10 Issues To Watch As ESG Remains Alive And Well In 2024

By **Heidi Friedman** (January 1, 2024)

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With all of the legislation being enacted against environmental, social and corporate governance factors, as well the increase in greenwashing, diversity, environmental justice and shareholder litigation, companies have been asking whether ESG is still a driving force for business. The answer is a resounding yes.

Data collected as recently as October 2023 confirms that ESG is not going anywhere. While some companies are softly retreating to terminology like "corporate responsibility" or "sustainability," the substance that makes up the components of their ESG programs and goals is sticking because stakeholders demand it.

Three-fourths of Americans believe companies need to positively affect society, and the large U.S. corporations that best meet stakeholder needs saw a 4.5% higher profit margin and a 2.3% higher return on equity and paid five times more in dividends.[1]

At the same time, 70% of potential employees are more likely to apply for and accept a job from a socially responsible organization, and 92% of U.S. investors believe a company with a strong ESG performance deserves a premium valuation of its share price.[2] And look how far the world has come without any regulation.

Yet as we enter this new era and move away from solely voluntary disclosures, it will be more important than ever for companies to continue to develop authentic ESG programs that align with company values and stakeholder input and keep these programs fluid and flexible.

Here are 10 ESG-related items to evaluate, and watch in 2024:

1. The SEC's Rule For Climate-Related Disclosures

While no one has a crystal ball, the vast majority of ESG professionals believe that the U.S. Securities and Exchange Commission will work its way through the almost 16,000 comments it received and issue the long-awaited final rule for climate-related disclosures.

While it is likely that the final rule will be challenged, its approach to Scope 3 emissions — greenhouse gas, or GHG, emissions up and down the value chain — will affect public companies that have to directly report to the SEC as well as many private companies through the flow-down impact public companies impose on their suppliers.

Hopefully, the public companies are ready and have set up a process that will support their climate-related financial reporting to be as reliable as their historic financial reporting.

2. California Laws and Interpretations

With regulations from the California Air Resources Board, or CARB, interpreting the state's new climate laws, S.B. 253 and S.B. 261 and A.B. 1305, California wins the prize for being first out of the gate with new ESG laws regulating companies that do business in the state.

Yet CARB is tasked with telling the world what these vague and difficult to interpret laws mean. CARB has until Jan. 1, 2025, to complete this mission. The new laws will require Scope 3 disclosures by 2027, and California's requirements are generally broader than the proposed SEC rule, applying to both private and public companies that generate over $1 billion in gross annual revenue and do business in California.

There is also a new, very broad law imposing mandates on carbon offsets and net-zero disclosures, although it will be a while before the regulated community truly understands the full meaning of these new requirements and how they will interact with the other regulations arising on the federal level. While companies are eager to prepare, it will be interesting to see if CARB provides any previews next year.

3. The FTC Green Guides

As with the SEC rule, every company that makes any type of environmental claim wants to know when the Federal Trade Commission will issue its new Green Guides, the premier source aimed at preventing deceptive claims about the environmental benefits of products or services. The FTC was supposed to provide an update back in 2022, but we are still living with the 2012 version.

While the comment period for the Green Guides update ended in April 2023, many experts are not optimistic that the FTC will even issue the long-awaited update this year, due to the number of comments it received and the breadth of changes that will be required.

It will be important to monitor if 2024 is the FTC's year, as the update will be the instruction manual for how to make environmental marketing claims while mitigating the risk of greenwashing litigation. Businesses will also need to keep an eye out for increased FTC enforcement, which is expected to quickly follow the release of the update.

4. Checking if Materiality Assessment Has Gotten Stale

Many companies go through the strategic process of launching their ESG programs from the ground up with a materiality assessment, although the better term is a prioritization assessment.

This best practice tool allows an organization to gather information from stakeholders to identify which issues under the ESG umbrella are most important to employees, suppliers, customers and investors. Yet ESG programs need to stay nimble and fluid, and stakeholder values change over time.

Thus, a pre-COVID materiality assessment may not be serving a company well. Indeed, it may be time to initiate a reboot and consider even breaking the assessment down by business units or locations to get greater clarity around what really matters and where the company's goals should be focused and dollars should be spent.

5. What CSRD Disclosures Will Actually Look Like

While U.S. companies doing business in the EU have received a two-year reprieve, EU-based companies will be faced with the Corporate Sustainability Reporting Directive, or CSRD, next year. As of Jan. 1, European companies complying with the Non-Financial Reporting Directive are required to report on climate impact as well as various social topics, which is broader than the SEC rule. Other types of companies will be phased in from there.

The CSRD is intense and requires disclosure of double materiality, i.e., impact on the business and the climate, and auditing of data, which makes the mandates a whole new ball game for most businesses.

The goal is to improve the quality and reliability of this type of data for investors, but it will be interesting to see the practical effect. Thus, it is time to apply the company's best practices for disclosure of historical financial information to GHG emissions and other related environment impact statements that are provided as part of the CSRD directive.

6. Meeting TCFD Requirements

Task Force on Climate-Related Financial Disclosures, or TCFD, requirements seem to be the chosen standard to comply with both the upcoming SEC and CSRD mandates, but the TCFD published its final report in October of this year, which confirmed the momentum of companies disclosing TCFD-aligned information.

As the task force is disbanded, the International Sustainability Standards Board will take over monitoring climate-related disclosures and reporting to the Financial Stability Board, but the TCFD as the alleged "gold" standard will live on as the most accepted reporting framework, at least at this point in time.

7. Whether Courts Will Back Companies as Greenwashing and Diversity Claims Rise

Right now, many courts are facing pending motions to dismiss from companies trying to defeat consumer class actions and other fraudulent misrepresentation claims that fall into every growing bucket of greenwashing claims. While plaintiffs are pushing the envelope on these claims, companies are pushing back, and courts have been fairly aggressive in dismissing claims.[3]

Yet there are too many claims pending to count, and after the U.S. Supreme Court's June 29 Students for Fair Admissions v. President and Fellows of Harvard College decision on affirmative action, various groups also are aggressively going after diversity, equity, inclusion and belonging programs as well as filing reverse discrimination claims.[4]

While the Supreme Court's opinion in the Harvard case is pretty narrow, it does look like the lack of regulation around these issues has created a gap that may be filled with court precedent next year and that may require some companies to revisit and revise aspects of their ESG programs.

8. Decreased Interest in Carbon Offsets and Increased Litigation Related to Carbon Offset Contracts

There is a clear trend indicating that key ESG stakeholders will not accept carbon offsets in place of addressing root cause problems for GHG emissions; thus, this alleged "pay to play" replacement will be looked at very closely in the coming year. On Oct. 13, 2023, the U.S. District Court for the Central District of California threw out, with leave to amend, the Blackburn v. Etsy Inc. lawsuit, against an arts and crafts company related to carbon offset claims it made associated with shipping its products.

The risk to companies purchasing these offsets is compiled by the challenges inherent in the contracts and a company's ability to collect damages should the offset provider not be able to deliver.

Liquidated damages will most definitely not cut it when a company may face litigation and enforcement from an offset agreement gone bad. Injunctive relief may be helpful, but only if there is an action that can be forced, and oftentimes the offset just does not exist. This will remain a risky proposition in the coming years.

9. An Uptick in the Flow-Down Impact

Scope 3 emissions are the heart of every company's emissions. According to the 2000 U.N. Global Compact, a nonbinding United Nations pact to get businesses to adopt sustainable and socially responsible policies and report on them. Scope 3 emissions make up at least 70% of a company's emissions.

Some companies even report that Scope 3 emissions make up 95% of total emissions.[5] The pending regulatory framework will require a deeper dive into the full supply chain, both upstream and downstream, to even begin to tackle Scope 3.

Thus, there will be additional mandates to meet the Science Based Targets Initiative, a rigorous and expensive process that validates GHG emission calculations and data and allows a company that successfully completes the process to rely on the certification.

The days of customer surveys and forms and requests related to ESG are just beginning. Creating a single streamlined response framework and workflow will be critical.

10. A Way to Track Data Comprehensively

The No. 1 challenge businesses faced in 2022 is tracking data.[6] ESG professionals' email boxes are full of messages from companies trying to sell a one-size-fits-all solution; yet as of now, there is not a single product that can synthesize and amalgamate all of the data needed to substantiate a company's full set of goals and metrics under the ESG umbrella.

Between the use of AI and the development of more specific and streamlined reporting frameworks, it is highly likely that various solutions will emerge. In the interim, it remains critical to continue collecting data to back EVERY claim or statement that is made, to update it frequently and, ideally, to regularly audit the data. This is the best risk mitigation strategy available for now.

Conclusion

There are many significant developments on the ESG horizon as we shift into a new area of requirements and mandates. Be sure to make a New Year's resolution that includes tracking this ever-changing landscape. The seismic shifts that are expected in 2024 will impact all businesses, public and private. Put the resources in place now to allow your business to be agile and proactive in meeting stakeholder expectations for ESG and everything that falls under that ever-growing umbrella.

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should not be taken as legal advice.

[1]https://www.forbes.com/sites/forbesbusinesscouncil/2023/10/04/following-the-data-why-companies-should-prioritize-esg-and-tips-for-success/?sh=6124a8356df5.

[2] Id.

[3] See, e.g., David Swartz v. The Coca-Cola Company, N. Dist. CA (Nov. 18, 2022); Lizama, et al. v. H&M, E.D Missouri (June 2, 2023).

[4] See, e.g., Brian Craig v. Target, M.D. Florida (Aug. 8, 2023)

[5] Tackling the scope 3 challenge," PWC Global in collaboration with The Climate Group (October 28, 2022).

[6] https://admin.thompsonhine.com/wp-content/uploads/2022/12/ESG_An_Intensifying_Focus_2022.pdf.