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ESG — US State-Level Developments for Private Capital and Financial Institutions

Private capital providers, investors, asset managers, and financial institutions will likely continue to face a fragmented regulatory landscape on ESG matters.

Various US states have taken and continue to take action on ESG investing and other matters, with new variants emerging regularly. Some of the state bills, laws, and actions overlap thematically, and indeed some are based on common model bills. However, there are sufficient differences among them — and the politics and politicians underlying them — that make it prudent to review each state's profile separately. This activity has created a fragmented regulatory landscape for private capital providers, investors, asset managers, and financial institutions in particular, and one that promises to remain so (or even become more fragmented) in the near- to mid-term.

This resource provides a practical summary of selected key developments among many of the largest states by investment fund size. It aims to serve as an initial resource for private capital and related financial entities in understanding the major US state-level policies that may impact them.

These actions have generally fallen along one of several core themes or theories; however, the specific parameters and implementation have not been uniform from state to state. As such, it is important to investigate — on a law-by-law and entity-by-entity basis — how they may apply to particular entities and investment vehicles, as well as how to respond to the varying requirements in the most efficient and effective manner.

Latham & Watkins is actively monitoring this space; if you have any questions, please contact one of the parties listed below or the Latham lawyer with whom you normally consult.

Updated as of May 30, 2024

Arkansas

In 2023, Arkansas adopted several laws to restrict the consideration of ESG factors, including Senate Bill (SB) 62, which prohibits public entities from contracting with entities that have been determined to boycott the energy, fossil fuel, firearms, or ammunition industries. It also adopted House Bill (HB) 1253, which requires fiduciaries of state and local pension plans to consider only "pecuniary factors" in their decision-making. While HB 1253 provides certain limited caveats, these still restrict potential arguments that various ESG factors would be considered pecuniary in many situations.

Also in 2023, Arkansas adopted HB 1307, which among other things requires divestment of direct or indirect holdings with financial service providers that have been deemed to "discriminate against energy companies or firearm entities or otherwise refuse to deal based on environmental, social justice, and other governance-related factors," as such terms are defined under the law. Another 2023 law, HB 1845, assigned the authority for preparing this list to an ESG Oversight Committee.

California

California has adopted various laws regarding business entities' climate-related risk and emissions profiles. In October 2023, California adopted a suite of legislation addressing discrete aspects of this topic.

SB 253 requires public or private US entities doing business in California, with annual revenues of over $1 billion, to annually report their Scope 1 and Scope 2 greenhouse gas (GHG) emissions starting in 2026 and their Scope 3 emissions starting in 2027.

SB 261 requires public or private US entities doing business in California, with annual revenues of over $500 million, to submit a climate-related financial risk report starting in 2026, and biennially thereafter. Further information on these laws is available in our Client Alert. However, please note both of these laws are currently subject to litigation.

Assembly Bill (AB) 1305 requires public or private entities to make disclosures on their website if they make certain climate-related claims and/or participate in voluntary carbon offset markets within California. The law does not set a revenue threshold, and as such is expected to capture many entities in scope. The primary sponsor of AB 1305, Assembly Member Jesse Gabriel, introduced AB 2331 on February 12, 2024. That bill aims to clarify and amend certain elements of AB 1305, such as the disclosure timeline and the treatment of renewable energy credits/certificates. The bill passed the California Assembly on May 13, 2024, and now is before the California Senate.

SB 1036 would subject sellers of voluntary carbon offsets to California's consumer protection laws, and fine companies that sell offsets that are unlikely to be "quantifiable, real or additional." Governor Gavin Newsom vetoed a previous version of this bill, SB 390, on October 7, 2023, at the same time he signed the above climate bills into law. SB 1036 passed the California Senate on May 21, 2024, and now is before the California Assembly.

Beyond climate, California has also adopted a law requiring "venture capital companies" with sufficient ties to California to collect, and annually report starting in 2025, demographic information of the founding team members at companies in which they invest during the prior year. The scope of the law is broad, and may apply to investment vehicles that are not traditionally thought of as venture capital companies, including private equity funds and co-investment vehicles. Further detail is available in our Client Alert.

Florida

On May 5, 2023, Florida Governor Ron DeSantis signed into law HB 3, which restricts the use of certain ESG factors by asset managers and financial institutions. The law took effect July 1, 2023, and requires, among other aspects, that investment advisers or managers acting on behalf of Florida public pensions make investment decisions based only on "pecuniary factors." The law states that the definition of "pecuniary factor" excludes the "consideration or furtherance of any social, political, or ideological interests."

Read this Latham Client Alert for more information on HB 3.

On May 2, 2024, Governor DeSantis signed into law HB 989, which includes several provisions to expand the requirements of HB 3 relating to financial institutions.

In particular, HB 3 requires financial institutions to submit an attestation on a state-prescribed form that they are in compliance with the provisions against "unsafe and unsound" practices as defined under the financial institutions code (including not canceling, suspending, denying, terminating, or otherwise discriminating against the availability or terms/conditions of financial services based on a variety of bases).

HB 3 required this attestation for financial institutions "subject to the financial institution code." As such, in 2023, the prevailing view was that it only applied to state-chartered financial institutions. However, HB 989 amended this to say financial institutions "as defined in s. 655.005." This is defined as a "state or federal savings or thrift association, bank, savings bank, trust company, international bank agency, international banking corporation, international branch, international representative office, international administrative office, international trust entity, international trust company representative office, qualified limited service affiliate, credit union, or an agreement corporation operating pursuant to s. 25 of the Federal Reserve Act, 12 U.S.C. ss. 601 et seq. or Edge Act corporation organized pursuant to s. 25(a) of the Federal Reserve Act, 12 U.S.C. ss. 611 et seq."

The attestation form itself does not allow for much nuance and effectively requires attestation of compliance or non-compliance, which may be factually difficult to determine for certain financial institutions.

Georgia

Similar to Florida, on May 6, 2024, Georgia enacted HB 481, which prohibits, among other things, fiduciaries of its public retirement systems from sacrificing investment returns or accepting increased investment risks to promote nonpecuniary interests, including furthering social, political, or ideological interests. Subject fiduciaries include any retirement system administration or any person that with respect to that system exercises discretionary authority or control over the management or disposition of the system's assets, renders investment advice for compensation with respect to money or property of the system, or has any discretionary authority or control in the management or administration of the system. The law indicates that each fiduciary shall discharge its duties solely in the interests of plan participants and their beneficiaries and shall only make investments with care, skill, prudence, and diligence under the circumstances then prevailing that a prudent expert acting in like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims.

On April 22, 2024, Georgia enacted HB 1018, effective July 1, 2024, which bars financial institutions from assigning a merchant category code to firearm retailers. Such a code would allow institutions to differentiate firearm retailers from other general or sporting goods retailers. HB 1018 would thus bar institutions from discriminating against firearms retailers based on their engagement with the commerce of firearms or ammunition, including declining a lawful payment card transaction based solely on the assignment or nonassignment of a firearms code. The law provides a safety valve for financial institutions to take actions related to dispute processing, fraud management, or protecting transaction integrity from concerns relating to illegal activities or cyber risks.

Illinois

The Illinois Sustainable Investing Act went into effect on January 1, 2020. It requires all governmental entities in Illinois that manage public funds to "prudently integrate sustainability factors" into investment decision-making and analysis. The law states that "Sustainability factors may include, but are not limited to" (1) corporate governance and leadership factors; (2) environmental factors; (3) social capital factors; (4) human capital factors; and (5) business model and innovation factors.

Building on the Sustainable Investing Act, on July 28, 2023, Illinois adopted HB 2782. It requires investment managers that act as fiduciaries for any governmental agency to provide annual disclosure reports describing how the manager "prudently integrates sustainability factors" into their investment processes and decisions. HB 2782 went into effect on January 1, 2024.

Illinois also adopted SB 2152 on August 4, 2023. The bill gives the State Treasurer, upon an affirmative vote, the authority to manage proxy voting for shares held by the Illinois State Employees' Retirement System (SERS).

Various fossil fuel divestment bills, including SB 3717 and HB 5268 that would require state pension systems and the University of Illinois Foundation to divest from certain types of fossil fuel companies, have been introduced in the state legislature in 2024, which remain pending.

Louisiana

In early 2024, the Louisiana Senate introduced a bill, SB 5, to require fiduciaries of public retirement systems in the state to consider "only financial factors" in discharging duties with respect to such plan. Similar to certain other states, the bill would explicitly exclude "social, political, or ideological interests" from the scope of financial decisions. However, under the bill a fiduciary would be deemed to have acted to further such excluded interests if it takes any of several actions (e.g., advertising, communication with portfolio companies, participation in various initiatives or coalitions, or reporting) indicating that the fiduciary is considering anything beyond what is required by applicable federal or state law on several topics.

These topics include: (1) GHG emissions, including disclosures; (2) board/workforce composition, compensation, or disclosures; (3) environmental standards/disclosures; (4) access to abortion, sex or gender change, or transgender surgery; or (5) relation to firearms, ammunition, or components/accessories for same.

Maryland

Maryland passed HB 740 on April 4, 2022, which requires the State Retirement and Pension System (SRPS) to consider and manage climate-related risks in connection with the investment system's assets. The law also requires the SRPS to submit a report annually of risk assessments, including climate risks, and requires the chief investment officer to evaluate whether investment managers are "taking steps to transition to a more sustainable business model aligned with a low-carbon economy."

A separate law, HB 1212, which passed on May 9, 2024, requires the State Retirement Agency to hire a director of diversity, equity, and inclusion (DEI) to promote and support diversity both at the State Retirement Agency and in investment decisions. The law also requires the Investment Division of the State Retirement Agency to hire an individual to (1) monitor, evaluate, and quantify risks and effects of material ESG factors; (2) integrate consideration of material ESG factors into investment diligence and recommendations across asset classes; and (3) provide recommendation to the chief investment officers based on analysis of material ESG factors, including DEI.

Massachusetts

While Massachusetts policy has typically been to advance consideration of ESG factors, much of this has focused on public securities. The Massachusetts Pension Reserves

Investment Management (PRIM) Board, which manages the state's pooled investment fund of various state and local pension assets, approved proxy rules in February 2022 that allow for voting against directors at companies that are not aligned with the Paris Climate Agreement and Climate Action 100+, as part of a commitment to establish a framework with the goals of limiting global warming to 1.5ºC and reaching net zero emissions by 2050. The PRIM Board updated these guidelines in 2024 to outline their voting strategies, reaffirming their commitment to ESG as a value-enhancing investment and management strategy.

In the 2023–2024 session, the Massachusetts House and Senate have introduced various bills related to sustainable investment considerations for the Pension Reserves Investment Trust or the PRIM Board funds. These include H.2515 and S.1723 to authorize divestment from fossil fuel companies; S.1690, H.2591, and H.2503 to authorize divestment from ammunition and firearms, and H.2504 to mandate consideration of climate risk in public pension holdings. These bills remain in committee as of May 2024.

Michigan

The State of Michigan Investment Board publicly reports its investment policy, which outlines that the public Michigan funds are to follow the ESG directives set by the Michigan legislature. As of May 2024, no ESG-related polices have been enacted, and the fund's investing decisions are governed by the Public Act of 314.

In 2023, the Michigan House proposed HB 4381, a bill to limit state and local pension funds from considering ESG in investment strategies by restricting permitted considerations to "pecuniary factors." A similar bill was introduced in 2022, but neither has progressed beyond committee.

Minnesota

Minnesota legislators have also introduced several bills to promote or limit consideration of ESG factors in connection with state funds in recent sessions, but none has passed. For instance, SB 1225, introduced on February 6, 2023, would prevent the Minnesota State Board of Investment (MSBI) from investing in assets that exclude Minnesota companies on ESG grounds. HB 4790, introduced on March 11, 2024, on the other hand, would require MSBI to consider certain sustainability factors in its investment decisions.

On February 26, 2020, MSBI adopted a resolution "concerning environmental, social, and governance initiatives." Pursuant to this resolution, MSBI has taken several actions regarding ESG, including issuing ESG-related reports, engaging "with corporations on ESG related issues," and developing and implementing "plans for reporting and addressing ESG investment risks."

Missouri

On January 17, 2023, Secretary of State Jay Ashcroft proposed two securities rules that would require investment managers to obtain client consent before recommending any investment that may consider ESG factors. The rules were published in the Code of State Regulations on June 30, 2023, and went into effect on July 30, 2023. On August 10, 2023, the Securities Industry and Financial Markets Association (SIFMA) — a trade group that represents banks, asset managers, and broker dealers — filed a lawsuit in federal court, arguing that the rules are unconstitutional and preempted by federal law. In January 2024, a federal judge rejected Missouri's argument that SIFMA lacked standing to challenge the rules, and allowed the suit to proceed on January 5, 2024.

The rules are similar in substance and effect to HB 863, which was introduced in the legislature on January 18, 2023, but failed to pass during the 2023 session. A similar bill, HB 2799, was reintroduced in the 2024 legislative session on February 26, 2024.

Another bill, SB 177, which died in committee in the 2023 legislative session, would have prohibited state entities from giving preferential treatment to offerors, bidders, contractors, or subcontractors based on "ESG Scores." On March 3, 2024, state legislators introduced SB 1518, to repropose effectively identical legislation.

New Jersey

The New Jersey Division of Investment is a member of Climate Action 100+, and is subject to an ESG policy adopted in 2018 by the governing State Investment Council. The policy allows considering ESG analysis in evaluating fund assets, and the division describes sustainability as core to their role as a fiduciary. The division also maintains a standalone climate change policy, which recognizes the relationship between ESG policies, climate risk, and economic value. The policy outlines rules for considering climate change in investment and corporate governance decisions, including engagement with alternative investment fund managers, and provides for consideration of ESG factors in investment decisions insofar as the factors relate to risk, opportunity, and economic considerations.

In January and February 2024, the New Jersey Legislature introduced bills to prohibit the state from investing pension and annuity funds into certain industries. These bills include A1473/S2487 to prohibit investment in the tobacco industry, S1115 to prohibit investment into firearms for civilian use, S1595 to prohibit investment into and require divestment from nuclear weapons, and S198 to prohibit investment into and require divestment from certain large publicly traded fossil fuel companies. These bills remain in committee. All of these initiatives follow bills introduced in prior legislative sessions that did not make it out of committee.

New York

In the 2023–2024 session, the New York State Legislature introduced bills to establish a climate corporate data accountability act, S897C/A4123A, which would require certain businesses within the state to disclose GHG emissions and establish a climate accountability and emissions disclosure fund. The legislature will also consider S5437, a proposed requirement that companies subject to the supervision of the state Department of Financial Services with $500 million or more of gross revenue in the previous year to prepare and publish an annual climate-related financial risk report.

Other climate-related bills introduced in this session include S899/A1101 and S1953, to require City University of New York (CUNY) and State University of New York (SUNY) trustees and the New York State Teachers' Retirement System to divest from fossil fuel companies. The legislature will also consider S205, a bill to divest state funds from private prisons, and A1831, a bill to prohibit firms in which the New York State Common Retirement Fund invests from pledging corporate contributions to political action committees, to impose caps on contributions, and to require disclosure for executives at those firms. In contrast, bill A4090 was introduced to prohibit using ESG criteria as a screening method in investment decisions of state pension funds.

In February 2024, the New York State Common Retirement Fund announced measures to protect the state pension fund from climate risk, including restricting certain investments in oil and gas companies and increasing investment in the Sustainable Investments and Climate Solutions Program by $20 billion. This move follows a 2022 divestment from shale oil and gas companies, and is part of the fund's 2019 Climate Action Plan on sustainable investing. The fund previously adopted a target of net zero by 2040, guiding investment strategies and requiring divestment from companies that fail to meet minimum standards.

In 2023, the New York City Employees' Retirement System (NYCERS), the Teachers Retirement System (TRS), and the Board of Education Retirement System (BERS) also adopted implementation plans for achieving net zero by 2040. These plans provide for GHG emissions reductions targets in operations as well as public equity and corporate bond portfolios, actions to encourage asset managers to collaborate in these efforts, and commitments to measure and report implementation progress. However, an ongoing lawsuit against NYCERS, TRS, and BERS (*Wong v. NYCERS*) alleges breach of fiduciary duties under New York common law and New York insurance regulations to their pension plan participants and beneficiaries in response to the funds' divestment in fossil fuel companies. Among other relief, the claim seeks money damages, an order requiring defendants to make the pension plans whole for losses caused by the divestment actions, and appointment of an independent fiduciary to report on what fossil fuel-related investments should be added to the plans' portfolios.

North Carolina

On June 27, 2023, North Carolina passed HB 750, which prohibits the state from using ESG policies to hire, fire, or evaluate employees. That law also provides that the state treasurer shall consider only pecuniary factors in making investments and that environmental or social considerations may only be considered as pecuniary factors if they present economic risks or opportunities that qualified professionals would treat as material economic considerations under generally accepted investment theories. Governor Roy Cooper initially vetoed the bill, but the state House and Senate overrode that veto.

North Carolina has multiple pieces of pending legislation related to ESG. These include a bill to require public pension plan fiduciaries to consider only "pecuniary factors," a bill to prohibit financial institutions from refusing financial services on the basis of certain value-based criteria such as ESG factors, and a bill to prohibit state retirement systems and the state treasurer from considering ESG factors in awarding state contracts.

Ohio

Ohio has no notable laws regarding financial entities' consideration of ESG matters currently in effect, although the legislature has proposed certain bills to restrict consideration of ESG factors. For example SB 6, which passed the Ohio Senate on May 10, 2023, and is currently pending in the Ohio House, would require state investment boards to make investment decisions with "the sole purpose of maximizing the return on its investments" and prohibit such boards from taking actions "with the primary purpose of influencing any social or environmental policy or attempting to influence the governance of any corporation."

Oregon

Oregon has no notable laws regarding financial entities' consideration of ESG matters currently in effect, although the legislature has recently proposed several bills that would require state funds to incorporate or limit use of ESG factors. These included bills to require the state treasurer to include climate risk disclosures when marketing securities to potential investors (HB 3478), to require divestment from certain carbon-intensive sectors (HB 2601), and to require state pension plans to consider only "pecuniary factors" in their investments (HB 3219). None of these bills has progressed beyond committee. HB 4083 directs the state treasurer to make efforts to eliminate certain investments in thermal coal companies, and Governor Tina Kotek signed the bill into law on April 4, 2024.

On February 6, 2024, the State Treasurer released a plan for the Oregon Public Employees Retirement Fund (OPERF) to achieve a 60% reduction in emissions by 2035 and to have a net zero carbon emissions portfolio by no later than 2050.

Pennsylvania

In the 2023–2024 session, the Pennsylvania House introduced HB 334 to constrain the use of ESG factors by financial institutions. In particular, the legislation would prevent a financial institution from denying a financial service to any person "except to the extent justified by the documented failure to meet quantitative, impartial risk-based financial standards established in advance by the financial institution or in compliance with certain rules promulgated by the Pennsylvania Department of Banking and Securities." The bill would also require financial institutions to discuss any standards or guidelines based on ESG criteria to the department and disclose to any person denied financial services the specific standards, guidelines, and criteria used to support the denial.

In 2023, Pennsylvania Treasurer Stacy Garrity indicated a lack of support for ESG considerations in investing, describing it as advancing social objectives and not necessarily in line with the prudent investor standard guiding her duty as treasurer, though she has supported divestment on certain political issues.

Texas

On June 14, 2021, the Texas legislature passed SB 13, which prohibits multiple state entities from investing in financial companies that the Texas comptroller determines boycott fossil fuel energy companies. It also requires such entities to divest from these companies if they have investments. SB 13 also prohibits state government entities from entering into contracts with companies determined to be boycotting energy companies. The state comptroller has published and updates, at least annually, a list of financial companies that it deems to boycott energy companies. The comptroller released the first list in August 2022, an update in March 2023, and last updated its list in October 2023.

The law exempts state entities from divesting from indirect holdings in actively or passively managed investment or private equity funds or if the entity determines the requirements would be inconsistent with its fiduciary responsibilities for the investment of its assets or other laws.

As such, some funds in Texas may still incorporate certain ESG considerations. For example, the Teacher Retirement System of Texas adopted a policy on September 15, 2023, effective October 1, 2023, that directs the investment manager division to consider ESG factors material to long-term returns and risks.

In 2023, the Texas legislature enacted SB 833, which prohibits insurers from using ESG models, scores, factors, or standards to charge differing rates to business or risks in the same class. Various other bills to limit the consideration of ESG matters or to otherwise protect certain industries have been introduced in recent legislative sessions, such as HB 5245, HB 5252, and SB 2149. State policymakers have also been continually vocal about their opposition to ESG initiatives.

Virginia

Virginia has no notable ESG laws currently in effect regarding financial entities' consideration of ESG matters, although bills both to promote and limit certain ESG considerations have been proposed in recent years.

Washington

Washington has no notable laws currently in effect regarding financial entities' consideration of ESG matters, although the legislature has recently proposed several bills on state ESG investments and climate disclosures for business.

HB 1283 would require the Washington State Investment Board (WSIB) to publicly report analysis of ESG policies within its private and public market portfolios, including climate-related financial risk, social responsibility, and corporate governance, as well as the alignment of funds with the Paris Agreement and Washington's climate policy goals. The bill would also require the WSIB to provide at least three investment options for individuals participating in self-directed investment funds that are consistent with these ESG policies. The Washington House of Representatives first read the bill in 2023 and reintroduced it on January 8, 2024.

HB 2405 would require the WSIB to integrate sustainability factors into its investment decision-making, which should incorporate "at a minimum" corporate governance and leadership, environmental, social capital, human capital, and business model and innovation factors. The bill would also require the WSIB to develop proxy voting guidelines that recognize climate change as a business and systemic risk and support shareholder resolutions that call for entities to reduce activities that contribute to climate change, or provide public written comments on why the board chose not to support them. The bill is pending in the Washington legislature.

SB 6092, effectively now a "study only" bill, would require the Washington Department of Ecology to develop policy recommendations for climate-related disclosure requirements in Washington, including assessment of whether the climate reporting rules finalized by the US Securities and Exchange Commission are sufficient for tracking reporting entities' GHG emissions. The bill is still pending in the Washington legislature.

Wisconsin

Legislation introduced in the Wisconsin Senate on November 15, 2023, would prevent state agencies or any local government unit from considering social and governance criteria, DEI policies, or any other "political or ideological factors" in awarding grants, loans, or any other financial assistance. The bill failed to pass on April 15, 2024, when the legislative session adjourned without the bill having left committee.

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