



ESG Update: Assessing the Landscape in 2023

William J. Stellmach | Sean Sandoloski | John L. Brennan
March 23, 2023



Recapping Our Last Webinar on This Topic

- In April 2021, we presented a webinar on the litigation and enforcement perspectives concerning ESG investing (following an initial presentation in August 2020)
- Among other things, we discussed:
 - Rising ESG trends in 2021, including human capital management, litigation arising from Covid-19, scrutiny of greenwashing, and the proliferation of ESG ratings agencies.
 - European ESG trends.
 - Private sector “enforcement” of ESG standards.
 - An outlook for the Biden administration.
- Feel free to reach out to us if you would like the materials from our April 2021 webinar, or our August 2020 webinar.

Agenda

- 1. Update on the SEC's New Regime**
- 2. Recent Increasing Scrutiny of ESG**
- 3. ESG Under the 118th Congress**
- 4. Resolving Conflicting Pressures**

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Recap: Early Steps Taken by New SEC Leadership

- Gary Gensler nominated and confirmed as Chair.
- Appointment of known ESG proponents as acting director of Division of Corporate Finance, senior policy advisor for ESG issues, Senior Counsel for Climate and ESG to the Director of the Division of Corporate Finance.
- Acting Commissioner Lee directed the Division of Corporate Finance “to enhance its focus on climate-related disclosure in public company filings,” focusing specifically on 2010 guidance.
- Creation of Climate and ESG Task Force in SEC’s Division of Enforcement.



SEC Risk Alert



- In the Division of Examinations' April 9 Risk Alert regarding its "Review of ESG Investing," the SEC observed:
 - "lack of adherence to global ESG frameworks where firms claimed such adherence";
 - Lack of "adequate controls around implementation and monitoring of clients' negative screens (e.g., prohibitions on investments in certain industries, such as alcohol, tobacco, or firearms), especially if the directives were ill-defined, vague, or inconsistent."
 - "compliance programs that did not address adherence to global ESG frameworks to which the firms claimed to be adhering."

SEC Approval of Nasdaq Diversity Rule



- The SEC approved a rule that requires Nasdaq-listed companies (with some exceptions):
 - to have at least two board members who are diverse, or to explain why it does not; and
 - to disclose information about board diversity.
- Certain issuers are exempt from these requirements.

Comments from Chair Gensler

“Which data and criteria are asset managers using to ensure they’re meeting investors’ targets—the people to whom they’ve marked themselves as ‘sustainable’ or ‘green?’ I think investors should be able to drill down to see what’s under the hood of these funds. As there’s not a standardized meaning of these sustainability-related terms, I’ve asked staff to consider recommendations about whether fund managers should disclose the criteria and underlying data they use.”

Prepared Remarks Before the Asset Management Advisory Committee (July 7, 2021)



Steps Toward ESG Enforcement in 2022

- In 2022, the SEC proposed ESG-related disclosure rules.
 - March 2022 – the SEC proposed rules requiring public company registrants to disclose climate-related information.
 - May 2022 – the SEC proposed rule amendments that would require funds and advisers to disclose information regarding ESG strategies.



Steps Toward ESG Enforcement in 2022

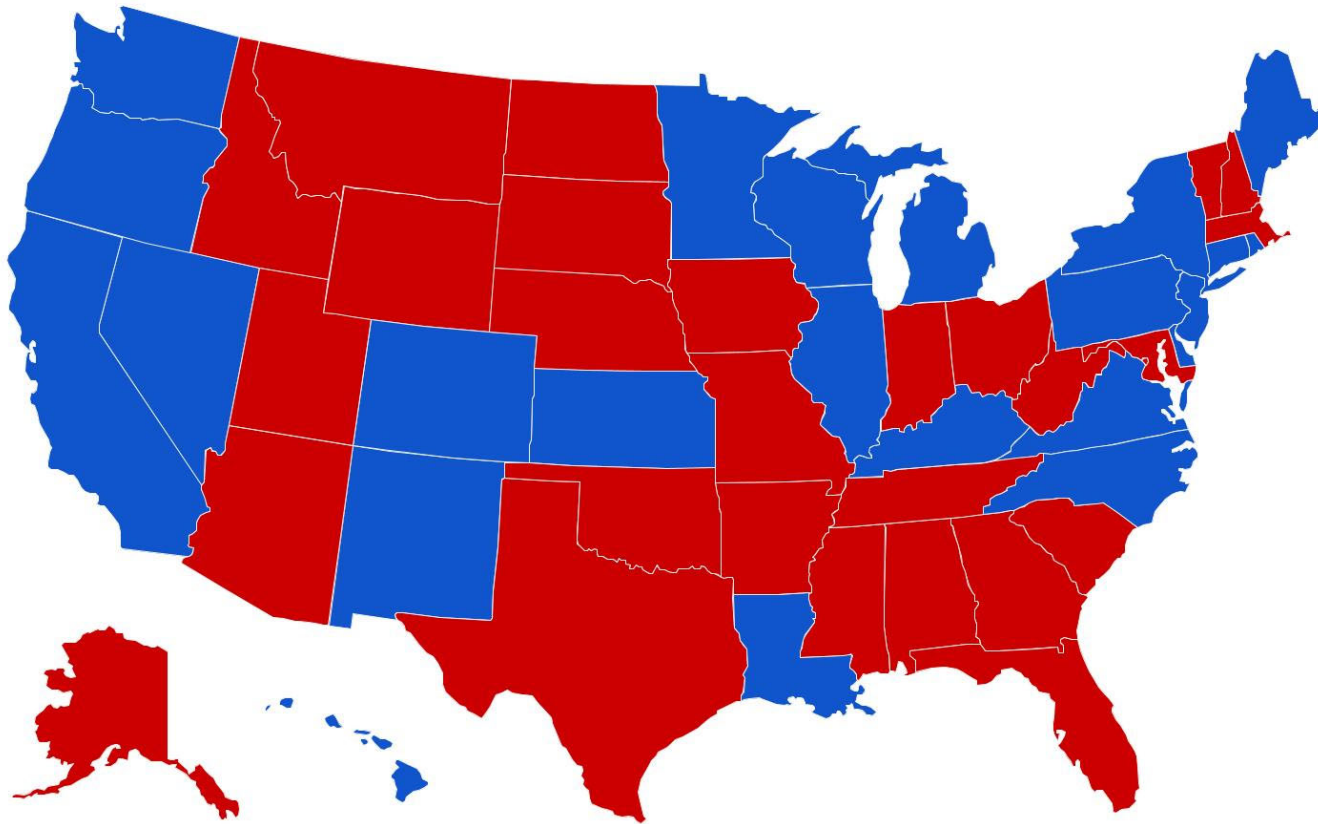
- The Climate and ESG Task Force has actively pursued enforcement actions:
 - Against an investment advisor, for misstatements and omissions concerning ESG considerations;
 - Against a Brazilian mining company, for misleading investors about safety of dams;
 - Against a U.S. mining company, for misleading investors about cost increases.
 - Against a robo-adviser, for misleading clients about fund compliance with Sharia Law.



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Challenges from State Governments



Letter from 19 Attorneys General



Mark Brnovich
Arizona Attorney General



Steve Marshall
Alabama Attorney General



Chris Carr
Georgia Attorney General



Todd Rokita
Indiana Attorney General



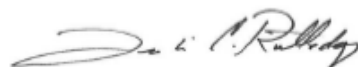
Daniel Cameron
Kentucky Attorney General



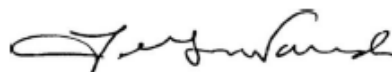
Lynn Fitch
Mississippi Attorney General



Doug Peterson
Nebraska Attorney General



Leslie Rutledge
Arkansas Attorney General



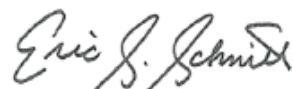
Lawrence G. Wasden
Attorney General of Idaho



Derek Schmidt
Kansas Attorney General



Jeff Landry
Louisiana Attorney General



Eric Schmitt
Missouri Attorney General



Austin Knudsen
Montana Attorney General



John O'Connor
Oklahoma Attorney General



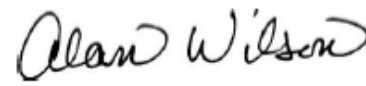
Ken Paxton
Texas Attorney General



Patrick Morrisey
West Virginia Attorney General



Dave Yost
Ohio Attorney General



Alan Wilson
South Carolina Attorney General



Sean Reyes
Utah Attorney General

Spectator or Quarterback?



ESG at Odds With Fiduciary Duties?

Top 3 Duties of a Fiduciary



The Duty to Act
in Good Faith

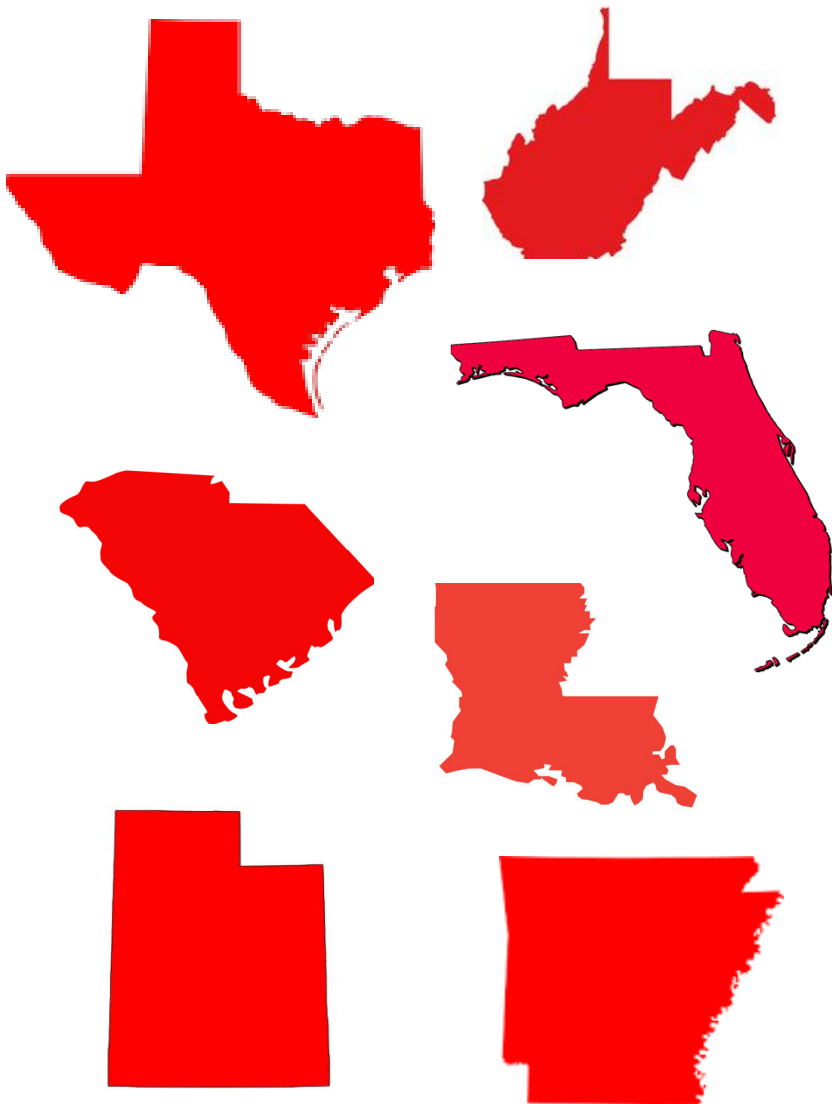


The Duty
of Care



The Duty
of Loyalty

State Boycotts of ESG Investments



State Investigation Into Major Banks

- 19 Republican-led states, led by Missouri's then Attorney General (and Senator) Eric Schmitt, launched an investigation into 6 banks.
- The investigation focuses on the banks' involvement in the United Nations' "Net-Zero Banking Alliance."
- Schmitt stated that the alliance "is a massive worldwide agreement by major banking institutions, overseen by the UN, to starve companies engaged in fossil-fuel related activities of credit on national and international markets. Missouri farmers, oil leasing companies, and other businesses that are vital to Missouri's and America's economy will be unable to get a loan because of this alliance."



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What to Expect from the New Congress

- With the Republicans in control of the House, similar investigative scrutiny can be expected at the federal level.
- According to reports, even before the election, corporate executives have been preparing for potential congressional hearings about ESG issues.
- Topics could include:
 - Climate;
 - Diversity;
 - Ties to China;
 - Censorship.



Putting Lawyers on Notice

The ESG movement attempts to weaponize corporations to reshape society in ways that Americans would never endorse at the ballot box. Of particular concern is the collusive effort to restrict the supply of coal, oil, and gas, which is driving up energy costs across the globe and empowering America's adversaries abroad. Over the coming months and years, Congress will increasingly use its oversight powers to scrutinize the institutionalized antitrust violations being committed in the name of ESG, and refer those violations to the FTC and the Department of Justice. To the extent that your firm continues to advise clients regarding participation in ESG initiatives, both you and those clients should take care to preserve relevant documents in anticipation of those investigations.


Sincerely,



Tom Cotton
United States Senator



Michael S. Lee
United States Senator



Charles E. Grassley
United States Senator



Marsha Blackburn
United States Senator



Marco Rubio
United States Senator

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House Committees' Subpoena Power



House Committee on Education and the Workforce

- The chair may authorize and issue subpoenas, and must notify the ranking minority member 24 hours in advance, to the extent practicable.
- “It is incumbent on the Department of Labor to ensure retirement savers are protected and that plan fiduciaries are not allowed to sacrifice retirement certainty in the name of non-financial goals.” -- chair Virginia Foxx (NC)



House Committee on Financial Services

- The chair may authorize subpoenas, which may be issued by the chair or by any designated member of the committee. The chair must notify the ranking minority member at least 48 hours in advance of the authorization and issuance of a subpoena.
- “The SEC’s proposal to require disclosure of information related to climate change that is not material for most companies is tone-deaf and misguided.” -- chair Patrick McHenry (NC)
- Rep. McHenry announced the formation of a Republican Working Group to “combat the threat” of ESG.



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House Committee on Oversight and Reform

- The chair may authorize and issue subpoenas without a vote by the committee or a subcommittee, and without any requirement to consult with or notify the ranking minority member.
- Climate disclosure requirements “would impose burdensome and unnecessary requirements on businesses of all sizes, including disclosure requirements of direct and indirect carbon emissions of third-party entities involved in a company’s operation.” – chair Rep. James Comer (WVa)



Attempted Overturn of Labor Department Rule

- “ I rise today to warn against our Administration’s unrelenting campaign to weaken our energy security, our national security and our economic security to advance, truly, their environmental and social agenda.” – Sen. Manchin
- “I just signed this veto because the legislation passed by the Congress would put at risk the savings of individuals across the country. They couldn’t take into consideration investments that would be impacted by climate, impacted by overpaying executives, and that’s why I decided to veto it. It makes sense to veto it.” – President Biden



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Counterweights to Republican Challenges to ESG

- Even after the transition of leadership in Congress, companies and investment managers will continue to face competing pressures from:
 - The SEC;
 - Non-governmental organizations;
 - Investors;
 - Foreign governments;
 - Consumers.



Irreconcilable Conflict?



Best Practices

- Ensure the accuracy of any disclosures.
- Maintain transparency about the basis for any claims made.
- Understand all applicable requirements.





Questions

Please use the Q&A function in the Zoom taskbar to submit your question to the Panelists

Thank You



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