HOUSE ESG OVERSIGHT FOCUSES ON PROXY VOTING; ISSUER ATTENTION IS ON CSRD

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INTRODUCTION

Throughout the 118th Congress, the US House of Representatives (House) has remained focused on oversight of environmental, social and governance (ESG) issues. In particular, the House Financial Services Committee (HFSC or the Committee) has led these efforts given its jurisdiction over the Securities and Exchange Commission (SEC), including with respect to non-financial corporate risk disclosure issues. In addition to hosting a number of hearings on the topic, and drafting and approving legislation in Committee targeting various Biden administration ESG-related regulatory projects, Committee Republicans created a House GOP ESG Working Group (Working Group) that recently issued a set of recommendations focused primarily on proxy voting. Other House committees have also engaged in ESG-related oversight and investigations. We anticipate there will continue to be a focus on ESG-related issues during the next Congress, though the direction of that focus will depend on the outcome of the upcoming election. In the meantime, European regulators are moving forward on implementation of the Corporate Sustainability Reporting Directive (CSRD), which becomes effective for large US issuers in 2026.

HFSC ACTIVITY

On Thursday, 1 August 2024, the Working Group, led by Chairman Bill Huizenga (R-MI) and HFSC Chairman Patrick McHenry (R-NC),issued its final staff report entitled "The Failure of ESG: An Examination of Environmental, Social, and Governance Factors in the American Boardroom and Needed Reforms." This report serves as the culmination of a multi-year effort led by Chairman Huizenga delving into various aspects of ESG, which concludes with a set of recommendations focusing on proxy voting issues, shareholder activism, materiality of climate-related financial risk, and the fiduciary duty of investment advisors.

As outlined in the final report, key recommendations identified by the Working Group include:

- "Reform the proxy voting system to safeguard the interests of retail investors.
- Promote transparency, accountability, and accuracy in the proxy advisory system.
- Enhance accountability in shareholder voting by aligning voting decisions with the economic interests of shareholders.

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- Increase transparency and oversight of large asset managers to ensure their practices reflect the pecuniary interest of retail investors.
- Improve ESG rating agency accountability and transparency to safeguard retail shareholders.
- Strengthen oversight and conduct thorough investigations into federal regulatory efforts that would contort our financial system into a vehicle to implement climate policy.
- Demand transparency, responsibility, and adherence to statutory limits from financial and consumer regulatory agencies.
- Protect US companies from burdensome European Union (EU) regulations, safeguarding American interests in global markets."

As part of this continued effort, the HFSC Subcommittee on Oversight and Investigations held a hearing on Tuesday, 10 September 2024, entitled "The Fall of ESG: Scrutinizing the Failed Use of Environmental, Social, & Governance Standards and the Influence of Proxy Advisors," during which Republicans echoed similar sentiments to those outlined in the final report. The Committee also held a hearing on "Oversight of the SEC" on Tuesday, 24 September 2024 in which all five SEC commissioners testified. The SEC's climate risk disclosure rule and other ESG-related issues were key topics of discussion.

HOUSE CONSIDERS ANTI-ESG LEGISLATION ON HOUSE FLOOR

As part of House Republicans' broader anti-ESG efforts, the House considered and passed various anti-ESG bills largely along party lines in September. Due to the partisan nature of these bills, they are not likely to advance in the Democrat-controlled Senate and instead largely serve as messaging bills for Republicans. More information on these bills is available below.

H.R. 3724

Accreditation For College Excellence Act Of 2023

End Woke Higher Education Act

H.R. 3724 was introduced in May 2023 by Rep. Burgess Owens (R-UT), who is running to lead the House Education & Workforce Committee Republicans next Congress. According to his press release, this bill would prohibit accreditors from requiring colleges to meet any "political litmus tests" as a condition of accreditation, such as adhering to diversity, equity and inclusion (DEI) standards. More information is available in the press release here and bill texthere.

H.R. 4790

Guiding Uniform And Responsible Disclosure Requirements And Information Limits (GUARDRAIL) Act Of 2023

Prioritizing Economic Growth Over Woke Policies Act

H.R. 4790 was introduced in July 2023 by Chairman Huizenga. The legislation would require companies to disclose only material information, require the SEC to publicly list and explain any non-material disclosure

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demands, establish a Public Company Advisory Committee within the SEC to enhance investor protection and market fairness, and mandate an SEC study into the potential impacts of the EU's CSRD and Corporate Sustainability Due Diligence Directive (CSDDD). More information on the bill is available here. This legislation is a compilation of four previously introduced Republican bills, which include:

- H.R. 4168, the Mandatory Materiality Requirement Act, originally sponsored by Rep. Huizenga;
- H.R. 4628, a bill to amend the Securities Exchange Act of 1934 to require the Securities and Exchange Commission to disclose and report on non-material disclosure mandates, and for other purposes, originally sponsored by Rep. Alex Mooney (WV-02);
- H.R. 4652, the Public Company Advisory Committee Act, originally sponsored by Rep. Frank Lucas (OK-03); and
- H.R. 4653, the Protecting US Business Sovereignty Act, originally sponsored by Rep. Dan Meuser (PA-09).

H.R. 5339

Roll Back ESG To Increase Retirement Earnings (RETIRE) Act

Protecting Americans' Investments From Woke Policies Act

H.R. 5339 was introduced by Rep. Rick Allen (R-GA) in September 2023. According to his press release, this bill would "require Employee Retirement Income Security Act (ERISA) retirement plan sponsors to prioritize financial returns over environmental, social, and governance, or ESG, factors when making investment decisions on behalf of their clients." The introduction of this legislation came after the Department of Labor (DOL) finalized a rule, entitled *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights*, which allows retirement plan fiduciaries to consider ESG factors when selecting investments. More information on the bill is available here.

LOOKING AHEAD

The extent of future efforts on ESG-related policy issues will likely depend upon the outcome of the pending federal election. The new administration and congressional leadership will face a busy policy agenda during the 119th Congress, and will work quickly to outline policy priorities that may include the economy and inflation, geopolitical conflicts, the upcoming expiration of key provisions of the Tax Cuts and Jobs Act, federal funding, addressing the federal debt limit, and more.

Despite this long list of legislative priorities, we expect that ESG may continue to be a priority amongst whichever party takes control of the White House, Senate and House. In the event that former President Donald Trump is elected, his administration would likely work to overturn Biden administration policies at the SEC, including the climate risk disclosure rule and the Department of Labor ESG guidance, whereas Vice President Kamala Harris, if elected, would likely double down on Biden administration policies and work to enact other ESG-related rules that have been pending, such as the SEC human capital disclosure rules. On the congressional side, if Democrats win control of the House, HFSC Ranking Member Maxine Waters (D-CA) is expected to regain the Committee gavel and would likely revitalize her focus on climate-related financial risks as well as DEI issues. If Republicans take

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control of the Senate, Ranking Member Tim Scott (R-SC) would likely win the gavel of the Senate Banking Committee and would likely focus on capital formation, oversight of federal regulators, and other issues unrelated to ESG.

Regardless of the outcome of the 2024 elections and subsequent regulatory or legislative efforts relating to ESG issues, the growing investor need for standardized and comparable disclosure of financially material risks, including climate-related risks, will persist. Therefore, many large US issuers are likely to continue to enhance their sustainability disclosures in accordance with standards issued by the International Sustainability Standards Board (ISSB) and the Global Reporting Initiative (GRI) as an investor relations imperative. ISSB standards generally relate to financial risks, while GRI standards generally apply to impacts or externalities, or what is referred to in Europe as "double materiality." Such standards can help guide American companies in fulfilling their emerging disclosure obligations in foreign and domestic jurisdictions which increasingly are mandating such disclosures as a condition of market access. Questions relating to substituted compliance and mutual recognition between regulatory regimes are subject to negotiation and are likely to be coordinated by the International Organization of Securities Commissions (IOSCO), which has endorsed the ISSB's standards. Importantly, the European Financial Reporting Advisory Group (EFRAG) is expected to propose standards for non-EU companies that are not already subject to CSRD in the first quarter of 2025. US issuers who are likely to be impacted should consider commenting.

Finally, last month the European Commission released a report entitled, "The Future of European Competitiveness," led by former President of the European Central Bank and former Italian Prime Minister, Mario Draghi. The report contains a candid assessment of European economic challenges and reviews the structural impediments to creation of the EU Capital Markets Union (CMU). The report makes a series of recommendations for maintaining European global competitiveness including, among others, a call to "take a new stance towards cooperation: in removing obstacles, harmonising rules and laws, and coordinating policies." It is against this backdrop that negotiations among global securities regulators about equivalence regimes for sustainability risk disclosures begins.

RELATED RESOURCES

As such, we expect to see continued legislative, regulatory, and oversight efforts related to ESG on both sides of the aisle, as well as internationally, though the scope of such efforts will largely remain unclear until after the upcoming election. Our firm has been and is well positioned to continue assisting clients in navigating this rapidly changing ESG policy landscape. To learn more about the current state of ESG in American public policy, as well as the firm's role in this space, please visit our previous publications, including:

- "SEC Issues Long-Awaited Climate Risk Disclosure Rule";
- "The EU CS3D Trilogue Nears Conclusion";
- "California Enacts Landmark ESG Legislation";
- "GOP ESG Bills Await US House Floor Consideration";
- "The ESG Debate Heats Up: State AGs Investigating Asset Manager Involvement in ESG Initiatives and Related Proxy Voting";

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- "ESG Investing and Proxy Voting: DOL's New Final Rule";
- "SEC Adopts Final Rule Requiring Additional Proxy Voting Disclosures";
- "Déjà Vu All Over Again: SEC Reverses 2020 Proxy Rules Changes and Proposes Shareholder Proposal Rule Changes";
- "SEC Takes First Step Toward Standardized ESG Disclosures for Funds and Investment Advisers";
- "SEC Issues Climate-Related Risk Disclosure Rule Proposal";
- "2023 ESG State Legislation Wrap Up"; and
- "Biden Administration ESG Activity Accelerates."

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