California Public Employees' Retirement System
Executive Office
400 Q Street, Sacramento, CA 95811 |Phone: (916) 795-3829 | Fax: (916) 795-3410
888 CalPERS (or **888**-225-7377) | TTY: (877) 249-7442 | **www.calpers.ca.gov**

Vanessa Countryman, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0609

Via email: rule-comments@sec.gov

June 12, 2021

Subject: The Securities and Exchange Commission's Request for Public Input on Climate-related Financial Disclosure

Dear Ms. Countryman,

On behalf of the California Public Employees' Retirement System (CalPERS), I write to express our views on the Securities and Exchange Commission's (SEC's or Commission's) request for public input on climate-related financial disclosure.

As the largest public defined benefit pension fund in the United States, CalPERS manages approximately $465 billion in global assets. We seek long-term sustainable, risk-adjusted returns through efficient capital allocation and stewardship in line with our fiduciary duty. CalPERS' motivation to address climate change is to ensure we address both risks and opportunities to ensure we can provide benefits in retirement, disability and health for our 2 million members. For every dollar that we pay in benefits, 55 cents come from investment returns. We are guided by CalPERS' Investment Beliefs[1] which recognize that "Long term value creation requires effective management of three forms of capital: financial, physical and human."[2] Accordingly, we expect fair, accurate, timely, and assured reporting about how companies manage their financial, physical and human capital to generate sustainable returns, and how they identify, monitor, and mitigate risks to those three forms of capital.[3]

Climate change is a systemic risk, so it is critical that investors can access clear disclosures of the risks it poses to long-term value creation by the companies in which they invest. Effective

[1] CalPERS Investment Beliefs, https://www.calpers.ca.gov/page/about/organization/calpers-story/our-mission-vision#investment-beliefs.
[2] Id.
[3] CalPERS Sustainability Principles. https://www.calpers.ca.gov/docs/forms-publications/governance-and-sustainability-principles.pdf

disclosures facilitate informed decision-making by providing transparent and relevant data on the economic performance and condition of a business. We expect companies to provide integrated representations of operational, financial, environmental, social, and governance performance in terms of both financial statement and non-financial statement results and prospects. However, the current disclosure regime for corporate reporting falls short of our expectations as investors, and we believe that companies should disclose better information in regulatory reports so that shareowners can more easily identify, assess and manage climate risk and opportunity.

CalPERS has long recognized the scale and multi-faceted nature of climate change, which poses opportunities and risks to our global portfolio across public and private markets. Scientific evidence demonstrates that reducing greenhouse gas (GHG) emissions is critical to slowing global warming and driving sustainable economic growth. Physical impacts pose short and long-term risks to our members' assets. These risks include rising sea levels, floods, severe storms, drought, and wildfires. Dramatic changes to the global energy economy, particularly as the world recovers from COVID-19, also pose transition risks as companies are challenged to adopt new strategies. In addition, companies are increasingly vulnerable to litigation. For investors navigating the complexity of climate change, it is essential to have detailed scenario-based corporate disclosures regarding the potential impact of both the transition and physical risks to companies' performance across time to help investors properly evaluate potential return on investment and to make informed comparisons among investment opportunities.

CalPERS has a long history of addressing the risks and opportunities of climate change through advocacy, engagement, research and integration of climate risk across the portfolio, supported by partnerships, as in Climate Action 100+ which we convened and co-founded. In 2016, our Board of Administration approved a 5-year Strategy for Sustainable Investment[4] which reflects the relevance of climate as a critical driver of risk and return to our portfolio. Guided by deep research, we advocate with regulators for sound public policy and corresponding high-quality standards for mandatory climate risk reporting, which is consistent, comparable, and reliably assured.

We have also supported the development of voluntary standards and reporting frameworks such as the Task Force on Climate-related Financial Disclosures (TCFD) to capture the risks and opportunities driven by climate change, climate policy, and emerging technology.[5] We carefully monitor material climate risks our portfolio companies face and used the TCFD framework for our own climate risk report titled the *CalPERS' Investment Strategy on Climate Change*.[6] We engage companies directly on their policies and plans to reduce GHG emissions and manage physical and transition risks. This includes targeted company engagements with those identified as "systemically important carbon emitters" supported through partnerships such as the Climate Action 100+ and the United Nation's Net Zero Asset Owner Alliance. Finally, we seek to integrate climate risk and opportunity into our investment decision-making across our portfolio. This includes establishing external manager expectations and reporting requirements and

[4] CalPERS 5-Year Sustainability Strategy. https://www.calpers.ca.gov/docs/board-agendas/201911/invest/item11b-01_a.pdf

[5] TCFD Website. https://www.fsb-tcfd.org/

[6] CalPERS' Investment Strategy on Climate Change June 2020, https://www.calpers.ca.gov/docs/board-agendas/202006/invest/item08c-01_a.pdf

curating research based on scientific data and evidence-based economic insights through our Sustainable Investment Research Initiative[7] and related projects to develop new tools for investment analysis, such as the Physical Risks of Climate Change reporting framework based on meteorological data.[8]

Given our extensive history of advocacy, engagement and integration through partnerships around the effective management of climate risk, we commend the SEC for its efforts to prioritize and modernize climate-related financial disclosures. The recent market volatility and trends resulting from the pandemic including its impact on climate cannot be ignored by investors. The pandemic has demonstrated with brutal clarity that tackling a systemic risk requires global cooperation and involves both the public and private sectors, driven by innovation at pace and scale.

The current trend towards progress in the management of climate risk is promising. For example, the new 2021 Federal Administration's priorities include climate.[9] The global movement on climate risk management continues to build with the IFRS Foundation's creation of an International Sustainability Standards Board (ISSB) being the most significant example. It is also notable that the International Accounting Standards Board has issued guidance that promotes including relevant climate risk consideration in financial statements.[10] This is an important development and one U.S. policymakers should consider in relation to accounting and audit.

In our thinking around the critical role of regulation in addressing climate risk, we return to a speech to the National Securities Administrators in 1949, SEC Commissioner, Hon. Harry A. McDonald stated, "The phrase 'in the public interest and for the protection of investors' appears repeatedly in the Federal securities acts. It is found in many of the State blue sky laws. Principally, 'the public interest' is the ultimate touchstone of all we do in the regulatory field."[11] For investors, for capital formation and in the public interest, the Commission needs to move swiftly and decisively to provide the rules which will ensure the management and mitigation of a systemic risk.

We appreciate the opportunity to provide comments on the SEC's regulation of climate-related reporting requirements for U.S. issuers in the context of an integrated disclosure system. Our detailed responses to each question are provided in the attached appendix.

---

[7] CalPERS SIRI Library. https://www.calpers.ca.gov/page/investments/sustainable-investments-program/esg-integration/siri-library

[8] CalPERS and Wellington. 2020. *Physical Risks of Climate Change (P-ROCC)*. https://www.wellington.com/uploads/2019/10/e01e2a4ed6fce336dce93f86f0af9883/physical-risks-of-climate-change_procc_framework.pdf

[9] Biden Administration Priorities. https://www.bu.edu/articles/2021/bidens-top-four-priorities-explained-by-leading-bu-experts/ (Covid-19, the economy, racial equality, climate change)

[10] Anderson, N. 2019. IFRS Standards and Climate Related Disclosures. https://www.ifrs.org/content/dam/ifrs/news/2019/november/in-brief-climate-change-nick-anderson.pdf

[11] McDonald, H.A. 1949. *Small Issues and the Public Interest.* Speech to National Association of Securities Administrators. https://www.sec.gov/news/speech/1949/071149mcdonald.pdf

We look forward to providing continued support to the Commission. Please contact Anne Simpson, Managing Investment Director, at [redacted] if you have any questions or would like to discuss our response.

Sincerely,

Marcie Frost
Chief Executive Officer

cc: Anne Simpson

Appendix

Questions for Consideration

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 has previous work to refer to. In 2010, the SEC issued "Commission Guidance Regarding Disclosure Related to Climate Change."[12] (2010 Climate Guidance). However, there has been little response from issuers. At this point, it is clear that the Commission must develop mandatory disclosure rules with line-item reporting which provide issuers with clarity on what is expected by investors on climate risk reporting.

The Commission is best placed to regulate, monitor, review, and guide standards for mandatory climate risk reporting directly. We do not see this as an appropriate role for a third party or outside body as it is fundamental to the SEC's investor protection, capital formation and public interest responsibilities.

Moreover, the development of standards for mandatory climate risk reporting will require funding. Therefore, the Commission will need to provide the necessary resources in order to conduct rulemaking directly. It is not clear that a third-party organization would pass the independence requirements, or that an organization willing to provide robust and transparent standards would in fact be funded from appropriate sources.

Climate risk disclosures should be provided in annual and other periodic filings as a part of the formal corporate reports required under Regulation S-X and Regulation S-K or disclosed as risk factors. Where the information is disclosed matters. Voluntary public disclosures do not match the force of regulatory disclosures. For example, mine safety disclosures were always publicly available, but only when such disclosures became a part of mandatory public disclosures did mines become safer with fewer lives lost.[13]

As providers of capital, we seek a true and fair view of the company's position and prospects in the annual reports and accounts to better assess the company's performance, business model and strategy including climate change risk. We also care whether people are being harmed, both economically and by exposure to health risks and fatalities in order to meet the financial goals of those strategies. This reflects our holistic approach to sustainable value creation which includes our understanding that long term value creation requires the effective management of financial, human and physical capital. There is also an immediate need for improved disclosure. In the near term, we face severe droughts and wildfires in the west, as well as more severe

---

[12] 2010 SEC Climate Guidance. https://www.sec.gov/rules/interp/2010/33-9106.pdf

[13] Christensen, H.B., L. Hail and C. Leuz, May 2021. Mandatory CSR and Sustainability Reporting: Economic Analysis and Literature Review. *ECGI.* 64; and Condon, M., 2020. Externalities and the Common Owner. Washington Law Review 95-1: 42. (Both works highlight that mine safety data was already publicly available but only when disclosures were required in regulatory filings did mine safety improve.) https://www.nber.org/papers/w26169

weather throughout the country. We ask that the Commission develop a robust and transparent disclosure regime that will provide investors the information necessary to make informed decisions and ensure companies effectively address issues that are in their power to address.

This would include addressing externalities created by the emitters of carbon and other pollutants that harm people. It is a widespread market belief that all humans will be eventually affected by climate change. It is also the case that the burden of harm falls disproportionately on vulnerable communities, particularly those of color. This poses the issue of environmental racism which needs to be addressed. An example is the petrochemical corridor where African Americans are currently impacted by practices in the oil and gas industry as highlighted by the Rolling Stone in a piece on Louisiana's "cancer alley."[14]

For portfolio reasons, investors want to minimize negative externalities that will impact their market wide holdings.[15] Market forces alone are not looking after the interests of those currently bearing the risks and burdens of the significant emitter industries. The Commission should address whether its role in protecting the public interest extends to those facing the burdens of the emitting industries without corresponding benefit or compensation for such burdens. In other words, while we pursue protecting lives and wellbeing through reducing climate change in the long run, there should be a check on emitters including the geographic concentration of such emissions currently.

The Commission can address disclosures through several channels, including as outlined by Samantha Ross, in her paper, *The Role of Accounting and Auditing in Addressing Climate Change.*[16] Ross highlights four steps the Commission can take within its current authority to address climate change. These steps include recommendations to:

- Fully enforce existing accounting and related disclosure requirements to reflect the financial impacts of the climate crisis and the transition to a low-carbon economy.
- Update disclosure, through a staff accounting bulletin and other guidance and rulemaking, to spread identified best practices about material climate-related information across industries and markets.
- Leverage the audit to build a solid bridge between climate-related risks and corporate financial reporting.
- Address the ways in which the existing U.S. accounting standards exacerbate systemic climate risks.

The staff accounting bulletin should mirror the IASB climate related guidance requiring that, where material, climate issues should be considered, and sustainable assumptions shown in drawing up accounts. It will be important to ensure that the detail is comprehensive and

---

[14] Juhasz, A. 2019. *Louisiana's "Cancer Alley" Is Getting Even More Toxic – But Resident's Are Fighting Back.* Rolling Stone. https://www.rollingstone.com/politics/politics-features/louisiana-cancer-alley-getting-more-toxic-905534/

[15] Condon at 11-48.

[16] Ross, S. 2021. *The Role of Accounting and Auditing in Addressing Climate Change.* Center for American Progress. https://cdn.americanprogress.org/content/uploads/2021/02/26043119/AccountingAssurance-report.pdf

specific about what companies need to do in order to comply. At a minimum the guidance should insist that when accounts are drawn up and audited they:

I. Take material climate issues into account
II. Show the material assumptions they have made which are germane to climate issues

2. *What information related to climate risks can be quantified and measured? How are markets currently using quantified information? 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? Should disclosures be tiered or scaled based on the size and/or type of registrant)? If so, how? Should disclosures be phased in over time? If so, how? How are markets evaluating and pricing externalities of contributions to climate change? Do climate change related impacts affect the cost of capital, and if so, how and in what ways? How have registrants or investors analyzed risks and costs associated with climate change? 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? How does the absence or presence of robust carbon markets impact firms' analysis of the risks and costs associated with climate change?*

The Research and Strategy Group in the CalPERS Investment Office brought together eleven asset managers and data providers across all the asset classes in which CalPERS invests as part of a Master Class on Sustainable Investment series. There were two lessons from this series: first, ESG metrics are relevant and widely used by the many asset managers across asset classes with varying degrees and levels of relevance and second, data providers are becoming more sophisticated in their approaches to integrating existing ESG data. Some of the most commonly used metrics are Scope 1, 2, and 3 greenhouse gas emissions, revenue from less carbon intensive sources, and proven fossil fuel reserves. These metrics reflect a point in time view which is backward looking and limits their applicability to conduct forward looking analysis. The most common use is to evaluate potential transitions risks if company, sector, or industry trends do not change, yet policy and technology evolve to incentivize a transition to a low carbon economy.

In Global Equity and Fixed Income, practices include exclusions based on carbon emission and fossil fuel reserves to more complex tilts away from companies that have higher emissions track records and have not made commitments to decarbonize. In the private asset classes, more bespoke and asset specific approaches are utilized because investors have a stronger controlling share. For Private Equity, metrics such as carbon emissions and "clean" revenues can be utilized to measure management performance where relevant. In the case of Real Assets, having location specific data allows investors to assess the physical risk of the asset as well as the transition risk or the hold period of the asset.

A disclosure that would significantly enhance investors' ability to assess the physical risk of public and private companies in their portfolios is the geographic location of physical assets

owned by the company and the source of key supply chains. This information would allow investors to understand which companies have supply chains and critical assets in geographies expected to experience increased frequency of severe weather events due to climate change and position portfolios accordingly. This would also allow investors to engage companies with higher physical risk to better understand how those risks will be mitigated.

CalPERS believes the scope of disclosure should be universal. Climate risk, especially physical risks, will impact a company regardless of its size and type, so should climate related disclosures.

A robust and functioning carbon market would enable price discovery and the ability to effectively hedge climate risk. Companies have been reported to evaluate their investment decisions and price their assets using an internal price of carbon. While CalPERS supports and encourages more companies to adopt this practice, a robust carbon market would create greater alignment between company objectives and investor goals by allowing assessment of these internal prices on carbon more effectively. Pursuing alternatives to carbon intensive practices also becomes more viable once the full cost of those carbon intensive practices is accurately priced.

The International Auditing and Assurance Standards Board provides a pathway for determining materiality in its *Non-Authoritative Guidance on Applying ISAE 3000 (Revised) to Extended External Reporting (EER) Assurance Engagements* issued April 2021.[17] The process an issuer uses to determine materiality is critical. It is also critical to be able to review the process to better assess when issuers are improperly opting out of disclosing items that are in fact material. This gets into an end-to-end review that would include assessments by the Public Company Accounting Oversight Board (PCAOB) to determine whether registrants follow the proper processes in making disclosure determinations. The Commission has full power in determining the regulatory requirements, how companies disclose pursuant to those requirements should be reviewed for compliance and whether they are making proper materiality determinations.

"Double materiality" is an important concept that is increasingly being discussed in Europe and other international markets. Christensen, Hail and Leuz address double materiality in their literature review of sustainability reporting for the U.S. market.[18] They define it as when shareholders care about a company's negative impact (externalities) on the environment or society even when this impact does not have immediate financial consequences. Getting additional information on such externalities is at the heart of investor requests for additional disclosures, particularly by universal asset owners such as CalPERS which are exposed to systemic risks, both on and off balance sheet. It is important to note that in the case of externalities, companies impose burdens on the public and do not provide corresponding compensation for those burdens. As such, this is a market failure that can be seen in terms of environmental racism when plants are located in communities least likely to resist their placement, as with cancer alley in Louisiana. It becomes more obvious with climate change in

[17] IAASB. 2021. *Non-Authoritative Guidance on Applying ISAE 3000 (Revised) to Extended External Reporting (EER) Assurance Engagements.*40-48. https://www.iaasb.org/publications/non-authoritative-guidance-applying-isae-3000-revised-extended-external-reporting-assurance

[18] Christensen at 9.

which extra burdens are placed on the entire market. Significant polluters are projected to reduce revenues of other companies in the market. As such, universal owners are appropriately concerned and desire to get the significant emitters to internalize their externalities.[19] The Commission has the authority given its duty to operate in the public interest to address negative impacts on the environment and society.

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.)?*

Properly developed mandatory disclosure in this area must be able to survive expected litigation. It is not clear how investors, registrants, and other industry participants could develop mutually agreeable disclosure standards that would meet the process requirements. The advantages of such groups exist when issues are nascent or when regulators fail to respond. We acknowledge the value of work carried out by initiatives such as the TCFD, SASB and the IRRC (the latter two now combined in The Value Reporting Foundation). However, it is time now for mandatory, market wide standards that impose minimum requirements supplemented by flexible industry specific reporting on a principle basis. Having a wide range of groups attempt to create standards has not worked for non-regulatory reporting where it receives little outside critique and is not subject to the same process requirements, and there is little threat of litigation from their work. In fact, it is unclear how a process other than basic Commission rulemaking would pass the Administrative Procedures Acts (APA) requirements.

We believe the Commission should develop complete standards for mandatory climate risk reporting, as such, it should do far more than establish minimum standards. It is not clear that the market will follow any standards other than those mandated by the Commission. We need only look at the 2010 SEC Climate Guidance as an example. The third-party standards have less authority than Commission guidance which issuers did not follow, so we see it as even less likely they would follow standards having even less authority. In the absence of regulatory action, investors are spending considerable resources to improve reporting through private ordering, via engagement, filing shareowner proposals, conducting proxy solicitations. However, given the scale of the challenge this is not only expensive, but inefficient and incomplete.

If the Commission were to set minimum disclosure requirements, it should include TCFD styled governance reporting and disclosure of Scope 1, 2 and where relevant, Scope 3 emissions. However, any minimum standards must go much further and address issues relevant to climate change, including pollutants beyond carbon, the production and disposal of plastics, the use of water, mining, the valuation of oil and gas reserves, among other items. Additionally, reporting should sufficiently cover the scope of environmental management practices performed by the company including detailed descriptions of environmental effects on the company, the company's impact on the environment, and the company's industry and customer transition

[19] Condon at 11-40.

towards more sustainable products, services or practices. In other words, the emitters of carbon and other pollutants should disclose how they are preventing and managing externalities and preparing for a just transition. A just transition focuses on the fairness of how companies deal with the externalities they produce and how governments deal with the externalities that they allowed companies to produce. The concept of the just transition is integral to the Paris Agreement and forms a significant part of the preamble to the accord.

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?*

Different industries have different climate impacts and different industries will be impacted by climate differently. It is important that the boards of companies make proper assessments and communicate relevant information to investors for decision making purposes about their particular company. There is a clear advantage for having standards that are more relevant on an industry basis.

Although material climate risks manifest in different ways, the initial focus in developing climate reporting standards should be on the "heavy emitters" regardless of sector/industry. For example, Climate Action 100+ is engaged in this work through development of the first benchmark to track firm net-zero transition progress (The Net-Zero Company Benchmark or the Benchmark).[20] The Benchmark assesses the performance of focus companies against the initiative's three high-level goals: emissions reduction, governance, and disclosure and draws on distinct analytical methodologies and data-sets to provide investors and other stakeholders with a robust tool to focus company engagement and action. The Benchmark is not a disclosure mechanism or database itself. It is an assessment tool, but the metrics include the following ten indicators:

1. Net-zero GHG Emissions by 2050 (or sooner) ambition
2. Long-term (2036-2050) GHG reduction target(s)
3. Medium-term (2026-2035) GHG reduction target(s)
4. Short-term (up to 2025) GHG reduction target(s)
5. Decarbonization strategy
6. Capital allocation alignment
7. Climate policy engagement (political lobbying)[21]
8. Climate Governance (to ensure 'climate competent' boards)
9. Just Transition (*not assessed for 2021*)
10. TCFD disclosure

This is an example of the types of information that should be provided by companies with climate risks in mind. Such information should be disclosed to investors in regulatory reports to enable better decision-making. Having regulatory standards levels the playing field within an industry. Currently, companies are not even required to share location of critical assets. This

[20] Climate Action 100+ Benchmark. https://www.climateaction100.org/progress/net-zero-company-benchmark/
[21] In addition to the Benchmark, InfluenceMap provides detailed Paris-aligned analyses of corporate climate lobbying. These are referenced in the Benchmark company assessments.

additional disclosure would aid significantly in decision-making and the public interest. The Benchmark is being supplemented by sector specific requirements which are being developed to inform Climate Action 100+ signatories in their engagement and proxy voting with this group of systemically important carbon emitters, which we estimate are responsible for the third largest source of Scope 1 and 2 global greenhouse gas emissions, after China and the United States.

The Climate Related Market Risk Subcommittee of the Market Risk Advisory Committee of the U.S. Commodity Futures Trading Commission (CFTC) issued a report, titled *Managing Climate Risk in the U.S. Financial System.*[22] CalPERS served on this Committee. The report included a number of findings, but the central message of the report is that "U.S. financial regulators must recognize that climate change poses serious emerging risks to the U.S. financial system, and they should move urgently and decisively to measure, understand, and address these risks."[23] The report further concludes that, "disclosure by corporations of information on material, climate-related financial risks is an essential building block to ensure that climate risks are measured and managed effectively."[24] Unfortunately, the report does not go far enough when addressing the 2010 Climate Guidance. It suggests that "In light of global advancements in the past 10 years in understanding and disclosing climate risks, regulators should review and update the SEC's 2010 Guidance on climate risk disclosure to achieve greater consistency in disclosure to help inform the market. Regulators should also consider rulemaking, where relevant, and ensure implementation of the Guidance. (Recommendation 7.5)"[25] The report properly noted the 2010 Climate Guidance is problematic but fails to acknowledge that the route to actual reporting is not through further guidance. There is a need for an effective rulemaking including mandatory disclosures.

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?*

Third party framework providers and standard setters have developed thoughtful and useful metrics and provided well researched information that will be useful to the Commission in developing its standards. For example, the TCFD offers useful market-driven disclosure guidance which pertains to scope 1, 2 and 3 emissions that the Commission should incorporate, as well as other potentially material environmental factors and information, but the framework does not drill down to line-item disclosures. However, the TCFD framework identifies the business sectors where they see the greatest risk. The TCFD recommendations are intended to be: adoptable by all organizations; included in financial filings; designed to solicit decision-useful, forward looking information on financial impacts; and to provide a strong focus on risks and opportunities related to transition towards a lower-carbon economy. Standard setters offer

---

[22] *Managing Climate Risk in the U.S. Financial System,* *https://www.cftc.gov/sites/default/files/2020-09/9-9-20%20Report%20of%20the%20Subcommittee%20on%20Climate-Related%20Market%20Risk%20-%20Managing%20Climate%20Risk%20in%20the%20U.S.%20Financial%20System%20for%20posting.pdf*
[23] Id. at ii
[24] Id. at iii
[25] Id. at viii

great research and reasonable approaches to making known risks more transparent to the market, but there is no substitute for direct Commission action in this area.

Further, there is a need to clarify the Commission's authority in rulemaking because too many appear to believe that the Commission is limited in its rulemaking ability to only issuer level "material" disclosures. Some have even created elevated requirements for extra material items and argue that only such issues should be disclosed. Commissioner Lee's recent *Myths and Misconceptions about Materiality* speech addressed many of the issues effectively.[26] However, the full Commission needs to clarify that it has the power to mandate climate-risk disclosures, and those regulations are not subject to a materiality requirement for the practical purposes shared in Commissioner Lee's speech.

Materiality is an important concept that is used by registrants when determining how to respond to regulatory disclosure requirements. We have often commented on materiality, most notably, when FASB attempted to make its materiality a "legal concept."[27] TSC Industries Inc. v. Northway[28] (TSC) is commonly noted as the seminal case on materiality. It is important to note that the holding in TSC is "**An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote."[29]** Investors currently vote on a number of issues and in each case, and in accordance with TSC, disclosures should include the information a shareholder would consider in deciding how to vote. This certainly includes information regarding how a company manages climate risk. The recent ExxonMobil proxy fight makes clear that investors want companies to provide such information.

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?*

Disclosure requirements should be updated, improved, augmented, or changed over time following the same process as disclosure requirements in existing regulations. There should not be a special process simply because the disclosures are sustainability focused. The Commission should not designate an outside standard setter if it is serious about establishing sustainability standards that will survive litigation and last past one administration. Given the highly

---

[26] Lee, A. 2021. *Myths and Misconceptions About Materiality. Speech* https://corpgov.law harvard.edu/2021/05/26/speech-by-commissioner-lee-on-myths-and-misconceptions-about-materiality/
[27] CalPERS Letter to FASB on Materiality. 2015. https://www.fasb.org/cs/BlobServer?blobkey=id&blobnocache=true&blobwhere=1175832354098&blobheader=application%2Fpdf&blobheadername2=Content-Length&blobheadername1=Content-Disposition&blobheadervalue2=497846&blobheadervalue1=filename%3DDISFR-C.ED.0036.CALPERS_JAMES_ANDRUS.pdf&blobcol=urldata&blobtable=MungoBlobs
[28] 426 U.S. 438 (1976), *TSC Industries, Inc. v. Northway, Inc.*, June 14, 1976. https://supreme.justia.com/cases/federal/us/426/438/
[29] Id.

politicized nature of this undertaking, the Commission will have to bring the work in-house in order to be successful. Many of the positive assertions about how quick and nimble an outside party might be in modifying or updating disclosures are not credible in the absence of evidence and often assume that the Commission would be able to simply make such modifications without imposing additional processes. Interestingly, the views also assume that there are no issues with the work currently being performed by outside bodies. This is not the case as highlighted by Lynn Turner, Barbara Roper and others in a recent letter to the Commission.

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?*

   There are a range of climate issues. Some should fit more solidly in the financial statements,[30] others are appropriate for presentation through Regulations S-K and S-X. The disclosures should be filed with the Commission and appear as part of the periodic reports.

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?*

   TCFD provides a useful framework to address these issues. We are interested in knowing that boards possess 'climate competence' in oversight of executive teams and staffs. It is important that corporate leaders have the relevant skills, knowledge and incentives to address sustainability issues including climate. Since climate change is a systemic risk requiring lasting solutions, properly linking executive compensation to climate and sustainability-related metrics incentivizes executives to focus on the long-term and is in line with CalPERS' views on executive compensation. We support full disclosure of climate risk reporting which provides insights on a company's alignment of its corporate lobbying and executive compensation to ensure a just transition. The Climate Action 100+ Net Zero Company Benchmark expands on the TCFD framework to include capital allocation, compensation and political lobbying as necessary elements for reporting to investors and believe these items are relevant for effective climate disclosures.

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*

[30] Anderson, N. (arguing that the potential financial implications arising from climate-related and other emerging risks may include, but are not limited to: asset impairment, including goodwill; changes in the useful life of assets; changes in the fair valuation of assets; effects on impairment calculations because of increased costs or reduced demand; changes in provisions for onerous contracts because of increased costs or reduced demand; changes in provisions and contingent liabilities arising from fines and penalties; and changes in expected credit losses for loans and other financial assets.)

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?

Investors need high-quality, universally applicable standards. We are supportive of the IFRS ISSB, but we believe that the SEC needs to provide mandatory rulemaking in parallel for structural reasons. For example, the U.S. has not been a significant funder of IFRS, does not primarily use IFRS Standards, and faces issues mapping certain disclosures directly given the differences in financial accounting approach and the differences in Management Commentary and U.S. Management, Discussion and Analysis. Finally, the U.S. is substantially more litigious than other markets. According to one source, the U.S. sees more than 75 percent of worldwide climate litigation in its courts.[31] As such, there are hurdles to overcome which would take much time to move to a single universal standard. Given the circumstances, the Commission should act directly, but can work closely with the ISSB to more efficiently develop a strategy and structure for internationally agreed sustainability standards.

Some, including John White, have suggested that the Financial Accounting Foundation (FAF) would be the preferred entity to house a body that would correspond to the ISSB. The FAF already oversees the Financial Accounting Standards Board (FASB) and the Governmental Accounting Standards Board (GASB). Structurally this might make sense, but investor concerns regarding FAF and FASB should be addressed prior to giving FAF a significant and complex investor issue like sustainability reporting.

10. *How should disclosures under any such standards be enforced or assessed? For example, what are the advantages and disadvantages of making disclosures subject to audit or another form of assurance? If there is an audit or assurance process or requirement, what organization(s) should perform such tasks? What relationship should the Commission or other existing bodies have to such tasks? What assurance framework should the Commission consider requiring or permitting?*

If placed within existing periodic reports, the disclosures can be assessed and enforced like other disclosures appearing in Regulation S-X, Regulation S-K or in risk factors. We expect assurance and auditing on climate risk to be in line with existing standards. Our goal is to get enhanced reporting of sustainability risks. We do not want to put roadblocks in front of getting such enhanced disclosure by making a premature argument about assurance prior to knowing what the disclosures may be. The existing audit and assurance framework provides a baseline and may not need to change, initially. Sustainability items that are appropriately placed in the financials will be fully audited. Other information will be reviewed and assured in line with where it is placed in the periodic reports. The Critical Audit Matters section is an example where useful considerations can be provided by the auditor, for example. When an item that needs elevated audit or assurance moves into mandatory reporting, we can have a discussion on appropriate audit and assurance for such an item. It is premature to address in the abstract. We do recognize that some sustainability items received some sort of assurance when placed in

[31] According to Sabin Center for Climate Change Law at Columbia Law School

sustainability reports, and in certain cases, some would like to see continuing assurance by third parties outside the audit on such items when placed in regulatory reports. However, we believe it is the case that once in regulatory reports, enforcement, audit and assurance generally improves, therefore we make no special argument for excluding auditing and assurance on items that have yet to be identified.

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?*

    There is no need for special certifications of climate disclosures if they fit into existing corporate reports. The existing certification regime will appropriately cover such disclosures in the normal course. If, for some reason, the disclosures are not placed in regulatory reports, then there is a need for CEO/CFO certification of the information provided.

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?*

    The SEC disclosure regime contains "comply or explain" requirements which allow for a more flexible approach for companies. While we understand the need to strike the right balance, mandatory reporting history has shown that which gets disclosed gets managed. The most glaring concern for us as long-term investors is the possibility that too much flexibility will weaken the quality, consistency, comparability and reliability of climate change disclosures. How it gets managed differs depending on where it is disclosed and how easy such disclosure can be avoided. It would be a shame to go through this entire process and have the market disregard the disclosure just like it disregarded the 2010 Climate Guidance. The Commission should require mandatory disclosures and carefully considered additional specific disclosures.

13. *How should the Commission craft rules that elicit meaningful discussion of the registrant's views on its climate-related risks and opportunities? What are the advantages and disadvantages of requiring disclosed metrics to be accompanied with a sustainability disclosure and analysis section similar to the current Management's Discussion and Analysis of Financial Condition and Results of Operations?*

    We would like to see integrated reports with the sustainability information alongside the financials. The TCFD framework provides a starting point whereby companies discuss strategy, governance, metrics and targets, plus scenarios on a range of climate-related issues that go well beyond carbon emission.

From an academic perspective, the creation of a Sustainability, Disclosure and Analysis (SD&A) which would be similar to the MD&A is interesting and creative, if done well.[32] We would like to make certain that disclosure in an SD&A would not prevent appearance in the financials for information that should otherwise appear in the financials. We acknowledge that an SD&A could be a target for those that oppose sustainability reporting generally. It appears that creating an SD&A would take a substantial amount of time, and there are pressing climate risk issues the Commission should address immediately. Further, we have an idea of what it means and how to treat information in the MD&A. Placing information in a new SD&A may create substantial arguments about how to treat disclosures in an SD&A. Does it include the same force as MD&A or is it just a sustainability report within a regulatory filing? However, an SD&A could constitute an elegant solution and address issues such as audit, assurance and certification more directly. Timing and an ability to finalize the rulemaking are keys here and leans more toward moving forward with a basic and traditional rulemaking on climate-risk.

14. What climate related information is available 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?*

It is important to note that market focus has primarily been on disclosures provided by publicly traded companies, but for the past few years, the majority of capital raised in the U.S. has not been generated through public offerings. To the contrary, the majority of capital raised in the U.S. is now often through "private" offerings, which do not have the disclosure obligations, investor rights, or other protections that are the hallmarks of efficient capital markets. Transparency and shareowner rights are essential to promoting corporate and executive accountability. For that reason, we and other fiduciaries remain committed to promoting a robust capital market which includes comprehensive management and mitigation of climate risk through global cooperation addressing both the public and private sectors. Many of the significant emitters are in fact private. There are some who believe that companies may simply spin-off "dirty plants" to improve company ratings when doing such would not reduce emissions. In any event, there needs to be end-to-end management of emissions including disclosures of such.

BlackRock's CEO, Larry Fink, raised the point recently,[33] stating: "policymakers and regulators must address corporate and executive accountability for sustainability choices in both the public and the private markets." This may require revisions to some of the exemptions and exceptions to the federal securities laws that have given rise to much of the recent private market expansion, but it may also entail enhancing information and rights for long-term stakeholders in the private markets as well. In our view, private sector voluntary reporting initiatives need to be buttressed by mandatory reporting requirements where practicable.

The TCFD framework identifies the business sectors with the greatest risk, and we believe a detailed assessment of risk across both public and private markets is critical. The need is to reduce climate risk which can only occur if there is full market participation. Our strategic plan

---

[32] Fisch, J. 2019. *Making Sustainability Disclosures Sustainable.* 107 Georgetown Law Journal 923. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3233053.

[33] https://www.brookings.edu/wp-content/uploads/2021/02/es_20210202_climate_blackrock_transcript.pdf.

includes Sustainable Investment Practice Guidelines[34] which each asset class for both public and private markets, including both debt and equity, set out how they identify and integrate these issues into investment decisions. It is clear to us that all asset classes need better information and a system that produces such.

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?*

Climate change is a global challenge and one we cannot afford to ignore as long-term investors, with an inviolable fiduciary duty to our members. The consequences of inaction will be measured not just in the impact on the environment, but also to workers and communities. Our view aligns with the U.S. National Climate Assessment's finding that "[c]limate change exacerbates existing vulnerabilities in communities across the United States, presenting growing challenges to human health and safety, quality of life, and the rate of economic growth."[35]

As outlined in our Governance and Sustainability Principles, effective risk management disclosures should include how a company identifies and manages impacts, or potential impacts, on local environments and communities including company's approach to material human capital issues (e.g., public health, land rights, and just transition in relation to workers). Therefore climate-related requirements crafted by the Commission would complement broader ESG disclosure standards, specifically human capital management disclosures.

As emphasized by the rise of a new class of worker through the pandemic (i.e. Frontline Essential Worker),[36] it is clear that businesses depend on the workforce as a source of value creation which, if mismanaged, could harm long-term performance. The size, scale and viability of a company's operations has a direct impact on the scope of potential human capital risks which underscores why these disclosures are being sought as shareowners push for greater transparency and society demands for all of its people to be valued.

However, current financial reporting rules require companies to disclose very little information about how human capital is measured or managed. In addition, reporting varies by company and too often what is reported fails to reflect reality. Furthermore, global reporting standards around the "S" of Environmental, Social, Governance have historically been weak. At a regulatory level, the recent SEC rulemaking[37] on human capital disclosures was non-prescriptive

---

[34] https://www.calpers.ca.gov/docs/global-equity-sustainable-investment-guidelines.pdf; https://www.calpers.ca.gov/docs/real-assets-sustainable-investment-guidelines.pdf

[35] Fourth National Climate Assessment, Volume II: Impacts, Risk, and Adaptations in the United States, U.S. Global Change Research Program (2017), https://nca2018.globalchange.gov/.

[36] According to the U.S. Department of Homeland Security, essential workers are those who conduct a range of operations and services that are typically essential to continue critical infrastructure operations. https://www.ncsl.org/research/labor-and-employment/covid-19-essential-workers-in-the-states.aspx#:~:text=According%20to%20the%20U..S,energy%20to%20defense%20to%20agriculture.

[37] https://www.sec.gov/rules/final/2020/33-10825.pdf

and did not go far enough to address the information gap between what company managers know about a company and what is revealed to investors. We have long-advocated for more line item disclosures as opposed to the purely principles-based approach more common globally. So, we are delighted to support the Commission's work to modernize corporate reporting which should including moving the market forward with respect to human capital disclosures including a substantially greater focus on diversity and the addition of certain identified metrics.

Comprehensive, high-quality, consistent, and comparable disclosures of climate risk, charitable and political expenditures, human capital management, and board diversity are critical to the long-term success of capital markets. Disclosures of such information will help investors allocate capital to companies that best meet their investment criteria and will encourage market participants to operate with an eye on long-term business strategy. Such disclosures will also encourage companies to be more mindful of these risks that could impact their operations, and will provide for greater transparency regarding cash flow, corporate expenditures, and public policy engagement.

The need for companies to disclose better information so that shareowners can more easily identify, assess, and manage risk and opportunity has been brought to the SEC's attention over the last several years. Through our participation on the SEC's Investor Advisory Committee, we urged the SEC to undertake a robust examination of the role human capital management plays in value creation and provided recommendations[38] on improving the corporate disclosure system to include specific disclosures regarding intangible assets, such as human capital. Specific human capital key performance indicators and metrics which provide distinct implications for the cost and value of a company's workforce include:

- Number of People employed (as part of the narrative business description; expand the existing requirement to breakdown full time, part time and contingent);
- Stability of the workforce (including voluntary and involuntary turnover and internal hire and promotion rates);
- Diversity data (including race/ethnicity);
- Training hours (per employee per year);
- Employee satisfaction (survey measures);
- Safety of the workforce (including frequency, severity and lost-time due to injuries, illnesses and fatalities, and percent of first-tier suppliers that were audited for safety and health compliance);
- Competitive conditions (including the productivity and competitive advantages of the issuer's employee population, relative to competitors and available pools of labor); and
- Existing executive compensation disclosure could be augmented, for example, to include useful summaries of material information about broader workforce compensation and incentive structures (including how performance, risk, compliance, and long-term

[38] https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac032819-investor-as-owner-subcommittee-recommendation.pdf (dated March 19, 2019)

sustainability are considered in setting pay and making promotion decisions more generally and through what organizational structures).

These themes are material to investors across many companies and should inform the Commission's future work on establishing mandatory risk reporting. Addressing these specific themes will produce a system of meaningful, uniform and comparable disclosures that will provide investors with a more comprehensive accounting of its workforce. This is significant because the most valuable part of many companies is its people, the human capital.

Related to human capital management disclosures is the need for more transparency into board diversity. We believe that diversity, equity and inclusion help companies improve their performance over the long-term because a multiplicity of backgrounds, experiences, and perspectives helps management address risk and seize opportunities in a more holistic manner. Our view is informed by research into the efficacy of a diverse board. For instance, the Office of the Illinois State Treasurer published a white paper titled "The Investment Case for Board Diversity" which provides an extensive and comprehensive review of academic and practitioner research on the value of gender and racial/ethnic board diversity for investors. The examination finds that "the gender and racial/ethnic composition of corporate boards does indeed have a material and relevant impact on company performance and investors."

Unfortunately, for too long, issuers have declined to provide this information. Given the lack of disclosures about board diversity, it is hard to get reliable data on racial diversity on boards, but third-party analysis appears to show that as many as 70 percent of Nasdaq companies' boards are not diverse at all.[39] The SEC has taken up the discussion on a few occasions and has always fallen short of actually addressing diversity disclosure. Without more comprehensive disclosures of board diversity, we and other investors are less able to evaluate the competitive advantages between companies, make more informed decisions, and allocate our capital to the investments and exercise stewardship to ensure long-term value creation.

To remedy this information asymmetry, boards should annually disclose their demographic information including race, ethnicity, and gender. Ideally, companies should disclose their Employer Information Report, known as the EEO-1 report, or similar workforce demographic data to enable shareowners to assess the board's diversity relative to its workforce and compare companies in similar industries. CalPERS and other investors have asked the SEC to expand disclosures for investors on a number of issues relevant to risk and return, including human capital. It is vital that the SEC act.

In conclusion, voluntary disclosures, quite simply, are insufficient to enable investors to obtain the information necessary to evaluate climate risks and opportunities. There is a need for comparability and consistency of disclosures, which help manage expectations and evaluate management. There would be major problems if a company began to selectively disclose particular information. Investors would have to use the only means available to address the problem which would be through votes in board of directors' elections or through litigation. Mandatory disclosures would bypass these issues. We appreciate the need to balance a variety

---

[39] Andrew Ross Sorkin, Jason Karaian, Michael J. de la Merced, Lauren Hirsch and Ephrat Livni, *Nasdaq Pushes for Diversity in the Boardroom.* https://www nytimes.com/2020/12/01/business/dealbook/nasdaq-diversity-boards html.

of considerations in determining the scope of climate-related disclosure requirements that would complement a broader ESG disclosure standard.