MITIGATING LEGAL RISK IN SUSTAINABILITY REPORTING

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As the annual wave of sustainability reports are being finalised for publication, businesses need to be aware of some of the potential pitfalls of over or under reporting on the aims, progress, detail and implementation of their sustainability-related actions.

"Sustainability reporting is coming under increasing scrutiny"

Sustainability reporting is coming under increasing scrutiny from academics, civil society organisations and claimant law firms, who may use the information for a number of purposes, including:

- to support academic reports which infer a connection between a business and suppliers with unhealthy health and safety, labour or environmental records;
- to allege "greenwashing" or "bluewashing" (in respect of social matters) of activities; or
- to allege a direct duty of care between the head office of a multinational company and those adversely affected by the operations of its subsidiaries or suppliers, with an associated responsibility for damages payouts.

All this is in addition to specific scrutiny of regulated activities, especially of sustainability-linked financial products.

"allegations that multinationals have unjustly profited from a failure by other legal entities to implement proper health and safety"

LEGAL RISK

Over the last four to five years, we have seen a significant increase in cases before the English courts (and to a certain extent in the Netherlands and Germany also) where an English domiciled multinational is alleged to have taken responsibility for the actions of overseas subsidiaries or supplier companies and/or assumed a direct duty of care or other responsibility for the treatment of individuals affected by operations in their value chain. Although the relevant line of case law started off by focussing on the responsibilities alleged to have been assumed by parent companies, this has now expanded to encompass allegations that multinationals have unjustly profited from a failure by other legal entities to implement proper health and safety, labour and environmental standards at the very beginning of their supply chain and across to the end of life disposal of assets.

A number of 'routes to liability' can be extracted from the relevant case law (which at this stage, has merely concluded that there is an arguable case in relation to the above scenarios, as opposed to an actual finding of liability after a full trial), including:

- exercise of management or joint management of the relevant activity;
- providing defective advice and/or promulgating defective policies that are then implemented as a matter of course;
- promulgating policies and taking active steps to ensure the implementation of those policies;
- 'holding-out' in its public documentation that it exercises a particular degree of supervision and control over a specific area; and
- failing to take appropriate steps to ensure that a potentially hazardous asset, which is under its control, would not cause harm to third parties.

Other allegations have also been made in ongoing court proceedings in England which have yet to be tested by the courts, including purchase of materials at a price that the business must have known could not be achieved without the use of forced/child labour and/or without paying a living wage.

As these are tortious claims, the applicable law is generally that of the jurisdiction in which the harm occurred, meaning that these principles will likely be applicable to multinationals operating in at least all countries which adopt English law as a base, including much of Anglophone Africa and many Asian countries, as well as some countries in South America.

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In addition, the last 10 years have seen a number of other legal claims being brought against multinationals (with varying degrees of success), including for false advertising (which is also a criminal offence in a number of jurisdictions), breach of regulatory duties where supply chain due diligence laws exist (particularly France) and in extreme cases, complicity in war crimes.

Relevant groups have also mooted the possibility of bringing claims against corporates on other bases (and in some cases, have already issued a pre-action letter, setting in motion the litigation process) including:

- misrepresentation claims in respect of IPOs; and
- claims that directors have failed to comply with their duties to act in a way that promotes the company's success and to exercise reasonable care, skill and diligence, by failing to put in place sufficient ESG-related policies.

"have in mind how the contents may be used by organisations looking to attack a business "

HOW DOES THIS TIE INTO SUSTAINABILITY REPORTING?

Claimant law firms use the statements made in sustainability reporting and other public reports (for example, annual reports and accounts) to justify allegations that a company has exercised management or control over the activities of another entity, or that they have held themselves out as controlling or having superior knowledge and expertise over another area, thereby creating a legitimate expectation that they would protect against specific harms which later occurred.

It is therefore important when drafting a sustainability report to have in mind how the contents may be used by organisations looking to attack a business and make appropriate adjustments where possible, to make themselves a less attractive target for such claims.

WHAT ABOUT REPUTATIONAL RISK?

As mentioned above, sustainability reports are also often used in academic research (resulting in published papers which are then used by civil society organisations as part of a wider advocacy campaign against corporates). For example, an academic may consider whether a business has complied with certain voluntary or "soft law" standards, whether its claims are supported by any external data and whether they match other available information on its supply chain.

"Ignoring these can have further reputational consequences"

Claims made in sustainability reports (or an alleged lack of transparency) may also form the basis of complaints to non-judicial bodies, such as the OECD National Contact Points or the UN Special Procedures Mandate Holders. Whilst neither of these bodies has the power to compel a corporate to take specific action, they can (and do) make recommendations to bring a corporate's practices into line with the relevant voluntary standards. Ignoring these can have further reputational consequences, as well as potentially derailing an already well thought out plan to implement an increasingly challenging sustainability programme over time. The company will wish to avoid interruptions to its journey towards integrating greater sustainability in a way which is achievable, in terms of time, resources and business planning.

WHAT SHOULD I DO?

Talk to the team at WFW if you would like us to advise on ways of mitigating legal and reputational risks arising from the sustainability reporting exercise.

KEY CONTACTS

SARAH ELLINGTON
PARTNER • LONDON

T: +44 20 3314 6317

SEllington@wfw.com

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