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The Origins and Consequences of the ESG Moniker

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THE ORIGINS AND CONSEQUENCES OF THE ESG MONIKER

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ESG is one of the most notable trends in corporate governance, management, and investment of the past two decades. Yet few observers know where the term comes from, who coined it, and what it was originally aimed to mean and achieve. As trillions of dollars have flowed into ESG-labeled investment products, and companies and regulators have grappled with ESG policies, a variety of usages of the term have developed that range from seemingly neutral concepts of integrating "environmental, social, and governance" issues into investment analysis to value-laden notions of corporate social responsibility or preferences for what some have characterized as "woke capitalism."

This Article makes three contributions. First, it provides a descriptive account of the history of the term ESG that was coined without precise definition in a collaboration between the United Nations and the financial industry to pursue wide-ranging goals. Second, it identifies and examines the main usages of the term ESG that have developed since its origins. Third, it offers an analytical critique of the term ESG and its consequences. It argues that the combination of E, S, and G into one term has provided a highly flexible moniker that can vary widely by context, evolve over time, and collectively appeal to a broad range of investors and stakeholders. These features both help to account for its success, but also its challenges such as the difficulty of empirically showing a causal relationship between ESG and financial performance, a proliferation of ratings that can seem at odds with understood purposes of the ESG moniker or enable "sustainability arbitrage," and tradeoffs that cannot be reconciled on their own terms. These challenges give fodder to critics who assert that ESG engenders confusion, unrealistic expectations, and greenwashing that could crowd out other solutions or inhibit accountability. These critiques are not necessarily fatal for the continued embrace of ESG, but can be understood to be intertwined with the characteristic flexibility and unfixed definition of ESG that was present from the beginning and will likely to continue into the future.

Keywords: environmental, social and governance, ESG, sustainability, corporate social responsibility, corporate governance

JEL Classification: G20, G28, G30, G34, K20, L21

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INTRODUCTION

ESG is at the center of global dialogue on corporate governance, management, and investment. Remarkably, it has "risen from an obscure and niche concept to a widely used term around the world."[1] As the creation and uptake of the term ESG took place gradually, then suddenly, its ubiquity has given way to assumptions that "everyone understands what they are referring to."[2]

ESG as an acronym for "environmental, social, governance" is a common denominator of the discourse using the term, but a deeper examination reveals that little beyond that understanding is fixed. The word that follows the famous refrain of "environmental, social, governance" shapeshifts from "criteria" to "factors," "standards," "strategies," "risks," "issues," "activity," or even "goals." Does ESG refer to "three criteria to evaluate a company's sustainability performance"?[3] Is it a "set of standards for a company's operations that socially conscious investors use to screen potential investments"?[4] Does it "put . . . money to work with companies that strive to make the world a better place"?[5] Or perhaps more broadly is it a new term or synonym for "corporate social responsibility" (CSR) or its cousin "sustainability"? Could the answer be that ESG simultaneously refers to all of the above?

As usage of the term ESG runs the gamut, trillions of dollars flow into ESG-labeled investment products, companies are implementing ESG strategies, and regulators are designing ESG policies. Views about the performance implications from ESG and the usefulness of ESG evaluations grow increasingly polarized – for some, ESG is seen to have enormous influence on corporate and

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[1] George Serafeim, *ESG: Hyperboles and Reality*, Harvard Business School Research Paper Series Working Paper 22-031 (Dec. 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3966695.
[2] *Id.* at 2.
[3] Alyce Lomax, *What is ESG Investing & What Are ESG Stocks?*, THE MOTLEY FOOL (May 2, 2022), https://www.fool.com/investing/stock-market/types-of-stocks/esg-investing/.
[4] Environmental, Social, Governance (ESG) Criteria, INVESTOPEDIA (Feb. 23, 2022), https://www.investopedia.com/terms/e/environmental-social-and-governance-esg-criteria.asp.
[5] E. Napoletano & Benjamin Curry, *Environmental, Social And Governance: What is ESG Investing?*, FORBES (Feb. 24, 2022), https://www.forbes.com/advisor/investing/esg-investing/.

investor behavior, for others it has none,[6] or worse it is greenwashing that misleads investors or stakeholders, inhibits corporate accountability, or crowds out other concepts and proposed solutions. Popular use of the term ESG has even seemed to take on some of these normative views or culture-laden notions that transcend technical ideas of investment screens, impact reporting, or the like. In common parlance, one regularly hears things such as "startups need ESG,"[7] buying a certain asset class such as gold is "not very ESG"[8] or that companies can "be" or "not be" ESG.[9] More colorfully, tech billionaire Elon Musk has exclaimed: "I am increasingly convinced that corporate ESG is the Devil Incarnate."[10]

As varied language and notions around ESG proliferate, this Article endeavors to provide an in-depth examination of the term itself and its implications. Although commonly used, few know where the term comes from, who coined it, and what it was originally aimed to mean and achieve. The first contribution of the Article is thus to provide a descriptive account of the history of the term ESG.[11]

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[6] Serafeim, *supra* note 1, at 2.

[7] Edward Robinson, *Startups Need ESG*, QUARTZ (Jan. 17, 2022), https://qz.com/emails/quartz-forecast/2113257/%E2%9C%A6-do-startups-need-esg/.

[8] *See, e.g.*, Oliver Telling, *ESG's Dirty Secret: Is Do-Good Investing Profitable, Or Even Doing Good?*, INVESTORS' CHRONICLE (Mar. 18, 2021), https://www.investorschronicle.co.uk/news/2021/03/18/esg-s-dirty-secret/ (quoting commentary that gold is "not very ESG").

[9] *See, e.g.*, Alan R. Palmiter, *Capitalism, Heal Thyself*, Wake Forest University School of Law Working Paper (Dec. 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3940395 (examining the "effect of being ESG" and the "effect of not being ESG" for companies); David F. Larcker, Brian Tayan & Edward M. Watts, *Seven Myths of ESG*, Stanford Closer Look Series (Nov. 4, 2021), https://www.gsb.stanford.edu/faculty-research/publications/seven-myths-esg (observing "we cannot always tell whether an initiative is truly ESG").

[10] @elonmusk, Twitter (Apr. 2, 2022, 10:14 PM), https://twitter.com/elonmusk/status/1510485792296210434. The tweet came in reply to one by prominent venture capitalist Marc Andreessen, who perhaps sardonically noted in response to a comparison of energy usage by clothes dryers in the U.S. and bitcoin mining that "Dirty clothes are ESG." *Id.*

[11] *See* Part I infra. Scholarly literature to date has not focused on the history of ESG as such, but descriptions of coinage of the term through United Nations initiatives can be found in Dorothy S. Lund & Elizabeth Pollman, *The Corporate Governance Machine*, 121 COLUM. L. REV. 2563 (2021) (providing an original descriptive account of the "complex governance system in the United States composed of law, institutions, and culture that orients corporate decisionmaking toward shareholders"), and Mariana Pargendler, *The Rise of International Corporate Law*, 98 WASH. U. L. REV. 1765 (2021) (arguing that "international corporate law" is a solution to "interjurisdictional externalities" and "political capture by domestic interest groups").

As the term spreads from its origins and takes on diverse meanings, the potential arises for confusion, unrealistic expectations, and co-optation to serve different goals. More simply, conversants in the debate about ESG might simply talk past each other as they use the term to refer to different concepts. The second contribution of the Article is to identify and examine the main usages that have developed over time. Specifically, it argues that ESG was coined to describe a set of issues that should be integrated into enhanced financial or investment analysis, and has taken on meanings related to risk management, been treated as a synonym or subset of CSR or sustainability, and characterized as a preference or activity. It has taken on connotations both positive and negative, as value-laden notions of "conscious" versus "woke" capitalism give way to perceptions of ESG as ideological, political, and subject to backlash.

Finally, as the term has now been in circulation for nearly two decades, it is time for an accounting of the promise and perils of putting E, S, and G together in one moniker. The third contribution of the Article is therefore an analytical critique of the term ESG and its consequences. It argues that the combination of E, S, and G into one term has provided a highly flexible moniker that can vary widely by context, evolve over time, and collectively appeal to a broad range of investors and stakeholders. These features both help to account for its success, but also its challenges such as the difficulty of empirically showing a causal relationship between ESG and financial performance, the proliferation of ratings that can seem at odds with understood purposes of the ESG moniker or enable "sustainability arbitrage," and tradeoffs that cannot be reconciled on their own terms. These challenges give fodder to critics who assert that ESG engenders confusion, unrealistic expectations, and greenwashing that could crowd out other solutions or inhibit accountability. Such critiques are not fatal for the continued embrace of ESG, but will likely endure as they are intertwined with the characteristic flexibility and unfixed definition of the term ESG.

The Article proceeds as follows. Part I tells the story of how ESG was coined and the strategic considerations and goals of doing so. Part II examines how various actors use the term with varied meanings today. Part III analyzes the consequences – perhaps intended and unintended – of attempting to address such a wide range of issues under one moniker.

I. The Creation and Diffusion of the ESG Moniker

The consideration of corporate governance and corporations' relationships with stakeholders, communities, the environment, and society writ large has a long history. Corporations and their role in society and purpose have been the subject of perpetual debate, going back to early corporations.[12] Over the past century, from the famous debate between Professors Adolf Berle and Merrick Dodd,[13] to the coining of the term "corporate social responsibility" in the mid-twentieth century,[14] and the rise

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[12] For an exploration of the history of corporate purpose through the purpose clause of charters from the Middle Ages to the twenty-first century, see Elizabeth Pollman, *The History and Revival of the Corporate Purpose Clause*, 99 TEX. L. REV. 1423 (2021). For a sampling of contemporary literature adding to the rich history of "corporate purpose" debate, *see, e.g.*, Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 CORNELL L. REV. 91, 94 (2020) (arguing against "the flaws and dangers" of "stakeholder governance"); Jill E. Fisch & Steven Davidoff Solomon, *Should Corporations Have a Purpose?*, 99 TEX. L. REV. 1310, 1310 (2021) (arguing that corporate purpose serves an "instrumental function" to "facilitate the goals of corporate participants"); Edward Rock, *For Whom Is the Corporation Managed in 2020?: The Debate over Corporate Purpose*, 76 BUS. L. 363, 364-67 (2021) (summarizing the contemporary corporate purpose debate including statements and proposals from academics, business leaders, and politicians); Leo E. Strine, Jr., *Restoration: The Role Stakeholder Governance Must Play in Recreating a Fair and Sustainable American Economy: A Reply to Professor Rock*, 76 BUS. L. 397, 400 (2021) (arguing that the American corporate governance system "needs an overhaul to fit a 21st century economy"); COLIN MAYER, PROSPERITY: BETTER BUSINESS MAKES THE GREATER GOOD 6 (2019) (discussing corporate purpose in terms of fulfilling business objectives rather than maximizing profits and noting related social and moral values in corporate purpose); The British Academy, *The Future of the Corporation: Principles for Purposeful Business* (Nov. 2019), https:// www.thebritishacademy.ac.uk/publications/future-of-the-corporation-principles-for-purposefulbusiness/ (examining the case for reforming business "around its purposes, trustworthiness, values and culture" and solving the problems of "people and planet").

[13] Adolf A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049 (1931); E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145 (1932); Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365 (1932).

[14] HOWARD R. BOWEN, SOCIAL RESPONSIBILITIES OF THE BUSINESSMAN 6 (1953). For literature tracing the history of corporate social responsibility, see Archie B. Carroll, *A History of Corporate Social Responsibility: Concepts and Practices*, *in* THE OXFORD HANDBOOK OF CORPORATE SOCIAL RESPONSIBILITY 19, 25 (Andrew Crane, Dirk Matten, Abagail McWilliams, Jeremy Moon & Donald S. Siegel eds., 2008); Ming-Dong Paul Lee, *A Review of the Theories of Corporate Social Responsibility: Its Evolutionary Path and the Road Ahead*, 10 INT'L J. MGMT. REVS. 53 (2008); Eric C. Chaffee, *The Origins of Corporate Social Responsibility,* 85 U. CIN. L. REV. 347 (2017); Mauricio Andres Latapi Agudelo, Lara Jóhannsdóttir & Brynhildur Davidstóttir, *A Literature Review of the History and Evolution of Corporate Social Responsibility*, 4 J. CORP. SOC. RESP. 1 (2019); Elizabeth Pollman, *Corporate Social Responsibility, ESG, and Compliance*, *in* THE CAMBRIDGE HANDBOOK OF COMPLIANCE 662 (Benjamin van Rooij & D. Daniel Sokol eds., 2021).

of "corporate governance" and its linkage with shareholder primacy,[15] the discourse and engagement with various questions related to the societal role of corporations, the duties of corporate directors, and externalities and impacts on stakeholders have taken many twists and turns.

This Part aims its focus at providing a descriptive account of the specific history of the term ESG and its diffusion in the early twenty-first century. Although the United Nations (UN) does not typically feature in contemporary discussions of ESG, it played a critical role in bringing about the term and mobilizing its spread.[16] The story begins with this international organization and its eventual connection and responsiveness to senior executives of global financial institutions, followed by a host of related initiatives and efforts that helped to spread the term until it reached rapid uptake in mainstream discourse.

A. The Foundation for ESG: The United Nations' Shift toward Collaboration with Business and Launch of the Global Compact

Since its founding in 1945, the UN has catalyzed and sponsored a number of initiatives relating to the world economy, development, the environment, human rights, and related issues affecting business and markets. Scholars and experts have recounted the changing tone of engagement between the UN and the business community over the decades. According to John Ruggie, "[h]istorically, UN entities have expressed varying degrees of ambivalence about the market generally and globalization in particular."[17] Earlier in its history, "[t]he UN saw itself as the champion of social justice and distributive policies and viewed the global economic system as more of an impediment than a solution to these ends."[18] Other scholars have explained that "[b]eginning in the 1950s, the UN was prompted

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[15] *See* Lund & Pollman, *supra* note 11, at 2569-78 (tracing coinage of the term "corporate governance" alongside the widespread adoption of shareholder primacy and the shareholder wealth maximization norm).
[16] *See* Pargendler, *supra* note 11, at 1794 ("UN initiatives not only coined the concept of ESG, but also critically mobilized support for the spread and influence of ESG factors around the globe, in addition to the dissemination of a business and human rights agenda more broadly.").
[17] John Gerard Ruggie, *The United Nations and Globalization: Patterns and Limits of Institutional Adaptation*, 9 GLOBAL GOV. 301, 303 (2003).
[18] *Id.*

to keep its distance from the corporate sector by the Cold War environment and the need to display a relative impartiality toward market economy and planned economy advocates alike."[19] An "antibusiness prejudice,"[20] or even "animosity," pervaded "the UN paradigm until the end of the Cold War."[21]

One notable reflection of this oppositional relationship with the private sector was the New International Economic Order (NIEO), a UN effort launched by a coalition of developing countries known as the G-77 that aimed at "structural reform and global redistribution" to aid the "global south."[22] A controversial aspect of the NIEO's platform in the 1970s and early 1980s involved an attempt to regulate transnational corporations.[23] During this time, the "UN systematically defended the notion that the transnationals, left to themselves, would further enlarge the gap between developed and developing countries."[24] And for many years, a Commission on Transnational Corporations, created after the declaration of the NIEO, pursued the drafting and adoption of a Code of Conduct for transnational corporations[25]—an effort that faced significant opposition as anti-business, especially from the United States, and was eventually phased out in 1992 when negotiations were formally suspended.[26] By around this time, various other initiatives were underway that shifted focus, such as the UN-sponsored Brundtland Report on the environment and development, published in 1987 that coined the term "sustainability."[27] The UN Commission (now Council) on Human Rights also

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[19] Jean-Phillipe Thérien & Vincent Pouliot, *The Global Compact: Shifting the Politics of International Development?*, 12 GLOBAL GOV. 55, 57 (2006).
[20] SYDNEY SAMUEL DELL, THE UNITED NATIONS AND INTERNATIONAL BUSINESS ix (1990).
[21] Thérien & Pouliot, *supra* note 19.
[22] *Id.* at 57-58 (discussing how "developing countries entered the organization en masse" in the 1960s and "the rise of the North-South conflict led the UN to make the regulation of the private sector, and of transnational corporations in particular, one of its top development priorities for over a generation"); *see also* Jennifer Bair, *Corporations at the United Nations: Echoes of the New International Economic Order?*, 6 HUMANITY 159, (2015) (discussing the NIEO).
[23] Bair, *supra* note 22, at 159; Ruggie, *supra* note 17, at 303-04.
[24] Thérien & Pouliot, *supra* note 19, at 57-58.
[25] Bair, *supra* note 22, at 159.
[26] *Id.* at 160; *see also* Pargendler, *supra* note 11, at 1795.
[27] REPORT OF THE WORLD COMMISSION ON ENVIRONMENT AND DEVELOPMENT: OUR COMMON FUTURE (1987), https://sustainabledevelopment.un.org/content/documents/5987our-common-future.pdf. An earlier event, the 1972

increased in prominence and became more active in examining how the UN might influence multinational corporations.[28]

Most notably, however, it was in the 1990s that the UN opened up to the corporate sector, described as "a change of 180 degrees."[29] It was in this phase that Koffi Annan, then-Secretary General of the UN, lay the groundwork for the initiative that created the term ESG. Following a meeting with leaders of the International Chamber of Commerce in 1998, Annan acknowledged: "There is great potential for the goals of the United Nations—promoting peace and development—and the goals of business—creating wealth and prosperity—to be mutually supportive."[30] The UN began to set up a host of public-private partnerships during this new period, reflecting a shift toward understanding business as part of the solution for advancing its goals.[31]

The key moment of this shift on the path to ESG was a speech at the Davos World Economic Forum in 1999 in which Kofi Annan proposed a "Global Compact," directly urging business leaders to join the UN in promoting principles that would provide a foundation for a sustainable global economy. The explosive surge in globalization at the end of the twentieth century was accompanied by gaps in global rule making on labor standards, human rights, and environmental protection—in turn feeding fears that a backlash against globalization might grow.[32] Annan explained:

> Globalization is a fact of life. But I believe we have underestimated its fragility. The problem is this. The spread of markets outpaces the ability of societies and their political systems to adjust to them, let alone to guide the course they take. History teaches us that such an imbalance between the economic, social and political realms

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UN Conference on the Human Environment "brought the industrialized and developing nations together to delineate the 'rights' of the human family to a healthy and productive environment." *Id.*

28 Bair, *supra* note 22, at 160.

29 Thérien & Pouliot, *supra* note 19, at 58-59 (quoting Gerd C. A. Junne, *International Organizations in a Period of Globalization: New (Problems) of Legitimacy*, *in* THE LEGITIMACY OF INTERNATIONAL ORGANIZATIONS (Jean-Marc Couicaud & Veijo Heiskanen eds., 2001)).

30 United Nations, Cooperation Between United Nations and Business, press release SG/2043, Feb. 9, 1998.

31 Thérien & Pouliot, *supra* note 19, at 59 (discussing the Global Alliance for Vaccines and Immunizations and the Global Digital Opportunity Initiative as examples of public-private partnerships facilitated by the UN); *see also* Ruggie, *supra* note 17, at 304-05 (discussing the "new consensus" captured by Kofi Annan's articulation of "the need for governments and international institutions alike to forge partnerships with the private sector and a wide range of civil society actors.").

32 Ruggie, *supra* note 17, at 309-10.

> can never be sustained for very long. The industrialized countries learned that lesson in their bitter and costly encounter with the Great Depression. In order to restore social harmony and political stability, they adopted social safety nets and other measures, designed to limit economic volatility and compensate the victims of market failures. Our challenge today is to devise a similar compact on the global scale, to underpin the new global economy.[33]

Furthermore, he noted that until people around the world have confidence that certain minimum standards and security will prevail, "the global economy will be fragile and vulnerable—vulnerable to backlash from all of the 'isms' of our post-cold-war world: protectionism, populism, nationalism, ethnic chauvinism, fanaticism and terrorism."[34] And so, he called on firms and business associations "to embrace, support and enact a set of core values in the areas of human rights, labour standards, and environmental practices."[35] In return, he offered assistance from the UN in "incorporating these agreed values and principles into [] mission statements and corporate practices" and facilitating a dialogue with other social groups.[36] Further, he noted that various interest groups were exerting "enormous pressure" for "restrictions on trade and investment," but he preferred to pursue the UN's "proclaimed standards" through the voluntary Global Compact that was "mutually supportive" of the UN and business.[37]

The Global Compact became operational in 2000, supported by various UN agencies and transnational nongovernmental organizations, with nine (now ten) principles on human rights, labor, environment, and anti-corruption.[38] Although the Compact attracted critique for its nonbinding structure and embrace of corporate trade and investment, participation "increased constantly," and

[33] Press Release, UN-Secretary-General, Secretary-General Proposes Global Compact on Human Rights, Labour, Environment, in Address to the World Economic Forum in Davos (Feb. 1., 1999), https://www.un.org/press/en/1999/19990201.sgsm6881.html.
[34] *Id.*
[35] *Id.*
[36] *Id.*
[37] *Id.*
[38] Ruggie, *supra* note 17, at 310-13; *see also* UN Global Compact, Our Mission, https://www.unglobalcompact.org/what-is-gc/mission.

became "more and more diverse in terms of geography and economic sectors."[39] Within just a couple years, approximately 1,000 firms were signatories to the Compact.[40] Building on these efforts, in 2003, the UN increased its focus on environmental matters by convening the first Institutional Investor Summit on Climate Risk, which led to the creation of the Investor Network on Climate Risk—"a politically active group of seventy investors representing seven trillion [dollars] in assets."[41]

Subsequently, senior executives of financial institutions and other companies that were signatories to the Global Compact "repeatedly expressed to the then U.N. Secretary General and to the Global Compact" the need for further efforts.[42] In response, in January 2004, Kofi Annan "wrote to the CEOs of 55 of the world's leading financing institutions inviting them to join in a [new] initiative," under the auspices of the Global Compact, titled "Who Cares Wins."[43] Out of this initiative came a report using the new term "ESG" and recommendations for different actors "on how to better integrate environmental, social and corporate governance issues in asset management, securities brokerage services and associated research functions."[44]

B. The Coining of ESG: The *Who Cares Wins* Report

Of the fifty-five invited, eighteen financial institutions from nine countries with total assets under management of over 6 trillion US dollars participated at the outset in the joint initiative with the UN, and with financial sponsorship from the Swiss Government.[45] The endorsing financial

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[39] Thérien & Pouliot, *supra* note 19, at 62-69.
[40] *Id.* at 67.
[41] Pargendler, *supra* note 11, at 1795-96.
[42] THE GLOBAL COMPACT, WHO CARES WINS: CONNECTING FINANCIAL MARKETS TO A CHANGING WORLD vii (2004) [hereinafter WHO CARES WINS] [listed as 2005 in some sources, e.g., https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/publications/publications_report_whocareswins__wci__1319579355342]. A list of then-recent initiatives by institutional investors on ESG issues included in the report might give a window into some of the activities and interests at the time: "climate change, corporate governance, issues relating to the pharmaceutical industry, the disclosure of payments to governments and the management of corruption and bribery cases." *Id.* at 21; *see also id.* (Exhibits 14-17).
[43] *Id.* at vii.
[44] *Id.* (executive summary).
[45] *Id.* Two additional organizations, Mitsui Sumitomo Insurance and China Minsheng Bank, later joined as endorsing institutions. CONFERENCE REPORT, INVESTING FOR LONG-TERM VALUE: INTEGRATING ENVIRONMENTAL, SOCIAL AND GOVERNANCE VALUE DRIVERS IN ASSET MANAGEMENT AND FINANCIAL RESEARCH (2005),

institutions included some of the world's largest banks including Goldman Sachs, Morgan Stanley, UBS, Credit Suisse Group, Deutsche Bank, HSBC, Banco do Brasil, BNP Paribas, as well as insurance companies such as Aviva, and investment advisors such as Innovest.[46]

For the goals of "stronger and more resilient financial markets," "sustainable development," "improved trust in financial institutions," and "awareness of mutual understanding of involved stakeholders," the report argued, above all, for a "better inclusion of environmental, social and corporate governance (ESG) factors in investment decisions."[47] In the view of the initiative participants, such ESG integration will "ultimately support the implementation of the Global Compact principles throughout the business world"[48]—reflecting the mutually supportive collaboration by the financial industry and the UN that were at the heart of the initiative.

On the financial industry side of this equation, the report further noted that "investment markets have a clear self-interest in contributing to better management of environmental and social impacts in a way that contributes to the sustainable development of global society."[49] A section of the report labeled "investment rationale" noted that studies confirmed "the business case" for "good management of ESG issues contribut[ing] to shareholder value creation."[50] It explained that "[c]ompanies with better ESG performance can increase shareholder value by better managing risks related to emerging ESG issues, by anticipating regulatory changes or consumer trends, and by accessing new markets or reducing costs" and "hav[ing] a strong impact on reputation and brands."[51]

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https://www.ifc.org/wps/wcm/connect/9d9bb80d-625d-49d5-baad-8e46a0445b12/WhoCaresWins_2005ConferenceReport.pdf?MOD=AJPERES&CVID=jkD172p.

[46] WHO CARES WINS, *supra* note 42 (endorsing institutions). Ivo Knoepfel has been credited as the author of the report. *See* Georg Kell, *The Remarkable Rise of ESG*, FORBES (July 11, 2018), https://www.forbes.com/sites/georgkell/2018/07/11/the-remarkable-rise-of-esg/?sh=1019d6f51695.

[47] WHO CARES WINS, *supra* note 42, at 3.

[48] *Id.* at vii.

[49] *Id.*

[50] *Id.* at 9.

[51] *Id.*

Companies should not focus on single issues, but instead the "entire range of ESG issues relevant to their business."[52]

Alongside these articulated goals and rationales, three points about the report's strategic choice of terminology stand out. First, the use of ESG, in contrast to other existing terms, was deliberate and emphasized throughout the report. It explained:

> Throughout this report we have refrained from using terms such as sustainability, corporate citizenship, etc., in order to avoid misunderstandings deriving from different interpretations of these terms. We have preferred to spell out the environmental, social and governance issues which are the topic of this report.[53]

Correspondingly, the report includes a list of examples for each E, S, and G, such as climate change and related risks, human rights, and management of corruption and bribery issues. It also notes that "ESG issues relevant to investment decisions differ across regions and sections."[54] With the benefit of hindsight, contemporary readers might indeed note that certain issues are missing on the list of examples that have become a prominent focus of ESG efforts in some regions in recent years such as human capital management and board diversity.[55]

Second, the report explained why the initiative participants included the G in their framing of ESG:

> Sound corporate governance and risk management systems are crucial pre-requisites to successfully implementing policies and measures to address environmental and social challenges. This is why we have chosen to use the term "environmental, social and governance issues" throughout this report, as a way of highlighting the fact that these three areas are closely interlinked.[56]

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[52] *Id.*
[53] *Id.* at 1-2.
[54] *Id.* at 6.
[55] The report lists example issues such as "[w]orkplace health and safety", "human rights", and "board structure and accountability," but not human capital management and disclosure or board and workforce diversity. *See id.* at 6. For a discussion of human capital management, and the wide range of issues it encompasses beyond workplace health and safety, and its context in the ESG movement, see George S. Georgiev, *The Human Capital Management Movement in U.S. Corporate Law*, 95 TULANE L. REV. 639 (2021). For a discussion of various rules and initiatives on board diversity, and the ESG movement's inclusion of diversity, equity, and inclusiveness, see Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1 (2022).
[56] WHO CARES WINS, *supra* note 42, at 2.

By way of example, the report noted that "better transparency and disclosure" and "linking executive compensation to longer-term drivers of shareholder value and improving accountability" can play a key role in implementing many recommendations.[57] It cited then-recent findings and recommendations released by the Conference Board Commission on Public Trust and Private Enterprise, laying out "best practice suggestions" on executive compensation, corporate governance, and audit and accounting issues, in the wake of 2001-2002 corporate scandals such as at Enron, WorldCom, and other companies.[58] With this framing, in the view of the initiative participants, G was not an anachronistic appendage or dissimilar concept, but rather a vital and connected set of issues and means of execution for relevant E and S issues.

Similarly, the report emphasized the possibility of mainstreaming the integration of ESG issues into "normal research and fund management functions."[59] It even provided a graphic illustrating "[o]ne (of many) possible organisational paths leading from mainstream [], to first generation screening []; to partial ESG integration in different asset classes []; to full ESG integration in research and portfolio management processes."[60] Notably, this language suggested an evolutionary process for investing practices toward more holistic analysis and presented a contrast to the Socially Responsible Investment (SRI) movement, which had been around for decades and was based on ethical and moral criteria, using mostly negative screens.[61] Sprinkled throughout the report were quotes from executives of large companies, financial institutions, and asset managers emphasizing the theme of alignment of

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57 *Id.*
58 *Id.* (citing CONFERENCE BOARD COMMISSION ON PUBLIC TRUST AND PRIVATE ENTERPRISE: FINDINGS AND RECOMMENDATIONS (2004)).
59 *Id.* at 38.
60 *Id.* at 39 (Figure 7).
61 *See, e.g.*, John H. Langbein & Richard A. Posner, *Social Investing and the Law of Trusts*, 79 MICH. L. REV. 72 (1980); Maria O'Brien Hylton, *Socially Responsible Investing: Doing Good Versus Doing Well In An Inefficient Market*, 42 AM. U. L. REV. 1 (1992); George Djurasovic, *The Regulation of Socially Responsible Mutual Funds*, 22 J. Corp. L. 257, 261-62 (1997); Benjamin J. Richardson, *Fiduciary Relationships for Socially Responsible Investing: A Multinational Perspective*, 48 AM. BUS. L.J. 597 (2011). For an exploration of the contrasts of SRI and ESG, see Blaine Townsend, *From SRI to ESG: The Origins of Socially Responsible and Sustainable Investing*, 1 J. IMPACT & ESG INVESTING 1 (2020); Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing By a Trustee*, 72 STAN. L. REV. 381 (2020).

ESG issues with risk-adjusted financial performance and shareholder value,[62] and how consideration of these issues "should be part of every financial analyst's normal work."[63]

Third, the report also suggested that in framing ESG issues and the need to integrate them into mainstream investment analysis, it would take a broad approach and use longer time horizons in construing issues that could be material:

> This report focuses on issues which have or could have a material impact on investment value. It uses a broader definition of materiality than commonly used — one that includes longer time horizons (10 years and beyond) and intangible aspects impacting company value. Using this broader definition of materiality, aspects relating to generally accepted principles and ethical guidelines (e.g. the universal principles underlying the Global Compact) can have a material impact on investment value.

This language conceptually tied the report's framing of the term ESG to issues relevant to investment value, as articulated in "the investment rationale," but made clear that it was not constricting itself to traditional or narrow notions of materiality.

The report concluded by stating the initiative participants' intentions for outreach to start a process "to further deepen, specify and implement the recommendations outlined in th[e] report."[64] This included plans to approach accounting standard-setting bodies (FASB, IASB, etc.), professional and self-regulatory organizations (AIMR, EFFAS, NYSE, NASDAQ, FAS, etc.), and investor relations associations (NIRI, DIRK, etc.).[65] Further, the participants planned to approach their own clients to assess their interest and needs for ESG-related research and investment services, and to engage platforms like the UNEP Finance Initiative, The Conference Board, and the World Economic Forum to start dialogue with investors, companies, regulators, stock exchanges, accountants, consultants, and NGOs.[66]

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[62] *See* WHO CARES WINS, *supra* note 42, at 1, 3, 4, 9, 21.
[63] *Id.* at 21, 27.
[64] *Id.* at 40.
[65] *Id.*
[66] *Id.*

C. The Diffusion of ESG: The Flywheel of UN Initiatives, Financial Institutions, Institutional Investors, and Their Networks

A moniker that might have been viewed as nothing more than a defined term in a technocratic report has instead seen a "meteoric rise."[67] The strategic framing of putting E, S, and G together was not inherently sticky; it was amplified through a number of UN initiatives and institutional support that helped to spread the term through the global investment community to stakeholders around the world. While the term ESG was mentioned in fewer than 1% of earnings call in the years immediately following the *Who Cares Wins* report, by 2021 it was mentioned in nearly one-fifth of earnings calls and a survey found that 72% of institutional investors implemented ESG factors.[68]

One of the early boosts to using the ESG frame came immediately on the heels of the *Who Cares Wins* report. The United Nations Environment Programme Finance Initiative (UNEP FI) Asset Management Working Group, composed of thirteen asset managers and pension funds, commissioned the international law firm Freshfields Bruckhaus Deringer to produce a study analyzing whether integration of ESG issues into investment policy was voluntarily permitted, legally required, or hampered by law and regulation in legal systems around the world.[69] The Freshfields report concluded that "the links between ESG factors and financial performance are increasingly being recognised" and so "integrating ESG considerations in an investment analysis… is clearly permissible and is arguably required in all jurisdictions."[70] The report came to be regarded as "[t]he single most

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[67] *See* McKinsey Quarterly, *Five Ways that ESG Creates Value*, Nov. 14, 2019, https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/five-ways-that-esg-creates-value.

[68] Debbie Carlson, *Mentions of 'ESG' and Sustainability are Being Made on Thousands of Corporate Earnings Calls*, MARKETWATCH (July 19, 2021), https://www.marketwatch.com/story/mentions-of-esg-and-sustainability-are-being-made-on-thousands-of-corporate-earnings-calls-11626712848.

[69] UNEP Finance Initiative, *A Legal Framework for the Integration of Environmental, Social and Governance Issues Into Institutional Investment* (foreward-p.1), Oct. 2005, https://www.unepfi.org/fileadmin/documents/freshfields_legal_resp_20051123.pdf. UNEP FI

[70] *Id.* at 13.

effective document for promoting the integration of environmental, social, governance (ESG) issues into institutional investment."[71]

The following year, the UNEP FI and the UN Global Compact launched the Principles for Responsible Investment (PRI)—again, a group of leading institutions jointly engaged with the UN to push forward the larger project of understanding the investment implications of ESG.[72] Under the PRI, institutional investor signatories can voluntarily commit to supporting and implementing six core principles that channel their power toward promoting the disclosure of ESG issues by portfolio companies and the integration of ESG issues in investment analysis, ownership policies, and within the investment industry itself.[73]

By this time, efforts at standard setting for "impact" or "sustainability" reporting started to evolve as well. The Global Reporting Initiative (GRI), which had launched its guidelines in 2000, the same year as the UN Global Compact, had initially focused on environmental conduct principles following public outcry over the Exxon Valdez oil spill.[74] By the mid-2000s, "demand for GRI

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[71] UN ENV'T PROGRAMME FIN. INITIATIVE, FIDUCIARY RESPONSIBILITY: LEGAL AND PRACTICAL ASPECTS OF INTEGRATING ENVIRONMENTAL, SOCIAL AND GOVERNANCE ISSUES INTO INSTITUTIONAL INVESTMENT 13 (2009); *see also* Joakim Sandberg, *Socially Responsible Investment and Fiduciary Duty: Putting the Freshfields Report into Perspective*, 101 J. BUS. ETHICS 143, 144 (2011) (describing the influence of the Freshfields report). In 2004, the Asset Management Working Group of the UNEP FI also commissioned studies by brokerage house analysts on the materiality of ESG issues to equity pricing. *See* UNEP FI, THE MATERIALITY OF SOCIAL, ENVIRONMENTAL AND CORPORATE GOVERNANCE ISSUES TO EQUITY PRICING: 11 SECTOR STUDIES (2004), https://www.unepfi.org/publications/investment-publications/the-materiality-of-social-environmental-and-corporate-governance-issues-to-equity-pricing/. It found "agreement that environmental, social and corporate governance issues affect long-term shareholder value" and "[i]n some cases those effects may be profound." *Id.* at 4.

[72] In 2005, Kofi Annan invited a group of the world's largest institutional investors to develop the PRI. It as a "20-person investor group drawn from institutions in 12 countries [a]d support by a 70-person group of experts from the investment industry, intergovernmental organisations and civil society." PRI, About the PRI, https://www.unpri.org/about-us/about-the-pri.

[73] PRI, What Are the Principles for Responsible Investment?, https://www.unpri.org/about-us/what-are-the-principles-for-responsible-investment; *see also* Virginia E. Harper Ho, *'Enlightened Shareholder Value': Corporate Governance Beyond the Shareholder-Stakeholder Divide*, 36 J. CORP. L. 59, 81-82 (2010) (discussing the primary goals of the PRI and the six principles). These efforts expanded in subsequent years. For example, the PRI and UNEP FI launched a joint initiative in 2016 that led to a 2019 report declaring that fiduciary duties requires investors to incorporate ESG issues into investment analysis and decisions, and a Global Statement on Investor Obligations and Duties with over one hundred signatories from fifty countries. UN ENV'T PROGRAMME FIN. INITIATIVE & PRINCIPLES FOR RESPONSIBLE INV., FIDUCIARY DUTY IN THE 21ST CENTURY: FINAL REPORT 8, 52 (2019).

[74] GRI, Mission & History, https://www.globalreporting.org/about-gri/mission-history/.

reporting and uptake from organizations steadily grew," and the guidelines were expanded and GRI opened up offices around the world.[75] Most critically, it broadened its focus from environmental conduct principles to ESG issues, and eventually transitioned from providing guidelines to global standards for reporting.[76]

The *Who Cares Wins* initiative, which originally coined the term ESG, also continued its efforts through 2008 in "a series of closed-door/invitation-only events for investment professionals, providing a platform for asset managers and investment researchers to engage with institutional asset owners, companies and other private and public actors on ESG issues."[77] Each event in the series looked in-depth at "a particular element of ESG mainstreaming," from the interface between investors and companies to the role of ESG in emerging markets investment.[78] A much larger universe of institutions had participated in initiative events by this time—from new bank participants such as Citigroup to companies like Nestlé and Royal Dutch Shell, and a wide array of non-profit organizations.[79]

The initiative culminated in a final report that identified impediments to wider uptake of ESG by the financial industry and offered a set of recommendations for each of the key market actors in the system.[80] It noted that "progress has not been uniform": "corporate governance is the concept that most easily captures mainstream minds" and the understanding and integration of financially-material environmental issues had also "advanced greatly."[81] The quality and amount of coverage of

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[75] *Id.*
[76] *Id.*
[77] Int'l Fin. Corp., Who Cares Wins, 2004-2008: Issue Brief at 2 [hereinafter IFC Issue Brief].
[78] THE GLOBAL COMPACT, OUTCOMES OF THE WHO CARES WINS INITIATIVE 2004-2008: FUTURE PROOF? EMBEDDING ENVIRONMENTAL, SOCIAL AND GOVERNANCE ISSUES IN INVESTMENT MARKETS (2008) [hereinafter WCW FUTURE PROOF?], https://documents1.worldbank.org/curated/en/476811468158704493/pdf/476600WP0Futur10Box338858B01PUBLIC1.pdf.
[79] *Id.* at 43-44. The global financial crisis was underway in 2008, at the conclusion of the Who Cares Wins initiative, and participants viewed it as having "reinforced the necessity for the financial industry to more diligently manage their risks, including those related to [ESG] issues." *Id.* at 3.
[80] IFC Issue Brief, *supra* note 77, at 2.
[81] WCW FUTURE PROOF?, *supra* note 78, at 16.

social/stakeholder issues, employee relations and human capital, and business ethics had lagged.[82] It was "understandable that change has sometimes been slow" because ESG "is about doing traditional investments better" and so it is "necessarily long term and adds value at the margin."[83] With "the learning phase [] drawing to a close" and "a springboard for scaling up ESG integration" in place, however, it ultimately observed that the majority of industry professionals that had participated in the initiative "believe that the investment system is well on track for ESG issues becoming mainstream."[84] Indeed, in less than a decade the groundwork had been set for the term ESG to reach ubiquity in subsequent years.

II. The Evolving and Varied Usages of ESG

As the ESG term was pushed out of closed-door meetings of financial institutions convened by the United Nations and into reports, further dialogue with a large network of market actors, and frameworks such as the PRI, it spread quickly and in ensuing discourse it became used in a variety of ways. Different usages of ESG are not necessarily mutually exclusive, but in some instances overlapping or in tension with each other. These varied usages and understandings of ESG reflect a diversity of views about justifications for the concept, its utility, and the like, as well as an untethering or lack of connection to the original framing from the *Who Cares Wins* report.

This Part examines several common ways in which the term ESG has been given meaning to date, starting from the primary sense in which the term ESG was used, as factors for integrating in investment analysis, and exploring evolving usage such as ESG as a means of risk management, as a synonym for CSR or sustainability, or as a preference or activity. Additional variations and usages are

[82] *See id.* at 24 (charting significantly different amounts and quality of coverage of ESG issues, with GHG emissions and other environmental issues and risks far ahead of social/stakeholder issues, employee relations and human capital, and business ethics).
[83] *Id.* at 17.
[84] *Id.* at 16.

undoubtedly possible and consensus on the meaning of ESG does not currently exist.[85] Scholars have previously observed that ESG lacks a "common theorization"—an agreement or shared beliefs establishing a common discourse on a term or concept.[86] Without such a common theorization, convergence on things such as ESG ratings is less likely.[87] A host of other implications arise from the strategic choice to combine E, S, and G in one moniker, and from the varying usages that have developed, which this Article takes up in subsequent discussion.

A. ESG as Factors for Investment Analysis

The *Who Cares Wins* report did not provide a singular definition of ESG beyond the acronym—but it repeatedly referred to being "a joint effort of financial institutions" to "develop guidelines and recommendations on how to better integrate environmental, social and governance issues in asset management, securities brokerage services and associated research functions."[88] Indeed, this language featured as a subtitle on the cover of the report.[89] As noted above, the report also listed example issues that fall under each E, S, and G, and focused on "issues which have or could have a material impact on investment value," while noting that it took a broad view of materiality and saw the G as interlinked with the E and S.[90] Although the report sometimes referred to broader goals such as "contribut[ing] to the sustainable development of global society," invoking language in the spirit of

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[85] *See* Elad L. Roisman, Comm'r, SEC, Keynote Speech at the Society for Corporate Governance National Conference (July 7, 2020), https://www.sec.gov/news/speech/roisman-keynote-society-corporate-governance-national-conference-2020 ("[T]here is not consensus on what, exactly, 'ESG' means."); *see also* Stavros Gadinis & Amelia Miazad, *Corporate Law & Social Risk*, 73 VAND. L. REV. 1401, 1414 (2020) ("Despite trillions of dollars poured into ESG investments, a decade of corporate soul searching, and a bevy of standard setters, one would be hard-pressed to come up with a consistent definition for this phenomenon."); Larcker et al., *supra* note 9, at 1 (noting that "considerable uncertainty exists over what ESG is" and "[d]espite the near universal push for ESG, consensus does not exist about the problem ESG is expected to solve").

[86] *See* Aaron K. Chatterji, Rodolphe Durand, David I. Levine & Samuel Touboul, *Do Ratings of Firms Converge? Implications for Managers, Investors and Strategy Researchers*, 37 *Strat. Mgmt. J.* 1597 (2016); Robert G. Eccles & Judith C. Stroehle, *Exploring Social Origins in the Construction of ESG Measures* (July 12, 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3212685.

[87] Eccles & Stroehle, *supra* note 86, at 8. Whether different raters measure the same construct in a similar way—what is known as "commensurability"—would also contribute to a greater likelihood of convergence on ratings. *See id.*

[88] WHO CARES WINS, *supra* note 42, at vii.

[89] *Id.* (cover), i.

[90] *Id.* at 2, 6.

the UN Global Compact, it heavily emphasized the "business case" justification and alignment with long-term value for shareholders.[91] On the whole, the picture that emerges from the report is that ESG refers to "information," "issues," "factors," or "criteria" that should be integrated into "normal" and "mainstream" investment analysis.[92] The report did not explain in any detail how such integration should be done.

The term ESG has been, and is, often still used in this vein as a way of referring to a set of issues that should be integrated into investment analysis. As a tool, ESG is often broken into component parts of E, S, and G, and explained by reference to underlying content that would be relevant to investor decision-making.

To take S as an example, as one scholar explained, "In the context of responsible investment, the S is meant to better evaluate how well positioned a company is for the long term, the reputational value it or its products gain from goodwill, the stability and long-term efficiency of its workforce, potential costs of labour conflicts, the political risk of conflicts with communities, the legal and reputational risks that it runs from potential problems with its supply chain employment practices or community protests, and so on."[93] Notably, there are a variety of ways in which the idea of stakeholders, social issues, and society may enter into ESG investment practice. Social information, for instance, might be integrated into valuation, into investment mandates such as exclusionary screens, or into standards of practice or principles that corporations are meant to adopt or against which their behavior will be measured.[94] A variety of frameworks for evaluating and engaging

[91] *See id.* at 3, 9-10.
[92] *See id.* passim.
[93] David Wood, *What Do We Mean by the S in ESG? Society as a Stakeholder in Responsible Investment* 553, *in* THE ROUTLEDGE HANDBOOK OF RESPONSIBLE INVESTMENT (Tessa Hebb, James P. Hawley, Andreas G. F. Hoepner, Agnes L. Neher, David Wood eds., 2015).
[94] *Id.* at 556-59.

corporations on social issues have developed, closely linked to ESG as a tool for investment or vehicle for investor-corporate dialogue.[95]

B. ESG as Risk Management

The broad scope of potential issues that could come under the words "environmental, social and governance," the wide-ranging and potentially diverging incentives of the UN and the financial industry, and the lack of specificity in definition by the *Who Cares Wins* initiative, opened up the possibility of the term ESG taking on a variety of meanings. By 2008, the year in which the initiative concluded, a survey of over 300 fund managers, of whom only 23% self-identified as "socially responsible investors," found that over 70% viewed ESG as a tool to identify investment opportunities as well as to manage risk.[96]

For many mainstream investors and asset managers, the key justification for incorporating ESG factors into investment analysis relates to their potential impact on portfolio-level risk-adjusted returns and the relationship between ESG factors and risk management at the company level.[97] Although not unqualified, a large body of research has found correlations between corporate financial and ESG performance, and some evidence of financial materiality of ESG factors to portfolio risk-adjusted returns.[98]

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95 *Id.* at 560.

96 Harper Ho, *supra* note 73, at 88 (citing Danyelle Guyett, *ESG Ratings of Fund Managers—a Step Closer Towards the Mainstreaming of ESG Integration*, MERCER (July 4, 2008)).

97 Virginia Harper Ho, *Sustainable Investment & Asset Management: From Resistance to Retooling* (Mar. 23, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4064317; *see also* Virginia Harper Ho, *Risk-Related Activism: The Business Case for Monitoring Nonfinancial Risk*, 41 J. CORP. L. 647, 647 (2016) (discussing "the exercise of shareholder power to promote firm management, mitigation, and disclosure of risk, including nonfinancial environmental, social, and governance (ESG) risks"). On ESG and systematic risk, see John C. Coffee, *The Future of Disclosure: ESG, Common Ownership, and Systematic Risk* (Eur. Corp. Governance Inst., Working Paper No. 541, 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3678197; Jeffrey N. Gordon, *Systemic Stewardship*, J. Corp. L. (forthcoming 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3782814.

98 *See* Ulrich Atz, Zongyuan (Zoe) Liu, Christopher C. Bruno & Tracy Van Holt, *Does Sustainability Generate Better Financial Performance? Review, Meta-analysis, and Propositions*, 8-9, 20-22 (2021), https://ssrn.com/abstract=3708495 (surveying 1,141 primary peer-reviewed papers and 27 meta-reviews published between 2015 and 2020 and finding evidence of a positive association between sustainability and financial performance at the firm level and risk-mitigating effects at the portfolio level); Gunnar Freide et al., *ESG and Financial Performance: Aggregated Evidence From More Than 2,000 Empirical Studies*, 5 J. SUSTAINABLE FIN. & INV. 210, 220-21, 225-26 (2015) (aggregating nearly 2,200 studies and concluding that the majority

Based on interviews and roundtable discussions with over three hundred participants, including the largest asset managers, investment banks, pension funds, proxy advisors, hedge funds, leading investors and sustainability advocates, Stavros Gadinis and Amelia Miazad found that "companies are using ESG on the ground" to help "identify and manage social risks to their business."[99] According to their findings, "ESG has evolved into a separate corporate function, whose mission is to monitor and manage the risks facing the company due to environmental and social impact."[100]

Unlike internal controls and accounting which operate under an externally-driven, rules-based framework, "ESG represents an attempt by companies to self-regulate their conduct."[101] Thus, in this understanding of ESG, "[t]he values that ESG promotes do not originate from an abstract moralistic philosophy of 'doing the right thing,' nor are they dictated by a central standard setter . . . [r]ather, they arise following a wide-ranging consultation with stakeholders, who are better positioned to take notice of potentially catastrophic company operations."[102] In an era in which bad public relations or corporate scandals could have devastating effects on a company's brand value, engaging stakeholders such as consumers and employees through "ESG practices" can provide useful information to manage key relationships and mitigate risk.[103] Instead of simply being a tool for evaluating a broader set of

found positive correlations between corporate financial and ESG performance but portfolio-level studies had more mixed results); *cf.* Jan-Carl Plagge & Douglas M. Grim, *Have Investors Paid a Performance Price? Examining the Behavior of ESG Equity Funds*, 46 J. PORTFOLIO MGMT. 123 (Feb. 2020) (finding that "return and risk differences of ESG funds can be significant but appear to be mainly driven by fund-specific criteria rather than by a homogeneous ESG factor"); Schanzenbach & Sitkoff, *supra* note 61, at 454 (noting "there is theory and evidence in support of risk-return ESG" but "this support is far from uniform, is often contextual, and in all events is subject to change, especially as markets adjust to the growing use of ESG factors").

[99] Gadinis & Miazad, *supra* note 85, at 1410.

[100] *Id.* at 1415.

[101] *Id.*

[102] *Id.* at 1426; *see also* Wood, *supra* note 93, at 562 (explaining that ESG, and particularly S, plays a role as "a lens with which to view corporate value, by identifying places where corporations or investments improve their financial performance through more effective management of human relations with employees, communities, or other stakeholders").

[103] *See* Gadinis & Miazad, *supra* note 85, at 1432-35.

investment factors, ESG has taken on meaning as a set of practices for proactive risk management, whether at the firm or portfolio level.

C. ESG as Corporate Social Responsibility

A different interpretation or meaning ascribed to ESG in contemporary parlance is a belief that it represents "a step towards a better world" that is tied to beneficial long-term social outcomes.[104] In short, ESG gets equated, or conceptually combined, with CSR. A variation of this equates ESG with a different term—sustainability.

For some, this usage may stem from a nuanced understanding or belief that broad social benefits may flow from using ESG as a tool for enhanced investment analysis. The preamble to the Principles for Responsible Investment itself draws this link, declaring, "We also recognize that applying these Principles may better align investors with broader objectives of society."[105] The original *Who Cares Wins* report also included language about broader social benefits—reflecting the UN's goals in the initiative and the values it aimed to serve through the Global Compact.[106] Thus, some usage of ESG reflects an understanding or belief that using it as a tool for enhanced investment analysis might create social benefits that non-ESG-related investing might not provide.[107] Although the use of ESG information in investment decision-making is not the same as pursuing broad social benefits, some view the two as inextricably linked and so language around ESG takes on the flavor of CSR discourse.

For example, Robert Eccles and co-author Judith Stroehle noted: "The terms 'sustainability', 'corporate social responsibility' (CSR) or environmental, social and governance' (ESG) have been used synonymously in the past, describing a firm's voluntary actions to manage environmental and social

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[104] Wood, *supra* note 93, at 553.
[105] PRI, What Are the Principles for Responsible Investment?, https://www.unpri.org/about-us/what-are-the-principles-for-responsible-investment#:~:text=Signatories'%20commitment&text=We%20also%20recognise%20that%20applying,with%20broader%20objectives%20of%20society.
[106] *See* WHO CARES WINS, *supra* note 42, at vii.
[107] Wood, *supra* note 93, at 553.

impact as well as positive contributions to society. [W]e believe that an organization's understanding of the former two can influence the latter."[108] In a similar vein, Lynn LoPucki suggested the following connection: "CSR is the abstract idea that corporations have a moral responsibility to voluntarily integrate environmental, social, and governance ('ESG') improvements into their business operations for the benefit of shareholders, other stakeholders, society as a whole, and the environment."[109] Stated differently, "CSR is adherence to the actual values of corporate stakeholders, and ESG is a set of measurements from which conclusions about CSR can be drawn."[110]

For others, they may simply think that ESG is a new synonym for CSR.[111] Some may have inferred this understanding from notions that the types of environmental and social issues that are often discussed under the moniker ESG are the same or similar as those of previous eras that were labeled CSR. For example, one scholar described ESG "as a subcategory of CSR and uses a metrics-driven format to measure a company's commitment to social responsibilities."[112] Others have observed, "the ESG movement sounds like older corporate social responsibility (CSR) movement—but with a new name."[113]

In this understanding of ESG as a synonym for CSR, it encompasses notions of moralistic or ethical value. It is a "normative (values-based) argument" to "inject social consciousness into both corporate and individual investment decisions."[114] Participants in the system that had been focused on values-driven activity imbued the term ESG with their views and in turn helped shape others'

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[108] Robert G. Eccles & Judith C. Stroehle, *Exploring Social Origins in the Construction of ESG Measures* (July 12, 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3212685.
[109] Lynn M. LoPucki, *Repurposing the Corporation Through Stakeholder Markets*, 55 UC DAVIS L. REV. 1445, 1447 (2021).
[110] *Id.* at 1448. A common variation is to combine ESG and CSR, perhaps to straddle the various meanings and connotations. *See generally, e.g.*, Mark J. Roe, *Corporate Purpose and Corporate Competition*, 99 WASH U. L. REV. 223, (2021) (referring throughout to "CSR/ESG" and "ESG/CSR").
[111] *See* Larcker et al., *supra* note 9, at 2 (noting that a viewpoint "held by many investors and members of the public, is that ESG is synonymous with corporate responsibility").
[112] Thomas Lee Hazen, *Social Issues in the Spotlight: The Increasing Need to Improve Publicly-Held Companies' CSR and ESG Disclosures*, 23 U. PA. J. BUS. L. 740, 745-46 (2021).
[113] Nives Dolšak, Jennifer J. Griffin & Aseem Prakash, *Is ESG Simply the Old CSR Wine in a New Bottle?*, REG. REV. (Mar. 28, 2022), https://www.theregreview.org/2022/03/28/dolsak-griffin-prakash-is-esg-old-csr-wine-in-new-bottle/.
[114] Larcker et al., *supra* note 9, at 2.

understanding of the values being promoted by ESG-related activity. For example, researchers have traced how the different "origins, philosophies, and 'purposes' of ESG shaped methods and data characteristics of two of the most important data vendors of their time."[115] Whereas Innovest developed a financial value-oriented methodology, KLD by contrast took a values-driven approach.[116] The *Who Cares Wins* initiative did not resolve the potential tensions between these approaches to understanding ESG – it emphasized the "business case" from the financial industry perspective but also promoted notions that the UN's goals would be served, which arose out of Kofi Annan's concern for building a social safety net around the globe and addressing gaps in human rights, labour standards, and environmental practices. This potential ambiguity left open the interpretation that ESG was a new term for what used to be called CSR and many market participants, non-profit organizations, and the like maintained such orientation and refocused their efforts into the new ESG movement.

D. ESG as a Preference

Finally, another characterization of ESG is that it represents "a preference or taste among some companies or investors."[117] In this common conceptualization, ESG is a means of "expressing a preference"[118]—like "voting" with one's money as a consumer or investor.[119]

As Georg Kell explained, "The rise of ESG investing can also be understood as a proxy for how markets and societies are changing and how concepts of valuation are adapting to these changes."[120] Corporations are challenged to adapt to changing consumer and investor preferences that

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[115] Robert G. Eccles, Linda-Eling Lee & Judith C. Stroehle, *The Social Origins of ESG? An Analysis of Innovest and KLD* (Aug. 20, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3318225.
[116] *Id.*
[117] Serafeim, *supra* note 1, at 14.
[118] *See id.*
[119] *See* Kell, *supra* note 46; *see also* Quinn Curtis, Jill Fisch & Adriana Z. Robertson, *Do ESG Mutual Funds Deliver on Their Promises?*, 120 MICH. L. REV. 393, 402 (2021) ("For some years, investing on the basis of ESG considerations was thought to be a preference predicated on ethical, political, religious, or other objectives rather than an investment strategy grounded in financial risk and return."); Schanzenbach & Sitkoff, *supra* note 61 (differentiating between ESG investing for moral or ethical reasons, which they call "collateral benefits ESG", and ESG investing for risk and return benefits, which they call "risk-return ESG").
[120] Kell, *supra* note 46.

"favor[] smarter, cleaner and healthier products and services," and "to leave behind the dogmas of the industrial era when pollution was free, labor was just a cost factor and scale and scope was the dominant strategy."[121]

In this spirit, investors and a wide range of stakeholders seek to align their activities with an expression of their values, whether political, ethical, or social, and ESG is a label vaguely signifying some level of attention to issues beyond the purely financial.[122] It is in this sense that one might hear that a company "is" or "is not" "very ESG" or that is possible to "do ESG."[123] And this usage contributes to some seeing ESG as "a virtue signal"[124] or even equating ESG with an ideological preference for "woke capitalism."[125] In turn, this understanding of ESG as a preference has catalyzed a "backlash" as it is not seen as a neutral concept or activity but rather one that is value-laden and ideologically or politically tilted.[126]

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[121] *See id.* For an argument that "index funds have engaged in a pattern of competitive escalation in their policies on [ESG] issues" in response to preferences of millennials as investors, customers, and employees, see Michal Barzuza, Quinn Curtis & David H. Webber, *Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance*, 93 S. CAL. L. REV. 1243 (2020).

[122] This view is illustrated by a 2021 survey by Broadridge finding that retail investors, particularly millennials aged between 25 to 40, seek to express their environmental and social preferences. Broadridge, *From the Retail Trading Frenzy to Growing ESG Trends, What Will Be in Proxy Season 2021?* (May 3, 2021), https://www.prnewswire.com/news-releases/from-the-retail-trading-frenzy-to-growing-esg-trends-what-will-be-in-proxy-season-2021-301281582.html.

[123] *See supra* notes 8 & 9; *see also* Matt Levine, *Everyone Wants to Do ESG Now*, BLOOMBERG (Mar. 21, 2022), https://www.bloomberg.com/opinion/articles/2022-03-21/everyone-wants-to-do-esg-now.

[124] *See* Dolšak et al., *supra* note 113; *see also* Gadinis & Miazad, *supra* note 85, at 1415 (observing the "definitional ambiguousness [of ESG] has given rise to a common misperception of ESG as a random and ever-sprawling assortment of objectives, influenced by fads and trends rather than hard business logic.").

[125] *See* Andrew Ross Sorkin et al., Larry Fink Defends Stakeholder Capitalism, N.Y. Times (Jan. 18, 2022), https://www.nytimes.com/2022/01/18/business/dealbook/fink-blackrock-woke.html (discussing BlackRock CEO Larry Fink's rebuttal to claims that ESG is "bowing to anti-business interests" and that "stakeholder capitalism" is "woke"); Kenneth Rapoza, *How The 'Woke' Capitalists Can Save America*, FORBES (Apr. 5, 2020), https://www.forbes.com/sites/kenrapoza/2020/04/05/how-the-woke-capitalists-can-save-america/?sh=3ee8507271ed (noting that international investment fund managers and the World Economic Forum have made ESG "a talking point for a good 10 years now, largely in response to the old lefty, anti-neoliberal World Social Forum" and "[t]hey all talk about diversity, equality, justice"); Paul Polman, *Critics of 'Woke' Capitalism Are Wrong*, FIN. TIMES (Jan. 24, 2022), https://www.ft.com/content/34cf61c7-345d-4277-bf18-c1dbdd8a91fc (discussing "woke capitalism").

[126] *See* Trillions, *The ESG Backlash*, BLOOMBERG (May 11, 2022), https://www.bloomberg.com/news/audio/2022-05-11/the-esg-backlash-podcast (observing critical views that large asset managers have supported ESG and become too "woke" and formed an "ideological cartel"); Richard Morrison, *The ESG Backlash*, NAT'L REV. (Mar. 9, 2022), https://www.nationalreview.com/2022/03/the-esg-backlash/ (discussing how "[c]onservatives have come to see this collection of business trends" towards ESG as "yet another 'woke' assault on mainstream society" and have "growing opposition to ESG" that will cause it "to hit a wall of resistance"); Aron Cramer, *After a Backlash Summer, ESG Needs to*

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The variety of usages of ESG that have developed over time reflect a diverse set of justifications, purposes, and views. Understanding the origins of the term helps shed light on how the possibility of these wide-ranging usages was left open at the outset by the lack of a more specific definition and conceptual grounding. Although ESG was coined to describe the types of issues to be integrated into investment analysis by the financial industry, it was connected to notions of more active engagement to manage environmental and social issues that could mitigate risks and create long-term value, and to UN goals and the principles of the Global Compact that more broadly aimed at producing social benefits, security, and sustainable development. As the term spread, it took on varied associations and meanings that reflect these underlying themes but also in some instances are quite far from where it began.

III. The Promise and Perils of the ESG Moniker

While ESG has become "pervasive,"[127] and taken on various meanings, the strategic choice to coin the term, putting together a wide variety of issues into one moniker, has received little focused examination. It is admittedly difficult to disentangle aspects of the conceptual and rhetorical construction of the term from underlying substantive debate of the merits of ESG that has ensued, and the notion of consequences flowing from such construction must necessarily be caveated in terms of causation that cannot be definitively ascribed. Nonetheless, as the term has now been in circulation for nearly two decades, it is possible to look back to gain insights into impacts of the choice to put E, S, and G into one term and better understand current challenges and potential paths for the future of ESG.

Get Back in the Game, FORTUNE (Sept. 20, 2021), https://fortune.com/2021/09/20/esg-backlash-summer/ (observing "the backlash against the momentum driving widespread adoption of [ESG] policies became a thing").

[127] Larcker et al., *supra* note 9, at 1.

A. The Flexible, Big Tent Approach of ESG and its Alignment Story

The combination of E, S, and G into one moniker has provided a highly flexible term that can vary widely by context, evolve over time, and collectively appeal to a broad range of investors and stakeholders. To explore the advantages of constructing ESG as an umbrella term, each one of these aspects should be considered in turn.

First, ESG was specifically designed to be globally applicable and customizable by context. As the *Who Cares Wins* report explained: "ESG issues relevant to investment decisions differ across regions and sections."[128] Instead of specifying what issues were intended to be integrated into investment analysis, this was left open beyond the words "environmental, social, and governance" and a short list of examples. One of the key examples of an ESG issue provided was the management of corruption and bribery—a topic that is particularly significant in some developing economies around the world and one of the pillars of the Global Compact, but is not front of mind in other geographic areas such as the United States, where board diversity is instead a top issue that has gained traction under the ESG moniker but did not appear on the original list.

Second, ESG was pitched at a highly generic level of phrasing and deliberately avoided words that were already loaded with connotations such as "responsibility," "citizenship," or "sustainability." Instead, the phrase simply combined categories of broad topics, which allows not only for variance by region or context, as discussed above, but also an evolution over time in meaning. Specific sub-issues can change in importance or conceptualization and still fit under the umbrella of the ESG moniker. For instance, "climate change and related risks" was listed as an example under E, and it has been a primary focus in the ESG movement, and as other issues such as water risks come to be appreciated they can be integrated without change to the existing term.[129] Similarly, "workplace health

[128] *See supra* note 54.
[129] *See, e.g.*, World Economic Forum, *We Need to Rethink ESG to Ensure Access to Water and Sanitation for All*, Aug. 20, 2021, https://www.weforum.org/agenda/2021/08/rethink-esg-to-ensure-access-to-water-and-sanitation-for-all/.

and safety" was listed as an example under S, and as a broader array of issues related to workers came into focus and took on the label of "human capital management," this too could easily be fit within the existing umbrella of ESG.[130] Further, as ESG was not coined by regulators as a legal term of art, investors themselves could be the drivers of the evolution over time in their areas of focus.[131]

Third, and perhaps most importantly, ESG has served as a "big tent,"[132] that collectively appeals to a broad range of investors and stakeholders, contributing to the ability of the concept to gain momentum in mainstream audiences. Whereas efforts under the label of CSR faced headwinds and were marginalized with the rise in shareholder primacy and wealth maximization in the late twentieth century, as researchers began to explore links to financial performance and build a "business case" it opened up a pathway for integration in the existing "corporate governance machine" of law, markets, and culture oriented towards shareholders.[133] The *Who Cares Wins* initiative explicitly framed ESG in terms of the business case for integrating issues into mainstream investment analysis, chose a term that was facially more neutral than other existing terms, interjected "governance" which had widespread buy-in from mainstream market actors, and emphasized the theme of aligning goals between those of the financial industry and the UN.[134] This allowed for understanding ESG as value enhancing, and thus threading the needle of legal debates and creating a "business opportunity" for a

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130 *See, e.g.*, Georgiev, *supra* note 55, at 639 (noting that human capital management has quickly rose in "prominence and uptake" and is "broadly fitting within the rubric of environmental, social, and governance (ESG) factors").

131 *See* Wolf-Georg Ringe, *Investor-Led Sustainability in Corporate Governance* (Sept. 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3958960 (arguing that "ESG engagement has the potential to become a very powerful driver towards a more sustainability-oriented future" because "investor-led priorities would follow a more flexible and dynamic pattern rather than complying with inflexible pre-defined criteria").

132 *See* Amanda M. Rose, *A Response to Calls for SEC-Mandated ESG Disclosure*, 98 WASH. U. L. REV. 1821, 1825 (2021) ("The breadth of topics embraced by ESG, and the breadth of motivations spurring the ESG movement, has created a big tent that has undoubtedly served a purpose in terms of helping the various causes of those involved to gain momentum."); *see also* Curtis et al., *supra* note 119, at 401 (""ESG is a rough label for an amalgamation of voices, interest groups, and substantive concerns.").

133 Lund & Pollman, *supra* note 11, at 2613.

134 *Supra* notes 50 & 62.

wide range of institutional players such as asset managers, ratings agencies, accounting firms and the like.[135]

At the same time, "values-based investors who care about whether, and how, corporations address (at least certain) ESG topics due to religious or sociopolitical commitments"[136] also found the ESG term and concept attractive. As the discussion above examines, for many observers ESG indeed became associated with CSR in various ways ranging from a close association based on a view of alignment of value and values to a more direct equating of the concepts so as to see ESG as CSR in a new bottle. Creating a term that could present itself as neutral or value-enhancing, while at the same time welcoming proponents of previous "social"-related concepts, enabled a diverse group of investors and stakeholders to embrace activity under such a term.

B. ESG as a Combination Giving Rise to Challenges and Critiques

Although coining the term ESG helped to create a flexible, big tent that could gain support from a diverse group of investors and stakeholders, it did not resolve tensions between different views of the purpose of ESG or the lack of consensus about the fundamental problem it is addressing. The combination of E, S, and G into one term has given rise to several challenges that are increasingly becoming apparent.

First, the characteristic flexibility that the term embodies by allowing for a variety of understandings of meaning, and a broad array of issues across space and time, has come with several potential downsides. An important challenge that has proven enduring in this regard is the difficulty of pinpointing empirically the relationship between ESG and economic performance. An enormous

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[135] *See* Lund & Pollman, *supra* note 11, at 2614-15; *see also* Rose, *supra* note 132, at 1823 ("ESG proponents also include members of an emerging corps of people and institutions who profit from the movement, including corporate sustainability officers, providers of ESG ratings and indices, accounting firms that offer ESG-related services, and managers of specialized ESG-investment vehicles."); Dana Brakman Reiser & Anne Tucker, *Buyer Beware: Variation and Opacity in ESG and ESG Index Funds*, 41 CARDOZO L. REV. 1921, 1992 (2020) (observing that "[r]ising interest in ESG investing has [] generated a huge market opportunity for the providers of ESG indices and metrics, who are [] capitalizing on this key moment").

[136] *See* Rose, *supra* note 132, at 1822-23.

amount of research has focused on the question and come up short in providing a definitive conclusion. Although significant evidence exists of such a link, the studies often bundle ESG issues together or rely on ESG performance ratings that bundle issues, and often leave unanswered which, if any, corporate policies or activities are actually related to financial performance and whether the relationship is causal.[137] We can understand this challenge, at least in part, as a function of the lack of clear definition of ESG and the fact that it is combining sometimes disparate and changing issues.[138] The mixed empirical evidence gives both proponents and critics of ESG something to point to in debates that will likely continue to rage on.

Similarly, the flexibility and wide-ranging understandings of the term ESG contributes to a multitude of approaches, with more than six hundred ESG ratings organizations and rankings worldwide, and substantial variation among ratings.[139] For some, this diversity is not problematic or it is viewed as a temporary situation as regulators around the world move to require disclosure of additional ESG-related information and companies provide more information on a voluntary basis. And, although there is room for improvement in ESG ratings, that does not mean that they are useless.[140] But for others, this multitude of ESG ratings is evidence that they are "inconsistent" and "subjective."[141] Moves to consolidate disparate ESG ratings systems could lock in inadequate standards in areas such as S that have lagged in development and been more difficult to find alignment

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[137] *See id.* at 1825-27; *see also* Atz et al., *supra* note 98.
[138] *See, e.g.*, Curtis et al., *supra* note 119, at 402 ("One challenge to analyzing the relationship between ESG and economic performance is the absence of a clear definition of ESG.").
[139] *See id.* at 403.
[140] *See* Serafeim, *supra* note 1, at 18. For example, in a study with Aaron Yoon, ESG ratings were found to be helpful in predicting future ESG related news. *Id.* (citing George Serafeim & Aaron Yoon, *Stock Price Reactions to ESG News: The Role of ESG Ratings and Disagreement*, REVIEW OF ACCOUNTING STUDIES (forthcoming).
[141] *See* Rose, *supra* note 132, at 1827; *see also* Hester M. Peirce, Comm'r, SEC, Scarlet Letters: Remarks Before the American Enterprise Institute (June 18, 2019), https://www.sec.gov/news/speech/speech-peirce-061819 (observing substantial variation in ESG ratings and questioning the viability of accurate evaluation).

among investors in assessing and quantifying.[142] This concern about ratings, together with other challenges, in turn feeds a range of critiques of ESG.

One such related challenge is that because ESG was coined in a way that combines wide-ranging issues, companies with diverging performance on E, S, or G can receive ratings that seem at odds with understood purposes of the ESG moniker.[143] For example, electric vehicle manufacturer Tesla is included in many ESG-labeled mutual funds and exchange-traded funds, but observers have pointed to potentially problematic S issues for the company, ranging from a string of racial and sexual discrimination lawsuits and employee reports of a "culture of racism," to supply chain concerns about the production of cobalt which may involve child labor and safety hazards.[144] Ironically, Elon Musk, the CEO of Tesla, has himself called out that "Exxon is rated top ten best in world for environment, social & governance (ESG) by S&P 500, while Tesla didn't make the list!"[145] He followed that "ESG is a scam. It has been weaponized by phony social justice warriors."[146] Although less hyperbolic, investors have similarly registered surprise when they realize that ESG funds they are invested in have large holdings in bank stocks instead of the wind and solar companies they are expecting.[147] Relatedly, as Virginia Harper Ho has observed, "[t]he limitations of ESG ratings and data have led many asset

[142] *See, e.g.*, Michael Posner, *Does Tesla Deserve to Be Treated as an ESG Champion?*, ETHICAL SYSTEMS (Feb. 8, 2022), https://www.ethicalsystems.org/does-tesla-deserve-to-be-treated-as-an-esg-champion/.
[143] A variation of this critique concerns the proliferation of approaches to ESG reporting. *See, e.g.*, Leo E. Strine, Jr., Kirby M. Smith & Reilly Steel, Caremark *and ESG, Perfect Together: A Practical Approach to Implementing an Integrated, Efficient, and Effective* Caremark *and EESG Strategy*, 106 IOWA L. REV. 1885, 1911-12 (2021) (noting the challenge that the proliferation of ESG reporting is "inefficient, encourages greenwashing and gamesmanship of the kind that has characterized corporate governance ratings, and threatens to engage companies more in the rhetoric of EESG than the reality of managing a corporation with the goal of being other-regarding toward company stakeholders and society").
[144] *See id.*; *Black Tesla Employees Describe a Culture of Racism*, L.A. TIMES (Mar. 25, 2022), https://www.latimes.com/business/story/2022-03-25/black-tesla-employees-fremont-plant-racism-california-lawsuit; Dana Hull & Bloomberg, *Tesla Sued By More Women Alleging Sexual Harassment at Plant*, FORTUNE (Dec. 14, 2021), https://fortune.com/2021/12/14/tesla-sued-sexual-harassment-fremont-plant/.
[145] @elonmusk, Twitter (May 18, 2022, 9:09 AM), https://twitter.com/elonmusk/status/1526958110023245829.
[146] *Id.*
[147] Laurence Fletcher & Joshua Oliver, *Green Investing: The Risk of a New Mis-Selling Scandal*, FIN. TIMES (Feb. 19, 2022, https://www.ft.com/content/ae78c05a-0481-4774-8f9b-d3f02e4f2c6f.

managers to expend their own resources to analyze ESG information at added cost, which also has fiduciary implications."[148]

Furthermore, the challenge is not simply that there may be misimpressions of what ESG means or widely varying performances between the components of E, S, and G that can give rise to questionable ratings. Without an integrated approach to ESG factors, "sustainability arbitrage" is possible for both companies and investors.[149] Good performance on one issue, such as low-carbon product development, could be strategically used to mask another, such as poor labor practices.[150]

In some instances, the challenge is not even a problematic rating due to unfortunate performance on an ESG component or more purposeful sustainability arbitrage, but instead inherent tensions between E and S that can arise due to business model or industry.[151] For example, "[a]dverse employment impacts are to be expected in companies in certain sectors such as energy and some regions that will have to execute an extensive transformation to reduce their GHG emissions and to ultimately stay on a path consistent with the net zero ambitions."[152] Environmental concerns and labor interests "are not always reconcilable" and divesting or decommissioning brown assets or transforming a business to new technology can lead to workers losing relevant skills, having lower wages, or getting laid off.[153] If labor has countervailing power it might be able to get concessions, but "it is also possible that balancing of different interests is too difficult and the process of net transition comes often to deadlock" or the company will not give due consideration to social impacts, which

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148 Virginia Harper Ho, *Sustainable Investment & Asset Management: From Resistance to Retooling*, City University of Hong Kong School of Law Legal Studies Research Paper No. 2022-006 (Mar. 23, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4064317. Relying on private initiatives to standardize ESG investment practices and report "has also created costly fragmentation and slowed the development of a level playing field for all investors." *Id.*
149 Alperen A. Gözlügöl, *The Clash of 'E' and 'S' of ESG: Just Transition on the Path to Net Zero and the Implications for Sustainable Corporate Governance and Finance*, SAFE Working Paper No. 325 (Feb. 6, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3962238
150 Nick Robins, Vanda Brunstig & David Wood, *Climate Change and the Just Transition: A Guide for Investor Action* (Dec. 2018), p. 18, https://cpl.hks.harvard.edu/files/cpl/files/jtguidanceforinvestors-1.pdf?m=1569856838.
151 Gözlügöl, *supra* note 149.
152 *Id.* at 4.
153 *Id.* at 4, 9.

could deepen inequality.[154] The potential for stakeholder conflicts arising from this clash between E and S has led to arguments for a "just transition" that promotes swift climate action at the same time as mitigating adverse effects for workers such as with Coasean bargaining or reorganization and re-training programs.[155] To the extent that ESG investors fail to take up the just transition issue, it can add to doubts about whether these investors "walk the talk."[156]

None of these issues are necessarily fatal to the success of the ESG movement, but they can be understood at least in part as stemming from the choice to combine issues in one moniker that may be in tension with each other or lead to tradeoffs that were not addressed in the initial framing. Although the initiative participants espoused the view that the "entire range" of ESG issues relevant to a business should be considered by companies and integrated into investment analysis,[157] and suggested that this approach was aligned with long-term shareholder value,[158] they did not explain how to do so or what to do when an individual component or activity may not enhance value for shareholders. Quite understandably, much was left to be figured out after the initial coining of the term ESG and championing consideration of a broad set of issues – but in hindsight it can be appreciated that the choice of the ESG term came with consequences, such as that priorities were not set in advance as would have been the case had initiative participants instead focused their firepower on a particular issue such as climate change. Additionally, the very flexibility and broad approach embodied by the ESG moniker that contributed to its meteoric rise has also led to challenges that gave fodder to critics.

The critiques of ESG are wide-ranging, from assertions of confusion, unrealistic expectations, and greenwashing to notions that it is crowding out other solutions or inhibiting accountability. As

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154 *Id.* at 17, 19-20.
155 *Id.* at 1; Robins et al., *supra* note 150.
156 Gözlügöl, *supra* note 149, at 27.
157 *See supra* note 52.
158 *See supra* notes 50 & 51.

George Serafeim, a leading scholar of ESG has succinctly observed, "ESG has rapidly become a household name leading to both confusion about what it means and creating unrealistic expectations about its effects."[159]

Commentary and changing positions from regulators can contribute to these impressions of problems with the ESG moniker. For example, some U.S. securities regulators have expressed concern about the use of the ESG label in mutual fund advertising because of worry that the vagueness of the term and "amorphous" issues it encompasses can give investors misimpressions of what they are buying.[160] On the other hand, they warn that having the Securities and Exchange Commission (SEC) standardize the definition of ESG would limit investor choice and put the SEC in the position of being the arbiter of what constitutes an acceptable ESG strategy.[161] As one SEC commissioner observed, "One person's ecofriendly windmill is another person's bird killer."[162]

To take another example, in 2020, the U.S. Department of Labor (DOL) issued a rule that removed all references to ESG and required that ERISA plan fiduciaries focus only on pecuniary factors. It explained that "by conflating unrelated environmental, social, and corporate governance factors into a single term, ESG invites a less than appropriately rigorous analytical approach" for corporate officers and directors to manage as part of the company's "business plan" and for qualified investment professionals to "treat as economic considerations" in evaluating investment.[163] After a change in presidential administration, however, the DOL reversed course and announced a proposed rule that would remove barriers to consideration of ESG factors in selecting investments and

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159 Serafeim, *supra* note 1, at 1.
160 *See* Roisman, *supra* note 85; Pippa Stevens, *'Fooling Ourselves' to Focus on 'Amorphous' Social Investing Factors, Says SEC Commissioner Peirce*, CNBC (Dec. 17, 2019), https://www.cnbc.com/2019/12/17/sec-commissioner-hester-peirce-calls-for-oversight-of-esg-funds.html.
161 Commissioner Hester M. Peirce, Lucy's Human: Remarks at Virtual Roundtable on The Role of Asset Management in ESG Investing (Sept. 17, 2020), https://www.sec.gov/news/speech/peirce-lucys-human-091720.
162 *Id.*
163 Financial Factors in Selecting Plan Investments, 85 Fed. Reg. 72,846 (Nov. 13. 2020) (codified at 28 C.F.R. § 2550.404a-1 (2020)), at 72,857.

exercising shareholder rights.[164] The DOL's disparagement of combining E, S, and G, and varied positions with changing political administrations, ultimately contribute to perceptions that it is not clear whether consideration of ESG issues comes at the expense of financial returns and, moreover, that ESG is ideologically or politically tinged. Such connotations and understandings could in turn fuel challenges to rulemaking that might otherwise help to address some of the existing problems, such as First Amendment challenges to new ESG-related disclosure rules promulgated by the SEC.[165]

Similarly, limited progress on E, and especially S, can lead observers to dismiss the ESG movement as largely ineffectual or "greenwashing."[166] For example, the former chief investment officer for sustainable investing at BlackRock asserted that ESG was "marketing gobbledygook" that "is actively misleading people" and creating a "dangerous distraction" from regulation that would fit the scale of problems such as climate change.[167] Others have noted that when news comes out about insincere commitments to ESG, "[a] movement meant to benefit the public good risks becoming a buzzword coopted to keep maximizing short-term profits."[168] Ironically, such statements reflect how the flexibility of the ESG moniker, and the unresolved tensions at its origins, may contribute to confusion about what it is meant to convey and ultimately achieve.

Many of these challenges and critiques are "hyperboles"[169] or at least can be partially sorted out with time. For example, although there is some cause for concern about the opacity to consumers

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164 US Department of Labor Proposes Rule to Remove Barriers to Considering Environmental, Social, Governance Factors in Plan Management (Oct. 13, 2021), https://www.dol.gov/newsroom/releases/ebsa/ebsa20211013.

165 *See* Elizabeth Pollman, *The Supreme Court and the Pro-Business Paradox*, 135 HARV. L. REV. 220, 251-54 (2021) (discussing potential First Amendment challenges to ESG-related disclosure rules).

166 Tim Quinson, *Greenwashing Is Increasingly Making ESG Moot*, BLOOMBERG (Mar. 16, 2022), https://www.bloomberg.com/news/articles/2022-03-16/greenwashing-is-increasingly-making-esg-investing-moot-green-insight.

167 Robert Armstrong, *The ESG Investing Industry Is Dangerous*, FIN. TIMES (Aug. 23, 2021), https://www.ft.com/content/ec02fd5d-e8bd-45bd-b015-a5799ae820cf (quoting essay by Tariq Fancy). On the false dichotomy between internal and external reforms for corporate governance and regulation, see Aneil Kovvali, *Stark Choices for Corporate Reform*, COLUM. L. REV. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4067505.

168 Michael O'Leary & Warren Valdmanis, *An ESG Reckoning Is Coming*, HARV. BUS. REV. (Mar. 4, 2021), https://hbr.org/2021/03/an-esg-reckoning-is-coming.

169 Serafeim, *supra* note 1, at 19.

of relying on the ESG label in investing,[170] there is also evidence that ESG funds are offering their investors increased ESG exposure without increasing costs or reducing returns.[171] New taxonomies could also be created to help investors make informed investment decisions.[172] Regulatory rulemaking could increase transparency about investment company names.[173]

Yet some aspect underlying the challenges and critiques stem from the construction itself of combining E, S, and G without definition into a singular term and with the stated intention of relevant issues varying by geography and company. Further, as the alignment between shareholder value creation and ESG performance was asserted from the outset but never fully proven or reconciled, a variety of meanings will likely continue to be ascribed to the ESG term. Understood in this light we can see that the challenges and critiques of ESG will not likely be resolved definitively because they are intertwined with the term and its origins. Appreciating the existing limits and uncertainties of ESG might, however, help identify areas in which investors, corporations, and regulators can take a more thoughtful approach.

Finally, as debate about ESG continues and memories of its origins fade, new proposals arise to change the ESG term by adding or subtracting words from its moniker. Such proposals might add emphasis to certain existing components, but would not likely alter the fundamental tension that exists between the term's flexibility and big tent approach and the corresponding challenges and critiques it engenders.

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170 *See, e.g.*, Dana Brakman Reiser & Anne Tucker, *Buyer Beware: Variation and Opacity in ESG and ESG Index Funds*, 41 CARDOZO L. REV. 1921 (2020) (providing data from 2018-2019 showing great variation among ESG funds that is "largely opaque to consumers—who rely on the ESG acronym at their peril").

171 Curtis et al., *supra* note 119, at 393.

172 *See, e.g.*, Eric C. Chaffee, *Index Funds and ESG Hypocrisy*, 71 CASE W. RES. L. REV. 1295, 1317-20 (2021) (proposing a taxonomy for ESG fund names).

173 The SEC has stated it plans to consider whether to propose amendments to the rule under the Investment Company Act that addresses investment company names that are likely to mislead investors. U.S. Securities & Exch. Comm'n, Sunshine Act Notice (May 18, 2022), https://www.sec.gov/os/sunshine-act-notices/sunshine-act-notice-open-052522.

For example, Leo Strine, the former Chief Justice of the Delaware Supreme Court, has proposed that another E be added to ESG to increase the salience of employees in ESG discussions and analyses.[174] Although such construction might laudably keep the treatment of workers in the mix of ESG issues commonly addressed, the S in ESG already included such a possibility and labor-related issues have been a key example since the *Who Cares Wins* initiative, building on one of the core principles of the Global Compact. Further, adding a component does not change the difficulty of empirical measurement and the potential for tensions and tradeoffs.

Another proposal, advanced by David Larcker and Brian Tayan, is to take the G out of ESG.[175] As a reflection of how the history of the term ESG has been lost, they observe that "[a] perplexing question is why governance—the 'G' in ESG—is included as a third factor."[176] In their view, "[g]overnance is unlike E and S" and "an ineffective measure of how socially responsible a company is" and so "[a] more honest assessment of a company's commitment to stakeholders would leave governance variables out of the rating."[177] Yet Larcker and Tayan seem to simply conceive of governance differently from the institutions that originally coined the term ESG. Instead of integrating consideration of governance mechanisms that are interlinked with E and S, and that execute on such policies, Larcker and Tayan characterize "governance [a]s an *overlay*" and "environmental and social components of ESG a[s] *outcomes*."[178] Such an approach might appeal to some ESG proponents, but likely only a fraction as the endorsing institutions of the *Who Cares Wins* initiative included some of the world's largest banks and they viewed G as crucially interlinked to fulfilling the promise of better

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[174] *See* Leo E. Strine, Jr., *Toward Fair and Sustainable Capitalism* 6 (Roosevelt Inst., Working Paper No. 202008, 2020), https://rooseveltinstitute.org/publications/toward-fair-and-sustainable-capitalism/.
[175] *See* Larcker et al., *supra* note 9, at 3 (arguing that it is a "myth" of ESG that it should include governance because "[t]he need for governance quality is universal among organizations"); David F. Larcker & Brian Tayan, *The Case for Taking the 'G' Out of ESG*, WALL ST. J. (Apr. 28, 2022), https://www.wsj.com/articles/esg-the-case-for-taking-out-the-g-11651004068.
[176] Larcker & Tayan, *supra* note 175.
[177] *Id.*
[178] *Id.*

environmental and social performance. Moreover, even if a component of ESG was removed, there would still be two, each with a multiplicity of possible sub-issues that could vary widely by context and over time, and thus not solving the difficulty of empirical measurement or the potential for tensions and tradeoffs.

Interestingly, it is often the S instead of G that is "single[d] out . . . as a different kind of category from its peers."[179] As David Wood explained, "The E invokes issues as such carbon intensity or energy and resource consumption that are easily quantifiable and with comparable units of measure; The G invokes industry standards of board structure, shareholder rights, or standards of business ethics on which there is relatively widespread agreement in principle; but the S invokes issues which are often hard to quantify, not so clearly linked to the risk/reward analysis in investment decision-making, and may touch on culturally specific norms that do not so easily translate into guidance for (often globally focused) investment decision-makers."[180] The S might be seen as "softer" or "mushier" than E and G, as well as "more likely to invoke ethical issues that lie beyond the scope of proper investment strategy or to require cultural judgments about potential consumer, reputational, or political risks that are particularly difficult to gauge."[181] In any event, whether it is the S or the G that is more unlike the others, such proposals and analyses of the divergence between ESG components only underscore that the term will likely continue to be the site of contestation even as its embrace has gone mainstream.

CONCLUSION

Within just a couple decades the term ESG has gone from closed-door sessions of financial industry executives and other institutional leaders gathered by the United Nations to the everyday

[179] Wood, *supra* note 93, at 554-55 ("There have been dozens, if not hundreds, of conference panels, blog posts, listserve chats, and other discussions that pose the S in ESG as a problem to be solved.").
[180] *Id.*
[181] *Id.* at 555.

lingo of investors, asset managers, corporate officers and directors, employees, and consumers around the world. This Article has provided an in-depth examination of the term and its implications, starting from its history and evolution in usage to the promise and perils of its construction. This exploration reveals that ESG has a specific origin, but is not a fixed concept beyond the combination of three categories of issues that underlie its moniker. The flexibility and big tent approach of the term ESG, and its facilitation of claims of alignment between value and values, are at once part of the success story in diffusing ESG widely and forming a diverse movement of proponents, but also the source of challenges and critiques that have emerged and will likely continue into the foreseeable future.