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**PROPONENT TESTIMONY ON HOUSE BILL 2436
The Kansas Public Investments and Contracts Protection Act**

**Presented to the House Committee on Financial Institutions and Pensions
By Kansas State Treasurer Steven Johnson**

March 8, 2023

Chair Hoheisel and Members of the Committee:

Thank you for the opportunity to testify in support of HB 2436, a bill that addresses various concerns regarding the utilization of environmental, social and governance (ESG) factors in state contracting and state investments to the detriment of taxpayer expense and the return on capital investments. House Bill 2436 seeks to ensure that in the context of state contracts and state investments, the focus of the law is clearly and solely on the financial interests of Kansas taxpayers and the beneficiaries of the state public investments, including the Kansas public employee retirement system.

As Kansas State Treasurer, I operate as a fiduciary on behalf of the state of Kansas. Each time I see the agency seal for the Office of the State Treasurer, I am reminded of my fiduciary responsibilities. The State Treasurer seal depicts a watchdog guarding a safe below the Latin phrase, "Semper Fidelis." This motto, which our office shares with the United States Marine Corps, means "always faithful." Our motto is closely aligned with the traditional meaning of "fiduciary duty." A faithful fiduciary prioritizes the interests of those they represent before their own self-interests. In the investment sector, a fiduciary acts solely in their client's best interest when they give advice and make investment decisions intended to maximize the return on their client's investment funds.

In recent years, the utilization of ESG factors in investment practices has interjected environmental, social, and governance goals into investment decisions. In the context of how individual investors seek to invest their own funds, ESG investing may be an option provided the investor makes his or her decision knowingly after full disclosure. However, in the context of the investment of public funds, these considerations are improper, often contradict other policy goals and considerations of the state, and ultimately weaken the financial condition of the state's investments. Placing ESG "scores" on subjective topics like "How well does a company safeguard the environment?" "Which investment opportunity has a more socially responsible operation?" or "Which corporate board is more diverse?" has allowed for personal beliefs and political preferences to interpose itself into the investment decision process and should not have a role in the investment of the state's assets.

Without a doubt, current ESG methods favor one political ideology over another. But we should keep in mind, there is constant turnover in the political process. At the Securities and Exchange Commission (SEC), Chairman and President Biden appointee, Gary Gensler, has embraced the idea that using ESG scoring falls within the fiduciary duties of the securities sector. However, a new President, with new appointees, could find new subjective ways to interject policy preferences into the definition of fiduciary duty. In a world where the trend is to politicize everything, when it comes to the return on investment, we cannot afford to lose focus. Addressing the use of subjective ESG criteria to redefine the duties of a fiduciary is key to upholding our responsibility.

The legislation before you is about pushing back against the subjective nature of ESG investing. When it comes to investing state dollars, the priority must remain focused on free market principals and embracing the traditional, non-politicized meaning of fiduciary duty. That duty acknowledges that the foremost goal of the investment of public funds is to produce the highest returns with the lowest possible risk.

This bill does three things to push back on fiduciaries and investment professionals who use the subjective nature of ESG to politicized their asset allocation and proxy voting.

1. First and foremost, this bill withdraws unregulated proxy-voting authority from all outside asset managers to ensure that shares of stock (including mutual and index funds) purchased with state funds are voted in the sole interest of the pension fund's beneficiaries rather than to advance ESG or other nonfinancial goals. Reducing the massive share-voting influence of ESG-supporting asset managers such as BlackRock and State Street would reduce their ability to elect directors or support activist resolutions.
2. Second, the contracting provisions contained in Section 2 of the bill ensure that no state agency or local government may give preferential treatment or discrimination based on ESG criteria. This provision also mandates contracting neutrality and non-discrimination throughout the public contracting process. This is especially important for the state's banking contract, which is up for renewal in 2024.
3. Third, Section 6 of the bill clarifies an existing state statute governing the KPERS investment objective, by giving clear direction that the KPERS funds cannot be used for investments, the purpose of which is for economic development or social purposes or objectives. The current prohibition language allows ESG to be inserted into the decisions of the board, so long as the "sole or primary" objective is not for "social purposes or objectives."

The bill does other things that are beneficial, including clarifying definitions and establishing enforcement mechanisms. Further, there may be other amendments offered that may be worthy of inclusion, but I ask the committee to keep the three principal goals in mind as it considers the bill.

As I have communicated for months, the primary goal of any Kansas ESG legislation should be to ensure the free market continues to operate unimpeded by the insertion of subjective, politically driven policy goals. As State Treasurer, I take my fiduciary duty seriously and want to make sure that the focus of the law is clearly and solely on the financial interests of Kansas taxpayers and the beneficiaries of Kansas public investments.