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Connecting Climate Change and the Law

Report Discusses Potential Impact of ESG Claims on Directors and Officers Insurance

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In its 2023 report on trends in directors & officers (D&O) liability insurance policies, Allianz Global Corporate & Specialty highlighted risks associated with evolving ESG regulation and the increasing pace of climate change litigation. According to the report, "companies continue to see pressure around ESG issues as regulations are implemented around the world. Failure to disclose and lack of implementation could potentially lead to increased litigation for carriers as organizations navigate company policies to lessen their environmental impact surrounding greenhouse emissions and exposures." With respect to regulatory activity in particular, the report observed that while criminal fines and penalties are not covered in D&O policies, a policy can cover defense costs unless and until unlawful conduct has been established. The report also cited as risks for carriers increasing climate-focused litigation against companies and their boards, noting that "the cumulative number of climate change-related litigation cases has more than doubled since 2015." Particular types of cases cited included those asserting claims for greenwashing, failure to comply with international agreements such as the Paris Agreement, and claims based on companies making insufficient progress toward articulated sustainability targets. Ultimately, according to Allianz, "companies with strong ESG frameworks and governance will likely find insurers more willing to offer capacity."

Taking the Temperature: We have frequently reported on the types of ESG-related enforcement activity or litigation cited in the Allianz report. As we discussed earlier this year, for example, shareholders filed a derivative action against the board of directors of an oil major in the High Court of England and Wales alleging that the directors had allegedly breached their legal duties under the UK Companies Act by failing to

implement a transition strategy aligned with the Paris Agreement. The case was subsequently dismissed in May based on the court's finding that the plaintiff failed to establish a *prima facie* case against the Board for its management of climate risks. The High Court has granted a hearing that will allow ClientEarth to argue for reconsideration.

As another example, in 2021, two members of the Universities Superannuation Scheme (USS), the principal pension plan provided by UK higher education institutions, sued USS and its directors on the grounds, among others, that they failed to act in the best interests of beneficiaries by not divesting the plan of fossil fuel investments, despite fossil fuels allegedly performing worst as a category among all plan assets, and the fact that results of a USS survey indicated that the majority of members favored divestment. That suit was dismissed (and is currently on appeal) based on the court's conclusion that plaintiffs failed to allege that the directors committed a deliberate or dishonest breach of duty or improperly benefited themselves at the expense of USS by continuing to invest in fossil fuels. We have reported on numerous additional types of climate-related lawsuits and enforcement actions, all being commenced with greater frequency, including suits against oil majors to compel greater emissions reductions, suits by citizens against states to redress harm allegedly caused by failing to prevent the consequences of climate change, and consumer class or individual actions or regulatory activity related to alleged greenwashing.

The concerns raised by Allianz regarding the potential adverse impacts of climate litigation are consistent with the conclusions in a working paper from the London School of Economics and Political Science that looked at over 100 climate-related lawsuits between 2005 and 2021. The study found that the filing of a climate-based litigation claim or corresponding unfavorable court decision reduced the market capitalization of the defendant company by about 0.41%, on average. It is not surprising, then, that insurers are concerned that litigation against directors and officers has the potential to cause an adverse material impact. Likewise, we reported on the findings in Goldman Sachs Asset Management's 12th annual insurance survey, where just over one-third of insurance executives surveyed stated that climate change could also affect their ability to insure for extreme weather events. In addition, the industry has struggled to navigate the political issues spawned by ESG issues in the U.S., where Republican state and federal officials have raised antitrust and other challenges to insurers that participate in the UN-convened Net Zero Insurance Alliance or other industry climate groups, leading to a host of insurers (including Allianz) leaving the organization. The NZIA seeks to have members transition their insurance or investment portfolios to net-zero by 2050, in order to contribute to the implementation of the Paris Agreement.