Judge's ruling in ESG case could spark chaos for 401(k) managers

By Brett Rowland | The Center Square
Jan 15, 2025

(The Center Square) – A federal judge's ruling could have sweeping consequences for how companies invest retirement savings in the U.S.

Judge Reed O'Connor ruled against American Airlines in a class-action lawsuit brought by a pilot. The pilot alleged American Airlines violated its responsibilities to employees by using BlackRock to manage some of the company's retirement funds despite the asset manager's public comments on ESG investing.

ESG investing considers non-financial criteria including environmental, societal and governance factors in investment decisions.

O'Connor ruled American Airlines violated its "duty of loyalty" under the Employee Retirement Income Security Act by failing to rein in BlackRock's ESG practices. However, the judge also ruled that American Airlines acted prudently in its oversight of BlackRock's management of the funds.

"The Court concludes that the facts compellingly demonstrated that Defendants breached their fiduciary duty by failing to loyally act solely in the retirement plan's best financial interests by allowing their corporate interests, as well as BlackRock's ESG interests, to influence management of the plan," O'Connor wrote in the ruling. "[American Airlines] acted according to prevailing industry practices, even if leaders in the fiduciary industry contrived to set the standard."

Lawyers who have been tracking this case warn that the ruling could have a ripple effect, potentially on nearly every retirement plan in the country.

Andrew Oringer, partner and general counsel at The Wagner Law Group, told Pensions & Investments that the ruling could have a chilling effect.

"Even if this decision is reversed, the fact that a court had gone to actual judgment for ERISA violations in the ESG context may well have a chilling effect on the taking into account of ESG considerations by ERISA fiduciaries, in the near term and maybe into the foreseeable future," he said. "ERISA fiduciaries tend to be conservative, and this kind of additional risk may well turn even pro-ESG fiduciaries in a 'who needs this' direction."

Carol Buckmann, founding partner of law firm Cohen & Buckmann, told P&I that she expects American Airlines to appeal, but wasn't confident about its prospects in the Court of Appeals for the Fifth Circuit, which she said "will probably not be sympathetic."

Asset management firms BlackRock, State Street, and Vanguard oversee more than $5.4 trillion in U.S. retirement assets, according to Bloomberg market share analytics.

"They're the Walmart, Target, and Amazon of index funds," Daniel Aronowitz, president of Encore Fiduciary, told Bloomberg. "Everybody has the same risk. By that standard, plaintiffs could sue almost every single 401(k) in the country."

The judge's decision comes as some companies move away from ESG practices.

BlackRock recently left the United Nations-backed Net-Zero Banking Alliance, a group "committed to aligning their lending, investment, and capital markets activities with net-zero greenhouse gas emissions by 2050."

Multiple Republican groups applauded that move. The Bull Moose Project called it "a HUGE victory for conservatives."

"The pressure has worked. BlackRock used to be a leader in the ESG movement – now they're listening to conservative voices," the group wrote in a post on X. "We're seeing a complete victory over the ESG movement. It's a proven loser for investors, and they know it."

U.S. Rep Jim Jordan, R-Ohio, said others should follow that example.

"This is a huge win for freedom and American prosperity," he wrote on X. "All U.S. financial institutions should follow suit and abandon the climate cartel and woke ESG policies."

Kent Lassman, the president and CEO of Competitive Enterprise Institute, described it as being a "good and productive step."

"There is no need to speculate why the company changed course," he wrote on X. "We don't know that. We do know that stepping away from the Net Zero initiative is a step away from diluting the focus of a company that has a legal and ethical fiduciary duty."

BlackRock left as it and about 60 companies are being investigated by Congress for allegedly colluding as a "woke ESG cartel" to "impose radical environmental, social, and governance goals on American companies."

Last month, Goldman Sachs was the first bank to withdraw from the alliance, followed by Wells Fargo. Citigroup, Bank of America, Morgan Stanley and JPMorgan also withdrew from the Net-Zero Banking Alliance, as The Center Square previously reported.

Blackrock said its "participation in NZAMi didn’t impact the way we managed client portfolios. Therefore, our departure doesn't change the way we develop products and solutions for clients or how we manage their portfolios. … Our commitment to helping our clients achieve their investment goals remains unwavering,” Bloomberg reported.

Last month, the U.S. House Judiciary Committee announced it was investigating more than 60 US-based asset managers' involvement in the alliance, including BlackRock Inc., JP Morgan Asset Management, Rockefeller Asset Management, State Street Global Advisors, among others.

The committee also issued a report, "Climate Control: Exposing the Decarbonization Collusion in Environmental, Social, and Governance (ESG) Investing," saying it found "direct evidence of a 'climate cartel' consisting of left-wing activists and major financial institutions that collude to impose radical environmental, social, and governance goals on American companies."

The Center Square contributor Bethany Blankley contributed to this report.