Center On Executive Compensation

VIA Electronic Delivery

Hon. Gary Gensler
Chair
Securities and Exchange Commission
100 F St., NE
Washington, DC 20549

RE: Comments on ESG Disclosures

Dear Chair Gensler:

The Center On Executive Compensation ("Center") is pleased to submit comments to the Securities and Exchange Commission ("SEC") providing its perspective on a prescriptive disclosure regime for Environmental, Social, and Governance ("ESG") data, specifically data related to human capital metrics ("HCM") or diversity and inclusion ("D&I").

The Center believes the current principles-based HCM disclosure framework adopted in 2020 provides an excellent and workable solution for all contemplated ESG, HCM, and D&I disclosures. Through this rule, companies are already required to disclose material information.

Additionally, investors have effective mechanisms with which to engage with Boards and management regarding additional ESG disclosures. These mechanisms have been widely used and resulted in additional disclosures sought by the investor community. Specifically, in 2020, 56 shareholder proposals requesting enhanced climate risk disclosures were withdrawn upon the company agreeing to provide the requested information following engagement with the proponent.[1] Given the effectiveness of the current system, imposing a prescriptive disclosure approach will fail to provide any additional benefits while at the same time presenting considerable risks and downside.

A prescriptive list of required data point disclosures – which cannot account for the unique characteristics of a particular company or industry – would effectively undermine the SEC's contemplated objective of improving the availability and usefulness of *relevant and material* disclosures. Only a principles-based approach allows companies and investors to effectively engage regarding which data points are relevant and material to each unique company and its long-term growth.

Implementing a prescriptive disclosure requirement would likely result in companies providing partially or wholly irrelevant data with far fewer cases of increasing useful and relevant disclosures. At worst, the resulting disclosures could be *misleading*, forcing companies to potentially provide additional correctional disclosure. Such a scenario runs counter to the fundamental principles of the federal disclosure regime.

We urge the Commission to continue to emphasize and enforce the existing principles-based rules currently in place and refrain from further rulemaking.

The Center is a research and advocacy organization that seeks to provide a principles-based approach to executive compensation policy from the perspective of the senior human resource officers of leading companies. The Center is a division of HR Policy Association, which represents the chief human resource officers of nearly 400 large companies, and the Center's more than 145 subscribing companies are HR Policy members who represent a broad cross-section of industries.

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[1] Berridge, Rob, "How climate proposals fared during the 2020 proxy season", September 14, 2020. Accessed: June 11, 2021 at https://www.ceres.org/news-center/blog/how-climate-proposals-fared-during-2020-proxy-season

Following are the Center's views regarding the SEC's Questions for Consideration: **#1, #3, #8, and #12**.

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?*

Disclosures should be built upon a principles-based framework with guidance from the SEC where necessary to ensure comparability of the most material metrics. ESG risks and opportunities are shifting from "niche" to primary concerns and various metrics are being developed (and discarded) in real time. Given the pace of these developments, the SEC should monitor the disclosures over time and provide additional guidance if market-developed disclosures and metrics are proving confusing, opaque, or immaterial. To date, however, investors have demonstrated a clear ability to engage and influence companies to craft additional disclosures which the investor community feels are relevant and material.[2]

If the Commission proceeds, companies should be able to provide the disclosure where they feel it makes the best logistical and thematic sense, whether that is in the current Form 10-K or the annual proxy statement.

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.)?*

The advantages of permitting investors and companies to work together – whether that be individually or in industry-specific groups – to mutually develop disclosure standards are very clear. *Only* through such an effective and market-driven process will the resulting disclosure be relevant and meaningful to the participating company thus providing the information and value sought by the investor community. A prescriptive approach on the other hand does not provide such benefits and a company's disclosure is as likely to be irrelevant or misleading as it is helpful.

The Commission has already set out minimum disclosure standards by requiring companies to disclose all material information related to ESG-related issues, including HCM. Given the effectiveness of engagement between companies and investors on ESG-related issues and the rapidly evolving nature of ESG-related disclosures, the Commission should refrain from implementing further ESG-related disclosure standards and instead continue to monitor the ongoing development of ESG disclosure issues.

However, if the Commission were to determine to implement a minimum disclosure framework, a company's participation – individually or as part of an industry-specific group – to engage and develop

[2] In 2018, Arjuna Capital filed proposals at 23 companies in the tech, financial and consumer sectors. The firm withdrew 22 of those after receiving commitments from the targeted companies to disclose more information about pay gaps and make commitments to closing them going forward. Mitchell, Patrick. "Press Release" April 24, 2019. Accessed on June 14, 2021 at http://arjuna-capital.com/news/press-releasegender-pay-causes-stir-at-wells-fargo-bank-of-america-meetings-disclosing-median-gender-pay-gap-receives-strong-support-from-shareholders/

disclosure standards on issues identified by investors should be considered as satisfying any established minimum disclosure standards.

On defining industry categories, if an effective silver bullet existed, the Center would certainly endorse its use. Unfortunately, relying on SIC – whether that be two or four digit – often results in mismatches and erroneous classifications. Therefore, the Center urges the Commission to continue to permit companies and investors to work together to establish disclosure frameworks organically.

8. *How, if at all, should registrants disclose their internal governance and oversight of climate-related issues? For example, what are the advantages and disadvantages of requiring disclosure concerning the connection between executive or employee compensation and climate change risks and impacts?*

Any requirement to disclose the internal governance and oversight of ESG issues should adhere strongly to the materiality standard. Investors have demonstrated they are perfectly willing to vote in opposition to management where they feel that boards are not disclosing or displaying sufficient oversight of ESG risks and opportunities.

Investors are increasingly engaging with companies about sought-after performance improvements in enhancing diversity and inclusion or reducing climate risk. Several companies have found that linking ESG performance to executive compensation is effective for clarifying goals and communicating priorities, but each company approaches this differently based upon culture, strategic goals, and long-term objectives.

Companies are already making far more in-depth disclosures about executive compensation than required by the Commission, including quantitative and qualitative performance metrics, payout rationale, and discussion on how executive compensation is tied to company strategy. The market is already adjusting to incorporating ESG performance into this compensation framework.[3] Such a principles-based framework should be maintained as it has demonstrated its effectiveness in the market today.

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?*

If a company and its investors determine that disclosure of a specific ESG metric is not material or is competitively sensitive, it is reasonable to state that as a rationale for not providing the specific disclosure. Maintaining and enforcing the currently implemented principles-based materiality approach to ESG disclosures would avoid the need for any additional "comply or explain" requirement entirely.

Conclusion

We fully endorse the Commission's efforts to solicit the input of investors, companies, and other stakeholders on the topic of ESG disclosures. We support the existing principles-based approach to these disclosures as it provides the needed flexibility for companies to craft disclosures that accurately represent their approach to ESG topics and educate investors on company efforts.

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[3] Kalfen, Donald. "Meridian Study on Use of ESG Metrics in Incentive Plans". May 25, 2021. Accessed June 14, 2021 at https://www.meridiancp.com/insights/meridian-study-on-use-of-esg-metrics-in-incentive-plans/

Companies and investors have already proven very effective at coming together to identify and create disclosures on ESG and HCM-related issues. We would urge the Commission to refrain from additional action and continue to permit investors and companies to work together to determine and disclose which ESG risks, opportunities, and metrics drive or inhibit growth and are therefore material and relevant.

Thank you for the opportunity to provide the Center On Executive Compensation's perspective in response to the Commission's request for public input on ESG disclosures.

Sincerely,

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Center On Executive Compensation

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Center On Executive Compensation