August 15, 2022

Ms. Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Re: **Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices, File No. S7-17-22 ("ESG Disclosure Proposal"); Investment Company Names, File No. S7-16-22 ("Fund Names Proposal")**

Dear Ms. Countryman,

On behalf of our 500,000 members and supporters across the country, Public Citizen is grateful for the opportunity to comment on the Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices, ("ESG Disclosure Proposal") and the Investment Company Names ("Fund Names Proposal") proposed rules. As an organization that focuses on retail investor protection, we agree with the Securities and Exchange Commission (Commission) that the name of a fund signifies its nature to investors. We support the Commission's goals of addressing misleading or materially deceptive names, especially as marketplace use of the terms "environmental, social, and governance," or "ESG" has evolved in recent years. We appreciate that the Commission has proposed amendments to the Investment Advisers Act and the Investment Company Act that would provide investors with more detailed information about how a fund incorporates ESG factors. It is critical that investors have access to information on which the funds' ESG claims are based so they can evaluate it themselves. Since these two proposed rules are closely related, we have combined our comments on both into one submission (submitted to both comment files) so as to speak to the interplay between a fund's name and its required disclosures. Below, we first address the fund names proposal, then the ESG disclosure proposal.

Fund Names Proposal

We support the proposed rule's purpose of preventing "greenwashing" by assuring that a fund's investment activity is focused in the manner that its name suggests. While "ESG" most accurately refers to the types of long-term risks a company may be exposed to, the term has also come to mean in common parlance investments that generally do not further perpetuate social ills such as human-generated climate change, gun violence, income inequality, personal data collection, or threats to democracy. For these reasons, the Commission is right to propose

updates to the Names Rule to match investors' common understanding of "ESG" so that fund names do not mislead investors regarding how the funds invest. Below, we respond to particular questions the Commission proposed.

Questions 1–15 (Expansion of the 80% Rule)

The Commission should expand the existing requirements, as proposed, to cover fund names that suggest an investment focus or include issuers that have particular characteristics in their portfolio such as those that focus on sustainable investments or promote ethical business practices. It is also appropriate to keep the scoping requirement as proposed so that it does not distinguish between types of investments and investment strategies. It is not reasonable to assume that retail investors believe that fund names reflect their underlying investments in some areas but not in others. The Names Rule should absolutely apply the 80% requirement to fund names with terms such as "ESG" and "sustainable" as proposed. Investors rely on these terms in fund names.

Questions 52–57 (Disclosures Regarding Terms in Fund Names)

We support the enhanced prospectus disclosures that require a fund to explain how it defines terms used in its name and provide the criteria it uses to select investments. Given the growing market share of "ESG"- related products and the increased investor interest in these types of investments, it is important that fund managers explain, in plain English, how they define the terms in the fund name so that investors may compare that to their understanding of the term. As stated above, investor expectations around terms such as "sustainable" or "socially responsible" are evolving, and it is critical that investors be able to easily understand how a fund defines them. Even when a fund is not in violation of the "materially misleading" standard, an investor could have a different expectation for the term "sustainable" than the fund manager intended, and she needs enhanced disclosure in order to determine if investing in this fund meets her expectations.

Questions 58–62 (Plain English and Established Industry Use of Terms)

The proposed requirement that funds subject to the 80% rule use terms in their names that are "consistent with those terms' plain English meaning or established industry use" is an important provision of the proposed rule because it prevents funds from defining a term such as "ESG" or "sustainable" in a way that is inconsistent with investors' expectations. While it is critical that an investor have access to information about how a fund defines a term used in the fund name, as stated above, in instances where investors only use fund names when making investment decisions, those names should not be inconsistent with investors' reasonable expectations. Additionally, the agency should clarify that, if an established industry use of a term is inaccurate or misleading, then the "established industry use" principle emphatically does not apply.

Questions 63–65 (Integration Funds)

We strongly support the proposed approach of considering the names of Integration Funds materially deceptive or misleading if they use terms that inaccurately suggest the funds' investment decisions are based on ESG factors. While the argument in favor of taking ESG factors into consideration when investing suggests that all investment advisors should be considering the long-term risks associated with their portfolio companies, the use of an ESG term in a fund name strongly suggests that the ESG factor has special significance in investment decisions. The ability for a fund to call itself ESG and benefit from that marketing while not considering ESG factors above any other material factors should not be allowed.

ESG Disclosure Proposal

We support the aim of the disclosure rule to provide investors with more detailed information about how investment advisors consider ESG factors for their funds. Increasing disclosure by investment managers and advisors is squarely within the Commission's mandate because transparency is key to efficient capital markets and investor protection. We also support the proposed rule's goal, in conjunction with the Names Rule, of preventing investment managers and advisors from misleading investors about how and to the extent to which a fund considers ESG factors. Millennials have been a significant demographic undergirding ESG investing with contributions of $51.1 billion to sustainable funds in 2020 compared with less than $5 billion in 2015. The trends of younger investors speak to longevity and that ESG investing is here for the long haul. According to polling retrieved by Yahoo Finance-Harris, about 95% of millennials and 97% of the subsequent Gen Z generation are familiar with ESG investing and indicated that a company's ESG factors played a role in their investment choices.[1] Beyond just Millennial and Gen Z investors, the market for ESG investing is continuing to expand significantly. According to Bloomberg Intelligence, ESG assets are primed to increase to $41 trillion by the end of 2022, and further estimates project ESG assets at $50 trillion by 2025.[2]

Questions 3-11 (Integration Funds)

We encourage the Commission to consider whether the proposed Integration Fund category serves the proposal's purpose. ESG integration continues to rise around the world, with "the proportion of global ESG users [at] 89%—up from 84% in 2021."[3] Investor demand for more

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[1] Tiffany Robertson, *Millennial and Gen Z Investors Grow to Embrace ESG Issues*, IMPACTIVATE (Dec 7, 2021), https://bit.ly/3pq5kPa.
[2] James Royal, *What is ESG investing? A guide to socially responsible investing*, BANKRATE (April 10, 2022), https://bit.ly/3JV1VkS.
[3] Jessica Ground, *ESG Global Study 2022*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE, (June 17 2022), https://tinyurl.com/yt6hrpxu.

comprehensive disclosures of ESG information as demonstrated through the shareholder proposals filed on a wide-range of ESG issues every proxy season—from political spending disclosure, to tax transparency, and more—cements both the deep investor interest in and the materiality of these issues.

As stated above, we support the provision in the Names rule that prohibits ESG Integration Funds from using the term "ESG" in their names. However, even with this caveat, it is hard to see how the Integration Fund category wouldn't result in investors being misled by at least some of those funds, if not a large proportion of them. Integration Funds would have an incentive to use their partial consideration of ESG factors in advertising or other materials in a manner that overstates the significance of those factors in their decision making, and it would be difficult for the Commission to fashion guardrails sufficient to foreclose every means of misleading investors. Moreover, many, if not most, funds ought to consider ESG factors at least to some degree, as those factors often overlap with what-- in the absence of ESG considerations--would simply be considered material risks. Therefore, by creating the category, the Commission would likely generate a heavy enforcement burden for itself—as well as leave many investors unprotected. The Commission should eliminate the Integration Fund category and simply require funds that use ESG terms in their names to provide disclosures at the ESG-Focused Fund level. This would not undermine the existing requirements for non-ESG funds to disclose material ESG risks to their investors, but would require funds seeking to use ESG terms in their names and marketing materials to provide the robust disclosures required under ESG-Focused Funds.

If the Commission keeps the Integration Fund category, we support the proposal to require that Integration Funds that consider GHG emissions provide more detail about their methodology in their prospectuses. If the Commission keeps the Integration Fund category, then it is imperative to maintain the provision in the Names rule that prohibits Integration Funds from using the term "ESG" in their names. We also suggest that the Commission require additional information about the Integration Fund category in the fund prospectus to ensure that investors are not misled by this classification. The Commission should require that upon the first use of the term "ESG Integration Fund" in their prospectuses and marketing materials, these funds should have to clarify that an ESG Integration Fund is a fund in which ESG factors do not determine the makeup of the fund. Even though an Integration Fund cannot use the term "ESG" in the fund's name, if the fund uses the term "ESG Integration" at the beginning of its prospectus or marketing materials without clarification as to the definition of the term, an investor may think the fund considers ESG factors more significantly than it does due to a lack of common understanding of the term "ESG Integration" as the Commission defines it for the purpose of this rule. Again, we believe that *any* use of terms like "ESG Integration" will have a tendency to overstate the significance of ESG factors in the fund's decision making to all but the most cautious and fine-print-wary investors, and therefore we believe the Commission should not create the category.

Finally, if the Commission establishes the Integration Fund category—or even if it does not—it should expressly clarify that nothing in the final rule is intended to diminish funds' ordinary obligations to disclose material information to investors. Even funds that are neither ESG Focused Funds nor Integration Funds will still be obligated to disclose information about ESG factors to the extent they are, or are closely related to, material risks. Indeed, given the prevalence and significance of analyzing ESG issues and risks, all investment advisors should be weighing ESG factors to some degree in their portfolios.

Questions 25- 51 (Disclosure for ESG-Focused Funds)

We support the Commission's goal to require detailed disclosure from ESG- Focused Funds so as to provide investors with the ability to determine whether a fund aligns with their investing goals. We also support the Commission's proposal to require a succinct disclosure in the Summary Table followed by more detailed disclosure later in the prospectus. This allows an investor to better understand a fund's ESG goals and strategy at- a- glance for comparative ease, while also allowing the investor to dig deeper into particular details.

We support the disclosure requirements for funds that track ESG indexes. It is critical for retail investors to understand whether the makeup of the ESG index their fund follows meets their ESG investing expectations. However, the proposal is not clear as to whether funds that track indexes will have as robust disclosures as actively managed funds. The Commission should consider ESG indexes actively managed and therefore subject to the same disclosure requirements as traditionally actively managed funds. Index providers often make decisions about what is included in an index that involves a not insignificant amount of discretion on the part of the provider.[4] In those instances the index provider functions the same as an investment advisor. The proposal requires ESG Focused funds that track an index to disclose a short description of the makeup of the index in the Summary Table, plus a lengthier discussion of the index's methodology later in the prospectus. We support these disclosures but encourage the Commission to clarify what it expects from the disclosures around an index's methodology and that those disclosures are just as robust as those for an actively managed fund.

Questions 58- 61 and 81-86 (Engagement Disclosure for ESG-Focused Funds)

We support the Commission's implicit recognition that many large fund managers hide behind claims of engagement strategies as a way of avoiding actual decarbonization. Investors deserve to know whether a fund's engagement strategy of holding securities in high polluting industries comes with a robust plan to hold those companies accountable for their transition plans or whether the fund managers are trying to solicit investments in the fund under the guise of being

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[4] Paul G. Mahoney, Adriana Robertson, *Advisors By Another Name*, (January 15, 2021), https://tinyurl.com/4wutfhaf.

ESG without having to divest from those industries. This applies to other ESG issues as well where fund managers can tout their engagement strategy as a way to avoid divesting from companies that have poor labor practices, obscured tax practices, or misaligned political spending.

We offer suggestions to improve the engagement metrics proposed by the Commission. The metrics the Commission proposes don't capture the entire picture of investor engagement and the Commission's focus on the number of meetings may result in funds increasing their number of meetings without meaningfully evolving their engagement strategy. We support the proposal's requirement that funds provide disclosure of "an overview of the objectives," the time horizon for those objectives, and how the fund measures the effectiveness of its engagements. This disclosure should be expanded to include details about whether the fund has criteria for when an engagement fails and whether the fund takes certain actions (withholds board votes, files shareholder resolutions, changes capital allocation) when engagement has failed. Additionally, as part of its discussion of engagement strategy, the fund should discuss what kinds of shareholder resolutions it will and won't support based on the ESG- related goals of the fund. Further, we believe it would be more useful to investors if funds have to quantify research and analysis of companies, report surveys or other correspondence with companies, report annual number of shareholder proposals filed, report any changes to the fund as a result of engagements, and report how many staff are involved in the engagement process, in addition to reporting the number of meetings held. Finally, if a fund has a net zero by 2050 target, it should be required to disclose intermediate milestones and the level of decreased emissions and transition investment they expect from investment targets to meet those milestones.

Questions 87-127 (Disclosure of GHG Emissions)

The Commission should remove the stipulation that only "publicly provided" Scope 3 emissions from portfolio companies must be disclosed and use the same standard as for Scopes 1 and 2 emissions: "comprehensive disclosure with reasonable estimates."

At the portfolio company level, direct emissions (Scope 1) and emissions from purchased electricity and heat (Scope 2) provide context for certain important financial estimates and assumptions, particularly related to the value of long-lived assets and the sustainability of certain operating costs. Disclosure of emissions from across the value chain (Scope 3) are perhaps even more critical, as they provide information about potential transition risks to a portfolio company's supply chain or revenue base and about opportunities to partner with customers and suppliers on mitigating this risk.

Reliance on only "publicly provided" data will yield unacceptable data gaps that will reduce the comparability and completeness of resultant emissions figures. It is currently a standard financial

industry practice to calculate financed GHG inventories for Scopes 1, 2, and 3 using a combination of publicly-available data, engagement with portfolio companies, and commercially available datasets from data aggregators like MSCI or CDP, which often rely on reasonable estimates to fill data gaps.[5] The SEC should look to the data quality hierarchy developed by the Partnership for Carbon Accounting Financials (PCAF)—the leading standard for calculating financed emissions—to establish more detailed guidance on data quality, and the Commission should expand the proposal's data hierarchy to require incorporation of "commercially-available" data as well.[6]

Additionally, the proposal's definition of "portfolio company" is appropriate and funds' investments in other funds and private funds should be included in the GHG emissions calculations. It is critical that fund-of-fund structures not be allowed to obfuscate GHG emissions risk or bypass reporting.

Funds should use measured data or reasonable estimations of underlying funds to determine their own GHG emissions, along with disclosure of their methodology, any significant estimates, assumptions, or uncertainties, and data sources. For parent funds that invest in other covered registered funds, GHG emissions data can be calculated by the share of the fund's investment multiplied by the GHG emissions of the investee fund. For funds for which no publicly reported data is available, funds should rely on engagement with investee funds and companies, commercially available data, and should be allowed to make reasonable estimates by using emission factors multiplied by available activity data, or if activity data are unavailable, economic data. To promote data comparability and quality, registrants should be required to use emission factors from the Environmental Protection Agency[7] if available, or if not, describe the alternative source used.

The Commission Should Continue Work to Require Disclosure of Key ESG Metrics from Issuers

We commend the Commission for prioritizing ESG disclosures for mutual funds. These funds have a significant impact on the livelihoods of many investors. With an unprecedented number of shareholder proposals voted on during proxy season, it is evident that investors have a renewed focus surrounding action on ESG.[8] We ask the Commission to swiftly adopt rules around ESG disclosure for funds and additionally we ask that the Commission require disclosure of all of the ESG issues, including climate; political activity; tax; diversity, equity, and inclusion; human capital management practices; and human rights from issuers.

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[5] *The Global GHG Accounting and Reporting Standard for the Financial Industry*, PARTNERSHIP FOR CARBON ACCOUNTING FINANCIALS, (Nov. 18, 2020), https://bit.ly/3piMlWL.
[6] *Id*.
[7] *Emission Factors for Greenhouse Gas Inventories*, ENVIRONMENTAL PROTECTION AGENCY (viewed on August 15, 2022), https://bit.ly/3QLBW1w.
[8] Garnett Roach, *Record-Breaking Proxy Season for ESG Proposals, Report Says,* CORPORATE SECRETARY, (March 17, 2022), https://tinyurl.com/2fm2nzf2.

We encourage the Commission to think about how the disclosure rules for investment advisors and investment companies will interact with future issuer disclosure rules on ESG issues. Until the Commission adopts requirements for issuers to disclose further ESG information such as human capital management, political activity, tax information, and human rights, investors will continue to lack a complete picture of how a fund is considering ESG factors because the investment advisors are not able to access consistent, comparable, and decision- useful underlying data.

We elaborated on the climate metrics we believe investors need in our comment to the Enhancement and Standardization of Climate-Related Disclosures for Investors proposed rule.[9] In particular, it is critical for the Commission to require disclosure around climate justice issues. Investors need to understand how companies assess, manage, and mitigate impacts on communities that stem from regular business operations, climate mitigation efforts, and transition activities. These include impacts caused by land use change and deforestation; infringement of land rights; natural resource extraction; disruption to local economies; air and water pollution; harm to public health and safety; and worker dislocation. Companies engaged in harmful activities that exacerbate climate change and racial and environmental injustices are increasingly exposed to operational, reputational, and liability risks that carry a heavy financial burden. Investors want more information on risks and plans to mitigate risk related to laws, regulations, or policies that require enhanced pollution controls, protection of Indigenous or tribal people's land rights, worker or public safety and health, and mitigation of negative environmental justice and community-level consequences.

Investors in the United States have made it increasingly clear that they value public country-by-country financial reporting as well. Public country-by-country reporting (PCBR) would require public multinational corporations to report a breakdown of taxes paid, revenue, employees, subsidiaries, and other pertinent financial information in each country where the company has operations. PCBR would reduce the desirability of multinationals shifting their profits to tax havens and would make investors aware if the companies in which they invest are using risky avoidance strategies. A report from the Institute for Taxation and Economic Policy illustrated how 55 extremely profitable US based multinational corporations paid nothing in U.S. taxes in 2020, and we believe this is information their shareholders have a right to know. This issue area is also a space where there is growing momentum when it comes to shareholder proposal activism. A recent example of this can be seen with the 2022 Amazon annual shareholder resolution calling for public tax transparency. In fact, more than 21% of independent Amazon

[9] Letter from Americans for Financial Reform, Public Citizen, Sierra Club, Ocean Conservancy, and The Sunrise Project to the Securities and Exchange Commission Re The Enhancement and Standardization of Climate-Related Disclosure for Investors (June 16, 2022), https://bit.ly/3dwXUHr.

shareholders voted in favor of public country-by-country reporting, a very strong showing considering this was a first-of-its-kind proposal at that company.[10]

Investors are also concerned about the erosion of democracy and the risks posed by the corporations spending undisclosed amounts of shareholder money in politics. In the U.S. our capital markets need a robust and fully functioning democracy to thrive. Following the attack on the U.S. Capitol on January 6th, 2021, many large corporations made the decision to suspend donations from their political action committees (PACs). The Conference Board, a global business membership and research nonprofit, surveyed corporations to learn more about their responses to the insurrection. Of the 84 firms that responded, "46% cited the belief that a stable democracy is necessary for a stable business environment," and nearly 45% cited concerns about the company's reputation.[11] A company's political activity–both its election spending and lobbying–is relevant to its shareholders because it can present significant reputational risk if not disclosed and managed properly. Many customers and the purchasing public are paying close attention to whether a company's political activity lines up with its corporate values. If there is a disconnect, companies can face bad press, boycotts, or targeted social media campaigns.

Public Citizen also supports issuer disclosure of human capital management and human rights data and associated risks. The Commission has listed a potential human capital management disclosure rule on its regulatory flexibility agenda recently and we hope to see a proposed version of that rule soon. It is critical for investors to understand how companies are thinking about their evolving workforce, especially in a post- pandemic landscape. Additionally, investors need comprehensive information about human rights risks throughout a company's supply chain and the steps taken to execute due diligence to mitigate human rights violations throughout the supply chain. Public Citizen supports an issuer disclosure rule on human rights due diligence.

Cost-Benefit Analysis for Both Proposals

Regarding cost-benefit analysis, the proposals show that the benefits of the rules exceed their costs and are in the interest of protecting investors. While cost-benefit analysis should not be a determinative factor for proceeding on the rules, these proposals in any event are overwhelmingly beneficial on net.

Conclusion

We appreciate the Commission taking our comments into consideration on these two rules. In summary, we support the Commission's mission to provide investors with better tools to understand how investment advisors and investment companies use the term "ESG" and to

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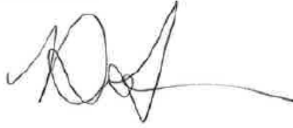
[10] *Shareholders Representing $144 Billion Endorse Tax Transparency Shareholder Proposal Co-filed by FACT Coalition Member,* FACT COALITION (May 27, 2022), https://bit.ly/3vtZH67.
[11] *Survey: Corporate PACs Took Unprecedented Action by Broadly Suspending Political Contributions Following Capitol Riot,* THE CONFERENCE BOARD (Feb. 12, 2021), https://tinyurl.com/2p8725zp.

reduce the instances of "greenwashing" in mutual fund names. We look forward to supporting the Commission's work to implement the rules. For any questions, please contact Rachel Curley [redacted].

Respectfully,



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Cc: The Honorable Gary Gensler, Chair
The Honorable Hester M. Peirce, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner
The Honorable Mark T. Uyeda, Commissioner
The Honorable Jaime Lizárraga, Commissioner