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ESG Disclosures and Litigation Risk

The past several years have seen a significant increase in the number of companies making public disclosures concerning environmental, social, and governance ("ESG") issues. Reflecting this trend, the World Economic Forum ("WEF") recently released a Consultation Draft of proposed common ESG metrics for companies to consider including in investor communications. While such ESG disclosures can provide substantial benefits for companies, including with respect to shareholder support and engagement, customer loyalty, and employee morale, they can also give rise to litigation and regulatory risk. As ESG-related issues have gained importance with investors and consumers, we have seen an increase in litigation and regulatory interest centered on such disclosures—a trend that we expect to continue.

Like any corporate disclosures, ESG-related statements that are later alleged to be materially inaccurate or misleading can become the basis for securities litigation. While such claims have often been dismissed on the grounds that general statements concerning a company's commitment to ethical conduct or social values are merely "aspirational" or corporate "puffery," some claims based on more specific or concrete statements have survived motions to dismiss, such as in the recent CBS case. Furthermore, to the extent that such ESG-related disclosures become more standardized and are made pursuant to a specific disclosure regime, it is less likely that courts would find such disclosures to be mere puffery.

Climate change-related disclosures have already provided one example of the heightened regulatory risk related to ESG-type disclosures. For many years, several state attorneys general have investigated the sufficiency of such disclosures, in some cases, reaching settlements that required changes to climate change-related disclosures, and in others, commencing litigation. Notably, the SEC, the principal federal regulator of corporate disclosures, was not involved in many of these cases. A widely adopted disclosure framework with standardized ESG-related disclosures could lead to increased SEC interest and enforcement activity.

One particular example in the WEF Consultation Draft highlights the potential litigation and regulatory risk from adoption of ESG-related disclosures. The Consultation Draft suggests that companies should disclose information about the percentage of employees and business partners who have received anti-corruption training along with the "Total number and nature of incidents of corruption confirmed during the current year." Needless to say, requiring companies to disclose the number of corruption incidents discovered during any particular year would have significant consequences on both the regulatory and civil litigation fronts.

Recognizing that there is growing momentum towards the development of a common framework for ESG disclosures, companies should evaluate the potential litigation and regulatory risks of proposed metrics and how they would adapt to a regime in which such metrics became a widely accepted standard.

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