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ESG Sustainability Spotlight

Q2 | 2024

Navigating the ESG Landscape: Risks, Opportunities, and Strategic Insights

In today's business world, environmental, social, and governance (ESG) issues have taken center stage, and companies, both public and private, are increasingly recognizing the significance of ESG responsibility. Today's executives, managers, and stakeholders find themselves navigating a complex landscape filled with risks and opportunities.

The ESG Imperative

ESG encompasses a broad spectrum of factors that impact a company's long-term sustainability and performance. Let's break down what each component entails:

- **Environmental (E)**: This dimension focuses on a company's impact on the environment. It includes considerations such as carbon emissions, resource usage, waste management, and climate change resilience.
- **Social (S)**: The social aspect encompasses how a company interacts with its employees, customers, communities, and other stakeholders, as well as the non-environmental impacts of its supply chain. Topics like diversity and inclusion, labor practices, human rights, and community engagement fall under this category.
- **Governance (G)**: Governance refers to the systems and processes that govern a company's decision-making. It involves board composition, executive compensation, transparency, and adherence to ethical standards.

The ESG Landscape Today

- **Heightened Focus:** Investors, regulators, and consumers are increasingly scrutinizing companies' ESG practices. Firms that prioritize ESG are better positioned to attract capital, retain talent, and build trust with stakeholders.
- **Regulatory Landscape:** In the U.S., federal regulators' loss of judicial deference may subject their evolving ESG-related regulations to increasing legal challenges. Despite the potential for uncertainty at the federal level, companies must stay informed about the additional state level and international requirements and restrictions to ensure compliance.
- **Shareholder Proposals:** Shareholders continue to push for greater ESG disclosure and action, with a particular focus on climate-related proposals. Crafting effective strategies to address these proposals is essential for companies seeking to align with investor expectations.
- **Political Dynamic:** As ESG has grown in prominence, it has also grown more controversial. It is not enough to know the rules where a company is located, companies need to know the rules everywhere they do business.

Alston & Bird's ESG Advisory Team

At Alston & Bird, our ESG Advisory Team provides strategic guidance to companies navigating the ESG landscape. Our services include:

- **Understanding ESG Dynamics:** We help companies grasp the nuances of ESG and tailor their approaches accordingly.
- **Regulatory Insights:** Our team stays abreast of ESG-related regulations worldwide, ensuring clients remain compliant.
- **Shareholder Engagement:** Crafting effective responses to shareholder proposals requires expertise. We guide companies in this critical area.
- **Risk Mitigation:** Minimizing litigation and enforcement risk is crucial. Our strategies and materials help companies proactively address potential legal challenges.

ESG Tracker and Sustainability Spotlight

Our ESG Tracker and this publication offer valuable insights into federal and state enforcement actions, litigation trends, and shareholder proposals. They serve as a resource for companies seeking to stay informed and make up-to-date decisions on all matters related to ESG.

Kevin Minoli, Elise Paeffgen, Cara Peterman, Dave Brown, Jason Outlaw

Environmental, Social & Governance (ESG) Team

JUNE

Lawmakers Encourage SEC to Finalize Greenwashing Rule

June 4, 2024 | Letter to Chair Gary Gensler

A number of lawmakers from both the House and Senate filed a letter on June 4, 2024 encouraging Securities and Exchange Commission (SEC) Chair Gary Gensler to ensure robust enforcement of existing SEC guidance on climate disclosure while the SEC's final climate risk disclosure rule is stayed. The letter notes that recent economic data suggests that climate change poses systemic risks to the national and global economy and argues that investors need access to reliable, standardized climate risk disclosures to fully evaluate the risks associated with their investments. The letter criticizes the SEC for adding a materiality qualifier to the final rule's emissions disclosures, which provides issuers with discretion to decide if their emission levels reach a materiality threshold and should be disclosed.

State Attorney General Actions

JUNE

Several State Attorneys General Defend Diversity, Equity, and Inclusion Initiatives Within Educational, Legal, Business Communities

June 20, 2024 | Letter to the American Bar Association, Fortune 100 CEOs, and Other Organizations Unfairly Targeted for Their Commitment to Diversity, Equity, and Inclusion.

Several state attorneys general drafted a comment letter addressing diversity, equity, and inclusion initiatives within legal and business communities. The letter from the attorneys general challenges attempts to correlate diversity measures with racial discrimination, among other things, and ultimately concludes by establishing the importance of diversity, equity, and inclusion programs and efforts in corporate, educational, legal, and philanthropic spaces. One key point the attorneys general make is that "companies with diverse leadership teams are associated with higher financial returns, and higher social and environmental impact scores." The letter follows a letter from a separate group of attorneys general challenging the American Bar Association's standards for approval of law schools after the Supreme Court's recent decisions on the constitutionality of considering race in higher education admissions.

MAY

Several State Attorneys General Oppose New Federal Rule on Environmental Standards for Infrastructure

May 21, 2024 | *State of Iowa v. Council on Environmental Quality*, No. 1:24-cv-00089 (D.N.D.).

Several state attorneys general filed suit against the White House Council on Environmental Quality (CEQ), challenging the CEQ's final rule implementing the National Environmental Policy Act (NEPA) that would require federal agencies to consider a variety of environmental and related factors—including climate change, environmental justice, and Indigenous Knowledge—when conducting environmental reviews under NEPA, among other things. The attorneys general contend that the proposed changes are arbitrary, without a valid federal statutory basis, and likely to result in uncertain and unpredictable outcomes. The attorneys general ultimately request, in relevant part, that the district court declare the final rule arbitrary and capricious, set aside the final rule, and enjoin the CEQ from implementing the final rule altogether.

APRIL

Several State Attorneys General Petition District Court to Defend EPA's Rule on Federal Greenhouse Gas Emissions Standards

April 23, 2024 | *Commonwealth of Kentucky v. U.S. Environmental Protection Agency*, No. 24-1087 (D.C. Cir.).

Several state attorneys general moved to intervene in a case brought by attorneys general from other states that challenges the U.S. Environmental Protection Agency's (EPA) final rule raising greenhouse gas emissions standards for light- and medium-duty vehicles (e.g., passenger cars, large pickup trucks, vans). The EPA's final rule would impose more stringent standards on greenhouse gas and other harmful pollutant emissions (e.g., nitrogen oxides, particulate matter) for light- and medium-duty vehicles with model years 2027 and later. The EPA estimates that, if implemented, its final rule would reduce greenhouse gas emissions by 7 billion metric tons through 2055.

The attorneys general seeking to intervene in the case argue that their right to intervene and defend the EPA's final rule is well established since harmful emissions that threaten public health and the environment would exacerbate the climate change and public health harms their states have already experienced. The attorneys general opposing the EPA's final rule did not oppose the motion to intervene in this case.

In a separate case, several attorneys general present similar arguments to intervene in a case brought by attorneys general from other states that challenges the EPA's final rule raising greenhouse gas emissions standards for heavy duty vehicles (e.g., freight trucks, delivery trucks, buses, shuttles, street sweepers). The attorneys general opposing the EPA's final rule either did not oppose the motion to intervene or took no position on the motion.

District Court Blocks Federal Agencies' Net-Zero Highway Emissions Rule

April 1, 2024 | *Commonwealth of Kentucky v. Federal Highway Administration*, No. 5:23-cv-00162 (W.D. Ky.).

A federal district court in Kentucky found that the U.S. Department of Transportation and Federal Highway Administration's (FHWA) highway emissions rule exceeds the FHWA's statutory authority and is arbitrary and capricious. The rule, if implemented, would require states receiving funds from the FHWA to measure greenhouse gas emissions and establish declining CO2 targets for on-road emissions to achieve net-zero emissions by 2050. In broad strokes, the court's reasoning is two-fold. First, the rule, as currently written, would allow the federal government to usurp state sovereignty and authority. Second, the rule advances no lawful goal, especially since the plaintiff states insist they would not seek to achieve declining CO2 emissions from their national highway system roadways.

Although the court granted the states' motion for summary judgment on the issue, the court declined to grant their request to vacate the rule or permanently enjoin its enforcement. Rather, the court limited its ruling to the 21 states since the rule "operates on a state-by-state basis, with no one state's compliance or coercion affecting that of any other state." The court also highlighted that litigation from other jurisdictions could further complicate its ruling and requests that the parties file supplemental briefs on a more well-adjusted remedy.

The 21 states implicated in this decision are Alabama, Alaska, Arkansas, Florida, Idaho, Indiana, Iowa, Kansas, Kentucky, Mississippi, Montana, Nebraska, North Dakota, Ohio, Oklahoma, South Carolina, South Dakota, Utah, Virginia, West Virginia, and Wyoming.

Litigation Tracking

JUNE

June 14, 2024 | *Western New York Youth Climate Council v. New York State Department of Transportation*, No. 808662/2024 (N.Y. Sup. Ct.).

The petition challenges the New York State Department of Transportation's (NYSDOT) consideration of greenhouse gas emissions and climate change impacts in its review of the NYS Route 33 Kensington Expressway Project in Buffalo. Specifically, the suit alleges that the NYSDOT violated the state's Climate Leadership and Community Protection Act and the New York State Constitution by misrepresenting the climate impacts, including increased greenhouse gas emissions, associated with the project.

MAY

May 10, 2024 | *State of Texas; State of Louisiana; State of Utah; State of West Virginia v. Securities and Exchange Commission*, No. 23-60079 (5th Cir.).

The Fifth Circuit dismissed for lack of standing a petition for review brought by Texas, Louisiana, Utah, and West Virginia challenging a final rule of the SEC requiring funds to disclose their votes on ESG matters. The rule went into effect on July 1, 2024. The states argued that they had standing because the states themselves suffer injury as investors in funds subject to the rule, because the funds will pass the costs of the rule on to all investors, and because of the states' "quasi-sovereign" interest in their citizens' economic well-being. The court found that the states did not establish standing to bring the petition for review and dismissed the petition without prejudice.

APRIL

April 5, 2024 | *Strickland v. United States Department of Agriculture*, No. 2:24-cv-00060 (N.D. Tex.).

A group of Texas farmers filed a motion for a preliminary injunction or, in the alternative, relief under 5 U.S.C. § 705 in the Northern District of Texas against the U.S. Department of Agriculture (USDA) challenging eight disaster relief programs managed by the USDA. They allege in the complaint that the USDA discriminated based on race and sex by creating a category of farmers defined strictly by race and sex, classifying those farmers as "socially disadvantaged" and then using different methods for calculating the amount and type of financial assistance. The plaintiffs seek an immediate injunction or stay halting the consideration of social disadvantage in the distribution of aid. On June 7, the court granted the motion in part and denied the motion in part. The court held that the defendants are enjoined from making or increasing payments or providing additional relief based on its definition of socially disadvantaged farmer or rancher. However, the USDA may still apply progressive factoring on future relief applications if done independently of the protected classes "race" and "sex."

Shareholder Proposals

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2024 Environmental Shareholder Proposal Trends

Early season results have continued the downward trend in average support for environmental proposals observed since 2021. These results largely reinforce the same shareholder proposal trends from last year.

As of June 30, 2024, approximately 190 known environmental proposals were submitted, 130 of them climate-related. Only **three** environmental proposals received majority support.

Trends in Proposal Topics

Rank	Proposal Description	Filed	Voted	Passed	Avg. Support (%)
1	GHG Emissions	61	30	3	27.1
2	Plastic/Sustainable Packaging	26	12	0	14.7
3	Climate Finance	17	8	0	20.7
4	Social Impacts of Climate Change Policies	15	4	0	18.2
5	Climate Lobbying	13	9	0	23.9
6	Sustainable Supply Chains	7	4	0	12.3
7	Pollution & Hazardous Materials	6	2	0	10.3
8	Water Use	5	1	0	28.7
9	Deforestation	4	1	0	3.3
10	Mining & Drilling	3	2	0	10

Conservative Proposals

- Of the 189 known environmental proposals, 15 were conservative proposals. 13 went to vote, with average support of 1.9%.
  - 8 companies sought no-action relief from the SEC. The SEC did not concur with 6 requests and concurred with the remaining on procedural grounds because the proposals did not meet the submission threshold.
- Anti-ESG proposals in general have increased by 19% to 112 proposals so far this season.
  - Social proposals make up the vast majority of anti-ESG proposals at 71% (80 out of 112).
  - 60 have gone to vote, with 33 proposals still pending.
  - None of the proposals have received majority support, with average support of 2.8%.

No-Action Letters

In general, the SEC staff "has nearly doubled the number of exclusions" of shareholder proposals compared with 2023. The major increase in exclusions is largely a result of an increase in the number of no-action requests filed by companies.

As of June 14, 2024, companies submitted 44 requests for no-action relief to the SEC related to environmental proposals. The SEC granted 21 of these requests and rejected 14, while 9 were withdrawn. Numerous climate proposals were excluded as "micromanagement," meaning the proposals were found to be too granular in their requests and were attempting to micromanage company activities.

Moving Forward

With the sustained level of involvement in the proxy process, it is likely that these trends will continue.

We can also expect that attention will shift to implications resulting from the 2024 election and any challenges to the SEC's climate rule.

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