

Navigating the Shifting ESG Landscape: Risks and Strategy

We are entering a dramatically changing world for ESG, marked by policy reversals under the Trump administration along with delays and scrutiny of proposed EU ESG legislation. Companies now face challenges on multiple fronts: adapting to political changes, ensuring regulatory compliance, mitigating litigation risks, and navigating international laws.

Changing Political Dynamics in the U.S. and EU

Recent years have seen many countries adopt or consider new ESG regulations, shifting ESG from the voluntary domain to the mandatory. In the present political climate, this shift presents challenges for companies planning for future ESG regulation, notably in the U.S. and EU.

In the U.S., the Trump administration and certain States are adopting an “anti-ESG” stance. Since taking office, President Trump has withdrawn from the Paris Agreement, reversed the Biden administration’s climate policies, and rolled back DEI programs.

Meanwhile, there are concerns that the EU may have pushed too far, too fast on ESG. To balance ESG regulation with EU competitiveness, the European Council seeks to simplify EU ESG reporting by 25%. The EU Commission has proposed an “omnibus” legislative package to streamline the Corporate Sustainability Reporting Directive, the Taxonomy Regulation and the Corporate Sustainability Due Diligence Directive. This included significant changes, such as removing 80% of companies from sustainability reporting requirements, postponing implementation deadlines, and introducing simplified reporting, especially for SMEs.

Companies should strengthen ties with industry groups and their advisers to stay informed on regulatory developments, develop market-standard approaches, and engage with regulators and stakeholders. For example, the one-year delay in the EU Deforestation Regulation's implementation was partly due to industry groups' concerns about readiness for the regulation.

Expansion of ESG-related Regulation

Despite uncertainties in the ESG landscape, businesses must navigate the rise of ESG-related laws globally. From a legal perspective, general counsel face three key hurdles:

- **Identifying applicable laws.** Determining the applicability of ESG laws can be complex, as it may vary by jurisdiction, product-type and industry. This is particularly challenging for global companies requiring detailed analysis of subsidiaries’ operations and financials.
- **Steps for compliance.** Legal counsel must translate laws into practical steps for the company, and secure buy-in across business functions, typically from the board of directors’ level and downwards.
- **Balancing priorities and deadlines.** Managing checklists and deadlines for different laws requires effective project and time management. Companies must allocate resources and plan for compliance with both immediate and distant deadlines, as compliance often takes time to achieve.

Rising Tide of Litigation Risks

ESG-related litigation is rising globally, with plaintiffs often succeeding against companies. To avoid its proven negative impact on economic value and reputation, companies face a three-pronged challenge:

- **Avoiding greenwashing.** Most ESG litigation stems from allegedly false or misleading statements about companies' environmental impact or practices. Examples include vague or exaggerated statements about environmental practices, carbon neutrality or net-zero emissions; claims lacking evidence or inconsistent with the company's business model; and claims based on controversial offsetting mechanisms.
- **Complying with stated ESG objectives and standards.** Companies also face scrutiny for lacking ESG commitments, or failing to meet stated goals. Recent cases pertain to inadequate environmental targets, misalignment of the business model with international climate commitments, and supply chain abuses.
- **Balancing ESG goals with stakeholder interests.** The growing "anti-ESG" movement, rooted in the U.S., targets companies with ESG goals such as climate transition. Recent examples include an action brought by U.S. state attorney general against major asset managers for allegedly disrupting the energy market by citing their climate commitments to compel companies to cut coal production.

To mitigate these risks, companies should consider:

- **Monitoring global ESG litigation.** Cases in one jurisdiction can inform similar actions elsewhere (e.g., a complaint in Australia against Qantas concerning its climate goals relied on the rationale of a Dutch Court's ruling against KLM).
- **Consistency and transparency in ESG goals or actions,** ensuring alignment with the company's business model, stakeholder expectations, and best practices. Progress and challenges should be communicated transparently and regularly.
- **Establishing internal systems and controls** to monitor, review, and approve all ESG-related advertisements and communications (including sustainability reports and webpages), ensuring they are unambiguous, verifiable, and compliant with regulations.

International Law Overlay

Corporate ESG policies are shaped by complex international legal frameworks, which also present companies with challenges. For instance, national laws often incorporate international standards, like the EU's ESG due diligence laws: the CS3D, the Batteries Regulation, and the Anti-Forced Labour Regulation. These laws require companies to adhere to various soft and hard norms of international law, such as international human rights and environmental conventions. The ESG due diligence procedures in these laws are often derived from international instruments like the UN Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises, which themselves allow complaints against companies for supply chain abuses.

Decisions from international judicial bodies, such as the European Court of Human Rights and the International Tribunal for the Law of the Sea, also shape the law by clarifying obligations, which can result in new domestic regulations or lawsuits affecting corporate policies.

Companies should monitor evolving trends in national and international ESG law and litigation to understand how the law will be developed, interpreted and applied. This helps in preparing for

compliance across jurisdictions without incurring penalties or significant costs. Additionally, companies should actively engage with domestic governments and industry groups to ensure their concerns are considered in developing regulations and best practices.

Authors

Nicolas Lockhart

Leonard Ng

Heather Palmer

Katie Chin

Shambhavi Pandey