



## **Public Input Welcomed on Climate Change Disclosures**

U.S. Securities and Exchange Commission ('SEC', 'the Commission'))

Submitted electronically

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### *Introduction*

The Institute for Agriculture and Trade Policy (IATP)<sup>1</sup> appreciates this opportunity to respond to some of the questions posed by the SEC in Acting Chair Alison Herren Lee's March 15 request for public input.<sup>2</sup> We do so as the SEC faces opposition rooted in what the late, great climate economist Frank Ackerman called in 2008 "the fear that overly ambitious climate initiatives could hurt the economy. Economists emphasizing that fear have, in effect, replaced the climate skeptics as the intellectual enablers of inaction."<sup>3</sup>

This fear can be translated into a Business as Usual claim that "overly ambitious" climate disclosure may hurt SEC listed companies and/or put them at a competitive disadvantage with firms in other jurisdictions not subject to disclosure requirements. Such a fear may be disguised in the all-purpose anti-regulatory claim that climate risk disclosures in the line items of 10-K and 10-Q SEC reporting forms,

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<sup>1</sup> The Institute for Agriculture and Trade Policy is a 403 c) non-profit organization headquartered in Minneapolis, MN, with offices in Washington, DC, Halliday, ME and Berlin, Germany. IATP has commented on dozens of Commodity Futures Trading Commission rulemakings since 2010. IATP is a member of Americans for Financial Reform (AFR) and has signed on to several AFR letters to the SEC. However, this is our first independent letter to the SEC. IATP is a signatory to an excellent AFR/Public Citizen disclosures analysis and recommendations letter to the SEC. We hope that Commission staff will pay particularly attention to the letter's appendix of highly specified climate and ESG "Essential Disclosures." IATP is also a signatory to a Public Citizen letter that focuses on the imperative to disclose political and electoral contributions related to climate and ESG issues. Such disclosures would enable investors, auditor, insurers and the public to know whether public corporate and bank commitments to "net zero by 2050" are contradicted by political and electoral contributions support for policies and officials opposed to action on climate and ESG issues.

<sup>2</sup> <https://www.sec.gov/news/public-statement/lee-climate-change-disclosures>

<sup>3</sup> Frank Ackerman, "Climate Economics in Four Easy Pieces," *Development* (2008) at 325.  
[http://frankackerman.com/publications/climatechange/Climate\\_Economics\\_Four\\_Easy\\_Pieces.pdf](http://frankackerman.com/publications/climatechange/Climate_Economics_Four_Easy_Pieces.pdf)

and other financial statements will be “unduly burdensome and costly” for SEC listed firms. We will not adapt here Dr. Ackerman’s four principles to improve climate economics to improving SEC climate disclosures. But we do advise the SEC to review these principles, particularly to ensure that the future of our grandchildren is not discounted in regulatory abuse of cost-benefit analysis, in which valid analysis is only that which has short-term monetary expression.<sup>4</sup>

Investor demand for information from climate related and ESG disclosures has been called ‘the new normal.’ According to the results of a survey by “Ernst & Young, 91% of institutional investors consider nonfinancial performance core to their investment decision making process over the past year [2020].”<sup>5</sup> The SEC must not succumb to political and issuer lobbying to limit climate and ESG disclosures only to those that have a material impact on a firm’s quarterly or annual financial statement. To adapt a balance sheet approach to disclosure will deprive investors, auditors, insurers and other interested parties of both quantitative and qualitative information about how SEC registrants (and eventually private equity and closely held firms) are changing their policies, production practices, human capital management, portfolio and capital allocations to meet the short, medium and long-term physical and transitional risks of climate change.

If the SEC allows its registrants to remain in the 20<sup>th</sup> century world of climate economic skepticism and to mollify investor demands for granular ESG and climate information with promises to become sustainable, U.S. investors may well choose to trade on platforms in jurisdictions with more comprehensive and comparable disclosure requirements. If investors cannot compare issuer disclosures, they may move their investments to jurisdictions that better protect investors by ensuring that they have access to comprehensive, comparable and reliable disclosure information. No matter how up to date financial trading technology is, trading algorithms will not prevent disruption of markets and capital formation by firms that are unprepared to adapt to climate and ESG related adversity on small and large scales over the short and long terms.

Finally, disclosure must be standardized, comparable, reliable and mandatory, because a large share of SEC registrant climate commitments, just measured in GHG reduction commitments, are weak to non-existent. For example, according to Institutional Shareholder Services, “Just over a third of the 500 companies in the S&P 500 stock index have set ambitious targets, it found, while 215 had no target at

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<sup>4</sup> Ackerman, “Critique of Cost-Benefit Analysis and Alternative Approaches to Decision-Making,” A report for Friends of the Earth England Wales and Northern Ireland, January 2008.  
[http://frankackerman.com/publications/costbenefit/Critique\\_Cost\\_Benefit\\_Analysis.pdf](http://frankackerman.com/publications/costbenefit/Critique_Cost_Benefit_Analysis.pdf)

<sup>5</sup> Helee Lev, “The new normal—Investors demand more ESG disclosures,” Goby, January 2, 2021,

all. The rest had weak targets.<sup>6</sup> The following comment and responses to SEC questions comprises a general comment and responses, plus responses that concern disclosure requirements that apply specifically to agribusiness and food processing companies.

### *General comment*

IATP generally supports granular, standardized, comparable and mandatory disclosure of climate related risks to the SEC. We believe that existing rules should be amended and amplified to accommodate climate and ESG disclosures, rather than creating a new and separate rule.<sup>7</sup> We agree that “the current path of climate disclosure will not provide the transparency that an increasing number of investors are seeking and, indeed, a properly functioning market requires—consistency of disclosures across time, comparability of disclosures across companies, and reliability of the information that is disclosed.”<sup>8</sup> Banks that finance SEC registered firms prefer a SEC standardized climate risk reporting, so they are not forced to choose among or synthesize their clients’ voluntary reporting standards when reporting the banks’ own climate physical and transition risks from consolidated audit trails.

The SEC should review the work of the voluntary climate financial and ESG standards initiatives to determine which elements of those standards might be incorporated into a proposed SEC disclosure rule.<sup>9</sup> All disclosures to the SEC and in audited financial reports should be overseen by the reporting firm’s Chief Financial Officer, attested to by the CFO and audited independently. The oversight process, attestation and auditors report could be included in item 9a, “Controls and Procedures” of the 10-K report. To reiterate, we support standardized and mandatory disclosure requirements with five multi-part recommendations. We conclude this comment with a mini-case study of disclosure issues for the meatpacking and dairy processing industries.

*First recommendation: build SEC capacity to evaluate disclosures of long-term physical and transitional risks based on long-term climate modeling*

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<sup>6</sup> Peter Eavis and Clifford Krauss, “What’s Really Behind Corporate Promises on Climate Change?” The New York Times, May 12, 2021.

<sup>7</sup> This is in partial response to question 7.

<sup>8</sup> Alexandra Thornton and Andy Green, “The SEC’s Time to Act: A New Strategy for Advancing U.S. Corporate and Financial Sector Climate Disclosures,” Center for American Progress, February 19, 2021. <https://www.americanprogress.org/issues/economy/reports/2021/02/19/496015/secs-time-act/#Ca=3>

<sup>9</sup> Responding to question 1.

The likelihood of and costs from climate change related weather events at the firm level can be estimated over a short term (e.g. 1-3 years) with the use of accounting and actuarial data.<sup>10</sup> However, reporting estimated physical and transition risks over the longer term rely on climate modeling that is subject to variables and uncertainties that cannot be quantified with the degree of certainty that investors and other market actors demand. A group of climate modelers recently warned, “Calls for the integration of climate science into risk disclosure and decision-making across many levels of economic activity has leap-frogged the current capabilities of climate science and climate models by at least a decade.”<sup>11</sup> This warning does not mean that the SEC should wait a decade for climate science and modeling to catch up to the demands of business for geo-spatially and temporally specific climate information for the SEC to initiate and finalize a rulemaking on climate disclosures. It does mean that the SEC needs in-house climate modeling expertise to evaluate whether the longer-term plans of a firm are adequate to mitigate its longer-term risks estimated by reporting entities according to their use of climate models.

For example, climate science has described the geo-physical ‘tipping points’ that will result in abrupt or irreversible changes to global and regional climates.<sup>12</sup> However, modeling how, when and to what extent those changes will impact corporate and financial sector assets and supply chains is subject to a number of climate scenarios, variables and uncertainties. The Commission should consider phasing in the reporting of longer-term physical and transitional risks to take into account the computer modeling capacity of reporting firms to estimate their firm level operational, credit, liability and market risks.<sup>13</sup> The Commission could also develop criteria to enable issuers to report longer-term risks and projects to mitigate and adapt to climate change with differentiated confidence levels similar to those consensus scientific reports, such as those of the International Panel on Climate Change.

*Second recommendation: tailoring climate and ESG disclosure requirements to industry groups vs. general disclosure requirements*

A second recommendation concerns the question of whether the SEC should develop uniform disclosure requirements for firms in all sectors and/or develop

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<sup>10</sup> E.g. “Actuaries Climate Risk Index,” National Association of Insurance Commissioners, March 16, 2021. [https://content.naic.org/cipr\\_topics/topic\\_actuaries\\_climate\\_risk\\_index.htm](https://content.naic.org/cipr_topics/topic_actuaries_climate_risk_index.htm)

<sup>11</sup> Tanya Fiedler et al, “Business risk and the emergence of climate analytics,” *Nature Climate Change*, Vol. 11, February 2021, at 91.

<sup>12</sup> Robert McSweeney, “Explainer: Nine ‘tipping points’ that could be triggered by climate change,” *Carbon Brief*, October 2, 2020.

<sup>13</sup> Response to question 2.

disclosure requirements for specific industries.<sup>14</sup> The cross-sectoral provisions of a disclosure rule should require that all firms should report their direct GHG emissions (Scope 1), emissions from purchased energy (Scope 2) and value chain emissions (Scope 3), including financed and insured emissions and emissions from land use change.<sup>15</sup> Given the complexity and variety of Scope 3 emissions, this reporting requirement should be phased in for small SEC registrants. Reporting could follow the Greenhouse Gas Protocol already used by most Fortune 500 companies for reporting to the CDP.<sup>16</sup>

In terms of U.S. emissions, “The EPA already provides data on the amount of greenhouse gases emitted by certain high-emitting industry sectors. Simply put, financed emissions can be estimated based on the percentage of each of these industries represented in a financial firm’s portfolios of loans, insurance policies, [and/]or investment funds.”<sup>17</sup> To this formula could be added reporting of the percentage of a firm’s debt used to finance emissions, their energy use, costs and sources. The SEC should review the “Global GHG Accounting and Reporting Standard for the Financial Industry”<sup>18</sup> for possible adoption in SEC rulemaking. These emissions disclosures can be reported in item 8 of the 10-k form, “Financial Statements and Supplementary Data.” IATP shares the view of the SEC’s Investment Advisory Committee that for data to be machine readable, they must be tagged according to an agreed and standardized methodology.<sup>19</sup>

A clear advantage of developing a general disclosure rule for all industries is that it can be done more rapidly. However, a general approach to disclosure, though more efficient in rulemaking, likely will be less effective in disclosing information needed by investors and other interested parties whose strategies focus on specific sectors. Another disadvantage of a general disclosure rule is, of course, the hortatory accusation that the SEC is imposing a one size fits all industries rule.

In response to question number 3, whether the SEC selects a two-digit Standard Industrial Classification (SIC) or a four-digit SIC (of a 6-digit SIC) to define industry

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<sup>14</sup> Response to question 4.

<sup>15</sup> Response to question 2.

<sup>16</sup> <https://ghgprotocol.org/>

<sup>17</sup> Thornton and Green, *op. cit.*

<sup>18</sup> “New Standard Developed to Help Financial Industry Measure and Report Emissions,” Greenhouse Gas Protocol, March 18, 2021. <https://ghgprotocol.org/blog/new-standard-developed-help-financial-industry-measure-and-report-emissions>

<sup>19</sup> “Recommendations of the Investor Advisory Committee Regarding the SEC and the Need for Cost-Effective Retrieval of Information by Investors,” Adopted July 25, 2013.

groups the selection should be a function of whether the SIC selected enables more comparable and comprehensive climate disclosures. The SIC classification system is intended to capture all business establishments, e.g. for tax policy purposes, of which SEC registrants are a subset. However, because “[t]he Office of Management and Budget (OMB) last updated the SIC in 1987,”<sup>20</sup> the SEC will have to work with OMB and the Department of Commerce to determine whether updating is required to collect and analyze information for the purpose of a climate and ESG disclosure rulemaking. The first kind of updating that comes to mind is SICs that reflect the establishment of new industries since 1987. Updating may also be required to better enable disclosure reporting and analysis from holding companies and firms with closely affiliated subsidiaries, e.g. Archer Daniels Midland and ADM Investment Services. These two entities have related but distinct disclosure profiles, e.g. ADM Investments likely would report only Scope 3 emissions, while Archer Daniels Midland would have to report all emissions and adaptation vulnerabilities, e.g. in storage, processing and transportation, that ADM Investment Services would not report.

A disadvantage of developing industry specific disclosure requirements is that it may take more time and SEC resources. However, this is a disadvantage that the SEC should embrace. The agency should work with industry groups to develop specific industry group disclosure requirements, rather than allowing (and waiting for) industry groups to lead the development of sector specific disclosure requirements.<sup>21</sup> The agency can work with industry specific ‘first movers’ to develop disclosure standards that most SEC registrants (plus eventually private equity and closely held companies) will recognize as relevant to their industries and feasible to implement.

The added granularity of industry group specific disclosure information will not only aid investors, auditors and other interested parties to assess which issuers have credible plans and investments to reduce emissions, adapt to climate change and respond to investor ESG concerns and shareholder resolutions. The added granularity will assist issuers and industry group associations in planning and investing to reduce their physical and transition risks within a disclosure framework to promote environmental justice in the communities, states and countries in which the issuers operate.

Climate change impacts different economic sectors unequally, entailing some specific sector wide disclosure reporting requirements. For example, meatpacking firms should report their annual animal processing data, because the number of animal units processed is a critical data point in estimating the SEC registrant’s per animal and total enteric methane, and manure storage methane and manure nitrous

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<sup>20</sup> “History of the NAICS Code,” NAICS Association, 2018. <https://www.naics.com/history-naics-code/>

<sup>21</sup> Response to question 3.

oxide.<sup>22</sup> Some industries have greater ESG impacts than others—e.g., chemical plants, oil refineries, meat packing plants, mining companies—that require ESG reporting for investors to compare issuers’ liability and reputational risks, personnel and benefit practices and measures to mitigate these impacts and reduce issuer ESG risks.

In sum, the Commission should tailor qualitative and quantitative disclosure requirements to SIC designated industry groups, following SIC updating by OMB. The guidance for sectoral disclosures by the Task Force on Climate Related Financial Disclosures<sup>23</sup> will also be useful for developing the disclosure rulemaking.

*Third recommendation: Ensure that all SEC registrants report their climate change adaptation vulnerabilities and their plans and investments to reduce those vulnerabilities*

All SEC registrants should disclose how they are adapting to climate change, both in qualitative narratives and in quantitative measures, in their operations and supply chains. These disclosures can be reported in item 7 of the 10-K report, “Management Discussion and Analysis of Financial Condition and Results of Operations.”

If adaptation were readily as measurable as estimated GHG reductions, perhaps adaptation would attract more corporate policy and investment commitments. SEC registrant adaptation vulnerabilities should be reported in 10-K item 1a , “Risk Factors.” The SEC should develop a disclosure rule with provisions specifically to measure adaptation vulnerabilities, planning and investments. Globally, according to a recent World Bank study, “by best existing estimates, of the total \$30 billion spent on adaptation in 2017-18, only roughly \$500 million--a mere 1.6%--came from private adaptation spending.”<sup>24</sup> The World Bank advocates public -private partnerships through its International Finance Corporation to use public funding to “de-risk” and catalyze private adaptation investment in developing countries.

The corporate and government priority on reducing emissions is to stop the momentum towards a 1.5° C world and its consequences. Four hundred and fifty-seven investor group with \$41 trillion under management stated to governments, “Strong policies, in line with limiting global warming to no more than 1.5-degrees

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<sup>22</sup> Giampiero Grossi et al, “Livestock and climate: Impact of livestock on climate and mitigation strategies,” *Animal Frontiers*, Volume 9, Issue 1, January 2019, 69–76, Figure 1.  
<https://academic.oup.com/af/article/9/1/69/5173494>

<sup>23</sup> “Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures,” Task Force on Climate-related Financial Disclosures, June 2017.  
<https://assets.bbhub.io/company/sites/60/2020/10/FINAL-TCFD-Annex-Amended-121517.pdf>

<sup>24</sup> “Unlocking Private Investment in Climate Adaptation and Resilience,” The World Bank Group, March 4, 2021.

Celsius, can accelerate and scale up private capital flows towards the net-zero transition.”<sup>25</sup> The strong implication is that governments must do the right thing before investments flow to the “net zero transition,” achieved either by reducing emissions and/or by purchasing emissions offset credits to do so. (See our remarks below on the net zero equation, and emissions trading.) IATP is perplexed about why the private sector is not as avid about making yearly adaptation commitments as it is about making ‘net zero’ commitments. Clear it is in the self-interest of SEC registrants to adapt to climate change and disclose how they are doing so.

The private sector must not wait to adapt until governments have “de-risked” their investments with government subsidies, loan guarantees and “regulatory certainty” in the uncertain climate world. If SEC registrants (and private equity and closely held companies) need “strong policies” to help them plan and invest to adapt their operations, products, supply chains and investments, the SEC can provide such “strong policies” by requiring those firms to submit annual climate adaptation plans, disclosing quantitatively and qualitatively what they have done and what they will do prior to 2030 to adapt. (Under current Business as Usual policies and practices, the onset of climate “tipping points” in 2030<sup>26</sup> will likely require major new adaptive revisions of policy, production practices, investments, to say nothing of revising the net zero commitments for 2050.)

*Fourth recommendation: monitor and stringently limit SEC registrant use of emissions offset credits and offset futures contracts to represent registrant GHG reductions to investors, auditors, insurers and other interested parties*

A fourth recommendation concerns SEC registrant use of emissions offset credits and offset futures contracts, particularly as traded in voluntary markets with no mandatory emissions cap, to claim annual and longer-term reductions of a firm’s reported emissions. Emissions offset credits and offset projects have been plagued by controversies over the scientific and accounting integrity of offset credits, human rights and environmental law violations by offset project developers, fraud and money laundering in the trading of offset credits and above all, the use of offset credits as an elaborate accounting scheme to reduce emissions on paper, while imprudently delaying a firm’s direct investment to reduce emissions.<sup>27</sup> Even

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<sup>25</sup> “2021 Global Investor Statement to Governments,” The Investor Agenda, March 2021.

<sup>26</sup> Timothy M. Lenton et al, “Climate tipping points—to risky to bet against,” Nature, Vol. 575, November 28, 2019.

<sup>27</sup> James Temple and Lisa Song, “The climate solution actually adding millions of tons of CO<sub>2</sub> into the atmosphere,” MIT Technology Review, April 29, 2021.  
<https://www.technologyreview.com/2021/04/29/1017811/california-climate-policy-carbon-credits-cause-co2-pollution/> and “Open letter to Mark Carney: Is scaling up voluntary carbon markets really what the climate needs?” Green Finance Observatory, December 22, 2020.



supporters of offset trading recognize that the quality of offset credits is poor and that “[T]reating carbon offsets as a commodity [on the futures markets] too soon will weaken the market, leading to less, not more, climate change mitigation.”<sup>28</sup>

The Task Force on Scaling Voluntary Carbon Markets (TSVCM) proposes to reduce the scientific integrity problems of offset projects with remote sensing technology and the accounting integrity problems with digital ledger technology and know your customer guidance.<sup>29</sup> Nevertheless, the Task Force has major disagreements among its members, that are emblematic of the difficulties in using offsets to ‘reduce’ emissions.<sup>30</sup> The final report will be the basis for pilot testing a TSVCM offset futures contract in late 2021.

The TSCVM estimate of global biogenic carbon offset potential, mostly for offset projects in a handful of developing countries, requires downward revision. According to a March 2021 scientific article on the over-estimation of CO<sub>2</sub> sequestration potential, “The future of the land sink, especially SOC [soil organic carbon] is particularly uncertain.”<sup>31</sup> The land sink is the fundamental resource underlying any and all land-based emissions offset projects that are, in turn, the underlying assets of emissions offset credits and offset futures contracts. And, as a matter of science, emissions from the long-term geological carbon cycle are not offset by nor can be equated with the short-term sequestration of biogenic carbon.<sup>32</sup> Notwithstanding climate science, promoters of offset credit and offset futures trading anticipate a trading boom.

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<https://greenfinanceobservatory.org/2020/12/22/is-scaling-up-voluntary-carbon-offset-markets-really-what-the-climate-needs/>

<sup>28</sup>“Comments on the Initial Recommendations of the Taskforce on Scaling Voluntary Carbon Markets (TSVCM).”, Carbon Direct, (carbon) Plan and Berkeley Carbon Trading Project, January 5, 2021, at 5. [https://carbon-direct.com/wp-content/uploads/2021/02/Carbon-Direct\\_Carbon-Plan\\_Berkeley-Carbon-Trading-Project\\_TSVCM-Comments-1.pdf](https://carbon-direct.com/wp-content/uploads/2021/02/Carbon-Direct_Carbon-Plan_Berkeley-Carbon-Trading-Project_TSVCM-Comments-1.pdf)

<sup>29</sup> A partial response to question 5.

<sup>30</sup> E.g. Jeff Shankleman and Akshat Rathi, “Wall Street’s Favorite Climate Solution Mired in Disagreements,” Bloomberg Green, June 2, 2021, and Steve Suppan, “Making carbon trading globally legitimate: The road show has begun,” Institute for Agriculture and Trade Policy, December 16, 2020.

<sup>31</sup> Carlos Terrer et al, “A trade-off between plant and soil carbon storage under elevated CO<sub>2</sub>,” *Nature*, Vol. 591, March 25, 2021. <https://www.nature.com/articles/s41586-021-03306-8>

<sup>32</sup> James Dyke, Robert Watson and Wolfgang Knorr, “Climate scientists: concept of net zero is a dangerous trap,” *The Conversation*, April 22, 2021, <https://theconversation.com/climate-scientists-concept-of-net-zero-is-a-dangerous-trap-157368> and Doreen Stabinsky, “Chasing Carbon Unicorns: The deception of carbon markets and ‘net zero,’” Friends of the Earth International, February 22, 2021. <https://www.foei.org/resources/publications/chasing-carbon-unicorns-carbon-markets-net-zero-report>

At a June 3 meeting of the Commodity Futures Trading Commission's Energy and Environmental Markets Advisory Committee (EEMAC), representatives of the Chicago Mercantile Exchange (CME) Group, the Nodal Exchange and the Intercontinental Exchange in London reported a great interest among market participants in using offset credit and offset futures trading to claim emissions reductions.<sup>33</sup> A representative of the California Air Resource Board (CARB) said that only 4% of emissions reductions for CARB compliance market entities could be achieved through the buying and selling of offset credits. In voluntary markets developed per the TSVCM proposal, there would be no enforceable limit to the use of offset futures and "customized" offset OTC contracts to claim emissions reductions.

The SEC does not have regulatory authority over emissions offset credits or offset futures trading, as the Commodity Futures Trading Commission (CFTC) does. Nevertheless, SEC registered companies are or are planning to trade offset credits and/or offset futures contracts to claim emissions reductions. Investors and broker dealers, particularly those marketing ESG investment products, will want to know about the investment quality of offset contracts, as well as the amount invested in them by SEC registrants, relative to the firms' capital allocation plans and programs for directly reducing their Scope 1, 2 and 3 emissions. They will want to know about the firms' liability and credit risks if either the underlying assets of their offset credits, i.e. emissions offset projects, and/or futures contracts are shown to lack environmental and/or accounting integrity or to have violated human rights and/or environmental laws. Investors will want to know whether any SEC registrant investments in purportedly permanent carbon sequestration (e.g. Direct Air Capture and Storage) were preceded by analysis of the possible consequences of technological or commercial failure of such investments. Investor and auditors will want to review if an SEC registrant's offset futures and offset credit trading strategy is coordinated with a plan to reduce registrant emissions directly or whether that trading is a profit center without a demonstrated plan or capacity to reduce emissions.

Here is a short illustration about the potential for market and capital formation disruption if technical failure or fraud in the underlying assets of offset credits and offset futures result in credit, liability and/or reputation risks for the SEC registrant that relies on offsetting for a major part of its claimed emissions reductions. IATP analyzed the CME's Global Emissions Offset (GEO) futures contract to understand the terms of the contract and why the CFTC staff allowed the CME to self-certify the consistency of the contract with CFTC rules, rather than to seek formal approval for a novel, second-generation offset futures contract unconnected to any emissions

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<sup>33</sup> To access the webcast of the EEMAC meeting, plus slide decks of the presenters, please go to <https://www.cftc.gov/PressRoom/Events/opaeventeemac060321>

reductions cap.<sup>34</sup> (The Commodity Futures Modernization Act of 2000 allows trading platforms to self-certify their new products, leading to a huge increase in new contracts that an understaffed CFTC cannot formally review and approve or reject from entry into trade.)

The underlying asset of the GEO futures contract is a price index of emissions offset credits accepted by the Carbon Offset and Reduction Scheme in International Aviation (CORSIA). If one or more of the eight offset credit verification registries, e.g. the United Nations' controversial Clean Development Mechanism<sup>35</sup>, approved by the International Civil Aviation Organization in March,<sup>36</sup> validates credits from fraudulent offset projects, or even projects that misrepresent emissions reductions, the price of those offset credits would fall. Those SEC registrants holding positions in fraudulent or deceptive CORSIA validated emissions offset credits would, at the least, suffer reputational risk, and perhaps liability and credit risks, at least among ESG investors.

SEC staff should develop a cooperative agreement with the CFTC to better understand the new offset products, trading volumes and trends, and excessive speculation and market events involving offset futures contracts and their underlying assets. SEC staff could question CFTC staff about ongoing development in offset futures and OTC trading, e.g. concerning automated trading and short selling of those contracts.

IATP believes that emissions offset contracts, particularly those trading in voluntary markets, pose risks to investors and other interested parties that should be reported to the SEC under item 1a "Risk Factors". A SEC registrants' expenditures on offset project development and offset credit and futures trading should be reported in item 7-a, "Quantitative and Qualitative Disclosures About Market Risk."

*Fifth recommendation: to enhance investor protection and capital market integrity, apply climate and ESG disclosure requirements to private equity and closely held companies currently exempt from SEC registrant recordkeeping, reporting and other requirements*

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<sup>34</sup> Suppan, "What underlies the underlying (asset) of CO<sub>2</sub> emissions offset futures contracts?" Institute for Agriculture and Trade Policy, March 31, 2021.

<sup>35</sup> E.g. "End the CDM," Carbon Market Watch, November 15, 2018. Carbon Market Watch, <https://carbonmarketwatch.org/2018/11/15/end-the-cdm/>.

<sup>36</sup> "ICAO Identifies Six Eligible Carbon Offsetting Programs for Aviation Industry," SDG Knowledge Hub, Institute for Sustainable Development, March 24, 2020. <https://sdg.iisd.org/news/icao-identifies-six-eligible-carbon-offsetting-programmes-for-aviation-industry/>

Our fifth recommendation is that the SEC develop climate disclosure requirements for SEC listed companies that can be quickly applied to private equity and debt firms following the withdrawal of their exemptions from SEC registration and reporting requirements. According to a financial disclosure advocates' letter sent on May 26, 2020 to SEC Chairman Jay Clayton, "In fact by 2019, nearly 70 percent of capital was raised outside of the SEC's public registration and disclosure regime."<sup>37</sup> Bloomberg reports that there are twice as many private equity-controlled companies as publicly listed companies.<sup>38</sup>

Chair Gary Gensler told NGOs in a recent Zoom call that SEC staff had begun a private equity and debt market analytical and regulatory workstream. Although the SEC cannot require mandatory disclosures of firms that are not SEC registered, the Commission should advise private equity and closely held firms that they should prepare to submit disclosures similar to what will be required of SEC registered firms, in anticipation of the application of disclosure requirements following the finalization of a rulemaking that removes private equity exemptions from SEC registration, reporting and requirements.

If private equity and closely held firms remain exempt from climate risk disclosure, not only will the SEC and investors have a very incomplete picture climate risk across economic sectors, but SEC listed firms may reorganize as private equity entities to avoid disclosure requirements, exacerbating the current unfair regulatory arbitrage advantages of private equity.

*A mini-case study on issues that may arise in industry group reporting, illustrated by the agribusiness sector*

In 2018, IATP co-authored a report that used the UN Food and Agriculture Organization's GLEAM methodology to estimate the emissions of 35 transnational meatpacking and dairy processing companies. A topline conclusion of the report was: "Together, the world's top five meat and dairy corporations are now responsible for more annual greenhouse gas emissions than ExxonMobil, Shell or BP."<sup>39</sup> But perhaps more important than what could be estimated using the GLEAM

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<sup>37</sup> <https://sites.duke.edu/thefinregblog/2020/05/26/letter-to-sec-on-corporate-transparency-and-accountability-and-the-coronavirus-pandemic/> at 4.

<sup>38</sup> "Everything is private equity now," Bloomberg Business Week, October 8, 2019. <https://www.bloomberg.com/news/features/2019-10-03/how-private-equity-works-and-took-over-everything>

<sup>39</sup> "Emissions Impossible: How big meat and dairy are heating up the planet," Institute for Agriculture and Trade Policy and GRAIN, July 2018 at 2. <https://www.iatp.org/sites/default/files/2018-08/Emissions%20impossible%20EN%2012.pdf>

methodology was the vast underreporting or non-reporting of meat and dairy processing Scope 3 emissions: “Fourteen of the 35 companies have announced some form of emission reduction targets. Of these, only six have targets that include supply chain emissions, yet these emissions can account for up to 90% of total emissions. The six companies that do pledge cuts in supply chain emissions are simultaneously pushing for growth in production and exports, driving their overall emissions up regardless of their intention to reduce emissions per kilo of milk or meat produced.”<sup>40</sup> The strategy of pledging cuts emissions while increasing production and exports rests on the use of emissions offset credits towards achieving the accounting goal of “net zero” emissions by 2050.

As one would expect, the meat and dairy industry have criticized both IATP’s estimates and the FAO methodology used to make them. For example, both the International Dairy Federation and the Global Dairy Platform, criticized our emissions estimates of 13 top global dairy firms in a June 2020 report, “Milking the Planet.”<sup>41</sup> The industry associations contend that the estimates failed to take into account the impact of mergers and acquisitions on individual company emissions. We responded, inter alia:

Our data shows that the milk processed by the 13 corporations went up by 8% in two years and their emissions went up by 11%. We compared the emissions these companies were responsible for between 2015 and 2017. The increase in their milk intake and emissions is significant and merits global attention. How much of that increase is due to mergers and acquisitions rather than an increase in the number of animals producing milk is unclear due to lack of corporate transparency in publicly reporting these figures. Making public 1) the number of total additional animals producing milk per company and 2) the number of additional milk-producing animals due to mergers and acquisitions would provide a useful set of data points for further analysis. Our calculations, indeed, include mergers and acquisitions because companies and their investors **must own the climate footprint and risk** they add to their operations due to mergers and acquisitions.<sup>42</sup>

The climate risk point of this illustration is not that IATP’s estimates are irreproachable, but that the lack of corporate transparency in reporting climate risks, when they are reported at all, results in disputes that likely will delay making long-term investments to reduce those risks.

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<sup>40</sup> Ibid.

<sup>41</sup> Shefali Sharma, “Milking the planet: How Big Dairy is heating the planet and hollowing rural communities,” Institute for Agriculture and Trade Policy, June 15, 2020.

<sup>42</sup> Sharma, “Questions and Answers: Milking the Planet,” Institute for Agriculture and Trade Policy, March 25, 2020.

In general, agriculture is one of the economic sectors most vulnerable environmentally and financially to climate change. Estimates of physical risks and costs to U.S. agricultural production from climate related disasters have benefitted by U.S. federal measurements and reporting of climate change impacts. Geo-spatial mapping of U.S. Drought Monitor data, combined with commodity specific crop insurance indemnifications, produce county level data on estimated crop losses, crop yield losses and the costs to both farmers and tax-payer subsidized crop insurers, annually or over longer periods.

For example, during the widespread and severe U.S. drought of 2012, crop indemnification payments due to drought-related crop losses or reduced yields amounted to about \$16 billion. But because row crop insurance policies indemnify 10-15% less than the full value of crops or crop yields lost to drought, the overall costs to U.S. row crop farmers is higher.<sup>43</sup> However, according to the Fourth National Climate Assessment, the Business as Usual solution to drought—irrigation—may no longer be available in some parts of the United States: ““Expanded irrigation is often proposed as a strategy to deal with increasing crop water demand due to higher trending temperatures coupled with decreasing growing-season precipitation. However, under long-term climate change, irrigated acreage is expected to decrease, due to a combination of declining water resources and a diminishing relative profitability of irrigated production.”<sup>44</sup> Climate change related subsidies to U.S. farmers and ranchers pass through farmers and ranching operations to pay crop and livestock insurance brokers, input dealers, machinery dealers, agricultural data service, crop consultants, commodity brokers, diesel fuel providers and other food and agricultural system firms that only now are starting to reckon with their climate financial risks.

Whether investor groups are demanding such climate risk information of agribusiness as they are demanding it of other sectors is a hard question to answer. When the Climate Action 100+ investor group contracted with the Transition Pathway Initiative (TPI) to evaluate climate disclosure assessments provided by 167 of the largest industrial emissions companies, just seven of them (Bayer Ag, Bunge, Coca Cola, Danone, Nestlé, Unilever and Walmart) by our count were, in part or whole, involved in agribusiness or food processing. According to TPI, four companies satisfied two of ten disclosure criteria, two satisfied four criteria and one satisfied no criteria. The most frequently satisfied criterion among the seven

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<sup>43</sup> E.g., David Rodziewicz and Jacob Dice, “Drought Risk in the Agriculture Sector,” *Economic Review*, Federal Reserve Bank of Kansas City, Chart 2, December 3, 2020.  
<https://www.kansascityfed.org/research/economic-review/v105n2Rodziewicz-Dice-drought-risk-agriculture-sector/>

<sup>44</sup> *Fourth National Climate Assessment*,  
[https://nca2018.globalchange.gov/downloads/NCA4\\_Ch10\\_Agriculture\\_Full.pdf](https://nca2018.globalchange.gov/downloads/NCA4_Ch10_Agriculture_Full.pdf) at 400.

companies was “climate governance.” Only six of 167 companies had capital investment plans that aligned with their goals to achieve net zero emissions.<sup>45</sup>

Only 12% of agribusiness and forestry firms that responded to The Task Force on Climate Disclosures survey in 2017, plus another 130 companies evaluated by State Street Global Advisors, disclosed their climate related financial risks and opportunities to TFCF expectations: “Overall, we found that there is little to no disclosure around the actual and potential impacts of climate related risks and opportunities on the organization’s specific businesses, strategy, and financial planning.”<sup>46</sup>

Data on the financial cost of physical risks to individual agribusiness firms from extreme weather events is not readily disaggregated, accessible or attributable to climate change impacts. For example, in September 2018, Hurricane Florence killed about 5,500 hogs and breached or over-topped 132 hog manure lagoons of farmers producing for Smithfield’s hog slaughtering facility (closed before the hurricane struck) in North Carolina.<sup>47</sup> U.S. federal agencies compensated Smithfield contracted farmers for their losses, including their losses of hogs and the corn and soy production used to feed the hogs. The North Carolina Department of Agriculture’s preliminary estimate of hog related losses from that one disaster was about \$500 million.<sup>48</sup> (Nobody compensated North Carolinians for the fish kills and public health costs of manure contaminated water.)

Given the history of hurricane damage to North Carolina agriculture and the increasing incidence and intensity of hurricanes on the U.S. East Coast,<sup>49</sup> a reasonable investor should assume that Smithfield will face greater physical and transitional risk from hurricanes, particularly if the liability terms in hog producer contracts shift any terms of risk from Smithfield-contracted hog farmers to Smithfield, and to its corporate parent, the Hong Kong-based Shuanghui (aka WH Group). A typical industry contract states, “You bear all risks of production of

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<sup>45</sup> “Companies,” Climate Action 100+, <https://www.climateaction100.org/whos-involved/companies/> and “2020 Progress Report,” <https://www.climateaction100.org/wp-content/uploads/2020/12/CA100-Progress-Report.pdf>

<sup>46</sup> Rahki Kumar, “Effective Climate-Risk Disclosure in the Agriculture and Forestry Through the Lens of the Task force on Climate Disclosures,” State Street Global Advisors, March 2019.

<sup>47</sup> Steve Suppan, “Bailing out a Chinese-owned, U.-located corporate subsidiary,” Institute for Agriculture and Trade Policy, October 4, 2018.

<sup>48</sup> [https://files.nc.gov/ncosbm/documents/files/Florence\\_Agriculture\\_rev20181026.pdf](https://files.nc.gov/ncosbm/documents/files/Florence_Agriculture_rev20181026.pdf) at 29.

<sup>49</sup> E.g. Jeff Berardelli, “Climate change is making hurricanes more dangerous,” Yale Climate Connections, July 18, 2019.

market hogs until delivery to our plant and acceptance of hogs by us.”<sup>50</sup> Where do climate risks lie in Smithfield, beyond in the farmer’s take it or leave it contracts? In 2013, when Smithfield was acquired by Shuanghui, whose investors included Goldman Sachs, New Horizon Capital, Kerry Group, CDH Investors, Temasek, Peter Fuhrman of China First Capital wrote, “A Chinese company isn’t buying Smithfield. A shell company in the Cayman Islands is.”<sup>51</sup>

Smithfield represents itself as an environmentally sustainable corporation, claiming to reduce its GHG emissions 30% by 2030 along its value chain.<sup>52</sup> Currently Smithfield’s 10-K report risk line item provides no quantified estimate of its physical risks from climate change and only the barest qualified statement on its physical and transitional risks:

Natural disasters, such as flooding and hurricanes, can cause the discharge of effluents or other waste into the environment, potentially resulting in our being subject to further liability claims and governmental regulation as has occurred in the past. See “Item 1. Business—Regulation” for further discussion of regulatory compliance as it relates to environmental risk. We have incurred, and will continue to incur, significant capital and operating expenditures to comply with these laws and regulations.<sup>53</sup>

Such a terse description of Smithfield’s risks are wholly inadequate to describe its serial environmental regulatory violations (and the fines paid), the litigation related to its operations (and the cost of settling the lawsuits), worker safety and health violations and Smithfield’s increasing climate related vulnerabilities. Smithfield is far from alone among even just meatpacking firms in minimizing its risk disclosures to investors. But this information minimalization is untenable, particularly in the global climate change and agriculture context in which transnational agribusiness operates.

The most recent meta-study estimates that food system GHGs account for about a third of global anthropogenic emissions. Of that portion  $\frac{3}{4}$  derive from food system activities from pre-production (e.g. production of inputs) to primary agriculture to post-production activities (e.g. processing, packaging, transporting). The other  $\frac{1}{4}$  of

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<sup>50</sup> [http://www.fao.org/fileadmin/user\\_upload/contract\\_farming/samples/Hormel-8.pdf](http://www.fao.org/fileadmin/user_upload/contract_farming/samples/Hormel-8.pdf)

<sup>51</sup> Cited in Shefali Sharma, “*Two Converging Rivers: Understanding Shuanghui’s Acquisition of Smithfield*,” Institute for Agriculture and Trade Policy, June 6, 2013.

<sup>52</sup> <https://sustainability.smithfieldfoods.com/>

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<https://www.sec.gov/Archives/edgar/data/91388/000009138816000064/a201510k.htm#s81A7B2C2B1EA521898776F6A31EACD8B> at 15.



food system GHG production results from land use change for agricultural production.<sup>54</sup> The authors claim their data shows “conventional IPCC [International Panel on Climate Change] categories, used by countries to report emissions in the National GHG inventory, systematically underestimate the contribution of the food system to total anthropogenic emissions.”<sup>55</sup> As GHG measuring technology and accounting methodology becomes more precise and rigorous, the percentage of GHGs attributed to agriculture, particularly in the high global warming potential gases methane and nitrous oxide, are likely to increase under current trends.<sup>56</sup>

One reason for a systematic underestimation of agricultural underestimated of GHGs is methodological, e.g. excluding the agricultural supply chain (Scope 3) emissions that food system captures. Another reason could be that countries underestimate food system emissions because their agribusinesses underestimate or don’t report their emissions.<sup>57</sup> Since the United States does not regulate methane and nitrous oxide emissions from the burgeoning number and increasing size in animal units of Concentrated Animal Feeding Operations<sup>58</sup>, disclosure of such emissions to the SEC may be the next best, albeit indirect, means to reduce agribusiness emissions.

## *Conclusion*

IATP thanks the Commission for its consideration of this input. If the Commission votes to accept the staff proposal for a rulemaking on climate risk disclosure,<sup>59</sup> IATP will provide comments at all stages of the rulemaking. Although the SEC’s rulemaking agenda is large, varied and complex, there is perhaps no single rulemaking that will serve investors, sustainable capital market formation and the public interest more than the implementation of a robust climate risk and ESG disclosure rule.

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<sup>54</sup> Francesco N Tubiello *et al*, “Greenhouse gas emissions from food systems: building the evidence base 2021 *Environ. Res. Lett.* **16** 065007 at 1. <https://iopscience.iop.org/article/10.1088/1748-9326/ac018e/pdf>

<sup>55</sup> *Ibid.*

<sup>56</sup> “United Nations Methane Report Underscores Need to Regulate Emissions from Big Meat and Big Dairy to Respond to Climate Crisis,” Institute for Agriculture and Trade Policy, May 6, 2021.

<sup>57</sup> E.g. Zoe Dean “Climate Commission more concerned about placating dairy industry than tackling climate crisis,” Greenpeace Aotearoa, June 9, 2021.

<sup>58</sup> E.g., Christopher Walljasper, “Large animal feeding operations on the rise: Several states see shifts in animal production since 2011,” Midwest Center for Investigative Reporting, June 7, 2018. <https://investigatamidwest.org/2018/06/07/large-animal-feeding-operations-on-the-rise/>

<sup>59</sup> <https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=202104&RIN=3235-AM87>

