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Prepared for the U.S. House of Representatives, Committee on Financial Services, Subcommittee on Investor Protection, Entrepreneurship and Capital Markets

"Building a Sustainable and Competitive Economy: An Examination of Proposals to Improve Environmental, Social and Governance Disclosures"

Comments on the Climate Risk Disclosure Act of 2019

July 10, 2019

Chair Maloney, Ranking Member Huizenga, and members of the Subcommittee:

Thank you for the invitation and opportunity to appear before you today. I am the CEO and President of Ceres, a nonprofit organization working with many of the most influential investors and companies to build sustainability leadership within their own enterprises and to drive sector and policy solutions throughout the economy. Through our membership networks of more than 100 plus companies and 160 investors, we work with these private sector leaders to tackle the world's biggest sustainability challenges, including climate change, water scarcity and pollution, and deforestation. We believe today's hearing is timely and necessary and we appreciate your attention to these challenges. Congressional action is crucial to ensure capital markets are transparent and fair and protect investors from material risks, such as those from climate change, whether those risks arise in short, medium or long term timeframes. We thank this subcommittee for focusing on the importance of corporate environmental, social and governance (ESG) disclosures. My remarks will primarily be confined to a discussion of the **Climate Risk Disclosure Act of 2019**, although I will touch generally on the critical importance of other types of ESG disclosure requirements.

Ceres' investor network includes more than 160 North American investors representing $26 trillion in assets under management.[1] This network advances leading sustainable investment practices, corporate engagement strategies, and key policy and regulatory solutions. These financial leaders are working under the assumption that climate change creates a material financial risk to their portfolios and these risks are worthy of further examination as it relates to their investments.

Many of these investors are also engaging the world's largest corporate greenhouse gas emitters on climate change through the global initiative Climate Action 100+, of which we are a founding partner organization. This collaboration includes investors from around the world with more than $33 trillion in assets under management who are engaging companies on improving their governance practices, curbing emissions, and strengthening climate-related financial disclosures.

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[1] https://www.ceres.org/networks/ceres-investor-network

We appreciate the opportunity to share our views on the critical need for mandatory corporate disclosure of the financial risks posed by climate change to better protect the investing public and position companies to thrive in a just and sustainable zero-carbon global economy.

Ceres' work on corporate sustainability and climate risk disclosure

Ceres was founded 30 years ago by a group of investors and environmentalists who had a vision of a better way to do business. They began to evaluate the role and responsibilities of companies and investors to comprehensively integrate sustainability — the real cost of pollution, the financial implications of resource depletion, the impacts of climate change, and water scarcity and pollution — into their financial analysis as key financial and corporate issues. It was clear — even 30 years ago — that the costs of environmental degradation to our economy was a monumental and global cost with implications for every sector of our economy, every company and their employees operating within it, and to our communities

This coalition of investors, public pension fund trustees, labor unions, religious investors and environmentalists crafted a groundbreaking code of conduct for companies called the Ceres Principles — a set of guidelines calling for integrating sustainability into practices, into reporting and into setting goals for continuous improvement.

Ceres went on to co-found the Global Reporting Initiative (GRI), setting the standard for corporate sustainability reporting, now a mainstream practice used by nearly 13,400 companies worldwide. I am very happy to testify today alongside my friend and colleague Tim Mohin, who leads the GRI, the leading global sustainability standard.

Within a decade, environmental and social issues were beginning to be considered and reported on as corporate financial imperatives, not merely externalities. New frameworks for reporting highlighted the risks and opportunities — providing the tools to not only measure corporate performance on environmental, social and governance (ESG) issues, but also to act on them.

Today, Ceres works with hundreds of the largest companies worldwide to improve reporting, including with Ceres Company Network members, a group of 50+ US based companies, nearly 75 percent of them Fortune 500 firms, which we influence through direct stakeholder engagement, standard-setting and regular benchmarking. Through our global collaboration — We Mean Business — we work with hundreds of global companies to address climate issues through better reporting (both sustainability reporting as well as full integration into financial filings), setting science-based emissions reduction targets and addressing public policy initiatives.

Since the founding of our investor network in 2003, the interest of some of the worlds' largest investors has continued to grow given the clear and substantial financial risks to their portfolios and their need to receive adequate information to make investment decisions. Ceres has worked with investors to make the case to the U.S. Securities and Exchange Commission (SEC or Commission) to prioritize improving the disclosure of material climate-related and other sustainability risk in financial filings. Ceres and our members have met frequently with SEC leadership and staff, drafted petitions to the SEC asking for interpretive guidance on climate risk disclosure, and evaluated the SEC's and corporations' approaches to climate disclosure.[2] Our work led the SEC to issue *Commission Guidance Regarding Disclosure Related to Climate Change* on January 27, 2010, the first guidance issued by a securities regulator explaining how existing disclosure rules apply to the physical, business, and legal developments related to climate change.[3]

In July 2016, Ceres organized a letter,[4] signed by 45 investors representing $1.1 trillion in assets under management, noting that in regard to climate change, "existing SEC rules have not, as applied by the Commission to date, produced sufficient information for investors to evaluate material risks, which we believe are becoming increasingly significant to companies in multiple sectors." The letter also noted that staff at the SEC have issued very few comment letters about the inadequacy of current climate risk disclosures, and have not "pursued enforcement actions for failure to meet disclosure requirements, despite a very active financial risk and disclosure enforcement agenda in other areas."

Regarding the need for SEC rules to improve climate risk disclosure, the letter continues:

> In a number of cases, additional guidance or line-item disclosure requirements are needed to elicit consistent, comparable, decision-useful narrative and metrics-based sustainability information that is useful to investors. For example, the business plans of many oil and gas, electric power, and coal companies appear to pose material financial risks to investors, because they are based on forecasts for increasing demand that fail to take into account the accelerating transition to a low carbon global economy. Even as enforcement actions may be warranted to address materially inadequate disclosures by these companies under the existing rules, new disclosure rules regarding the alignment of business plans with the greenhouse gas reduction targets of the Paris agreement may be necessary.

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[2] https://www.ceres.org/resources/tools/sec-sustainability-disclosure-search-tool; https://www.ceres.org/resources/reports/cool-response-sec-corporate-climate-change-reporting; https://archive.ceres.org/resources/reports/sustainable-extraction-an-analysis-of-sec-disclosure-by-major-oil-gas-companies-on-climate-risk-and-deepwater-drilling-risk/view.
[3] https://www.federalregister.gov/documents/2010/02/08/2010-2602/commission-guidance-regarding-disclosure-related-to-climate-change. See also https://www.sec.gov/news/press/2010/2010-15.htm and https://www.nytimes.com/2010/01/31/opinion/31sun3.html.
[4] https://www.ceres.org/news-center/press-releases/unprecedented-response-investors-call-sec-improve-reporting-climate

Widespread support for improving climate and sustainability risk disclosure

Data from recent reports from the Intergovernmental Panel on Climate Change (IPCC) and the U.S. government (National Climate Assessment) have demonstrated the urgent need for improved corporate disclosure and performance in response to climate change. The U.S. Fourth National Climate Assessment found, in the worst case scenario, that the economy could lose as much as 10-14 percent of its GDP by the end of the century.[5] In terms of sectoral impacts, the report found, "With continued growth in emissions at historic rates, annual losses in some economic sectors are projected to reach hundreds of billions of dollars by the end of the century—more than the current gross domestic product (GDP) of many U.S. states."[6]

The IPCC's Special Report from September 2018 found that global warming of 1.5 ºC is projected to inflict up to $54 trillion in damage to the global economy by 2100, while warming of 2 ºC is projected to inflict up to $69 trillion in damages in the same time period. Just last week, Moody's Analytics reconfirmed those finds in a new report, stating that such warming will "universally hurt worker health and productivity" and that more frequent extreme weather events "will increasingly disrupt and damage critical infrastructure and property."[7]

Initiatives led by companies and institutional investors worldwide have recognized these reports and in response have elevated the urgency of climate action and disclosure.

Some of the largest financial firms, corporations and investors worldwide have worked together for the last four years, as members of the Financial Stability Board's (FSB) Task Force on Climate-related Financial Disclosures (TCFD), to create globally applicable guidelines for climate-related financial disclosures.[8] The TCFD was created because G20 nations asked the Financial Stability Board to study how to improve climate risk disclosure in financial filings worldwide. The TCFD has been an important factor in elevating this issue on the agendas of companies and governments in the last four years.

For several years, investors have released global statements to world government leaders urging them to accelerate climate action and improve corporate climate risk disclosure. In June 2019, 477 investors with $34 trillion (USD) in assets, a record number of signatories, urged world government leaders to step up ambition on climate change and enact strong policies by

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[5] U.S. Global Change Research Program, *Fourth National Climate Assessment Volume II: Impacts, Risks and Adaptation in the United States* at 1360 (Figure 29.3), showing projections of direct damage to the current U.S. economy for six impact sectors as a function of global average temperature change.
[6] *Fourth National Climate Assessment Volume II: Impacts, Risks and Adaptation in the United States — Report in Brief at 13.*
[7] https://www.washingtonpost.com/climate-environment/moodys-analytics-says-climate-change-could-cost-69-trillion-by-2100/2019/07/02/f9fb94ac-99cb-11e9-916d-9c61607d8190_story.html?utm_term=.c58fab6519e0
[8] https://www.fsb-tcfd.org/publications/

2020 to achieve the goals of the Paris Agreement, including phasing out thermal coal power and pricing carbon.[9]

This statement is notable for its emphasis on improving corporate climate risk disclosure in financial filings, including asking governments to commit to implementing the TCFD recommendations in their jurisdictions and other items. Regarding climate risk disclosure, investors called on governments to do the following:

- Commit to improve climate-related financial reporting.
- Publicly support the TCFD recommendations and the extension of its term.
- Commit to implement the TCFD recommendations in their jurisdictions, no later than 2020.
- Request the FSB incorporate the TCFD recommendations into its guidelines.
- Request international standard-setting bodies incorporate the TCFD recommendations into their standards.[10]

And some of the largest asset management firms in the world have thrown their weight behind improving corporate climate risk disclosure and performance. In 2017, State Street Global Advisors (SSGA) stated, "Over the course of four years, SSGA has held over 240 climate-related engagements with 168 companies. Through these engagements we found that few companies can effectively demonstrate to investors how they integrate climate risk into long-term strategy. This is particularly important for companies in the oil and gas, utilities and mining sectors where long investment horizons could render assets stranded."[11] SSGA also called on high-impact sector companies to provide disclosures on board oversight of climate risks, long-term greenhouse gas (GHG) emissions goals, carbon price assumptions, and the impacts of scenario planning on long-term capital allocation decisions.[12]

BlackRock has named climate risk disclosure as one of its top corporate engagement priorities for several years. The company's approach to engagement on climate risk notes:

> For companies most directly impacted by climate change, we expect the whole board to have demonstrable fluency in how climate risk affects the business. The company should explain the board's oversight of its executives' approach to managing and mitigating the risk. Over the next few years, we expect that companies will enhance their disclosures related to climate risk, as awareness and understanding of the potential impacts of climate change and the TCFD's recommendations spreads.[13]

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[9] Global Investor Statement to Governments on Climate Change, *available at* https://www.ceres.org/news-center/press-releases/477-investors-usd-34-trillion-assets-urge-g20-leaders-keep-global
[10] Id.
[11] https://www.ssga.com/investment-topics/environmental-social-governance/2017/perspectives-on-effective-climate-change-disclosure.pdf
[12] Id.
[13] https://www.blackrock.com/corporate/literature/publication/blk-commentary-engaging-on-climate-risk.pdf

In addition, Larry Fink of BlackRock has written about the close ties between sustainability and financial performance:

> Profits are in no way inconsistent with purpose – in fact, profits and purpose are inextricably linked. Profits are essential if a company is to effectively serve all of its stakeholders over time – not only shareholders, but also employees, customers, and communities. Similarly, when a company truly understands and expresses its purpose, it functions with the focus and strategic discipline that drive long-term profitability. Purpose unifies management, employees, and communities. It drives ethical behavior and creates an essential check on actions that go against the best interests of stakeholders. Purpose guides culture, provides a framework for consistent decision-making, and, ultimately, helps sustain long-term financial returns for the shareholders of your company.[14]

Companies' climate risk disclosure and performance

Public disclosure of sustainability and climate risk information is not just about the act of reporting. The value of this disclosure is two-fold. First, if the data provided is robust and comparable, it can meet the needs of investors and other stakeholders for information about sustainability risks and opportunities facing companies, and the sustainability risks those companies impose on society.

Second, disclosure is valuable for its ability to stimulate ingenuity and strategic thinking by businesses, which can improve sustainability performance, increase a company's competitiveness in a resource-constrained economy and create shareholder value. Ceres' research has found examples of companies that provide good discussions of climate risks in financial filings and also undergo in-depth analysis of the strategic risks and opportunities from climate.

For example, American International Group (AIG) presents climate as a business risk and an opportunity. AIG's 2017 annual financial filing notes that climate change-related catastrophic events pose a threat to property and could create lost assets, increase claim costs, and interrupt operations.[15] AIG recognizes that legal, regulatory and social responses to climate change may affect the company's business, such as the potential for new regulations that contradict the company's current assumptions. AIG also frames climate change as an opportunity; the company says its underwriting, product development, modeling and

[14] https://www.blackrock.com/americas-offshore/2019-larry-fink-ceo-letter
[15] American International Group, Inc., Annual Report on Form 10-K for The Year Ended December 31, 2016 (Feb. 23, 2017). http://www.aig.com/investor-relations/sec-filings

sustainability practices can adapt to climate-related risks and provide customers with innovative products and services that anticipate these risks.[16]

PepsiCo links environmental performance to risks for its business operations, finances and brand reputation. In its 2017 annual financial filing, the company identifies the potential adverse effects of water scarcity on its supply chain and business operations.[17] Higher production costs and investments in water-efficient technologies could encumber the company's business and financial performance. At the same time, PepsiCo says failing to maintain high ethical, social, and environmental practices, such as a failure (or a perception of a failure) to act responsibly with respect to water use, human rights in the supply chain or public health concerns, could affect PepsiCo's reputation and brand image. Water scarcity therefore poses a double risk: not only can lack of water negatively affect the company's business operations and finances, a failure to be water efficient may adversely affect consumer perceptions of its brands.[18]

Ceres' research has found that companies that disclose climate-related financial risks in annual financial disclosures—such as Baxter International Inc., Molson Coors Brewing Company, and Procter & Gamble—are nearly twice as likely to have time-bound commitments to reduce GHG emissions than companies that do not.[19]

On the other hand, we have seen too many examples of companies that were insufficiently prepared for climate risks face challenges within recent years. This includes electric power companies that had to temporarily shut down generating facilities because the water used for cooling was too warm to work properly, automakers and chipmakers that suffered losses due to floods in Thailand affecting their manufacturing plants, and oil and gas companies which suffered damage to oil refineries due to storm surge or hurricanes. For example, one study found that Toyota suffered $1.25 billion and Honda $1.4 billion in lost operating profits due to the Thailand floods.[20]

The most recent example is the power company PG&E, which some have called the first climate change related bankruptcy. Extensive damage from 2017 and 2018 wildfires "was due in large part to extremely hot, dry conditions that spawned more frequent and intense fires."[21] The

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[16] AIG case study excerpted from Ceres, Turning Point: Corporate Progress on The Ceres Roadmap for Sustainability at 59, available at http://www.ceres.org/turningpoint.
[17] PepsiCo Inc., Form10-K for the Year Ended December 31, 2016 (Feb. 15, 2017). http://www.pepsico.com/Investors/SEC-Filings
[18] PepsiCo case study excerpted from Ceres, Turning Point: Corporate Progress on The Ceres Roadmap for Sustainability at 59.
[19] Ceres, *Turning Point: Corporate Progress on The Ceres Roadmap for Sustainability* at 50.
[20] Masahiko Haraguchi, Upmanu Lall, *Flood risks and impacts: A case study of Thailand's floods in 2011 and research questions for supply chain decision making*, International Journal of Disaster Risk Reduction (2014) at 7 (Table 6), citing Toyota and Honda press releases.
[21] https://www.forbes.com/sites/chunkamui/2019/01/24/pge-is-just-the-first-of-many-climate-change-bankruptcies/#657981497e5f

bankruptcy has not only caused billions in losses for shareholders, but also losses to insurers, customers and creditors, and losses to taxpayers due to disaster relief costs.[22]

The energy sector and climate risk disclosure

For decades, investors have been engaging with fossil fuel companies around the risks and opportunities associated with climate change. These investor-led initiatives have ranged from efforts to increase company investment in renewable energy to improving operational efficiency to addressing methane emissions and beyond.

However, for much of that time, companies largely dismissed investor concerns about the potential for dramatic shifts in business as usual market dynamics resulting from global action to address climate change. Fossil fuel companies expressed skepticism about the need to factor in the possibility of a broad, global set of initiatives that would lead to meaningful policy intervention on climate change.

Nearly without exception, the world's leading oil and gas companies have based long-term business planning on a business as usual, rising fossil fuel demand, outlook. Given that the industry regularly invests in projects with multi-decadal time horizons, the decisions companies make today will help determine their financial viability far into the future. Widespread assumptions that the future will resemble the past created a false sense of certainty and optimism regarding technology and climate risk, leading, in many cases, to inefficient deployment of capital.

Key among the steps that investors have called for is an assessment of the impacts on a company's portfolio and business strategy of policies and restrictions consistent with achieving the globally agreed upon target to limit global average temperature rise to well below two degrees Celsius above pre-industrial levels. This request achieved new urgency when the 21st Conference of the Parties to the United Nations Framework Convention on Climate Change achieved unanimous agreement and outlined a clear path to achieve this target in Paris in December 2015.

The Paris Agreement goal of keeping global temperature rise well below two degrees Celsius, and aspiring to a 1.5 degree goal, is already shaping the national policy decisions of major economies—and the world is actively working to shift away from fossil fuels to less carbon-intensive fuel sources.

Many corporations around the world, including some of the largest international oil and gas companies, have not fully incorporated the adoption of a binding two degrees or less Celsius climate accord into their business planning. In some cases, executives from those companies

[22] Id.

have expressed a view that a two degrees Celsius cap on climate warming will not prove achievable. Yet for the past two decades or more, energy companies have operated under a set of assumptions about the future business environment that are looking increasingly unrealistic.

Irrespective of whether governments actually achieve a two degrees Celsius cap (or 1.5 degrees, which is now the scientific goal) on global temperature increases, it cannot be ignored that many governments are making major commitments to the low-carbon transition by tightening regulations and performance standards designed to reduce the use of oil and coal. But perhaps just as significant from the point of view of a global transition in energy usage, societal patterns for fuel use are also changing through the advent of digital technologies that provide energy savings or alter choices among different fuels. Given the long capital horizons in the oil industry, where investments made today may not pay off for decades, it is imperative that the industry be particularly attuned to the potential for disruptive change. In considering how the business landscape for the energy sector may change given these trends in the coming decades, companies need to consider multiple variables at once.

That is why investors have urged companies to conduct low-carbon scenario analysis, which allows a company to design a strategy that is resilient to multiple possible outcomes.[23] Shell and Equinor have used scenario analysis to redesign their long-term strategies—including dramatic increases in their clean energy investments. Such an approach has been endorsed by the TCFD, and by large asset managers like State Street and Blackrock, as discussed above. Even the Pope, at a recent Vatican convening of oil sector executives, endorsed TCFD-focused scenario analysis as a key tool to help companies prepare for a low-carbon future.[24]
In the transportation sector, investor demand for low-carbon scenario analysis is also rising. Transportation is the largest and fastest growing source of U.S. GHG emissions, yet U.S. companies in the sector, including truck and auto manufacturers, have been slow to conduct and disclose information about low carbon scenario analyses. Given tightening global regulations and disruption in the transportation sector from new technologies (including electrification and automation), as well as from new business models for mobility, disclosure of climate scenario analyses, along with other risks, are critical in order to enable companies and investors to assess a variety of outcomes and future climate risk.

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[23] See Ceres reports providing guidance to companies on undertaking and disclosing scenario analyses, covering electric power (https://www.ceres.org/news-center/press-releases/new-ceres-framework-enables-us-electric-power-industry-assess-climate) and oil and gas (https://www.ceres.org/resources/reports/framework-2-degrees-scenario-analysis-guide-oil-and-gas-companies-and-investors).
[24] See *The Energy Transition & Care For Our Common Home: Participant Statement on Climate Risk Disclosures*, available at https://news.nd.edu/assets/323601/2019_vatican_disclosures_statement_final.pdf; Notre Dame president co-signs climate change accords with energy and investor executives at Vatican summit, June 14, 2019, available at https://news.nd.edu/news/vatican-and-notre-dame-co-sign-climate-change-accords-with-energy-and-finance-executives/.

Over the past year, many of the largest electric power companies and biggest greenhouse gas (GHG) emitters in the power sector have undertaken climate scenario analysis, released more robust climate risk reports and made deeper commitments to medium- and long-range greenhouse gas emission reductions. These actions have come at a crucial time, with the release last fall of the Special Report on Global Warming of 1.5 °C[25] by the Intergovernmental Panel on Climate Change (IPCC) highlighting the critical needs for the power sector to achieve net zero emissions before 2050 and to supply clean energy to support a broader range of uses in order to avoid the worst impacts of climate change.

U.S. power companies that have issued reports based on climate scenario analyses include AES Corporation, PPL Corporation, Duke Energy, Southern Company, Dominion Energy, and CMS Energy. Out of these disclosures, one of the strongest is from the Virginia-headquartered AES Corporation. The company's climate scenario report[26] is well aligned with the recommendations of the TCFD and utilizes three climate scenarios, including a "well-below 2-Degree Celsius" scenario. AES details its new focus on four primary "Clean Energy Growth Platforms" – illuminating pathways of opportunity aligned with clean energy transition in the areas of energy efficiency, renewables and energy storage.

By way of another example, late last year Minneapolis-headquartered Xcel Energy disclosed its long-range GHG reduction plans, announcing a bold new commitment to provide 100 percent carbon-free electricity to its customers by 2050 and achieve an 80 percent reduction by 2030. In March 2019, Xcel also released its report "Building a Carbon-free Future"[27] based on analysis tied to the Paris Agreement targets of well-below 2°C and 1.5°C, and the company subsequently has announced more detailed clean energy transition plans tied to specific generating assets.

It is encouraging to see these leading examples, yet there is a broad range of companies in the electric power sector and beyond that have yet to undertake and/or disclose an assessment of their exposure to climate risk – a troubling gap that legislation like this could help bridge.

The SEC's approach to climate risk disclosure

In 2007, Ceres worked with a group of investors, including one of the largest U.S. pension funds, the California Public Employees' Retirement System (CalPERS), to file a petition[28] with the SEC for interpretive guidance on disclosing the material financial risks posed by climate change. I testified before the Senate Banking Committee in 2007 about the importance of the

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[25] https://www.ipcc.ch/sr15/

[26] https://s2.q4cdn.com/825052743/files/doc_downloads/2018/11/AES_Climate_Scenario_Report111318.pdf

[27] https://www.xcelenergy.com/company/corporate_responsibility_report/library_of_report_briefs/a_carbon_free_future

[28] https://www.sec.gov/rules/petitions/2007/petn4-547.pdf

SEC acting on that petition, speaking on behalf of 22 petitioners, include leading institutional investors in the U.S. and Europe managing more than $1.5 trillion in assets, that we mobilized in support of that guidance.[29] And in 2010, the SEC issued first-of-its-kind disclosure guidance on climate risks under Chair Mary Schapiro's leadership.[30]

Since then, as discussed above, climate risk has become a mainstream concept among the global investment community. The guidance has been an important factor in changing how our capital markets approach climate risk. It does a great job of showing how climate change poses significant risks in a range of industries, and it explains when companies are required to disclose physical risks, regulatory risks and opportunities, and other material issues in financial filings.

But the guidance has only had a meaningful impact when SEC leadership and staff made an effort to ensure issuers used it. The guidance initially led to a jump in the percentage of S&P 500 companies that reported climate risks in SEC filings, from 45 percent in 2009 to 56 percent in 2010. And in 2010 and 2011, SEC staff issued 49 comment letters to companies in cases where their disclosure was inadequate.[31]

Yet today, the SEC is doing very little to ensure companies disclose material climate risks and opportunities. A search for SEC comment letters asking issuers to improve their climate-related disclosure in Commission filings reveals only one such letter from January 2017 to the present, to the company FLEX LNG Ltd.[32]

Unfortunately, today the SEC climate disclosure guidance is not being implemented or enforced. In many ways it appears that the SEC is abdicating its responsibilities and, at the present time, its efforts are simply not resulting in meaningful improvement in the quality of climate risk disclosure in financial filings.

Climate Risk Disclosure Act of 2019

Ceres supports climate disclosure rules at the SEC because of the need for comparable, robust reporting that meets investors' needs and helps companies manage risks. Also, because of the urgency of the climate crisis, we cannot afford to continue hoping that SEC leadership will prioritize climate risk disclosure and fully implement the 2010 climate disclosure guidance.

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[29] https://www.banking.senate.gov/hearings/climate-disclosure-measuring-financial-risks-and-opportunities; https://archive.ceres.org/press/press-releases/major-investors-state-officials-environmental-groups-petition-sec-to-require-full-corporate-climate-risk-disclosure
[30] https://www.federalregister.gov/documents/2010/02/08/2010-2602/commission-guidance-regarding-disclosure-related-to-climate-change
[31] https://www.ceres.org/resources/reports/cool-response-sec-corporate-climate-change-reporting
[32] https://searchwww.sec.gov/EDGARFSClient/jsp/EDGAR_MainAccess.jsp?search_text=%22climate%20change%22&sort=Date&formType=FormUPLOAD&isAdv=true&stemming=true&numResults=10&numResults=10

Voluntary disclosure, such as sustainability reporting, is and will remain important for companies to communicate their impacts on people and the environment, and the risks and opportunities they face. But only rules can provide investors with the robust disclosure they need *from all companies* to make better investment decisions.

As discussed above, climate change—from rising sea levels and extreme storms to the rapid transition to new, low-carbon technologies—poses material financial risks to companies across all sectors of the economy. We have already seen companies in industries like electric power, oil and gas, coal and insurance suffer losses because of their slow reactions to the climate crisis, and we will see more losses unless companies rapidly improve their strategies, actions and disclosures related to climate.

The **"Climate Risk Disclosure Act of 2019"** will allow the market — through investors and others — to better assess risks posed by climate change and take advantage of opportunities, spurring both public and private sector action on the issue, while promoting financial stability across the U.S. economy.

The Act would require issuers to identify and disclose physical risks and transition risks related to climate change, with the latter defined expansively to include not only changing markets and new technologies, but regulatory risks related to Federal, State and local laws and international agreements. It would also require issuers to disclose an evaluation of potential financial impacts, risk management strategies, and any corporate governance processes and structures related to climate change. These requirements are carefully designed to meet the needs of investors without imposing undue burdens upon corporations. The requirements also build upon voluntary climate disclosure standards that have arisen in the last twenty-five years and that many companies already implement.[33]

The Act would require the SEC to issue final climate disclosure rules within one year, in conjunction with the EPA Administrator, the Secretary of Energy, the Administrator of NOAA, the Director of the Office of Management and Budget, and the head of any other Federal agency determined appropriate by the Commission ("climate principals"). Including consultation with agencies with extensive expertise in the risks and opportunities posed by climate change is very helpful and should result in reporting requirements that take account of rapidly evolving scientific findings about climate change.

The Act includes several other provisions that are closely aligned with the needs of investors and climate disclosure developments in recent years:

- It would require the SEC to establish climate disclosure metrics specialized for specific sectors, including finance, insurance, transportation, electric power and non-renewable

[33] See, for example, the CDSB Climate Change Reporting Framework, https://www.cdsb.net/what-we-do/reporting-frameworks/climate-change and the TCFD disclosure recommendations, https://www.fsb-tcfd.org/publications/final-recommendations-report/.

energy. Investors have been increasingly focused on helping to develop and encourage the use of industry-specific metrics, such as those developed by the Sustainability Accounting Standards Board,[34] which help them better evaluate how climate risk presents different types of risks to different industries.[35] In addition, the focus on these industries make sense, as they face the most significant risks and opportunities related to climate change.

- It would require disclosure of input parameters, assumptions and analytical choices regarding climate scenario analyses, and would require companies to consider a business as usual warming scenario ("baseline scenario"), a well below two degrees Celsius scenario, and any additional climate analysis scenario considered appropriate by the Commission, in consultation with the climate principals. These requirements are essential to a transparent scenario analysis, are well aligned with the expectations Ceres and investors we work with have laid out,[36] and are responsive to shortcomings in various scenario analyses that companies have disclosed in recent years.[37]

SEC inaction to improve climate disclosure is especially concerning given the progress that other regulators around the world are making. For example, the UK government just announced plans to establish a joint task force with its financial regulators to analyze the most effective way to approach climate disclosure, including exploring the possibility of mandatory reporting.[38] Even other U.S. financial regulators are considering these risks. Just a few weeks ago, members of the Commodity Future Trading Commission (CFTC) held a meeting focused on climate related financial risks.[39] Expert witnesses discussed the impact of climate change on the future stability of the global financial system, financial industry approaches to the mitigation of such risks, and challenges that lie ahead for regulators and participants in the derivatives industry. CFTC Commissioner Rostin Behnam plans to form a subcommittee focused exclusively on examining climate related financial market risk.[40] The SEC should be taking similar steps to consider the risks climate change poses to the financial system and to the various industries it oversees.

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[34] https://www.sasb.org/standards-overview/download-current-standards/
[35] The SASB Technical Bulletin on Climate Risk found "that climate change affects 72 out of 79 industries (93 percent of the capital markets, or $27.5 trillion) but manifests differently from one industry to the next" (https://library.sasb.org/climate-risk-technical-bulletin/).
[36] See the Global Investor Coalition on Climate Change's series of "Investor Expectations on Climate Change" Sector reports, available at https://globalinvestorcoalition.org/reports/. Individual reports cover steel companies, oil and gas, automotive, electric power and mining.
[37] See, for example, https://www.ceres.org/news-center/press-releases/new-exxon-report-step-forward-investor-disclosure-climate-change-falls
[38] See UK Government, *Green Finance Strategy: Transforming Finance for a Greener Future* (July 2019) at 15, available at https://www.gov.uk/government/publications/green-finance-strategy. The report also welcomed the actions being taken by UK regulators with respect to disclosure, such as the Financial Conduct Authority's October 2018 discussion paper which sought views on the value of introducing a requirement for financial services firms to report publicly on how they manage climate risks to their customers and operations (Id.).
[39] https://www.cftc.gov/PressRoom/Events/opaeventmrac051219
[40] https://www.cftc.gov/PressRoom/SpeechesTestimony/behnamstatement061219

Current corporate disclosure on climate risk in SEC filings is still minimal and does not enable investors to compare how companies are managing this risk. The market is currently lacking this vital information, and as a result, we could be dramatically undervaluing the financial impacts on the economy. I therefore urge Members of the Subcommittee to support the "Climate Risk Disclosure Act of 2019."

Related issues

I also appreciate that this hearing is considering regulations in regards to mandatory human rights due diligence and disclosure. Similar to what I've discussed in my comments on climate risk disclosure, voluntary corporate reporting on human rights is an inadequate tool for fully assessing the scope and severity of business's impacts on human rights. Current voluntary frameworks on human rights risk disclosure are piecemeal, poorly enforced, and do not meet the needs of investors. Disclosure in financial filings is generally inadequate:

> "Ceres and CookESG Research found that S&P 500 companies disclosed more information about workers' rights and workplace practices than about human rights, equal employment, and anti-discrimination policies. Foreign companies generally disclosed more information than their U.S. competitors. Overall, however, companies failed to detail the financial implications of human and workers' rights-related risks and opportunities."[41]

Mandatory human rights due diligence – coupled with effective enforcement – can be a critical tool to spur private sector action on systemic human rights issues, to which large multinational companies are direct contributors. With the legislation under consideration, the US would join a number of other countries already implementing some form of mandatory human rights due diligence regulations, including the UK, France, and Australia.

Climate and sustainability risk disclosure should not be considered in a vacuum — policy makers should also take into account whether the SEC continues to permit investors to raise these issues in shareholder proposals. For decades, shareholder proposals have been a critical tool investors rely upon to encourage companies to disclose and mitigate sustainability risks. Despite the rapid growth in ESG-themed investing[42] and the significant improvements in corporate governance that have resulted from proposals,[43] some in the corporate community have been pushing for SEC rule changes that would curtail investors' rights to include proposals

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[41] Ceres press release, *New SEC Search Tool Finds Inadequate Human and Workers' Rights Disclosure in Financial Filings* (May 31, 2018), available at https://www.ceres.org/news-center/press-releases/new-sec-search-tool-finds-inadequate-human-and-workers-rights-disclosure. See also https://www.ceres.org/news-center/blog/financial-filings-require-decision-useful-disclosure-human-rights.
[42] https://www.ussif.org/trends
[43] https://www.ussif.org/files/Public_Policy/Comment_Letters/Business%20Case%20for%2014a-8.pdf, p. 6

on companies' proxy ballots. I ask that you continue to exercise your oversight authority to protect the shareholder proposal process.

As you are likely aware, the SEC recently announced plans for rulemaking[44] focused on changes to Rule 14a-8, possibly including raising the thresholds for filing and/or re-filing shareholder proposals. We thank Chairwoman Waters for her attention to this issue, as evidenced by her amendments that were filed and adopted as part of the Financial Services and General Government House Appropriations bill. Ceres continues to believe that the current process offers both access for investors and protection for companies against resolutions that are not relevant, appropriate, or demonstrate sufficient interest from shareowners. We encourage additional steps be taken to preserve the existing SEC rules.

Nearly all shareholder proposals are advisory, meaning that corporations are under no legal obligation to act even if a majority vote in favor of a resolution. Numerous benefits associated with the form of 'shareholder democracy' enabled by the current process are detailed in two white papers by Ceres, ICCR, and USSIF.[45] The existing rules allow shareholders of all sizes to project their interests by aggregating their voices through voting. Through shareholder engagement and voting, investors act as a sort of immune system for capital markets, seeking out emerging risks and sending signals to companies to fix problems before they cause crises.

In addition, some corporate trade associations argue that shareholder proposals are costly, but when companies allow the proposals onto their proxy ballots without legal challenge, the costs are quite small. Costs include adding 1-2 pages to the proxy statement including the 500 word resolution and (typically) an opposition statement by the company. Time spent by corporate boards on things like the opposition statement can be viewed as a benefit to companies since proposals are required to address significant, unaddressed policy issues for the company. Overall, the benefits to companies and society of shareholder proposals are significant and outweigh the costs, which are negligible.[46]

As for climate risk disclosure, there is strong mainstream recognition of the value of shareholder proposals. A Goldman Sachs equity research report, "Shareholder engagement in the age of transparency," states, "We believe shareholder resolutions can offer additional insight into emerging material risks and externalities for issues, as well as management responsiveness." The report also notes that support for environmental and social shareholder proposals has been rising for several years, with nearly 30% of the votes, on average, placed in favor of shareholder proposals.

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[44] https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201904&RIN=3235-AM49
[45] https://www.ussif.org/files/Public_Policy/Comment_Letters/Business%20Case%20for%2014a-8.pdf; https://www.iccr.org/sites/default/files/resources_attachments/investor_response_to_chamber_14a-8_nov_9_final_2.pdf
[46] https://corpgov.law.harvard.edu/2017/06/15/the-dangerous-promise-of-market-reform-no-shareholder-proposals/

Conclusion

This subcommittee's work to advance corporate ESG disclosure could not be happening at a better time. Ceres' research shows that nearly 400 of the 600 largest publicly traded companies in the U.S. have commitments to reduce GHG emissions, 300 actively manage water resources, and nearly 300 actively protect employees' human rights.[47] Companies have begun to incorporate sustainability risks and opportunities into their decision-making in ways we could not have dreamed of thirty years ago. The Climate Risk Disclosure Act of 2019 is an essential part of the next 30 years of progress.

Thank you.

[47] https://corpgov.law.harvard.edu/2019/06/15/get-us-there-the-ceres-strategic-plan/