

August 16, 2022

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Submitted electronically via <https://www.sec.gov/cgi-bin/ruling-comments>

RE: SEC File No. S7-17-22; Environmental, Social, and Governance Disclosures for Investment Advisers and Investment Companies

Dear Ms. Countryman:

Silver Regulatory Associates LLC (“Silver”) welcomes the opportunity to comment on proposed rule by the U.S. Securities and Exchange Commission (“SEC” or “Commission”), “Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices” (the “Proposed Rule”).¹

About Silver Regulatory Associates LLC

Silver Regulatory Associates LLC provides consulting services to investment advisory firms. We offer services with respect to (i) regulatory and compliance processes; (ii) ESG; and (iii) due diligence. Established in 2018, Silver has advised over 100 clients operating in a variety of investment strategies and asset classes, including private equity, hedge fund, venture capital, crypto/digital asset, real estate and infrastructure, fixed income, private credit, and more. Our stringent, yet practical, approach reflects Silver’s roots in regulatory compliance rigor and investment firm business realities.

Support and Commentary related to the Proposed Rule

Environmental, Social, and Governance (“ESG”) practices are increasingly being adopted by investment advisers in the United States.² The Commission’s focus on ESG, including its April 2021 ESG Risk Alert,³ creation of its Climate and ESG Taskforce⁴ and similar actions have formed a foundation of initial guidance and best practices against which U.S. investment advisers can evaluate their ESG practices.

Silver’s ESG clients consider their ESG practices and disclosures through the regulatory compliance lens of the Investment Advisers Act of 1940, as amended (“Advisers Act”) and/or the Investment Company Act of

¹ See Proposed Rule, *Environmental, Social, and Governance Disclosures for Investment Advisers and Investment Companies*, Release No. 33-11068, 34-94985 (June 17, 2022) [hereinafter Proposed Rule].

² At the start of 2020, global sustainable investment reached USD35.3 trillion in five major markets, a 15% increase in the past two years, which includes a 42% increase in the U.S. (2018-2020): <http://www.gsi-alliance.org/wp-content/uploads/2021/08/GSIR-20201.pdf>

³ <https://www.sec.gov/files/esg-risk-alert.pdf>

⁴ The Climate and ESG Task Force was formed by the SEC on March 4, 2021, to develop initiatives to proactively identify ESG-related misconduct: <https://www.sec.gov/news/press-release/2021-42>

1940, as amended (“Investment Company Act”). As our clients’ ESG practices change over time, Silver provides guidance for continued compliance with the SEC’s developing position and proposed rules around ESG disclosures and their application.

Silver is supportive of the Commission’s efforts to clearly describe the ESG disclosure requirements it deems reasonable to support its mandate to protect investors; maintain fair, orderly and efficient markets; and facilitate capital formation.

We encourage the Commission to align with its historic, principles-based approach to rule making rather than a more prescriptive, rules-based approach. Our responses to the Proposed Rule, and our recommendation to enhance and further clarify the Commission’s expectations are reflected in the sections below.

Definitions Used in the Proposed Rule:

The Proposed Rule defines “Integration Fund” as: *“A fund that considers one or more ESG factors alongside other, non-ESG factors in its investment decisions, but those ESG factors are generally no more significant than other factors in the investment selection process, such that ESG factors may not be determinative in deciding to include or exclude any particular investment in the portfolio.”*⁵

Silver questions whether the category of “Integration Fund” is appropriate to include as part of the Commission’s definition hierarchy. Silver’s ESG practice serves many investment advisers who do not distinguish or market their fund strategies as “ESG” strategies. However, these same clients describe their investment practices related to the evaluation and consideration of ESG risks and opportunities as an “integration” approach. For clarity, this term is used to describe how the review of ESG risks and opportunities is integrated into the investment management process.

The difference between an adviser’s investment management practices as compared to the description of its fund vehicles is significant. Under the definition hierarchy in the Proposed Rule, identifying a fund as an “Integration Fund” may ultimately be misleading and may result in increased investor confusion. Silver urges the Commission’s continued evaluation of this term and would ultimately support the Commission’s decision to remove the term from the final rule.

If the Commission seeks to include the term “Integration Fund” in the final rule, Silver views the definition of “Integration Fund” as overly broad in its current form. We believe this definition is likely to be over-inclusive and may lead to the misrepresentation of an investment adviser’s practices and perspectives on ESG.⁶

For example, an adviser may “consider” an ESG factor for an investment in its fund without an explicit intention to do so, because an E, S, or G risk (e.g., worker health and safety) is deemed relevant when evaluating a prospective investment. However, this evaluation may occur as a result of the manager’s traditional due diligence process, and not promulgated by way of formal ESG-related practices. Based on this fact pattern, the investment vehicle could be improperly categorized as an “Integration Fund” pursuant to the Proposed Rule.

⁵ Proposed Rule, *supra* note 1, at 316-317.

⁶ *Id.* at 53-54.

In order to clarify its disclosure standards, Silver recommends the Commission consider the following amendments to the definition of “Integration Fund”: *“A fund that intentionally and systematically considers one or more ESG factors alongside other, non-ESG factors in its investment decisions, in line with the Fund’s ESG practices, but those ESG factors are not weighted more significantly than other factors in the investment selection process, such that ESG factors may or may not be determinative in deciding to include or exclude any particular investment in the portfolio.”*

Form ADV Disclosures

Form ADV is required to be completed by all investment advisers who are subject to registration with the SEC. The Proposed Rule considers updates to Part 1 and Part 2 of the Form ADV. Part 1 requires information about an investment adviser’s business, ownership, clients, employees, business practices, affiliations, and any disciplinary events of the adviser or its employees. Part 2 requires investment advisers to prepare narrative brochures that include plain English disclosures of the adviser’s business practices, fees, conflicts of interest, and disciplinary information.⁷

Silver is generally supportive of including ESG disclosures in the Form ADV. Our investment adviser clients typically adopt an ESG policy that describes the approach and strategy related to evaluating and managing material ESG risks and opportunities throughout the investment process. At the core of this effort is the adviser’s determination that ESG risks and opportunities have (and will continue to have) a material financial or operational impact on their fund investments. However, in our experience, disclosure related to an ESG policy or associated practices are not typically included in Form ADV filings. The Proposed Rule clarifies the SEC’s position that this information is reasonable to include.

Proposed Changes to Part 2A of Form ADV

Item 8: Methods of Analysis, Investment Strategies and Risk of Loss

The Proposed Rule requires advisers to provide a description of the ESG factor or factors they consider and disclose to clients how they incorporate these factors when providing investment advice, including when recommending or selecting other investment advisers.⁸

An investment adviser bears the responsibility to determine what ESG risks and opportunities may impact a prospective or current investment. For certain advisers, the universe of potentially material ESG risks and opportunities may be naturally limited due to the adviser’s investment thesis and/or investible universe. However, in Silver’s ESG practice, we observe that the universe of potentially material ESG risks and opportunities for a prospective or current investment can be broad, and the determination of materiality is a key driver in isolating the ESG factors that are ultimately considered when an adviser selects or manages an investment. Silver believes a better disclosure requirement would include a description of an investment adviser’s ESG practices, along with a sample of the types or categories of ESG factors the adviser generally evaluates.

Similarly, Silver believes that describing every ESG factor an investment adviser may evaluate during the investment process will not produce useful information in investment decision making

⁷ <https://www.investor.gov/introduction-investing/general-resources/news-alerts/alerts-bulletins/investor-bulletins-71>

⁸ Proposed Rule, *supra* note 1, at 129.

for an investor or evaluation of risks by the Commission. This requirement could potentially lead to the description of a large volume (>100) of ESG factors that may be relevant to an adviser's investment thesis, but would not lead to a description of an adviser's process to determine which ESG factors should be reviewed or may ultimately impact its investment decisions, engagement activities, or other monitoring actions. Silver is supportive of disclosures that would require an adviser to explain its ESG practices, including what is meant when the adviser states ESG factors are incorporated into investment decisions.

Pursuant to the Form ADV, Part 2A instructions for Item 8, an adviser must describe the methods of analysis and investment strategies it uses in formulating investment advice or managing assets.⁹

Silver recommends that the Commission refrain from any requirement for advisers that consider ESG factors as part of their significant strategies to state that "the consideration of ESG factors may lead to the adviser selecting or recommending an investment that may not generate the same level of returns as investments where the adviser does not consider ESG factors."¹⁰

In Silver's ESG practice, our client's consideration and evaluation of ESG factors is generally undertaken to ensure all risks that may impact the financial or operational performance of an investment are fully vetted. In these cases, the consideration of ESG factors may lead the adviser to select or recommend an investment that may generate a higher level of return as compared to investments where the adviser does not consider ESG factors. This language in the Proposed Rule could potentially create confusion for investors when reviewing an adviser's disclosures, and lead to an improper conclusion that the consideration of ESG factors is associated with greater risk of a decreased return.

Due to the significant differences in ESG approaches and strategies, Silver recommends advisers be required to describe the applicable risks in their own words, as the adviser deems relevant based on the current Form ADV instructions and SEC guidance. This approach aligns with the Commission's disclosure requirements for all other risks an adviser may include in the Part 2A and ensures that prescriptive language does not ultimately lead to inaccurate disclosures.

Item 17: Voting Client Securities

The Proposed Rule requires an investment adviser that has specific voting policies or procedures to include one or more ESG considerations when voting client securities to describe which ESG factors are considered and how the adviser considers them.¹¹

Silver recommends advisers be required to describe their voting policies and procedures in their own words. The SEC's prescriptive approach to Item 17 may lead to over-disclosure of proxy voting practices that are not often exercised and draw undue attention to ESG proxy procedures that would not otherwise be warranted. For example, several of Silver's ESG clients accept authority to vote client securities and have updated their proxy voting procedures to indicate that the adviser will vote ESG-related proxies in the best interest of its clients. Under such circumstances, this adviser would need to explicitly disclose that it has agreed to vote ESG-related

⁹ <https://www.sec.gov/about/forms/formadv-part2.pdf>

¹⁰ Proposed Rule, *supra* note 1, at 246.

¹¹ *Id.* at 134.

proxies in the same manner as it votes other proxies. Silver does not believe this information is useful for investors or the Commission. Rather, Silver believes the obligation to make an adviser's proxy voting record and procedures available, as currently required, is sufficient for investors to best understand an adviser's specific proxy-related practices.

Proposed Changes to Part 1A of Form ADV

Pursuant to the Form ADV instructions, Part 1A requires information about an investment adviser's business, ownership, clients, employees, business practices, affiliations, and any disciplinary events of the adviser or its employees.¹²

The SEC indicated that its proposed changes to Part 1A would provide the Commission and current and prospective advisory clients with important information about advisers' consideration of ESG factors in their advisory businesses, including the specific factors they consider, the types of ESG-related strategies they employ, and potential conflicts of interest with related person ESG providers. Further, this information would provide the Commission with comparability across advisers and advance the SEC's regulatory goal of gaining a more complete understanding of advisers' considerations of ESG factors in their separately managed account and private fund management businesses.¹³

To facilitate the Commission's objective to better understand an adviser's consideration of ESG factors for its advisory clients, Silver recommends the SEC generally rely on the information disclosed in Part 2A of the Form ADV (*see section, "Proposed Changes to Part 2A of Form ADV, Item 8: Methods of Analysis, Investment Strategies and Risk of Loss" of this letter for additional comments*).

Silver encourages the Commission to evaluate whether the amendments contemplated by the Proposed Rule are aligned with the stated intention of the Form ADV, Part 1A. In our view, the information anticipated to be collected pursuant to the Proposed Rule is uniquely specific, and out of sync with the general use of Part 1A.

Silver is not supportive of the Proposed Rule's requirement that advisers report on Part 1A whether they consider one or more ESG factors as part of the adviser's proxy voting policies and procedures. Silver believes disclosures related to proxy voting policies and procedures should be disclosed in the Part 2A (*see section, "Proposed Changes to Part 2A of Form ADV, Item 17: Voting Client Securities" of this letter for additional comments*).

Silver is not supportive of the Proposed Rule's required disclosure of an advisers' use of ESG indexes, including disclosure of additional information such as the name and legal entity identifier, if any. Currently, the SEC does not cause investment advisers to disclose their use of comparison indexes or specific data sources on the Part 1A. Silver believes an adviser should include this information in relevant sections of the Part 2A, such as Item 4: "Advisory Business"¹⁴, as such disclosure is deemed responsive to Part 2A instructions.

¹² See *supra* note 7.

¹³ Proposed Rule, *supra* note 1, at 156.

¹⁴ Item 4 of Form ADV, Part 2A requires investment advisers to describe their advisory business in detail, including, but not limited to the types of advisory services offered. Silver believes this is the correct place to disclose the ESG indexes or data sources the adviser may use when making investment decisions and providing investment advisory services, if the use of such indexes or data sources is material. See *supra* note 9, at 7.

Silver is supportive of the Proposed Rule’s requirement for advisers to report whether they follow any third-party ESG framework(s) in connection with their advisory services, and to report the name of the framework. For example, many of Silver’s ESG clients are public signatories to the United Nations-backed Principles for Responsible Investment (“PRI”). Silver would find a corresponding disclosure on the Form ADV, Part 1A indicating PRI membership to be useful when reviewing a client’s disclosures and believes investors would similarly find utility in this disclosure. Silver further recommends the SEC request a link to any public filings or reports that are made with respect to an ESG framework, in a similar manner to an adviser’s website disclosure, as required in Item 1.I of the Part 1A.

Finally, the SEC may consider clarifying its language with respect to third-party ESG frameworks to ensure advisers disclose all relevant information related to this request: *“We also propose to require advisers to report whether they follow, or are formal member of, any third-party ESG framework or ESG initiatives in connection with their advisory services.”*¹⁵

Timing/Compliance Dates

The Proposed Rule indicates that, the compliance date of any adoption of this proposal for the following items would be one year following the effective date, which would be sixty days after the date of publication in the Federal Register: (i) the proposed disclosure requirements in prospectuses on Forms N-1A and N-2, (ii) the proposed disclosure requirements for UITs on Form N-8B2; (iii) the proposed regulatory reporting on Form N-CEN, and (iv) the proposed disclosure requirements and regulatory reporting on Form ADV, Parts 1 and 2.¹⁶

Silver recommends the Commission extend this compliance timeline from one year to, at minimum, 18 months. In the SEC’s most recent update to the Marketing and Advertising Rule in May of 2021, the SEC allowed for an 18-month compliance period.¹⁷ Unlike the changes to the Marketing and Advertising Rule, the Proposed Rule includes amendments and disclosures that have not been previously contemplated by a regulatory or other public filing, and additional time is merited. Silver encourages the Commission to extend the compliance date to provide sufficient time for registrants to evaluate their compliance obligations under the final rule, undertake the requisite analysis related to the Commission’s definition hierarchy, prepare to update related policies and procedures impacted by the disclosure requirements of the final rule, and seek additional guidance from the Commission or expert third parties, where relevant.

Alignment with Existing Reporting Frameworks

Silver calls the Commission’s attention to Regulation (EU) 2019/2088, commonly referred to as the “Sustainable Finance Disclosure Regulation” or “SFDR”. SFDR also utilizes a definition hierarchy to describe the extent to which an investment adviser takes sustainability into account as part of investment decision making. In the Commission’s evaluation of the definition hierarchy included in the Proposed Rule, Silver believes it is imperative that the Commission create clear guidance for advisers that are registered with the SEC and have disclosure obligations to the European Commission.

¹⁵ Proposed Rule, *supra* note 1, at 158.

¹⁶ *Id.* at 169.

¹⁷ <https://www.sec.gov/news/press-release/2020-334>

Many of Silver’s clients act as advisers or sub-advisers to “Article 8” products, defined by SFDR as, investment products that “promote, among other characteristics, environmental or social characteristics, or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices.”¹⁸

It is unclear, based on the current form of the Proposed Rule, what disclosure obligations an adviser to an “Article 8” fund would be required to make to comply with the SEC’s disclosure standards. Based on the increasing prominence of “Article 8” funds, as well as increasing attention from investors related to “Article 8” disclosures Silver believes the SEC’s efforts to harmonize its definition hierarchy with consideration to SFDR would be useful to registrants and investors.

Conclusion

Silver is supportive of enhanced ESG disclosures by investment advisers registered with the SEC and is aligned with the Commission’s view that the rules and regulations under the Advisers Act and Investment Company Act have not resulted in consistent, comparable ESG disclosures across its registrants. Accordingly, enhancements and amendments are not unreasonable as ESG practices continue to evolve in the U.S.

However, as the Commission acknowledges, ESG is a broad term that encompasses a wide variety of actions and activities.¹⁹ Silver recommends the SEC consider the important differences between advisers that demonstrate intentional and systematic ESG practices, and advisers that evaluate an ESG risk or opportunity pursuant to their fiduciary duty. Silver believes it is reasonable for the Commission to enhance disclosure obligations for advisers that demonstrate intentional and systematic ESG practices. Advisers that inadvertently evaluate an E, S, or G factor as a part of their fiduciary duty (e.g., due to the natural relevance of an ESG factor to an investment), should not define or disclose these actions as an ESG practice or activity. Silver believes such disclosure will inevitably lead to investor confusion and will contribute misinformation as the SEC seeks clarity on ESG practices.

We encourage the Commission to consider the comments submitted by investment advisers and investment companies that will be immediately subject to the Proposed Rule. In certain instances, as indicated in our comments above, we believe the Proposed Rule creates duplicative disclosure obligations. In other instances, the Proposed Rule requires disclosures that may not be useful to investors or the Commission. In all instances, disclosure requirements should be established to support the SEC’s mandate to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.

Silver is a member of the Alternative Investment Management Association (“AIMA”), a Signatory to the PRI and a service provider to clients who are also members of AIMA, PRI, as well as the Investment Company Institute and other financial industry organizations. Silver supports the positions expressed in the comment letters submitted by each respective organization.

We thank the Commission for its hard work and effort that is represented by the Proposed Rule, and for the opportunity to submit our comments. Please do not hesitate to contact us if we can be of further assistance.

¹⁸ <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32019R2088>

¹⁹ Proposed Rule, *supra* note 1, at 7-9.

Respectfully,



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