August 16, 2022

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Environmental, Social, and Governance Disclosures for Investment Advisers and Investment Companies (Release Nos. 33-11068, 34-94985, IA-6034, IC-34594; File No. S7-17-22)

Dear Ms. Countryman:

The American Securities Association[1] (ASA) submits these comments regarding the Securities and Exchange Commission's (SEC or Commission) proposed rule entitled "Environmental, Social, and Governance Disclosures for Investment Advisers and Investment Companies" (Proposal). The Proposal would establish an extensive and prescriptive disclosure regime for funds and investment advisers regarding environmental, social, and governance (ESG) issues and how ESG issues are integrated into the investment process.

General

The ASA is supportive of efforts by the SEC to prevent the practice of "greenwashing," which involves investment funds making misleading or false claims about how they use ESG, "sustainability" or other similar criteria to screen or incorporate portfolio companies into their investment process. The dramatic growth of the ESG industry and the number of funds that label themselves as some version of "ESG-friendly" justifies a close inspection by regulators.

However, the Proposal, as written, would not adequately address greenwashing or inform investors about the true extent of ESG integration by funds or investment advisers. Instead, it would establish enormously costly disclosure requirements for funds and advisers to provide certain information that investors may have little interest in. Even more concerning, the Proposal would likely lead to homogenization of "ESG" investing and treat virtually every investment fund as some version of an ESG fund.

[1] The ASA is a trade association that represents the retail and institutional capital markets interests of regional financial services firms who provide Main Street businesses with access to capital and advise hardworking Americans how to create and preserve wealth. The ASA's mission is to promote trust and confidence among investors, facilitate capital formation, and support efficient and competitively balanced capital markets. This advances financial independence, stimulates job creation, and increases prosperity. The ASA has a geographically diverse membership base that spans the Heartland, Southwest, Southeast, Atlantic, and Pacific Northwest regions of the United States.

Our concerns and thoughts on the Proposal are discussed in further detail below.

I. The SEC should recognize its existing authority to prevent greenwashing.

As justification for the Proposal, the SEC states that investors "face a lack of consistent, comparable, and reliable information among investment products and advisers that claim to consider one or more ESG factors" which creates a "risk that a fund or adviser's actual consideration of ESG does not match investor expectations, particularly given that funds and advisers implement ESG strategies in a variety of ways."[2]

Funds or advisers making misleading or false claims about the use of ESG criteria or standards is already prohibited by SEC regulations. The Proposal itself restates several rules already in place that the SEC can use to prevent false or misleading statements, including 17 CFR 275.206(4)-8 which prevents advisers to pooled investment vehicles from misleading investors. It also cites the Marketing Rule, which prohibits an adviser from engaging in any misleading or false advertisements.[3]

In 2021, the SEC established a Climate and ESG Task Force within the Division of Enforcement.[4] The task force was charged with identifying "any material gaps or misstatements in issuers' disclosure of climate risks under existing rules" and to analyze "compliance issues relating to investment advisers' and funds' ESG strategies." In June, the task force announced its first enforcement action against an investment adviser for making misleading claims regarding their consideration of ESG factors.[5] And last month, the Director of the SEC's Division of Enforcement acknowledged the broad authority the SEC has to prevent ESG misinformation, testifying before the House Financial Services Committee that the SEC's antifraud authority is "adequate" to address the issue.[6]

Misleading or false claims about ESG – or any topic – by a fund or investment adviser are serious investor protection issues and the SEC should act to prevent them. However, prior to issuing any final rule, we urge the SEC to consider whether it needs any new rules given that existing rules cover the practices described in the Proposal.

Further, by declining to define "E", "S", or "G", we understand that the SEC wants to maintain flexibility as the sector matures. However, this could expose firms to unnecessary risk and lead to regulation by enforcement where SEC staff uses a subjective, evolving definition of ESG when convenient. Without a clear definition, firms are left to decide what constitutes "ESG" and

[2] Proposal at 7-9
[3] Proposal at 168
[4] https://www.sec.gov/news/press-release/2021-42
[5] https://www.sec.gov/news/press-release/2022-86
[6] Oversight of the SEC's Division of Enforcement. House Financial Services Committee Subcommittee on Investor Protection, Entrepreneurship, and Capital Markets (July 19, 2022).

will be constantly updating policies and procedures as enforcement occurs, not as directed by Administrative Procedure Act rulemakings.

II. The Proposal will not assist investors in their understanding of "ESG" investing or ESG-labeled products.

The Proposal describes the substantial growth of ESG products over the last several years, noting that funds integrating ESG strategies grew from $12 trillion in 2018 to $17.1 trillion in 2020. However, the term "ESG" remains ill-defined, yet the number of topics that fall under the category of "ESG" seem to expand year after year. It is no surprise that investors may be confused how one ESG-labeled product differs from another, or what specific E, S, or G issues a fund may consider and incorporate into its investment process.

Rather than a simple, principles-based approach where funds that label themselves as "ESG" could provide a short description of what topics they consider, the Proposal creates a cumbersome new regime that divides funds into different categories and would result in voluminous – but not useful – new disclosures.

It is telling that the SEC has declined to define the term "ESG" within the Proposal. While we agree that a clear definition of ESG would be useful, it makes little sense to mandate standardized disclosures for funds and investment advisers regarding a topic that the SEC itself cannot easily explain. It's not lost on us that the lack of an ESG definition is more likely a feature, not a bug associated with this new investment phenomenon.

We do not believe these disclosures would reflect the continuous expansion of issues that routinely find their way into the ESG bucket. In fact, it could lead to unnecessary disclosures because firms and advisers have no guidance on what actually constitutes ESG. This will only lead to an increase in investor confusion. The ASA echoes some of the concerns that Commissioner Peirce raised in her dissenting statement on the Proposal:

> E, S, and G cannot be adequately defined, nor will they be, should the proposal eventually find its way into the Code of Federal Regulations. All you will learn from the proposed definitions is that "E" stands for environmental, "S" stands for social, and "G" for governance, but I suspect that you already knew that. The cool kids already have moved on to "*E*ESG"—*Employees*, Environmental, Social, and Governance…Imagine trying to conjure up a definition that not only met the universe of current understanding, but was flexible enough to grow to meet the hour-by-hour expansion of just what makes up E, S, and G.[7]

The SEC should also explore the level of actual investor interest in ESG strategies and the demand for more information regarding the integration of E, S, or G factors. A recent FINRA Foundation/National Opinion Research Center survey found that when making investment decisions, 54% of investors "never or rarely" consider environmental impacts and 44% "never or

[7] https://www.sec.gov/news/statement/peirce-statement-esg-052522

rarely" consider a companies' actions or statements related to social issues. And, a stunning 25% of investors also believe that "ESG" stands for "earnings, stock, growth."[8] We think the SEC should take this into consideration.

III. The consideration of "one or more" ESG factors to trigger disclosure requirements for funds and investment advisers will treat every fund as an "ESG" fund.

The Proposal would establish a category of funds known as "integration funds" which are defined as strategies that "consider one or more ESG factors alongside other, non-ESG factors in investment decisions…ESG factors may be considered in the investment selection process but are generally not dispositive compared to other factors when selecting or excluding a particular investment."[9] Integration funds would be required to report on what specific E, S, or G factors they consider as part of an ESG strategy.

We believe the Proposal's expansive definition of integration funds—not even counting the Commission's request whether to expand it even more (see Proposal at 30)—would encompass just about *every* fund as an integration fund. Even if a fund only considers core "G" issues as part of its investment and proxy voting process – as funds have done for years and long before "ESG" became a household term – they would be considered integration funds and have to disclose information about their overall ESG strategy. This will only sow confusion as investors would be led to believe such a fund also incorporates certain "E" or "S" factors as well. Indeed, this encourages the very "greenwashing" the proposal is aimed at preventing. What's more, requiring advisers who have always considered governance issues as risk factors to comply with additional reporting requirements will ultimately increase costs for investors.

This will also lead to a homogenization of investment strategies and products, needlessly handcuffing fund managers and investment advisers' ability to provide their clients with the specific exposure they seek. The Proposal improperly blurs the line between funds that consider ESG factors as they relate to evaluating the fundamentals and risks of an investment, versus funds that actively seek to achieve ESG goals, even if that means sacrificing some performance. For these reasons, if the SEC adopts a final rule regarding ESG reporting requirements, we believe it should not include an Integration Fund category.

IV. The Proposal does not adequately consider the costs of compliance that would result from implementation.

Were the Proposal to be implemented, fund managers and investment advisers would have to re-orient their compliance procedures to determine how every holding and investment or voting decision potentially implicates "ESG" topics. The Proposal's economic analysis does not

[8] https://www.finrafoundation.org/sites/finrafoundation/files/Consumer-Insights-Money-and-Investing.pdf
[9] Proposal at 14

adequately consider the time and resources funds and advisers will have to divert in order to make these determinations and provide the required disclosure.

This is especially problematic when considering the SEC's outstanding proposal on fund names.[10] Under that proposal, funds would have to undertake ongoing examinations of every holding to determine whether it continues to meet the criteria implied by a fund name. Yet the economic analyses of both rule proposals do not consider how they would work in tandem or the cumulative costs of both rules going into effect. The SEC must conduct a more thorough analysis of both compliance and economic costs prior to making any final decisions on the Proposal.

V. The SEC has again provided an inadequate public comment period

The Commission has many other proposed rulemakings currently out for public comment. Like the proposal discussed here, it is extremely challenging for the public to provide comprehensive feedback in a 60-day time period, particularly when the Proposal is related to other outstanding initiatives, including the climate change disclosure proposal and the fund names rule. The SEC must provide adequate time for the public and stakeholders to review and analyze the proposals. The SEC has also not considered in its economic analysis how the Proposal is affected by other outstanding rule proposals, including the climate disclosure proposal and the proposal regarding fund names. This allows for a full cost-benefit analysis, including identifying potential unintended consequences on market participants.

Conclusion

While the ASA supports efforts to protect investors from misleading or deceptive ESG marketing, the Proposal misses the mark and will further obfuscate the ESG universe for investors.

We believe the SEC should continue to use its current authority to prevent greenwashing and to address instances when a fund or investment adviser violates existing regulation. We look forward to working with the SEC on this issue and serving as a resource for commissioners and staff.

Sincerely,

Christopher A. Iacovella

Christopher A. Iacovella
Chief Executive Officer
American Securities Association

[10] https://www.sec.gov/rules/proposed/2022/33-11067.pdf