Taylor Nchako, Northwestern University
Lisa Benjamin, Lewis & Clark Law School*

ESG Backlash in the United States—Investor Concerns or "Red Scare"?

Abstract: The United States lags far behind its counterparts regarding regulation on ESG investing. Part of this delay stems from a perceived "ESG backlash," which has contributed to the SEC's reluctance to require industry to disclose ESG practices. The regulatory landscape has now shifted, with the SEC proposing two ESG-centric rules—the ESG Fund Disclosure Rule and the ESG Names Rule.

Both rules have garnered numerous comments from academics, industry, investors, NGOs, and political actors. But the interest—and backlash—extends beyond public comments. States, investors, and other entities have instituted litigation that challenges ESG and anti-ESG policies alike. Amid this conflict, it is still unclear whether ESG backlash is investor-led or a political tool. To determine the source of the backlash, we analyze the comments for and against both rules. We also examine previous and ongoing ESG litigation to uncover whether these trends foretell litigation against the SEC rules.

Keywords: ESG, SEC, politics, institutional investors, securities

I. Introduction

ESG has a storied history in the United States. Over time, the Securities and Exchange Commission (SEC) has grown increasingly accepting of mandating disclosures related to ESG issues. At the same time, political actors and other entities have grown increasingly vocal against ESG considerations in investment. This part gives an overview of the history of investor ESG concerns and the present political climate surrounding the global ESG movement.

A. History of the ESG Movement in the United States

The environmental, social, and governance (ESG) framework has its roots in socially responsible investing (SRI) and corporate social responsibility (CSR). Socially responsible investing included divestment from morally or religiously corrupt practices, such as the Vietnam War and South Africa's

* Taylor Nchako is the Climate and Clean Energy Fellow at Northwestern Pritzker School of Law, Northwestern University, USA. Lisa Benjamin is an Associate Professor of Law at Lewis & Clark Law School, USA. Please direct correspondence to taylor.nchako@law.northwestern.edu and lbenjamin@lclark.edu. The authors thank Chris Marquez for his excellent research assistance.

apartheid government (Schanzenbach and Sitkoff 2020, 392–93). At the same time as SRI's rise, CSR emerged as a management principle in the 1980s (Madden and Berger-Wallister 2023, 932–33). While SRI emphasized ethical and stakeholder considerations (Schanzenbach and Sitkoff 2020, 388), scholars have increasingly linked CSR with profitability and the corporate purpose of shareholder primacy (Madden and Berger-Wallister 2023, 937–38). Under the CSR view, the stakeholder interests reflected in CSR operate as risk management tools to ensure profitability for shareholders. ESG, then, is an investment tool that merges the SRI focus on stakeholder interests with the CSR focus on corporate profitability (ibid. at 932; Schanzenbach and Sitkoff 2020, 388–89).

The SEC first encountered ESG concerns in the 1960s and 1970s, when interest groups advocated for the agency to require civil rights and environmental disclosures (Fisch 2019, 934). The SEC determined that its materiality standard did not support disclosure of a corporation's social and environmental matters because these matters were not inherently financial. This dichotomy between financial materiality and ESG factors continues to drive the SEC's approach to mandatory disclosure. As such, the SEC has generally only required disclosure of ESG factors if it is related to another required disclosure or if it corrects an otherwise misleading required disclosure (ibid. at 935). An exception to this is the SEC's mandatory disclosure of executive compensation, which it determined was financially material to investors.

In response to political pressures, however, the SEC has mandated disclosure of certain ESG factors. In 2007, for example, investor advocacy pushed the SEC to require disclosure of climate change risks that it deemed material (Fisch 2019, 937). Global politics have shaped the SEC's approach as well, as the international attention on board diversity pushed the SEC to require corporate disclosure of methods used in considering board diversity (ibid. at 938). Similarly, the 2010 Dodd–Frank Act required the SEC to respond to human rights issues in global mining supply chains with mandated disclosures on critical minerals and natural resource extraction.[1] Perhaps influenced by the pandemic's spotlight on workplace issues, the SEC began requiring companies to report human capital information in amendments to Regulation S-K in 2020 (Ho 2022, 286). And in 2021, the SEC established its Climate and ESG Task Force to bring actions against companies and funds making misstatements and misrepresentations about ESG (Crutchlow 2024). While this piecemeal approach may have sufficed when ESG factors were the concern of a minority of NGOs, consumers, and ethical investors, it no longer matches the now ubiquitous demand for ESG information from various agencies, creditors, insurers, and shareholders (Ho and Park 2019, 259–60). This demand is particularly salient in comments solicited by the SEC on the need for ESG disclosure (Ho 2022, 288).

Absent a comprehensive ESG disclosure requirement in the United States, shareholder activism and voluntary reporting have attempted to fill the gaps (Ho and Park 2019, 291). Shareholder activism primarily takes the form of shareholder proposals to address ESG issues and sometimes to produce ESG information. However, the nonbinding nature of shareholder proposals makes them a poor substitute for mandatory disclosure (ibid. at 293–94). Voluntary reporting occurs in company sustainability reports that vary in length, subject matter, and detail (Fisch 2019, 944). The inconsistency of voluntary disclosure is not useful for investors in comparing the information. As such, global frameworks have emerged to standardize disclosure by setting standards and rating sustainability practices (ibid. at 944–46). Yet ratings agencies themselves are inconsistent, and voluntary standards

[1] Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 1502(b), 1504, 124 Stat. 1376, 2213–18, 2200–22 (2010).

cannot ensure the level of quality, accuracy, and comparability that investors require to make informed choices (Berg et al. 2022, 1316). All these shortcomings produce a costly system for investors to analyze ESG information (Ho and Park 2019, 266–69).

B. *Recent ESG Action by the SEC*

In part due to these deficiencies, the political winds have shifted toward a comprehensive ESG disclosure framework. Global actors like the United Nations, the OECD, and the G20 as well as individual countries encourage ESG disclosure reform (Ho 2020, 71). Domestically, institutional investors, which hold one-fifth of all managed assets in the United States, have been major users of ESG information (Ho and Park 2019, 262). Indeed, institutional investors petitioned the SEC to adopt ESG disclosure rules in 2018 (ibid. at 252). In 2020, BlackRock, one of the "big three" index funds in the United States, released a letter stating that climate risk is financial risk and urging companies it invests in to publish ESG disclosures (Benjamin 2022, 11–12). At the federal level, the Biden administration has named one component of ESG, climate finance, as a priority (ibid. at 8–9). Moreover, the SEC's distinction between financial risks and ESG is increasingly questioned. Scholars have noted that ESG factors *do* affect financial returns, and thus meet the SEC's materiality definition (Ho and Park 2019, 261). Further, a 2020 GAO report found that institutional investors consider ESG to be relevant to a firm's long-term financial performance (US Government Accountability Office 2020). On the heels of these trends, the SEC proposed two ESG-centric rules in 2022: the ESG Fund Disclosure Rule and the ESG Names Rule. The ESG Names Rule has been finalized, while the ESG Fund Disclosure Rule has not.

The ESG Names Rule largely updates the SEC's longstanding Names Rule by requiring a fund that suggests an ESG investment focus in its name to invest at least 80 percent of their portfolio in ESG assets. 17 C.F.R. § 270.35d-1. By contrast, the ESG Fund Disclosure Rule is more comprehensive. It increases a fund's obligations based on whether it is considered ESG Integration, ESG-Focused, or ESG Impact. Each level has its own requirements in addition to the requirements for the level below it. First, funds that consider ESG as part of other factors (ESG Integration) must disclose limited information about how they consider those factors. Next, funds that use ESG as an important factor (ESG-Focused) must disclose the methodologies used to apply those factors. Funds that seek to achieve a specific ESG goal (ESG Impact) must disclose the measurements of progress and projected timeline for achieving the goal. Additionally, ESG-Focused Funds that consider greenhouse gas emissions or that use stakeholder activism must disclose their portfolio's carbon footprint and weighted average carbon intensity and the strategies employed, respectively. Similar principles apply to advisors who consider ESG when providing services.[2]

C. *ESG Backlash*

While there has been increased support for ESG globally and domestically, there has been significant domestic backlash against ESG in the United States. In 2023, conservative state lawmakers across the country proposed 165 anti-ESG bills in thirty-seven states. Yet only twenty-two bills in sixteen states became law (Gibson and Sawyer 2023, 3). These bills typically prohibit: (1) contracts between state and local governments and financial institutions that "boycott" fossil fuels and other industries, (2)

[2] Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices, 87 Fed. Reg. 36654-01.

state and local retirement funds' use of certain asset managers, (3) state, local, and private entities' considerations of ESG factors when selecting contractors, and (4) private financial institutions' consideration of certain factors when analyzing potential borrowers (ibid. at 13, 20, 27, 30). Many of these bills have not passed. Among those that did pass are Texas's and Kentucky's prohibitions on state agency contracts with companies "boycotting" fossil fuels (15). Other Republican-led states, such as Arkansas, Florida, Indiana, and West Virginia, also jumped on the "anti-ESG" bandwagon (21). Notably, anti-ESG bills were most successful in states that received less coordinated industry pushback (41).

The anti-ESG movement has spread to the federal level as well. Congressional Republicans have introduced bills to discourage banks from avoiding ESG-risky businesses and to ban retirement plan trustees from considering ESG (Gibson and Sawyer 2023, 45). According to the US House Judiciary Committee's press releases (2023a; 2023b; 2023c; 2023d), the committee subpoenaed institutional investors BlackRock, State Street Global Advisors, Vanguard, and Arjuna Capital in December 2023 for information regarding coordination on ESG goals as part of a federal antitrust probe. The committee also subpoenaed sustainability investment organizations Ceres, As You Sow, and the investor alliances Climate Action 100+ and Glasgow Financial Alliance for Net Zero (GFANZ).

In light of the difficulty of passing legislative actions, the anti-ESG movement has shifted toward executive and administrative action. For instance, Missouri's secretary of state passed two "disclosure" rules, which define "unethical practices" as including failure to disclose to customers that a professional incorporates a social objective or other nonfinancial objective in investment decisions and require firms to issue state-written disclosures to clients.[3] Many other states have shifted to increasing enforcement of existing anti-ESG laws (Ropes & Gray LLP 2024). Litigation has been increasing as well, with Tennessee's attorney general suing BlackRock alleging that it "downplayed" its consideration of ESG factors when investing (Morgan Lewis 2024). These developments build on litigation against the Department of Labor's ERISA ESG Rule, which has claimed, inter alia, that ESG threatens investment returns (Clark 2023).

Despite the political fire, it is unclear how sharp a decrease in ESG investing the anti-ESG movement has caused. Large investors like JPMorgan and State Street left the global investor coalition Climate Action 100+ in February 2024. Around the same time BlackRock transferred its membership in the coalition to BlackRock International. Though the institutions cited "independence" as the reason for leaving the coalition, the timing coincides with backlash from states (Jessop and Kerber 2024). On the other hand, researchers posit that the decline in ESG may be a cyclical phenomenon like the demand for luxury goods (Lacker et al. 2024). And some investors have opted to rephrase their ESG strategies, replacing ESG with terminology such as "sustainability" or "responsible investing," or foregoing labels altogether (Cooley LLP 2024). Still other investors have sued states over their anti-ESG policies.

Like the anti-ESG movement, the anti-anti-ESG movement has made its way to the legislative and executive branches. In May 2024, for instance, city and state treasurers, comptrollers, and pension administrators implored banks and asset managers to vote against certain ExxonMobil directors in response to the company's suit against activist investor Arjuna Capital LLC (For the Long Term 2024). Some states, like Illinois, Colorado, Oregon, and Maryland, have also passed bills that either protect or promote ESG considerations by state investment bodies (Ropes & Gray LLP 2024). Congress, too,

[3] Complaint at 1–2, Sec. Indus. & Fin. Mkts. Ass'n v. Ashcroft, No. 2:23-CV-4154-SRB (W.D. Mo.).

has gotten involved. Some congressional Democrats issued a letter urging the SEC to adopt the ESG Fund Disclosure Rule (Schatz et al. 2024). Democratic House Judiciary Committee members have asked Florida officials for information about its anti-ESG policies (Nadler and Correa 2024). This begs the question: is the backlash against ESG a reflection of investor concerns, or simply part of a "red scare"—ESG being used as a political football, disconnected from legitimate financial concerns?

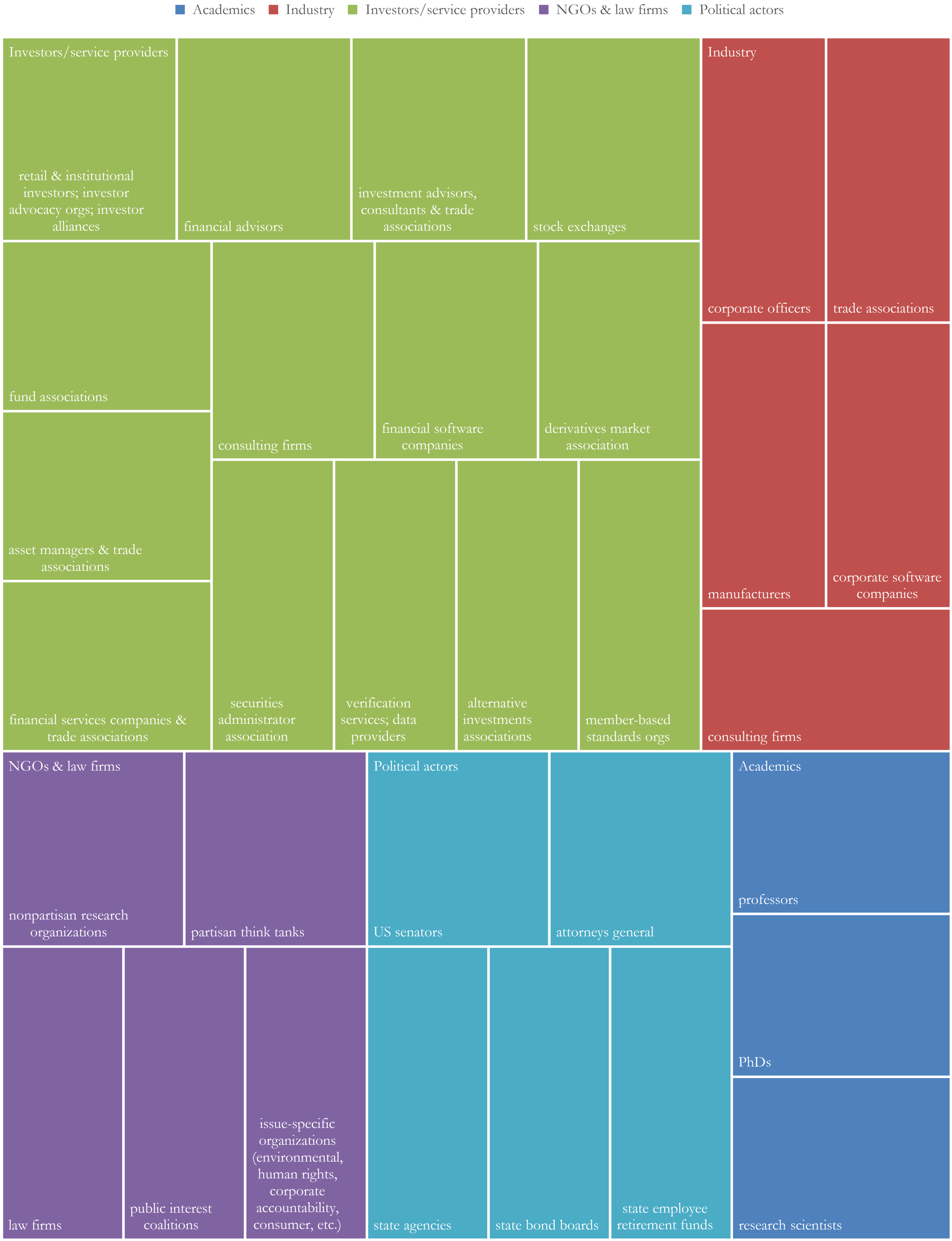
We analyze the comments both for and against the two proposed SEC rules to identify whether the "ESG backlash" is grounded in real industry concerns, or whether ESG investing is being used by red states to punish industry for "boycotting" fossil fuels and other influential industries. We then consider previous and ongoing litigation involving ESG backlash against the Department of Labor's ERISA ESG Rule, as well as ESG-focused litigation regarding "anti-ESG" rules, to determine whether these litigation attempts foreshadow what an ESG backlash regarding the SEC rules might look like in the future.

II. Methodology

To determine the level of backlash to the proposed rules, we categorized commenters along two dimensions. The first dimension separated commenters into five identity groups, as they defined themselves. First, "academics" include researchers both within and outside the legal field. Second, "industry" comprises natural and legal persons who are or otherwise serve corporations that sell securities. Third, "investors/service providers" are natural and legal persons who invest in corporations or provide services to investors such as offering a fund or stock exchange. This also includes associations of service providers. Where a commenter was primarily focused on investment activities, but may have members that represent industry, we used their primary characteristic as an investor to categorize them. Fourth, "NGOs and law firms" are entities that have a policy goal and offer legal services, respectively. Law firms explicitly note that their comments reflect the views of the firms, not their clients, so we have separated them from the "investors/service providers" group. Fifth, "political actors" includes agencies, legislators, and other government officials like attorneys general. We have omitted individuals without a title and students from our analysis due to the limited number of substantive comments from these groups. Figure 1 illustrates the groupings.

The second dimension categorized commenters into those "for" and those "against" the rule. Commenters were deemed "for" the rule if they offered full support, offered support with changes, or offered changes to specific parts of the rule. Commenters were deemed "against" if they urged full denial or offered a new approach to the rule altogether.

Figure 1: Categories of Commenters



III. The SEC ESG Fund Disclosure Rule

The ESG Fund Disclosure Rule requires ESG funds—including business development companies and exchange-traded funds—and advisors to disclose their ESG strategies to investors in their prospectus and brochures, respectively. The Rule's layered approach distinguishes between ESG Integration Funds (funds that consider ESG alongside other factors) and ESG-Focused Funds (funds that use ESG as a significant consideration), with ESG Impact Funds (funds that seek to achieve a specific E, S, or G goal) as a subset of the latter. ESG Integration Funds must describe how the fund incorporates ESG factors in their investment process.

ESG-Focused Funds have a higher burden, which includes disclosures on the types of methodologies, frameworks, indices, or screens applied, and a summary overview of the fund's priorities. The requirement is even higher for ESG Impact Funds, which must also disclose how the fund measures progress and the timeline for achieving its goal. Finally, ESG-Focused Funds that consider greenhouse gas emissions must disclose the carbon footprint and weighted average carbon intensity of their portfolio, and funds that use proxy voting or issuer engagement must disclose how they implement those strategies. Like funds, advisors must disclose the ESG factors they consider, and the methodologies, screens, or indices used.

A. Academics

Few self-described academics challenged the ESG Fund Rule. One commenter considered climate change to be a nonexistent threat. Another believed that the SEC should focus its efforts on existing rules. The third, a law professor, noted that the Rule threatens the reporting system and will not survive legal challenges. In particular, the commenter outlined seven legal issues with the Rule: (1) its costs exceed its benefits, (2) it relies on union and state pension funds' support for the Rule despite their conflict of interest, (3) the mandatory disclosures are not material, (4) the estimates required are too speculative, (5) the Rule targets carbon emissions, not financial reporting, (6) the Rule compels corporate speech, and (7) the economic analysis includes irrelevant and inconsistent information. According to the commenter, these issues produce three legal deficiencies: The Rule is arbitrary and capricious, it violates the First Amendment, and it does not meet the economic analysis requirements as set forth in *Business Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011).

By contrast, seven academics supported the ESG Fund Rule, all offering improvements. The comments expressed proposals to: remove Impact Funds from the classification, require companies to aggregate data for international holdings, require prospectus statements regarding how investments are used in funds, mandate disclosures on short-term climate goals, remove fund categories, explain why greenhouse gas emissions are the only required ESG metric, require more metrics for shareholder engagement, and expand the economic analysis. These comments emphasized matching the Rule to industry practice and strengthening the Rule's viability.

B. Industry

Industry comments against the ESG Fund Rule were relatively idiosyncratic but seemed generally concerned with the cost. Farmers were concerned that the scope 3 emissions reporting will burden their daily operations. An industry book publisher noted that tracking emissions will be inconsistent and noncomparable. A corporate officer believed ESG to be irrelevant to shareholders and a ploy to pay consulting firms. An association of small businesses characterized the Rule as unnecessary but offered amendments to codify exemptions for small investment adviser businesses and to define ESG. Finally, the US Chamber of Commerce objected to the Rule's potential compliance cost and its detailed structure writ large. The Chamber suggested a simple, principles-based ESG Fund Disclosure Rule.

Here, too, comments supporting the Rule outnumbered those against it. Some commenters simply expressed agreement with the Rule. Proposals to increase disclosure on proxy voting and shareholder engagement reflected those raised by academics. Others suggested that the SEC: separate climate-related disclosures from Form 10-K, extend the compliance due date, redefine "Integration," separate Impact Funds from Focused Funds, require more disclosure about third-party service providers, remove the definition of "ESG engagement meetings," require a strategy overview for all funds, and screen funds that have high ESG ratings as an incident of the industry they invest in, rather than intentionality. Contrary to an industry comment against the Rule, one comment recommended *not* defining ESG.

There were also comments specific to the energy sector, all of which were concerned their industry is not perceived as "E" enough, but all supportive of the Rule. A public gas association expressed concerns that the Rule would pass on higher costs to consumers. A nuclear energy association requested that the SEC consider how nuclear contributes to decarbonization. And a renewable natural gas association opposed the ban on including carbon offsets in carbon footprint measurements, in part because its members rely on offsets.

C. Investors and Service Providers

Investor comments against the ESG Fund Rule addressed the cost on various stakeholders, including retirees, retail investors, private companies, funds, advisers, and business development companies. Many of these comments urged the SEC to use its existing authority and stressed the disruption to capital markets. Other comments addressed the funds covered, with some urging the SEC to eliminate categories and regulate all funds while others advocated expanding the Rule beyond only those that consider themselves ESG funds to all funds that engage in ESG considerations. Multiple trade associations expressed dissatisfaction with the length of the public comment period, particularly in conjunction with other SEC rulemakings like those for the ESG Names Rule and the Climate Disclosure Rule. Similarly, NASDAQ was concerned with regulatory fragmentation and urged the SEC to at least delay implementation of the ESG Fund Rule until after the Climate Disclosure Rule's compliance due date. Some idiosyncratic issues include underenforcement, politicizing individual financial choices, and a proposal to exempt derivatives markets.

There are over six times as many investor comments for the Rule as against the Rule. Multiple retail investors supported the Rule. Institutional investors and service providers made suggestions for fund categories, greenhouse gas reporting, investment advisors, proxy voting and shareholder engagement, and timing. Some comments suggested that the SEC remove all categories, others proposed removing "Integration Fund," and still others proposed redefining "Integration Fund" and "Focused Fund." Several comments suggested limiting greenhouse gas reporting to climate-focused "E" funds while others proposed expanding it to all funds. Similarly, comments differed about whether to include scope 3 emissions reporting. Many comments preferred a limit on reporting requirements for investment advisors, in part to reduce overstating an ESG focus and to limit burdens on small and midsized investment advisors. Commenters also emphasized narrative disclosures, particularly in shareholder engagement and proxy voting. With respect to timing, commenters urged the SEC to wait until the Climate Disclosure Rule is finalized. These concerns largely reflected a focus on properly distinguishing ESG funds, considering ESG regulations in other jurisdictions, and enhancing clarity.

D. NGOs and Law Firms

The most common arguments against the ESG Fund Rule in this category asserted that it increases politicization, eschews materiality, imposes unnecessary cost, limits investment choice, and is inherently arbitrary. Law firm comments against the Rule similarly note the Rule prioritizes comparability over materiality and is overly broad. Like the Chamber of Commerce, one firm suggested a principles-based approach. Another firm offered six legal challenges to the Rule: (1) it is unconstitutionally vague because it does not define ESG, (2) it exceeds the SEC's authority to address materiality and conflicts of interest, (3) it encourages investment advisors and companies to consider ESG factors as distinguished from financial return objectives, thereby violating their fiduciary duties, (4) it is a pretext for the SEC to advance ESG activist and asset manager goals, (5) it violates the major questions doctrine because it will cause vast economic disruption, and (6) it violates the nondelegation doctrine because the SEC lacks expertise in climate.

There are over three times as many comments from this category of commenters for the Rule as against the Rule. Comments for the Rule noted that the Rule would improve consistency, reliability, and comparability. The comments regularly emphasized certain changes. The SEC should elevate the "S" as much as it has emphasized the "E." It should improve fund categories, either by removing "Integration Fund," renaming the funds, or redefining the funds. Several comments suggested an expansion of proxy voting and shareholder engagement disclosures and scope 3 emissions reporting. Organizations also requested that funds be required to disclose their top three investments and note in their proxy statements if they do not consider greenhouse gas emissions. Many also commended the potential for the Rule to harmonize with ESG regulations in other jurisdictions.

E. Political Actors

Five state offices opposed the ESG Fund Rule. Akin to agricultural industry concerns, an agricultural agency worried about the burden of scope 3 emissions reporting. Likewise, a bond finance agency noted the cost of the Rule for municipal issuers. Six US senators requested information regarding the agency's capacity amid its increased rulemaking.

Attorneys general of twenty-one states jointly raised three broad legal arguments against the Rule: (1) the SEC lacks authority to adopt the Rule because it is not part of the agency's core statutory authority to regulate misrepresentations and materiality, and it violates the major questions doctrine, (2) the Rule violates the First Amendment prohibition on compelled speech, and (3) the Rule is arbitrary and capricious because the cost-benefit analysis is unsound, it repeats the Climate Disclosure Rule, it is a pretext for ESG activists, the SEC did not consider reasonable alternatives, the SEC ignored its statutory mandate to simplify disclosures, and because the Rule is unconstitutionally vague for failure to define "ESG."

Unlike in the other categories, political actors for the Rule submitted fewer comments than those against. One state retirement fund proposed improvements to the Rule, including to rename "Impact Funds," require all funds to disclose greenhouse gas emissions, and improve flexibility to accommodate the evolving nature of ESG. Additionally, attorneys general of seven states jointly supported the Rule.

F. Summary of Comments

In sum, comments both for and against the ESG Fund Disclosure Rule mentioned the impact on certain groups like investment advisors, the confusion among fund categories, the relevance or irrelevance of greenhouse gas emissions reporting, and the appropriate level of reporting on proxy voting and shareholder engagement. Many investor objections targeted compliance costs and flexibility, rather than ESG per se. Those that contested SEC's authority to regulate ESG disclosures were political actors, a law firm, and a law professor—not investors or industry.

IV. The SEC ESG Names Rule

The SEC Names Rule has not been updated since 2001, and the proposed Rule is designed to prevent investor confusion. Its expanded scope covers ESG-named funds, to prevent greenwashing—or ESG-washing—by funds and business development companies. Under the proposed Rule, fund names that indicate investments in environmental, social, or governance factors must invest at least 80 percent of their portfolio in assets that advance those goals. The prospectus for ESG-named funds must also disclose how those aims will be advanced by the fund. For ESG Integration Funds, the SEC has determined that using ESG terminology in their name is materially deceptive or misleading; thus, ESG Integration Funds cannot use descriptors such as "sustainable," "green," or other ESG indicators in their names. Finally, funds may only depart from compliance with the Rule under certain enumerated circumstances and must monitor compliance every thirty days.

A. Academics

Academics commenting on the ESG Names Rule addressed complications with "ESG" as a measurable concept. Those against the Rule predicted it will not create meaningful benefit for investors. One economics scholar noted the ESG Names Rule ignores market competition and will impose substantial costs without much benefit to investors. Two law professors concluded, from empirical analysis, that the Rule will disrupt legitimate ESG strategies because it overemphasizes greenwashing and places too much value on the name of a fund as an informational tool for investors. Somewhat similarly, academics in favor of the Rule suggested that the SEC clarify how the remaining 20 percent of a fund's assets factor into the name, bolster the economic analysis, and recognize the subjectivity of "ESG."

B. Industry

There are few industry comments on the ESG Names Rule. The US Chamber of Commerce argued that the ESG Names Rule will bring increased costs and investor confusion due to the subjectivity of "ESG," and that it is unnecessary because the SEC has existing authority to remedy misleading or fraudulent fund names. By contrast, industry supporters of the Rule commend it for addressing greenwashing. One company suggested that the SEC require more descriptive ESG fund names.

C. Investors and Service Providers

Like industry commenters, investors against the ESG Names Rule pointed to the cost of compliance, investor confusion, and the shift from objective fund descriptors to subjective, overly broad fund strategies and characteristics. Comments also noted the restrictiveness on derivatives markets, temporary noncompliance, and investment advisors' ability to serve their clients. Multiple commenters suggested that the ESG Fund Disclosure Rule is a better mechanism to address greenwashing in funds. Others noted the SEC's failure to consider the interconnectedness of the ESG Names Rule and the ESG Fund Disclosure Rule, arguing that it amounts to arbitrary and capricious rulemaking.

One investor association raised two legal challenges to the Rule. First, that the SEC lacks authority to promulgate the Rule because it is too vague to be an exercise of its authority to define "misleading" and it ignores the materiality requirement. Second, that the Rule violates the First Amendment in three ways: (1) It is a content-based restriction on speech related to ESG terms, (2) it restricts a fund's ability to speak without providing sufficient justification, and (3) it compels speech by requiring public disclosure of a fund's assets and compliance periods.

Investors in favor of the Rule addressed compliance and clarifications. Numerous commenters addressed the temporary noncompliance provision, the frequency of reporting requirements, and inflexibility for certain funds. Commenters also requested clarifications on distinctions between assets, the materially deceptive and misleading standard, and inconsistencies with the ESG Fund Disclosure Rule. Some specific issues included faith-oriented strategies, index funds, and unit investment trusts.

D. NGOs and Law Firms

NGO and law firm commenters against the ESG Names Rule questioned its applicability to investment strategies, its cost, the subjectivity of "ESG," and the temporary noncompliance provision. Some objected that the Rule will limit investor choice and mislead investors. One law firm raised three legal challenges to the Rule: (1) The SEC did not determine that a particular word or phrase is deceptive or misleading; moreover, it did not define "ESG," (2) the Rule unjustifiably departs from existing practice that applies the 80 percent test only at the time of investment, and (3) the costs outweigh the benefits.

Seven times as many NGO or law firm commenters supported the Rule. Some asked for clarification regarding the relevant ESG factors, the applicability to index funds and derivatives, and the absence of a safe harbor. Others emphasized the social aspects of "ESG" and the need to expand regulation to all asset managers. A law firm expressed concerns with the SEC's focus on the scope of the Rule rather than potential legal issues with its structure. In particular, the commenter noted that the Rule may be unlawfully retroactive if it applies to transactions that have already occurred. To remedy this, the commenter asserted, the SEC should clarify that the Rule will not apply to preexisting funds; instead, the SEC should police misleading or deceptive funds by adjudicative order. The comment also noted that some of the procedural requirements may exceed the SEC's authority to define misleading terms.

E. Political Actors

As with the ESG Fund Disclosure Rule, the political actors category is the only instance where comments against the Rule exceeded comments in favor of it. A group of US senators again requested information regarding the SEC's capacity amid its accelerated rulemaking. There were no comments from political actors in favor of the Rule.

F. Summary of Comments

Commenters both for and against the ESG Names Rule addressed similar concerns with the Rule's clarity and applicability to certain groups. Though the ESG Names Rule received fewer comments than the ESG Fund Disclosure Rule, commenters did question the role of "ESG" in the ESG Names Rule, with some investors listing legal challenges to its use. In general, there seem to be more questions about the proposed ESG Names Rule's efficacy in reducing misleading fund names. The legal issues raised in comments could signal future litigation claims, but the comments also echo prior litigation against other ESG actions.

V. ESG Backlash: What Lessons for the SEC?

The proposed SEC rules have already attracted a lot of attention from asset managers, industry associations, NGOs, academics, and attorneys general. It is likely that litigation will be initiated around any finalized rules, but it is not yet clear by whom. This part examines previous ESG litigation—first against the Department of Labor's ERISA ESG Rule, then against ESG investment strategies, and finally against anti-ESG actions—to identify trends in ESG backlash.

A. The First Wave—ERISA Litigation

In 2022, the Department of Labor (DOL) finalized a rule clarifying that "prudent investing" under the Employment Retirement Income Security Act of 1974 (ERISA) may require consideration of ESG factors. 29 C.F.R. § 2550.404a-1. This 2022 Rule unwound the Trump-era 2020 Department of Labor Rule, which listed the only "pecuniary factors" that a plan fiduciary was allowed to consider, ESG not included (US Department of Labor 2022). After the DOL finalized the 2022 Rule, litigation ensued. It falls under two buckets: cases that challenge the Rule and cases that challenge plan fiduciaries that consider ESG factors.

In *Utah v. Walsh*, twenty-six states, three oil/natural gas companies, and one individual sued the Department of Labor, claiming that the Rule violates ERISA and the Administrative Procedure Act (APA). No. 2:23-CV-016-Z, 2023 WL 6205926 (N.D. Tex. Sept. 21, 2023). The plaintiffs argued that ERISA's plain text prohibits the consideration of nonpecuniary factors, even when two options have the same financial benefits. The plaintiffs also claimed that the Rule did not rebut the 2020 Rule's findings, did not identify who was negatively affected, and relied on inconsistent and irrelevant factors. Relying on *Chevron* and comments to the Rule, the district court rejected each of these arguments. Considering the Supreme Court's overturn of *Chevron* in *Loper Bright Enterprises v. Raimondo*, 144 S. Ct. 2244 (2024), the Fifth Circuit remanded the case to be decided under the nondeferential standard the Supreme Court set forth. *Utah v. Su*, 109 F.4th 313 (5th Cir. 2024).

Beneficiaries have lodged claims against the ERISA Rule too. In *Braun v. Walsh*, two individuals raised claims similar to those in *Utah v. Walsh*. Additionally, Braun alleged a violation of separation of powers because Congress did not delegate authority to the DOL to make environmental policy. No. 2:23-cv-00234, 2023 WL 3540096 (E.D. Wis.). *Braun* has yet to be decided. In *Spence v. American Airlines, Inc.* and *Wong v. NYC Employees' Retirement System*, employees argued that their employment retirement plans breached ERISA's duty of loyalty and prudence by investing in funds that pursue ESG, which is a nonpecuniary policy goal.[4] The complaints focus on potential losses to employees' retirement funds, as ESG funds may not perform as well as other funds. As of the time of this writing, *Spence* is pending while *Wong* has been dismissed for lack of standing. *Wong v. NYC Employees' Retirement System*, No. 652297/2023 (Sup. Ct. N.Y. July 2, 2024).

These cases demonstrate backlash from both investors and political actors against ESG investing. The allegations that the 2022 Rule violates ERISA and the APA reflect some of the comments opposing the SEC's rules as outside its statutory authority. And the claims that target separation of powers reflect the Supreme Court's recent imposition of the major questions doctrine. *West Virginia v. EPA*, 597 U.S. 697 (2022). This again mirrors comments against the SEC rules as violative of that doctrine.

B. *The Second Wave—Anti-ESG Litigation*

Anti-ESG litigation has begun in earnest, much of it led by political actors who target agencies and institutional investors. In May 2023, seventeen state attorneys general moved for the Federal Energy Regulatory Commission to revoke BlackRock's authorization to own over $10 million in utility stock because BlackRock no longer operates as a passive investor, but as an "environmental activist."[5] In September of the same year, the states of Texas, Louisiana, Utah, and West Virginia sued the SEC for its new proxy vote disclosure rule, arguing that it was arbitrary, capricious, and in excess of its authority in part because it promoted an "ESG agenda."[6] Then in December 2023, the state of Tennessee sued BlackRock under the Tennessee Consumer Protection Act for allegedly engaging in deceptive practices by pursuing ESG strategies in non-ESG funds. Complaint, *Tennessee v. BlackRock, Inc.*, No. 23cv-681 (Cir. Ct. Tenn. Dec. 18, 2023). In March 2024, the Mississippi secretary of state issued a cease-and-desist order against BlackRock, accusing it of making materially false statements by endorsing ESG investments and asserting that ESG investments benefit financial outcomes. *BlackRock, Inc.*, Order No. LS-24-6726 (Miss. Sec'y of State Sec. Div. Mar. 26, 2024). Five months later, Indiana filed a similar cease and desist order against BlackRock (Smith 2024). Numerous cases have also been filed challenging the SEC's Climate Disclosure Rule, with plaintiffs ranging from states and conservative groups to companies and environmental advocates (Balsanek et al. 2024). Some of these claims echo comments against the SEC's ESG Fund Disclosure Rule, invoking exceeding authority, the major questions doctrine, compelled speech, and arbitrariness and capriciousness.

Contrary to the environmental focus in many other actions, so far investor suits have focused on the "S" in ESG. The National Center for Public Policy Research, a conservative think tank dedicated to "'fighting back' against 'woke politicized capital and companies,'" brought a shareholder derivative

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[4] Spence v. Am. Airlines, Inc., No. 4:23-CV-00552-O, 2024 WL 733640 (N.D. Tex. Feb. 21, 2024); Complaint, Wong v. NYC Emp. Ret. Sys., No. 652297/2023 (N.Y. Sup. Ct. May 11, 2023).

[5] Motion to Intervene and Motion for Relief at 3, BlackRock, Inc., No. EC16-77-002 (U.S. Fed. Energy Regul. Comm'n May 10, 2023).

[6] Texas v. SEC, No. 23-60079, 2023 WL 5985329, at *17 (5th Cir. Sept. 5, 2023). This suit was dismissed. 2024 WL 2106183 (5th Cir. May 10, 2024).

suit against Starbucks for its diversity, equity, and inclusion initiatives.[7] The court dismissed the case with prejudice, noting that the plaintiff sought to pursue its personal policy agenda and did not represent the majority of shareholders. Similarly, nonprofit Alliance for Fair Board Recruitment challenged the SEC's authority to approve NASDAQ rules requiring companies to disclose the race, gender, and sexuality of their directors. It also raised arbitrary and capricious arguments and compelled speech arguments. *Alliance for Fair Board Recruitment v. SEC*, No. 21-60626, 2024 WL 1327980 (5th Cir. Mar. 21, 2024). In a rehearing en banc, the Fifth Circuit found the SEC's approval of the NASDAQ rules was arbitrary and capricious and violated the major questions doctrine. All. for Fair Bd. Recruitment v. Sec. & Exch. Comm'n, No. 21-60626, 2024 WL 5078034 (5th Cir. Dec. 11, 2024).

There have also been anti-ESG suits against investors. In January 2024, ExxonMobil sued investors Arjuna Capital and Follow This to exclude their shareholder proposal from its proxy statement because it dealt with ordinary business matters.[8] Because the proposal demanded that Exxon accelerate its emissions reductions, Exxon alleged, it sought to change the company's daily business rather than increase financial performance or shareholder value. The court dismissed the claim once Arjuna promised not to resubmit similar proposals.[9]

As with the anti-ERISA cases, administrative law doctrine pervades anti-ESG litigation. In addition, agency actions have garnered First Amendment compelled speech challenges. Again, these claims mirror the legal challenges some groups noted in their comments on the SEC ESG Fund Disclosure Rule and ESG Names Rule.

C. The Third Wave—Anti-Anti-ESG Litigation

Investors and service providers have countered anti-ESG efforts. The Kentucky Bankers Association argued that Kentucky's "anti-ESG" legislation, and the attorney general's subsequent subpoenas and civil investigative demands regarding investment practices, exceed the AG's authority and impede the free speech and freedom of association of capital.[10] After dismissing the First Amendment claims, the court remanded the case to state court. Similarly, the Missouri Securities Industry and Markets Association sued the Missouri Secretary of State and Missouri Securities Commission challenging Missouri's "anti-ESG" disclosure rule. The plaintiff claimed that the rule is preempted by federal law, constitutes compelled speech, and is unconstitutionally vague. The court granted the plaintiff's motion for summary judgment.[11] In Texas, a pending case involves a sustainable investing organization challenging a statute that divests from funds Texas categorizes as boycotting fossil fuels. The plaintiffs argue that the statute impinges on freedom of speech and association and is unconstitutionally vague.[12]

State employees have also sued over divestment statutes. In a case that was ultimately dismissed on standing grounds, a state employee challenged Texas's statute that mandates state institutions divest from funds that the state determines boycotts Israel. *Abdullah v. Paxton*, 65 F.4th 204 (5th Cir. 2023), *cert. denied*, 144 S. Ct. 188 (2023). The plaintiff argued that the statute violates the First

[7] Nat'l Ctr. for Pub. Pol'y Rsch. v. Schultz, No. 2:22-CV-00267-SAB, 2023 WL 5945958, at *1–2 (E.D. Wash. Sept. 11, 2023).
[8] Complaint, Exxon Mobil Corp. v. Arjuna Capital, LLC, No. 4:24-cv-00069-O (N.D. Tex. Jan. 21, 2024).
[9] Exxon Mobil Corp. v. Arjuna Capital, LLC, No. 4:24-CV-00069-P, 2024 WL 3075862 (N.D. Tex. June 17, 2024).
[10] Hope of Kentucky, LLC v. Cameron, No. 3:22-CV-00062-GFVT, 2023 WL 6406212 (E.D. Ky. Sept. 29, 2023).
[11] Sec. Indus. and Fin. Mkts. Ass'n v. Ashcroft, No. 23-CV-04154-SRB, 2024 WL 3842112 (W.D. Mo. Aug. 14, 2024).
[12] Complaint, Am. Sustainable Bus. Council v. Hegar, No. 1-24-CV-1010 (W.D. Tex. Aug. 29, 2024).

Amendment as overbroad, unconstitutionally vague, and running afoul of the establishment clause. Comparable developments arose in Oklahoma, where a judge granted a state employee's temporary injunction against a statute that mandates state institutions divest from companies that "boycott" fossil fuel companies. Order, *Keenan v. Russ*, No. CV-2023-3021 (Okla. Dist. Ct. May 7, 2024). In addition to finding the statute unconstitutionally vague, the court also found that the statute's political motivations violated the state constitution's directive to administer pensions for the sole benefit of employees. This latter argument illustrates that federal law is not the only ground for successful anti-anti-ESG suits. On a broader scale, anti-anti-ESG suits reflect arguments similar to those in anti-ESG actions, particularly the First Amendment claims.

The three waves of litigation have largely built on one another. ERISA litigation centered on the statute and the Administrative Procedure Act. Anti-ESG litigation expanded statutory and APA claims to incorporate state law claims. Anti-ESG litigation also introduced the major questions doctrine and First Amendment jurisprudence. In both instances, many of the actions have been brought by states, fossil fuel companies, or conservative organizations. On the flip side, investors and their service providers—the group that agency rules are designed to protect—have mostly sued to enjoin anti-ESG laws, relying on First Amendment, preemption, and, recently, state law arguments. Comments against the SEC's ESG rules reflect the same trends—legal challenges are raised mostly by noninvestor groups and focus on statutory authority, the Administrative Procedure Act, the major questions doctrine, and the First Amendment.

The promulgation of the final ESG Names Rule in September 2023 provides insights into what may lie ahead once the ESG Fund Disclosure Rule is finalized. The SEC made four major changes to the proposed ESG Names Rule: (1) The final Rule abandons the proposed temporary noncompliance requirements, (2) it reduces some obligations for derivatives markets and closed-end funds/business development companies, (3) it requires funds to include a definition of the terms in its name, and (4) it does not categorize ESG Integration funds as materially deceptive or misleading. These changes address comments about flexibility, cost, and efficacy. The changes do not seem to amend the proposed Rule to stifle legal challenges. In fact, the final Rule expressly discounts legal challenges raised in the comments. Despite an investor group and a law firm raising legal challenges in the comments, there has not been litigation against the ESG Names Rule. Potential plaintiffs may await the resolution of ongoing cases that raise the same challenges, or perhaps they anticipate the promulgation of the more contentious ESG Fund Disclosure Rule. Either way, the lack of investor-led litigation against the ESG Names Rule matches trends in prior litigation.

VI. Conclusion

Comments against the SEC's ESG Fund Disclosure Rule and ESG Names Rule demonstrate investor concern with the flexibility and efficacy of the rules, rather than the subject matter of ESG. While ERISA litigation featured somewhat diverse plaintiffs against the ERISA ESG Rule, anti-ESG litigation and anti-anti-ESG litigation seem much more biased, taking the form of politicians rather than investors. If these litigation trends continue, and the rules' comments forecast the commenters' legal positions, then ESG backlash indeed seems to be a political football rather than a legitimate investor concern.

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