REWARD VALUE

OPEN LETTER IN RESPONSE TO THE REQUEST FOR PUBLIC COMMENT ON PROPOSED U.S. CLIMATE CHANGE DISCLOSURES

To the honorable Gary Gensler, Chairman of the U.S. Securities and Exchange Commission

June 17th, 2022

Dear Chair Gensler,

Reward Value Foundation (RVF) is a not-for-profit research initiative based in the Netherlands. Our mission is to support the development of remuneration policies that contribute to long-term sustainable and inclusive value creation. Most corporations today claim to be purpose-led, putting people and the planet first. But the efforts of millions who join them are undermined by outdated financial incentives that reward CEOs to deliver short term gains at all costs. The Foundation seeks to further the debate on executive remuneration with investors, universities, and the business community at large to modernise executive pay as a catalyst for positive change. Through our research and collaborative initiatives, RVF aims to develop evidence-based, long-term, sustainable, and stakeholder-inclusive executive remuneration policies.

The U.S. Securities and Exchanges Commission (SEC) has released a request for public comment regarding the content of their proposal to implement and standardise climate-related disclosures by U.S. registered companies.[1] Comments are encouraged to provide analysis of "any aspects of the proposed amendments, other matters that might have an impact on the proposed amendments, and any suggestions for additional changes".[2] Upon review of the proposal, RVF recognizes its potential as a historic leap forward for the U.S. regulatory environment. The proposal's framework ensures that companies in the United States are transparent regarding climate-related risks and that investors can make sustainable, climate-friendly decisions.

We therefore wish to offer our commentary and insight to the SEC regarding elements of the proposal. RVF has identified three areas of interest relevant to the endeavours of our organisation that we wish to address:

- Joining the Global Community in Climate-related Disclosure Frameworks
- Board and Management Governance of Climate-related Risks
- Adoption of Climate-linked Remuneration Disclosures

I. JOINING THE GLOBAL COMMUNITY IN CLIMATE-RELATED DISCLOSURE FRAMEWORKS

Reward Value Foundation acknowledges and supports the SEC's inspiration from the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Since 2017, the TCFD has provided a clear and concise set of guidelines for both regulatory and private sectors. As of September 2021, the TCFD recommendations had received endorsements by over 2,600 organisations and had been adopted by twelve governments, notably the global investment hubs of the European Union, Singapore, Canada, Japan, and South Africa.[3] The regulatory agencies of New Zealand, the United Kingdom, Switzerland, and Hong Kong are set to adopt the recommendations in the coming years.[4] Despite the widespread adoption of the TCFD recommendations by U.S. actors in the private sector, the United States has notoriously

[1] Securities and Exchanges Commission (2022) https://www.sec.gov/news/press-release/2022-46.

[2] U.S. Securities and Exchanges Commission (SEC) https://www.sec.gov/rules/proposed/2022/33-11042.pdf p. 292.

[3] 2021 TCFD Status Report . *Task Force on Climate-related Financial Disclosures*. https://assets.bbhub.io/company/sites/60/2021/07/2021-TCFD-Status_Report.pdf p. 3.

[4] What is the TCFD and why does it matter? . *Deloitte*. https://www2.deloitte.com/ch/en/pages/risk/articles/tcfd-and-why-does-it-matter.html.

suffered from a piecemeal and often discordant climate-related disclosure framework among companies. Robust and uniform metrics on financial data that chart companies' exposure to climate-related risks and opportunities are highly needed. The alignment of SEC policy with TCFD guidelines in governance, strategy, risk management, and metrics opens the door for a more collaborative international approach to sustainable and climate-friendly corporate governance practices.

Moving forward, it is thus imperative that the regulatory actors of the United States recognise the importance of standardisation on the international level. The guidelines of the TCFD have served as an effective starting point for such standardisation, which has proved impressively applicable across a diverse array of countries. Jurisdictions have found common ground with the guidelines. However, we at Reward Value suggest international standardisation goes even further, particularly concerning the International Sustainability Standards Board (ISSB). In March 2022, the ISSB released the first draft of their climate-related disclosure framework, during which ISSB Chair Emmanuel Faber remarked:[5]

"*Rarely do governments, policymakers and the private sector align behind a common cause. However, all agree on the importance of high-quality, globally comparable sustainability information for the capital markets. These proposals define what information to disclose, and where and how to disclose it.*"

The ISSB framework has received endorsements from the G7, G20, the Financial Stability Board and the International Organization of Security Commissions.[6] The B20 under the Italian Presidency highlighted the importance of the ISSB developing a baseline global sustainability reporting standard while allowing flexibility for interoperability with national and regional requirements and taking into account the need to avoid disproportionate burdens on small and medium-sized enterprises. Mobilizing private finance is critical to reaching the goals of the Paris Agreement and the 2030 Agenda. International Financial Institutions (IFIs), together with national governments and national development agencies, have a significant role to play in incentivizing and unlocking private climate financing to facilitate an economy wide transition.[7] RVF strongly recommends that the SEC both monitors the current developments of the ISSB framework and ensures U.S. regulatory compatibility with the final product.

II. BOARD AND MANAGEMENT GOVERNANCE OF CLIMATE-RELATED RISKS

In accordance with the TCFD recommendations on corporate governance, the SEC's proposal calls for the disclosure of "certain information concerning the board's oversight of climate-related risks and management's role in assessing and managing those risks".[8] It is essential to know where senior level responsibility and expertise lies, for accountability purposes but also from a governance / management systems point of view. It is relevant to know which policy commitments are implemented in practice, and by whom. This would include the strategy on non-financial issues that details forward looking information and a statement of management responsibility. From the proposal, we have isolated questions 34 through 39 posed by the SEC regarding such disclosures and address them in whole.[9] Concerning board and

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[5] ISSB delivers proposals that create comprehensive global baseline of sustainability disclosures . *IFRS*. https://www.ifrs.org/news-and-events/news/2022/03/issb-delivers-proposals-that-create-comprehensive-global-baseline-of-sustainability-disclosures/.

[6] Global Sustainability Reporting Edges Closer Through ISSB Baseline . *Environment Analyst*. https://environment-analyst.com/global/108089/global-sustainability-reporting-edges-closer-through-issb-baseline.

[7] https://www.b20italy2021.org/wp-content/uploads/2021/11/B20_ResponsivenessReport_30-11.pdf

[8] U.S. Securities and Exchanges Commission (SEC) https://www.sec.gov/rules/proposed/2022/33-11042.pdf p. 93.

[9] Ibid., p. 98-99.

management oversight, Reward Value Foundation expresses its support for the following proposed disclosure requirements:[10]

- *Require a registrant to identify any board members or board committees responsible for the oversight of climate-related risks*
- *Require disclosure of whether any member of a registrant's board of directors has expertise in climate-related risks, with disclosure required in sufficient detail to fully describe the nature of the expertise*
- *Require a description of the processes and frequency by which the board or board committee discusses climate-related risks*
- *Require disclosure about whether and how the board or board committee considers climate-related risks as part of its business strategy, risk management, and financial oversight*
- *Require disclosure about whether and how the board sets climate-related targets or goals and how it oversees progress against those targets or goals, including the establishment of any interim targets or goals*

It is essential that boards recognise climate-related risks as akin to traditional corporate concerns, and that this perspective is normalised in their corporations' risk management strategy. For both shareholders and stakeholders to be properly informed of a corporation's climate strategy, transparency of board behaviour, composition, and goal setting is fundamental. The SEC has asked whether their current rules, which require a registrant to provide the business experience of its board members, removes the need for a disclosure of a relevant board member's experience with climate-related risk.[11] The transition to sustainable practices in all sectors has been a highly collaborative process and has blurred the lines between industries and their relevant skillsets. Therefore, to limit disclosure to only the business experience of a board member could generate an informational gap for investors, who would be unable to determine climate-related risk experience obtained outside the traditional business setting. Disclosure on governance is essential and should have a central space as it reflects whether a company's commitments are followed through. There needs to be transparency in particular about the Board's expertise, setting targets and addressing business model related aspects of sustainability strategies, as well as integration of KPIs in incentives. These KPIs must be relevant and long-term focused in order to balance more inherently short-term financial metrics.

III. ADOPTION OF CLIMATE-RELATED REMUNERATION DISCLOSURES

Reward Value Foundation welcomes the proposal's discussion of ESG-linked executive remuneration and its request for public comment regarding its relevance. However, we encourage the SEC to reconsider their decision to not implement a remuneration-related disclosure under the umbrella of the examined proposal. RVF recommends that the SEC undergo specific consideration of a disclosure requirement asking a company to declare any links between executive remuneration and the creation of sustainable, long-term value. As argued by the SEC, current regulation in 17 CFR 229.402 (b) mandates the disclosure of "all material elements of a registrant's executive compensation, including the objectives of the registration's compensation programs and what each compensation program is designed to reward". Reward Value acknowledges that this existing framework of guarantees companies disclose their executive

[10] Ibid., p. 94-95.
[11] Ibid., p. 98.

remuneration frameworks, irrespective of their linkage to climate-related risks or other ESG-oriented goals.

However, we strongly believe that the downward pressures on registrants that would accompany a mandated disclosure of executive remuneration linked to long-term value creation could encourage companies to better view the climate transition as a chance for not only adaptation in corporate governance practices, but innovation as well. The climate-related disclosure framework of the ISSB addresses executive remuneration design through two key proposed disclosures:[12]

- *The percentage of executive management remuneration recognised in the current period that is linked to climate-related considerations*
- *A description of how climate-related considerations are factored into executive remuneration*

Reward Value Foundation is optimistic that future cooperation and alignment with the ISSB proposal framework will reopen the conversation for the SEC to implement a climate-linked remuneration disclosure, as well as disclosures on linkages to sustainable, long-term value creation. Incorporating climate-related performance criteria in executive remuneration, addressing material environmental issues, will further align executives to corporate purpose. It is essential that companies put their money where their mouth is and therefore demonstrate their commitment to a sustainable climate through related capex investments, R&D investments, and executive remuneration design.

Sincerely,

Reward Value Foundation

Link to our earlier review of the sec's proposal of "enhancement and standardization of climate-related disclosures for investors"

Executive remuneration today is driven by incentives that may no longer align with shareholder interests or reflect broader societal responsibilities.

Reward Value Foundations' mission is to support the development of remuneration policies that contribute to long- term sustainable and inclusive value creation. The Foundation seeks to further the debate on executive remuneration with investors, business schools, and the business community at large to develop evidence-based, long-term, sustainable, and stakeholder-inclusive executive remuneration policies.

Reward Value Foundation is a not-for-profit research initiative. Reward Value can be reached by email (contact@rewardvalue.org). For more information on Reward Value please visit our website www.rewardvalue.org.

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[12] International Financial Reporting Standards (IFRS) https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/issb-exposure-draft-2022-2-climate-related-disclosures.pdf. p. 42.

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