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ESG in the Disputes and Contentious Regulatory Sphere—a Mini-series: Introduction to ESG in the Disputes and Contentious Regulatory Sphere

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The growth of ESG issues

Environmental, Social, and Governance issues (or "**ESG**") have rapidly carved out a space for themselves in the collective corporate consciousness. Until relatively recently, corporates may have been expected to "do the right thing" in response to a range of ESG issues, but outside of a few specific areas, such as Modern Slavery or Anti-Bribery and Corruption (where the legislature has intervened either at national or supra-national level) there has been little in the way of legislative or regulatory oversight of corporate responsibility in the ESG space.

An earlier wave of "corporate social responsibility" initiatives in the private sector responded to the ever-increasing expectations of conscious consumerism in the "governance" sphere. More recently, a surge of high-profile global events (not least the COVID-19 pandemic and the Black Lives Matter movement), has pushed issues under the "social" branch of ESG, including labour conditions, diversity, and employee wellbeing, to the forefront. Focus on climate change and other environmental factors is more pronounced than ever before. Perhaps unsurprisingly, national legislatures are now scrambling to find ways to formalise and incorporate ESG into the legislative and regulatory framework. Although ESG issues are holistic, in that they impact across a corporate's entire business, we are likely to find that the legal landscape relating to ESG concepts rapidly becomes vast, disparate, and varied across jurisdictions.

As these measures come into effect, corporates will be focused on meeting the ESG standards of the jurisdictions in which they operate, including implementing procedures to minimise the risk of non-compliance. For now at least, the litigation and regulatory risk will likely be back-of-mind. However, as an increasing number of corporates look to share positive stories about the ways in which their business is changing, an awareness of the potential pitfalls of the ESG-related legal landscape at an early stage has the potential to mitigate and protect against future civil litigation and regulatory enforcement. First and foremost, corporates must be cautious that representations about their ESG credentials are true and not misleading or exaggerated.

No one article or series of articles could possibly hope to cover all (or even most of) the aspects that make up the litigation and regulatory landscape in respect of ESG issues. Instead, in this mini-series, we will consider a range of litigation and contentious regulatory risks:

- Click here for our thoughts on "*ESG in Civil Litigation*" in which we consider the risks corporates face by way of disputes with shareholders, consumers and other third parties and the impact of the growth of class actions (or group actions) in the U.K.; and

- Click here for our overview of "*Regulatory and Criminal Offence Risks in the ESG Context*" in which we examine the potential regulatory risks, including FCA Climate-Related Reporting Requirements, with a focus on the requirements of the regulatory regimes and the potential penalties. In addition, we will address potential sources of criminal liability for directors as well as commercial organisations.

Of course, as with all new and developing areas of law, the "litigation tail" cannot be allowed to "wag the corporate dog"—put shortly, the risk of contentious disputes must be seen in the context of the many benefits and opportunities the ESG landscape might bring. However, an early recognition and mitigation of these risks of potential litigation or regulatory investigations could put the well-prepared corporate in an advantageous position.

In the current climate, it is clear that there are increasing compliance and regulatory obligations and more complex multi-jurisdictional regulatory frameworks in relation to ESG issues for companies to navigate. At the same time, criminal liability for directors and corporates is increasingly being used as a deterrent for non-compliance, with a potentially expanding circle of persons for whose actions a company may be held criminally liable. For many corporates, these risks will not be new, and instead will represent part of the growing to-do list of the in-house compliance team. However, what we can all agree on, is that as legislative and regulatory frameworks in the ESG space expand, so do the obligations of corporates.

What should corporates be doing?

To address this expanding ESG matrix, what can corporates do to comply with the regulatory frameworks which apply to them and avoid the seemingly inevitable tide of ESG litigation? The first step is simply to be alive to the risks and the myriad ways in which disputes might occur. In particular:

- Corporates must now include ESG standards as part of the due diligence process for vetting third parties, and, more than ever, they must regularly review and strengthen corporate governance procedures. One key outcome of the increased focus on ESG issues is that the compliance function has grown in importance.

- Beyond this, each corporate needs to think carefully about the areas in which third party claims are likely to arise in its business—it will be different for everyone. The legal and risk teams should consider whether they have sufficient oversight of these areas, and whether they need to input into the formulation of policy in those areas. Businesses should then give consideration to their reporting mechanisms—focusing on the fact that public-facing documents and statements are likely to be the starting point for any claimant seeking to bring a claim. An appropriate balance needs to be struck between exhibiting the good work / progress the company is making and over-reaching in the name of good corporate citizenship.

- In addition, careful thought should be given to the governance matrix of the entire corporate structure. How are the policies of subsidiaries made, promulgated, implemented, and enforced? Consider whether this should be done at subsidiary level, or be consistent across the group. The risks facing each subsidiary are likely to be different, so consider where the relevant expertise lies.

As the U.K. Government appears to be eager to show that the U.K. is serious about ESG and good business practices, it is essential that corporates have the requisite internal mechanisms in place to be able to take a proactive approach to developments in legislation in the U.K. and in other jurisdictions, as well as addressing regulatory requirements and enforcement concerns. Corporates that adapt to these changes will be better able to focus on achieving their commercial goals whilst exhibiting positive corporate citizenship.

This is all a question of balance and proportionality. As noted above, the risks of potential ESG-related litigation and investigations must be weighed against the potential positives that legal obligations to report on ESG activities might bring, such as the potential branding and consumer benefits of making your corporate stance on ESG issues known to potential clients and customers, and in making positive changes for the future. Although it is important to be alive to the possibility of ESG risks, we must not forget that ESG is, overall, a positive step for corporate responsibility both here and abroad.

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