June 11, 2021

Commissioner Allison Herren Lee
US Securities and Exchange Commission

Public Input on Climate Change Disclosures

Dear Commissioner Lee,

We welcome the work of the US Securities and Exchange Commission (SEC) and on behalf of Actual Systems, Inc., appreciate the chance to submit public comments on the important issue of Climate Change related disclosures.

Climate change is the defining challenge of the next century. We are now in the Impact Era, where enterprises will rise or fall by their ability to set and execute against ESG goals. This Era is driven by consumer behavior, cost of capital, technological innovation, supply chain pressures, changing international mandates, and innumerable other key factors. The ability for a corporation to meet its ESG and climate goals and mandates is now material to its ability to remain competitive. Investors in these corporations need clear, comprehensive, and accurate disclosures to quantify their risk and potential return. A mandatory disclosure framework elevated to the level of existing financial disclosures is key for investors to make informed decisions, and will help maintain the competitiveness of American corporations as new climate-conscious markets emerge around the world.

Climate change related disclosures can not be separated from ESG disclosures. Climate change has major social and governance implications with respect to mitigations and adaptations. We encourage the Commission to consider incorporating ESG disclosures more broadly, and applaud the Commission's critical work towards developing disclosure standards and frameworks which will improve investor confidence and American competitiveness in this new Impact Era

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1. How can the Commission best regulate, monitor, review, and guide climate change disclosures in order to provide more consistent, comparable, and reliable information for investors while also providing greater clarity to registrants as to what is expected of them? Where and how should such disclosures be provided? Should any such disclosures be included in annual reports, other periodic filings, or otherwise be furnished?

The Commission can best regulate, monitor, review, and guide climate change disclosures by incorporating a new climate-change and ESG focused reporting framework into Regulation S-X, with the same level of form and content requirements as existing financial disclosures. Today's climate reporting frameworks are typically freeform in nature - while frameworks such as the TCFD (Task Force on Climate related Disclosures)[1] give voluntary suggestions for disclosures, they provide significant leeway to the reporting organization in terms of the form and content. Incorporating these disclosures into Regulation S-X would make benchmarking, analysis, risk assessment, and other functions more effective for the investment community at large and the Commission. In addition, standardizing the form and function of reporting would highlight solution gaps to the market at large, incentivizing technological and business process innovation in ESG at large.

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2. Are there specific metrics on which all registrants should report (such as, for example, scopes 1, 2, and 3 greenhouse gas emissions, and greenhouse gas reduction goals)? What quantified and measured information or metrics should be disclosed because it may be material to an investment or voting decision?

Yes, there should be baseline requirements including scopes 1, 2, 3, GHG (Greenhouse Gas) and GHG reduction goals. In addition, registrants should report:

A. Specific environmental regulations which they are subject to in each region that they operate
B. Their progress towards meeting these regulations
C. Benchmarks against other registrants with similar business process needs.

Do climate change related impacts affect the cost of capital, and if so, how and in what ways?

Cost of capital is a measure of risk and opportunity, and climate change impacts both these metrics in numerous ways.

- **Disasters** - organizations without a climate adaptation and related ESG plan will face significant and increased disruption from disasters which will become more frequent and severe. This will increase insurance costs, personnel costs, and lead to material losses and disruptions in operations.
- **Technology** - organizations which adopt modern, more efficient technologies have substantially lower OpEx, improving margins and profitability relative to competitors using legacy solutions. For example, fleet electrification substantially shrinks energy supply chains, can insulate OpEx from geopolitical factors, reduces maintenance costs,

[1] https://www.fsb-tcfd.org

enables organizations to generate their own power and diversify their revenue base by selling power, among other things.

- **Market Pressure** - as organizations face increased pressure from consumers and investors to enhance and execute against their ESG and climate plans, they'll pressure companies in their supply chain to strengthen their own ESG and climate plans. Suppliers that don't adopt the latest technologies or adapt to increasing disasters will become less competitive or even a reputational risk to customers and risk losing contracts.
- **Regulations** - tightened rules, technological mandates, etc can all lead to fines, revoked licenses, and other risks to doing business.

Several studies[2] have shown a significant correlation between ESG plans and cost of capital, ranging from 25 to over 100 bps depending on the sector and region of an organization.

What are registrants doing internally to evaluate or project climate scenarios, and what information from or about such internal evaluations should be disclosed to investors to inform investment and voting decisions?

Registrants engaged in evaluating and projecting climate scenarios today typically work with subject matter experts and consultants, or have internal sustainability teams working to project the impacts of various climate change scenarios on their organizations. As analytical tools become more prevalent and usable, with the ability to share modeling and results with key stakeholders at various levels of resolution while protecting business confidential information, it's likely that registrants will begin to publish and promote their own internal climate modeling as a signal to the investment community and market at large (including consumers) of their climate resilience and ESG planning (see A, B, C in the sub-question below). *Requiring* disclosure at the level of S-X will be key; companies will be motivated by market or contractual pressures to go beyond and disclose the details about internal analysis to relevant stakeholders.

How does the absence or presence of robust carbon markets impact firms' analysis of the risks and costs associated with climate change?

It's important not to conflate mitigations with adaptations or the cost of doing nothing. There are three distinct risks and costs at play here:

A. The risks and costs associated with mitigating an organization's impact the climate
B. The risks and costs associated with deploying adaptations which minimize the impacts of climate change on the organization by improving resiliency
C. The risk and costs associated with dealing with the impacts of climate change in the absence of proactive adaptations

The presence and absence of carbon markets is only relevant to the analysis of (A) above, the risks and costs associated with mitigating an *organization's impact on the climate*. An organization that has completely mitigated its emissions and reached net-zero emissions can still face substantial losses if their region faces a major disaster if they don't also invest in adaptations.

[2] https://www.msci.com/www/blog-posts/esg-and-the-cost-of-capital/01726513589

Climate change mitigations are focused on reducing emissions, delaying the pace and total impact of climate change. Carbon markets are focused on setting a price for mitigation. They track the cost of removing (or avoiding) a unit of emissions and are a way for organizations with direct mitigation costs higher than the most efficient market price to pay others to reduce emissions on their behalf. The market price per unit of emissions will always reflect the costs and performance of technological and natural solutions such as DAC, forestry, solar and battery, etc. As the relevant technologies become widespread and more easily available, the cost floor per carbon credit will naturally fall -- though the credit price will be bid up by increasing demand as environmental regulations are tightened.

Adaptations are focused on an organization's own resiliency to the effects of climate change, be they natural (fires, floods) or human caused (civil unrest). The impact of reduced CO2 emissions lag the reductions by several years[3], and the risks and costs associated with climate change are set to *increase* with increasing warming that lead to more frequent and costly disasters. The risks and costs associated with adapting to climate change will depend on the specific physical exposure of an organization's operations and assets to a changing environment, regulatory and consumer pressures, etc, and will require an analysis based on geospatial information, not generalized market data.

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3. What are the advantages and disadvantages of permitting investors, registrants, and other industry participants to develop disclosure standards mutually agreed by them? Should those standards satisfy minimum disclosure requirements established by the Commission? How should such a system work? What minimum disclosure requirements should the Commission establish if it were to allow industry-led disclosure standards? What level of granularity should be used to define industries (e.g., two-digit SIC, four-digit SIC, etc.)?

4. What are the advantages and disadvantages of establishing different climate change reporting standards for different industries, such as the financial sector, oil and gas, transportation, etc.? How should any such industry-focused standards be developed and implemented?

5. What are the advantages and disadvantages of rules that incorporate or draw on existing frameworks, such as, for example, those developed by the Task Force on Climate-Related Financial Disclosures (TCFD), the Sustainability Accounting Standards Board (SASB), and the Climate Disclosure Standards Board (CDSB)?[7] Are there any specific frameworks that the Commission should consider? If so, which frameworks and why?

Response to Questions 3, 4, 5

ESG impacts are *horizontal*, based on business processes employed by a company, not on the broadly-defined industry vertical that the company falls within. Disclosure standards should be standardized across industries through existing reporting frameworks (see response to question 1), and the specific calculations and appendices which feed into the calculations should be selected based on the relevant business processes. Organizations should be able to assemble the relevant calculations and appendices to create a disclosure

[3] https://www.nature.com/articles/s41467-020-17001-1

package that is relevant and comprehensive, covering the specific business processes employed by the company.

There are several advantages to doing this. While two companies may fall in the same industry with identical 2- or 3-digit SICs, one may be completely integrated through the value chain while another is highly specialized. Subjecting both companies to the same reporting requirements is counterproductive - it will be an undue burden on one, and not capture the full scope of the other. Pushing standards making to industries is also duplicative, as each industry would likely come up with different ways to benchmark and report on business processes identical to both. These differing standards would then make it impossible to benchmark and track process-based progress towards ESG goals.

Required rules and frameworks are likely to vary globally. Defining a single, well understood disclosure standard which mirrors financial disclosure and reporting where inputs can be adapted to business and local needs is key.

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6. How should any disclosure requirements be updated, improved, augmented, or otherwise changed over time? Should the Commission itself carry out these tasks, or should it adopt or identify criteria for identifying other organization(s) to do so? If the latter, what organization(s) should be responsible for doing so, and what role should the Commission play in governance or funding? Should the Commission designate a climate or ESG disclosure standard setter? If so, what should the characteristics of such a standard setter be? Is there an existing climate disclosure standard setter that the Commission should consider?

See response to question 5: the form and content of disclosures should be separated from the analytical process required to achieve the reported results. The form and content of disclosures should be set by the Commission itself, at the same level as existing financial disclosures. However the analytical processes used to drive the disclosures may be computed using the most applicable methodology and available for audit in the organization’s system of record. See reply to section 2 for further discussion.

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7. What is the best approach for requiring climate-related disclosures? For example, should any such disclosures be incorporated into existing rules such as Regulation S-K or Regulation S-X, or should a new regulation devoted entirely to climate risks, opportunities, and impacts be promulgated? Should any such disclosures be filed with or furnished to the Commission?

See answer to question 1 - these disclosures should be elevated to the same level as existing financial disclosures due to their materiality. As a result, the simplest path for reporting would be to expand existing rules including S-K and S-X as appropriate to include climate and ESG related disclosures.

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9. What are the advantages and disadvantages of developing a single set of global standards applicable to companies around the world, including registrants under the Commission's rules, versus multiple standard setters and standards? If there were to be a single standard setter and set of standards, which one should it be? What are the advantages and disadvantages of establishing a minimum global set of standards as a baseline that individual jurisdictions could build on versus a comprehensive set of standards? If there are multiple standard setters, how can standards be aligned to enhance comparability and reliability? What should be the interaction between any global standard and Commission requirements? If the Commission were to endorse or incorporate a global standard, what are the advantages and disadvantages of having mandatory compliance?

A single set of global standards is key in today's world. Supply chains are long and cross borders, with value added in several jurisdictions. Investors are increasingly seeking to hold companies to their ESG commitments through the supply chain down to suppliers in Tier 4, 5, and beyond. As a result, reporting at the corporate level will involve rolling up reports globally into a single S-X or similar form. By driving a globally-applicable standard from the outset, the Commission can greatly improve the efficiency of this reporting and enable reporting compliance through an organization's entire value and supply chain.

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11. Should the Commission consider other measures to ensure the reliability of climate-related disclosures? Should the Commission, for example, consider whether management's annual report on internal control over financial reporting and related requirements should be updated to ensure sufficient analysis of controls around climate reporting? Should the Commission consider requiring a certification by the CEO, CFO, or other corporate officer relating to climate disclosures?

Yes. Accuracy and reliability of reporting and disclosures are critical to instill confidence in investors and other stakeholders. Requiring certification by a corporate officer will drive accuracy and reliability by incentivizing the selection of the most appropriate and relevant analytical processes (see answer to question 6) to generate a company's disclosures.

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12. What are the advantages and disadvantages of a "comply or explain" framework for climate change that would permit registrants to either comply with, or if they do not comply, explain why they have not complied with the disclosure rules? How should this work? Should "comply or explain" apply to all climate change disclosures or just select ones, and why?

A "comply or explain" framework would incentivize registrants to make climate and ESG metrics and data a central part of their systems of record. Registrants which find themselves complying with fewer sections than their peers would be pressured into improving internal analytical and reporting capability. It's only possible to manage what's measured - a "comply or explain" framework would drive organizations to measure key climate indicators within their organization and execute on programs which their investors deem material. Registrants have incredibly varied business processes, climate risks, and ESG requirements, so allowing organizations to "comply or explain" would also reduce the need for the Commission to set

disclosure rules on a sector, industry, or organizational level and instead focus on proactive audit, enforcement, and benchmarking.

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14. What climate-related information is available with respect to private companies, and how should the Commission's rules address private companies' climate disclosures, such as through exempt offerings, or its oversight of certain investment advisers and funds?

The simplest way to address the climate disclosures of private companies is to operationalize the tools and reporting structures of climate information - such as by defining an EBITDA for ESG as discussed previously. Many funds (or their LPs) have diversified portfolios and exposure to both the public and private markets. By defining a standard that can be widely applied, it's straightforward to leverage an investment advisor or funds own operational need to be able to perform diligence and internal benchmarking towards standardized reporting and compliance.

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15. In addition to climate-related disclosure, the staff is evaluating a range of disclosure issues under the heading of environmental, social, and governance, or ESG, matters. Should climate-related requirements be one component of a broader ESG disclosure framework? How should the Commission craft climate-related disclosure requirements that would complement a broader ESG disclosure standard? How do climate-related disclosure issues relate to the broader spectrum of ESG disclosure issues?

A broader, unified ESG framework is critical. Environmental, social, and governance goals and outcomes are all interlinked. Mandating climate-related disclosures (E) without elevating Social and Governance (SG) will leave investors in the dark about the effects of climate-related risks, adaptations, and mitigations on a company or fund's operational environment. Just because something is climate-responsible does not mean it's socially-responsible. For example, a large CPG company may be able to reduce its climate impact by switching from plastic to bioplastic packaging. But if the bioplastics are created with poor and exploitative labor practices, it could jeopardize the company's ability to meet these climate goals over the long term as foreign governments begin to enforce labor rules more strictly and the company loses access to its bioplastics supply chain. Climate programs occur in the real word and have real impacts on local communities - disclosures along all of ESG axes should be required, not just the impacts on climate.