OFFICE OF THE ILLINOIS STATE TREASURER
MICHAEL W. FRERICHS

May 31, 2022

The Honorable Gary Gensler, Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: S7-10-22 The Enhancement and Standardization of Climate-Related Disclosures for Investors

Chair Gensler,

I am writing to voice my support for the SEC's proposed rule to enhance and standardize climate-related disclosures for public companies and foreign private issuers.

As the Treasurer of the State of Illinois, I am responsible for safeguarding and prudently investing approximately $50 billion on behalf of the State, units of local government, and retirement and college savers. To effectively execute my fiduciary duties as State Treasurer, and to ensure compliance with state law,[i] my office integrates financially material sustainability factors into our investment decisions, including climate-related factors where warranted.

As a complement to traditional financial analysis, the integration of sustainability factors provides an additional layer of decision-useful information by which we can better assess the risk and return prospects of individual companies, investment funds, and other investment vehicles. These activities are critical in our endeavor to provide the highest level of service, stewardship, and financial value to our beneficiaries and participants.

Companies, investors, and government officials alike are increasingly aware of the material risks posed by climate change to our economy, financial markets, and investment portfolios. In Illinois, the state legislature has taken the position that consideration of environmental factors (among other factors) is vital to maximizing the safety and performance of public funds.[ii] The science is clear: "the world faces unavoidable multiple climate hazards over the next two decades with global warming of 1.5° Celsius," and the window to avert catastrophic consequences is closing fast.[iii] While many businesses and economies are already facing the physical impacts of climate change with the onset of more frequent and severe weather events, the adverse effects of unchecked warming are projected to be far worse, causing irreversible disruptions and losses of resources, ecosystems, and infrastructure.[iv]

Given these growing risks, governments and businesses around the world are seeking to achieve a massive transformation to a world with net-zero greenhouse gas emissions. As governments and businesses aim to transition to a net-zero economy, investors face a great deal of uncertainty. Many industries are facing major shifts in regulation, supply and demand forces, asset values, and higher costs of doing business, which creates increased volatility and market disorder. At the same time, other areas of the economy are poised for growth and well-prepared to manage changing market conditions, which provides an opportunity for investors. These conditions create decision-making challenges and resource burdens for investors, and particularly for long-term investors with portfolios constructed to achieve diversification, preservation of capital, and sustainable returns.

What makes the present situation even more challenging and burdensome is the lack of consistent, comparable, and standardized disclosures on climate-related risks and opportunities. Many companies do not disclose decision-useful climate-related information, including:

- **Physical and Transition Risks** – Whether and to what extent the company is exposed to material physical and/or transition risks and what impacts these risks pose to the business strategy, financial planning, capital allocation, business model, and outlook.
- **Greenhouse Gas (GHG) Emissions** – The company's Scope 1, 2 and 3 greenhouse gas emissions, which should include standardized disclosure of Scope 3 emissions as this information is decision-useful, enabling investors to better assess and compare the vulnerabilities of a company's business model to transition risks.
- **Targets and Goals** – Whether the company has targets and/or goals to reduce GHG emissions.
- **Transition Plan** – Whether the company has a transition plan that describes how the company intends to address climate-related risks and opportunities, achieve stated GHG reduction targets or goals, and manage climate-related human capital and community impacts.
- **Governance and Risk Management Processes** – Whether and to what extent the company has governance and risk management processes in place for identifying, assessing, and managing climate-related risks, including how the company determines the materiality of climate-related risks, whether the board of directors includes any member with expertise in climate-related risks. or whether the company has designated a specific board director or committee responsible for climate risk oversight.

While in recent years, more companies have provided voluntary climate disclosures in the aforementioned areas – and those companies should be recognized – the current disclosure landscape is best-characterized as disorderly, inefficient, and unreliable. Right now, investors and their service providers must wade through a chaotic array of reports, voluntary disclosures, and third-party databases that are inconsistent, incomparable, and incomplete. This places a significant burden on investors seeking to methodically integrate material climate factors into fundamental investment processes, including company analysis, manager analysis and due diligence, portfolio risk assessment, asset allocation, and investment stewardship activities. In short, it makes it harder and more costly to perform our fiduciary duty and serve the people of Illinois.

The time has come for clear rules for climate-related disclosure. With this proposed rule, the SEC is responding to a widespread need among investors, companies, index providers, rating agencies, and financial markets for clear, consistent, and comparable reporting standards on climate risks and opportunities.

It is critically important that companies disclose the full range of decision-useful information, as the proposed rule prescribes (and as outlined in the bullet list above), which includes climate-related risks, GHG emissions, targets and goals, transition plans, and governance and risk management processes.

It is also important that companies file disclosures with the SEC and disclose climate-related matters in the financial statement footnotes, as the proposed rule prescribes, which will help ensure that investors have access to accurate, reliable, and highly scrutinized information.

As an institutional investor, the proposed rule is anticipated to yield numerous direct benefits for the Office of the Illinois State Treasurer, including but not limited to:

- **Direct Cost-Savings**

  The availability of standardized and accessible climate-related data could potentially save the Illinois Treasury tens of thousands of dollars every year – if not more – in money that would otherwise be spent on specialty databases and service providers.

  Under present conditions, institutional investors are often obliged to hire outside consultants or specialty providers to access comprehensive climate-related data and assess climate-related risks across their investment portfolio. These resource demands are likely to grow as the physical and transition risks of climate change increase. By creating clear and consistent reporting standards for climate-related information, the proposed rule will level the playing field, reduce information asymmetries, and provide broad access to comparable, reliable, and comprehensive quantitative and qualitative information. This will drive efficiencies in the market and save investors money on data collection and analysis, which is currently very resource-intensive and lacks standardization.

In addition, by phasing in assurance requirements over time and creating a specific location within financial statements where climate impacts are disclosed, the proposed rule will help ensure that investors have access to high-quality, highly scrutinized information that does not require (or requires a lesser degree of) additional assurance or verification costs borne by the investor.

- **Improved Investment Analysis and More Informed Investment Decisions**

  The availability of comparable, reliable, and comprehensive climate-related information will empower our investment analysts and officers to make more informed decisions.

  For example, personnel in our Division of Portfolio & Risk Analytics review individual security issuers, evaluating each by their financial condition, outlook, creditworthiness, and management of material sustainability factors, including climate factors where relevant. Equipped with comparable, reliable, and comprehensive data on a company's GHG emissions, for example, our team will be better positioned to assess a company's potential exposure to operating and capital costs for mitigating GHG emissions, as well as its exposure to a potential increase in regulatory risks and compliance costs. Our team will also be better equipped to assess whether a company may face added difficulties and costs in reducing GHG emissions compared to peers, which could result in significant adverse impacts in the form of asset write-downs, costs of obtaining carbon credits, or unanticipated increases in operating and capital expenditures. Under present conditions, such cost and comparative analyses are rife with issues, ranging from a lack of data to unreliability to reporting inconsistencies.

- **More Effective and More Efficient Investment Stewardship Practices**

  The availability of standardized climate-related information will enable the Illinois Treasury and its partners to better execute fundamental investment stewardship duties, including corporate engagement and proxy voting.

  Corporate engagement and proxy voting are vital functions to best-in-class investment management. These practices often result in improved governance and reporting practices at companies, which benefits investors from increased oversight and management of material risks, increased disclosure of decision-useful information, and increased expected performance.

  Regarding corporate engagement, our office actively communicates and works with portfolio companies both independently and through investor coalitions, such as Climate Action 100+, the Ceres Investor Network, and the Human Capital Management Coalition. This includes targeted engagements with companies on their disclosure and management of climate-related risks and opportunities, including companies identified as "systemically important carbon emitters" by Climate Action 100+.[v]

Given the absence of established climate disclosure standards, investors now spend considerable resources, both internally and via external providers, engaging companies to obtain baseline disclosure on climate-related risks, GHG emissions, targets and goals, transition plans, and governance processes. Not only is this work resource-intensive, given the scale of the challenge and the demands of initiating unique engagements, filing shareholder proposals, and conducting proxy solicitations, it is inefficient. The proposed rule will yield robust and comparable climate disclosures across public companies, thereby reducing the need for intensive disclosure-based engagements. At the same time, the availability of standardized climate disclosures will equip investors with more reliable and detailed information that they can use to better identify leaders and laggards and develop smarter engagement strategies.

Institutional investors and their service providers will also be better positioned to execute proxy voting duties when equipped with comprehensive and comparable climate data. Like others, the Illinois Treasury integrates climate-related information in proxy voting decisions, both related to shareholder proposals and the election of directors. For the latter, directors are not supported when the board has failed in its oversight responsibilities, including when there is an inadequate response to systemic risks, such as climate change, that may have a material impact on performance.[vi] Our office may vote against directors at companies that have failed to set GHG emissions reduction targets or failed to disclose material climate risk exposures and how the company governs, manages, and mitigates those risks. Under present conditions, it is challenging and resource-intensive to obtain consistent, comprehensive, and comparable data to execute such a policy and hold directors accountable for failures to address material climate risks. The proposed rule will better ensure that investors have clear, consistent, and comprehensive data by which they can make informed voting decisions that drive enhanced governance, risk management, and reporting practices.

Thank you for your diligent work on this critical topic, and should you have any questions, please do not hesitate to contact Max Dulberger, Director of Corporate Governance & Sustainable Investment, [redacted]

Sincerely,

Michael Frerichs

Michael W. Frerichs
Illinois State Treasurer

cc: Vanessa A. Countryman, Secretary

[i] Illinois Sustainable Investing Act (30 ILCS 238), available at: www.ilga.gov/legislation/ilcs/ilcs3.asp?ActID=4027&ChapterID=7
[ii] Ibid.
[iii] International Panel on Climate Change, Sixth Assessment Report: Impacts, Adaptation and Vulnerability, February 28, 2022, available at https://www.ipcc.ch/report/ar6/wg2/resources/press/press-release.
[iv] International Panel on Climate Change, Special Report: Global Warming of 1.5 Degrees Celsius, available at: https://www.ipcc.ch/sr15/chapter/spm/.
[v] Climate Action 100+, Companies, available at: https://www.climateaction100.org/whos-involved/companies/.
[vi] Office of the Illinois State Treasurer, 2022 Proxy Voting Policy Statement, available at: https://illinoistreasurergovprod.blob.core.usgovcloudapi.net/twocms/media/doc/sto%20-%202022%20proxy%20voting%20policy%20statement.pdf.

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