July 11, 2023

The Honorable Patrick McHenry
Chairman
House Financial Services Committee
2134 Rayburn House Office Building
Washington, DC 20515

The Honorable Maxine Waters
Ranking Member
House Financial Services Committee
2221 Rayburn House Office Building
Washington, DC 20515

Dear Chairman McHenry, Ranking Member Waters, and Members of the Committee,

On behalf of Green America, I write in support of the Committee's important role in ensuring the efficiency, effectiveness, and accountability of the federal government and all its agencies.

Green America is the nation's leading green economy organization. Founded in 1982, Green America provides economic strategies, organizing power, and practical tools for businesses and individuals to solve today's social and environmental problems. We have over 300,000 individual members and supporters as well as almost 2,000 members in our Green Business Network. Our mission is to harness economic power — the strength of consumers, investors, businesses, and the marketplace — to create a socially just and environmentally sustainable society.

One of Green America's most important areas of work is responsible finance, including socially responsible investing, better banking, and shareholder advocacy. Our members and supporters are committed not just to talking about sustainability, but to aligning their money with their values, especially with regard to preserving a livable planet for current and future generations. Younger members in particular are interested in earning competitive returns with socially responsible investing.

We write to provide Green America's perspective regarding hearings on environmental, social, and corporate governance (ESG) convened by the House Financial Services Committee this July, including the preliminary report on ESG Climate Related Financial Services Concerns by the ESG Working Group.

We would like to challenge several underlying assumptions in this report and other memos from the majority, and clarify several important foundational truths:

- ESG performance is on par or better than conventional investing, especially in the long term.
- Environmental, social, and governance considerations are material and pecuniary, not political.
- The shareholder proxy voting process gives retail investors a critical voice in corporate governance, and reforms suggested by the majority would stifle, not promote, that voice.

ESG performance is on par or better than conventional investing, especially in the long-term.

Multiple research studies show that returns on socially responsible investing are on par or better than investing not based on ESG principles, especially over the long term. For example:

- According to Morningstar's 2022 Sustainable Funds US Landscape Report, most sustainable funds delivered stronger total and risk-adjusted returns than their respective Morningstar Category indexes. Over half of sustainable funds finished in the top half of their Morningstar Category, led by equity funds. Data for the previous five years showed even better results – the returns of 74 percent or sustainable funds ranked in the top half and 49 percent in the top quartile of returns.

- In 2021, the Morgan Stanley Institute for Sustainable Investing released a study, Sustainable Funds Outperform Peers during 2020 Coronavirus. The Institute found that in a year of extreme volatility and recession, funds focused on "on environmental, social and governance (ESG) factors, across both stocks and bonds, weathered the year better than non-ESG portfolios." The research analyzed more than 3,000 US mutual funds and ETFs, finding that sustainable equity funds outperformed non-ESG peer funds by a median of 4.3 percent in 2020.

- The NYU Stern Center for Sustainable Business released a 2021 meta study, ESG and Financial Performance: Uncovering the Relationship by Aggregating 1,000 Plus Studies Published between 2015-2020. The report found that 59 percent of studies showed that ESG investments had a similar or better performance relative to conventional investment approaches, while only 14 percent found negative results. It also concluded that "ESG investing appears to provide downside protection, especially during social or economic crises."

The reason ESG investing works is that it seeks out information about risk and opportunity that is not necessarily reflected on a company's balance sheet. For example, if a company routinely dumps toxic chemicals into communities where it works, underpays and overworks its employees, and skirts basic safety practices, that poses a financial risk. Eventually these poor practices will catch up with that company, and investors and shareholders will be caught holding the bag. On the flip side, if a company takes advantage of burgeoning markets in clean energy, provides fair pay and benefits for its workers, and contributes to its community, that company is positioned for stable growth and greater profitability.

ESG investing exists because millions of Americans, including Green America's members and supporters, want to invest in companies that practice it. That's why $8.4 trillion – or $1 in $8 under asset management – are invested in sustainable assets as of 2022, according to the US SIF Foundation's Report on US Sustainable Investing Trends. Socially responsible investing that takes environmental, social, and corporate governance (ESG) factors into account has been steadily growing for decades.

Using ESG principles to help inform investing is not a breach of fiduciary duty. On the contrary, **not** taking all factors related to risk and opportunity into account could be seen as a breach of fiduciary duty. Individual, institutional, and public asset managers should be free to consider all information when making critical investment decisions. This is how the free market works. It is not the role of government on the federal or state level to tell asset managers how to manage investments for their clients.

Environmental, social, and governance considerations are material and pecuniary, not political.

Environment
The economic risks and impacts of the climate crisis are real. This March, the Intergovernmental Panel on Climate Change – the world's climate scientists – issued a "final warning" to humanity that we must act immediately and decisively to lower greenhouse gas emissions in order to avoid runaway global warming that will irreversibly harm the one planet humans have ever called home. We are already experiencing the economic impacts of climate events, from storms to droughts to extreme heat and cold.

Companies face physical risks resulting from climatic events, such as wildfires, storms, and floods. According to the National Oceanic and Atmospheric Administration, the year 2022 saw 18 billion-dollar-or-more weather and climate disasters that caused $176.9 billion in damages, the third-highest year on record. The number of such events has been steadily rising, with 33 in all of the 1980s, 57 in the 1990s, 67 in the 2000s, 131 in the 2010s, and we are already 60 just three years into the 2020s with 1,460 deaths and counting. Already 2023 is shaping up to be the hottest year on record, with the hottest day ever recorded in human history on July 4. Extreme heat is now killing more Americans than ever.

So far the earth has warmed 1.2°C since pre-industrial times. Deloitte finds that if we allow warming to reach 3°C, the global economy will lose $178 trillion by 2070 through a lack of food and water, a loss of jobs, worsening health and well-being, and reduced standard of living. On the flip side, if the world acts now to achieve net zero emissions by 2050, the transformation of the economy could increase the size of the world economy by $43 trillion in net present value terms from 2021-2070.

Companies also face both risk and opportunity from policy action needed to transition the economy off fossil fuels. Companies that invest in clean energy and energy efficiency are booming. Global renewable power capacity is now expected to grow by 2,400 gigawatts over the next five years, an amount equal to the entire power capacity of China today, according to the International Energy Agency. Despite uncertainty in the overall economy, jobs in the clean energy industry have seen double-digit increases, especially in Michigan, Texas, California, and West Virginia, according to the Department of Energy.

On the flip side, fossil energy of the past must be phased out – and the fossil fuel industry knows it. Last year the fossil fuel industry made record profits – but instead of using that money to transition their business model to the clean energy of the future, they are doubling down on fossil-fuel extraction – and bankrolling efforts to prevent workers from using their retirement investments to push companies to address the social and environmental concerns that negatively affect them and our financial system.

At its heart, this fight is about how large corporations should behave in our society: Should they focus on short-term, risky value extraction or long-term, sustainable value creation? Retirement funds, pensions, endowments, and college funds rely on long-term investments, where ESG makes a material difference.

Social

Failure to address racial equity issues within a company creates risks for shareholders, including risk of reputational damage, litigation, and adverse policy and regulatory action. Company actions that contradict stated positions create substantial risks and raise concerns about the adequacy of governance and oversight. Such actions entail significant costs to both the company and the economy.

Failure to address racial gaps for Black Americans in wages, housing, education, and investment has cost the U.S. economy $16 trillion over the last 20 years, according to a Citi analysis of the economic cost of racial inequality in the United States. If those gaps were closed, $5 trillion could be added to U.S. GDP over 5 years -- a primary driver of returns for long-term investors.

That is why shareholder proposals related to racial equity received strong support in 2022. A majority of the 20 largest asset managers — those with more than $1 trillion in assets under management — voted in favor of a majority of shareholder proposals on racial equity audits, board diversity, political spending and lobbying activity, human capital management, and tech company product and service issues, according to the Equity in the Boardroom report from February 2023.

Racial equity audits — an essential mechanism for management and oversight of risks associated with systemic racism — saw increased support from shareholders in 2022, with average support increasing from 33 percent to 44 percent, and six receiving majority support, the report said.

Governance

A company's political spending and lobbying can present significant reputational risk if not disclosed and managed. Many customers and the purchasing public – including Green America's members and supporters -- are paying close attention to whether a company's lobbying lines up with its corporate values. If there is a disconnect, companies face bad press, boycotts, or targeted social media campaigns.

According to the Conference Board, 87 percent of companies say the environment for corporate political activity is the most challenging in memory and likely to become even more so. Corporate political activity is being scrutinized not just by the media and employees, but by shareholders who are focused on whether a company's lobbying and political contributions are consistent with its public stances.

Customers and shareholders are concerned about corporate political spending and lobbying because a functioning democracy is foundational to a stable economy and sustainable long-term value creation. The United States is experiencing an erosion of democracy, as evidenced by decreased public trust in elections, voter suppression efforts, lack of transparency regarding political spending and lobbying, among other concerning trends, according to the Brookings Institution.

Costs of anti-ESG legislation

This year 165 anti-ESG bills and resolutions were introduced in 37 states. Some legislation requires state treasurers or comptrollers to create a blacklist of companies the state is not allowed to invest in or do business with. Such restrictions result in significant costs:

- A Wharton School study found that two 2021 Texas laws banning cities from contracting with banks that have ESG policies cost an extra $303 million to $532 million in higher municipal bond interest rates.
- A report by Econsult Solutions found that taxpayers in Florida, Kentucky, Louisiana, Missouri, Oklahoma, and West Virgina could owe up to $708 million in additional interest charges on municipal bonds due to anti-ESG laws and proposals.
- A Bloomberg article shows that Texas is paying 19 basis points more than California and Florida is paying 43 basis points – almost half a percentage point – more in interest rates on the bond market because they prohibit contracts with lenders that consider ESG.
- Indiana's budget office found that a bill forcing pension funds to divest from asset managers that consider ESG factors would cost $6.7 billion over the next decade in sub-market returns, force retirees to increase their contributions, and impose an additional $550,000 in administrative costs per year. Amended legislation now puts the estimated costs to pensions funds at $5.5 million.
- The Kansas Division of the Budget found that an anti-ESG bill could cost the Kansas Public Employees Retirement System upwards of $3.6 billion over the next ten years.

Public support for ESG

Despite the concerted campaign to push anti-ESG bills across dozens of states, multiple polls and focus groups show that public opinion clearly supports responsible investing.

- A poll by Penn State and ROKK Solutions found that 63% of respondents – including 70% of Republicans -- say the government should not set limits on ESG investments. The poll found 76% of voters feel companies play a vital role in society and should be held accountable to make a positive impact on the communities in which they operate. This finding is consistent across political lines, with a majority of both Republicans (69%) and Democrats (82%) in agreement.
- In focus groups conducted by JUST Capital in December 2022, participants said companies should be "good corporate citizens" and make a positive impact on society, especially by paying their employees a fair, living wage. They also saw ESG as part of a sound investment strategy.
- Polling by Climate Power and Data for Progress in March 2023 found that most respondents think financial managers should be able to consider ESG factors in investment decisions, and they support investing public retirement funds in clean energy assets.

Investors also see ESG as a critical part of their fiduciary duty: 85% of investors are interested in responsible investing, 86% believe companies with sustainability practices may be better long-term investments, and 84% are interested in sustainable investments that can be tailored to their needs, according to US SIF: The Forum for Sustainable and Responsible Investment.

The shareholder proxy voting process gives retail investors a critical voice in corporate governance, and reforms suggested by the majority would stifle, not promote, that voice.

The ESG Working Group's preliminary report on ESG Climate Related Financial Services Concerns lists as its top priority "reform of the proxy voting system to safeguard the interests of retail investors." However, the revisions this report calls for would squash a critical tool that allows retail investors to protect their investments by providing an efficient way to communicate their views on material issues.

The SEC shareholder proposal rule, in place for 50 years, has been used to encourage companies to adopt policies that are now widely viewed as best practice, driven initially by shareholder proposals. For example, electing directors by majority vote rather than a plurality was a radical idea when shareholders first proposed it over a decade ago, but is now the norm at large-cap U.S. companies. SEC rules exclude proposals that address the day-to-day management of companies but preserve the right of investors to debate perspectives on emerging issues that are relevant to companies' futures.

We would like to address some specific claims made by the ESG Working Group's preliminary report.

Shareholder proposals are not a significant burden for public companies.
The only mandatory cost under the shareholder proposal rule is for the company to publish a proposal of up to 500 words on its proxy ballot. All other spending is discretionary, and almost all shareholder proposals are non-binding. The board does not have to do anything in response to a proposal.

Shareholder proposals constitute a small percentage of overall proxy votes each year. According to the Council of Institutional Investors, most public companies do not receive any shareholder proposals. On average, 13% of Russell 3000 companies received a shareholder proposal in a particular year between 2004 and 2017. In other words, the average Russell 3000 company receives a shareholder proposal once every 7.7 years. For companies that receive a shareholder proposal, the median number is one per year.

Raising thresholds for ownership and resubmission would squash the voice of small investors.
Currently, in order to file a shareholder resolution at a given company, a person must have owned at least $2,000 of company securities for at least one year. The working group proposes raising that

threshold to continuous ownership of at least $2,000 of the company's securities for at least three years; continuous ownership of at least $15,000 of the company's securities for at least two years; or continuous ownership of at least $25,000 of the company's securities for at least one year.

Such revisions would hamper the participation of small and diverse investors in the shareholder resolution process. These smaller investors can have a great impact on corporate practice. According to data compiled by the Sustainable Investments Institute, 176 resolutions on social and environmental topics came to a vote at U.S. companies in 2019. Many were filed by investors with small ownership thresholds. The proposals received an average of 25.5% support, demonstrating that proposals of interest to a large portion of a company's shareholder base can originate with smaller investors.

Likewise, the working group proposes raising the voting thresholds needed to resubmit a shareholder resolution from 3%, 6% and 10% in the first, second and third year respectively, to a vote of 5%, 15%, and 25% in order to resubmit a shareholder resolution the following year. Again this would squash the voice of small and diverse investors, especially as concerns emerging issues.

In some cases, it can take years for issues such as climate risks, human rights assessments, and governance reforms to be recognized as important to a company's returns. Through long-term investor engagement and education, corporate boards and shareholders often eventually do adopt proposals that had less support at first but are now seen as best practices.

In 2020, the SEC raised ownership and resubmission thresholds to respond to pressure from corporate trade associations, presenting significant hurdles to filing and resubmitting shareholder proposals. Raising these thresholds again would shut out small investors and leave emerging issues unaddressed.

Proxy advisory firms do not wield excessive influence over investors.
Many pension funds and other institutional investors review research and recommendations from proxy advisors but vote according to their own guidelines and policies. According to proxy advisor ISS, 85% of its top 100 clients use a custom voting policy.

Institutional investors do not "robo vote" proxy advisor recommendations. An NYU-UPenn study finds that the impact of recommendations by ISS is significantly reduced when company-specific factors are taken into account. The proposed curbs on proxy advisors could undermine the voice of investors by limiting the information available and further tilting votes on key proposals in favor of management.

Thank you for your consideration of these important matters regarding responsible finance. Please do not hesitate to reach out if you have any questions or would like any other information.

Sincerely,

Cathy Cowan Becker
Responsible Finance Campaign Director
Green America

cc: Members of the House Financial Services Committee
cc: Members of the House Sustainable Investment Caucus