ESG

# ESG Insights: 10 Things That Should Be Top of Mind in 2024

***By Paul A. Davies, Sarah E. Fortt, and Betty M. Huber***

In some ways, 2023 was a challenging year for environmental, social, and governance (ESG). This topic can invoke strong and diverse opinions, and debates regarding what ESG should or should not cover, or indeed, whether or not "ESG" itself is consistent with long-term investor interests and the board's fiduciary duties, proliferated. However, after cutting through these debates and focusing on the varying degrees of importance enterprises place on ESG matters, we see that in 2023, business leaders continued to focus on how certain issues impact their bottom line as well as their corporate reputation, risk exposure and management, and corporate value.

Despite the current challenging environment, regulators have taken extensive steps to embed ESG into the global regulatory landscape. For example, in 2023, ESG-related regulatory trends continued to advance in multiple jurisdictions. At the same time, we also saw increased fragmentation in the US, particularly with respect to issues concerning ESG investment considerations and diversity. Litigation trends also continued, as did the increased awareness of value chain vulnerabilities and risks, leading to companies making strategic decisions associated with corporate opportunities and risk management. At the same time, more traditional questions regarding board composition and investor activism continued to be informed by evolving ESG perspectives.

We anticipate that all of these trends will continue. In this context, the fifth annual installment of our ESG Top 10 Insights highlights the developments and trends we see as likely to define ESG in 2024.

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## 1. As More Mandatory ESG Requirements Come into Effect, Associated Potential Liabilities Are Likely to Correspondingly Increase, with Companies Facing Additional Pressure to More Effectively Integrate ESG into Their Practices and Financial Statements

2024 presents a turning point in the ESG regulatory landscape, with various laws, including reporting requirements, coming into effect. The EU Corporate Sustainability Reporting Directive (CSRD) entered into force in January 2023, with the first companies subject to reporting requirements (in addition to a requirement to report in alignment with the EU's Taxonomy) in relation to their financial years commencing in 2024. The Corporate Sustainability Due Diligence Directive (CSDDD), which was politically agreed by the European Union in December 2023, also likely will be formally published in early 2024, and in-scope companies will need to begin assessing how the Directive may impact them.

In addition, the International Sustainability Standards Board (ISSB), which issued its inaugural voluntary global sustainability disclosure standards in 2023, is poised to play a more important role in the ESG reporting space, with jurisdictions including Australia, Canada, Hong Kong, Japan, Malaysia, New Zealand, Nigeria, Singapore, and the United Kingdom, among others, expressing their intent to adopt the ISSB standards in national law. The

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US Securities and Exchange Commission's (SEC) 2024 regulatory agenda includes the finalization of its proposed climate disclosure regulation and ESG funds rule, as well as other ESG-related proposed rulemaking such as human capital management and board diversity.

And yet, in the United States, California arguably beat the SEC to the punch, passing a suite of climate-related disclosure laws in 2023 that come into effect between 2024 and 2026 and require similar, albeit slightly different, disclosures as the SEC's proposal. Beyond climate and sustainability-specific obligations, rules regarding sustainable finance, anti-greenwashing, and investment labels,[1] rules regarding human rights and labor considerations in value chains,[2] and emerging regulatory expectations regarding deforestation, biodiversity, and waste reduction are all positioned to make an impact in 2024.

## 2. Additional Regulatory Developments, Including Regulation That Applies to Private Companies, Likely Will Result in Increased Enforcement and Litigation, Including Company-versus-Company Claims

On the heels of this coming wave of regulation, we also anticipate a rise in ESG-related enforcement and litigation. While 2023 brought an increase in climate- and greenwashing-related enforcement and litigation, the full extent of ESG-associated disputes likely will only begin to emerge once the breadth of anticipated ESG regulation comes into force.

Moreover, while certain ESG and sustainability-related regulation is specifically focused on publicly listed companies, a significant number of regulatory developments apply to private companies. With emerging regulations requiring companies to gather information from business partners, the litigation potential is significant, including company-versus-company litigation, as organizations increasingly depend on each other to provide ESG-related data and build bespoke provisions into private contracting to address future regulatory requirements.

While to date, many of the ESG-related cases brought against companies have been initiated by governmental or regulatory bodies or by activist groups, the increase in ESG-related regulation, including regulation that focuses on companies' value chains, will likely result in more private litigation.

## 3. In the Midst of an Unprecedented Election Year and Rising Global Tensions, Companies Will Increasingly Need to Use Discretion and Sophistication to Inform Their ESG Strategies

2024 will bring elections to approximately half of the world's population, including in the United States, India, the European Union, and, in all likelihood, the United Kingdom. The outcome of those elections will have long-term implications on global economies, conflicts, trade negotiations and policies, and energy prices, and will therefore directly influence how ESG develops in the United States and globally. The US presidential election will likely further highlight political divides in the United States and the West more broadly, and companies may increasingly get caught in the crossfire.

2023 brought increased fragmentation among US states' approaches to ESG legislation and regulation, with California adopting climate change disclosure legislation at the same time Florida, Idaho, Kansas, and Texas pushed back on a range of ESG-related matters, including through legislation and actions by their attorneys general. More than half of US states have now adopted pro- and/or anti-ESG legislation or regulation, or taken another ESG-related action.

At the federal level, the Biden administration continued to move in the opposite direction of the prior administration.[3] At the same time, the US Supreme Court's June 2023 ruling in *Students for Fair Admissions v. Harvard* that universities can no longer consider race in admissions decisions has resulted in significant activism and litigation against

companies and other organizations, notwithstanding the relatively limited scope of the Court's decision. These diversity-related developments, which have involved a range of claims, are likely to continue in 2024 and beyond.

However, 2024 will bring more than the US presidential elections and ESG tensions and activism in the United States. The continued conflicts between Russia and Ukraine and in the Middle East, as well as presidential, general, and state elections happening throughout the world, are likely to weigh into ESG world developments as well as corporate priorities. And an increased appreciation of the truly global nature of ESG developments and risks is likely one of the lessons 2024 has for us. These developments present uncertainties which could result in ESG regulatory developments and complexity and affect the broader economic and commercial landscape in which entities operate.

## 4. Corporate ESG Goals and Board Oversight of ESG Will Likely Come under Increased Pressure and Become Subject to Enhanced Stakeholder Scrutiny

A majority of Forbes Global 2000 companies have made significant climate commitments.[4] 2024 represents an important year, as it is the final period before many climate-related pledges are due in 2025—a situation which is unprecedented in global history. In addition, for companies with 2030 goals, 2024 might be the first year in which they begin to analyze the degree to which their ambitious targets are in fact achievable. With the rise in mandatory regulatory requirements, companies may find that they are required to publicly assess and report more detail on the "how" associated with their goals sooner than they originally anticipated.

For example, California's new law CA AB 1305 requires certain companies to provide details on how "interim progress" toward a net zero, carbon neutrality, or other greenhouse gas reduction claim or target is being measured, and thus as a practical matter, what those interim goals are and how they were set. CSRD also establishes reporting requirements for those that have set public ESG goals.

During the 2024 proxy season, we expect companies to continue to place an emphasis on board oversight of ESG matters. This is in part due to the SEC universal proxy rules potentially making it easier for organized and well-funded shareholder groups to seek board seats or advance their agendas via threatened or actual proxy fights based on isolated ESG topics. To foster effective board oversight, companies may want to consider how to appropriately weigh ESG topics that are important to their investors (and potentially other stakeholders, including employees). Messaging of ESG oversight and director skills will also likely be a focus of attention in 2024.

## 5. Artificial Intelligence Will Be More Central in Organizations' ESG Considerations and Regulators' Priorities

Regulators around the globe, including the European Union, the United States, the United Kingdom, Japan, and Israel, are applying existing authority to adopt laws and regulations affecting artificial intelligence (AI). As relevant to ESG, this regulatory activity will impact AI governance and how companies evolve and demonstrate their AI practices.

In 2023, we saw many governments pass laws or take other actions to address the various ethical and social risks posed by AI, acknowledging that irresponsible use of AI could exacerbate social harms such as discrimination, bias and disinformation, and displacement of workers. In 2024, we expect increased focus, including additional guidance and regulations.

For instance, in October 2023, US President Biden issued an executive order (EO) addressing the safety and security of AI, stating that the US federal government "will enact appropriate safeguards against [. . .] unintended bias, discrimination [. . .] and other harms from AI."[5] The EO ordered various federal agencies to ensure that their use of AI,

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and use by their respective regulated entities, address algorithmic discrimination. Further, the EO directs the US Secretary of Labor to publish by April 2024 principles with specific steps for employers to take with regard to job evaluations, health and safety implications of AI in the workplace, and implications for workers of employers' AI-related collection and use of their data.

Some companies already are disclosing their use of AI, and how their models are trained. In addition, there has been an increase in the number of public company AI risk factors in Annual Reports on Form 10-K filed in 2023. We expect more AI risk factors, including those disclosing these social and ethical risks—and board oversight thereof—in the 2024 10-K, and proxy season. With this backdrop, 2024 will likely usher in more laws and guidance addressing the use of AI.

## 6. While Many ESG Legal Developments to Date Have Been in Europe and North America, Developments Worldwide Will Require Businesses to Focus on ESG More Than Ever, Including in Their Value Chains

Over the past decade, ESG regulation has often been focused on developments in Europe and North America. However, that trend is shifting, and will likely continue to shift in 2024 and beyond. 2023 brought a number of developments in Africa, Asia, and South America, including:

- The Johannesburg Stock Exchange (JSE), following the 2022 launch of its first Green Finance Taxonomy, urging South African companies to take action on sustainability in advance of JSE mandating requirements, potentially consistent with the ISSB standards;
- Nigeria announcing that it will be an early adopter of the ISSB standards, with disclosure requirements for Nigerian companies starting as early as 2024;
- Mexico launching the country's Sustainable Taxonomy, and Brazil becoming the first country to adopt the ISSB standards via resolution from its securities and exchange commission;
- Singapore making traction in relation to sustainable finance and launching a public consultation regarding potentially aligning with ISSB standards;
- Hong Kong proposing enhanced ESG disclosures;
- China adopting a range of ESG developments and transitioning its energy system;
- South Korea introducing new guidelines regarding ESG ratings and greenwashing;
- India releasing new rules for ESG investment funds; and
- Australia consulting on national sustainability standards, the consultation of which will heavily leverage the ISSB standards.

As the ESG regulatory tapestry continues to expand, the global ESG policy makers are likely to take into consideration a broader range of ESG perspectives, including just transition and climate reparations. Calls for understanding the need for a plurality of energy transitions—where the transitions of different regions and industries proceed at different speeds—including at COP29, are likely to increase as the ESG and sustainability conversation includes a broader range of global perspectives.

## 7. Cross-Border Considerations Will Add Pressure on Companies to Have Greater Visibility and Produce Greater Transparency with Respect to Their Value Chains

Previously, we predicted that value chain transparency and the navigation of value chain risks would become an increasing focus in 2023.[6] Not only did that increased focus materialize in 2023, it arguably has paved the way for these matters to become even more significant in 2024 and beyond.

While CSDDD gets a lot of the attention in the value chain sustainability regulatory space, it is by no means the only emerging regulation that demands

companies to have greater visibility into, and produce greater transparency with respect to, their value chains. Among the other regulations and requirements likely to have the biggest impact in 2024 and beyond are Germany's Supply Chain Due Diligence Act, the Uyghur Forced Labor Prevention Act in the United States, and the new EU Deforestation Regulation, which will begin to apply to companies from the end of 2024.

However, in addition to law and regulation that is focused on value chain sustainability, end consumers have become increasingly focused on the provenance of the goods and services they purchase. Also, companies and corporate value chains, including supply and shipping considerations, may be forced to navigate complex challenges, as trade routes and trade policy face new and evolving global political disputes. As more requirements, investors, and customers focus on these matters, companies are likely to navigate them through a combination of re- or near-shoring, data access and monitoring technology, and liability and risk shifting.

## 8. The Business of ESG Will Become Busier, and Increasingly the Focus of Regulation and Trade Policy

ESG rating agencies, consultancies, data companies and platforms, and technology companies, as well as legal, accounting, and auditing teams are all poised to become busier as more mandatory requirements come into effect. The growing diversity of perspectives on ESG is likely to increase the appetite for expertise, as companies choose to outsource this compliance burden. Companies and funds will look to revisit their investor base and accommodate all ESG viewpoints. More regulatory focus on the carbon markets—including carbon pricing, the quality and use of offsets, and other carbon market mechanisms[7]—is likely to impact how companies plan for net zero, carbon neutrality, or other commitments to reducing greenhouse gas emissions.

In addition, with the European Union and other jurisdictions increasingly looking to regulate ESG rating providers, organizations that rely on ESG ratings should consider the degree to which such reliance is informed and transparent. These trends (as well as those discussed above and below) are pushing companies in the same direction—toward more robust verification of their ESG initiatives and efforts.

## 9. Greenwashing Scrutiny, Regulation, and Litigation Will Continue, While Some Will Question Where the Line Is with Respect to Permissible Marketing Efforts

In 2023, regulators and legislators worldwide passed regulations to curb greenwashing. Noteworthy examples include the SEC's September 2023 Names Rule amendments, the UK Financial Conduct Authority's (FCA) December 2023 final rules on sustainability disclosures and investment labelling, and the EU's amendments to the Unfair Commercial Practices Directive and potential amendments to the Sustainable Finance Disclosure Regulation (SFDR). In addition, the SEC continues to issue comment letters on registrants' climate change disclosures and focus on the substantiation of ESG claims in fund marketing and other materials.

Several high-profile greenwashing enforcement actions, cases, and public criticisms were directed in 2023 against companies for everything from allegations regarding misstatements about ESG investments to claims regarding sustainable fuels and consumer products. During 2024 and beyond, the US Federal Trade Commission is poised to update its "Guides for the Use of Environmental Marketing Claims," commonly known as the Green Guides, which are incorporated by reference in various US state consumer protection laws. Cross-jurisdictional differences in greenwashing standards may also result in increased risks, as companies' global claims and advertisements come under increased scrutiny.

With greenwashing allegations on the rise, some businesses took more nuanced approaches in 2023 to their ESG-related efforts, initiatives, and disclosures.

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However, the volume of ESG and sustainability-related claims and disclosures to date, as well as regulatory appetite to adopt and enforce ESG-related regulation, means that greenwashing allegations and fallout are likely to continue for the foreseeable future.

## 10. The "Green Beyond Climate" Space, Including the Focus on Natural Capital, Seems Poised to Continue to Grow and Attract Both Capital and Regulation

In September 2023, the Taskforce on Nature-Related Financial Disclosures (TNFD) released its final framework. Styled similarly to the Task Force on Climate-Related Financial Disclosures (TCFD), which is now widely adopted by companies voluntarily and worked into regulatory regimes, the TNFD framework focuses on nature, as opposed to the TCFD framework's focus on climate. Biodiversity and natural capital reporting requirements have also been adopted by a number of jurisdictions in recent years, including by France in 2021, through the adoption of a new biodiversity agreement at COP15 in 2022, and in one of the European Sustainability Reporting Standards (ESRS) which includes a number of biodiversity and ecosystems-related disclosure requirements for entities subject to the CSRD.

In addition to these developments and the EU Deforestation Regulation mentioned above, other "green" areas coming into focus include circular economy and waste considerations.[8] This increased focus by regulators and investors on "green" areas beyond climate is likely to continue into 2024 and beyond. These developments are arguably further buttressed by the regulatory interest in value chain sustainability and integrity.

## Conclusion

If there is one certainty in ESG, it is change. 2024 will bring predictable and unpredictable events, some of which will surely alter the ESG landscape permanently. To successfully navigate this increasingly complex and varied space, companies may want to consider steps such as adopting more integrated and nuanced approaches to ESG, including by identifying internal ownership, building internal controls, establishing budgets for outside expertise, and mapping cross-jurisdictional regulatory requirements.

Understanding the ESG implications of business relationships may become increasingly important, as will internal training and coordination. As ESG and the nature of the conversations on ESG issues continue to evolve, the organizations that approach environmental and social risks and opportunities with a balance of creativity, curiosity, and strategic focus, while listening to a diversity of stakeholder perspectives, are likely to best navigate ESG and the challenges and questions it poses.

### Notes

1. Such as the UK Financial Conduct Authority's Sustainability Disclosure Requirements, the EU's proposed revision of SFDR, and the SEC's proposed ESG disclosures for investment advisers and investment companies.
2. Including Canada's recently enacted Modern Slavery Act and similar existing laws in the United States, United Kingdom, and Australia.
3. For example, the February 2023 Labor Department rule clarifying when fiduciaries can consider ESG factors when evaluating plan investments continues to be subject to court and potential congressional challenge, and the Environmental Protection Agency announced at COP28 in Dubai a final rule regarding methane and other air emissions reduction.
4. Net Zero Tracker announced in November 2023 that the 1000th company among the Forbes Global 2000 had set a net zero target, with many other Forbes Global 2000 establishing significant GHG reduction targets.
5. White House, Executive Order on the Safe, Secure, and Trustworthy Development and Use of Artificial Intelligence (Oct. 30, 2023) available at *https://www.whitehouse.gov/briefing-room/presidential-actions/2023/10/30/executive-order-on-the-safe-secure-and-trustworthy-development-and-use-of-artificial-intelligence/*.

6. *See* our article at *https://www.globalelr.com/2023/01/esg-insights-10-things-that-should-be-top-of-mind-in-2023/*.
7. For example, the EU's Carbon Border Adjustment Mechanism and the pending US PROVE It Act which addresses both greenhouse gas accounting and trade policy.
8. For example, in 2023, the European Union proposed new rules to promote the repair of goods and also made progress on its rules regarding waste from electrical and electronic equipment.

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