

COMMENT

GOVERNMENT-MANDATED ESG DISCLOSURE: IT'S NOT EASY BEING GREEN*

ABSTRACT

Currently, in the United States, there are no national standards or guidelines to ensure that companies who claim to be sustainable or socially conscious are accurately reporting their business practices. To that end, in the spring of 2022, the Securities and Exchange Commission (SEC) proposed rule amendments intended to increase the scope and standardize the reporting requirements and disclosures for Environmental, Social, and Governance (ESG) factors for ESG-focused investment vehicles. This Comment explores the historical relevance of ESG, these proposed rules, and potential implications and impacts on environmentally efficient economics and corporate social sustainability and responsibility.

The proposed rules are aimed at decreasing greenwashing litigation liability, increasing fund transparency for investors and investment efficiencies, internalizing externalities, and creating a widely understood and consistent standard with which all industries can comply. However, critics raise concerns about the

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impracticability of creating all-encompassing standards, the difficulties for industries to comply and properly report on ESG factors, and most pressing, whether the SEC has the statutory authority to promulgate and enforce these rules at all. This Comment explores the delicate balance between the arguably noble goals the SEC is working to achieve and the potential hardships these rules may impose on both public and private companies.

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I. INTRODUCTION

“When you break new ground, the first transactions are always challenging and complicated. But scale and speed are the goals for climate and conservation finance; there’s an urgency here to apply new ways of thinking to find creative solutions.”¹

In March and May of 2022, the Securities Exchange Commission (SEC) proposed rules designed to standardize and mandate line-item environmental, social, and governance (ESG) reporting requirements for public funds holding themselves out to be focused on ESG initiatives.² These proposed rules represent a significant departure from the current materiality standards that apply to fund reporting and disclosures. If adopted,³ these rules will have major implications for companies that will likely need to increase capacity and devote greater internal resources to comply with the more stringent reporting requirements.⁴

Part II of this Comment explores the history and evolution of ESG in general and as it relates to investment vehicles, as well as its importance in a greater context. It then explains what the SEC-proposed rules would change (and for whom) and what the rules are purportedly intended to accomplish. Part III identifies potential legal and business-related implications, including the likelihood of a rise in greenwashing litigation, increased corporate transparency, possible investment efficiencies, and challenges facing industries that would need to adopt new (or better) compliance and reporting operations. Then, it analyzes likely future legal challenges to the SEC’s authority to enact and enforce these rules and the polarizing public responses to the proposal.

1. *McKinsey Quote of the Day*, MCKINSEY & CO. (Mar. 14, 2023), <https://www.mckinsey.com/featured-insights/quote-of-the-day/december-21-2022> [<https://perma.cc/9PKL2ZAY>] (quoting Marisa Drew, Chief Sustainability Officer of Standard Chartered, commenting on Asia’s transition to net-zero).

2. *See Proposed SEC Climate Disclosure Rule*, BLOOMBERG L. (Aug. 15, 2022), <https://pro.bloomberglaw.com/brief/proposed-sec-climate-disclosure-rule/> [<https://perma.cc/FUP8-4S2M>].

3. Shortly before the publication of this Comment, in March of 2024, the SEC finalized one of the two discussed disclosure rules. *SEC Adopts Rules to Enhance and Standardize Climate-Related Disclosures for Investors*, U.S. SECS. & EXCH. COMM’N (Mar. 6, 2024), <https://www.sec.gov/news/press-release/2024-31> [<https://perma.cc/KNJ9-BMPA>]; For consistency, the Author will continue to refer to both rules as “the proposed rules” and will maintain the analysis as to the potential implications and impacts of these rules, which we still have yet to experience.

4. *See Proposed SEC Climate Disclosure Rule*, *supra* note 2.

II. BACKGROUND

A. *What Is ESG Investing?*

While traditionally, investors primarily ignored nonfinancial reporting when making investment decisions, in today's social climate, investors are more frequently hedging their investment strategies using assessment criteria analyzing a company's environmental, social, and governance factors.⁵ The "environmental" factor is composed of a company's operations' long-lasting environmental impacts and what that company is doing to positively steward the natural world.⁶ These impacts may be direct or indirect greenhouse gas emissions or even the company's overall susceptibility to major physical climate risks and the impacts of climate change, including resiliency in the face of potential flooding and fires.⁷ The "social" aspect focuses on the company's management, including its treatment of human resources and its relationship to the community in which it operates.⁸ Examples include evaluating whether the company offers fair wages to its employees, which can extend to its supply chain partners—especially relevant for suppliers operating in lesser-developed economies with lax labor standards compared to the United States.⁹ Last but not least, the "governance" prong is related to the governing structure of the company, including the makeup and diversity of its leadership, its compensation structures, overall internal and external transparency, and the

5. See Pete Michaels & Alyssa Scruggs, *The Rise of Shareholder Activism and Litigation Related to Environmental, Social, and Governance Investing*, A.B.A. SEC. LITIG., Spring 2021, at 18. Broadly, there are three classifications of ESG funds: "exclusionary funds, which select categories of companies to exclude; single-theme funds, which select companies that fit or support a general theme; and best-in-class funds, which include companies that are the best in their industries for specified ESG criteria." *Id.*

6. David McSweeney & Lisa Shelton, *Corporate Financial Disclosures and Environmental, Social, and Governance Concerns: Evolving Issues*, NAT. RES. & ENV'T, Summer 2020, at 23.

7. Kyle Peterdy, *ESG (Environmental, Social, & Governance)*, CORP. FIN. INST., <https://corporatefinanceinstitute.com/resources/esg/esg-environmental-social-governance/> [https://perma.cc/4WDN-MGZF] (last visited Mar. 4, 2024).

8. *Id.*

9. *Id.* Additional concerns within the social prong of ESG have been exacerbated in the wake of Russia's invasion of Ukraine in February 2022. See Carla Nunes & Marianna Todorova, *Global Developments in ESG Disclosures May Have a Significant Impact on U.S. Companies*, KROLL (Mar. 9, 2023), <https://www.kroll.com/en/insights/publications/valuation/valuation-insights-first-quarter-2023/global-developments-in-esg-disclosures> [https://perma.cc/RJN6-6NSX].

quality of shareholder rights.¹⁰ This element is often assessed by analyzing a company's leadership's alignment with stakeholder expectations and its internal accountability structures.¹¹

This foundational trio has become pivotal in many institutional investors' investment strategies and can be assessed using ESG scores, which are issued by a growing number of ESG-rating agencies.¹² Unsurprisingly, over time, the array of ESG-focused investment vehicles has increased in popularity and availability, including green bonds,¹³ mutual funds, exchange-traded funds (ETFs), and index funds.¹⁴ It is now widely accepted that focusing on increasing initiatives that positively impact an ESG assessment can put a company in a better position to identify risks for disasters preemptively and, therefore, implement proactive and scalable solutions.¹⁵

B. *Historically Speaking and the Evolution into the ESG We Know Today*

These social responsibility factors, now recognized globally by the acronym ESG, are not novel concepts in the corporate world, but rather have morphed through the years to grow into the solid trio we see today. Environmentally—and socially—responsible factors evolved together from what was first termed Environmental, Health, and Safety (EHS) standards, then rebranded as the “Corporate Sustainability” movement in the 1990s, which further evolved into the Corporate Social

10. *What Is the “G” in ESG?*, S&P GLOB. (Feb. 24, 2020), <https://www.spglobal.com/en/research-insights/articles/what-is-the-g-in-esg> [<https://perma.cc/V2M4-6RCS>].

11. Peterdy, *supra* note 7. As ESG factors for publicly traded companies are more heavily scrutinized and companies are confronted with external inquiries and performance demands, ESG concerns rise to the forefront of stakeholder outreach and advocacy regarding internal policies, procedures, and management systems. McSweeney & Shelton, *supra* note 6.

12. Peterdy, *supra* note 7.

13. Green bonds (of which the first was issued in 2007 by the European Investment Bank for more than \$800 million) are used to invest in projects that further positive environmental initiatives or provide climate benefits. *Explaining Green Bonds*, CLIMATE BONDS INITIATIVE, <https://www.climatebonds.net/market/explaining-green-bonds> [<https://perma.cc/5KQU-G7DU>] (last visited Mar. 19, 2023). By December 2020, more than one trillion dollars had been issued in green bonds cumulatively. *Id.*

14. Peterdy, *supra* note 7.

15. Amy Lin Meyerson, *From Disruption to Environmental, Social, and Governance (ESG) Achievements and Sustainable Growth*, CT LAW., May/June 2021, at 4 (containing an address from Amy Lin Meyerson, the 2020–2021 President of the Connecticut Bar Association (CBA) explaining the CBA's commitment to ESG factors in operations and future decision-making).

Responsibility (CSR) revolution of the early 2000s, before finally emerging as ESG in the late 2010s and into the present day.¹⁶

Traditionally, investors viewed companies' efforts to engage in positive social responsibility efforts with a highly critical lens because they believed the initiatives were "risks that would eat into profits" and provided little to no economic benefit.¹⁷ Further, some investors thought that "the 'consideration of ESG by pension funds and other financial institutions and intermediaries in investment decisions was unlawful or a breach of fiduciary duties.'"¹⁸ These old-school investors were known to argue that companies' only motive for ESG-focused reporting was to purposefully convey false impressions of social consciousness by fabricating positive environmental and social responsibility endeavors and making grand promises that they never intended to fulfill—all to enhance their reputations as good community citizens.¹⁹ However, this pessimistic outlook seems to mostly be a thing of the (not-so-distant) past—though amid recent disruptions and uncertainty in the financial industry, some research has shown that investors are again "more s[k]eptical and pessimistic about environmental, social, and governance (ESG) investing than they were a year ago."²⁰

ESG, as a term, was first used in 2004 by the United Nations (UN) to develop guidelines to integrate environmental, social, and governance concerns into the financial reporting sphere.²¹ In 2006,

16. Peterdy, *supra* note 7. In the '90s, corporate social responsibility was also propelled to the forefront via the "Triple Bottom Line" concept that proposed a framework of three distinct prongs to measure corporate success: people, planet, and profit. *See History of ESG*, PREQIN, <https://www.preqin.com/preqin-academy/lesson-5-esg/history-of-esg> [http://perma.cc/Y34U-J8XT] (last visited Mar. 19, 2023).

17. *See* Meyerson, *supra* note 15.

18. *Id.*

19. *See id.*

20. Jean-Baptiste Andrieux, *Investors More Pessimistic About ESG Investing than a Year Ago*, MONEY MKTG. (Oct. 18, 2022), <https://www.moneymarketing.co.uk/news/investors-more-pessimistic-about-esg-investing-than-a-year-ago/> [https://perma.cc/65GL-R3WZ]; *see also* Saijel Kishan, *ESG Funds Seen Underperforming Broader Market in 2023: Survey*, BLOOMBERG (Nov. 10, 2022, 9:00 AM), <https://www.bloomberg.com/news/articles/2022-11-10/esg-funds-seen-underperforming-broader-market-in-2023-survey> [https://perma.cc/68DF-AZFU]. Regardless, the Biden administration has made it clear that addressing climate change and equality issues continues to be among the nation's top priorities. Meyerson, *supra* note 15.

21. *See* R. Krishnamoorthy, *Environmental, Social, and Governance (ESG) Investing: Doing Good to Do Well*, OPEN J. SOC. SCIS., July 2021, at 189, 191. At the time, it was mostly voluntary for organizations to report or market what we now call ESG initiatives, and it was primarily regarded as an effort to "do good to be seen as good" rather than as a rigorous legislative movement or to avoid financial consequence or enforcement. *Id.* at 191. In conjunction with this laissez-faire ESG attitude, ESG reporting remained largely a secondary focus and not seen as a financial benefit. *Id.* at 190–91.

the UN integrated ESG criteria into their Principles for Responsible Investment (PRI) Report, and required that it be incorporated into the financial evaluation of all companies.²² At the time it was incorporated, there were only sixty-three investment companies (with assets totaling \$6.5 trillion) who signed on to the proposition and agreed to incorporate ESG evaluations in their reporting structures.²³ In 2017, a global survey of 475 institutions, reported by Business Wire, found that 68% of respondents indicated that incorporating ESG reporting and emphasis in their business models actually improved their returns.²⁴ Additionally, 77% reported that they invested in ESG strategies because of the positive impact they had on companies' financial performance.²⁵ And, by 2018, the world saw a dramatic increase in ESG investment vehicle types, totaling an astonishing \$18 trillion in assets.²⁶

However, a frustrating lack of guidance and standardization has created inconsistency with the assessment and transparency of ESG reporting for financial and nonfinancial indicators.²⁷ Until recently, companies based most of what they included in their ESG disclosures on Supreme Court precedent set in *TSC Industries, Inc. v. Northway, Inc.*, which was later reaffirmed in *Basic Inc. v. Levinson*, or even broader, in various voluntary sustainability report frameworks.²⁸ The “materiality” principle for disclosure derived from *Basic Inc.* (adopted for public reporting requirements) established that any relevant fact could be considered “material” to a company’s disclosure depending on the significance a reasonable investor would place on the information.²⁹ The widely debated issue of what *actually* constitutes a material financial risk has been vastly influenced by the far-reaching effects and

22. Betsy Atkins, *Demystifying ESG: Its History & Current Status*, FORBES (June 8, 2020, 4:49 PM) <https://www.forbes.com/sites/betsyatkins/2020/06/08/demystifying-esgits-history--current-status/?sh=4b3935852cdd> [<https://perma.cc/3APF-27D5>].

23. *Id.*

24. *Id.* Defiantly, in May 2017, ExxonMobil shareholders thwarted company management and passed a vote to require the world’s largest oil and gas company to provide ESG disclosures in the form of a report on the impacts climate change has on its business, in the wake of the Paris Climate Agreement. *Id.*

25. *Id.*

26. Krishnamoorthy, *supra* note 21, at 192.

27. Javier El-Hage, Note, *Fixing ESG: Are Mandatory ESG Disclosures the Solution to Misleading ESG Ratings?*, 26 FORDHAM J. CORP. & FIN. L. 359, 364–65, 381 (2021).

28. *Proposed SEC Climate Disclosure Rule*, *supra* note 2. See generally *Basic Inc. v. Levinson*, 485 U.S. 224 (1988).

29. *Basic Inc.*, 485 U.S. at 224, 239–40, 250 (holding that materiality in a merger context depends on the probability that the transaction will be consummated and its significance to the issuer of the securities, and therefore must be determined on a case-by-case basis).

economic downfall of the global pandemic.³⁰ ESG management, in particular, has come under fire, with the pandemic highlighting how global recovery actions taken by companies should be in alignment with whatever ESG principles they purport to have in place.³¹

C. *Why Do ESG Disclosures Matter?*

As ESG and corporate responsibility reports and initiatives have seen massive gains in popularity, they have simultaneously prompted worldwide scrutiny. Even without government mandates, ESG reporting is trending towards the norm with 90% of S&P 500 firms publishing sustainability reports in 2019.³² PricewaterhouseCoopers (PwC) predicted that at least 60% of *all* mutual fund assets will be ESG-centered funds by 2025.³³ Additionally, PwC is predicting ESG-focused investments in the realm of nearly \$34 *trillion* by 2026, nearly doubling from the \$18.4 trillion reported in 2021.³⁴

In addition to governmental pressure, the increased attention ordinary consumers are paying to ESG factors seems to be one of the leading influences pushing companies to consider their ESG implications.³⁵ With Millennials and Gen Z consumers highly valuing ESG-focused initiatives, their combined 55% representation in today's workforce is a driving factor in companies' efforts to utilize ESG in attracting, engaging, and retaining employees.³⁶ CEO of investment giant BlackRock, Larry Fink, notes that the company is focused on increasing its integration of ESG factors in investment decisions and believes that "[a] company's ability to manage environmental, social and

30. See El-Hage, *supra* note 27, at 386–88.

31. See Marc S. Gerber et al., *The New Normal: ESG Drivers and the COVID-19 Catalyst*, SKADDEN (Nov. 12, 2020), <https://www.skadden.com/insights/publications/2020/11/the-new-normal> [<https://perma.cc/XQK4-WJ5T>].

32. Elsa Allman & Joonsung (Francis) Won, *Can ESG Disclosure Improve Investment Efficiency?*, WORLD BANK: WORLD BANK BLOGS (Sept. 20, 2021), <https://blogs.worldbank.org/allaboutfinance/can-esg-disclosure-improve-investment-efficiency> [<https://perma.cc/ES6V-QU3F>]. This figure demonstrates a dramatic increase in reporting, as only 20% of these same firms published sustainability reports in 2011. *Id.*

33. Meyerson, *supra* note 15, at 4.

34. Ryan Stanton, *ESG-Focused Institutional Investment Seen Soaring 84% to US \$33.9 Trillion in 2026, Making Up 21.5% of Assets Under Management: PwC Report*, PRICEWATERHOUSECOOPERS (Oct. 10, 2022), <https://www.pwc.com/gx/en/news-room/press-releases/2022/awm-revolution-2022-report.html> [<https://perma.cc/K432-MJ5M>].

35. See Krishnamoorthy, *supra* note 21, at 192 (explaining that “the rise of millennials who were far more civic and environmentally conscious and the rise of women in the workforce helped propel social causes within organizations and markets”).

36. Atkins, *supra* note 22.

governance matters demonstrates the leadership and good governance that is so essential to sustainable growth.”³⁷

Aside from the consumer-driven aspect, well-defined ESG initiatives can positively enhance business performance.³⁸ There is a large body of research that has found that companies paying attention to ESG factors and integrating ESG-focused initiatives realize higher equity returns and reduce downside risk by lowering loan and credit default swap spread and receiving higher credit ratings.³⁹ Focusing on ESG transparency and strategy can facilitate top-line growth, reduce costs, minimize regulatory and legal interventions, increase employee productivity, and optimize investment and capital expenditures.⁴⁰ In that way, facilitating robust and inclusive ESG policies can be an effective way to prop up a company's competitive edge.⁴¹

D. A Rundown of the Proposed Rules and How They Apply

As early as March 2021, the SEC anticipated widespread need for oversight in the ESG arena and announced the creation of a new Climate and ESG Enforcement Task Force.⁴² The following March, the SEC proposed the “Issuer Rule,” which included amendments requiring “public companies to provide certain climate-related financial data, and greenhouse gas emissions

37. *Id.* In a letter, Fink drew a hard line and committed to only invest BlackRock dollars in firms with a “vital social purpose and those deliberately endeavoring to create social impact and value-creation.” Krishnamoorthy, *supra* note 21, at 192. Congruently, the corporate business roundtable adopted stakeholder value principles as the main reason for any organization's existence and a total of 181 CEOs endorsed the idea that organizations, as part of a broader ecosystem, adopt stakeholder approaches that will allow for win-wins for any stakeholders within and outside the organizations circle. *Id.* In December of 2018, Citibank also vowed to include human rights mitigation requirements when making financing decisions. Sarah Fortt et. al., *ESG Matters: Texas-Size Challenges in Managing Supply Chains*, TEX. BAR J. 852, 852 (2019).

38. See Witold Henisz et al., *Five Ways that ESG Creates Value*, MCKINSEY Q. (Nov. 14, 2019), <https://www.mckinsey.com/capabilities/strategy-and-corporate-finance/our-insights/five-ways-that-esg-creates-value#/> [<https://perma.cc/Q26G-JNJU>].

39. *Id.*

40. *Id.* Due to the “heightened social, governmental, and consumer attention on the broader impact of corporations, as well as by the investors and executives . . . [t]he magnitude of investment flow suggests that ESG is much more than a fad or a feel-good exercise.” *Id.*

41. Betsy Atkins, *Strong ESG Practices Can Benefit Companies and Investors: Here's How*, NASDAQ (June 5, 2018, 8:01 AM), <https://www.nasdaq.com/articles/strong-esg-practices-can-benefit-companies-and-investors-2019-03-13> [<https://perma.cc/V94F-FJ92>].

42. Roger E. Barton, *The Greenwashing Wave Hits Securities Litigation*, REUTERS (Sept. 22, 2022, 10:42 AM), <https://www.reuters.com/legal/legalindustry/greenwashing-wave-hits-securities-litigation-2022-09-22/> [<https://perma.cc/3W3S-RADX>].

insights, in public disclosure filings.”⁴³ This rule would mandate that companies disclose Scope 1, 2, & 3 emissions which are not only the emissions that they are directly responsible for, but also emissions from companies in their supply chain, and emissions from the use of their products.⁴⁴

For reference, Scope 1 emissions are defined as any “direct greenhouse gas emissions that occur from sources that a company owns or controls,” which include “emissions from manufacturing activities and vehicles.”⁴⁵ Scope 2 emissions go on to encompass “indirect greenhouse gas emissions that occur from the generation of energy a company buys and consumes in its operations.”⁴⁶ And, even more expansively, Scope 3 emissions are inclusive of emissions that are “the result of assets . . . by a company that the company indirectly impacts in its value chain.”⁴⁷ These companies can be upstream or downstream from the target company, and can include “purchased goods and services, waste generation, business travel, downstream transportation, distribution and use of products sold, and the end-of-life treatment of products sold.”⁴⁸

In May of 2022, the SEC subsequently proposed the “Investor Rule,” requiring that “ESG-focused funds and firms disclose more specifics about their ESG strategies in materials [including] fund prospectuses and annual reports.”⁴⁹ These proposals will impact registered investment companies, business development companies (referred to collectively as “funds”), and registered

43. *Proposed SEC Climate Disclosure Rule*, *supra* note 2.

44. Gina N. Falaschi, *SEC’s Proposed ESG Rule: Key Takeaways for Public and Private Companies*, PITT. BUS. TIMES (Dec. 1, 2022), <https://www.bizjournals.com/pittsburgh/news/2022/12/01/key-takeaways-about-sec-proposed-esg-rule.html> [<https://perma.cc/C92G-SNQ8>]. These different “scopes” can include direct emissions from the manufacturing and production of products, but also any emissions that are secondary in the process—such as energy consumed by admin in offices—and further expand to include anyone in the company value chain—suppliers’ emissions for any material that is outsourced, transportation of the products, consumer emissions when using the products, and beyond. *See id.*

45. *Id.*

46. *Id.*

47. *Id.* Scope 3 emissions, in particular, are shrouded with uncertainty. They require extensive assumptions about often unpredictable human behavior and numerous other estimations to report a final number. *Id.* They are also problematic because if there are companies in the same value chain reporting all the emissions in that value chain, and then reporting their numbers to each other, the same emissions can be counted multiple times. *See id.*

48. *Id.* Scope 3 emission requirements are proposed to be included only if the target company considers them “material.” *Id.*

49. *Proposed SEC Climate Disclosure Rule*, *supra* note 2.

investment advisers.⁵⁰ The degree of disclosures prompted by the rules will hinge upon the degree to which ESG factors are determined to be core to the fund's strategy.⁵¹ The funds that have more closely aligned themselves with ESG factors and purport to be "sustainable" will have heightened disclosure requirements, ostensibly to substantiate their commitment to those ESG principles and give investors a better understanding of their associated investment risks.⁵²

Before these proposed rules, the SEC had not required extensive, line-item disclosures of ESG-related matters, and these rules would expand far beyond the materiality standard discussed by *Basic Inc.*⁵³ The new standard being proposed would order public companies to expressly disclose any "climate-related risks totaling 1% or higher of a total line item in [their] relevant financial statements."⁵⁴

According to the SEC, the rules are "designed to provide consistent standards [surrounding] ESG disclosures, allowing investors to make more informed decisions."⁵⁵ The rules would require "additional specific disclosure[s] . . . regarding ESG strategies in fund prospectuses, annual reports, and adviser brochures."⁵⁶ Additionally, they would "implement a layered, tabular disclosure approach for ESG funds to allow investors to compare ESG funds at a glance; and [require] certain environmentally focused funds to disclose the greenhouse gas (GHG) emissions associated with their portfolio investments."⁵⁷ Some funds would need to provide further specifics regarding their strategies, including any environmental or social impacts they seek to achieve through their ESG initiatives and the metrics with which they measure their progress in realizing those impacts.⁵⁸

50. Maia Gez et al., *SEC Proposes Amendments to Rules to Regulate ESG Disclosures for Investment Advisers and Investment Companies*, WHITE & CASE (June 13, 2022), <https://www.whitecase.com/insight-alert/sec-proposes-amendments-rules-regulate-esg-disclosures-investment-advisers-investment> [<https://perma.cc/786P-DGAU>].

51. *Id.*

52. *See id.*

53. *Proposed SEC Climate Disclosure Rule*, *supra* note 2; *Basic Inc. v. Levinson*, 485 U.S. 224, 239–40 (1988).

54. *Proposed SEC Climate Disclosure Rule*, *supra* note 2.

55. *ESG Disclosures for Investment Advisers and Investment Companies Fact Sheet*, SEC 1, <https://www.sec.gov/files/ia-6034-fact-sheet.pdf> [<https://perma.cc/MN5A-W7GV>] (last visited Mar. 31, 2024). The SEC emphasizes the inconsistency in companies' interpretations of ESG factors in the past and highlights the problems related to significant differences in how companies report the ESG data, criteria, and strategies, including the possibility for a fund to greatly exaggerate its commitment and consideration of ESG factors. *Id.*

56. *Id.*

57. *Id.*

58. *Id.*

The rules will apply differently based upon whether and which ESG fund-type applies to each fund's investment decision.⁵⁹ An Integration Fund will be categorized as “[a] fund that considers one or more ESG factors along with other, non-ESG factors in investment decisions where those ESG factors are generally no more significant than other factors in the investment selection process.”⁶⁰ An ESG-Focused Fund will be “[a] fund that focuses on one or more ESG factors by using them as a significant or main consideration 1) in selecting investments or 2) in its engagement strategy with the companies in which it invests.”⁶¹ According to the SEC, it “will explicitly consider a fund's name and sales literature as possible indicators that the fund's investment decisions incorporate ESG factors as a significant or main consideration.”⁶² And then, an ESG Impact Fund will be categorized as “a subset of ESG-Focused Funds,” and defined as “a fund that seeks to achieve a specific ESG impact or impacts.”⁶³

III. IMPACTS AND IMPLICATIONS

A. *The Bid to Improve Transparency Through Standardization*

Some advocates argue that previous attempts to integrate sustainability into nonfinancial filings have proved inadequate in improving transparency.⁶⁴ To that end, consistent, reliable, and easily comparable disclosures of ESG-related risks and opportunities are necessary so investors are getting sufficient information to make informed investment decisions.⁶⁵ Indeed, companies that have already voluntarily included ESG-related disclosures in their external communications have distinguished themselves not only through more favorable financial performance but also by elevating their reputations amongst socially conscious

59. Kevin J. Harnisch et al., *U.S. SEC Proposes New ESG Disclosure Rules for Funds and Advisers*, NORTON ROSE FULBRIGHT (June 2022), <https://www.nortonrosefulbright.com/en/knowledge/publications/915ef285/us-sec-proposes-new-esg-disclosure-rules-for-funds-and-advisers> [<https://perma.cc/W7E9-L4TB>]. These fund types can be determined by firms conducting confidential internal reviews of their own ESG metric incorporation into relevant investment strategies in combination with the presentation of those ESG strategies within their marketing materials. *Id.*

60. *Id.*

61. *Id.* Any indications that a fund may fall within the ESG-Focused or ESG Impact Fund categories may require greater resources internally to better handle the significant increase in disclosure requirements proposed in the new rules. *Id.*

62. *Id.*

63. *Id.*

64. McSweeney & Shelton, *supra* note 6, at 26.

65. *Id.*

consumers and investors.⁶⁶ However, the lack of consistency in U.S. reporting on ESG-related practices may cause confusion and muddy the investing waters, disincentivizing global investment in U.S. companies. In general, American companies have been falling seriously behind their European and Asian counterparts when assessing the quality and consistency of ESG and sustainability reporting, with sixteen of the bottom twenty-five worst-ranked ESG-reporting companies headquartered in the United States.⁶⁷

Investors are not simply more inclined to provide investments to funds and companies that are reporting positive indices related to ESG, some are also demanding it. In the fall of 2018, investors controlling and managing nearly \$5 trillion in assets petitioned the SEC to mandate standardized sustainability disclosures for public companies.⁶⁸ And, in 2020, BlackRock identified 244 portfolio companies—one of which being ExxonMobil—had made insufficient progress in incorporating climate-related risks into business models and disclosures; Blackrock turned down investing in fifty-three of those companies.⁶⁹

B. *Investment Efficiency and Internalizing Externalities*

Firms often change their investment behaviors because financial reporting can “reduc[e] information asymmetries and agency costs, improv[e] external monitoring, and reduc[e] inefficiencies in managerial decisions.”⁷⁰ However, given the historical reporting limitations, it was difficult for investors to understand exactly how funds account for and quantify ESG factors in investment decisions, and the impacts their investments can have on the issues they are claiming to address.⁷¹

66. *See id.*

67. Elsa Allman & Joonsung Won, *The Effect of ESG Disclosure on Corporate Investment Efficiency*, EUROFIDAI-ESSEC PARIS DEC. FIN. MEETING 2021, Oct. 2022, at 9–12., <https://ssrn.com/abstract=3816592> [<https://perma.cc/65FJ-NLSL>].

68. Cydney Posner, *Heat's On for Climate Change Disclosure Rules*, COOLEY PUBCO (Oct. 4, 2018), <https://cooleypubco.com/2018/10/04/climate-change-disclosure-petition/> [<https://perma.cc/Q2LJ-K2EZ>].

69. Declan Harty, *BlackRock Voted Against Management at 53 Companies over Climate Concerns*, S&P GLOB. MKT. INTEL. (July 14, 2020), <https://www.spglobal.com/marketingintelligence/en/news-insights/latest-news-headlines/blackrock-voted-against-management-at-53-companies-over-climate-concerns-59426142> [<https://perma.cc/YX5D-PXH7>].

70. Allman & Won, *supra* note 32.

71. Sara Dewey, *The SEC's Proposed ESG Rules Aim to Provide Better Information to Investors*, ENV'T & ENERGY L. PROGRAM (July 7, 2022), <https://eelp.law.harvard.edu/2022/07/the-secs-proposed-esg-rules-aim-to-provide-better-information-to-investors/> [<https://perma.cc/S784-66RJ>].

Opponents argue that mandatory ESG disclosures may generate negative externalities.⁷² However, better-quality standards relating to ESG disclosures may lead to tangible capital market benefits.⁷³

Mandated ESG disclosures have been associated with increases in firm value in China, Denmark, Malaysia, and South Africa.⁷⁴ These mandates not only naturally increase the availability and quality of ESG reporting models, they also have had beneficial effects on firms' abilities to forecast earnings and practice proactive mitigation of negative ESG-related incidents.⁷⁵ Studies have also found links between mandatory disclosure and higher earnings quality and lower likelihood of stock price crashes.⁷⁶ Outside of mandatory reporting, voluntary disclosure may even facilitate the procurement of better financing conditions for firms by attracting dedicated institutional investors.⁷⁷ Studies have shown that nonfinancial reporting (i.e., ESG disclosures and sustainability reporting) does play a key role in improving investment efficiency, creating significant positive benefits for the economy.⁷⁸

C. *Practical Challenges with Application*

Notwithstanding the benefits that go hand-in-hand with increased ESG awareness and attention, in the current state of reporting ambiguity, the more specific details and calculations of a company's ESG score or rating are difficult to explain, pinpoint, or compare even amongst the same or similarly situated

72. See Allman & Won, *supra* note 67, at 15. Examples include firms already disclosing ESG information and being penalized for differentiating themselves from their competitors, which will result in necessarily higher costs and a reduction in shareholder value. See *id.*

73. *Id.* at 10–12. Benefits can include improved liquidity, lower cost of capital, higher asset prices, and more informed corporate decisions. *Id.* at 12.

74. Ioannis Ioannou & George Serafeim, *The Consequences of Mandatory Corporate Sustainability Reporting* 8, 30 (Harv. Bus. Sch. Rsch., Working Paper No. 11-100, 2017), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1799589# [<https://perma.cc/QZM6-SYN2>]. These increases in firm value arise because investors and others in capital markets have naturally increased the importance of sustainability reporting by de facto integration of ESG performance into their standard evaluation models, creating more available dollars for companies with mandated, standardized ESG reports. See *id.* at 7.

75. See Allman & Won, *supra* note 67, at 5, 12, 14–15.

76. *Id.* at 12 (arguing that “equity markets perceive that disclosure regulation of nonfinancial information will lead to net costs for firms with weak ESG performance, and benefits for those with a strong performance”).

77. *Id.*

78. *Id.*

industries. There remain significant variances in definition and “measuring” with some ESG-scoring agencies grouping as many as thirty-seven different “key ESG issues” into their respective categories; some incorporating the Ten Principles of the UN Global Compact as guideposts to measure “twenty-eight [unique] ESG issues and forty-five ‘hot topics’”; and one scoring agency incorporating more than 380 different factors into each assessment.⁷⁹ These inconsistencies illustrate a larger problem: a broadly encompassing term like “ESG” may mean different things to different people or industries. This tension may not be easily resolved by a government-mandated set of disclosures.⁸⁰

1. *Compliance and Reporting Hurdles.* As noted, quantifying ESG can be difficult and time-consuming, considering the vast array of information that is encompassed by the ESG factors.⁸¹ As companies face higher degrees of regulatory scrutiny amid heightened awareness of the threat of greenwashing claims, organizations have run into challenges in the compliance arena.⁸²

Even though the proposed rules will attempt to “standardize” data sets and level the ESG playing field, the historically piecemeal approaches to compliance that many companies have employed may be ineffective and inefficient, and will require those companies to jump hurdles to meet new requirements.⁸³ These companies will have to overcome barriers in the form of fragmented approaches and limited perspective, weak corporate governance structures, relative regulatory inexperience, pervasive data shortfalls, and technological limitations.⁸⁴

79. El-Hage, *supra* note 27, at 363–65.

80. For a more in-depth look at some of these tensions, see *infra* Section III.E.

81. Krishnamoorthy, *supra* note 21, at 193–94. It is difficult to estimate the wide range of factors, but due to its broad range, ESG could require specific measurement standards for things as different as air pollution, gender diversity, and executive compensation structures. *Id.* Even today, the four major ESG-rating companies that dominate the market—MSCI ESG, Sustainalytics, RepRisk, and ISS—have widely fluctuating methodologies and assessment methods with unique scoring criteria that are often at odds with each other. El-Hage, *supra* note 27, at 363–64.

82. Lorenzo Fantini et al., *ESG Compliance in an Era of Tighter Regulation*, BCG (Sept. 20, 2022), <https://www.bcg.com/publications/2022/navigating-esg-compliance-in-an-era-of-tighter-regulation> [<https://perma.cc/BDE6-VFXK>].

83. *Id.* In many companies, the tracking of ESG factors is assigned to various departments individually, where sustainability may track environmental issues and procurement and human resources may track internal governance issues. *Id.* However, this approach has not been wholly effective at shielding companies from penalties or from facing negative public backlash. *Id.*

84. *Id.*

Due to the historical uncertainty and inconsistency, it may be hard for companies to overcome these reporting obstacles in time to be found compliant with the sweeping changes proposed by the rules.⁸⁵ Further, many of the companies that will be directly or indirectly implicated by the proposed rules are not currently under the same degree of regulatory scrutiny, so they have limited experience and resources to deal with the emerging and intricate regulations.⁸⁶

In addition to companies' lack of experience in participating in any kind of standard ESG reporting—and even with government-mandated disclosures—concepts like “sustainability” are inherently hard to quantify.⁸⁷ This may create trouble for businesses looking to showcase their efforts to globally integrate ESG gains and impacts in their day-to-day business structure.⁸⁸ All of these challenges will likely result in unexpected cost increases and potentially even greater legal liability for unprepared companies.

2. *Unintended Consequences for Private Companies.* With increased national pressure on all companies—private and public—an emphasis on quality ESG reporting is likely inevitable regardless of their stock offerings. Though the rules are theoretically only applicable to publicly traded companies—to stay within the SEC's purview—by including required disclosure of Scope 3 emissions, the proposed rules are expected to have a significant impact on private companies that are in the “value chain” of larger public companies.⁸⁹ Given their power dynamic, larger, publicly traded companies will likely ask that private companies in their value chain be responsible for estimating their own greenhouse gas emissions, which will levy an additional burden on those smaller companies. This burden-shift will potentially create the need for an outside consultant to (as

85. See *id.* For example, many companies allow individual departments to deploy their own risk assessments, including unique ESG assessments, which makes for a difficult holistic approach and cohesive ESG strategy. *Id.*

86. *Id.*

87. Fabrizio Tocchini & Grazia Cafagna, *The 5 Biggest Hurdles to Effective ESG Reporting*, WOLTERS KLUWER (July 20, 2022), <https://www.wolterskluwer.com/en/expert-insights/the-5-biggest-hurdles-to-effective-esg-reporting#> [<https://perma.cc/EPT8-3UHX>].

88. *Id.* Businesses may also find it difficult to convey to investors how their sustainable activities have impacted their bottom lines. See *id.*

89. Sarah K. Williams, *ESG for Private Companies: How Regulations Will Trickle Down*, WIPFLI (Nov. 15, 2022), <https://www.wipfli.com/insights/articles/vflt-esg-for-private-companies-regulatory-trickle-down-effect> [<https://perma.cc/AJZ2-F532>]; Falaschi, *supra* note 44.

accurately as possible) assist with compiling the data and calculating final reportable figures.⁹⁰ With ESG disclosures becoming the new standard for evaluating companies, nonregulated private companies will be pressured to produce quality ESG disclosures—regardless of their desire to provide them voluntarily—to appear more attractive to customers and business partners, and continue being competitive in the market.⁹¹

Though the intended incentive for these rules is portrayed as boosting companies' sustainability and environmentally conscious practices, the breadth of the new required disclosures may end up actually discouraging companies from going public as they face increased barriers to entry into the publicly traded sphere.⁹² Though widespread ESG reporting will undoubtedly result in increased expenditures and hardship initially for private companies, these disclosures do have the potential to increase value in the private sector, similarly to publicly traded companies. If able to withstand the initial investment period, in the long term, private companies can still reap the benefit of providing complete, high-quality ESG disclosures.⁹³

D. Legal Implications and Challenges

1. *Greenwashing Litigation.* One of the stated goals of the proposed rules is the creation of transparent and standardized disclosure practices concerning ESG factors with an eye toward potentially preventing funds and investment advisers from “greenwashing” their investment decisions.⁹⁴ Greenwashing is the misrepresentation of a company, product, process, or investment fund as more environmentally friendly, socially responsible, or

90. Falaschi, *supra* note 44.

91. *Id.*

92. *Id.* These disclosures will likely also become material during mergers and acquisitions transactions and will require increased due diligence to account for potential risks that a merger or acquisition may have on its climate disclosures. *Id.*

93. Williams, *supra* note 89. Studies have shown that private companies providing strong ESG disclosures will benefit from employee attraction and retention, access to new funding sources and business partners, increased consumer bases, better financial performance, and enhanced enterprise value. *Id.*

94. Hester M. Peirce, *Statement of Environmental, Social, and Governance Disclosures for Investment Advisers and Investment Companies*, SEC (May 25, 2022), <https://www.sec.gov/news/statement/peirce-statement-esg-052522> [<https://perma.cc/V8GJ-8D2M>]. SEC Chairman Gary Gensler has stressed that greenwashing is a key concern—even going so far as to charge BNY Mellon Investment Advisor, Inc. for providing material misstatements and omissions concerning their ESG quality reviews. *Id.* Gensler has emphasized that the proposed rules will provide consistency for asset managers' ESG strategies, therefore preventing inadvertent greenwashing by increasing understanding of the baseline ESG disclosures required for each fund. *Id.*

sustainable than it actually is.⁹⁵ This concept has been extended further to apply to companies falsely touting ESG benefits while simultaneously refraining from disclosing any negative ESG-related consequences.⁹⁶ Engaging in these misleading statements or potential omissions can open up securities issuers to litigation liability and negatively impact investors.⁹⁷

On May 25, 2022, SEC Commissioner Hester Peirce explained that a key impetus for the agency's undertaking in this ESG-focused rulemaking is driven by a legitimate concern about the practice of greenwashing by investment advisers and investment companies.⁹⁸ Commissioner Peirce went on to say, "[t]his concern is real because advisers can mint money by calling their products and services 'green' without doing anything special to justify that label."⁹⁹

ESG investing has seen monumental growth in a relatively short time period, which has created an opportunity for new enforcement in the face of previously little oversight and inconsistent standards.¹⁰⁰ Critics have argued that it can "be difficult in most cases to plausibly allege a materially misleading misstatement or omission in a fund disclosure on the theory that a 'green' fund is not 'green enough.'"¹⁰¹ Going forward under the new standard, plaintiff-shareholders engaging in securities litigation would be required to allege and establish causation—that is, produce evidence that a drop in the fund's share price was caused by the alleged misstatement or omission in the fund's ESG disclosures.¹⁰²

However, the Commissioner voiced concern that while enforcement proceedings shed light on the problem, they also illuminate an already existing solution: currently, when advisors inaccurately characterize their ESG practices, rules and regulations that already apply can be enforced.¹⁰³ Peirce believes

95. Barton, *supra* note 42.

96. *Id.*

97. *Id.*

98. Peirce, *supra* note 94.

99. *Id.*

100. *SEC Targets Greenwashing and Other Misleading ESG Claims*, CHAPMAN (July 20, 2022), <https://www.chapman.com/publication-sec-targets-greenwashing-and-other-misleading-esg-claims> [<https://perma.cc/VD3E-8KDG>].

101. Amy D. Roy et al., *Litigation Risks Posed by "Greenwashing" Claims for ESG Funds*, HARV. L. SCH. F. CORP. GOVERNANCE (Apr. 25, 2022), <https://corpgov.law.harvard.edu/2022/04/25/litigation-risks-posed-by-greenwashing-claims-for-esg-funds/> [<https://perma.cc/QEM3-UD5M>].

102. *Id.*

103. Peirce, *supra* note 94.

that a new rule to address greenwashing uniquely, therefore, should not be a high priority.¹⁰⁴

Alternately, it seems that government-mandated disclosure standards may increase companies' liability in greenwashing litigation if significant steps are not taken to ensure all data is reported and presented correctly within the purview of the disclosure requirements.¹⁰⁵ With many companies already under fire for taking too many liberties in describing their "good citizenship," this presents a real and not insular problem. In a 2022 survey conducted by Harris Poll for Google Cloud, 72% of 1,491 executives surveyed in North America admitted to overstating their sustainability efforts (greenwashing) in the past.¹⁰⁶ With such strict and broad sweeping regulations proposed, community and shareholder activists may have an even bigger arsenal with which to bring greenwashing suits against companies engaging in substandard reporting, regardless of the materiality to the bottom line.

2. *Major Questions Doctrine Challenges to the SEC's Authority—West Virginia v. Environmental Protection Agency.*¹⁰⁷ Any final rule issued by the SEC on environmental disclosures will likely face legal challenges. Challengers could find support in the Supreme Court's recent decision in *West Virginia v. Environmental Protection Agency*.¹⁰⁸ Scholars maintain that "[t]he Court's opinion in *West Virginia v. EPA* may be instructive as to how courts could view the SEC's disclosure rules, particularly to the extent that such rules do not necessarily pertain to materially misleading statements or omissions."¹⁰⁹

In its June 30, 2022 ruling in *West Virginia*, the Supreme Court limited the EPA's power to regulate greenhouse gas emissions via

104. *Id.* Peirce goes on to acknowledge the impracticality issues from a regulatory perspective of trying to define ESG factors more fully and calls rule application "awkwardly ambiguous." *Id.*

105. Companies can face class action greenwashing lawsuits for marketing with seemingly innocuous phrases like "sustainability" and "environmental stewardship," as evidenced by lawsuits against Whole Foods and Burt's Bees Cosmetics for saying that their ingredients "come from nature," and even against KLM for a tagline touting "[b]e a hero, fly CO2 zero." Shawn Collins & Lisa M. Northrup, *The Legal Risks of Greenwashing Are Real*, BLOOMBERG L. (July 25, 2022, 3:00 AM), <https://news.bloomberglaw.com/environment-and-energy/the-legal-risks-of-greenwashing-are-real> [<https://perma.cc/WK9E-J7X8>].

106. *Id.* Nearly two-thirds of those same surveyed executives also questioned the authenticity behind their companies' sustainability initiatives. *CEOs Are Ready to Fund a Sustainable Transformation*, GOOGLE CLOUD 2, https://services.google.com/fh/files/misc/google_cloud_cxo_sustainability_survey_final.pdf [<https://perma.cc/NA36-FZAM>] (last visited Mar. 18, 2023).

107. *West Virginia v. Env't Prot. Agency*, 142 S. Ct. 2587, 2609–10 (2022).

108. *SEC Targets Greenwashing and Other Misleading ESG Claims*, *supra* note 100. See generally *West Virginia*, 142 S. Ct. 2587.

109. *SEC Targets Greenwashing and Other Misleading ESG Claims*, *supra* note 100.

the Clean Power Plan, when it held that Section 111(d) of the Clean Air Act (CAA) did *not* explicitly grant EPA the authority to devise a scheme setting carbon dioxide emission caps.¹¹⁰ The Court rests its analysis on the major questions doctrine and explains that “cases in which the ‘history and the breadth of the authority that [the agency] has asserted,’ and the ‘economic and political significance’ of that assertion,” require a different approach than usual, and must provide no hesitation that Congress meant to confer such vast authority.¹¹¹ The Court stresses that EPA’s actions prior to the promulgation of the Clean Power Plan were within Section 111 of the CAA because they were based on applications of schemes that would reduce pollution by regulating each source to operate more cleanly, instead of enacting an overarching “system” reducing pollution by shifting activity from dirty to clean sources.¹¹²

This decision could provide a legal basis for challenges to other administrative regulations with similar sweeping and significant economic and political impacts, including the SEC’s proposed ESG investment disclosure rules. As the Court held in *West Virginia*, the agency will be required to show “clear congressional authorization” to withstand a challenge to its authority to enact these broad disclosure requirements.¹¹³

The SEC has claimed statutory authority under the Securities Act of 1933 and the Securities Exchange Act of 1934.¹¹⁴ The relevant statutes grant authority to “compel disclosures that are ‘necessary or appropriate in the public interest or for the protection of investors.’”¹¹⁵ The SEC argues that the climate and ESG factor disclosures are within their purview because climate and ESG-related risks can produce financial consequences for investors considering large investment strategies in publicly traded companies.¹¹⁶ Further, the Commission points to “the Report on Climate-Related Financial Risk 2021 published by the

110. *West Virginia*, 142 S. Ct. at 2614–16.

111. *Id.* at 2608, 2614.

112. *Id.* at 2607, 2610.

113. *Id.* at 2614.

114. Taryn Zucker et al., *West Virginia v. EPA Casts a Shadow over SEC’s Proposed Climate-Related Disclosure Rule*, HARV. L. SCH. F. CORP. GOVERNANCE (Aug. 3, 2022), <https://corpgov.law.harvard.edu/2022/08/03/west-virginia-v-epa-casts-a-shadow-over-secs-proposed-climate-related-disclosure-rule/> [<https://perma.cc/E7WU-X556>]; Sec. Act of 1933 (1978); Sec. Exch. Act of 1934 (1978).

115. Zucker et al., *supra* note 114.

116. *Id.*

Financial Stability Oversight Council,” detailing the threats posed by climate-related risks at “firm and financial system levels.”¹¹⁷

Upon adoption, critics will likely use the major questions doctrine precedent to challenge the SEC’s statutory authority to regulate climate and ESG disclosures by mirroring the above reasoning used by the Court in *West Virginia*.¹¹⁸ In its defense, the SEC could argue that, under precedent set in *Chevron v. Natural Resources Defense Council*, it should be afforded deference in its interpretation of the language in the Securities Act and the Securities Exchange Act, and that its interpretation of the language is a rational and permissible construction of the statute.¹¹⁹ And, while the majority opinion in *West Virginia* does not mention *Chevron*, the dissent notes that it could have the potential to apply, unless it could be shown that Congress repeatedly and historically denied an agency the power in question, effectively “negating the agency’s claimed authority.”¹²⁰ This would mean that challengers would need to show a history of Congress denying the SEC authority to regulate in this realm.

Even considering the Court’s recent jurisprudence seemingly pointing to a pattern of decreased administrative authority and deference, the SEC’s claim of statutory authority is still murky at best. And, as detailed below, a significant portion of the public response seems to agree. With the Court coming closer and closer to fully overturning its decision and rationale in *Chevron*, this would spell disaster for anything the SEC does that the Court views as stepping on the toes of Congress’s legislative powers.

E. Public Response

Due to the arguably broad sweep of the SEC’s regulatory authority in the ESG arena and in consideration of the proposed rules’ potential implications for both private and publicly traded

117. *Id.*

118. Even before the *West Virginia* holding was released, debate existed as to whether the major questions doctrine could invalidate the SEC’s promulgation of these climate-related disclosure rules. Coy Garrison et al., *ESG Implications of Supreme Court’s Decision in West Virginia v. EPA*, STEPTOE (July 5, 2022), <https://www.steptoel.com/en/news-publications/esg-implications-of-supreme-courts-decision-in-west-virginia-v-epa.html> [https://perma.cc/HYX6-878T]. It has been noted that the SEC rests on a broad interpretation of its statutory authority to promulgate these rules, which may be undermined by the Court’s decision in *West Virginia*. *Id.*

119. *Chevron v. Nat’l Res. Def. Council*, 467 U.S. 837, 842–85 (1984) (“[I]f the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency’s answer is based on a permissible construction of the statute.”).

120. *West Virginia v. Env’t Prot. Agency*, 142 S. Ct. 2587, 2634–36 (2022) (Kagan, J., dissenting).

companies, the public response to the rule promulgation has been vast and varied.¹²¹ Of the 13,289 marketed and organization-sponsored form letters submitted in the public comment period, 83% express broad support for the proposed climate disclosure rules while only 17% are boldly opposed.¹²² However, of the 2,487 individualized submissions, the split was decidedly more contentious, with 54% expressing support and 42% in opposition.¹²³

1. *Positive Responses.* The array of organizations and individuals offering support for the proposed rules represents a diverse section of the population, including Democratic politicians, nongovernmental organizations, individual corporations, professional services organizations, and a range of academics.¹²⁴ Supporters highlighted the proposed rules' effects on environmental protection, informed investor decision-making, enablement of investors to protect themselves and their investments from climate-related risk, standardization of climate disclosures, increased transparency and accountability for companies, and better alignment with other international and foreign regulatory frameworks that already mandate and standardize ESG disclosures.¹²⁵ Notably, only about 3% of the submissions in support of the rules proactively argue that the rules do in fact fall within SEC's statutory authority.¹²⁶

121. The SEC received more than 15,000 comment submissions during the public comment period. Jacob H. Hupart et al., *What Public Comments on the SEC's Proposed Climate-Related Rules Reveal—and the Impact They May Have on the Proposed Rules*, MINTZ (July 20, 2022), <https://www.mintz.com/insights-center/viewpoints/2022-07-20-what-public-comments-secs-proposed-climate-related-rules> [https://perma.cc/M3F7-PBEV]. For comparison, during the public comment period for recent SEC-proposed rules designed to manage cybersecurity risk, only 144 comments were submitted. *Id.*

122. *Id.*

123. *Id.* Additionally, only 4% of the individualized letters did not express a position on the matter. *Id.* However, despite substantial public backlash, the SEC is unlikely to back down from this rule promulgation, to bring U.S. securities law in closer alignment with international law, but also with climate activism and the general corporate movement toward widespread ESG disclosure. Jim Tyson, *ESG Backlash Unlikely to Derail SEC Climate Risk Rule*, CFO DIVE (Oct. 17, 2022), <https://www.cfodive.com/news/esg-backlash-unlikely-derail-sec-climate-risk-rule-sustainability/634297/> [https://perma.cc/A3YV-RMBK].

124. Hupart et al., *supra* note 121. While the substantive arguments of these groups varied widely and focused on specialized areas (unsurprisingly, environmental organizations were mostly concerned with broad implications for the clean-energy transition and corporations were more apt to focus on the financial consequences and heavy burden of the rules), the groups did share some common and consistent threads. *Id.*

125. *Id.*

126. *Id.* This reluctance to pursue a statutory legal argument on behalf of the SEC seems to signal the upcoming difficulty the SEC is likely to face in any future challenges in court. *Id.*

The Center for American Progress (CAP), a policy institute, is among those expressing support for the proposed rules in their public comment.¹²⁷ CAP argues that these rules are urgently needed to expand basic ESG disclosure requirements to fulfill investment advisers' fiduciary duties.¹²⁸ CAP explicitly voices its support of the SEC's statutory authority, though it does not attempt to cite specific statutory language or rest on precedent, instead relying upon the Commission's consistency and practice "over many decades."¹²⁹ However, CAP goes one step further and suggests that to protect U.S. investors fully, the Commission should require *all* investment funds to follow the mandated direct and indirect GHG emission disclosure rules, instead of the current proposed scope that includes the three defined ESG-related fund groups.¹³⁰

Some states have publicly supported the proposed rules as well. A seven-state coalition of Attorneys General submitted a comment supporting the proposed ESG rules and urged the SEC to adopt them.¹³¹ This coalition argues that investors need consistency and reliability concerning ESG-based investment products and strategies and that these rules begin to provide that stability to investors.¹³² The letter also includes an acknowledgment that the wild growth in ESG Investment Funds,

127. Alexandra Thornton, *CAP's Comment on the SEC Proposed Rule on Disclosures by Certain Investment Advisers and Companies About ESG Investment Practices*, CTR. FOR AM. PROGRESS (Aug. 17, 2022), <https://www.americanprogress.org/article/caps-comment-on-the-sec-proposed-rule-on-disclosures-by-certain-investment-advisers-and-companies-about-esg-investment-practices/> [https://perma.cc/XMT6-VL64].

128. CAP, Comment Letter on Proposed Rule on Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices (Aug. 16, 2022), <https://www.sec.gov/comments/s7-17-22/s71722-20137284-307841.pdf> [https://perma.cc/9BQ8-QQR6]. This is in stark contrast to the historical attitudes discussed earlier that argued participation in ESG-focused activities and reporting to be a breach of that very same fiduciary duty. *See supra* note 18 and accompanying text.

129. CAP, Comment Letter, *supra* note 128. CAP goes on to specifically point out that there have been many promulgated rules that require disclosure of certain information about a fund's fundamental characteristics, and the Commission's attempts to standardize other types of disclosures, as well. *Id.*

130. *Id.*

131. N.Y. Off. of the Att'y Gen. et al., Comment Letter on Proposed Rule on Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, 1, 6–7 (Aug. 16, 2022), <https://www.sec.gov/comments/s7-17-22/s71722-20136434-307474.pdf> [https://perma.cc/E4R9-GF7D] (including signatures from: Letitia James, New York Attorney General, Rob Bonta, California Attorney General, Kathleen Jennings, Delaware Attorney General, Kwame Raoul, Illinois Attorney General, Brian E. Frosh, Maryland Attorney General, Keith Ellison, Minnesota Attorney General, and Matthew J. Platkin, New Jersey Acting Attorney General).

132. *Id.* at 1, 3.

in conjunction with the historical lack of consistent disclosure standards, has created the potential for fraud and demands enhanced disclosure metrics.¹³³

2. *Negative Responses.* Predictably, individualized letters opposing the proposed rules include Republican politicians, a large range of individual corporations, trade industry groups, and other nongovernmental organizations.¹³⁴ Interestingly, though again unsurprisingly, the common themes in the submissions criticizing the proposed rules included legal arguments that the rules are beyond the scope of the SEC's legal authority, that increased costs associated with remaining in compliance with the rules are both extensive and unreasonable, and that the rules are unnecessary because the science associated with climate change is unsettled and preliminary at best.¹³⁵

However, SEC Commissioner Hester Peirce is not sold on the efficacy of the rules in their proposed form and has acknowledged that the proposal touches on some questions raised by critics but embodies a fundamentally different approach.¹³⁶ The Commissioner is concerned that, while the proposal avoids explicitly defining what each environmental, social, and governance prong actually means, it still implicitly uses the disclosure requirements to induce substantive changes in funds' and advisers' ESG practices, creating confusion and uncertainty when the goal is to clarify expectations.¹³⁷ She further raises concerns that investors will pick up the tab for the latest fad "ESG exploits" without seeing much benefit given what she believes is this ongoing lack of clarity.¹³⁸

Large corporations have taken issue with the more stringent requirements and are naturally worried about the wide-sweeping range of the reporting requirements. In its public comment responding to the new rules, ExxonMobil recommends retaining the traditional *Basic Inc.* materiality threshold, eliminating the

133. *Id.* at 2–3.

134. Hupart et al., *supra* note 121. Industries that were well-represented in this group included fossil fuels and other extractive-based industries. *Id.*

135. *Id.* Notably, while very few of the submissions in support of the proposals appealed to the legal authority argument, about 31% of the critical submissions raised the concern that these rules fall outside of the SEC's scope of authority. *Id.*

136. Peirce, *supra* note 94.

137. *Id.*

138. *Id.* Commissioner Peirce goes on to say that she would have supported a proposal requiring less invasive questions about the ESG products and services, including asking what the label means with respect to each of those products or services, what is used to make the product that lines up with ESG factors, and what the cost of those ESG initiatives would be to potential investors. *Id.*

requirements that would include line-item disclosures, continuing to allow issuers to furnish climate-related information voluntarily, and proposes excluding Scope 3 GHG emissions from the overall requirements.¹³⁹ ExxonMobil goes on to express its concern with the enormous costs associated with providing information that it believes would fail to meet a reasonable materiality threshold and would be inconsistent because they would be based on significant degrees of technical estimations and numerous assumptions.¹⁴⁰ It also agrees that more useful and consistent standards are necessary to properly address indirect emissions under Scope 3, and, in response, it believes that the SEC should give industries more time to create the proper scientific and technical approaches necessary to more soundly measure these types of emissions.¹⁴¹

In a country facing intense polarization and an increased political divide, these proposed rules have many critics calling ESG mandates a form of “woke capitalism.”¹⁴² Former Vice President, Mike Pence said, “ESG is a pernicious strategy, because it allows the left to accomplish what it could never hope to achieve at the ballot box or through competition in the free market.”¹⁴³ Congruently, the rules have been heavily rejected by business lobbying groups and Republicans.¹⁴⁴ Twenty-four Attorneys General from Republican-controlled states wrote to the SEC and called the new proposals “an ill-advised misadventure into environmental regulation.”¹⁴⁵ As with the other critics of the new rules, these Attorneys General are concerned with potential increased compliance costs and argue that increased reporting will stall innovation in the ESG-investing sector.¹⁴⁶

139. ExxonMobil, Comment on the Proposed Rule for the Enhancement and Standardization of Climate-Related Disclosures for Investors, 3–4, 8 (June 17, 2022), <https://www.sec.gov/comments/s7-10-22/s71022.htm> [<https://perma.cc/CLB5-U8BG>].

140. *Id.* at 3, 8.

141. *Id.* at 4. Further, ExxonMobil has asked the SEC to expand safe harbor provisions in the Act, eliminate requirements that mandate updating reports that predate the effective date of the Proposal, and “[p]rovide significantly more time to implement necessary information gathering and reporting systems.” *Id.* It proposes an additional three-year compliance timeline before allowing reporting periods to be governed by any new disclosure requirements. *Id.*

142. Tyson, *supra* note 123.

143. *Id.*

144. Tim Quinson, *Corporate Backlash over SEC Climate Plan Takes Shape*, BLOOMBERG (July 13, 2022, 5:00 AM), <https://www.bloomberg.com/news/articles/2022-07-13/corporate-backlash-over-sec-climate-plan-takes-shape-green-insight> [<https://perma.cc/7G8Q-27MR>].

145. *Id.*

146. Dewey, *supra* note 71.

IV. CONCLUSION

Increased awareness and demand for the corporate world to engage in better social responsibility has prompted a corporate culture that is paying more attention to its environmental, social, and governing footprints and structures. With swift advances in technology that make it far easier for laypeople to search for information instantaneously, corporations around the world are trending toward providing consumers and investors with the ESG-related reports and disclosures they crave. However, with such a wide-encompassing array of factors and a lack of guidance, assessing companies' true social costs remains difficult.

These SEC-proposed rules that will increase reporting requirements have the potential to increase investment efficiencies, improve fund transparency, and standardize and clarify ESG standards across industries. Further, these rules will allow organizations an opportunity to be deliberate in the types of activities they choose to hold out as environmentally, socially, or governance friendly. However, this burgeoning landscape will not escape growing pains. Companies will need to clear hurdles to increase the financial and human resources dedicated to ensure compliance and accurate reporting of their activities, while navigating complex and novel regulatory strategies, which have never been imposed in the ESG-investment realm. The SEC, in turn, should provide the requisite leeway and time for these companies to meet the new standards.

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