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The House Financial Services Subcommittee on Investor Protection, Entrepreneurship and Capital Markets held a hearing today on "Building a Sustainable and Competitive Economy: An Examination of Proposals to Improve Environmental, Social and Governance Disclosures."

CHAIRWOMAN CAROLYN MALONEY (D-NY) called the hearing to order. She said that investors overwhelmingly want companies to disclose ESG information, because evidence has shown a correlation between ESG performance and economic success. Many companies already disclose some ESG information, but Maloney believes that more can be done. These disclosures are not standardized, and are often not detailed or broad enough, and cannot be easily compared.

Other federal agencies have already recognized the value of ESG disclosures, she said, citing an announcement today from the CFTC. Now it's time for the SEC to act. Several of the bills under consideration today would require the SEC to set standards for ESG disclosures. She described the provisions of the five pieces of legislation under review today:

- H.R.____, the "ESG Disclosure Simplification Act of 2019" [DRAFT]
- H.R.____, the "Shareholder Protection Act of 2019" [DRAFT]
- H.R.____, the "Corporate Human Rights Risk Assessment, Prevention, and Mitigation Act of 2019" [DRAFT]
- H.R.____, To require issuers required to file an annual or quarterly report under the Securities Exchange Act of 1934 to disclose the total amount of corporate tax such issuer paid in the period covered by the report, and for other purpose [DRAFT]
- H.R.____, the "Climate Risk Disclosure Act of 2019" [DRAFT]

Those who say the SEC shouldn't mandate ESG disclosures because they should only require information that is material are misguided, she said. The SEC is in no position to know what is or isn't material, and they have a long history of requiring disclosures of nonmaterial information.

REP. BILL HUIZENGA (R-MI) the Subcommittee's ranking member said that ESG data and criteria span a range of issues, including subjective judgments of what a "harmful" activity constitutes. SEC Commissioner Hester Peirce has said that ESG stands for "enabling shareholder graft," and has said that "naming and shaming" has become a profitable game. Companies have voluntarily increased their ESG disclosures, but should be focusing on meaningful material information that gives investors the information they need to invest wisely.

Best practices will bubble up to the top, Huizenga said. If these disclosures are good business, companies will move to adopt them. They should not be forced upon companies under penalty of law, and every company should be able to make its own decisions about which of these disclosures are material. Politically mandated disclosures will only create new barriers to IPOs and suppress those numbers further. Huizenga said the SEC needs to focus on its current mandates, and that mandating further disclosures will do more harm than good. Lawmakers should be trying to encourage more IPOs, not harm them.

REP. JUAN VARGAS (D-CA) said his bill, the ESG Disclosure Simplification Act of 2019, was timely because investors increasingly consider this information to be material, and evidence shows that companies that consistently provide this information perform better and deliver more stable returns. This isn't about naming and shaming, he said; this is about protecting investors and the environment. Last fall a coalition of asset managers petitioned the SEC for a rulemaking on ESG disclosures, which was the impetus for his bill.

"Climate change is real," he said. "It's not a Chinese hoax." Therefore it's important to have this information readily available, and standardized.

REP. PATRICK MCHENRY (R-NC), ranking member of the full Committee, said that Congress needs to help everyday investors, and can best do that by making markets more competitive. The number of publicly listed companies has declined by half, and today's hearing misses the mark in ignoring this trend. The proposals under consideration today would discourage companies from going public, and discourage public companies from remaining public.

Chairwoman Maloney welcomed the witnesses:

- Tim Mohin, Chief Executive, Global Reporting Initiative (GRI)
- James Andrus, Investment Manager-Financial Markets, Sustainable Investment, CalPERS Investment Office
- The Honorable Paul S. Atkins, Chief Executive Officer, Patomak Global Partners
- Degas A. Wright, CFA, Chief Executive Officer, Decatur Capital Management, Inc.
- Mindy S. Lubber, President and Chief Executive Officer, Ceres

Testimony

MR. MOHIN described GRI as the largest standard-setter for ESG practices. GRI welcomes the ESG Disclosure Simplification Act of 2019. It would level the playing field for companies and investors, and would not increase reporting burden because the vast majority of companies are already reporting this information. What it would do is make it easier for investors to compare practices.

Mohin described the history of GRI, which operates on the principle that "you manage what you measure." Measuring ESG performance improves it; Mohin said he'd seen this in practice. It's not just about accountability to investors; it also helps guide decisions within the company.

GRI completely revamped its governance model by modeling it on the one used for financial standards. About 600 companies currently use the GRI standard, representing about 80% of the Dow Jones Industrial Average.

The global market for this information is exploding, Mohin said, because investors know that nonfinancial information can have significant effects over the long term. It's essential that this Committee focus on a single global standard. He said that Rep. Vargas's bill will protect investors, help unlock free trade, and help align capital to sustainable business practices.

MR. ANDRUS described CalPERS as "a reasonable investor." He applauded the Committee's efforts to build accountable, sustainable corporate governance.

CalPERS is the largest private pension fund in the United States, he said. The CalPERS Board has developed governance and sustainability principles that guide its investment decisions and proxy voting. The Board adopted a five-year ESG strategic plan in 2016, and his testimony today is based on the principles of that plan.

Long-term investors can use more information in several areas, Andrus said, including human capital disclosures.

CalPERS principles call for robust board oversight and disclosure of corporate charitable and political activities to ensure alignment with business strategies and protect corporate assets. He cited the Citizens United decision's call for prompt disclosures of this activity, and urged Congress and the SEC to move quickly to require them.

Next, he said, detailed disclosures related to climate risk are essential. ESG disclosures should be robust and consistent, integrated into other reporting. Corporations should adopt maximum progressive policies supporting human rights, so CalPERS supports that bill as well.

CalPERS' principles also call for a focus on emerging systemic risk and fostering actions to mitigate these risks. Current tax disclosures in the US do not provide investors with sufficient information to adequately assess companies' values and risks. The legislation before the Subcommittee would require disclosure of overly aggressive international tax planning arrangements, and CalPERS supports it.

MR. ATKINS said he wanted to focus on the significant costs imposed by disclosure requirements on both large and small businesses, investors, workers, and the economy. The SEC has generally focused on information it considers important to the "reasonable investor." Disclosure costs are real and not harmless, he said; just three provisions of Dodd-Frank cost industry more than $2 billion a year.

Disclosure overload is being used as a blunt instrument to try to impose normative outcomes, and a growing body of evidence shows that they hinder the goal of sustainable growth. Atkins pointed to the decline in IPOs, which affects the broader American economy, and particularly job growth.

The Treasury Department under the Obama administration recognized this and put a task force together to study the problem; of the CEOs surveyed, almost 75% cited public disclosures as a major barrier to IPOs. The JOBS Act of 2012 recognized this as well, and lifted regulatory burden on emerging growth companies. The number of IPOs has risen since then, but more remains to be done.

All of the bills under consideration today are well-intentioned, but many of them would duplicate existing requirements and most of them would create new and unnecessary burdens.

MR. WRIGHT described his company, Decatur Capital Management. He is an investment manager who conducts research on behalf of his clients, and has found that ESG disclosures often provide material information. Political contributions, in particular, are often material, as CEOs believe that political uncertainty represents risk. As political risks increase, political contributions increase. Therefore, large political contributions reflect a company's sense of greater political risk, and stock prices often decline accordingly.

The impact of climate risk on securities pricing is difficult to measure for several reasons, but as an investor, he treats climate risk as one factor among many. Current levels of emissions and emission targets are important for manufacturing companies, for example.

The amount of income tax a company pays is material to its financial success. Corporate tax avoidance programs, while perfectly legal, may suggest underlying regulatory or reputational risk, and therefore that information is material as well. Disclosure of human rights and value chain risk is also material, he said. He supports all the bills under consideration today.

MS. LUBBER thanked the Subcommittee for considering these bills. Her organization, Ceres, addresses investing for sustainability. They strongly support the Climate Risk Disclosure Act of 2019. These bills are rooted in the principles of transparency, materiality, and the right of investors to have the information necessary to evaluate prospects for long-term returns.

Ceres runs an investor network for environmental sustainability, and their investors believe that climate/sustainability risk is a material risk embedded in the financial system. "Risks are risks, and they need to be disclosed."

In 2010, Ceres petitioned the SEC to issue the first climate disclosure guidance, which is not being enforced. Despite this guidance, nearly half of the largest 600 US companies still don't provide decision-useful disclosures about climate-related risks. Many that do provide disclosures are just issuing boilerplate, effectively meaningless. Investors aren't getting the information they need about how their portfolios are exposed to climate risk. Requiring meaningful disclosure will lead to innovation and smarter management — she repeated, "What gets measured, gets managed."

Climate change is the greatest risk facing the economy, she said, from food/agriculture to transportation/energy to manufacturing and on and on. Apple, Levi Strauss, The Gap and others understand this, which is why they're disclosing these risks. Companies that provide these disclosures are more likely to set relevant goals and have resilience plans in place. She said the requirements of the bill under consideration are thoughtful and should be effective.

Q&A

CHAIRWOMAN MALONEY asked Mr. Andrus whether he considers ESG disclosures to be material.

"Yes," he said. All the bills under consideration today deal with material information. There's no one definition of materiality; one definition focuses on the past, while another considers probability x magnitude, focusing on the future. The SEC focuses on "forward information," with a two-pronged test that would include all the information called for by the bills under consideration today.

Beyond that, he said, is the debate over what information "reasonable investors" want. He considers CalPERS a "reasonable investor," and they want more of this information. It's not a US-only issue, either; investors all over the world are focused on these issues.

Maloney asked Mr. Wright whether he agreed with this. Wright did.

Maloney asked Mr. Mohin whether the SEC could build on GRI's work in this area. Mohin said yes, and his written testimony discusses this at greater length. International standards are important, as seen in the development of international standards that FASB aligned with. He recommends that the SEC refer to an independent standard-setter like GRI.

Maloney asked Ms. Lubber whether Mr. Casten's bill would require sufficient detail for climate disclosures, and how important it is for the SEC to promulgate sector-specific requirements. Lubber said this bill was perfectly consistent with the SEC's mandate, because these risks are real, as PG&E has found.

REP. HUIZENGA asked how it helped CalPERS beneficiaries when the fund lost $3 billion by divesting from tobacco-related products. He noted that the new president of CalPERS has criticized the fund for prioritizing social goals over profitability.

He asked Mr. Atkins to describe how IPOs help the economy. Atkins said that IPOs help private companies attract more capital. Huizenga asked whether these bills would encourage IPOs or drive more companies into the private capital world. Atkins said that requirements like these are among the biggest impediments to IPOs.

Huizenga said he'd been dealing with the after-effects of Dodd-Frank's conflict minerals prohibition, which will cost billions per year and impose a role on the SEC that it doesn't want. He asked Atkins what he thought of Mohin's suggestion that GRI set standards for the SEC to follow. Atkins said it was best to leave these decisions to the private market.

Huizenga asked Atkins whether the federal government should be forcing large and small companies to disclose this information, when some companies are already doing it voluntarily. Atkins said it would raise both direct and indirect costs. Huizenga said that keeping this voluntary would be most effective.

REP. VARGAS asked Mr. Atkins whether he believed that climate change was real. Atkins said it doesn't matter what he thinks. Vargas said it matters to him. Atkins said he hadn't studied it, but obviously it was a topic of discussion in the public sphere. Vargas pressed him on this, but Atkins said he hadn't focused on it.

Vargas said that when we learned that CFCs were destroying the ozone layer, we took action that proved effective. Fires in California are bigger and hotter, and insurance actuaries are seeing the facts. That's why these disclosures are important, and he's sorry that the US isn't leading on this.

Vargas asked whether these disclosures might actually increase shareholder value, rather than reducing it. Mohin agreed with this, and thanked Vargas for introducing the legislation. If these issues were disclosed in an orderly fashion, investors would be better equipped to make decisions. Companies that use the GRI standards for reporting are seeing their benefits, but it's important to level the playing field and require this reporting from everyone.

Andrus agreed that this is valuable information, which is why they're asking for comparable information from all companies.

Vargas said that climate change isn't the only issue, but it's "super important."

REP. MCHENRY yielded to **REP. FRENCH HILL (R-AR).**

Rep. Hill said he believed that officers and directors of public companies have a fiduciary duty under the business judgment rule. Material information should be disclosed, and that's a fundamental part of our system. In general, he thinks companies do this. They balance this with the costs associated with reporting. He said that CalPERS' decisions have not benefited its beneficiaries, but beyond that, the declining number of public companies means CalPERS has fewer investment choices.

Hill too cited the conflict minerals rule as an example of good intentions doing harm; a constituent told him that her company's compliance with the rule costs it $250,000 a year, with no feedback about whether they're complying appropriately or not. Nor have they ever had a question from an investor about conflict minerals. Congress shouldn't be deciding on materiality when a board hasn't decided something isn't material, he said.

Finally, Hill read an alarming article warning against a climate disaster that could submerge Florida and the Netherlands within the next 50 years — and said that the article had been written in 1978.

Hill asked Mr. Atkins whether penalties exist for failing to disclose material information. Atkins said yes, from both the SEC and private litigation. Hill repeated that officers and directors should have the discretion to make decisions about what is and isn't material.

REP SEAN CASTEN (D-IL) said that more than 200 of the world's largest listed companies have said that climate change could cost them more than $1 trillion, but US investors generally don't have information about the impact of climate change on companies' business plans.

It's not just private investors, either; Casten asked Chairman Powell at a hearing earlier this year whether Fannie and Freddie are calculating climate change-related risks to 30-year mortgages on properties in low-lying areas, and Powell said "that would be an interesting thing to think about," but he wasn't sure. "That's a big deal," Casten said. The SEC wasn't created to allow companies to hide information; it was created to ensure the disclosure of information to protect investors.

Casten said that his bill would effectively end the implicit subsidies to companies that aren't currently disclosing these risks. He entered into the record a letter signed by 33 companies endorsing his bill.

Casten cited a G-20 study that found only about 25% of the largest companies disclose climate risk. He asked Ms. Lubber whether his bill would represent a meaningful improvement for investors. Lubber said, "No question." These disclosures need to be consistent and comparable, and the SEC should require them. This ought not to be considered an extraordinary additional burden, she said.

Casten asked Mr. Mohin whether companies would need to "reinvent the wheel" to comply with his bill, or are the templates largely in place? Mohin said the templates are largely in place.

Casten asked Mr. Wright what the long-term risks to investors are from companies that fail to disclose these risks. Wright said that many companies have already started to report this information voluntarily, but it's not consistent, so it's important to get this consistency.

REP. ANN WAGNER (R-MO) said the US continues to experience a slump in the number of new businesses, and the number of IPOs remains about half what it was 20 years ago. She noted the growth in new companies abroad, especially in China, and said the US ought to be encouraging more growth and more IPOs — more investment opportunities, more choices for Main Street investors. China produced more than 1/3 of the world's IPOs last year, she said, and asked Mr. Atkins why we should be concerned about this. Atkins said robust capital markets are good, but going to the public market has become more expensive and subjects companies to a lot more regulatory expense.

Wagner asked how the JOBS Act has encouraged more IPOs. Atkins described its provisions to increase access to capital. Wagner asked what else Congress should be doing. Atkins said, "Reduce regulatory burden," and again cited the conflict minerals law.

REP. HUIZENGA suggested that since companies are already doing things they perceive to be good practice, new federal laws may not be necessary.

REP. BILL FOSTER (D-IL) cited an LSE report that found climate change litigation has been brought in at least 28 countries, with investors bringing cases against companies for failing to disclose climate change risk. He asked what the rise in lawsuits tells us about the need for better disclosures. Lubber said they're seeing more lawsuits, not only from investors but also relating to fiduciaries and board members of these companies. Board members say they want more information, they don't want to be sued; they understand their fiduciary obligation. Making this information available to everyone will help. Without additional disclosures, litigation will grow. Foster said that requirements for disclosure would probably reduce litigation. "Better information leads to better decisions," Lubber said.

Andrus said there's increasing evidence that this information is material, and needs to be disclosed.

Foster asked Mr. Wright how having comprehensive emissions information in a given sector could help investors make decisions. Wright said that environmental data affects stock prices, and better information would help everybody. Where companies are making transitional plans that can be priced into their stock valuation.

REP. WARREN DAVIDSON (R-OH) said he thought today's witnesses just want to look at a broader definition of fiduciary duty. He asked whether each of their firms currently use ESG standards in investment decisions.

Mohin said they were standard-setters, so don't make investment decisions. Andrus said yes. Atkins said they were a consulting firm, so don't make investment decisions. Wright said yes. Lubber said that all their member firms make decisions based in part on ESG risks. Davidson said the studies are varied on the performance of companies that use ESG standards.

He drilled Andrus about the underfunding of CalPERS, but Andrus said it was important to note that today's discussion is about disclosures. Davidson quoted Jason Perez as saying it cost CalPERS $8 billion to divest from tobacco, and suggested that this was a violation of CalPERS' fiduciary duty. Ohio teachers don't care about ESG if their retirement isn't secure. He thinks the market should make these decisions, and asked Atkins about decisions to move from one company in a sector to another based on ESG factors. Atkins said that ESG disclosures are often squishy.

Davidson said he'd like to have a hearing on how proxy advisors are influencing ESG.

REP. DAVE SCOTT (D-GA) asked Ms. Lubber to go into more detail about the relationship of ESG performance to overall performance. He asked for an example of a social change, too.

Lubber gave the example of Nike, which suffered a "reputational catastrophe" that affected its bottom line when it was revealed that young children were sewing their soccer balls. Nike put standards in place to prevent this. Pepsi has implemented a "performance with purpose" program that sets ESG goals for its supply chain, which has improved its supply chain management overall. They're studying these issues and disclosing them, and it forces them to manage them better.

Scott said that Nike had recently had a situation come up with its Betsy Ross flag sneakers, and asked Ms. Lubber to comment on this. Lubber said that reputational risk to companies can influence shareholder value, as recently happened to Apple when it learned that chemicals were harming its workers. Nike's made thoughtful ESG decisions that have carried some risks but have ultimately paid off in higher revenues as they've taken actions consistent with consumer values.

REP. ALEX MOONEY (R-WV) asked Mr. Atkins about one bill's requirement that companies disclose tax payments country by country; are SEC employees international tax experts? If not, is it appropriate for Congress to pass a bill like this? Atkins said this was problematic, and most of these disclosures are probably immaterial.

Mooney said these bills are pushing the SEC beyond its mandate. He yielded to **REP. HUIZENGA**, who introduced five articles for the record about how ESG investments have weakened CalPERS' portfolio. Huizenga said he thought it was stupid of Nike to pull the Betsy Ross shoes, but this was their decision, and these decisions should be left to private companies rather than to the SEC or "some private side-car organization."

REP. KATIE PORTER (D-CA) asked Mr. Atkins about his service as an SEC Commissioner from 2002 to 2008, which she described as "a set-up for the global economy blowing up." Part of his job was to regulate the biggest broker-dealers, she said, and while he was there the SEC created the Consolidated Supervised Entity Program. That program included five investment banks, some of which are no longer in existence; the point of the program was for the SEC to make sure these banks didn't collapse. Porter asked how these banks felt about the CSEP and its capital standard.

"I don't recall, offhand," Atkins said.

Porter said they were actually very happy. She asked whether SEC had assessed the stability of these banks before they entered the program. Atkins said the staff had assured him they were stable and had the wherewithal to administer the program. Porter said that Harvey Goldschmidt had expressed concerns about it. Atkins said he'd asked staff about it because he too wanted to make sure they had the resources necessary to withstand a crisis.

Porter said the collapse had happened on his watch, and that Atkins had then inveighed against labor unions, civil rights groups, and gay rights groups engaged in shareholder activism, and called companies that made changes in response to this activism "weenies." She asked how he was in the position to make that criticism.

Atkins said this was an unfair comparison. Porter asked whether he'd want this committee to assert more oversight over the SEC, "because I'd probably be there for that." Atkins said that many financial institutions were more beleaguered than the ones in the CSEP.

Porter asked Atkins what his current job is. Atkins said that he's a consultant. Porter asked what he charges. Atkins said it depended on the project. Porter said she was struggling to understand why anyone would pay him, when he didn't stand up in the financial crisis but is now labeling other companies "weenies."

REP. HUIZENGA said this was inappropriate. **REP. VARGAS**, in the chair, asked whether Rep. Porter was quoting Mr. Atkins directly. Rep. Huizenga said she'd called him a weenie. Rep. Vargas said the witness was not a member of a protected class, and Rep. Porter's time had expired. "I feel very confident that I have made my point," Rep. Porter said.

Someone (couldn't identify) insisted on a point of order that decorum be preserved. Rep. Vargas consulted with counsel, and said that the point of order was not sustained.

REP. SEAN DUFFY (R-WI) asked Mr. Mohin how much he makes. Mohin said he didn't think that was material. Duffy said the hearing was all about disclosure, and Rep. Porter had found it appropriate to ask Mr. Atkins. Mohin said it was publicly available in GRI's annual report. Duffy pressed him. Mohin said that last year it was $250,000.

Duffy asked Mr. Andrus, who said he made $300,000. Mr. Wright said he chose not to answer that because he was a business owner.

Duffy asked Mohin whether it should be disclosed when a bank served a particular type of client. Mohin said his organization were standard-setters, and whether to use them was up to companies and regulators. Duffy broke out — this was a question about whether banks should have to disclose whether they serve gun businesses, or abortion clinics, or THC, or detention centers . . . Mohin said this was quite an interesting question, because GRI's independent board chooses which standards should go through their process, and none of these issues has made it that far. They haven't risen to the level of sustainability issues.

Duffy asked what they do want disclosed, on the social side. Mohin said that GRI has 33 topic-specific standards, including human rights, ethics, environment, health and safety. Duffy asked who sets the environmental standards. Mohin said it was independent experts. Duffy asked how funds the GRI. Mohin said it was 70% self-funded, 30% grants, mostly from governments that cite the standards in statutes.

Duffy said they should focus less on ESG standards and more on returns. He foresees CalPERS coming to Congress for a bailout because their commitment to ESG has bankrupted them. He said disclosures are an effort to exert political pressure instead of passing a law. Atkins agreed with this. Duffy scoffed at global warming predictions, saying they'd never come to pass.

REP. STEVE STIVERS (R-OH) asked Mr. Andrus whether he'd read the WSJ's disparaging article about CalPERS. Andrus said he hadn't. Stivers asked Andrus who he works for, who his fiduciary duty is to, and what he considers his goal. Andrus said he works for the benefit of CalPERS' pensioners and the workers of the state of California. Stivers asked what happened in the recent Chairman's race. Andrus said Mr. Perez had won the race for a board election. Stivers asked why the last chair had lost her seat. Andrus said he didn't know.

Stivers said it was angry pensioners who didn't think the fund was focused enough on returns. He asked what CalPERS' return had been — 7%? Andrus said that was their discount rate; for the last ten years, their return has been higher. Stivers noted that they'd recently had to change their amortization on investment losses from 30 years to 20 years, which required increased contributions from members. Andrus said this was correct. Stivers said that in this case, he'd be a lot more focused on increasing the rate of return.

Stivers asked Mr. Atkins who decides materiality for a company; the company, Atkins said. Stivers asked who was in the best position to decide materiality for a company. The company, Atkins said. Stivers had Atkins agree that the most important social justice purpose for a pension fund was to protect pension funds. He had Atkins repeat that reducing the number of IPOs is harmful to Main Street investors. Since some companies do voluntarily disclose this information, he said, people who care about ESG issues can just invest in them.

REP. HILL asked Mr. Atkins why a bill should be necessary to require additional tax disclosures, since corporations already report this information in 10-Ks. Atkins repeated that this was "problematic." Companies already need to report material information about tax liability and litigation. Hill said that many large corporations already disclose revenue and tax information by country or region; do we need more segmented analysis? Atkins said no.

Looking at the bill that would require companies to disclose political contributions or lobbying expenditures over $10,000, Hill said this had been the subject of many proxy proposals that have failed. What's the issue, he asked; don't investors already have the opportunity to ask for this via proxy? Atkins said these proposals do usually fail, though they've passed in a couple of companies. Hill said companies have an obligation to disclose material risks, with civil and criminal penalties associated for not reporting, but the beauty of the system is that each company gets to determine materiality for itself.

REP. VARGAS, in the chair, submitted statements for the record from the Carbon Disclosure Project, Public Citizen, the Council for Institutional Investors, the Fact Coalition, Principles for Institutional Investment, Morningstar, Professors Cynthia Williams and Jill Fish, TIAA, and the International Accountability Roundtable. He thanked the witnesses for their testimony. Members have five legislative days to submit additional questions, statements, and extraneous materials for the record.