IMPAX Asset Management
Adviser to Pax World Funds

August 16, 2022

Vanessa A. Countryman
Secretary, Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Subject: Comments on File Number S7-17-22, Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, and on File No. S7-16-22, Investment Company Names

Dear Ms. Countryman and SEC Commissioners,

Impax Asset Management is a specialist manager focused on investing in the transition to a more sustainable economy. We are writing with comments on the SEC's proposed amendments to the so-called Name rule as well a new proposed rule regarding enhanced disclosures by certain investment advisers and investment companies regarding environmental, social, and governance (ESG) investment practices.

We appreciate the Commission's desire to better define the nature and scope of funds and strategies that incorporate ESG or sustainability-related factors into their investment approach. As the proposed rule notes, investor interest in such funds has grown considerably over the past several years. Moreover, many aspects of ESG or sustainability are not precisely defined, which has arguably led to a proliferation of approaches that may not be well understood by investors.

We also appreciate that the Commission has refrained from taking a granular, taxonomic or overly prescriptive approach, instead allowing participants in the marketplace to explain what they mean when they use certain terms to describe their investment processes. Very few ESG or sustainability-related issues have straightforward binary characteristics; instead, they span a continuum, and different investment portfolios or different investors may make different judgments on whether or where particular activities may fall along the sustainability spectrum.

Finally, we appreciate the Commission's concerns about "greenwashing". We share those concerns.

It is our view, however, that the proposed rules are not ideally designed, or even necessary, to achieve their objectives, for reasons set forth below.

Proposed Amendments to the Investment Company Names Rule pose some challenges

While we generally favor the Commission's recommended amendment to the Names Rule as applicable to a wider category of funds, including ESG or Sustainability-related funds, we also believe it poses some challenges. Should firms choose to classify their funds as "ESG Integration" funds because ESG factors are not "the main" or "dispositive" decision criteria, but still choose to use an ESG or sustainability-related name for a fund because sustainability factors are still important criteria, would that be permissible under the proposed Names rule so long as at least 80% of the names in the fund met the firm's own definition of ESG or sustainability? Or are only "ESG-focused" funds permitted to use an ESG or sustainability-related name? Does meeting the 80% test for holdings regarding ESG or sustainability-related criteria automatically mean that a fund is an "ESG-focused" fund or is that determined by whether ESG or Sustainability-related factors are the most "significant", "main" or "dispositive" factor in securities selection?

Also, since the category of "Integration" funds is broad enough to permit almost any approach to ESG or sustainability in investment management, is there a risk that commentators or third parties may be tempted to lump all Integration funds together and view the entire category as greenwashing? Could this in turn open "Integration" funds to potential litigation or enforcement actions? These questions seem to arise from the Names rule proposal, but we are not sure they are answered by that proposal.

Finally on the Names rule, it could be a problem for so-called best-in-class ESG or sustainability-related funds. There are ESG indexes and passive strategies that invest in sector/industry ESG leaders in broadly diversified funds. Some of these are broadly diversified to meet the needs of certain institutional investors who have stricter limits on tracking error to major benchmark indexes. Because of those restrictions, broadly diversified ESG index funds might be classified as integration funds, as ESG is not the main focus or dispositive in index construction. However, it is also entirely possible for a best-in-class ESG index to have 100% of its holdings meet its particular best-in-class ESG criteria. If such a fund cannot use an ESG- or sustainability-related name, this could actually create more confusion among investors who are then unable to distinguish these funds from parent indexes or index universes.

Singling out ESG or Sustainability-focused Funds is otherwise unnecessary and unwarranted

The principle that underpins the proposed rules is providing accurate and adequate information to investors, something that is squarely in the Commission's purview and jurisdiction. However, we are concerned that the Commission is singling out ESG or sustainability-focused funds for a level of scrutiny, definition and disclosure that is not being required of other funds – without a sufficient factual basis or adequate rationale for doing so.

Many investors arguably lack detailed understanding of the investment processes involved in many different kinds of funds with many different names and investment strategies. For example, there are funds with names that give little insight into their investment processes, including language like "new horizons", "durable value", "capital income" "new perspective", among others. The average investor may not understand the import of many of these names, or the investment processes of the funds, or the particulars of investing in general, and yet ESG or sustainability-focused funds are being singled out as the only investment discipline that is poorly understood by investors and in need of greater definition and clarity. Even terms like "small cap," "growth," "value", "alternatives" may not be widely understood among the investing public, nor are there precise definitions for all of these terms; they can be and are used differently by different practitioners. Again, however, only one category of fund is being singled out for additional scrutiny and disclosure.

It is our understanding that the Commission has historically refrained from specifying reporting requirements for particular investment strategies or approaches. In this instance, however, the

Commission has suddenly taken a very different approach, applicable to only to a certain category of investments, which appears to be a departure from tradition. We are concerned that the Commission has not made a compelling case supported by sufficient facts to justify such a departure.

The SEC does not need additional authority to address "greenwashing"

On page 8 of the proposed rule, the SEC states that funds and advisers *"may exaggerate their ESG practices or the extent to which their investment products or services take into account ESG factors. With respect to environmental and sustainability factors, this practice is often referred to as 'greenwashing'."* We understand that this does happen, but the SEC already has authority under anti-fraud provisions of federal securities laws to investigate and take appropriate action with respect to funds that misrepresent what they do. We note that earlier this year the SEC brought enforcement actions against two financial firms and is investigating a third regarding ESG practices, prior to the release of this proposed rule.[1] We are not at all clear on how the proposed rule will make it less likely that a firm will "greenwash" or more likely that the Commission will be in an improved position either to prevent the same or take action to enforce federal securities laws once violated.

Proposed fund classifications will not dispel confusion or add clarity

The effort to categorize different types of ESG or sustainability-focused funds will not in our view provide significant enlightenment to investors. The categories themselves raise more questions than they answer, do not reflect how investment processes actually work or funds are managed in the real world, and are somewhat overlapping. The proposed classifications for "ESG integration" funds and "ESG-focused" funds, in particular, are not clearly delineated nor are the categories themselves sufficiently distinct. Many existing strategies that incorporate ESG or sustainability factors could fit comfortably in either, or uncomfortably in both.

For example, an Integration fund may "consider one or more ESG factors alongside other, non-ESG factors in investment decisions" but they are "generally not dispositive", while an ESG-focused fund uses ESG factors as "significant or main consideration[s]" in making investment and engagement decisions. It is difficult in practice to distinguish clearly between these two. Whether a factor is "dispositive" or "significant" or the "main" factor in a particular fund strategy may itself depend on its interplay with other factors and other elements of the investment process, including financial factors unrelated to ESG, market conditions and other considerations. We know of few investment approaches where a single factor is "dispositive", and this includes a variety of investment approaches across a range of asset classes, among both funds that incorporate ESG and those that do not. The proposed rule therefore introduces a false simplicity for classification purposes that is not reflective of how funds are actually managed in the real world.

For example, our investment process at Impax focuses on investing in the transition to a more sustainable economy, which means we look for investment ideas among industries and sub-industries we believe are higher in opportunity and lower in risk, enjoying tailwinds rather than headwinds in this transition. We invest in companies positioned to benefit from this transition – their products or services

[1] David Isenberg, "'When an Advisor lies,' the SEC Acts: Enforcement Head," *Ignites*, July 20, 2022.

may address issues like the low-carbon transition, sustainable agriculture, or the circular economy. We also include ESG analysis in our fundamental research of companies to the extent we consider those factors to be material. But that does not mean that a single factor or even "ESG" factors more generally are the "main" driver of investment decisions. We also conduct extensive financial analysis focusing on factors such as earnings, valuation, leverage, P/E ratios, and the like, but seldom if ever are any of these the "main" factor in an investment decision either.

A rigorous stock selection process requires a robust analysis that covers a range of factors and it is simply not the case that a single factor or even a grouping of factors are typically the "main" or most "significant" factor. In the end, stock selection is the portfolio management team's decision after weighing everything, i.e., all factors they deem material. We are concerned that the Commission's proposed rule overly simplifies portfolio management, and again, only for investment offerings that incorporate ESG or sustainability-related factors but for no one else in the marketplace.

We also view the ESG strategy overview table, proposed for ESG-focused funds on page 36 of the proposed rule, as a poor vehicle for characterizing an investment process that truly integrates ESG or sustainability-related factors into investment decisions. For example, except for a small number of criteria in some of our strategies relating to weapons and tobacco, almost *none* of the top-down macro analysis or bottom-up fundamental analysis we do can be shoehorned into categories called "applies an inclusionary screen" or "applies an exclusionary screen." The sustainability-related risks and opportunities we analyze compare companies with their peers across multiple dimensions, and companies may or may not meet our standards for investment at any given time; calling that an "inclusionary screen" or an "exclusionary screen" is simply inaccurate and misrepresents not only our process but also the investment processes of many if not most funds that incorporate ESG or sustainability-related factors.

Rather than utilizing the three categories proposed in the rule, which may not accurately reflect the investment approaches of many if not most ESG or Sustainability-focused funds, we suggest that the Commission consider other approaches such as that, for example, put forward by the CFA Institute. That approach uses five classifications that more accurately capture the range of strategic approaches to ESG or sustainability-related investing. The CFA Institute identifies best-in-class, exclusionary screening, ESG integration, impact investing, and sustainability themed investing as approaches to sustainable investing, and also suggests the types of disclosure appropriate to each strategy.[2] Some funds may use more than one of these tools. Some of what the SEC has included in the proposed rule could be easily adapted to that framework, but it should be noted that that framework does not require funds to classify themselves in one category, but more realistically recognizes that a single fund may use multiple approaches.

Reporting on proxy voting and engagement is already sufficient

We also note that the SEC is proposing to require some funds to report, in the summary table, whether the fund considers proxy voting and engagement with issuers part of their ESG strategies. Any fund registered under the Investment Company Act of 1940 is already required to publish its proxy voting

[2] CFA Institute, "Global ESG Disclosure Standards for Investment Products," 2021. Global-ESG-Disclosure-Standards-for-Investment-Products.pdf (cfainstitute.org)

guidelines, according to the SEC's 2003 rule.[3] As the agency stated in that rule, "[t]his increased transparency will enable fund shareholders to monitor their funds' involvement in the governance activities of portfolio companies, which may have a dramatic impact on shareholder value." It is easy to infer that the SEC regards proxy voting as part of the investment strategy of *any* registered fund, and that is reflected in the proxy voting guidelines and proxy votes that funds and fund families disclose. Clearly, governance, at a minimum, is regarded as material to investment decision making. But the proposed rule does not establish compelling reasons for additional reporting requirements applicable only to ESG or sustainability-focused funds. This strikes us as arbitrary and unnecessary, given both the amount of information available on how funds vote and the fact that proxy voting is usually a key part of any investment product.

If there is any additional disclosure that would be useful to investors on proxy voting and voting guidelines, one thing that could be useful is for investment managers with more than one fund to explain why they voted differently on the same ESG or sustainability-related issues, at the same companies, for different funds. It is not clear why, given the fact that proxy voting "may have a dramatic impact on shareholder value" according to the SEC's own rule, different votes on a single issue at a single company would differ by fund.

Greenhouse gas emissions disclosure

It is increasingly clear that climate change can have material impacts on both business and economic outcomes. The United Nations Framework Convention on Climate Change has urged, in the strongest terms, that the world reduce its net emissions to zero by midcentury in order to avoid a climate catastrophe. The economic impacts of climate change are likely to be dramatic. For example, the Brookings Institution estimates that if emissions are not abated, global GDP could well be more than 20% lower than if we were to curb emissions.[4] One of the world's largest insurance companies, Swiss Re, notes that the world economy could lose up to 18% of its GDP if no action is taken to mitigate climate change.[5] It is important to global economies and capital markets that emissions be reduced, if possible, to net zero by midcentury. The risks associated with not doing so are enormous.

We are concerned, however, that choosing this single reporting standard of GHG emissions for any fund that "consider[s] environmental factors" is not only unduly burdensome but is not tailored to provide investors with information that will be useful to them. It may be an appropriate metric for funds that focus on climate change among other environmental issues, but there are also funds that focus on other environmental issues, such as natural resources or biodiversity. While climate is one measure of environmental impact, it is not the only one and may not even be a major focus of some "environmental" strategies.

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[3] Securities and Exchange Commission, "Final Rule: Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies," 17 CFR Parts 239, 249, 270 and 294, Effective April 14, 2003. Final Rule: Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies; Release Nos. 33-8188, 34-47304, IC-25922 (sec.gov)

[4] Marshall Burke, "The global economic costs from climate change may be worse than expected," Brookings Institution, December 9, 2015.

[5] "World economy set to lose up to 18% GDP from climate change if no action taken, reveals Swiss Re Institute's stress-test analysis," Swiss Re Group, 22 April 2021, World economy set to lose up to 18% GDP from climate change if no action taken, reveals Swiss Re Institute's stress-test analysis | Swiss Re.

Even for investment portfolios that consider climate change, the carbon footprint of a portfolio is only one measure of the portfolio's contributions to mitigation and adaptation. The exposure of the portfolio to physical risks, which is more about where the portfolio's assets and key supply chain nodes are located than it is about specific company emissions, could also be seen as a key measure of portfolio exposure to climate change. It is also the case that a portfolio that focuses on environmental solutions, including climate solutions, may look misleadingly out of line with emissions reduction ambitions. This is because some of those solutions, things like wind turbines, solar panels or clean water equipment and technologies, are found in the industrials and materials sectors where relatively high carbon emissions involved in manufacture are necessary to avoid emissions over the longer term. We suggest that if the Commission mandates emissions reporting, the requirement should only be mandated for funds that focus primarily on climate risks and opportunities rather than on environmental strategies more broadly.

Conclusion

We appreciate the Commission's interest in providing more clarity to investors on the use of ESG or sustainability-related criteria in investment funds. However, we would urge you to carefully consider the wisdom of singling out ESG or sustainability-focused funds for new required disclosures not applicable to other funds, particularly where information is already sufficient for investor needs (e.g. proxy voting and proxy voting guidelines). Most importantly, we would advise against the creation of unrealistic categories or definitions that no not reflect how such funds are actually managed and arguably do not provide additional, helpful information to investors.

Sincerely,

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President

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