

COMMENT LETTER

February 10, 2017

ICI Response to FSB Task Force Consultation on Climate-Related Disclosure (pdf)

February 10, 2017 Task Force on Climate-related Financial Disclosures c/o Financial Stability Board CH-4002 Basel, Switzerland Re: Task Force Consultation and Report on Climate-related Financial Disclosures Dear Task Force Members: The Investment Company Institute,¹ on behalf of our entire fund membership, appreciates the opportunity to comment on the Task Force on Climate-related Financial Disclosures' report and consultation regarding climate-related financial disclosure. We respectfully request that you consider this letter along with the response we submitted through the required online portal. As public companies issuing securities and as large investors in US and international financial markets, ICI members are keenly interested in policies that promote a well-functioning financial system able to withstand the periodic shocks that are an inevitable part of our complex, global marketplace. We seek to provide meaningful input on global financial initiatives, such as this one, that may have significant implications for investment funds that are comprehensively regulated and eligible for public sale,² for their investors, and for the broader financial markets. 1 The Investment Company Institute (ICI) is a leading global association of regulated funds, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US\$18.6 trillion in the United States, serving more than 95 million US shareholders, and US\$1.6 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC. 2 For ease of discussion, we use the term "funds" below to refer to: (i) regulated US funds (or US mutual funds), which are comprehensively regulated under the Investment Company Act of 1940; and (ii) stock and bond funds that are organized or formed outside the US and substantively regulated to make them eligible for sale to retail investors, such as funds domiciled in the EU and qualified under the UCITS Directive. 2 We have three significant concerns with the Task Force's report and recommendations: • They are premised on a link between climate-related disclosure and risk to global financial stability, for which the Task Force provides no supporting data or analyses; • They are unnecessary in light of existing disclosure requirements; and • They are not feasible for funds to implement. We explain each of these concerns below. First, the Task Force asserts that its recommendations are necessary to promote global financial stability. They are, it says, intended to address "the need for better information to support informed investment, lending, and insurance underwriting

decisions to improve understanding and analysis of climate-related risks and opportunities, and over time, to help promote a smooth rather than an abrupt transition to a lower-carbon economy.” According to the report, “this transition to a lower-carbon economy requires significant and, in some cases, disruptive changes across economic sectors and industries in the near term” that may cause “severe financial shocks and sudden losses in asset values.” The report, however, provides no data or any other basis for this conjecture.³ While particular investments can conceivably carry risks related to climate change, neither the Financial Stability Board (FSB) nor the Task Force provide any basis for concluding that any such investment risks pose a threat to global financial stability. Policymakers and regulators in many jurisdictions have acquired significant experience addressing financial stability risk in a number of areas in the wake of the global financial crisis. Areas of successful focus have included increasing the resiliency of depository institutions, implementing reforms to the regulation and oversight of credit rating agencies, implementing comprehensive over-the-counter derivatives markets reforms, and enhancing regulatory cooperation and information sharing between jurisdictions. Investment risks related to climate change clearly do not fit within this rubric. Moreover, any evaluation of the need for new climate-related disclosure should remain within the sole purview of the relevant, and appropriate, standard setters and national regulators—in the case of asset management, this responsibility should reside solely with the International Organization of Securities Commissions (IOSCO) and national securities regulators.⁴ The Task Force’s recommendations address matters that are squarely within the competence of capital markets regulators, and we believe IOSCO, if any organization, should evaluate the necessity of any new disclosure related to climate change. This approach properly directs these important responsibilities to

³ In writing this letter, we do not intend to express any particular view on global climate change. Rather, this letter reflects our views on the necessity and feasibility of the Task Force’s recommendations as they would apply to funds. We also question the notion that there is a link between the recommended disclosure and global financial stability.

⁴ We recognize that many of our members already incorporate environmental, social, and governance (ESG) criteria into their investment process. Many reports suggest that interest in ESG investing will continue to increase. See, e.g., “Trump Policies Unlikely to End Sustainable-Investing Trend,” Wall Street Journal (Feb. 6, 2017).

³ regulators expert on asset management and the capital markets. It also contemplates accounting for existing regulation in each jurisdiction. Second, the Task Force’s recommendations are unnecessary because many regulatory regimes already require public companies to disclose material information, including material information related to climate change. We see no reason to treat disclosure of climate-related information in a different manner. In fact, it would be inappropriate for the Task Force to dictate the nature and detail of any single risk factor. Rather, asset managers appropriately consider climate-related information, to the extent that it is material information, as simply one piece of a mix of information that they use to make investment decisions. A survey of energy company annual reports, for example, shows material risk disclosure that includes risk factors—in addition to material climate-related risk—such as regulatory and litigation risks, project management, security concerns, research and development, operational efficiency, and safety, business controls, and environmental risk management. Asset managers are experts at analyzing these different material risks and making investment decisions accordingly. In fact, investment markets are forward-looking and are designed to evaluate material risks that may affect the future value of investments. The Task Force’s supplemental guidance for asset managers likewise is unnecessary given its overlap with existing securities laws. In the US, the Investment Company Act of 1940 already ensures that the market and investors have access to appropriate material information about each fund, tailored to its investment strategy and risks as well as information on its current

activities. The precise legal standard is that funds must provide investors with a prospectus that discloses “the principal risks of investing in the Fund, including the risks to which the Fund’s portfolio as a whole is subject and the circumstances reasonably likely to affect adversely the Fund’s net asset value, yield, and total return.”⁵ In the EU, the European Securities and Markets Authority (ESMA) similarly requires funds to provide investors with a “narrative presentation of risks materially relevant to the fund.”⁶ Under existing standards, each fund must evaluate its particular disclosure obligations. To give the Task Force a sense of the types of climate-related disclosure funds are making, we reviewed a sample of prospectuses for energy sector funds. We found disclosure of investment risks including climate change, price fluctuations caused by real and perceived inflationary trends and political developments, demand for energy fuels, energy conservation, the success of exploration projects, tax and other governmental policies, weather or meteorological events, the cost assumed in complying with environmental safety regulations, alternative energy sources, increases in energy efficiencies, and global events such as instability in the Middle East. ⁵ See SEC Form N-1A, Item 4. ⁶ See ESMA, UCITS IV Directive, Key Investor Information Document (KIID). The KIID is the European analog to the summary prospectus that many US mutual funds use. ⁴ Third, asset managers simply are not able to disclose aggregated data about fund portfolio companies when the underlying data for individual companies is not available. In particular, the Task Force recommends that asset managers disclose normalized greenhouse gas (GHG) emissions associated with a fund’s portfolio companies. Given the lack of GHG data availability and consistency, any data aggregation would be incomplete at best, and potentially even misleading.⁷ * * * * * We appreciate the opportunity to participate in this consultation. If you have any questions regarding our comments or would like additional information, please contact me at (202) 326-5815 or david.blass@ici.org. Sincerely, /s/ David W. Blass David W. Blass General Counsel Investment Company Institute ⁷ The Task Force’s acknowledgement of the lack of this data does not assuage our concerns.