further noted that the issue is becoming more intense as nursing home costs spiral. The agencies said that the 2021 annual median cost of a single room in a nursing home was nearly $110K. That represented a nominal increase of 60 percent, and an inflation-adjusted increase of 19 percent, since 2004. The average stay is thought to be 1 year and 4 months. The agencies admitted that once a resident has exhausted personal financial resources in a way that legitimately provides for Medicaid to pick up the difference, the nursing homes must often wait long periods of time for their Medicaid reimbursement. At that point, "some nursing home begin attempting to collect costs from the resident's family members and friends."

The CFPB said it issued a companion circular confirming how trying to collect nursing home debts based on illegal contract terms can violate the FDCPA and FCRA. The CFPB said it does not enforce the NHRA, but it warned that the NHRA makes requiring third-party guarantees of payment "unenforceable."

Joint letter. The agencies issued a joint "notification letter" addressed to all "[n]ursing facilities and debt collectors" dated Sept. 8, 2022. The letter warned the facilities about "invalid and unenforceable" resident contract terms, and that some facilities have "attempted to evade" statutory prohibitions. The letter specifically warned that facilities that violate the NHRA "may be subject to enforcement action by state agencies and by CMS." It also warned assisting debt collectors. The letter urged facilities to "examine their practices" to ensure compliance with NHRA, FDCPA, and FCRA. The letter went on to describe, specifically, how these laws proscribe certain third-party guarantees and subsequent collection behaviors. The agencies said that the NHRA prohibits nursing facilities participating in Medicaid or Medicare from even requesting that any third party personally guarantee payment as a condition of admission. They warned that conflicting contract terms "are unenforceable."

The letter likewise reminded us that the FDCPA prohibits false, deceptive, or misleading representations as a means of debt collection. The agencies said that nursing facilities and their debt collectors could easily run afoul by misrepresenting that a third-party consumer must pay a debt based on an illegal and unenforceable Responsible Party clause. They said unfounded allegations about third-party financial wrongdoing would also violate the FDCPA.

The agencies reminded that the FCRA, meanwhile, prohibits the furnishing of inaccurate information to consumer reporting agencies. The agencies emphasized that reporting that a third party owes a debt to a nursing home when such a claim is based on an illegal contract "may demonstrate that furnishers lack reasonable written policies and procedures regarding the accuracy and integrity of information they furnish."

The CFPB simultaneously published Circular 2022-05 to clarify CFPB policy on these issues and to advise parties with the authority to enforce federal consumer financial law. The circular contains a comprehensive recitation of statutes, regulations, and case law pertinent to enforcing the FDCPA and FCRA in light of the agencies' joint findings.

The CFPB said that consumers can submit complaints about their debt collection issues by visiting the CFPB's website or by calling the agency.

Digital Identity Vulnerabilities Shape Threat and Innovation Landscape, FinCEN Official Says

Jimmy Kirby, Acting Deputy Director of the Financial Crimes Enforcement Network (FinCEN), delivered remarks at the 2022 Federal Identity Forum & Exposition (FedID) in Atlanta, Georgia. Kirby focused the talk on the role of digital identity in emerging threats to the financial system, in addition to the ways the private and public sectors are addressing those threats and collaborating together, according to a copy of the prepared remarks.

Digital identity. First, Kirby discussed the opportunities and challenges of digital identification. Many of FinCEN's authorities are designed to help financial institutions and law enforcement identify customers and the nature of their activity. "The digital identity framework has the potential to spur innovation in financial products and services across the legacy financial system," Kirby said, "as well as digital assets and emerging central bank digital currencies."

In particular, Kirby cited source verification and interoperability as important digital identity features and said consumer permissioned identity evidence that is stored cryptographically and accessed via token exchange offers significant potential. It is imperative, Kirby said, to find "identity solutions that preserve privacy and security, promote financial inclusion, and protect the integrity of the financial system."

Emerging threats. Second, Kirby discussed emerging threats to financial institutions as the industry migrates toward online and non-face-to-face formats. This development, he said, has created new opportunities for abuse and new risks from traditional players, such as efforts to evade sanctions on Russia for its invasion of Ukraine. Security breaches and data hacks have also exposed personally identifiable information, which bad actors seek to exploit.

Many identity vulnerabilities occur at the verification state or entail impersonation or compromise. Verification failures often reflect processes that are insufficient, circumvented, not completed, or not in place. In 2021, financial institutions reported to FinCEN a substantial year-on-year increase in potential identity verification, impersonation, and compromise-related suspicious activity, Kirby said.

Responsible innovation. Third, Kirby said combatting financial crimes must be a proactive effort and involve adaptation and innovation. FinCEN is exploring ways to leverage government digital identity services like state mobile driver's licenses. FinCEN is also working to implement the Anti-Money Laundering Act of 2020. "Our regulations and reporting requirements, as well as identity systems and the way in which we analyze data, need to evolve along with the threats," Kirby said.

Expanding partnerships and feedback loops. Fourth, Kirby emphasized collaboration between public and private sectors and said FinCEN is seeking partnerships related to digital identity. He cited ongoing collaborations such as FinCEN's Innovation Hours, where companies can showcase innovative approaches against money laundering and the financing of terrorism. The Bank Secrecy Act Advisory Group (BSAAG) is another channel for communication between financial institutions, trade groups, and federal and non-federal regulators and law enforcement agency representatives.

CFPB Extends Comment Period for Information on "Employer-Driven Debt"

The Consumer Financial Protection Bureau is giving the public additional time to comment on the effect "employer-driven debt" may have on consumers. The Bureau in June issued a request for information seeking comment on the prevalence and impact of debts employers may impose on workers, giving the public until September 7, 2022, to weigh in. The comment period now ends on September 23, 2022. In its initial request for comment, the CFPB said it had found troubling instances of employers passing on debt to consumers through policies such as requiring employees to purchase equipment or undergo training and reimburse the company for the expense. The Bureau said it found many of the instances occurred in industries dominated by a small number of employers.

The Bureau said it is looking for real-world experiences with employer-driven debt as well as quantitative data. The extension of the comment period "will allow interested persons more time to pull together" information, the CFPB said.

The CFPB issued its request after a group of Democratic senators asked CFPB Director Rohit Chopra to look into the practice of companies requiring workers to pay back training costs if they leave the company within a certain time period. So-called training repayment agreements (TRAs) can tether employees to their jobs and keep them from seeking better ones, said the senators, including Banking Committee Chairman Sherrod Brown (D-Ohio) and Sen. Elizabeth Warren (D-Mass).

The CFPB's request for information was designed to determine whether consumers have a meaningful choice in accepting employer-driven debt products such as TRAs, and to understand their terms and conditions. "Our inquiry is about studying the effects of an emerging form of debt that may have the potential to trap employees in place," Chopra said at the time.

The CFPB said it is particularly interested in hearing from consumers, worker organizations and labor unions, as well as social service organizations, consumer rights and advocacy groups, legal aid attorneys, academics and researchers, small businesses, financial institutions, and state and local government officials.

The Bureau said it will analyze the information "in the service of better understanding the relationship between labor practices and the market for consumer financial products or services and identifying priority areas for future action."

OFAC Updates Cyber-Related Sanctions Regulations

The Department of the Treasury's Office of Foreign Asset Control (OFAC) has amended, and reissued in their entirety, regulations related to cyber-related sanctions. The comprehensive final rule replaces regulations that were issued in 2015, and includes additional interpretive and definitional guidance, general licenses, and other regulatory provisions that will provide further guidance to the public. The final rule is effective on September 6, 2022. The publication of the final rule triggered automatic administrative updates to roughly 140 entries on the specially-designated nationals (SDN) list. The assets of individuals and companies on the SDN list are blocked and US persons are generally prohibited from dealing with them.

OCC Prioritizes Agility, Credibility, and Fairness in 2023–2027 Strategic Plan

The Office of the Comptroller of the Currency announced it has released its strategic plan for fiscal years (FY) 2023–2027 outlining the agency's approach to achieving three strategic goals of agility and learning, credibility and trust, and leading on supervision as the banking system evolves. The strategic plan outlines how the OCC will fulfill its mission of ensuring that national banks and federal savings associations operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations.

Agility and learning. According to the strategic plan, the risk profile of banking is rapidly evolving, and a solid understanding of traditional banking risks is not enough to ensure safety and soundness for banks and fairness for individuals and communities. The rapid pace of change creates increasingly complex financial, compliance, operations, technology, cybersecurity, and resiliency risks, and banks must be agile and shift to a culture of continuous learning.

To achieve its goal of agility and learning over the next five years, the OCC will (1) promote an organizational culture that seeks workforce diversity, inclusivity of thought, experiences, and knowledge, and brings multiple perspectives to bear on issues, especially divergent views; (2) enhance and promote an adaptive mindset and culture of continuous learning, including the critical thinking skills necessary to meet rapidly evolving bank regulatory challenges; (3) enable information to flow easily through the agency and promote influence through sharing and collaboration and enable flexible resource sharing to be responsive to changing priorities while maintaining mission activities without disruption; (4) transform the agency's talent management strategy and practices to attract, engage, develop, retain, and promote diverse employees, including those with diversity of education, experience, and perspective; and (5) develop and implement an approach that empowers staff to exercise judgment and use their discretion by ensuring alignment across the agency and ensure that processes and operations are modernized and updated accordingly.

Credibility and trust. The OCC earns and safeguards the public's trust by being highly credible to a wide range of stakeholders. According to the strategic plan, effective bank supervisions support a strong and fair banking system, enabling individuals, communities, and the US economy to thrive. The health, resilience, and trust of those stakeholders are the ultimate measures of the OCC's success.

To achieve its credibility and trust goals over the next five years, the OCC will (1) prioritize safeguarding the public's trust and ensure the federal banking system is safe, sound, and fair; (2) push its limits on how it communicates by challenging its traditional communication practices, developing effective feedback loops, and being bold in seizing opportunities to tell its story and share its work with internal and external stakeholders; (3) through transparency, bolster the credibility of its actions, processes, and decisionmaking and increasing awareness of the OCC's mission, tools, and resources to drive better outcomes; (4) approach outreach and engagement with stakeholder strategically, especially on complex and emerging issues facing the banking system; and (5) hold all levels within the OCC accountable for strengthening credibility, reliability, and trust with internal and external stakeholders.

Leading on supervision as banking system evolves. The OCC is viewed by peer agencies and international bodies as a leader on both traditional and emerging bank supervision issues. Focusing on risk allows the agency to invest time and resources necessary to be knowledgeable and credible on innovations and emerging trends and practices affecting the banking industry, such as digitalization and climate risk management. The OCC has renewed its focus on fairness, and, while firmly grounded in its mission, is open-minded about the evolution of innovative services, non-traditional products, and technologies. This allows the agency to discern risks from opportunities and adapt supervisory practices accordingly. To achieve its goal of leading on supervision over the next five years, the OCC will (1) enhance the implementation of risk-based supervision, enabling the agency to be nimble giving the changing landscape of banking activities and financial services; (2) ensure the federal banking system provides fair access and treats customers fairly, integrating fairness with safety and soundness; (3) invest time and resources necessary to cover innovations and emerging issues that may affect safety, soundness, and fairness in banking; (4) deepen collaboration with other regulators domestically and internationally; and (5) promote strengthening and modernizing community banks, with a focus on small business and underserved communities.

SECURITIES/SECTION 20/ BROKER-DEALER

Office of the Investor Advocate Releases Research Study on Fund Performance Benchmarks

On September 19, 2022, researchers from the SEC's Office of the Investor Advocate (OIAD) released an independent research study examining the impact of mutual fund performance benchmarks on investor decisionmaking, and potential strategic behavior by firms in displaying benchmarks. This study examines market data and the results of a large behavioral experiment to understand how funds employ benchmarks and how investors respond to benchmark presentation.

The research study was published on the OIAD website and has been placed in the comment file (No. S7-09-20) for a rulemaking package that would, among other things, modernize open-end fund shareholder reports. The proposal, which was proposed by the Commission in August 2020, features concise and visually engaging shareholder reports that would highlight information that is particularly important for retail investors to assess and monitor their fund investments.

Analysis of the research study may be informative for evaluating comments on the proposed requirements for funds' performance disclosure. The authors are making this analysis available to allow the public to consider this supplemental information. Comments on this supplemental information may be submitted to the comment file (File No. S7-09-20) for the proposal.

OIAD was established by Congress in 2014 as an independent office within the SEC. The Office provides a voice for investors as decisions are made at the SEC.

SEC Proposes Rules to Improve Risk Management in Clearance and Settlement and to Facilitate Additional Central Clearing for the US Treasury Market.

On September 14, 2022. The Securities and Exchange Commission today proposed rule changes that would enhance risk management practices for central counterparties in the US Treasury market and facilitate additional clearing of US Treasury securities transactions. The proposed rule changes would update the membership standards required of covered clearing agencies for the US Treasury market with respect to a member's clearance and settlement of specified secondary market transactions. Additional proposed rule changes are designed to reduce the risks faced by a clearing agency and incentivize and facilitate additional central clearing in the US Treasury market.

"The Securities and Exchange Commission plays a critical role in how the Treasury market functions, including to help ensure that these markets stay efficient, competitive, and resilient," said SEC Chair Gary Gensler. "One aspect of that role is our oversight of clearinghouses for Treasury securities. While central clearing does not eliminate all risk, it certainly does lower it. In 2017, however, only 13 percent of Treasury cash transactions were centrally cleared. Thus, I think there is more work to be done with respect to the amount of Treasury activity that is centrally cleared. I think that these rules would reduce risk across a vital part of our capital markets in both normal and stress times. This advances our three-part mission."

Specifically, the proposal would require that clearing agencies in the US Treasury market adopt policies and procedures designed to require their members to submit for clearing certain specified secondary market transactions. These transactions would include: all repurchase and reverse repurchase agreements collateralized by US Treasury securities entered into by a member of the clearing agency; all purchase and sale transactions entered into by a member of the clearing agency that is an interdealer broker; and all purchase and sale transactions entered into between a clearing agency member and either a registered broker-dealer, a government securities broker, a government securities dealer, a hedge fund, or a particular type of leveraged account.

With respect to customer margin, the proposal would permit broker-dealers to include margin required and on deposit at a clearing agency in the US Treasury market as a debit in the customer reserve formula, subject to certain conditions. In addition, the proposal would require clearing agencies in this market to collect and calculate margin for house and customer transactions separately. Finally, the proposal would require policies and procedures designed to ensure that the clearing agency has appropriate means to facilitate access to clearing, including for indirect participants.

The proposing release will be published on SEC.gov and in the Federal Register. The public comment period will remain open for 60 days following the publication of the proposing release in the Federal Register.

FUTURES/DERIVATIVES/SWAPS/ COMMODITIES

CFTC Charges Digital Asset Derivatives Platform and Miami Resident with Facilitating Unlawful Futures Transactions, Failing to Register, and Attempted Manipulation of Native Token

On October 3, 2022, the Commodity Futures Trading Commission today announced it filed a complaint in the

US District Court for the Southern District of Florida against Florida resident Adam Todd and four companies he controlled—Digitex LLC, Digitex Limited, Digitex Software Limited, and Blockster Holdings Limited Corporation. The complaint alleges that Todd and his companies operated a digital asset exchange under the trade name "Digitex Futures." Todd and Digitex Futures are charged with illegally offering futures transactions on a platform other than a designated contract market and also with attempting to manipulate the price of the Digitex Futures native token.

In its continuing litigation, the CFTC seeks full restitution, disgorgement of ill-gotten gains, civil monetary penalties, permanent trading and registration bans, and a permanent injunction against further violations of the Commodity Exchange Act (CEA), as charged.

"The CFTC's action against Adam Todd and Digitex Futures underscores the primacy of the CEA's core registration provisions that are designed to ensure the structural integrity of our nation's derivatives markets." said Acting Director of Enforcement Gretchen Lowe. "Further, the CFTC will vigorously investigate potential manipulative trading activity to ensure confidence in markets remains strong."

Case Background

The complaint alleges that from approximately May 2020 through May 2022, Todd and Digitex Futures operated a digital asset derivatives exchange from an office in Florida. The Digitex Futures exchange allegedly sought participation from US customers through web-based solicitations, despite the fact Todd knew such participation subjected Digitex Futures to US regulation.

In addition to the alleged registration and regulatory violations, the complaint states Todd attempted to manipulate the price of DGTX, the exchange's "native currency," between approximately May 2020 and August 2020. Digitex Futures required users to deposit DGTX into their accounts to margin their trading on the futures exchange. According to the complaint, throughout the summer of 2020—the time when the exchange was readying for "launch"—Todd repeatedly attempted to, in his words, "pump" the price of DGTX as reported by third-party exchanges.

Todd allegedly accomplished his "pumping" activity by, among other things, deploying a "bot" on third-party exchanges he designed to be "always buying more than it was selling" and by filling large over-the-counter orders to purchase DGTX on third-party exchanges rather than out of the Digitex Futures "treasury." The complaint alleges Todd took these steps intending to increase the price of DGTX, as reported by third-party exchanges, even though he acknowledged this practice would result in trading losses because Todd knew the higher DGTX price would benefit the vast amounts of DGTX held by the Digitex "treasury."

The CFTC appreciates the assistance of the Australian Securities and Investments Commission, Central Bank of Ireland, Cyprus Securities and Exchange Commission, Gibraltar Financial Services Commission, Seychelles Financial Services Authority, and St. Vincent & the Grenadines Financial Services Authority.

COURT DEVELOPMENTS

Debtor Had No Standing to Pursue an FDCPA Claim Against a Creditor

In its third ruling on a Fair Debt Collection Practices Act matter, the US Court of Appeals for the 11th Circuit has determined that the debtor in the case lacked Article III standing and dismissed the suit without prejudice. This was a shift in thinking from an April 2021 ruling from the Court that the debtor had standing. That opinion was subsequently vacated after subsequent guidance from a relevant Supreme Court ruling and another ruling in favor of standing, and the matter then returned to the 11th Circuit for an en banc hearing. In an 8-4 decision, the Court found that the debtor lacked Article III standing and dismissed the case without prejudice. (*Huntstein v. Preferred Collection and Management Services, Inc.*, 11th Cir., No. 19-14434, Grant, B.).

History of the Case. This case arose when a debtor incurred a medical debt for medical treatment for his son. The hospital assigned the debt to a collection agency which then hired a mail vendor for collection. The collection agency sent electronic data concerning the treatment and debt to the mail vendor. The vendor used that information to print and send a dunning letter. The debtor then filed suit against the collection agency for violation of the Fair Debt Collection Practice Act, in particular 15 USC §1692c(b), which indicates that collectors "may not communicate, in connection with the collection of any debt, with any person other than the consumer…without prior consent of the consumer."

The suit was filed in Florida federal court, where the trial court found that the debtor lacked Article III standing for the suit and dismissed the action for failure to state a claim. It was appealed to the 11th Circuit, which initially ruled in April 2021 that the debtor did have standing and could pursue the suit, but that opinion was vacated in October 2021 with a new opinion, similarly indicating that the debtor had standing to sue. The Court then voted to take the case en banc.

Current Decision. The 11th Circuit finds that the debtor, in this case, lacked Article III standing and dismissed the case without prejudice. In this case, the debtor who alleged the violation of the statute had to establish real harm in order to have standing. The question was whether the statutory violation had some sort of common-law analog. The prior 11th Circuit ruling indicated that the statutory violation had a close relationship to the tort of public disclosure of private facts. The subsequent Supreme Court ruling—*TransUnion LLC v. Ramirez*, 141 SCt. 2190 (2021)—indicated that in order to determine whether an alleged intangible harm is concrete or real, courts are to see if the harm alleged matches up with any "traditionally recognized as providing a basis for lawsuits in American courts." An exact duplicate of the tort is not required, but the allegations cannot be missing any element essential to liability of the tort in question.

The majority concludes that the debtor's claimed standing must fail because the disclosure which is the basis for debtor's claims lacks the element of publicity. "Without publicity," writes the court, "there is no invasion of privacy—which means no harm, at least not one that is at all similar to that suffered after a public disclosure."

A concurring opinion from two judges agrees in the result and notes that not only is the element of publicity missing, but that the debtor's complaint also failed to allege a highly offensive disclosure, also a prerequisite for the tort of public disclosure of private facts.

Scathing dissent. That said, four judges joined a dissenting opinion that sees the case very differently. The dissent claims that the majority's approach forces the statutory violation to exactly match a tort, in which case Congress is essentially reduced to a scrivener, codifying existing torts into new legislation. The dissent supports a "kind-degree" framework for comparison of a statutory violation with an existing tort. Under such a theory, a plaintiff must show that his alleged injury is similar in kind to the harm addressed by a common-law cause of action, but not that it is identical in degree. The dissent indicates that most circuits agree with such an interpretation, and that the debtor has sufficient standing and his case should be allowed to go forward. [*Huntstein v. Preferred Collection and Management Services*, Inc. (11th Cir)]

Non-Consumer Attorney Lacked FDCPA Standing

The US Court of Appeals for the Eighth Circuit Court affirmed the Eastern District of Missouri District Court in granting judgment on the pleadings to a collector in an FDCPA suit by a non-consumer attorney who was contacted in regard to the debt of a person he did not represent. While the Court agreed with the trial court that the collector's conduct did violate the Federal Debt Collection Practices Act, it also affirmed that the attorney lacked standing to bring the suit. A dissenting opinion would have overturned the lower court ruling, and the matter of standing turned on the interpretation of the applicable statute. (*Magdy v. I.C. System, Inc.*, No. 21-3010, Shepherd, B.).

In July 2020, a collection agency sent a letter to an attorney in regard to a debtor who was not his client. The attorney spent time and resources hunting a client who he never represented. Soon thereafter, the attorney sued for violation of 15 U.S.C. §1692c(b) which prohibits a debt collector from contacting a third party ("any person") about the collection of a debt without the prior consent of the consumer. The trial court granted the collector's motion for judgment on the pleadings, as the non-consumer attorney lacked standing to sue. The attorney appealed that ruling, and the appellate court affirmed it.

There was no question that the collector violated the statute, only whether the non-consumer attorney had standing to sue for the violation. The court noted that the central inquiry was whether the attorney's interests fell within the zone of interests of the statute invoked.

The court read that particular statutory section as written to protect consumers and not third parties, noting that if the consumer consents, the collector can send "a relentless stream of letters to a third party without running afoul of §1692c(b)." As the court construed the purpose of the statute as being protecting of consumers and not third parties, it also concluded that the attorney was outside the zone of interests of the statute and could not invoke its protections.

The attorney cited a state case that had allowed third-party recovery under the statute, but the 8th Circuit distinguished the case, noting that the claimant was the debtor's girlfriend, who was told by the collector that the debtor's brother was in trouble, a message that caused emotional harm to both the debtor and the girlfriend. In the instant case, the attorney had no relationship with the relevant consumer, and that consumer was not a co-plaintiff.

There were other matters also discussed in this case. The attorney complained that while he had asked to amend his claims, the trial court had not allowed him to do so. The 8th Circuit indicates that the attorney had failed to comply with the local rules of Civil Procedure, and that not allowing him to amend his complaint was not an abuse of discretion. The attorney also asked that the suit be remanded to state court rather than dismissed, but the 8th Circuit did not agree.

A dissenting opinion from Judge Stras construed the relevant statute very differently. The dissenting opinion notes that the attorney did sustain the damage of his wasted time and trouble, and that he is indeed "any person" not the consumer, sufficient to draw the collector's conduct within the statute in question. The dissenting opinion was also dubious over the judicial parsing of the statute by the majority in this case, noting that "when statutes have multiple purposes, trying to narrow it down to just one becomes an exercise in 'looking over a crowd and picking out your friends.'" To the dissenting judge, the language of the statute would include the non-consumer attorney, and if this was not the intention of the statute, it could always be amended by Congress. [*Magdy v. I.C. System, Inc.*]