UCSD UNDERGRADUATE LAW REVIEW

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Enhancing Fund Governance to Combat Greenwashing in ESG Securities Under Delaware Law

ABSTRACT. A concern in the growing ESG investment landscape is greenwashing, which is the misrepresentation of sustainability credentials in financial products. Due to gaps in fiduciary law, fund managers and corporate directors in Delaware, the leading jurisdiction for corporate and fund governance in the US, have been able to include ESG criteria like labor policies, board diversity metrics, or greenhouse gas emissions targets in investment strategies without a strong financial justification or efficient oversight procedures. Fiduciaries may rely on ESG factors that have no proven connection to risk-adjusted returns if there is no statutory financial materiality standard, which increases the possibility of misleading investors. Although opinions are still dispersed and primarily reactive, cases like *Spence v. American Airlines*, *SEC v. BNY Mellon*, and *Gatz Properties v. Auriga Capital* show a growing judicial awareness of these risks. Specifically amending Delaware Titles 8, 12, and 6 to create a default financial materiality threshold and directing fiduciaries across corporations, trusts, and other entities would be a more successful strategy. With the implied covenant of good faith and fair dealing, this default rule would preserve contractual flexibility while restricting ESG integration to financial considerations unless specifically permitted. By doing this, Delaware can strengthen fiduciary discipline, reduce greenwashing, and make ESG-related investment practices more transparent.

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INTRODUCTION

Environmental, Social, and Governance (ESG) securities are seeing an unprecedented influx of funds, with U.S. sustainable fund assets reaching $344 billion by the end of 2024, a 6.3 percent increase from 2023.[1] However, this ESG investing boom has incentivized investment banks and asset managers to engage in "greenwashing." The Australian Securities and Investments Commission (ASIC) describes greenwashing in the financial sector as "the practice of misrepresenting the extent to which a financial product or investment strategy is environmentally friendly, sustainable or ethical."[2] The U.S. Securities and Exchange Commission (SEC) does not provide an official definition of greenwashing. The lack of clarity has led many fund managers to self-interpret ESG investment criteria, which deters capital investment in American ESG funds and assets. This hinders American firms from maximizing organic growth, risking the stability of their business.

Despite the growing institutional interest and flows into ESG funds, this market growth outstripped the regulatory safeguards. While anti-fraud measures permit ex-post enforcement, no U.S. regulatory framework provides for ex ante standardized ESG definitions, measurements, or disclosure to be employed by companies or asset managers. This rulemaking gap in ESG-specific regulation allows fund managers to craft ESG-positive narratives while leaving out material risks, eroding investor confidence, and elevating fiduciary risk. With the SEC now relying on discretionary enforcement and the judiciary's piecemeal disposition of ESG fiduciary cases, the absence of statutory regulation prescribing ESG financial materiality renders Delaware fund governance uniquely vulnerable.

In order to curb greenwashing and bring fiduciary oversight into line with financial standards, this paper poses the following question: To what degree can Delaware corporate and fund law be changed to impose a financial materiality threshold on ESG claims? The goal is to assess how Delaware, the country's leading corporate domicile, can strengthen fiduciary duties pertaining to ESG investing–particularly for funds set up as LLCs, LPs, or statutory trusts–by enacting legislation that restricts ESG integration to financially significant factors unless otherwise agreed.

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[1] Noemi Pucci, *Global ESG Fund Flows Increase in Q4*, Morningstar, Jan. 29, 2025, https://www.morningstar.com/sustainable-investing/global-esg-fund-flows-increase-q4.

[2] *How to Avoid Greenwashing When Offering or Promoting Sustainability-Related Products*, Austl. Sec. & Invs. Comm'n (ASIC), Jun., 2022, https://asic.gov.au/regulatory-resources/financial-services/how-to-avoid-greenwashing-when-offering-or-promoting-sustainability-related-products/.

Greenwashing is a rampant form of fraud within the financial sector today. 34 percent of self-labeled ESG funds in the United States have been found to participate in greenwashing, and these funds are more likely to underperform.[3] This phenomenon has placed investment banks and fund managers in a position of greater influence. They underwrite, structure, and distribute sustainability-linked financial instruments, including ESG ETFs, impact investment funds, and green bonds. These firms hold discretion over which ESG factors to consider as long as they can prove the financial materiality of their decision. According to a report from ESG research provider RepRisk AG, there has been a 70 percent increase in climate-related greenwashing incidents in the past year among banks and financial firms.[4] Studies show that, as of 2020, only 35 percent of Russell 1000 companies employed third-party verification for their ESG disclosures, while only 3 percent of those subjected complete ESG reports to audits.[5] Most audits have focused narrowly on specific metrics, such as greenhouse gas emissions, which have led to substantial gaps in the assurance process. Furthermore, the quality and reliability of those audits are unreliable, with less than 7 percent providing high levels of assurance; methodologies differ significantly between providers, creating more inconsistencies.[6]

The court system has yet to establish a precise legal definition of ESG factors in precedent cases. Instead, a range of legal interpretations have been given, leaving the regulatory landscape ambiguous and challenging to enforce consistently. Given that regulatory bodies struggle to delineate the threshold at which ESG considerations materially impact financial conditions, a structured and enforceable definition of ESG is necessary. For the purpose of this paper, ESG can be defined as a set of criteria to evaluate the impacts a company could make and their consequences concerning three critical areas: Environmental, Social, and Governance. Environmental factors relate to the impact of a company on the natural world through clean energy use or emissions reductions. Social criteria assess how the company interacts with employees, customers, and societies at large regarding labor practices and the socio-economic impact of

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[3] Ariadna Dumitrescu et al., *Defining Greenwashing*, SSRN, 21 (Dec. 26, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4098411.

[4] Matthias Fürer, *RepRisk Data Suggest Increase in Greenwashing and Rise of Social Washing*, RepRisk, Oct. 3, 2023, https://www.reprisk.com/research-insights/news-and-media-coverage/reprisk-data-shows-increase-in-greenwashing-with-one-in-three-greenwashing-public-companies-also-linked-to-social-washing.

[5] Lisa M. Fairfax, *ESG Hypocrisy and Voluntary Disclosure*, 26 N.Y.U. J. Legis. & Pub. Pol'y 127, 169 (2024).

[6] *Id*.

operations. Governance refers to company leadership, equity, transparency, and the practice of ethics. ESG investments support companies showing positive corporate behavior in environmental standards, social causes, and inclusivity in their governance.

The possibility of regulatory reversals under the Trump administration, which has pledged to roll back recent ESG-focused federal mandates, has only increased uncertainty. This article evaluates the fundamental statutory gaps that persist irrespective of the party controlling the SEC, but makes no predictions regarding administrative changes. Regulatory efforts such as the Federal Trade Commission's (FTC) "Guides for the Use of Environmental Marketing Claims" (the Green Guides) explicitly address misleading environmental claims to ensure consumer protection, stating that environmental marketing claims must be substantiated by "competent and reliable scientific evidence."[7] More regulatory guidance is offered through the SEC amendment to Rule 35d-1 of the Investment Company Act of 1940, known as the "Names Rule," which mandates that investment funds with ESG-related names must adopt a "policy to invest, under normal circumstances, at least 80 percent of the value of its assets in investments in accordance with the investment focus that the fund's name suggests."[8]

Moreover, the SEC's adopted *Rules to Enhance and Standardize Climate-Related Disclosures for Investor*s impose specific mandates for the disclosure of climate-related risks, greenhouse gas (GHG) emissions, and governance practices. According to the final rule, registrants must provide "information about a registrant's climate-related risks that have materially impacted, or are reasonably likely to have a material impact on, its business strategy, results of operations, or financial condition."[9] Under these regulations, companies must disclose "any oversight by the board of directors of climate-related risks and any role by management in assessing and managing the registrant's material climate-related risks."[10]

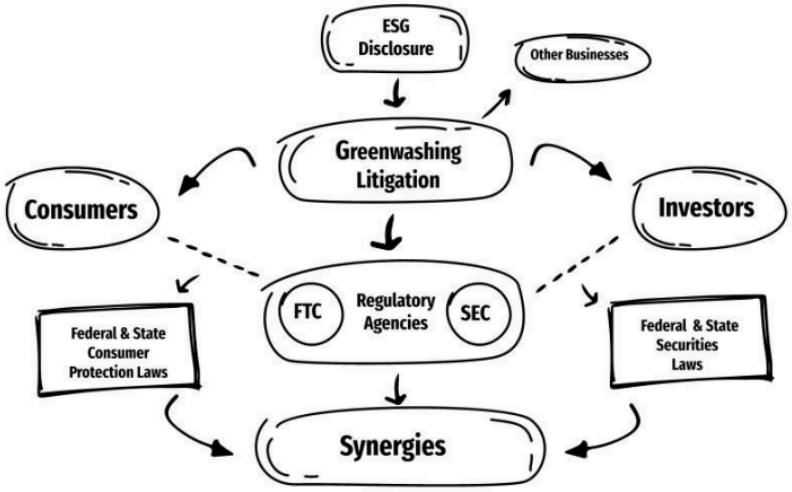
Despite these advancements, there remains a systemic regulatory gap. While existing anti-fraud provisions permit regulatory agencies to sanction misleading ESG disclosures after the fact, no comprehensive framework currently requires firms to adhere proactively to standardized ESG definitions, metrics, or disclosure obligations. Financial regulators thus possess limited tools to proactively prevent greenwashing,

[7] 16 C.F.R. § 260.2 (2025).
[8] 17 C.F.R. § 270.35d-1(a)(2) (2025).
[9] The Enhancement and Standardization of Climate-Related Disclosures for Investors, 89 Fed. Reg. 21,668 (Mar. 28, 2024).
[10] *Id*. at 21,674.

exposing investors to misleading ESG representations. This paper addresses that critical gap by analyzing how the Delaware judiciary can enhance fund governance to align ESG investing more explicitly with fiduciary duties. Part 1 outlines Delaware's fiduciary framework and its limitations in effectively regulating ESG investments, comparing duties across corporate directors, trustees, and fund managers. Part 2 discusses contemporary regulatory responses to greenwashing, emphasizing recent enforcement trends and emerging state-level legislation clarifying ESG disclosure standards. Part 3 proposes a prescriptive approach grounded in Delaware statutory law, advocating court-supervised third-party audits for verifying ESG claims and establishing a statutory financial-materiality threshold for ESG integration. This proposal seeks to balance fiduciary rigor with the implied covenant of good faith and fair dealing, preserving existing contractual flexibility while enhancing transparency and accountability.

I. FUND GOVERNANCE IN THE ESG LANDSCAPE

A. Bridging FTC and SEC Enforcement Gaps in ESG Materiality



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The FTC and SEC serve distinct yet complementary roles in regulating

[11] Barbara Ballan & Jason J. Czarnezki, *Disclosure, Greenwashing, and the Future of ESG Litigation*, 81 Wash. & Lee L. Rev. 545, 552 (2024) (source of Figure 1).

ESG-related disclosures and combating greenwashing. The FTC is responsible for preventing "unfair or deceptive acts or practices in or affecting commerce."[12] In contrast, the SEC oversees investment funds and securities markets, ensuring that investor disclosures do not violate federal securities laws, such as the Securities Act of 1933 and the Securities Exchange Act of 1934. The SEC enforces ESG-related compliance in investment funds and corporate filings, as demonstrated by its "Names Rule" and climate-related disclosure requirements, whereas the FTC targets ESG misrepresentation at the consumer level. These regulatory frameworks overlap in Delaware fund governance: corporate directors must make sure ESG statements do not amount to deceptive marketing under FTC scrutiny, while fund managers must strike a balance between investor expectations and the SEC's materiality requirements. Fund managers are vulnerable to both SEC enforcement actions for misleading investors and FTC claims for deceptive ESG branding of financial products available to non-accredited investors, thus limiting the scope of the FTC's regulatory authority on investment securities.

The SEC derives its authority to enforce securities disclosure rules under several statutory provisions, including Sections 7, 10, and 19(a) of the Securities Act of 1933 and Sections 12, 13, 15, and 23(a) of the Securities Exchange Act of 1934. Section 7 of the Securities Act mandates that registration statements "shall contain such other information, and be accompanied by such other documents, as the Commission may by rules or regulations require as being necessary or appropriate in the public interest or for the protection of investors."[13] Similarly, Section 10 stipulates that the prospectus shall "contain such other information as the Commission, by rules or regulations deemed necessary or appropriate in the public interest and for the protection of investors."[14] Section 19(a) grants the Commission "authority from time to time to make, amend, and rescind such rules and regulations as may be necessary to carry out the provisions of this title."[15] The statutory foundation for the SEC's rulemaking authority in the ESG domain is established by these provisions.

Complementing the 1933 Act, the Securities Exchange Act of 1934 imposes further obligations on issuers. Section 12 requires issuers to register securities by filing "Such information, in such detail...as the Commission may by rules and regulations require, as necessary or appropriate in the public interest or for the protection of

[12] Unfair methods of competition unlawful; prevention by Commission, 15 U.S.C. § 45(a)(1) (2018).
[13] Securities Act of 1933, § 7, 15 U.S.C. § 77g (2018).
[14] *Id*. § 77j.
[15] *Id.* § 77s(a).

investors."[16] Section 13 obligates issuers of registered securities to "file with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security."[17] Section 15 empowers the Commission to regulate brokers and dealers, and Section 23(a) authorizes the Commission to "have power to make such rules and regulations as may be necessary or appropriate to implement the provisions."[18] The final rule emphasizes that these statutes provide the legal foundation for enhanced climate-related disclosures, affirming that the new requirements intend to support investor protection and market transparency.

Under these powers of enforcement, the SEC has sought to impose stricter regulations regarding ESG-related disclosures through rulemaking amendments to the Securities Act of 1933 and the Securities Exchange Act of 1934. While the SEC has tried to encourage transparency consistent with its disclosure rules, there is no judicial precedent whereby ESG is clearly defined as a legalized standard concept. In these circumstances, the courts have neither established nor negated any singular legal definition of ESG, nor statutory law or authoritative guidance lawfully established it, leaving the regulatory authorities to deduce the terms of ESG on an ad-hoc basis. Such a state of doubt has made the development of uniform compliance standards with ESG investment and disclosure rest on subjectivist factors, which are prone to shift from industry to industry. Lacking an absolute legal definition, ESG remains subject to varying interpretations, rendering compliance and regulation challenging and facilitating greenwashing. The SEC 2024 Final Rule concerning climate-related disclosures also points to this vulnerability: "The climate-related information that these companies currently provide, however, is inconsistent and often difficult for investors to find and/or compare across companies."[19] Therefore, the financial materiality of ESG-related securities is in doubt, posing enforcement problems and increasing the likelihood of greenwashing. The proposed and rejected SEC May 2022 ESG Fund and Investment Adviser Disclosure Proposals "do not define ESG or related terms but, instead, would direct funds and investment advisors who incorporate one or more ESG factors to disclose how (1) ESG factors play a role in their portfolio investment selection procedures and (2) ESG factors are integrated into their investment

[16] Securities Act of 1933, § 7, 15 U.S.C. § 78l (2018).
[17] *Id.* § 78m.
[18] *Id.* § 78o.; *Id.* § 78w.
[19] The Enhancement and Standardization of Climate-Related Disclosures for Investors, 89 Fed. Reg. 21,668 (Mar. 28, 2024) (final rule) (effective date delayed pending judicial review, 89 Fed. Reg. 25,207 (Apr. 12, 2024)).

strategies."[20]

Yet, this broad language fails to clarify what constitutes financial materiality within the ESG context, particularly for securities whose valuations are influenced by social or environmental considerations rather than traditional financial metrics. The legal standard for materiality in securities law was established by the U.S. Supreme Court in *TSC Industries, Inc. v. Northway, Inc.* In this case, the Court held that information is material if "there is a substantial likelihood that a reasonable shareholder would consider it important" in making an investment decision, or if it would have significantly altered the "total mix" of information made available.[21] This definition emphasizes the importance of information that could influence an investor's assessment of a company's financial performance and prospects. In the context of ESG factors, financial materiality pertains to how these non-financial elements impact a company's cash flows and overall financial value creation. Therefore, when ESG considerations are financially material, they can significantly affect the returns and valuation of investment holdings.

Since ESG securities often derive value from intangible factors such as sustainability commitments or corporate governance structures, a precise definition of financial materiality is essential to ensure regulatory consistency and investor protection. This difficulty is similar to long-standing problems in financial reporting that have to do with how goodwill, an intangible asset that is prone to overstatement or misrepresentation, is treated. ESG-related intangibles also need well-defined disclosure standards, much like the Financial Accounting Standards Board and the SEC have had to define when goodwill impairments become material under Generally Accepted Accounting Principles and federal securities law. As reaffirmed in *TSC Industries, Inc. v. Northway, Inc*., omissions or misstatements are only actionable if they are material under SEC Rule 10b-5 and Section 10(b) of the Securities Exchange Act of 1934.[22] Significant discrepancies and differing opinions about what financial materiality in ESG securities means have been revealed by self-reporting, creating regulatory uncertainty and possibly misleading investors. Companies and fund managers have been able to selectively highlight positive sustainability metrics while leaving out financially significant risks due to the absence of standardized ESG disclosure frameworks.

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[20] Gary Shorter, *Introduction to Financial Services: Environmental, Social, and Governance (ESG) Issues*, Cong. Research Serv., IF11716 (2022).

[21] TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438 (1976).

[22] *Id.* at 445.

The SEC enforcement action against BNY Mellon is an optimal example to demonstrate the lack of robust policies and procedures underpinning ESG-related disclosures, highlighting how firms have overstated their ESG credentials in a bid to win investments.[23] The question at the heart of *SEC v. BNY Mellon* is whether or not the bank's misleading ESG disclosures also violated federal securities laws by overstating the degree of its ESG consideration and oversight into investment decisions. More simply, the case asks if existing regulations are sufficient to keep banks from artificially marketing themselves as ESG funds to attract investors.

In *SEC v. BNY Mellon*, the SEC found that between July 2018 and September 2021, the bank marketed certain ESG-labeled funds as being under rigorous ESG screening. BNY Mellon Investment Adviser, Inc. ("BNYMIA") made material misstatements and omissions in mutual fund prospectuses, board minutes, and responses to investment companies' request for proposal responses that all investments in its Overlay Funds were reviewed for ESG quality by a Responsible Investment Team, violating Section 206(4) of *The Investment Advisers Act of 1940*.[24] The SEC discovered that a significant portion of the investments in these funds had not undergone the promised ESG scrutiny. In one case, nearly 25 percent of an Overlay Fund's net assets were investments that lacked an ESG quality review at the time of investment.[25]

The SEC discovered that BNY Mellon had made material misstatements by indicating ESG quality reviews were being conducted on all investments when, actually, the bank's sub-adviser had discretion to invest outside of ESG screening. These misstatements were included in marketing materials, such as legally binding documents like mutual fund prospectuses, which omitted that certain investments could entirely bypass ESG review. As stated in the SEC's order, "A reasonable investor reading an Overlay Fund prospectus could mistakenly conclude that all portfolio holdings selected by the Sub-Adviser were subject to an ESG quality review."[26] This omission rendered BNYMIA's disclosures incomplete and constituted a negligent misrepresentation in violation of Section 206(2) of the Investment Advisers Act. The SEC's order further emphasized that "scienter is not required to establish a violation of Section 206(2), which may rest on a finding of simple negligence."[27] As a result, the SEC imposed a $1.5 million civil penalty for violations of Sections 206(2) and 206(4)

[23] *In re* BNY Mellon Inv. Adviser, Inc., Investment Advisers Act Release No. 6032, Investment Company Act Release No. 34591, 2022 WL 16647156 (May 23, 2022).
[24] *Id.*
[25] *Id.* at 4.
[26] *Id.*
[27] *Id.*

of the *Investment Advisers Act of 1940* and Section 34(b) of the *Investment Company Act of 1940.*[28]

The SEC's antifraud provisions, including Rule 10b-5, require that all statements regarding investment strategies be truthful and not omit material facts necessary to make disclosures not misleading.[29] However, the lack of ESG-related disclosures leaves firms with broad discretion in defining and applying ESG criteria. In the case of *SEC v. BNY Mellon*, they applied Sections 206(2), prohibiting investment advisers from engaging "in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client," and 206(4) of the Investment Advisers Act of 1940, granting the SEC authority to define and prevent "fraudulent, deceptive, or manipulative" acts through rulemaking.[30]Additionally, Section 34(b) of the Investment Company Act of 1940 was enforced, making it unlawful for any person to make "any untrue statement of a material fact in any registration statement, application, report, account, record, or other document" filed with the SEC.[31]

B. ESG Oversight and Fiduciary Duty: Bridging The Accountability Gap

This section explores what fiduciary compliance with ESG investment commitments entails and argues that the crux of this obligation lies in how financial materiality is defined and applied. Delaware is the logical jurisdiction for scrutinizing this issue regarding the precision of explicit ESG-related fiduciary duties because it is the domicile to a significant proportion of the United States' corporate charters, including "most carbon-major corporations."[32] Despite being historically shareholder-focused, its legal framework is becoming increasingly important in new climate litigation trends that reinterpret fiduciary duties in light of environmental risk: "this second wave of litigation has important implications for directors... [it] elevates the risk profile of climate change from an ethical concern to a significant financial risk that directors are legally obligated to consider."[33] The historical share of climate impacts and damages attributable to carbon-major corporations can now be measured

[28] *BNY Mellon*, Release No. 6032., *supra* note 23.
[29] 17 C.F.R. § 240.10b-5 (2024).
[30] Investment Advisers Act of 1940 § 206(2), 15 U.S.C. § 80b-6(2) (2018).
[31] Investment Company Act of 1940 § 34(b), 15 U.S.C. § 80a-33(b) (2018).
[32] Lisa Benjamin, *The Road to Paris Runs Through Delaware: Climate Litigation and Directors' Duties*, 2 Utah L. Rev. 313, 321 (2020).
[33] *Id.* at 313.

using new scientific methods.[34] Delaware law, which historically focused on shareholder wealth maximization, is being pressured by courts and stakeholders to adapt as "corporate fiduciary duties and the shareholder wealth maximization norm... compel directors to identify and assess the risks of climate change to the corporation."[35] This evolution positions Delaware as a pivotal jurisdiction for statutory ESG reform.

However, Delaware's current fiduciary framework is still ill-prepared to regulate ESG integration with the clarity and consistency that investors and financial markets are increasingly demanding. Among the primary drivers of this challenge is the ambiguity about where ESG factors fit within fiduciary duty under Delaware law. The fiduciary duties of corporate directors and fund managers differ: while corporate directors owe fiduciary duties to shareholders primarily under Delaware's General Corporation Law, fund managers owe duties directly to investors under Title 12.[36] Delaware, the principal corporate jurisdiction of the United States for financial firms selling ESG-labeled securities to domicile in, does not have a substantial ESG verification requirement as part of its fiduciary duty scheme.[37] These duties are not well-suited to the nuances of ESG claims and sustainability-linked financial products. First, I will distinguish the respective fiduciary duties of corporate directors vs. fund managers. While corporate directors owe fiduciary duties primarily to shareholders under Delaware's shareholder primacy model, fund managers owe duties directly to investors as beneficiaries. Then, I will show that these duties are inappropriate for regulating ESG investments.

Under Title 8 of Delaware General Corporation Law (DGCL), the two most fundamental fiduciary duties owed by corporate directors and officers are the duty of care and the duty of loyalty.[38] The Delaware Supreme Court in *Cede & Co. v. Technicolor, Inc.* reaffirmed that corporate directors owe fundamental fiduciary duties, stating, the directors of Delaware corporations cannot breach "any one of the triads of

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[34] Richard Heede, *Tracing Anthropogenic Carbon Dioxide and Methane Emissions to Fossil Fuel and Cement Producers*, 122 Climatic Change 229 (2013).

[35] Benjamin, *supra* note 32, at 320.

[36] Del. Code Ann. tit. 12, § 3302(a) (1999).

[37] Amy Simmerman et al., *Delaware's Status as the Favored Corporate Home: Reflections and Considerations*, Harv. L. Sch. F. on Corp. Governance (May 8, 2024), https://corpgov.law.harvard.edu/2024/05/08/delawares-status-as-the-favored-corporate-home-reflections-and-considerations/.

[38] The State of Delaware, *The Delaware Way: Deference to the Business Judgment of Directors Who Act Loyally and Carefully*, https://corplaw.delaware.gov/delaware-way-business-judgment/ (last visited Apr. 24, 2025).

their fiduciary duty–good faith, loyalty, or due care."[39] The duty of care requires that these corporate officials act with the degree of care that an ordinarily careful and prudent person would use under similar circumstances and make decisions in good faith, with the honest belief that the action taken is in the best interest of the company or the fund.[40] The duty of loyalty dictates that the best interests of the corporation, its shareholders, or the fund beneficiaries be placed ahead of any personal or conflicting interests of a director, officer, fund manager, or controlling shareholder.[41] This duty prevents the directors from representing the business in transactions where their interests conflict with those of the corporation and requires fund managers to avoid self-dealing or anything that places their interests above those of the investors.[42] Good faith is regarded by Delaware law as a component of the duty of loyalty rather than as a separate fiduciary duty. This clarification was established in *Stone v. Ritter*, where the Delaware Supreme Court held that "the failure to act in good faith may result in liability because the requirement to act in good faith 'is a subsidiary element[,]' i.e., a condition, 'of the fundamental duty of loyalty.'"[43] The Court further explained that bad faith includes circumstances where "the fiduciary intentionally fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties."[44] Thus, a director's failure to establish or monitor internal reporting systems may constitute a breach of the duty of loyalty if it amounts to a "sustained or systematic failure of the board to exercise oversight."[45] In such cases, the breach does not arise from simple negligence but from the director's deliberate indifference to known responsibilities. Accordingly, Delaware courts require a showing that "the directors knew that they were not discharging their fiduciary obligations" to impose liability based on a lack of good faith.[46]

Generally, when considering the fiduciary duty of corporate directors, interested parties fall into one of two categories: shareholders or stakeholders. Shareholders are those with a direct share of the investment, while stakeholders include employees, customers, suppliers, the community, and government entities whose interests may intersect with corporate activities indirectly. Unlike in jurisdictions like California that

[39] Cede & Co. v. Technicolor, Inc., 634 A.2d 345, (Del. 1994).
[40] Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985).
[41] Guth v. Loft, Inc., 5 A.2d 503, 511 (Del. 1939).
[42] *Id.* at 518.
[43] Stone ex rel. AmSouth Bancorporation v. Ritter, 911 A.2d 362, 370 (Del. 2006).
[44] *Id.*
[45] *Id.* at 363.
[46] *Id.* at 371.

have embraced stakeholder theory, enabling directors to consider broader interests in society, Delaware's corporate governance structure is still firmly anchored on shareholder value.[47] Boards are expected to promote long-term corporate value and to weigh shareholders' objectives above the interests of other stakeholders.

Fund managers, however, work under a different fiduciary arrangement because of the needs particular to financial products and investments. Fund managers' fiduciary duties vary depending on the legal structure of the fund. In Delaware, funds are structured as corporations, limited liability companies (LLCs), limited partnerships (LPs), or trusts, with each imposing distinct fiduciary obligations. If a fund is structured as a corporation, then it is subject to fiduciary duties of care and loyalty as outlined above. ESG investing is permissible under trust fiduciary law only if two conditions are satisfied: (1) the trustee reasonably concludes that ESG investing will benefit the beneficiary directly by improving risk-adjusted return, and (2) the trustee's exclusive motive for ESG investing is to obtain this direct benefit.[48] Under the "sole interest rule" under Sections 404(a)(1)(A) and 404(a)(1)(B) of the Employee Retirement Income Security Act of 1974 (ERISA), fund managers must act "solely in the interest of the participants and beneficiaries and for the exclusive purpose of providing benefits,"[49] making ESG integration permissible only when it demonstrably enhances risk-adjusted returns.[50]

LLCs and LPs, on the other hand, may make explicit contractual restrictions or eliminations on the duties of care and loyalty, but are bound to the duties of good faith and fair dealing. For LLCs, the Delaware Limited Liability Company Act (Title 6) allows the LLC agreement to "expand or restrict or eliminate" fiduciary duties of a member or manager, but "the limited liability company agreement may not eliminate the implied contractual covenant of good faith and fair dealing."[51] Similarly, in LPs, the Delaware Revised Uniform Limited Partnership Act (Title 6) permits the contract among the partnership to "[expand] or restrict or eliminate" fiduciary duties of a

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[47] Martin Lipton et al., *Understanding the Role of ESG and Stakeholder Governance Within the Framework of Fiduciary Duties*, Harv. L. Sch. F. on Corp. Governance (Nov. 29, 2022), https://corpgov.law.harvard.edu/2022/11/29/understanding-the-role-of-esg-and-stakeholder-governance-within-the-framework-of-fiduciary-duties/.

[48] Max M. Schanzenbach & Robert H. Sitkoff, ESG Investing: Theory, Evidence, and Fiduciary Principles, J. Fin. Plan., Oct. 2020, at 42.

[49] 29 C.F.R. § 2550.404a-1 (2023).

[50] David A. Cifrino, *The Politicization of ESG Investing*, Harv. ALI Soc. Impact Rev. (Jan. 24, 2023), https://www.sir.advancedleadership.harvard.edu/articles/politicization-of-esg-investing.

[51] 6 Del. Code § 18-1101(c) (2024).

partner or other person, but "the partnership agreement may not eliminate the implied contractual covenant of good faith and fair dealing."[52] This similarity of statutory language between LLCs and LPs indicates Delaware's emphasis on contractual freedom in defining fiduciary obligations within Title 6 of the Delaware Code. While LLCs and LPs offer relatively more flexibility, allowing parties to contract around core duties as long as they uphold the baseline obligation of good faith and fair dealing, the sole interest rule governing trusts is the strictest of these three regimes. It only allows ESG investing when it materially serves the financial interest of beneficiaries.

The Delaware Supreme Court in *Gatz Properties, LLC v. Auriga Capital Corp.* affirmed that good faith and fair dealing are always binding,[53] even with contractual modifications to the duties of care and loyalty. Further, good faith and fair dealing subject fund managers to the entire fairness standard. The court noted, "Section 18-1101(c) of the LLC Act provides...the [LLC] agreement may not eliminate the implied covenant of good faith and fair dealing."[54] It also recognized that, under the governing LLC agreement, the manager was subject to the equitable standard of entire fairness in a conflict-of-interest transaction: "We conclude that Section 15 of the LLC Agreement, by its plain language, contractually adopts the fiduciary duty standard of entire fairness, and the 'fair price' obligation which inheres in that standard."[55] This ruling established that fiduciary duties in LPs and LLCs, while modifiable, remain fundamental in protecting investors from self-dealing and managerial conflicts of interest.

However, the Delaware Court of Chancery, in the same litigation, had gone further, holding that managers of LLCs owe default fiduciary duties of care and loyalty under traditional equitable principles unless expressly disclaimed in the operating agreement.[56] The court emphasized, "The Delaware Limited Liability Company Act explicitly applies equity as a default, and our Supreme Court, and this court, have consistently held that default fiduciary duties apply to those managers of alternative entities who would qualify as fiduciaries under traditional equitable principles, including managers of LLCs."[57] The court further explained that fiduciary obligations persist unless the LLC agreement explicitly eliminates them, stating, "Here, the LLC agreement makes clear that the manager could only enter into a self-dealing

[52] 6 Del. Code § 17-1101(d) (2024).
[53] Gatz Props., LLC v. Auriga Capital Corp., 59 A.3d 1206, 1212–13 (Del. 2012).
[54] *Id.* at 1213; 6 Del. Code § 18-1101(c) (2024).
[55] *Id.*
[56] Auriga Capital Corp. v. Gatz Props., LLC, 40 A.3d 839, 851–52 (Del. Ch. 2012).
[57] *Id*. at 849.

transaction, such as its purchase of the LLC, if it proves that the terms were fair."[58]

Importantly, the Delaware Supreme Court chose not to expressly adopt or reject the Court of Chancery's broader holding regarding the default application of fiduciary duties under the Delaware LLC Act. While Delaware law permits contractual adjustment of the fiduciary duties of care in LLCs and LPs, by default, the fundamental principles of care, loyalty, and good faith apply absent express waiver.[59] It described that part of the lower court ruling as unnecessary to its case holding, cautioning against judicial restraint overreach in interpreting LLC fiduciary duties when the legislature has remained silent. In line with this, while the Supreme Court affirmed the holding and recognized the enforceability of contractual fiduciary requirements and the non-waivability of the implied covenant, it did not necessarily affirm the view that fiduciary care and loyalty duties apply to LLC managers by default. The rulings highlight the significance of fund managers' adherence to such duties, particularly in the field of ESG investing, where transparency and accountability are key to assuring investor confidence and compliance with governance demands. By clearly defining fiduciary obligations and including ESG-specific obligations within fund governance, Delaware law can enhance investor safeguards and minimize greenwashing risks in ESG investment products.

In re Caremark International Inc. Derivative Litigation established a foundational principle in corporate governance by clarifying the duty of oversight as a component of the duty of loyalty.[60] The Delaware Court of Chancery articulated that corporate directors should ensure the existence of an adequate internal monitoring and compliance system.[61] The court emphasized that:

> a director's obligation includes a duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists, and that failure to do so under some circumstances may, in theory at least, render a director liable for losses caused by non-compliance with applicable legal standards.[62]

This ruling underscored that a director's fiduciary duty requires a proactive approach

[58] *Auriga*, 40 A.3d, *supra* note 56, at 843.
[59] *See Auriga*, 40 A.3d, *supra* note 56, at 848–53.; *Gatz Props.*, 59 A.3d, *supra* note 53, at 1212–14.
[60] *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996).
[61] *Id.* at 968 (explaining that directors must implement adequate internal monitoring and reporting systems).
[62] *Id.* at 968–69.

to risk oversight. However, the court also set a high bar for liability, clarifying that a director cannot be held personally liable just for an oversight failure unless it amounts to a sustained or systemic failure to exercise oversight: a standard that courts have since applied in derivative litigation.[63]

The case involved allegations that Caremark's board failed to adequately monitor the company's compliance with federal health care laws, which resulted in regulatory violations and significant financial penalties. The court recognized that while directors are not expected to monitor every corporate activity in detail, "only a sustained or systematic failure of the board to exercise oversight–such as an utter failure to attempt to assure a reasonable information and reporting system exists–will establish the lack of good faith that is a necessary condition to liability."[64] This ruling provided that directors are not liable for business misjudgements in themselves but can be held accountable if they knowingly disregard warning signs or fail to implement any control measures. Although fund governance is the main topic of this paper, this precedent is used to show how Delaware law has long linked the duty of loyalty to the effectiveness of internal risk monitoring systems. This reasoning can and should be applied to sustainability-related risks in investment vehicles bearing the ESG brand. Since ESG-associated dangers persist in impacting financial performance and reporting to regulatory bodies, the *Caremark* standard has emerged as even more relevant, such that directors' boards who fail to include monitoring of ESG within their governance models are exposed to liability if such failures result in material harm to the corporation or its shareholders. If ESG-related risks are essential to the fund's brand and investment strategy, then neglecting to put governance systems in place that track them could be a breach of fiduciary duty, since ESG funds promote themselves on their dedication to sustainability standards.

Marchand v. Barnhill expanded on *Caremark's* precedent by reiterating the necessity for corporate boards to oversee "mission-critical risks" that could expose the corporation to financial, legal, and reputational harm.[65] The Delaware Supreme Court reversed the Court of Chancery's dismissal, finding that Blue Bell Creameries' directors failed to make any meaningful oversight of food safety compliance. The court emphasized that "directors have a duty to exercise oversight and to monitor the

[63] *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, *supra* note 60, at 971 (establishing that liability requires a "sustained or systemic failure" to exercise oversight); *Ritter*, 911 A.2d at 370–73.
[64] *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, *supra* note 60, at 968–69.
[65] Marchand v. Barnhill, 212 A.3d 805, 809 (Del. 2019).

corporation's operational viability, legal compliance, and financial performance."[66] The ruling established that a board's "utter failure to attempt to assure a reasonable information and reporting system exists" is an act of bad faith and a breach of the duty of loyalty.[67] The court underlined the point that *Caremark* oversight obligation arises where a board utterly fails to carry out its duty to monitor "mission-critical" risks material to the company's business operations. The failure by Marchand to implement any reporting framework or governance procedure for food safety compliance at Marchand proved the board's failure to act in good faith, triggering a public health crisis and immense loss.

The facts of the case present the consequences of an ineffective system of monitoring. A listeria outbreak at Blue Bell Creameries killed three people and forced the company to recall all of its products nationwide. Unlike a scenario where a board establishes a compliance system but fails to monitor it adequately, the court found that "Blue Bell's board had no committee overseeing food safety, no full board-level process to address food safety issues, and no protocol by which the board was expected to be advised of food safety reports and developments."[68] This lack of protections left the board without knowledge regarding essential health risks, inviting exceedingly expensive financial and reputational loss to the corporation. The court further included that directors must at least act with good faith to establish a risk-monitoring system for mission-critical risks.

This precedent has broader implications. It establishes that any actor subject to the duty of loyalty, which includes fund managers, must exercise oversight over mission-critical risks. Fund managers operating under Delaware law who fail to monitor ESG-related risks may breach their fiduciary duties, particularly when such risks are central to the fund's investment thesis or marketing strategy. Only managers in LLPs or LLCs that have explicitly waived the duty of loyalty by contract may be exempt. Thus, Marchand supports the view that ESG risks, when material to financial performance or regulatory compliance, demand oversight systems that satisfy fiduciary standards.

Under Delaware fiduciary law, decisions are guided by the duties of care and loyalty, with shareholder value serving as the foundational goal for both fund managers and corporate directors. Directors and managers may decide to include sustainability-related metrics in their strategy to improve long-term value or

[66] *Barnhill*, 212 A.3d, *supra* note 65.
[67] *Id.*
[68] *See Barnhill*, 212 A.3d, *supra* note 65, at 810.

risk-adjusted returns, even though ESG integration is not strictly necessary. But after they do, Delaware law requires them to put in place sufficient oversight mechanisms to make sure ESG pledges are not misrepresented or poorly handled, especially under the *Caremark* standard. The duty of loyalty holds people accountable for failing to keep an eye on mission-critical risks,[69] which increasingly include significant ESG considerations. With less fiduciary restraint, fund managers in LLCs and LPs that have contractually waived the duty of loyalty maintain greater discretion and offer a feasible structure for investors looking to pursue ESG-focused investment goals. Nonetheless, Delaware law imposes legal accountability for the strength of the ensuing oversight and reporting procedures rather than for the adoption of ESG in and of itself for the majority of fiduciaries who voluntarily commit to ESG goals. Fiduciaries continue to be in a precarious position; they are empowered to incorporate sustainability when it makes financial sense, but they run the risk of being held liable if their efforts lack internal controls or materially mislead investors in the absence of clearer statutory boundaries around which ESG factors qualify as pecuniary reasons.

C. Evolving Role of Financial Materiality and ESG in Fiduciary Standards

The section above established that fund managers and corporate directors who commit to ESG investment generally have significant obligations to oversee continued compliance with relevant regulations. This responsibility applies to how investment firms market ESG funds and how they evaluate ESG disclosures made by their portfolio companies. In practice, greenwashing can originate from either side: asset managers may misrepresent their ESG screening or integration practices, or the disclosure of misleading sustainability claims by these portfolio companies to attract capital without conducting sufficient due diligence.[70] This section assesses what this compliance entails, and sees how the divisive use & definition of the term "financial materiality" lies at the core of the ESG debate. According to the SEC, a fact is financially material "if there is a substantial likelihood that a reasonable investor would consider it important in deciding how to vote or make an investment decision, or, put another way, if the information would alter the total mix of available information."[71] Some argue that ESG metrics are not financially material because they do not reflect

[69] Stone v. Ritter, 911 A.2d 362, 370 (Del. 2006).
[70] *See BNY Mellon*, *supra* note 23.
[71] U.S. Sec. & Exch. Comm'n, *Commission Guidance Regarding Disclosure Related to Climate Change*, Release Nos. 33-9106, 34-61469, 75 SEC Docket 837, at 10 (Feb. 2, 2010).

any information about a company's financial fundamentals. Others, such as the investment firm BlackRock, have asserted that "sustainability characteristics...can provide insight into the effective management and long-term financial prospects of a fund."[72] In this sense, a company's investment in ESG initiatives may reflect a forward-looking, long-term plan to maximize profits. In this section, I will discuss how to interpret relevant regulations in light of different readings of "financial materiality" and advocate for a unified standard for the word.

ESG regulation is essential to reassure investors that they are not being misled about the quality or objectives of securities in the investment marketplace. While the FTC's "Green Guides" outline standards to prevent deceptive environmental marketing claims, their lack of substantive updates since 2012 and primary focus on consumer products rather than investment funds limit their direct relevance to developing enforceable ESG disclosure standards in financial reporting.[73] For instance, these Guides do not touch upon the marketing practices of investment firms selling ESG funds, leaving considerable gaps in oversight for financial products with far-reaching implications.

While the SEC has proposed new ESG disclosure requirements to enhance transparency in ESG fund marketing, including the proposed Names Rule Amendment, such initiatives will remain incomplete without statutory clarification of financial materiality in ESG investments. Former SEC Chair Gary Gensler highlighted the issue of self-reporting, noting that there is currently "a huge range of what asset managers might disclose or mean by their [ESG] claims."[74] Gensler emphasized that robust disclosures and rules are necessary for protecting investors and ensuring they can make informed decisions based on reliable data that is not determined by subjective and potentially biased standards. He remarked that the lack of consistent and comparable disclosures allows funds to mislead investors by overstating their ESG focus. Gensler further stressed the importance of facilitating investors to "drill down to see what's under the hood of these funds" to verify alignment with their goals.[75]

Despite these proposals, enforcement remains limited, as the absence of guidelines for oversight mechanisms of ESG data collection and integration into investment decision-making continues to provide openings for financial services companies to

[72] State of Tennessee *ex rel.* Skrmetti v. BlackRock, Inc., 23 S.W.12d 618 (Tenn. Cir. Ct. 2023).
[73] Fed. Trade Comm'n, *Environmental Marketing* (2012), https://www.ftc.gov/business-guidance/advertising-marketing/environmental-marketing.
[74] Gary Gensler, Chair, U.S. Sec. & Exch. Comm'n, Statement on ESG Disclosures Proposal (May 25, 2022), https://www.sec.gov/newsroom/speeches-statements/gensler-statement-esg-disclosures-proposal.
[75] *Id*.

exploit ambiguities and perpetuate greenwashing practices. A BNP Paribas poll showed that over 70 percent of investors see poor data as a major barrier to effective ESG investing, indicating systemic issues in ESG data quality and availability.[76] A study analyzing SEC comment letters related to climate change and ESG disclosures revealed a significant decrease in enforcement actions. Between April 1, 2023, and December 31, 2024, the SEC issued only 119 relevant comment letters, compared to 271 letters in the prior 21-month period–a decline of over 50 percent.[77] This reduction suggests a potential weakening in regulatory oversight during that time frame.

Delaware law should approach the issue of combating greenwashing by clarifying the fiduciary duties of fund managers under its current statutes, which play a central role in structuring, marketing, and managing ESG financial products. Current fiduciary requirements do not specifically define the boundaries of ESG integration such that fund managers can market sustainability-linked funds without assurance that ESG factors contribute to risk-adjusted financial returns. To address this gap, Delaware must codify "pecuniary ESG" ("risk-return" ESG) as distinct from "nonpecuniary ESG" ("collateral benefits ESG") to ensure that ESG integration is linked to financial materiality rather than discretionary social objectives.[78] In this framework, "financial materiality" would be equivalent to "pecuniary ESG". Under fiduciary duties owed by fund managers under Delaware law, risk-return ESG factors like environmental hazards, labor policies, and governance requirements are permissible if they unmistakably increase profitability, reduce regulatory risk, or maximize corporate goodwill in terms of increasingly profitable financial returns.[79] To maintain ESG integration within fiduciary duty boundaries, Delaware needs to have clear legal standards that compel fund managers to justify ESG-based investment decisions in terms of financial materiality. Material impact benefits should be shown through SEC disclosure requirements and financial reporting standards.

This section examines *Tibble v. Edison International* and *Spence v. American Airlines Inc.*, which provide context on the limits of nonpecuniary ESG investment strategies under fiduciary duty standards. Fund managers are vulnerable to litigation

[76] Chris Newlands, *Data Shortfall Undermines ESG Investment, Asset Managers Warn*, Fin. Times, Dec. 9, 2024,
https://www.sec.gov/newsroom/speeches-statements/gensler-statement-esg-disclosures-proposal.
[77] Jacob H. Hupart et al., *A Quantitative Analysis of Comment Letters Issued by the SEC Concerning Climate Change Disclosures: Further Developments*, MINTZ INSIGHTS CENTER (Feb. 19, 2025).
[78] Max M. Schanzenbach & Robert H. Sitkoff, *supra* note 48, at 42.
[79] Soc. Sec. Admin., *Trust Investments and the Prudent Investor Rule*, Program Operations Manual System § 07240.009 (2004).

risks from investors who claim misrepresentation and fiduciary duty claims that contest ESG-driven investment choices that lack a clear profitability connection in the absence of clear financial materiality standards. This issue was central in *Tibble v. Edison International,* where the Supreme Court reaffirmed that a fiduciary's duty is not a one-time obligation at the moment of investment selection but an ongoing responsibility. The Court ruled, "Under trust law, a trustee has a continuing duty to monitor trust investments and remove imprudent ones. This continuing duty exists separate and apart from the trustee's duty to exercise prudence in selecting investments at the outset."[80] This duty is distinct from the initial selection of investments, as "a trustee has a continuing duty to monitor trust investments and remove imprudent ones."[81] The Court further emphasized that "a fiduciary must discharge his responsibilities 'with the care, skill, prudence, and diligence' that a prudent person 'acting in a like capacity and familiar with such matters' would use."[82]

Since managers must show that ESG-aligned investments serve pecuniary goals rather than ideological preferences, this principle poses increased risks for fund governance in the context of ESG. Fund managers may be held liable for violating their fiduciary duties under Delaware law, specifically the duty of prudence, if ESG factors do not yield obvious, financially material gains. *Tibble* underscores that fiduciaries must conduct "a regular review of their investments with the nature and timing of the review contingent on the circumstances."[83] This translates into the requirement for precise, measurable ESG metrics that exhibit financial materiality in ESG governance. However, the lack of a standardized methodology in the current SEC framework exposes fund managers to possible liability.

Moreover, the *Tibble* decision warns that fiduciaries cannot rely on a passive approach, stating that the trustee must "systematic[ally] conside[r] all the investments of the trust at regular intervals" to ensure that they are "appropriate" to ensure continued prudence.[84] ESG-focused fund managers are further burdened by this requirement, which requires them to continually demonstrate that ESG investments have a sound financial foundation despite changing market conditions. Courts may hold fund managers accountable for failing to show that ESG factors result in observable financial gains if there is a lack of statutory clarity.

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[80] Tibble v. Edison Int'l, 575 U.S. 523, 529 (2015).
[81] *Id.* at 526.
[82] *Id.* at 524.
[83] *Id.* at 528.
[84] *Id.* at 529.

Therefore, fund governance structures remain vulnerable in the absence of a legal framework that harmonizes fiduciary duty principles with ESG disclosure obligations. This is because they may be accused of greenwashing when ESG investments underperform or of breaching fiduciary duties when ESG integration lacks a clear financial rationale. The opinion of the court in *Tibble* makes clear that "[w]hen the trust estate includes assets that are inappropriate as trust investments, the trustee is ordinarily under a duty to dispose of them within a reasonable time."[85]

The case of *Spence v. American Airlines Inc.* provides a detailed examination of the intersection of ESG investing and ERISA fiduciary obligation. The Texas Federal Court specifically considered whether fiduciaries had breached their obligations by allowing investment managers like BlackRock to include ESG objectives in retirement fund management. The plaintiff maintained that the practices violated ERISA's obligation of prudence and loyalty by placing non-financial ESG values ahead of investment returns. The court, siding with the plaintiff, ruled that ERISA mandates fiduciaries act "solely in the interest of the participants and beneficiaries and for the exclusive purpose of providing benefits to participants and their beneficiaries" under 29 U.S.C. § 1104(a)(1)(A)(i).[86] This statutory requirement is rooted in the common law of trusts, emphasizing that fiduciaries must act with an "eye single" to the financial interests of plan participants.[87]

The ruling underscored that ESG integration into fiduciary investment decisions must be justified based on financial materiality. The court cited *Fifth Third Bancorp v. Dudenhoeffer*, reiterating that fiduciary duties under ERISA extend only to "financial benefits" and the term does not cover nonpecuniary benefits.[88] Additionally, the court found that allowing ESG considerations without clear evidence of financial benefit constituted a breach of fiduciary duty. The court emphasized that fiduciaries must provide a "reasoned decision-making process" when selecting investment options and ensure that each option "remains in the best interest of plan participants."[89]

The decision also addressed the risks of "collateral benefits ESG," where investment strategies are driven by non-financial motivations such as ethical or social goals. The court cautioned that such strategies could lead to liability under ERISA's sole interest rule, prohibiting fiduciaries from being influenced by third-party interests or personal

[85] *Tibble,* 575 U.S., *supra* note 80, at 530.
[86] Spence v. Am. Airlines, Inc., 718 F. Supp. 3d 612, 620 (N.D. Tex. 2024).
[87] *Id*. at 621.
[88] *Id.* at 620.
[89] *Id.*

motivations. The opinion referenced *Pegram v. Herdrich*, stating that "perhaps the most fundamental duty of a [fiduciary] is that he must display... complete loyalty to the interest of the beneficiary and must exclude all selfish interest and all consideration of the interests of third persons."[90]

Furthermore, the ruling addressed the broader implications of ESG-related proxy voting. The court noted that BlackRock had used its delegated proxy voting authority to advance ESG initiatives, leading to concerns about conflicts of interest. The court determined that defendants "acted disloyally by failing to keep American's corporate interests separate from their fiduciary responsibilities, resulting in impermissible cross-pollination of interests."[91] The ruling ultimately highlights the need for fiduciaries to ensure that ESG investments align with financial returns rather than external policy objectives.

Investment managers now have the burden of proving that ESG considerations lead to better risk-adjusted returns as opposed to just fitting in with broader societal or policy preferences. By establishing that ESG investing must be economically justified on ERISA grounds, the *Spence* case reinforces the importance of statutory particularity in defining financial materiality within fiduciary investment arrangements. Without a clear regulatory definition, ESG investments remain vulnerable under the sole interest rule, placing fiduciaries at risk of legal exposure for prioritizing nonpecuniary ESG goals over financial performance. This ruling demonstrates the increasing judicial skepticism of ESG investment frameworks that do not show measurable financial benefits. The ruling marks a change in the way ERISA's fiduciary duties are interpreted, making it harder for fiduciaries to defend ESG-driven investment strategies in the absence of strong financial evidence.

Judicial reliance on trust law principles further reinforces the high standard of fiduciary conduct expected under ERISA. To underscore that point, the Texas Federal Court invoked the trust-law pedigree of ERISA's fiduciary standards:

> ERISA's fiduciary duties "draw much of their content" from the common law of trusts. . . . The "prudent person" standard is based not on a prudent layperson, but on a prudent fiduciary who is "acting in a like capacity," and is "familiar with such matters," and is making

[90] *Am. Airlines, Inc.*, 718 F. Supp. 3d., *supra* note 86.
[91] *Am. Airlines, Inc.*, 718 F. Supp. 3d., *supra* note 86, at 55.

> decisions for "an enterprise of a like character and with like aims."[92]

This formulation emphasizes that when making investment decisions, fiduciaries must use judgment based on expertise rather than their subjective ethical preferences.

Tibble and *Spence* demonstrate that, rather than imposing ESG obligations on investment managers, fiduciary duties more often function as legal constraints, particularly for firms governed by ERISA. Fund managers have an ongoing obligation to ensure that the financial products they offer pursue investments for clearly "financially material" reasons. This creates a tension, as there is no standardized method for pricing intangible assets such as ESG compliance, and intangible asset valuation is already controversial, even when such factors may offer real value through risk mitigation. In this way, fiduciary duties act as a limitation on ESG investing. Regulatory developments in accounting standards, particularly those that incorporate intangible asset valuation, may provide the framework investment managers need to demonstrate the financial materiality of ESG considerations. However, in the absence of standardized valuation methods, investment managers face limitations in articulating pecuniary justifications for ESG investments; yet, in many cases, they can exploit regulatory ambiguity to market ESG products without conducting meaningful due diligence.

II. GREENWASHING IN THE FINANCIAL SERVICES SECTOR

A. Greenwashing and the Case for Enhanced ESG Oversight

This section examines greenwashing regulation in the context of ex post enforcement actions against investment firms, ultimately arguing that ex ante regulation is necessary to govern ESG disclosures. Although the FTC has sought to establish guidelines for ESG-related marketing claims, these efforts have primarily focused on corporate entities rather than investment managers. Consequently, most legal actions involving investment firms rely on general consumer protection statutes, often alleging that firms misled investors through statements made in prospectuses or other required disclosures. This framework, however, remains insufficient to address the growing complexities of ESG investment practices. As a 2022 report from PwC highlights, investor skepticism is widespread: 87 percent of investors suspect that

[92] Brief for the United States as *Amicus Curiae* Supporting Petitioners at 20.; *Tibble v. Edison Int'l*, No. 13-550 (U.S. Dec. 2014), 2014 U.S. S. Ct. Briefs LEXIS 4292.

corporate sustainability disclosures include some degree of greenwashing, and many indicate that external assurance would increase their confidence in reported ESG information.[93] To restore credibility in ESG investment products, regulatory agencies must move beyond general fraud standards and advance targeted, ESG-specific disclosure requirements and enforcement mechanisms.

While ex-post regulation has occasionally worked against greenwashing, these enforcement mechanisms are not clear, consistent, or predictive to guide investment managers in advance. An example is *Tennessee v. BlackRock*, where the Tennessee Attorney General sued under the state Consumer Protection Act for misleading ESG disclosures. The complaint cited misrepresentations by BlackRock regarding the extent of ESG integration in its funds and contradictions between public statements and internal net-zero commitments. In *Tennessee v. BlackRock*, "BlackRock has misled consumers about the scope and effects of its widespread ESG activity...constitut[ing] deceptive acts and practices under the Tennessee Consumer Protection Act ('TCPA'), including Tenn. Code Ann. § 47-18-104(a) and (b)(27)." The TCPA prohibits "unfair or deceptive acts or practices" in trade, including material misrepresentations or omissions likely to mislead consumers.[94] The Tennessee Attorney General claimed that BlackRock's internal ESG commitments and proxy voting behavior to net zero and decarbonization contradicted its external representations to investors.

The complaint alleged that "BlackRock's pattern of deception has played out primarily in two areas: (1) misrepresenting that some of its funds do not integrate ESG factors, while committing to ESG goals behind the scenes; and (2) overstating the financial relevance of ESG objectives to investors."[95] BlackRock's proxy voting record showed that "BlackRock has voted in favor of shareholder proposals pushing for aggressive climate targets, despite telling investors that it only considers ESG where it impacts financial returns."[96] The fundamental issue arises when deciding whether BlackRock's ESG-related statements were materially misleading under the TCPA and how to define a financially material impact on ESG investment returns. In BlackRock's case, deciding what ESG factors constituted a financially material impact on an investment's outlook was up to their discretion. Thus, there was no clarity surrounding how BlackRock could implement its investment strategy under the guise of ESG. The

[93] *The ESG Execution Gap: What Investors Think of Companies' Sustainability Efforts*, PwC (2022), https://www.pwc.com/gx/en/issues/esg/global-investor-survey-2022.html.
[94] Tenn. Code Ann. § 47-18-104(b)(27) (2024).
[95] State of Tenn. ex rel. Skrmetti v. BlackRock, Inc., No. 23CV-618 (Tenn. Cir. Ct. Williamson Cnty. 2023).
[96] *Id.*

Attorney General identified this regulatory gap and argued that omissions can count as deception if they mislead consumers about a product's characteristics or benefits. Crucially, many observers note that BlackRock's inconsistencies were less a deliberate scheme than a by-product of the "wild-west" phase of ESG marketing: the firm leaned into broad ESG rhetoric in 2018-19, swiftly revised its website once lawyers flagged emerging liability, and then–somewhat unexpectedly–found those earlier claims repurposed as evidence of deception.

To settle the case without admitting wrongdoing, BlackRock agreed to transparency measures, including the requirement to "to clarify ESG disclosures," mandating that "when communicating with investors in Tennessee concerning investments or transactions in securities, BlackRock shall use the terms 'financially material' or 'financial materiality' consistent with the definition of 'material' under U.S. securities law."[97] BlackRock also agreed to third-party audits of up to 50 U.S. companies where BlackRock cast proxy votes on environmental or social issues, with a requirement that BlackRock retain all materials provided to the auditor for at least two years.[98] While this model is comprehensive in ensuring BlackRock's compliance over the next two years, such sector-specific measures need to be codified to clarify regulatory gaps of what constitutes financial materiality in ESG securities. A precise definition of pecuniary ESG can limit the gray areas surrounding how to consider the financial materiality of a potential ESG investment. The settlement in *Tennessee v. BlackRock* demonstrates that any deviation from accurate ESG disclosure can constitute a misrepresentation that violates fiduciary duties and erodes investor confidence.

At the same time, the BlackRock settlement also suggests that some degree of accountability is taking place. Although regulatory enforcement is reactionary, the sanction demonstrates that large financial institutions can be compelled to adopt verification, monitoring, and reporting systems for mission-critical risks concerning ESG disclosure quality. In this sense, the BlackRock case reflects the risks of greenwashing and a nascent regulatory capacity to correct misleading ESG practices. For investment managers, the episode underscores a practical desire for ex-ante regulatory guidance: clear rules on "financially material ESG" would legitimize product labelling, enhance investor confidence, and reduce the likelihood that marketing copy written in good faith one year will be deemed deceptive the next. Still, the absence of binding, universal standards means that even high-profile enforcement may be more

[97] *BlackRock, Inc*., No. 23CV-618, *supra* note 95.
[98] *Id.*

symbolic than structural. If there is no binding verification of ESG metrics with requisite oversight, such standards pose the risk of making ESG disclosures marketing tools rather than a yardstick of sustainability.

The problem is further exacerbated by a lack of reporting measures and regulatory supervision, which facilitate greenwashing. The FTC's "Green Guides," initially introduced to combat deceptive environmental claims in consumer goods, fail to address the unique challenges posed by ESG-labeled financial products.[99] These challenges include the complexity of these financial products, the lack of standardized criteria for what constitutes an ESG investment, and the potential for nuanced misrepresentation by investment firms. Because these guidelines have not been updated since 2012, they fail to address specific complexities such as the diverse structures of sustainability-linked bonds and loans or the variable performance targets tied to environmental metrics.

The Green Guides require environmental claims to be supported by competent and reliable scientific evidence and communicated with clear and conspicuous disclosures, but stop short of providing specific quantitative standards for sustainable investments. For instance, while the Green Guides demand that marketers avoid overstating benefits and qualify general claims to prevent consumer deception, they do not include measurable criteria for differentiating a genuinely sustainable financial product from one that employs vague ESG language.[100] The lack of such specificity creates an environment where financial institutions can craft ESG claims that are misleading or non-descriptive.

The shortcomings of current ESG disclosure rules have led to increased scrutiny, with noncomparable and inconsistent disclosures offering greenwashing opportunities. The SEC's final climate disclosure rules lack clear guidance on what materiality is in this case, offering opportunities for uneven interpretation and litigation. It states that "The final rules establish a hybrid disclosure system that combines prescriptive rules with a reliance on the 'broad-based concept of materiality.'"[101] This regulatory uncertainty has put fund managers in a precarious position, as "materiality determinations, which are initially made by management, can be influenced by subjective factors such as personal experiences and biases."[102] As a result, "there is no

[99] *Guides for the Use of Environmental Marketing Claims*, 77 Fed. Reg. 62,122 (Oct. 11, 2012) (codified at 16 C.F.R. pt. 260).
[100] *Id.*
[101] Ballan & Czarnezki, *supra* note 11, at 650 (critiquing final rule's disclosure framework).
[102] Ballan & Czarnezki, *supra* note 11.

clear guideline or bright-line test to determine what constitutes materiality in this context, leaving room for inconsistent interpretation and litigation; nor are the disclosure requirements...clear in terms of what needs to be disclosed and under what circumstances."[103]

Ex post enforcement can still serve a useful role when paired with strong statutory guidance, as demonstrated in California's application of its consumer protection statutes. California has enacted its Unfair Competition Law (UCL) to hold companies accountable for greenwashing. The UCL forbids "unlawful, unfair or fraudulent business act[s] or practice[s]" and false advertising, providing a powerful tool for both regulators and private plaintiffs in battling deceptive ESG claims.[104] A clear example of the UCL's applicability to greenwashing is seen in *Woolard v. The Glad Products Company et al.*

In *Woolard v. The Glad Products Company et al.*, the plaintiff alleged that Glad misrepresented the recyclability of its trash bags, misleading consumers into thinking that the bags were environmentally friendly. The lawsuit contended that this misrepresentation violated California's UCL, the California Consumers Legal Remedies Act, and the California False Advertising Law. The court emphasized that "Defendants misleadingly name and otherwise label the Products 'Recycling' bags and market them using imagery that reasonable consumers understand to indicate recyclability, even though the Products themselves are not recyclable anywhere in the Nation."[105] Furthermore, the court emphasized that "marketing trash bags designed for municipal 'recycling' is thus inherently misleading," and that "consumers who purchase 'recycling' bags do so to positively impact the environment by practicing sustainable habits, and they are unaware that municipal use of these bags harms the environment and is impeding sustainability goals nationwide." [106]

The case of *Woolard v. The Glad Products Company et al.* illustrates how effective UCL can be, indirectly bringing greenwashing into perspective by making corporations accountable for misleading marketing. California's approach builds a regulatory scheme wherein companies cannot try to manipulate ambiguities in ESG as a source for their green marketing. While Delaware narrowly frames fiduciary duties in terms of shareholder interests, California's reliance on consumer protection statutes

[103] Ballan & Czarnezki, *supra* note 11.
[104] Cal. Bus. & Prof. Code, Ch.5 § 17200 (West 2023).
[105] Craig Woolard v. The Glad Products Co. & The Clorox Co., No. 3:24-cv-00504-JO-BLM, at 11 (S.D. Cal. 2024).
[106] *Id.* at 10.

emphasizes protecting consumers and investors from deceptive ESG claims. This contrast reveals a more general tendency in California to extend transparency and accountability for corporate conduct to regulatory norms that serve a broader range of stakeholders.

Moreover, the flexibility in enforcement provided by the UCL enables California to address the constantly changing face of greenwashing practices. Because the UCL does not require proof of consumer deception but relies on the deceptiveness of the unsubstantiated ESG claim itself, this lowers evidentiary burdens and allows pre-emptive action against greenwashing.[107] This proactive approach indicates California's focus on consumer and investor protection from deceptive practices, in contrast to Delaware's more shareholder-oriented fiduciary framework. In creating mechanisms for directly addressing greenwashing, California has set a model for how states can adopt regulatory steps emphasizing accountability and transparency.

However, consumer protection enforcement mechanisms alone do not instill investor confidence or guide fund governance. There remains a lack of confidence in operating through CPAs and litigation systems ex-post. ESG-labeled investments require clear and credible information to determine their alignment with financial materiality. This is where California's forward-looking legislation provides a clearer model for reform.

B. Delaware's Fiduciary Gaps and California's ESG Disclosure Mandates

California has implemented robust measures through legislation such as the Climate Corporate Data Accountability Act (SB 253). The bill would require large corporations to report in detail on their emissions of greenhouse gases, including Scope 1, or direct emissions; Scope 2, indirect emissions generated by purchased electricity; and Scope 3, indirect emissions created by the company's supply chain.[108] The applicability of SB 253 extends to entities formed and domiciled anywhere in the United States, provided they have a total annual revenue exceeding $1 billion and do any business in California.[109] It requires the California Air Resources Board (CARB) to develop regulations that require these entities to publicly disclose and obtain

[107] Cal. Bus. & Prof. Code §§ 17200–17209 (West 2025).

[108] Cal. S.B. 253, 2023-2024 Reg. Sess. (Cal. 2023).

[109] David R. Carpenter et al., *California's New Climate Disclosure Laws Under Fire in New Lawsuit Against California Air Resources Board*, Sidley Austin LLP (Feb. 1, 2024), https://www.sidley.com/en/insights/newsupdates/2024/02/californias-new-climate-disclosure-laws-under-fire.

third-party assurance of three categories of GHG emissions annually, regardless of location. Verification by third-party auditors, independent and qualified, credibly accredited by the CARB, will be carried out. This kind of verification serves to eliminate biases in self-reporting, a common problem affecting the credibility of ESG claims.[110] Further, this will involve a requirement for businesses to file the reports with CARB on an annual basis, to display the data publicly on a digital platform, further adding elements of transparency, which stakeholders from multiple levels can more easily analyze.

California's Climate-Related Financial Risk Act, SB 261, supplements SB 253 in terms of enhancing corporate transparency regarding greenhouse gas emissions and climate-related financial risks.[111] SB 261 mandates that, on or before January 1, 2026, and biennially thereafter, any "covered entity"–defined as a business with over $500 million in total annual revenues that "does business in California"–must prepare and publicly disclose a "climate-related financial risk report" detailing its exposure to climate-related financial risks and the "measures adopted to reduce and adapt to" those risks.[112] These disclosures must follow international best practices by being "in accordance with the recommended framework and disclosures contained in the Final Report of Recommendations of the Task Force on Climate-related Financial Disclosures (June 2017)... or pursuant to an equivalent reporting requirement".[113] Each covered entity must make its report "available to the public, on its own internet website" in order to encourage public accountability.[114]

Importantly, SB 261 defines "climate-related financial risk" as a "material risk of harm to immediate and long-term financial outcomes due to physical and transition risks," explicitly including risks to "corporate operations," "provision of goods and services," "supply chains," "capital and financial investments," "shareholder value," "consumer demand," and "financial markets and economic health".[115] This thorough framing guarantees that corporate governance takes into account both transitional risks–shifting laws, market fluctuations, or technological innovation–and physical risks–wildfires, floods, and droughts.

Without consistent disclosure mandates across jurisdictions, fund managers must often navigate ESG data that is "self-created," lacks standardization, and is derived from

[110] Cal. S.B. 253, *supra* note 108.
[111] Carpenter et al., *supra* note 109.
[112] Cal. S.B. 261, § 38533(a)(4), 2023–2024 Reg. Sess. (Cal. 2023).
[113] *Id.* at § 38533(b)(1)(A)(i).
[114] *Id.* at § 38533(c)(1).
[115] *Id.* at § 38533(a)(2).

"first-party" standards, allowing companies to selectively collect and report information to their advantage.[116] Many environmental claims are made "without the support of independent third-party certification," meaning companies "can decide which data to collect and how that data will be processed in the first place."[117] For asset managers trying to incorporate ESG risks into portfolio analysis, particularly across state lines, the lack of standardized disclosure protocols poses systemic challenges. Both fiduciary oversight and regulatory enforcement are compromised by the ensuing fragmentation. Due to its significant role in corporate governance, Delaware is under pressure to close this regulatory gap by implementing a uniform ESG disclosure standard that lowers the risk of greenwashing and clarifies financial materiality within ESG fund governance.

While the California model of mandatory ESG disclosures (e.g., SB 253 and SB 261) sets a high bar for transparency, Delaware must consider the reputational and competitive implications of adopting similar mandates. Delaware has long held its status as the most business-friendly jurisdiction in the United States precisely because of its deference to private ordering and flexible fiduciary defaults. Overly rigid statutory ESG mandates, especially those resembling California's comprehensive Scope 1, 2, and 3 emissions reporting, may alienate corporate constituencies who value Delaware's permissive, investor-choice model. A shift too closely aligned with California's approach could risk undermining Delaware's appeal as a low-cost, contractually flexible corporate domicile. Therefore, while this paper recommends greater ESG accountability, it does so with the caveat that any proposed reforms should preserve Delaware's hallmark deference to private contracting, perhaps through safe harbors or opt-in structures for financial materiality thresholds rather than blanket mandates.

Delaware, the leading corporate domicile, can learn from California by adopting financial materiality as the defining test for ESG disclosures, akin to California's SB 261, which would allow Delaware to plug the existing regulatory gap and provide more explicit guidelines for fiduciaries grappling with the evolving ESG landscape. This would provide corporate boards and fund managers with clarity so that ESG-based decision-making is aligned with fiduciary obligations under Delaware law. This disciplined approach to ESG incorporation would boost investor confidence and reduce the risk of greenwashing or misrepresentation-related litigation.

Delaware follows its own "prudent investor" rule under Title 12 that closely mimics Uniform Prudent Investor Act standards. This standard favors prudence but

[116] Ballan & Czarnezki, *supra* note 11, at 554.
[117] *Id.* at 555.

does not explicitly address incorporating ESG considerations or distinguish between pecuniary and nonpecuniary ESG. Delaware's corporate governance framework might be better served by adopting a model such as California's SB 261 (Climate-Related Financial Risk Act), which positions ESG risks as financially material and harmonizes them with traditional fiduciary principles. Delaware, the leader in corporate governance jurisdictions, ought to follow suit with SB 253 and mandate reporting for Scope 1, 2, and 3 emissions in disclosure statements. This greater transparency would benefit fund managers so that they can perform their fiduciary duty by making more informed investment decisions. Corporate directors' and fund managers' fiduciary responsibilities are interdependent on one another; directors' commitment to transparent reporting has a direct impact on the ability of fund managers to monitor and recognize investment risks accordingly. By recognizing the significance of corporate disclosure procedures in fund governance requirements, Delaware can increase the integrity of its financial markets as well as maintain investors' confidence.

American regulatory frameworks for the governance and oversight of ESG-focused funds remain disparate, particularly when one gets into the subtleties of ESG-labeled financial products. While the Green Guides of the FTC indeed do target deceptive environmental marketing regarding consumer goods, they are silent on the unique complexities created by ESG-branded investment vehicles, leaving a regulatory gap that has inadvertently encouraged greenwashing.[118] Even the SEC, though it has floated proposals to heighten ESG transparency, does not provide guidelines on how to define financial materiality in the context of ESG securities.[119] In contrast, California has proactively enacted state laws, such as SB 253 and SB 261, mandating comprehensive disclosures of greenhouse gas emissions and climate-related financial risks for large corporations operating within its jurisdiction. Delaware-incorporated companies that meet the revenue thresholds and conduct business in California are already subject to these disclosure obligations under California law. However, for Delaware-based corporations not operating in California, similar mandates do not currently exist. The governance of funds is significantly impacted by this regulatory discrepancy. Any entity "doing business in California" that satisfies the required revenue thresholds is subject to SB 253 and SB 261, regardless of its incorporation or place of residence.[120] This includes LLCs, LLPs, Delaware-incorporated corporations, and trusts that operate in

[118] Fed. Trade Comm'n, *Environmental Marketing* (2012).
[119] Gensler, *Statement on ESG Disclosures Proposal* (May 25, 2022).
[120] California Air Resources Board, *Information Solicitation to Inform Implementation of California Climate-Disclosure Legislation: Senate Bills 253 and 261, as Amended by SB 219* (Dec. 16, 2024).

California. Because of this, a variety of fund structures with Delaware domiciles are now subject to ESG disclosure requirements if they create a connection with California.

Because Delaware's fiduciary framework is still focused on discretionary disclosure and shareholder primacy, there is regulatory uncertainty surrounding the integration of ESG. The current opt-in nature of ESG reporting leads to inconsistent and often unverifiable sustainability claims, creating challenges for stakeholders aiming to assess an organization's true environmental and social impact. California, on the other hand, has pushed for stronger ESG disclosure requirements that focus primarily on financial materiality. Delaware courts have historically recognized the need for tailored fiduciary oversight in industries with mission-critical risks. Delaware courts could mandate audits conducted by independent court-appointed or jointly selected third parties when plaintiffs make credible allegations of greenwashing. These audits would assess whether ESG claims match the underlying investment practice, whether sustainability attributes are not exaggerated or misrepresented, and whether nonpecuniary ESG factors are not used as primary factors in the due diligence process. These audits and heightened investor communication can create a more transparent and accountable ESG governance framework that would protect both investor and market integrity.

III. RECOMMENDATIONS FOR ENHANCING FUND GOVERNANCE

A. Strengthening Legal and Regulatory Frameworks for ESG Governance

The two main problems described in the previous sections are the ambiguity surrounding the fiduciary obligations that fund managers and corporate directors have under Delaware law when taking ESG factors into account, as well as the inefficiency of the regulatory frameworks that are in place now, which mostly rely on reactive rather than preventive enforcement. By clearly defining fiduciary standards of financial materiality, requiring thorough ESG disclosures and compliance oversight, and fortifying enforcement mechanisms through specific statutory amendments and increased consumer protection remedies, Delaware should improve its fund governance framework to close these gaps. The following suggestions address the regulatory deficiencies analyzed in Part 2, the fiduciary ambiguities analyzed in Part 1, and the lessons gained from California's proactive approach.

Delaware should have a more formalized procedure in place to delineate financial materiality within ESG financial products that mirrors how intangible assets are treated

under Generally Accepted Accounting Principles (GAAP). Within GAAP, "many aspects of ESG show up on the balance sheet as intangible assets, which are defined as non-monetary assets that cannot be seen or touched, such as goodwill, brand equity, intellectual properties, licensing, customer lists, and research & development."[121] However, these items are recognized on the balance sheet only when they are acquired–individually or through a merger or acquisition–or purchased outright; internally generated brand equity, goodwill, or most research-and-development outlays are normally expensed rather than capitalized. The rationale is that an external purchase price supplies an objective, auditable measure of fair value. Applying the same discipline to ESG factors would mean that environmental compliance, workforce relations, or governance transparency could be credited with balance-sheet value–or with risk-mitigating "capital" in a fund-governance context–only when they produce demonstrable, quantifiable financial benefits such as reduced regulatory penalties, lower operating costs, or verifiable reputation-driven revenue gains. In short, for ESG considerations to meet a financial-materiality threshold, they must show either a direct economic return or measurable downside protection, just as an acquired intangible must pass GAAP's recognition and subsequent-measurement tests.

California's SB 253 and SB 261 are good examples of how climate-related ESG factors can be analyzed under the standards of financial reporting conventions on intangible assets. Similar to intellectual property and goodwill requiring measurable financial impact of balance sheet recognition, these California bills demand that companies disclose and quantify the financial impact of greenhouse gas emissions and climate-related financial risk. The disclosures mandated under SB 253 of Scope 1, 2, and 3 greenhouse gas emissions and under SB 261 of climate-related financial risk are the kind of formal, numerical data for which GAAP rules demand intangible assets to be assigned a monetary value. But business-friendly Delaware ought to be a borrower, not a copycat. It should be capable of selectively adding such components as emissions disclosures, whereby the same data is directly attributable to financial performance or risk management, without the need for sweeping mandates that destroy its contractual adaptability. Delaware must concentrate on investor-focused financial materiality in requiring ESG disclosures only where these are material to shareholder value or fiduciary performance, thus elevating ESG reporting to the same standard of requirements as intangible asset accounting requirements using GAAP.

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[121] Natalie Runyon, *An Analysis of Financial Materiality in the Wake of the "Woke" and ESG Debate*, Thomson Reuters Inst., Sept. 12, 2023, https://www.thomsonreuters.com/en-us/posts/esg/financial-materiality-woke-debate/.

An example within fund governance of how financial materiality has been made evident within ESG disclosures is Lazard Inc.'s 2023 Sustainability Accounting Standards Board (SASB) Disclosure Index. The global asset management and financial advisory firm compiled detailed disclosures relating to the process of incorporating consideration of ESG factors into the investment decision-making processes, management of risks, and client-related strategies.[122] They aim to link ESG topics and cash-flow or cost-of-capital outcomes. Through compliance with SASB accounting standards, Lazard exemplifies its transparency and financial materiality of ESG factors in its investment disclosures. However, it's important to note that while SASB standards provide a structured framework for ESG disclosure on an industry basis, they currently lack statutory authority. Because 2022 reforms placed SASB standards under the International Financial Reporting Standards Foundation and its new International Sustainability Standards Board, the framework now sits alongside IFRS financial-statement rules used in more than 140 foreign jurisdictions.[123] By contrast, U.S. issuers that file under U.S. GAAP still treat SASB as a voluntary supplemental regime rather than an authoritative source akin to FASB Accounting Standards Codification. In short, SASB/ISSB is embedded in the IFRS architecture internationally, whereas in the United States, it remains an optional overlay on GAAP reporting.

The SEC has not mandated SASB adoption, which allows companies and fund managers to decide whether to follow the guidelines or not. This voluntary nature can lead to inconsistencies in ESG reporting between peers in the same industry or companies across industries. For those ESG fund managers who wish to engage with companies in which they have not invested, the threat of withholding future investment capital can be a powerful incentive. By signaling that sound ESG practices increase the likelihood of investment, fund managers can catalyze companies to enhance their ESG performance. This market-led approach offers flexibility and responsiveness, potentially achieving ESG objectives without the need for regulatory mandates.

Historically, Delaware has prosecuted false advertising, and thus any potential greenwashing claims, under the Delaware Deceptive Trade Practices Act (DTPA). Under this DTPA, a representation by a person in a business, trade, or commerce that goods or services have sponsorship, approval, characteristics, ingredients, uses, benefits,

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[122] Lazard Inc., *2023 Sustainability Accounting Standards Board (SASB) Disclosure Index* (2023).

[123] Int'l Sustainability Standards Bd., *ISSB and SASB Standards—How They Work Together* (IFRS Found., 2023).

or quantities they do not have is defined as a deceptive act.[124] The provision gives a clear statutory basis against false or exaggerated ESG claims in financial product marketing. Similarly, the Delaware Securities Act governs fraudulent practices in connection with the offer, sale, or purchase of securities, prohibiting "any device, scheme or artifice to defraud" and "any untrue statement of a material fact or [omission]" in securities transactions.[125] As such, the statute already represents an important device for ensuring investor disclosure and thus could be extended to explicitly encompass ESG misstatements.

For instance, amending the DTPA and the Delaware Securities Act to include "greenwashing" as a specific deceptive or fraudulent act would clarify a legal predicate for enforcement. The Delaware Securities Act already empowers the Director to bring actions in the Court of Chancery to restrain or enjoin acts which constitute a violation of the Act, and to seek ancillary relief including restitution, rescission, or the appointment of a receiver.[126] Furthermore, the proposal labels greenwashing as a violation of the Securities Act and thus ensures that fraudulent ESG-related disclosures in the context of securities offerings are within the jurisdiction of regulatory oversight. Investors who suffer damage from misleading statements of products related to ESG may invoke this statutory foundation as the basis for injunctive relief, damages, or other restitution in Chancery. It would provide litigants with a clear statutory means of redress, in addition to the Director's power under § 73-602 to compel compliance and ancillary equitable relief. For example, the Court of Chancery may, under the Act, grant ancillary relief "as may be appropriate in the public interest," order restitution, or appoint a conservator to oversee remedial measures in cases involving ESG misrepresentation.[127] These reforms would put Delaware in a better position to hold fund managers accountable for lying to investors about ESG and build on the many pre-existing statutory and equitable remedies.

The integration of the fiduciary duty model with current consumer protection laws like the DTPA and Delaware Securities Act would promote compliance through explicit assignment of enforcement power and actionable scope of ESG claims. Specific extension of standing to sue from the regulatory director to specifically include direct victim individual investors for ESG misrepresentations would increase accountability and offer better incentives for fund managers to report ESG facts honestly. Second,

[124] Del. Code Ann., 6 Del. C. § 2532(a)(5) (2023) (deceptive trade practices).
[125] Del. Code Ann., 6 Del. C. § 73-201 (2023) (employment of manipulative and deceptive devices).
[126] Del. Code Ann., 6 Del. C. § 73-602 (2023) (injunctions).
[127] *Id.*

altering procedural features, such as shifting the burden of proof to fund managers to establish ESG claims on a prima facie showing of possible misrepresentation, would more squarely align enforcement mechanisms with fiduciary responsibilities. Such reforms would put the Delaware judiciary to hold fund managers more accountable for fraudulently misleading investors about the ESG qualities of a financial product offered to the general public.

At the heart of any reform attempt lies the operationalization of "pecuniary ESG" ("risk-return ESG") in contrast to "nonpecuniary ESG" ("collateral benefits ESG"). Hence, under that demarcation, risk-return ESG could include factors, such as environmental risks, labor practices, and standards of governance, that either improve risk-adjusted financial returns or mitigate risk. Such factors can be permitted under the prudent investor rule if they credibly contribute to enhancing profit, reducing legal or regulatory penalties, or strengthening corporate goodwill in ways that improve returns.[128] These are well within the managerial discretion recognized under the business judgment rule, wherein the directors of a corporation must act on an informed basis, in good faith, and in the honest belief that the action taken was in the company's best interests.[129] These approaches generate or preserve measurable economic value and, thus, do not violate Delaware's precedent that directors and fund managers may not divest returns without justification.[130]

Nonpecuniary ESG, by contrast, addresses moral, social, or philanthropic concerns that do not directly link to risk-adjusted returns. In these instances, Delaware's unwavering commitment to shareholder primacy prescribes caution. As articulated in *eBay Domestic Holdings, Inc. v. Newmark*, the Delaware Court of Chancery stated unequivocally that "promoting, protecting, or pursuing non-stockholder considerations must lead at some point to value for stockholders."[131] The court found that directors breach their fiduciary duties when they act to protect a business strategy that openly eschews stockholder wealth maximization unless expressly authorized.[132] In that case, the court rejected the argument that directors of Craigslist could adopt a corporate strategy to prioritize community interests over shareholder value without explicit shareholder consent. Instead, it emphasized that "the directors are bound by fiduciary duties to promote the value of the corporation for the benefit of its

[128] Schanzenbach & Sitkoff, *ESG Investing: Theory, Evidence, and Fiduciary Principles* (Oct. 1, 2020).
[129] Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985).
[130] Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).
[131] eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1 (Del. Ch. 2010).
[132] *Id*.

stockholders. Directors are not at liberty to sacrifice stockholder value in the hope of achieving other benefits or goals."[133] This principle applies directly to support the "sole interest" rule under the trust law of ERISA, that fiduciaries should operate within well-defined boundaries when the law or beneficiaries explicitly permit them to operate otherwise.

Delaware should amend its LLC/LLP Law Title 6, Trust Law Title 12, and DGCL Title 8 business entity statutes to create a single statutory financial materiality threshold that regulates the incorporation of ESG considerations into fiduciary decision-making. This statutory default rule would specifically restrict fiduciaries, including corporate directors, trustees, LLC managers, and LLP partners, from taking into account ESG factors that materially and demonstrably improve or safeguard the financial interests of partners, shareholders, or beneficiaries (pecuniary ESG). The implied covenants of good faith and fair dealing would act as a judicial check on potential abuse of fiduciary discretion in all three statutory frameworks. This would stop fiduciaries from using ambiguous or comprehensive ESG-related contractual language to justify investment actions that lack true financial justification, self-dealing, or greenwashing.

In order to codify a statutory presumption that fiduciaries may only take into account ESG factors that are expressly justified by demonstrable financial materiality to the trust's beneficiaries, Title 12, which regulates trusts and fiduciary investment standards, should amend §3302 (Prudent Investor Rule). This presumption, as inspired by ERISA's sole interest rule as interpreted in cases like *Spence v. American Airlines*, would limit fiduciaries to ESG factors demonstrably linked to financial performance unless explicitly authorized by investors or beneficiaries. If the trust instrument expressly permits consideration of nonpecuniary ESG goals, this presumption may be contractually overridden, so long as it does not contravene the implied covenant of good faith and fair dealing. This strategy strikes a balance between settlor intent and fiduciary discipline, which is consistent with Delaware's emphasis on trust design flexibility. By borrowing from the 2022 DOL ESG rule and adapting it into Delaware's shareholder-centric environment, the state creates a far clearer climate for fund managers: they remain safe in adopting ESG strategies that genuinely improve financial performance, and vice versa, must obtain explicit investor permission before pursuing purely moral ends.[134]

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[133] *Newmark*, 16 A.3d, *supra* note 131, at 34.

[134] *Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights*, 87 Fed. Reg. 73,822 (Dec. 1, 2022) (to be codified at 29 C.F.R. pt. 2550).

Title 8 of the DGCL, governing the fiduciary duties of officers and directors of a company, needs to be amended to include an implied financial materiality requirement in the context of ESG integration under duties of care and loyalty. Specifically, the law needs to enact that corporate fiduciaries are only permitted to consider ESG factors that are related to enhancing or maintaining long-term corporate value or shareholder returns. This would enact case law precedents such as *eBay v. Newmark*, which underscore the obligation of directors to act in the financial interests of shareholders and prohibit trading off returns on behalf of other ideological or social objectives without shareholder consent. The amendment would further require directors to substantiate ESG-driven decisions with a written rationale grounded in financial analysis, such as risk mitigation, goodwill preservation, or compliance cost savings.

Significantly, such ESG monitoring would remain subject to the *Caremark* standard, which mandates directors to implement and oversee internal controls so that mission-critical risks, including material ESG factors, are properly monitored. While directors retain business judgment deference, failure to implement adequate oversight over ESG disclosures or commitments could be a breach of fiduciary duty under *Caremark*. Including a financial materiality threshold in the DGCL could offer statutory clarity, aligning ESG integration with current fiduciary duties and judicial expectations for monitoring.

The same default financial materiality standard for ESG factors should be adopted by amending Title 6, which regulates Delaware's LLCs and LLPs. The statutory revision should include a default rule that restricts fiduciary discretion to pecuniary ESG considerations–those that have a definite and quantifiable impact on the economic interests of members or partners–because fiduciary duties in these entities are more flexible and strictly regulated by contractual agreements. However, the law should specifically permit LLC or LLP agreements to extend or limit this standard per Delaware's deference to freedom of contract in alternative entities. The implied covenant of good faith and fair dealing must still apply to such changes, which must be expressly mentioned in the operating or partnership agreement. This change is warranted because, although Delaware LLC and LLP law provides for a great deal of contractual flexibility under 6 Del. C. §§ 18-1101 and 17-1101, this flexibility has also resulted in disparities in the interpretation and application of fiduciary duties, particularly in new fields like ESG investing. Delaware can give courts and parties legal certainty without compromising the contractual framework that distinguishes these alternative entities by establishing a clear financial materiality default. A default of this kind would serve as a clarifying baseline, lowering the possibility of opportunistic

fiduciary behavior while preserving the ability for private ordering to take precedence in situations where parties consciously decide to take into account more general ESG objectives.

B. Enhancing Fiduciary Accountability and Enforcement Mechanisms

An axis on which Delaware could proactively address greenwashing is through the Court of Chancery's equitable powers. Historically, Delaware has often relied on private litigants to allege derivative fiduciary breaches after the fact. However, the strategic use of equitable remedies can protect consumers and investors immediately. This misrepresentation leads to investments that do not align with investors' financial interests or ethical preferences, thereby violating their duty of loyalty. In the deal, BlackRock agreed to perform regular third-party audits, be more transparent about its ESG practices, and increase engagement with investors. Mandatory third-party audits verifying ESG claims routinely and independently would meet investor and regulatory standards.

Courts have established that while corporate directors are afforded business judgment deference, they may still be held liable for breaches of duty that involve "acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law."[135] By contrast, fund managers must "act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use."[136] These statutes suggest that company directors may incorporate ESG factors as part of the duty to promote shareholder value, while fund managers should consider ESG investments in terms of financial prudence and how well they improve risk-adjusted returns and align with the investment objectives of beneficiaries.[137] Delaware law leaves a gap in regulation on which type of ESG factors can be considered financially material. The lack of SEC guidance on pecuniary ESG criteria means that fund managers have discretion in determining whether ESG factors are financially material under their fiduciary duty.[138]

To remove the current ambiguity concerning fiduciary consideration of ESG factors in fund management, Delaware should adopt a financial materiality standard

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[135] Del. Code Ann., 8 Del. C. § 102(b)(7) (2023) (provision protecting personal liability with conditions).
[136] Del. Code Ann., 12 Del. C. § 3302(a) (1999).
[137] Schanzenbach & Sitkoff, *ESG Investing: Theory, Evidence, and Fiduciary Principles* (Oct. 1, 2020).
[138] Gensler, *Statement on ESG Disclosures Proposal* (May 25, 2022).

that clearly distinguishes between pecuniary and nonpecuniary ESG. Significantly, such reform would be in line with Delaware's existing restriction that the implied covenant of good faith and fair dealing may not be waived in LLC and LP agreements, and would clarify how ESG factors apply to that covenant. In so doing, it would provide courts with a clear criterion for the implementation of the entire fairness standard in cases where fund managers are accused of breaching their fiduciary duties by prioritizing nonpecuniary ESG goals. As recent commentary observes, "the Delaware courts' application of the entire fairness standard of review when there is fraud on the board is not a new concept, but it has recently become a focus area."[139] A statutory threshold would, hence, aid judicial enforcement by providing an objective measure of financial materiality against which to tune both the fairness of process and the fairness of price in ESG-driven decisions.

If a manager or director adopts nonpecuniary ESG factors without investor or beneficiary consent and, in so doing, departs from otherwise efficient risk-adjusted returns for the benefit of personal or ideological preferences, Delaware courts could view such a scenario as a breach of their duty of loyalty. Fiduciaries shall act with prudence for the beneficiaries' exclusive benefit and financial performance. Incorporating nonpecuniary ESG objectives without authorization may be the functional equivalent of a conflict-of-interest transaction. For instance, courts could apply an entire fairness review, where the Delaware Supreme Court explained that when entire fairness is the applicable standard of judicial review, the defendant fiduciary has the burden of persuasion to demonstrate that the transaction represented the product of both fair dealing and fair price.[140]

The entire fairness review requires fiduciaries to prove the procedural integrity of their decision-making process, fair dealing, and that the transaction is congruent with the beneficiaries' financial interests, fair price. As the court in *Weinberger v. UOP, Inc.* stated:

> The concept of fairness has two basic aspects: fair dealing and fair price. Fair dealing embraces questions of when a merger transaction was timed, initiated, structured, negotiated, and disclosed to the directors and how the approvals of the directors and the stockholders were

[139] Leo E. Strine, Jr., et al., *Fiduciary Duties of the Board of Directors: In the Wake of the Financial Crisis and the Era of Shareholder Activism*, Stan. L. Sch. Rock Ctr. For Corp. Governance, 25 (2010).
[140] Kahn v. Lynch Comm'c Sys., Inc., 638 A.2d 1110, 1117 (Del. 1994).

obtained...[141]

Applying this framework to ESG integration, the fair dealing concept would be done by investigating if fiduciaries conducted an adequate analysis, obtained independent advice, and disclosed material information. Fair price would test whether the integration of ESG factors would be consistent with the financial interests of the beneficiaries and would not inappropriately favor ideological or nonpecuniary goals. For instance, in the case of a green energy project, should a fiduciary justify an investment as a hedge against regulatory risks or to create a better long-term profile of profitability, courts would review whether the fiduciary acted with good faith through detailed analysis of the risk-return profile of the project, use of qualified and independent advisers, and providing transparent information relevant to the beneficiaries. Without such evidence, a court might reasonably conclude that the fiduciary did not adhere to the exacting standards articulated in *Kahn* and *Weinberger* and, therefore, breached its duty of loyalty.

Courts may demand that fiduciaries credibly show that the ESG justification is legitimate and consistent with the beneficiaries' financial interests. The complete absence of any procedural protections weighs very strongly against fairness.[142] The Delaware courts may similarly insist that the approach provides evidence of increasing the risk-adjusted return, reducing material risk, third-party validation of the ESG metrics, deep analyses that present the association between ESG factors and financial performance, and extensive disclosures to the beneficiaries. Where the stated reason is pretextual or a sham for nonpecuniary motives, the court may shift its analysis to an entire fairness review to ensure compliance with fiduciary obligations. As explained in *Tibble v. Edison International*, fiduciary responsibilities are ongoing, involving repeated supervision in addition to initial investment decisions. In practice, repeated ESG conformity under Delaware's regime ought to include mandated periodic ESG reviews and public disclosures, not just reactive audits triggered by lawsuits. Fund managers should implement systematic internal systems of ESG conformity, comparable to those required under the Caremark doctrine. Fund managers and directors would actively track ESG commitments so they remain financially material and within the fiduciary scope.

Furthermore, legal reforms could further expand private rights of action. Investors who take the view that they have been directly deceived by mislabelled ESG offerings

[141] Weinberger v. UOP, Inc., 457 A.2d 701, 711 (Del. 1983).
[142] *Lynch Commc'n Sys., Inc.*, *supra* note 140, at 1121.

could sue directly, rather than via derivative claims. Because greenwashing tends to be a matter of marketing or disclosure, it is injurious to investors in their direct capacity rather than their derivative one as shareholders in the corporation.[143] Accordingly, under a revised Title 12, these injured investors could circumvent derivative litigation procedural hurdles and thus have strengthened remedies to recover damages. The second advantage of a rule change is increased accountability because once the fund managers become aware that an easier path may be direct litigation for injured investors, they would more carefully scrutinize their ESG claims.

Consistent with that approach, equitable deference could be preserved for "risk-return ESG" cases that align with the prudent investor rule, provided there are no red flags signaling a breach of fiduciary obligations. In contrast, "ESG conflict" cases–in which personal beliefs or philanthropic objectives outweigh financial justifications–would warrant heightened scrutiny akin to an entire fairness review. The court, in so holding, would offer essential guidance on how plaintiffs can effectively challenge suspect ESG claims without discouraging fiduciaries from incorporating valid risk-return ESG factors that align with Title 12's emphasis on prudence and beneficiary-focused decision-making. Accordingly, if a manager's decision-making process demonstrates credible alignment with risk-adjusted returns, the court could find compliance with the prudent investor standard. Instead, if the process reveals nonpecuniary ESG factors being taken into consideration during the investment decision-making process, stricter judicial oversight naturally ensues.

Delaware can sharpen fiduciary accountability for greenwashing by pairing the Court of Chancery's equitable toolkit with an ex-ante valuation rule that treats ESG claims much like GAAP treats purchased intangibles. At present, directors receive business-judgment deference unless their conduct evinces bad faith, while trustees and fund managers must meet a prudent-investor test that focuses on risk-adjusted returns. Yet neither regime supplies a bright-line standard for deciding when an ESG factor is "financially material" (i.e., pecuniary) versus "non-pecuniary." Borrowing GAAP's logic, Delaware could require that an ESG attribute be credited to fund value only when it produces demonstrable, auditable economic benefits, just as goodwill or a patent is recorded only when acquired for an objective purchase price and subjected to periodic impairment tests. This statutory threshold would operate ex ante: if an ESG

[143] Nicole Gehrig & Alex Moreno, *An Exploration of Greenwashing Risks in Investment Fund Disclosures: An Investor Perspective*, CFA Institute: Research & Policy Center (Sept. 2023), https://rpc.cfainstitute.org/sites/default/files/-/media/documents/article/industry-research/greenwashing-report.pdf.

feature cannot show a quantifiable boost to cash flow, cost of capital, or risk mitigation, the manager must treat it as non-pecuniary and obtain explicit beneficiary consent before sacrificing returns.

Codifying that gate-keeping rule would streamline the Chancery Court's two-track review. "Risk-return ESG" that satisfies the pecuniary materiality test would continue to enjoy the protection of the prudent-investor rule: absent red flags of disloyalty, courts would defer to the manager's economic calculus. By contrast, "ESG conflict" decisions–those motivated by personal ideology or third-party interests–would trigger entire fairness scrutiny unless pre-authorized. Under Weinberger and its progeny, the burden would then shift to the fiduciary to prove both fair dealing (robust process, independent advice, full disclosure) and fair price (ESG integration genuinely enhances the beneficiaries' economic position). Where the justification is pretextual, Delaware judges could impose rescission, surcharge, or fee-shifting in equity, mirroring the remedial bite applied when fraud on the board taints a related-party transaction.

Complementing this ex-ante filter, Delaware could refine the Consumer Protection Act as an ex-post backstop. Aligning DCPA deception standards with the GAAP-style materiality rule would let defrauded investors sue directly, rather than derivatively, when ESG branding strays from the pecuniary boundary. The prospect of direct liability, buttressed by Chancery oversight, would incentivize managers to install Caremark-like compliance systems: periodic third-party audits of ESG data, documented valuation models linking ESG inputs to financial outputs, and plain-English disclosures that distinguish pecuniary from value-aligned but non-pecuniary objectives. Together, the ex-ante valuation rule and an ex-post DCPA remedy would close the greenwashing gap, allowing Delaware to enforce ESG promises with the same rigor it applies to any other representation that affects asset value.

CONCLUSION

While ESG investing takes hold, Delaware law's failure to define standardized fiduciary responsibilities has created a regulatory gray area open to fund managers and corporate directors as a tool of greenwashing investment vehicles. This paper has demonstrated how greenwashing, or the false representation of sustainability credentials, undermines the integrity of ESG markets and exposes investors to excessive risk. While the SEC and FTC have begun to oversee misstatements about ESG, their regulations operate after the fact and do not determine fiduciary standards in advance. The lack of enforceable standards for disclosure related to ESG permits investment companies to set ESG terms for themselves, which facilitates manipulative branding

tactics that ultimately destroy investor confidence.

Case law, including *SEC v. BNY Mellon*, shows how misleading ESG disclosures in mutual fund prospectuses resulted in SEC sanctions for violating antifraud rule requirements. Similarly, in *Spence v. American Airlines*, the court reaffirmed ERISA's sole interest rule and held that fiduciaries who use ESG considerations without a direct connection to investment performance risk violating the duty of loyalty. Other cases–*Tibble v. Edison International*, *Pegram v. Herdrich*, and *Fifth Third Bancorp v. Dudenhoeffe*r–also support the judicial inference that fiduciary ESG integration needs to be pecuniary unless expressly enabled otherwise. Together, these cases confirm that ESG misrepresentation, rather than ESG investment itself, is the target legal vulnerability of greenwashing.

Delaware's current fiduciary landscape, as entrenched in Title 8 for corporations, Title 12 for trusts, and Title 6 for LLCs and LLPs, does not have uniform statutory guidance on ESG integration. This provides fiduciaries with the ability to exercise significant discretion, frequently without the supervision necessary to ensure that ESG considerations contribute to providing risk-adjusted returns. The analyses of *Gatz Properties v. Auriga Capital Corp.*, *In re Caremark*, and *Marchand v. Barnhill* indicate that while Delaware courts anticipate fiduciaries to monitor mission-critical risks, there is no standard to determine when ESG is one. Fiduciaries are open to liability unless the system is reformed, not because they use ESG, but because they lack a process to justify it when asked to do so.

In response to this weakness, this article proposes one statutory financial materiality standard in Delaware's fiduciary codes. The proposed reform would restrict fiduciaries from considering only such ESG factors that lead to financially advantageous outcomes, except where expressly authorized by shareholders or beneficiaries. This model preserves contractual flexibility, especially for LLCs and LLPs, while triggering the implied covenant of good faith and fair dealing as a judicial umbrella. By establishing a clear default rule, Delaware can preserve its dominance in corporate law while reducing litigation risk and rebuilding investor confidence in ESG markets.