Antitrust Risks of ESG Initiatives: Rhetoric vs. Reality

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Recently, there have been rumblings of antitrust enforcement in response to the increasing prominence of corporate policies furthering environmental, social and governance ('ESG') goals. The ESG moniker has been used as shorthand for a broad range of initiatives by private actors, including collaborative efforts to issue industry-wide "best practices," adherence to environmentally conscious production processes, and commitments to sustainable investing. Despite the arguably laudable objectives of the ESG movement, there are indications that multi-firm ESG initiatives have fallen in the crosshairs of antitrust enforcers. Most notably, elected representatives of U.S. oil and gas constituents have threatened antitrust liability against financial institutions that have adopted lending or investing policies aimed at climate change, particularly those favoring net-zero growth for carbon emissions. This article traces the growing likelihood of antitrust challenges to ESG policies, and explains why the threat of enforcement actions does not necessarily equate to an increased risk of liability. We also discuss how firms can mitigate their exposure to potential antitrust liability by refraining from forms of concerted conduct that have been deemed *per se* unlawful under antitrust law, and identify which types of coordinated activity are typically permitted where reasonable safeguards to competition exist.

Recent Enforcement Threats

Like many areas of contemporary American culture, climate change and sustainability issues have been characterized by deepening partisan divisions – and antitrust enforcement is no exception. Indeed, virtually all threats of U.S. antitrust enforcement against ESG initiatives have come from elected Republican officials. Five Republican Senators, including the Ranking Members of the Judiciary Committee and the Subcommittee on Competition Policy, issued a letter in November to ESG practice leaders at dozens of law firms warning them "to fully inform clients of the risks they incur by participating in climate cartels and other ill-advised ESG schemes." In the lower chamber, Republican members of the House Judiciary Committee have launched an antitrust investigation into the activities of Climate 100+. Various Republican elected officials have also placed a target on the backs of leading asset managers and financial institutions by naming them as perpetrators of "climate cartels." Coordinated climate mitigation efforts are facing greater antitrust scrutiny in Europe as well, albeit from regulators generally seen as more aligned with liberal policy positions. For example, the European Commission launched a dawn raid this past May on several fashion

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houses that had previously signed an open letter calling for more sustainable and eco-friendly industry practices.

The most likely immediate sources of U.S. antitrust challenges to climate initiatives appear to be Republican State Attorneys General and fossil fuel interests. In addition to the Federal Trade Commission and Justice Department, state attorneys general and private parties with antitrust standing are permitted to file enforcement actions arising from violations of federal antitrust law. Indeed, nineteen states announced in October their launch of a joint antitrust investigation into major banks' participation in the United Nations' Net-Zero Banking Alliance. The action is particularly significant considering that NZBA now reportedly includes more than 120 member banks representing 40% of global banking assets. By contrast, federal antitrust enforcers have not signaled an intent to target climate or other ESG initiatives, though Federal Trade Commission Chair Lina Khan and Assistant Attorney General Jonathan Kanter have also made clear that ESG coordination is not exempt in any way from antitrust liability.

While anticipating and defending against antitrust enforcement actions can be costly, the actual risks of antitrust liability (and potentially catastrophic damages) stemming from ESG initiatives are far more opaque than Republican officials' broadsides would suggest. For example, in September 2019, the DOJ opened an antitrust investigation into four automakers after the companies reached an agreement with the state of California to adhere to emissions standards more restrictive than those imposed under federal law. Less than six months later, and following allegations of political bias, the DOJ concluded its investigation without further action. As the next several paragraphs explain, different modes of coordinated conduct present varying risks of antitrust liability, and businesses should tailor their ESG policies accordingly.

Section 1 of the Sherman Act

The degree of antitrust risk associated with ESG activities – as with all business conduct – will depend on the specific conduct at issue, and the manner in which the coordinating firms carry out the arrangement. The primary statute regulating coordination between independent entities is Section 1 of the Sherman Act, 15 U.S.C. § 1, which forbids "conspiracies" in restraint of trade. Because every contract is a restraint of trade to at least some extent, the courts have long held that only "unreasonable" restraints of trade violate Section 1.

It is also settled law that some types of restraints "always or almost always tend to restrict competition and decrease output," and therefore should be treated by the courts as unlawful *per se*. First in this limited class of conduct is price-fixing among competitors, which is considered to be a "naked" restraint on competition and has been called the "archetype example" of *per se* unlawful restraints. In other words, price-fixing schemes are always unlawful, regardless of the parties' motivations or how the particular scheme affects consumers. Less clear is whether group boycotts, in which multiple competitors agree not to deal with another competitor, are *per se* illegal; courts

have characterized group boycotts as *per se* illegal in some instances while declining to do so in others. It is this more ambiguous "boycott" arrangement that we typically see referenced in calls for antitrust enforcement against climate initiatives.

In cases where alleged boycotts are found to fall short of "naked" restraints, the challenged conduct is analyzed under the default antitrust standard known as the "rule of reason." Thus, where banks are alleged participants in a group boycott of borrowers failing to meet specific climate standards, courts will apply the rule of reason if the purported conduct is found not to be a "naked" restraint subject to *per se* illegality. Rule of reason analysis requires the government enforcer or private plaintiff to demonstrate with economic evidence that on balance, the challenged conduct is anticompetitive rather than procompetitive. Under the rule of reason, it is very difficult for a plaintiff to meet the burden of proof, and claims are frequently defeated by the defense's identification of a plausible procompetitive justification for the conduct. Regarding net-zero lending initiatives, it may be that efforts to slow or reverse climate change, as a means of preserving banking consumers' very lives, is a procompetitive purpose for the lending policies.

Guidelines for Risk Mitigation

Because there is less antitrust exposure where conduct is subject to rule of reason analysis rather than the *per se* rule, firms can mitigate their risk of liability by avoiding conduct that typically falls under the *per se* rule. The following general guidelines may be helpful:

- Avoid participating in any ESG-related industry group that has not vetted its protocol with a reputable outside antitrust counsel. The group's antitrust advice should be transparent.
- Before joining any ESG-related industry group, a company should discuss its proposed participation with its own antitrust counsel.
- Be clear that each company-member will exercise its own independent business judgment in deciding whether to unilaterally adopt any goals or guidelines. Generally, do not agree with industry competitors to be bound by industry rules of conduct.
- Never agree with an industry group to boycott any specific customer or competitor.
- Participate in industry benchmarking surveys only to the extent that the surveys have been developed explicitly in conformance with federal antitrust enforcement guidelines for benchmarking.
- Consider antitrust defenses that may be available in specific circumstances, such as the *Noerr-Pennington* defense.

Conclusion

In the coming months, Republican state attorneys general and House Republicans are expected to pursue antitrust investigations into climate-focused ESG initiatives. Enforcement actions may

follow, including from private plaintiffs. Firms wishing to adopt and implement ESG policies with minimal antitrust risk should remain alert and thoughtful as to the processes by which they participate in industry-wide initiatives. The costs associated with defending participation in such initiatives may be ultimately unavoidable for some, but the ability to mitigate the risk of antitrust liability – and even costlier damages – is within the reach of all.

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