RESPONDING TO INCREASING ESG RISKS: AN EMPIRICAL EXAMINATION OF THE CHANGING IN CORPORATE STRUCTURE FROM THE TOP S&P100 COMPANIES

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ABSTRACT

This Article demonstrates that the legal risk arising from potential ESG liability is increasing due to growing pressure from courts, legislators, and regulators. To illustrate the effects of this movement on ESG governance, this Article focuses on companies that make up the S&P100 to provide an in-depth analysis of what governance structures have been adopted by them and how they dialogue with the ESG legal risk companies are exposed to. It shows that S&P100 companies facing greater ESG legal risk are more likely to design separate corporate governance structures for ESG matters. The results demonstrate that S&P100 companies operating in sensitive industries (where ESG risk is at its peak) usually create specific ESG executive positions. In light of these findings, this Article argues that further initiatives that push companies closer to the level of legal risk currently faced by companies within sensitive industries may cause a spike in the adoption of specific ESG governance structures, as directors and officers would seek protection against potential legal claims brought by shareholders or stakeholders. This has implications as the SEC puts forth a new standard on climate-related disclosures, ideological battles are fought over state-level ESG legislation, and courts attempt to find the balance for reconciling the Caremark framework with concerns over ESG issues.

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I. INTRODUCTION

The interest of companies in ESG matters has been consistently growing in recent years. Factors such as millennial patterns of behavior, pressure from international organizations, and investors have certainly played a significant role in this process.[1] Nevertheless, it should be noted that the growing role of ESG in corporate governance is more deeply rooted in a philosophical discussion of what should be the main corporate purpose.[2] Since the early 2000s, the idea of "sustainable development" has earned a prominent position among powerful and influential institutions.[3] At that time, the acceptance of the "triple bottom line" as a preferred way of doing business gave rise to initiatives such as the UN Global

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[1] Michal Barzuza, Quinn Curtis & David H. Webber, *ESG and Private Ordering*, 1 U. CHI. L. REV. 1, 14 (2022) (arguing that the rise of ESG is traceable to an important shift in demand as corporate stakeholders and the millennial generation in particular are increasingly willing to act on preferences regarding environmental, social, and worker-welfare consequences of corporate actions).

[2] Scott J. Shackelford, Anjanette Raymond, Martin A. McCrory & Andrea Bonime-Blanc, *Cyber Silent Spring: Leveraging ESG+T Frameworks and Trustmarks to Better Inform Investors and Consumers About the Sustainability, Cybersecurity, and Privacy of Internet-Connected Devices*, 25 U. PA. J. BUS. L. 505, 515 (2023) (pointing out that by the early 1990s the CSR and corporate constituency statutes provided fertile ground for the establishment of a new wave of corporate thinking that later became known as the Trible Bottom Line (TBL); the authors emphasize that TBL consists of the 3Ps, i.e., people (social responsibility), planet (environmental responsibility) and profit (economic gains and losses)).

[3] *Id*. at 517.

Compact.[4] The discussions around the triple bottom line helped to shape what we know today as ESG in business.[5]

Particularly with regard to corporate governance, this process has been reinforced by increasing pressure from courts, legislators, and regulators. For instance, after the *Boeing* and *Marriott* cases, there has been a lot of discussion on whether managers can be held accountable for failing to address ESG concerns.[6] The possibility of extending *Caremark* duties to encompass oversight over environmental and social matters sheds light on increasing legal risk for directors and officers who chose not to prioritize ESG. That said, Delaware courts still demand proof that (1) the issue in discussion is critical, (2) red flags were ignored by directors or officers, as the case may be, and (3) the relevant company was directly harmed.

Moreover, a new rule proposed by the SEC (*The Enhancement and Standardization of Climate-Related Disclosures for Investors*) may also play a substantial role in raising the legal risk for companies.[7] The new SEC regulatory standards will likely require companies to disclose information about (1) the oversight and governance of climate-related risks by the company's board and management, (2) how climate-related risks identified by the company have had or are likely to have a material impact on its business and consolidated financial statements, which may manifest over the short, medium or long-term, (3) how any identified climate-related risks have affected or are likely to affect the company's strategy, business model, and outlook, (4) the impact of climate-related events and transitions activities on the line items of a company's consolidated financial statement and related expenditures, and disclosure of financial estimates and assumptions impacted by such climate-related events and transitions activities, (5) scope 1 and scope 2 GHC emissions metrics, separately disclosed, expressed both by disaggregated constituent greenhouse gases and in the aggregate, and in absolute and intensity terms, (6) scope 3 GHC emissions and intensity, if material, or if the company has set a GHG emission reduction target or goal that includes its Scope 3 emissions, and (7) the company's climate-related targets or goals, and transition plan, if any.[8]

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[4] *Id.*

[5] *Id.* (commenting that by the early 2000s powerful and influential institutions, firms, and businesses actively encouraged business initiatives and reporting revolving around TBL and related concepts).

[6] Roy Shapira, *Mission Critical ESG and the Scope of Director Oversight Duties*, 2022 COLUM. BUS. L. REV. 732, 801 (2022).

[7] *Id.* at 771 (explaining that when Yahoo and Equifax experienced cyberattacks, investors filed federal class actions claiming they were harmed by misleading statements or omissions).

[8] *See* 17 C.F.R. Part 200, 230, 232, 239, 249, and 279, *Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices*, at 39, SEC. & EXCH. COMM'N, https://www.sec.gov/rules/proposed/2022/ia-6034.pdf [https://perma.cc/Q4WX-CZB8]. (Statement about proposed climate related disclosure rules

If enacted, these rules will impact the ESG litigation risk faced by companies in two main ways. First, climate-related issues will more likely become "critical," meaning they will have more chances of satisfying *Caremark*'s criteria of critical issues that should be overseen by directors and officers.[9] This is mainly because the lack of oversight on these issues would have to be disclosed, and therefore could more tangibly cause reputational damages.[10] Second, misleading, or incomplete disclosure reports may give rise to securities class actions. And that means the new climate-related disclosure rules put forth by the SEC may impact not only the litigation risk of companies headquartered in the U.S. but also foreign companies with securities listed in U.S. capital markets.[11]

With regard to the legislative branch, apart from the aforementioned SEC legislation, there is no expectation that new federal laws will be enacted soon to expand the accountability of companies, their respective directors, and managers, concerning ESG matters. At the state level, the signs are mixed. Some states, such as California and New York, discuss stricter disclosure rules than those proposed by the SEC.[12] However, other states passed "anti-ESG" legislation aimed at discouraging or even prohibiting the adoption of ESG criteria in the investment process of players under government influence.[13]

Notwithstanding the state legislation movement, generally, the scenario portrays increased legal risk for companies, directors, and officers about ESG matters.[14] This helps to explain why companies are progressively willing to create

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according to GHC Protocol, cited by the SEC) ("[I]n its proposed new climate-related disclosure rules, "scope 1 emissions are direct GHG emissions that occur from sources owned or controlled by the company", scope 2 emissions are "those emissions primarily resulting from the generation of electricity purchased and consumed by the company", and scope 3 emissions are "all other indirect emissions not accounted for in scope 2 emissions.").

[9] *See* Shapira, *supra* note 6, at 777 (discussing if board-level failure to consider steps to mitigate climate-related risks give rise to a viable Caremark claim).

[10] *See* Shapira, *supra* note 6, at 778 (arguing that finance and accounting literature have long documented that reputational ramifications of corporate misbehavior toward the environment are negligible). Nevertheless, if SEC's climate-related rule is enacted, such kind of misbehavior would have to be reported to the market. It is also important to consider that GHG emissions would not be the only environmental matter covered by SEC's new rule.

[11] This is a significant risk for foreign issuers in American markets. For instance, in *In re Petrobras Securities Litigation*, United States District Judge Jed Rakoff approved a $3 billion settlement against Petrobras, the Brazilian oil company. *See* John C. Coffee Jr., *Global Settlements: Promise and Peril*, 22 U. Pa. J. Bus. L. 1, 5 (2019).

[12] *See infra* notes 63-67.

[13] *See infra* notes 68-71.

[14] *See, e.g.*, Corbin Hiar, *Fear of climate lawsuits spreads beyond fossil fuel industry*, E&E NEWS (Mar. 27, 2023, 6:56 AM), https://www.eenews.net/articles/fear-of-climate-lawsuits-spread-beyond-fossil-fuel-industry/ [https://perma.cc/NQN5-7SRN] (discussing that more than a dozen companies outside the oil industry have disclosed climate-chance-related legal risks to investors over the last three years and how that would indicate a growing sensitivity among businesses to the

ESG key positions.[15] Other data indicate that such positions are more or less likely to be empowered according to the industry in which companies operate.[16] And clearly, the industry's level of ESG risk is correlated to the likelihood of companies appointing an empowered Chief-Security Officer - CSO. For instance, oil and gas companies are keener to appoint an empowered CSO compared to entertainment and media companies or e-commerce platforms.[17]

With that in mind, this Article investigates if the enhanced pressure from investors, court precedents, legislation, and regulation – therefore increasing ESG litigation risks – will push companies to (1) embed ESG matters in traditional corporate governance structures such as the audit committee or the nominating & corporate governance committee, and/or (2) create corporate governance structures specifically designed to oversee ESG issues.

Part I of this Article addresses the rise of stakeholderism at the expense of shareholder primacy, briefly reviewing the theoretical foundations for ESG practices and governance.[18]

Part II analyzes the role of the regulatory front in the growing importance of ESG matters. Particularly, the SEC's recent proposal entitled *The Enhancement and Standardization of Climate-Related Disclosures for Investors* is discussed. This section explains the role of federal and state legislation on ESG matters. Later, it evaluates the courts' contribution to the abovementioned process. It discusses how the standards of action for directors got progressively stricter, as per *Caremark*, a paradigmatic decision in this period, responsible for changing the approach to board oversight duties, which has become much more proactive rather than reactive.[19] More recent decisions such as in *Marchand*, *Marriott*, *Boeing,* and *McDonald's* cases, made the *Caremark* framework as applied by Delaware courts severer. Moreover, shareholders may file class actions to discuss ESG matters. This is a trend started in other countries that may gain momentum in America, especially if the SEC enacts climate-related disclosure rules.

Part III presents empirical research in which the ESG governance model of the companies that make up the S&P100 is studied. First, it provides an analysis of

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prospect of facing legal challenges for releasing large amount of carbon dioxide into the atmosphere).

15 Federica Urso, *Number of company sustainability officers triples in 2021 - study*, REUTERS (May 4, 2022, 1:08PM), https://www.reuters.com/business/sustainable-business/number-company-sustainability-officers-triples-2021-study-2022-05-04/ [https://perma.cc/BXR4-TUMX].

16 PwC, *How empowered is your CSO?* https://www.pwc.com/gx/en/issues/c-suite-insights/the-leadership-agenda/how-empowered-is-your-cso.html [https://perma.cc/JPB4-BYXM].

17 *See id.* (finding that 42% of chief sustainability officers appointed in the oil & gas industry are "empowered" *versus* 26% in the entertainment & media sector and 14% in the e-platforms sector, respectively).

18 *See* Lucian A. Bebchuk & Roberto Tallarita, *The Perils and Questionable Promise of ESG-Based Compensation*, 48 J. OF CORP. L. 37, 43 (2016).

19 Shapira, *supra* note 6, at 744.

the profile of companies that are more sensitive to ESG reactions from the investors or benefit more from their consumers from a higher level of attention to ESG matters generally. This analysis is then juxtaposed with the subsequent empirical research, which focuses on answering two questions with regard to S&P100 companies: (1) do they embed ESG matters in traditional corporate governance structures such as the audit committee or the nominating & corporate governance committee? and/or (2) do they create corporate governance structures specifically designed to oversee ESG issues?

Finally, Part IV concludes. In light of the findings, this Article argues that growing ESG risks from diverse fronts will move companies closer to the level of litigation risks currently faced by firms operating in sensitive industries. That scenario may influence those companies to consider designing specific executive positions for overseeing ESG matters, as occurred in the case of S&P100 companies operating in sensitive industries.[20]

II. THE PHILOSOPHICAL DEBATE: SHAREHOLDER VS. STAKEHOLDER PRIMACY

The philosophical debate about what the ultimate goal of companies should be is a long-standing and balanced one.[21] In recent years, the pendulum has greatly tilted to the side of stakeholderism.[22] In short, stakeholderism is an approach that advocates corporations should seriously consider not only the interests of shareholders, but also those of workers, consumers, and communities.[23] Although the social aspects of corporations have origins tracing back to the ancient Roman Laws,[24] in contemporary America this idea has been closely associated with the notion of corporate social responsibility.[25]

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[20] For the purposes of this research, we considered executive ESG governance structures solely C-level positions expressly mentioned in companies' proxy statements or ESG reports.

[21] C. A. Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-First Century*, 51 U. KAN. L. REV. 77, 77 (2002) (stating that since the late nineteenth century, Americans have debated what duties large corporations might have to their workers, customers, neighbors and public at large).

[22] *See infra* note 47.

[23] Stephen M. Bainbridge, *Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship*, 82 CORNELL L. REV. 856, 877 (1997).

[24] Eric C. Chaffee, *The origins of corporate social responsibility*, 85 U. CIN. L. REV. 347, 351 (2017).

[25] *See* Antony Page & Robert A. Katz, *Is Social Enterprise the New Corporate Social Responsibility?*, 34 SEATTLE U. L. REV. 1351, 1351-52 (2011) (explaining the debate between the notion of corporate social responsibility *versus* shareholder theory has been around since the 1930s; arguing that CSR's perceived lack of progress since then created space for progressive corporate law, which according to the authors is the most muscular and structural iteration of CSR, in other words, a collection of proposals aimed at remaking corporate law to encourage processes and outcomes more beneficial to the interests of stakeholders).

A. Outlining the Corporate Purpose Debate: Main Ideas and Differences

Corporate social responsibility does not advocate that companies should not seek profits, but as a practical result of the theory there might be situations where corporate directors should serve the interests of non-shareholders and society at large rather than maximize shareholder value in the short-term.[26] Corporate social responsibility and stakeholderism are predecessors of ESG, in the sense that their proponents intensely discussed how corporate decisions should take into account third parties' interests (*i.e.*, stakeholders).[27]

A common feature of stakeholderism proponents is the (at least partial) rejection of Ronald Coase's classic responses to the reason for firms' existence.[28] Blair and Stout, for example, reject the idea that firms exist only as a way to mediate principal-agent problems or as a way to tackle problems associated with the coordination of productive activities since it would be too costly to write and enforce contracts (property rights approach).[29] The authors advocate for a *team production approach*, where more emphasis is put on the role of directors, who would constitute an independent hierarchy with fiduciary duties for the company itself, and only instrumentally for any of its participants.[30] Supporters of this model claim that "public corporation law encourages directors to serve the joint interests of *all* stakeholders who comprise the corporate "team" by generally insulating them from the demands of *any* stakeholder group, including shareholders."[31]

Shareholder value, in its turn, is conceptually quite simple. Its proponents hold that by seeking to increase profits, firms achieve their social purposes.[32] In a recent article, David H. Webber elaborates on that point by noting that even the most prominent articulators of stakeholderism recognized the "easy sound-bite explanation" of shareholder primacy as a great advantage.[33] According to Weber,

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26 See Maurico Andres Latapi Agudelo, Lara Johannsdottir & Brynhildur Davidsdottir, *A Literature Review of the History and Evolution of Corporate Social Responsibility,* 4 INT'L J. CORP. SOC. RESP. 1, 3 (2019) (explaining historically the idea is about balancing profit maximization with creating and maintaining the demands of clients, labor force and the community).

27 *See* Page & Katz, *supra* note 25, at 1357 (discussing the role of Adolf A. Berle, Jr. work as a "collateral antecedent of CSR advocates", as in 1954 Berle recognized Dodd's argument that corporate powers were held in trust for the community rather than for shareholders). Thus, the idea of taking into serious consideration third parties' interests (other than shareholders' interests) in corporate decisions has been vividly discussed in America for decades.

28 Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 257 (1999).

29 *Id.* at 258.

30 *Id.* at 289.

31 *Id.* at 288-89.

32 *Id.* at 289.

33 David H. Webber, *The Humanities Strike Back: (E)ESG and Justice Strine Challenge Gamer Shareholder Primacy*, 24 U. PA. J. BUS. L. 875, 876 n.3 (2022) (citing Lynn A. Stout, *The Problem*

the simplicity of shareholder primacy generates competition "with a single endpoint, basically a game, and that the exhilarating tournament that results, separate and apart from any ethical or instrumental justification, is an underestimated aspect of shareholder primacy's appeal." [34] Theoretically, shareholder primacy is closer to a utilitarian view, in the sense that it would be an ideal structure since its incentives meet the rationale of "greatest-good-for-the-greatest-number."[35]

Proponents of stakeholderism, however, are not satisfied with the argument simplicity or the "game appeal" of shareholder primacy. They are not content with the conclusion that firms should aim only to generate profit for their shareholders.[36] Rotman's opinion sums up well this kind of objection. According to him, "the fact that the shareholder primacy model is easier to fulfill says nothing about whether it is a more appropriate basis for assessing the role of corporate management in corporate governance."[37]

Despite the longevity and complexity of the corporate purpose debate, back in the 1990s and early 2000s only a minority of voices called for broader objectives for companies other than value maximization for their shareholders.[38] Even fewer voices understood that the American legislation was not based upon the premise that the company's directors should manage its business with the sole objective of generating value for shareholders. [39] It is as if the aura of the "end of history" that marked the geopolitics and world trade of that time also extended to corporate

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of Corporate Purpose, 2012 ISSUES GOV. STUD., 3 (2012), https://www.brookings.edu/wp-content/uploads/2016/06/Stout_Corporate-Issues.pdf)

[34] *Id.* at 876.

[35] Mark J. Roe, *The Shareholder Wealth Maximization Norm and Industrial Organization*, 149 U. PA. L. REV. 2063, 2065 (2001).

[36] Blair & Stout, *supra* note 28, at 287.

[37] Leonard I. Rotman, *Debunking the "End of History" Thesis for Corporate Law*, 33 B.C. INT'L & COMPAR. L. REV. 219, 269 (2010).

[38] R. Edward Freeman, *The Politics of Stakeholders Theory: Some Future Directions*, 4 BUS. ETHICS Q. 409, 411 (1994) (commenting on the principle that puts forward the idea that the primary function of the corporation is to enhance the economic well-being, or serve as a vehicle for the free choices of, the owners of the corporation; and noting that this principle is embodied in the law of the corporations which has historically directed managers and directors to direct the corporation's affairs in the interests of stockholders, using well-grounded business judgement).

[39] Blair & Stout, *supra* note 28, at 287-88 (elaborating that contemporary corporate scholars of the time were divided between those who understood that the role of directors was to maximize the interests of the corporation's shareholders and the "communitarians" or "progressives" who rejected shareholder primacy on normative grounds and argued that directors should run corporations with due regard for interests of other potential stakeholders; however, the authors comment that despite their disagreements, both understand that American corporate law follows the shareholder primacy model; The argument was built primarily on the existence of the derivative suits and the voting power of the shareholders).

law.[40] The shareholder-oriented model of governance was virtually unanimous by the 1990s.[41]

B. 2008 Financial Crisis and the Path toward ESG Corporate Measures

However, over time the shareholder primacy view was increasingly called into question. This converged with some blows suffered by the classic liberal economic philosophy after the global financial crisis of 2008 and more spotlight on the challenging ideas of authors who defied rational choice theory.[42] Specifically, in the realm of corporate law, an interesting challenge to the academic hegemony of shareholder primacy dates to 2010, when Rotman wrote the provocative *Debunking the "End of History" Thesis for Corporate Law.* In the Article, Rotman argues, among other things, that American jurisprudence is much less explicit about the support of the shareholder primacy's arguments than Hansmann and Kraakman suggested.[43] According to Rotman, corporate judgments, such as *Dodge v. Ford*, *Shlensky v. Wrigley*, and *Unocal v. Mesa Petroleum Corp.*, do not fit as comfortably well into the "end of corporate law" hypothesis.[44]

Thus, in the context of the beginning of the 2010s, stakeholder theory was gaining traction as a potential challenger to the hegemony of shareholder primacy. British author Andrew Keay published in 2010 the influential article *Stakeholder Theory in Corporate Law: Has It Got What It Takes?* Keay highlights an important difference in premise between stakeholder theory and shareholder primacy theory. The former relies on the professional and trustworthy performance of directors, while the latter is skeptical of the performance of directors, assuming they will act opportunistically or insufficiently.[45]

This entire movement culminated with the reversal of the situation in the last decades. As a clear demonstration of this, one could point to the fact that in 2019 the Business Roundtable announced the release of a new statement on

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[40] The "end of history" vibe was well captured in President William Jefferson Clinton's State of the Union Address on January 23, 1996. *See generally* Bill Clinton, Vice President of the United States, State of the Union Address (Jan. 23, 1996), in Nat. Arch. <https://perma.cc/L2K9-WPT7> (*e.g.*, when he comments more than once that the era of big government is over, and elaborates about America's favorable geopolitical moment affirming, among other things, that for the first time since the beginning of the nuclear age Russian missiles were not a pointed to America and North Korea had frozen its nuclear program).

[41] Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L. J. 439, 439 (2001).

[42] *See generally* Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism is Not an Oxymoron*, 70 U. CHI. L. REV. 1159, 1159-60 (2003).

[43] Rotman, *supra* note 37, at 229.

[44] *Id.* at 269.

[45] Andrew Keay, *Stakeholder Theory in Corporate Law: Has It Got What It Takes?* 9 RICH. J. GLOB. L. & BUS. 249, 298 (2010).

companies' purposes, in which 180 CEOs pledged to direct their companies for the benefit of all stakeholders – customers, employees, suppliers, communities, and shareholders.[46] According to the SEC Newgate ESG Monitor Report: (1) 78% of people believe that companies must be good citizens and consider their commitment to other people and the planet, and (2) 71% have the expectation they should launch ESG actions, no matter how small.[47]

There was some concern that an eventual paradigm shift to stakeholder capitalism in America could cause money to flee to jurisdictions where the risk-return ratio was better. In 2008, Kent Greenfield admitted this type of investor decision is always relative. However, Greenfield argued that given the power and stability of American markets, as well as the fact that European markets were more protective from the point of view of stakeholders, it would not make sense to expect capital flight.[48] Nowadays, this sort of observation seems to have aged well to European markets, but it may not make sense in relation to other competing emerging centers. If the demands of stakeholder capitalism are too high or applied by the courts in a dismantled way, one cannot rule out in advance the risk of capital and business exodus to (1) other regulated markets, or (2) even out of securities and capital markets law, as in the case of the offshore crypto economy.[49]

This authority opt-in or out problem has already been identified specifically with regard to SEC's regulatory framework. For George S. Georgiev, the current costs of a reporting public company are so high (*e.g.*, by providing public disclosure regularly, monitoring trends and risks affecting business, setting executive compensation programs, and establishing certain corporate governance arrangements) that it may be better for some firms to simply avoid the strictest regulatory scheme.[50] This would be possible because several exceptions for accessing popular savings privately can be exploited by competent lawyers and managers.[51] Private capital markets, Georgiev continues, are as abundant as public capital markets, so the status of a public company is irrelevant if the goal is simply to access capital.[52] Recently, John C. Coffee, Jr. made a similar point with regard specifically to ESG disclosures by defending that as ESG disclosure becomes more costly, we may see the ratio between public and private firms owning "dirty energy" assets shift significantly to private companies.[53] According to him, the

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[46] *See* Bebchuk & Tallarita, *supra* note 18, at 43 n.19.

[47] SEC NEWGATE, ESG MONITOR 2022, 1,12 (2022) https://www.secnewgate.com/upl/sec-newgate-esg-monitor-2022-uk.pdf [https://perma.cc/MG2M-KU9M].

[48] Kent Greenfield, *Corporate Ethics in a Devilish System*, 3 J. BUS. & TECH. L. 427, 434 (2008).

[49] For a discussion regarding regulatory arbitration *see*, *e.g.*, Tarullo, *infra* note 55.

[50] George S. Georgiev, *The Breakdown of the Public—Private Divide in Securities Law: Causes, Consequences, and Reforms*, 18 N.Y.U. J. L. &BUS. 221, 224 (2021).

[51] *Id.* at 224-225.

[52] *Id.* at 225.

[53] John C. Coffee, Jr., *Climate-Risk Disclosures and "Dirty Energy" Transfers: "Progress" Through Evasion*, THE CLS BLUE SKY BLOG (Jan. 25, 2022), https://clsbluesky.law.columbia.edu/20

problem in such case is that "dirty energy" would not decrease, but rather it would shift toward private owners.[54]

In a somewhat prophetic way, in 2014 Daniel K. Tarullo discussed the rise of macroprudential regulation after the 2008 global financial crisis. Tarullo expressed concerns, however, on the risk of financial activities' migration to zones outside of the regulatory perimeter.[55] Tarullo's logic was that the strengthening of capital, liquidity, and other regulations in the wake of the financial crisis would create significant opportunities for regulatory arbitrage, with firms simply opting out of the relevant framework.[56] This type of arbitrage has gained momentum in recent years, favored by various flexibilizations in the legislation that have expanded boundaries of private capital markets, while at the same time promoting an increase in observance costs for public companies.[57]

This Article does not purport to present an answer to the speculation of whether emerging ESG litigation risks for companies and their management may undermine the strength of American public securities markets *vis-à-vis* private markets or cause money to flee from America to other competing financial centers.[58] Notwithstanding, it is crucial to have this background in mind when interpreting the growing pressure on companies from several ends regarding ESG matters. It is reasonable to assume companies will carefully consider the costs and benefits of adapting their governance structures to greater ESG litigation risks or minimizing the litigation risk by moving away from public markets, or even the U.S. when that makes sense.

III. FRAMING AND VISIBILITY OF ESG LIABILITY/RISKS

There is currently no legislation in the United States that specifically mandates firms to make ESG disclosures. Similarly, no federal law mandates the adoption of any form of ESG governance or sets forth a stricter form of directors'

22/01/25/climate-risk-disclosures-and-dirty-energy-transfers-progress-through-evasion/ [https://perma.cc/FV5F-64EP].

[54] *Id.*

[55] Daniel K. Tarullo, Keynote Address at Yale Law School Conference on Challenges in Global Financial Services (Sept. 20, 2013), in *Macroprudential Regulation*, 31 YALE J. ON REG. 505, 520 (2014).

[56] *Id.* at 520-521.

[57] Georgiev, *supra* note 50, at 224, 240 (noting that notwithstanding the formal distinction between public and private companies, capital, and markets, the boundaries of these two legal realms are blurred; adding that public capital flows to private companies, private capital is increasingly abundant, and firms can effectively escape the costly public company status, which is both more costly and much less essential to firm success than ever)

[58] This sort of discussion is usual particularly when we debate the preservation of Delaware's preeminent position as an international supplier of corporation law. *See*, *e.g.*, Ian J. Murray, *Hughes v. Hu: Territorial Adjustments in Determining Caremark Liability for Foreign-based Delaware Incorporated Companies*, 80 MD. L. REV. 1247, 1248 (2021).

and officers' liability for ESG matters. The enaction of such legislation, however, might be just one climate or social crisis away if we pay attention to recent legislative history.[59] For instance, back in 2001 when the Enron crisis happened, the scandal was widely used to justify a series of reforms in corporate and securities law.[60] Senator Paul Sarbanes, commenting on what inspired him to co-author the Sarbanes-Oxley Act, expressly mentioned the Enron case as a sign that there would be "broad, deep, systemic and structural" problems in markets.[61] In 2002, a Senate Committee on Government Affairs report stated the legislator approved the Sarbanes-Oxley Act of 2002 in the wake of the Enron scandal. The legislator included the auditor independence provisions as well as the requirement for accounting firms' lead audit partners to rotate every five years.[62] Thus, one should not rule out the possibility of Congress taking bolder action if the winds start blowing in another direction. A crisis often justifies stricter corporate legislation.

The discussion around everything involving ESG issues in the United States is marked by an ideological divide that is not necessarily as drastic in other countries. Consequently, states often adopt conflicting positions on ESG matters. For instance, the State of Minnesota recently passed a law that aims to get the state to be carbon-free from the year 2040 onwards.[63] In the same vein, legislators from the State of California recently introduced two bills on ESG-related matters: the California Climate Corporate Data Accountability Act (SB 253) and the Climate-Related Financial Risk Act (SB 261). SB 253 would require US-based organizations with total revenues over $1,000,000,000 that do business in California to publicly disclose their greenhouse gas emissions by the GHG Protocol.[64] SB 261, on the other hand, would require large corporations to prepare and submit an annual climate-related financial risk report, publicly disclosing their

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[59] *See* Saul Elbein, *5 things to know about the growing fight over ESG*, THE HILL (Jul. 13, 2023, 2:58 PM). https://thehill.com/policy/equilibrium-sustainability/4095977-5-things-to-know-about-the-growing-fight-over-esg/ [https://perma.cc/2URA-KQPF] (elaborating on the political environment with regard to proposals regarding climate-related disclosures). Hence, despite the point this Article makes here, in the present days enthusiastic and loud political forces in America do not view the ESG agenda as urgent or even necessary.

[60] Nance Lucas, *An interview with United States Senator Paul S. Sarbanes*, 11 J. OF LEADERSHIP. & ORG. STUD. 3, 3-4 (2004).

[61] *Id.*

[62] STAFF OF THE S. COMM. ON GOV'T AFF., REP. ON FINANCIAL OVERSIGHT OF ENRON: THE SEC AND PRIVATE-SECTOR WATCHDOGS (Oct. 7, 2002), https://www.govinfo.gov/content/pkg/CPRT-107SPRT82147/html/CPRT-107SPRT82147.htm [https://perma.cc/CAJ9-6KF8].

[63] Minn. Dep't of Com., *Governor Walz Signs Bill Moving Minnesota to 100 Percent Clean Energy by 2040* (Feb 7, 2023), https://mn.gov/commerce/news/?id=17-563384 [https://perma.cc/Q5MP-CNUL].

[64] S.B. 253, 2023 Leg., 2023-2024 Regular Sess. (Ca. 2023); *California SB 253 and SB 261: What Businesses Need to Know*, PERSEFONI (Apr. 21, 2023), https://www.persefoni.com/learn/california-sb253-sb261 [https://perma.cc/4K22-DF2T].

climate-related financial risks and the measures they are taking to mitigate these risks.[65] New York State Bill A 4123 would require businesses with over $500 million in revenue to report to the Air Resources Board the company's climate-related financial risks and measures to address such risks.[66] In addition, New York State Bill S 897 would require businesses with over $1 billion in revenue to report emissions annually to an emissions registry and to independently verify the disclosures.[67]

In other states, however, "anti-ESG" laws have either been passed or are currently in the process of discussions.[68] For instance, Florida recently passed an "anti-ESG" law barring state officials from investing public money to promote ESG goals and prohibiting ESG bond sales in the state.[69] Additionally, Idaho's House of Representatives recently passed three bills that, among other things: (1) would prevent state and local governments from signing contracts with companies that refuse to do business with companies because of the production, sale, or distribution of weapons or production of fossil fuels, (2) prevent banks and credit unions classified as public depositories from boycotting companies for arms manufacturing or fossil fuel production, and (3) would provide that state contracts could not be signed or denied based on ESG standards. In that respect, it is relevant to mention the existence of a political alliance with almost 20 states to "push back against the ESG agenda."[70] Despite the importance of the pushback to ESG in the political arena, the path forward is not clear, as "the vast majority of anti-ESG bills failed to progress through legislative chambers, including in ten states fully controlled by Republicans."[71]

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65 S.B. 261, 2023 Leg., 2023-2024 Regular Sess. (Ca. 2023); *California SB 253 and SB 261: What Businesses Need to Know*, PERSEFONI (Apr. 21, 2023), https://www.persefoni.com/learn/california-sb253-sb261 [https://perma.cc/4K22-DF2T].

66 Leah Malone, Emily Holland & Carolyn Houston, *ESG Battlegrounds: How the States Are Shaping the Regulatory Landscape in the U.S.,* n.33 (March 11, 2023), HARVARD L. SCH. F. ON CORP. GOVERNANCE, https://corpgov.law.harvard.edu/2023/03/11/esg-battlegrounds-how-the-states-are-shaping-the-regulatory-landscape-in-the-u-s/ [https://perma.cc/7SR8-NDUA].

67 *Id.*

68 Marc S. Gerber, Greg Norman & Simon Toms, *ESG Mid-Year Review: Key Trends in 2023 Thus Far,* HARVARD L. SCH. F. ON CORP. GOVERNANCE (July 31, 2023), https://corpgov.law.harvard.edu/2023/07/31/esg-mid-year-review-key-trends-in-2023-thus-far/ [https://perma.cc/8V4Q-KGBG] (stating approximately 100 anti-ESG bills have been introduced in state legislatures around the country).

69 Isla Binnie & Ross Kerber, *DeSantis signs sweeping anti-ESG legislation in Florida*, REUTERS (May 3, 2023, 12:51 AM), https://www.reuters.com/business/sustainable-business/desantis-signs-sweeping-anti-esg-legislation-florida-2023-05-02/ [https://perma.cc/G9E9-8W8K].

70 News Release, Staff of Fla. Governor Ron DeSantis, *Governor Ron DeSantis Leads Alliance of 18 States to Fight Against Biden's ESG Financial Fraud*, (Mar. 16, 2023), https://www.flgov.com/2023/03/16/governor-ron-desantis-leads-alliance-of-18-states-to-fight-against-bidens-esg-financial-fraud/ [https://perma.cc/Z9Y8-2UNN].

71 *See 2023 Statehouse Report Anti-ESG State Legislation Tracker & Analysis*, PLEIADES STRATEGY https://www.pleiadesstrategy.com/state-house-report-bill-tracker-republican-anti-esg-

The ideological battle at the state level is one factor that increases companies' ESG legal risk.[72] To illustrate this point, it may be that directors are forced to ponder the implications of conflicting risks: for example, (1) the litigation risk for lack of oversight over diversity, equity, and inclusion (DEI) matters, should any harmful event occur, and (2) state legislation that may be hostile to the adoption of programs until now commonly adopted by DEI departments.[73] Put differently, the lack of cohesion around the issue increases the risk of litigation on this front, and forces companies to walk a tightrope.[74]

The perception is that lawmakers and regulators in the United States have had a harder time finding consensus around ESG issues than in other comparable jurisdictions, such as the UK or the European Union.[75] Notwithstanding such perception, investors already have at their disposal the important channel of class actions to obtain compensation in the face of companies presenting misstatements or omissions in market disclosures. This risk even affects foreign companies publicly listed in the United States, as they are subject to federal security laws.

There is also clearly growing pressure to provide investors with more information and quality material on ESG issues. One display of that is *The Enhancement and Standardization of Climate-Related Disclosures for Investors*, proposed by the SEC in 2022. The SEC's proposed rules would amend its

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attacks-on-freedom-to-invest-responsibly-earns-business-labor-and-environmental-opposition [https://perma.cc/VNG3-UE3T] (last visited Aug. 5, 2023). *See* also, *GDP by State*, BUREAU OF ECON. ANALYSIS, https://www.bea.gov/data/gdp/gdp-state [https://perma.cc/3MEF-ZMAE].

[72] Elbein, *supra* note 59 (noting that for many important Wall Street banks, the ring-wing attack on ESG became severe enough to constitute a risk on its own). *See* Patrick Temple-West & Brooke Masters, *Wall Street titans confront ESG backlash as new financial risk*, FIN. TIMES (Mar. 1, 2023), https://www.ft.com/content/f5fe15f8-3703-4df9-b203-b5d1dd01e3bc [https://perma.cc/CH36CJ4E].

[73] *See* Emily A. Bushaw & Elizabeth Gardner, *State Anti-DEI Initiatives Explained*, PERKINS COIE (Apr. 25, 2023), https://www.perkinscoie.com/en/news-insights/state-anti-dei-initiatives-explained.html [https://perma.cc/VP3S-4H8X] (arguing that although State Anti-DEI efforts are focused on state agencies and higher education institutions, private employers should take note as these efforts as broader attacks on ESG initiatives).

[74] *See, e.g.*, *Students for Fair Admissions, Inc. v. President & Fellows of Harvard Coll.*, 600 U. S. 181 (2023) (Thomas, J., concurring) ("The Constitution's colorblind rule reflects one of the core principles upon which our Nation was founded: that all men are created equal."); For an opposite view, *see*, *e.g.*, *Students for Fair Admissions, Inc. v. President & Fellows of Harvard Coll.*, 600 U. S. (2023) (Sotomayor, J., dissenting) ("The Equal Protection Clause of the Fourteenth Amendment enshrines a guarantee of racial equality. The Court long ago concluded that this guarantee can be enforced through race-conscious means in a society that is not, and has never been, colorblind"). *See also* Lauren Weber, *Companies Expect New Challenges to Diversity Policies After Court Ruling*, THE WALL ST. J. (June 30, 2023, 5:30 AM), https://www.wsj.com/articles/companiesexpectnew-challenges-todiversitypolicies-after-court-ruling-4bf48c1d.

[75] Malone, Holland & Houston, *supra* note 66.

regulations of the Securities Act of 1933 and Securities Exchange Act of 1934[76] by requiring registrants to provide the market with certain weather-related information in registration statements and annual reports.

A. Disclosure Standards and Director's Expertise Rules for Investors´ Protection

Under the proposed rule, the registrant must make available a range of information about the board's governance items, if applicable. The first item, according to SEC's original proposal, was supposed to identify any board members or board committees responsible for oversight of climate-related risks. The responsible board committee may be an existing committee, such as the audit committee or risk committee, or a separate committee to focus on climate-related risks.[77]

The next proposed item would require the registrant to disclose any expertise of climate-related risks among the company's board of directors. Should any directors have climate-related expertise, companies are then obligated to describe in detail the extent of the board member's knowledge.[78] The proposed rule would still require: (1) a description of the processes and frequency at which the board or board committees discuss climate-related risks, (2) how the board is informed of climate-related risks and how often the board lists such risks, (3) discretion as to whether and how the board or board committees consider climate-related risks as part of the company's business strategy, risk management, and financial oversight, and (4) disclosure about whether and how the board sets climate-related targets or goals and how it oversees progress against those targets or goals, such as establishing any interim targets or goals.[79]

The SEC's purpose with these requirements would be to assist investors in (1) understanding whether and how the board or board committees understand climate-related risks, when reviewing and guiding business strategies and action plans, when establishing and monitoring the implementation of risk management policies and performance objectives, when reviewing and approving annual budgets, and when overseeing large expenditures, acquisitions, and divestitures, and (2) assessing whether management has adequately implemented processes to identify, assess, and manage climate-related risks.

On another front, the SEC proposed in May 2022 amendments to rules and reporting forms to promote consistent, comparable, and reliable information to

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[76] The Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 Fed. Reg. 21334 (proposed May 12, 2022) (proposing to amend Regulations S-K and S-X, requiring climate-related disclosures).

[77] *Id*. at 21359.

[78] *Id.*

[79] *Id.* at 21359-60.

investors concerning the incorporation by funds and advisers of ESG factors.[80] The SEC's proposed changes in this regard would apply only to a few registered investment advisers, advisers exempt from registration, registered investment companies, and business development companies.[81] The proposed rule, if enacted, would require "additional specific disclosure requirements regarding ESG strategies to investors in fund registration statements, the management discussion of fund performance in fund annual reports, and adviser brochures."[82] The SEC's proposed rule separates investment funds into three main categories, *i.e.*, integrated funds, impact investing, and ESG-focused funds. The latter would include "funds that apply inclusionary or exclusionary screens, funds that focus on ESG-related engagement with the issuers in which they invest, and funds that seek to achieve a particular ESG impact."[83]

As with virtually any discussion involving ESG matters, the SEC's proposed rules aiming to enhance disclosures by investment advisers and investment companies received mixed reactions from the public. For instance, one asset manager commented that the division of funds into three categories would be problematic, chiefly because they do not reflect how the industry takes ESG considerations into investment and stewardship decision-making.[84] Other commentators criticized the category of "integration funds" on the basis that the category would be broad enough to permit almost any approach to ESG or sustainability in investment management and thus would open the door for greenwashing.[85] However, on the other hand, another market participant praised the SEC's proposed approach of dividing funds into categories and then applying enhanced disclosure requirements to funds that fit any of these categories.[86]

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[80] Press Release, U.S. SEC & Exch. Comm'n., SEC Proposes to Enhance Disclosures by Certain Investment Advisers and Investment Companies About ESG Investment Practices (Aug. 16, 2022).

[81] *Id.*

[82] 17 C.F.R. Part 200, 230, 232, 239, 249, 274, and 279, Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, U.S. SEC. & EXCH. COMM'N 1, 20 (May 25, 2022), https://www.sec.gov/rules/proposed/2022/ia-6034.pdf [https://perma.cc/Q4WX-CZB8].

[83] *Id.* at 24.

[84] *See* E-mail from Sarah Adams, Chief Sustainability Officer, Vert Asset Mgmt. LLC, to Vanessa A. Countryman, Sec'y, U.S. Sec. & Exch. Comm'n (Aug. 29, 2022). https://www.sec.gov/comments/s7-17-22/s71722-20137751-308097.pdf [https://perma.cc/3VM9-JFSC].

[85] *See, e.g.,* Letter from Joseph F. Keefe, President, Impax Asset Mgmt., & Julie Fox Gorte, Senior Vice President for Sustainable Investing, Impax Asset Mgmt., to Vanessa A. Countryman, Sec'y, U.S. Sec. & Exch. Comm'n (Aug. 16, 2022) (https://www.sec.gov/comments/s7-17-22/s71722-20138305-308363.pdf) [https://perma.cc/5ALD-E24X].

[86] *See* Letter from Jennifer L.C. Wu, Managing Dir., Glob. Head of Sustainable Investing, J.P. Morgan Asset Mgmt., to Vanessa Countryman, Sec'y, U.S. Sec. & Exch. Comm'n (Aug. 16, 2022), (https://www.sec.gov/comments/s7-17-22/s71722-20136187-307162.pdf) [https://perma.cc/6EXG-XKYA].

B. The Role of Courts in Raising Companies' ESG Litigation Risks

Abstaining from addressing ESG matters, or not having in place a proper governance structure can generate many risks for companies and directors. Shareholders who feel harmed have two main legal actions at their disposal, *i.e.*, derivative actions and class actions. Derivative actions are filed for the benefit of the company and usually are based upon a failure in the oversight duties of directors and officers over critical subjects. Shareholders may also sue alleging damages caused by misstatements or omissions in corporate disclosures.[87] In recent times, ESG litigation risks for companies, directors, and officers increased significantly on both of these fronts. The *Caremark* framework, applicable to derivative actions got stricter, as courts are increasingly willing to recognize non-legal matters as critical issues that must be overseen by directors (and officers). The risk of class actions has also been increasing over the past few years.

1. The Risk of Derivative Actions: Rising Patterns or Oversight Duties

Caremark was a paradigmatic decision in the 1990s, that is capable of changing the approach to board oversight duties. *Caremark* created incentives for directors to act more proactively rather than reactively.[88] Shapira summarizes the change this precedent represented by commenting that "prior to *Caremark*, directors could assume that everything was fine until someone in the company flagged a problem to them."[89] In other words, *Caremark* clarified that directors' oversight duty can only be satisfied if directors actively monitor information and reporting processes they have implemented.[90] In that context, Delaware courts see board committees as an important governance structure for fulfilling boards' oversight and accountability functions.[91]

Caremark was responsible for introducing a system in which problems have to be reported to the board. The board on its turn has to react to red flags that are raised.[92] The standard for using *Caremark*, however, is quite high. Based on

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[87] *See* Marco Dell'Erba & Michele Doronzo, *Sustainability Gatekeepers: ESG Ratings and Data Providers*, 25 U. PA. J. BUS. L. 355, 383-84 (2023) (indicating that ESG litigation is an even broader category that encompasses cases such as litigating ESG ratings providers for poor evaluation of companies or lack of transparency in ESG methodologies; mentioning the example of Isra Vision, a German processing company, that sued the North American proxy advisory firm Institutional Shareholder Services who gave Isra a poor ESG rating, aiming to obtain an injunction to block the publication of the rating).

[88] Shapira, *supra* note 6, at 744.

[89] *Id.*

[90] Lisa M. Fairfax, *Board Committee Charters and ESG Accountability*, 12 HARV. BUS. L. REV. 371, 387 (2022).

[91] *Id.* at 388.

[92] Shapira, *supra* note 6, at 744-45.

the framework, plaintiffs must necessarily prove that the directors knew they were breaking their duties.[93] Negligence, or even gross negligence would not be sufficient to establish liability on the part of the directors, and judges can only find that the duty of oversight has failed if the plaintiffs demonstrate bad faith on the part of the directors.[94]

Some legal scholars recognize the role of the Delaware Courts in enforcing the oversight duty of directors through the *Caremark* framework.[95] Shapira synthesizes the framework and discusses which ESG risks are critical or not, regardless of whether they are legal or reputational risks.[96] The author cites the 2009 *Citigroup* and 2011 *Goldman Sachs* decisions, where there was a distinction between legal compliance risk oversight and business risk oversight.[97] Shapira points out, however, that this understanding has been overcome in more recent decisions, starting with *Marchand*.[98]

In *Marchand*, Shapira argues, it is a possible reading to conclude this is a case about oversight of critical reputational risks.[99] Here, the Delaware Court held that for an ice cream-selling company, product quality failures can be detrimental to operations, regardless of whether the company meets certain minimum requirements or not.[100] The Court specifically concluded the absence of a board committee charged with monitoring food safety was a fair allegation of dispositive deficiency.[101] In other words, the court "highlighted the link between effective board oversight and board committees."[102]

Later, in September 2021, the *Boeing* court confirmed a tendency of increased willingness to apply stricter board oversight examination, via the "mission critical designation."[103] It also corroborated an enhanced readiness to grant outside shareholders access to internal documents for investigation of potential failure of oversight claims.[104] In *Boeing*, shareholders challenged the company's directors and officers by arguing that they were not sufficiently

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93 *Id.* at 745 ("*Caremark* called on judges to show restraint, and to impose liability only when it is clear that directors *knew* they were breaching their duties.").
94 *Id*. at 745.
95 *Id.* at 736 (emphasizing the increasing willingness of Delaware courts to apply heightened scrutiny of board oversight efforts and "grant outside shareholders access to internal company documents in order to investigate failure-of-oversight claims").
96 *Id.* at 750.
97 *Id.* at 751-52. *See In re* Citigroup Inc. S'holder Derivative Litig., 964 A.2d 106, 131 (Del. Ch. 2009). *See In re* Goldman Sachs Group, Inc. S'holder Litig., Civ. No. 5215–VCG, 2011 WL 4826104, at *20–*24 (Del. Ch. Oct. 12, 2011).
98 Shapira, *supra* note 6, at 752-53.
99 *Id.* at 753.
100 *Id.*
101 *Marchand v. Barnhill*, 212 A.3d 805, 822–23 (Del. 2019).
102 Fairfax, *supra* note 90, at 389.
103 Shapira, s*upra* note 6, at 748.
104 *Id.* at 749.

attentive to airplane safety before the first accident and were irresponsive to red flags after the first crash.[105] In the October 2021 *Marriott* case, the court further broadened the scope of the *Caremark* framework, admitting the possibility of a legal claim based on the oversight analysis of nonlegal risks, although the outcome of the case was favorable to the defendant.[106]

In a December 2022 article, Douglas P. Baumstei and others explain that since *Marchand,* the Delaware courts are more willing to allow *Caremark* claims to go ahead with the motion to dismiss phase if there is plausibility.[107] Moreover, the authors claim the new Climate-Related Disclosures rules proposed by SEC on March 21, 2022, if approved, could foster ESG-related *Caremark* claims.[108] Similarly, Lipton and other authors wrote in a March 2023 article that addressing ESG factors and other risks is consistent with the duty of care obligation and the board's obligation under *Caremark* to implement and monitor systems to recognize material risks and address risks already identified.[109]

The Court of Chancellor underscored in another recent case the usefulness of risk management and compliance structures in dismissing claims for breach of fiduciary duties against NiSource's board in the *City of Detroit Police and Retirement Sys. v. Hamrock*.[110] The Court specifically mentioned the board had several committees tasked with monitoring and evaluating strategic, compliance, operational, and financial risks, including the Audit Committee, Risk Management Committee, and the Environmental, Safety, and Sustainability (ES&S) Committee.[111]

The possibility of extending *Caremark* to ESG matters is not unscathed from backlash. Bainbridge is one of the voices who has criticized this possibility, warning that "such an extension would be highly undesirable," since "Caremark was wrong from the outset."[112] Nevertheless, *de lege ferenda* criticisms do not

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[105] *Id.* at 748.
[106] *Id.* at 756.
[107] Douglas P. Baumstein, Jacob Hupart, Jonathan Kravetz & Ellen Shapiro, *Caremark Liability Following the SEC's New ESG Reporting Requirements*, JD SUPRA (Dec. 19, 2022), https://www.jdsupra.com/legalnews/caremark-liability-following-the-sec-s-3622547 [https://perma.cc/W2BY-J563].
[108] *Id.*
[109] Martin Lipton, Watchell Lipton Rosen & Katz, *On the Debate Regarding ESG, Stakeholder Governance, and Corporate Purpose*, HARVARD L. SCH. F. ON CORP. GOVERNANCE (March 14, 2023), https://corpgov.law.harvard.edu/2023/03/14/on-the-debate-regarding-esg-stakeholder-governance-and-corporate-purpose [https://perma.cc/6HQV-Z36N].
[110] Martin Lipton et al, *Risk Management and the Board of Directors*, WACHTELL, LIPTON, ROSEN & KATZ1, 6 (Sep.2022), https://www.wlrk.com/webdocs/wlrknew/ClientMemos/WLRK/WLRK.28180.22.pdf [https://perma.cc/44YV-J8WY].
[111] *City of Detroit Police & Fire Ret. Sys. v. Hamrock*, C. A. 2021-0370-KSJM 1, 2 (Del. Ch. Jun. 30, 2022).
[112] Stephen Mark Bainbridge, *Don't Compound the Caremark Mistake by Extending it to ESG Oversight*, BUS. LAW. (Sep. 2021) at 6, https://ssrn.com/abstract=3899528 [https://perma.cc/V7KP-

change the fact that the *Caremark* framework has been extended by Delaware courts' recent cases to include the oversight of non-reputational risks and could reach ESG matters more clearly in the future.[113]

It is also worth mentioning this discussion is not restricted to Delaware courts but spreads to other states. For instance, in May 2023, the California Second District Court of Appeal applied *Caremark* for a derivative lawsuit against the officers of Sempra Energy and officers and directors of Southern California Gas Company (SoCalGas), a subsidiary of Sempra Energy.[114] The demand discussed a natural gas leak in the Aliso Canyon Natural Gas Storage facility.[115] In this particular case, the Court of Appeal held that the California Corporations Code standards for exculpation are consistent with *Caremark*.[116] However, in a split decision the California court decisively disagreed with the plaintiffs.[117] The court concluded that board meeting minutes demonstrated the existence of some level of board oversight. According to the decision, that was sufficient for not penalizing the defendants under the *Caremark* framework and relevant legislation.[118] The California court's decision underscores the importance of board-level committees responsible for overseeing and monitoring business risks. In this specific case, Sempra had set up a Board-level Environmental, Health, Safety, and Technology Committee in monitoring safety matters, including storage and safety. The periodic discussions held by such committees and the board were important in getting the case decided in favor of the defendants.

Recently, the Delaware Court of Chancery expanded *Caremark*'s potential liability to officers for failure to supervise.[119] The case relates to several sexual harassment issues that faced McDonald's in 2015 and an alleged failure to address

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636N] ("Such an extension would be highly undesirable. First, Caremark was wrong from the outset. In the original Caremark decision, the unique procedural posture of the case, which was such that it would not be appealed, gave Chancellor Allen an opportunity to write "an opinion filled almost entirely with dicta" that "drastically expanded directors' oversight liability." In doing so, Allen misinterpreted binding Delaware Supreme Court precedent and ignored the important policy justifications underlying that precedent") (quoting Todd Haugh, Caremark's Behavioral Legacy, 90 TEMP. L. REV. 611, 618 (2018)).

[113] Shapira, *supra* note 6, at 756.

[114] Keith Paul Bishop, *Court of Appeal Applies Caremark/Marchand to Directors of a California Corporation But the Result May Surprise You*, N'TL L. REV. (Jun. 6, 2023), https://www.natlawreview.com/article/court-appeal-applies-caremarkmarchand-to-directors-california-corporation-result-may [https://perma.cc/DZB6-49FT].

[115] *Id.*

[116] *Id.*

[117] *Id.*

[118] *Id.*

[119] *Delaware Court of Chancery holds for the first time that duty of oversight applies to officers*, DAVIS POLK (Feb. 07, 2023), https://www.davispolk.com/insights/client-update/delaware-court-chancery-holds-first-time-duty-oversight-applies-officers [https://perma.cc/2QRW-YZ47].

those issues at the company.[120] Vice Chancellor Travis Laster of Delaware's Court of Chancery rejected a first motion to dismiss filed by McDonald's then-Global People Officer, expressly holding for the first time that officers own the same corporate oversight duties as directors.[121] As a result, officers must: (1) make a good-faith effort to establish information systems, and (2) do not ignore red flags.[122] The ruling recognized there are differences regarding the oversight expected from directors and officers.[123] Directors normally have company-wide oversight portfolios, while officers will generally have a constrained area of authority. Nevertheless, the court also emphasized that if a red flag is sufficiently prominent, even if an officer from a different area should not turn a blind eye. Rather, the officer is expected to report the issue upward.[124]

This environment results in the need for both directors and officers to develop policies to protect themselves from the risk of being targeted by thse *Caremark* framework. In this context, courts may want to know, for example: (1) whether the board receives information and regularly discusses risks from the company, (2) whether processes are raising yellow and red flags for officers and the board, and (3) whether there are policies and procedures in place to substantiate the board's good-faith efforts to implement and oversee systems and policies to address critical risks to the company.[125]

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[120] *Id.*

[121] Deborah Birnbach, Caroline Bullerjahn, Jennifer Burns Luz & Adam Slutsky Goodwin, *McDonald's Part Two: Delaware Court of Chancery Dismisses Caremark Claims Against Directors Arising From Sexual Harassment Issues*, JD SUPRA (Mar. 8, 2023), https://www.jdsupra.com/legalnews/mcdonaldsparttwodelawarecourtof1255817/ [https://perma.cc/MW3Z-AGX7].

[122] *In re* McDonald's Corporation Derivative Litig., C.A. No. 2021-0324-JTL, at 22-24 (Del. Ch., Jan. 23, 2023).

[123] *Id.* at 36 ("The role of the board in providing oversight for officers also illustrates how a case could result in different outcomes as to different actors. While it seems likely that if a court found a board liable for breach of an oversight obligation, then the officers with responsibility for that area also would be liable, the converse is not true. A board could direct an officer to establish an information system to cover their area, or a board could reasonably believe that an officer had established one. If the officer failed to fulfill those responsibilities, and the board did not consciously act in bad faith by not following up, then the directors would be in a position to hold the officer accountable without facing oversight liability themselves").

[124] *Id.* at 42 ("For similar reasons, officers generally only will be responsible for addressing or reporting red flags within their areas of responsibility, although one can imagine possible exceptions. If a red flag is sufficiently prominent, for example, then any officer might have a duty to report upward about it.").

[125] Shaun Mathew & Daniel Wolf, *Ten Questions for Board Chairs Preparing for Activism and Hostile Takeovers*, HARVARD L. SCH. F. ON CORP. GOVERNANCE (June 19, 2023) https://corpgov.law.harvard.edu/2023/06/19/ten-questions-for-board-chairs-preparing-for-activism-and-hostile-takeovers/ [https://perma.cc/D9RX-SR3U] ("While there is no one-size-fits all approach and each company (and each board) is different, the following questions may be helpful to consider in making sure the board is prepared. […] Are there policies designed to protect directors (and officers) from potential Caremark claims? Is the board regularly briefed on enterprise risks and is there a process for internal and external yellow and red flags (including from whistleblowers) to be elevated to

Therefore, despite the unavoidability of the risk of being targeted with derivative actions, directors and officers have at their disposal a toolkit with several governance measures that can be employed. Those measures can reduce the chance of suffering defeat if a shareholder brings forward a *Caremark* claim.

2. The Risk of Class Actions: failures in corporate´s disclosure duties

Companies may face class actions that are securities class actions moved by unsatisfied shareholders, or they may also be defendants in legal claims brought by harmed stakeholders, such as consumers. As this Article is focused on ESG governance issues, securities class actions are the most relevant.

This sort of class action may be filed mainly based on misstatements or omissions in companies' disclosure documents concerning ESG matters. As mentioned earlier, even though the new proposed SEC rules are not yet in force, companies have been increasingly wary of this type of lawsuit filed against them.[126] This helps to explain why companies are beginning to specify ESG risks in the documents they make available to the market.[127]

Just to mention an example of this, ClientEarth, on behalf of Shell's activist shareholders, recently brought a class action claiming the company's directors are personably liable over their supposedly flawed strategy to meet climate targets.[128] The lawsuit was filed at the high court in England.[129] It is worth mentioning that Shell had previously announced that its energy transition strategy was "to become a net-zero emissions energy business by 2050."[130]

Here, it is important to note that, if enacted, the SEC's new rules on climate-related disclosures would increase companies' risk of being sued with securities class actions. For example, if any inaccuracies in the information provided in mandatory disclosures later come to be discovered, say, by an independent investigation by an ESG rating agency, there could be reputational damage to the company. Elaborating on this hypothesis, it is reasonable to imagine

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senior management and ultimately the board? Have policies and procedures been implemented to develop a record of the board's good faith efforts to implement and monitor oversight systems and develop policies to escalate risks that are mission critical to the company?").

[126] Hiar, *supra* note 14 ("Thirty-two companies have disclosed risks related to "climate litigation" or "climate change-related litigation" since 2020, according to an E&E News review of SEC filings. Half are fossil fuel companies, such as European oil and gas producers Shell PLC and Equinor ASA, […]").

[127] *Id.*

[128] Damian Carrington, *Shell Directors Personally Sued Over 'Flawed' Climate Strategy*, THE GUARDIAN (Feb. 9, 2023), https://www.theguardian.com/environment/2023/feb/09/shell-directors-personally-sued-over-flawed-climate-strategy [https://perma.cc/A9DD-WF83].

[129] *Id.*

[130] SHELL, *Achieving Net-Zero Emissions*, https://www.shell.com/powering-progress/achieving-net-zero-emissions.html [https://perma.cc/M6JF-FAXZ] (last visited Aug. 4, 2023).

that such reputational damage could be significant, resulting in several unfavorable news reports in the press. This sort of event could cause a drop in stock value. Investors that acquired stocks before knowing that the disclosed information was distorted could claim they had been harmed under Rule 10b-5 actions (*employment of manipulative and deceptive practices*).[131]

On the subject, it should be noted that even foreign companies would be exposed to the risk of class actions.[132] Of course, this is already a risk that they run today, but another disclosure obligation for a foreign company could be a new risk factor that companies should include in their equation when deciding about cross-listing in the U.S. markets. Notwithstanding, there are numerous other advantages to be considered by the managers and shareholders of foreign companies before making such a decision.

IV. EMPIRICAL RESEARCH: ESG GOVERNANCE IN S&P100 COMPANIES

The discussion above shows growing ESG litigation risks for companies and their management. Overall, it can be safely affirmed that stakeholderism has gained ground in its historic battle with shareholder primacy over the past few years. In addition, the most recent U.S. court precedents denote a trend toward a greater burden on company officers and directors concerning their duty of oversight of crucial risks. On top of that, federal legislation and regulations press officers and directors with a variety of demands for publicly held companies, whether at the level of disclosure or standards of conduct. As discussed above, some might say that it is simply no longer worth it to take a company public in the United States, as the means of private funding through differentiated securities law regimes have also multiplied in recent years.[133]

However, companies may have different views on incorporating ESG issues into their strategies, depending on the economic sector.[134] For instance, companies with higher ESG risk, operating in sensitive industries, are more exposed to stakeholder pressures to address the social and environmental impacts of their operations. Thus, it should be expected that companies operating in such industries have greater concern about incorporating ESG measures.

A. The Profile of Companies with Increased ESG Risks

Data reports seem to agree with the premise that industries in sensitive markets tend to invest more in ESG governance. According to a recent KPMG report, the tech industry has a slower implementation of ESG measures: "26% have

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[131] *See*, *e.g.*, *Halliburton Co. v. Erica P. John Fund, Inc.*, 573 U.S. 258, 283–84 (2014).
[132] Coffee, Jr., *supra* note 11, at 5.
[133] Georgiev, *supra* note 50, at 228, 314.
[134] *See*, *e.g.*, PwC, *supra* note 16.

significant incorporation of ESG into their strategic planning"; "34% say climate change is having a high impact on their company's investment/funding"; and "37% believe their governance experts are very effective."[135] On the other hand, consumer goods companies may be more likely to embed ESG programs within the company's strategic planning. A recent survey by PwC found that "83% of consumers think companies should be actively shaping ESG best practices."[136] Consumers care about the ESG actions of companies in this sector and can penalize companies that present unsatisfactory results to the public.

However, the literature is mixed when discussing if companies in sensitive industries tend to have superior ESG performance. For instance, Garcia et al. researched companies from emerging economies and found the larger the company's systemic risk, the higher the maximum value for environmental performance.[137] Some have attempted to demonstrate that companies operating in polluting industries such as oil, gas, and consumer goods are under more pressure from stakeholders regarding environmental and social impacts.[138]

It seems intuitive that for the oil and gas industry, the management of environmental, health, safety, liability, and reputational risks are key concerns for achieving long-term success.[139] There are many examples of environmentally damaging events from such industry, such as the Deepwater Horizon oil spill in the Gulf of Mexico, the Montara oil spill in the Timor Sea,[140] and the 2007 San Francisco Bay oil spill,[141] just to name a few. Despite that, Borghesi et al. found that companies in the aircraft, chemicals, and oil & gas industries tend to have below-average *corporate social responsibility* (CSR) levels, while companies in the consumer goods industry tend to have above-average CSR measures.[142]

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[135] *The ESG Imperative for Technology Companies*, KPMG (2020), https://assets.kpmg.com/content/dam/kpmg/us/pdf/2020/04/esg-imperative-for-tech-companies.pdf [https://perma.cc/2KK7-PNKH].

[136] Casey Herman, *How Much Does the Public Care About ESG?*, PWC https://www.pwc.com/gx/en/services/sustainability/publications/cop26/how-much-does-the-public-care-about-esg-pwc-cop26.html [https://perma.cc/Y9XX-T49S].

[137] Alexandre S. Garcia, Wesley Mendes Da Silva & Renato Orsato, *Corporate Sustainability, Capital Markets and ESG Performance*, INDIV. BEHAV. & TECH. FIN. INNOV. 287, 304 (2019).

[138] *Id.*

[139] David B. Spence, *Corporate Social Responsibility in the Oil and Gas Industry: The Importance of Reputational Risk*, 86 CHI. KENT L. REV. 59, 59 (2010).

[140] *WA oil spill 'one of Australia's worst'*, ABC NEWS (Aug. 24, 2009), https://web.archive.org/web/20091125112049/http://www.abc.net.au/news/stories/2009/08/24/2664927.htm [https://perma.cc/AN8T-U2FE].

[141] *Remembering Cosco Busan: An Overview of the 2007 Oil Spill*, OFFICE OF RESPONSE AND RESTORATION – NATIONAL OCEANIC AND ATMOSPHERIC ADMINISTRATION (Nov. 08, 2022), https://response.restoration.noaa.gov/remembering-cosco-busan-overview-2007-oil-spill.

[142] Richard Borghesi, Joel F. Houston & Andy Naranjo, *Corporate socially responsible investments: CEO altruism, reputation, and shareholder interests,* 26 J. CORP. FIN. 164, 165-66 (2014).

Moreover, another article researching the impact of *corporate social performance* (CSP) on measures of systemic, idiosyncratic, and total risk of firms, found that a higher CSP decreases the total and idiosyncratic risk of firms.[143] Remmer Sassen et al. found that "environmental performance generally decreases idiosyncratic risk, whereas total and systemic risk is only affected in sensitive industries."[144] Notwithstanding some ambiguities in the literature, it is clear that the economic sector in which a firm operates affects the ESG program of that company.[145] Studies seem to converge to the conclusion that companies providing the market with consumer products are more exposed to pressure from consumer groups.[146] In this sense, when companies apply corporate social responsibility measures strategically to pursue social objectives valued by the company's stakeholders, profitability tends to improve.[147]

Looking at this matter from the investor's point of view, an article dated 2016 found that ESG screening when applied to non-durable consumer goods and health technology industries has more positive effects.[148] On the contrary, when applied to the energy minerals industry, the result of ESG screening is underperforming. The same study also found that the application of ESG screening resulted in the lowest exclusions in the communications industry, while the energy and non-energy minerals industry had the highest number of exclusions.

Specifically on S&P500 companies, a 2017 study revealed that the level of disclosure is different in three areas (Environmental-Social-Governance).[149] The highest level of transparency was found in governance and the lowest was in environmental.[150] There were also significant differences in transparency in both disclosing information about specific social policies.[151] The study showed that industrials and information technology computed the lowest median ESG scores, while materials and telecommunications services computed the highest median ESG scores.[152]

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[143] Remmer Sassen, Anne-Kathrin Hinze & Inga Hardeck, *Impact of ESG factors on firm risk in Europe*, 86 J. BUS. ECON. 867, 867 (2016).
[144] *Id.*
[145] Giovanna Michelon, Giacomo Boesso & Kamalesh Kumar, *Examining the link between strategic corporate social responsibility and company performance: an analysis of the best corporate citizens*, 20 CORP. SOC. RESP. & ENV'T. MGMT. 81, 81 (2013).
[146] *Id.* at 85.
[147] *Id.* at 88.
[148] Tim Verheyden, Robert G. Eccles & Andreas Feiner, *ESG for All? The Impact of ESG Screening on Return, Risk, and Diversification*, 28 J. APPLIED CORP. FIN. 47, 51 (2016).
[149] Nabil Tamimi & Rose Sebastianelli, *Transparency among S&P 500 companies: an analysis of ESG disclosure scores*, 55 MGMT. DECISION 1660, 1660 (2017).
[150] *Id.*
[151] *Id.*
[152] *Id.* at 1671.

B. Methodology and Result of the Empirical Research

From the discussion in the previous chapters, it can be inferred that the industry in which a company operates may be a significant factor in the type of ESG governance that it adopts. Hence, this Section analyzes the S&P100 companies' ESG governance to verify if the companies surveyed: (1) embed ESG matters in traditional corporate governance structures such as the audit committee or the nominating & corporate governance committee, and/or (2) create corporate governance structures specifically designed to oversee ESG issues. These questions will be useful to conclude if, when the ESG litigation risk of a firm increases, the level of ESG corporate governance rises in parallel.

To standardize the search process and achieve more reliable results, this research only considered the information expressed in (1) the latest ESG Report released by the companies, and/or (2) the most recent proxy statement.[153] These are the two corporate documents with the most general information about public companies. Thus, the results presented here may not fully correspond to reality if the company has not disclosed the information we seek in the abovementioned documents. However, we concluded that these possible minor distortions would be considerably more acceptable than not having a rigid methodology for seeking out the information of our interest.

Also, for the present research, a "traditional governance structure" was deemed to be any position, committee, or forum customarily existing in the corporate structures of American firms, such as the audit and finance committee, governance and nominating committee, CEO, and CFO, among others. We did not consider in this category the positions, committees, or forums mostly dedicated to ESG matters. Moreover, for this research, "specific governance structures" are deemed to be committees, positions, or forums with competencies specifically linked to social or environmental matters.

1. Embedment of ESG matters in traditional corporate governance structures.

Starting with the first question above, collected data indicate that 98 of 100 analyzed companies had assigned some ESG competence to one or more traditional governance structures.[154] Of these 98 companies, 53 assigned ESG attributions solely to traditional board governance structures and 45 had both board and

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[153] The proxy statement is a mandatory document as per SEC relevant rules. The ESG Report has no prevision in the applicable securities laws, but an overwhelming majority of S&P100 companies prepare and disclose such document to the market.

[154] We considered "traditional governance structure" a governance body that typically exists in U.S. companies such as the audit committee or the nominating & corporate governance committee.

executive ESG governance structures.[155] To put it another way, none of the companies that assigned ESG competencies to traditional structures did so solely through executive governance structures.[156]

By delving into data per economic sector, it is possible to see that companies facing less ESG risks are also less willing to embed ESG matters in executive governance positions. On the contrary, companies facing a greater level of ESG risk are more likely to use both board and executive traditional governance structures to deal with ESG matters. As summarized in the figures below:

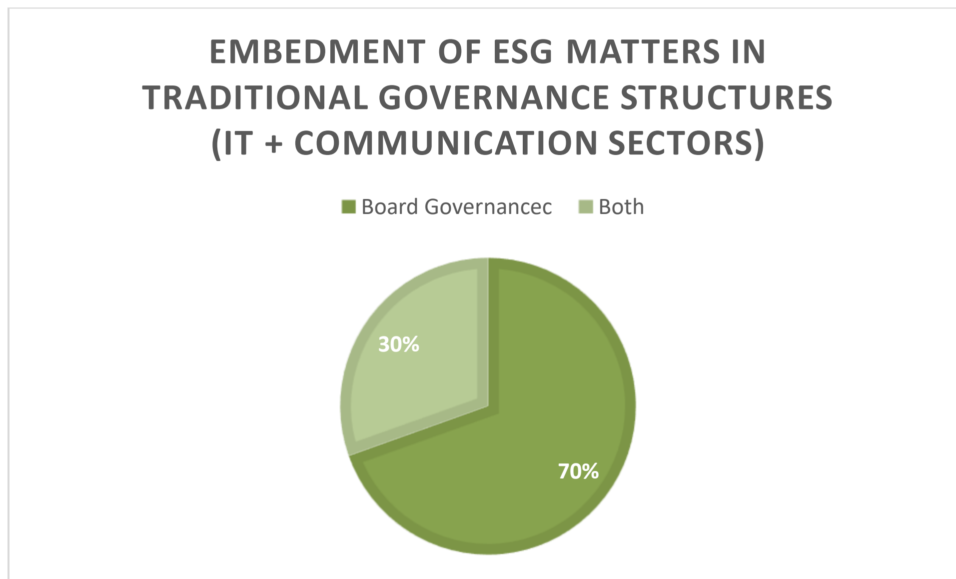

Figure 1. Embedment of ESG Matters in (x) traditional board governance or (y) both board and executive governance structures by S&P100 companies from the IT and Communication sectors (23 companies).

[155] Data from authors' research.
[156] *Id.*

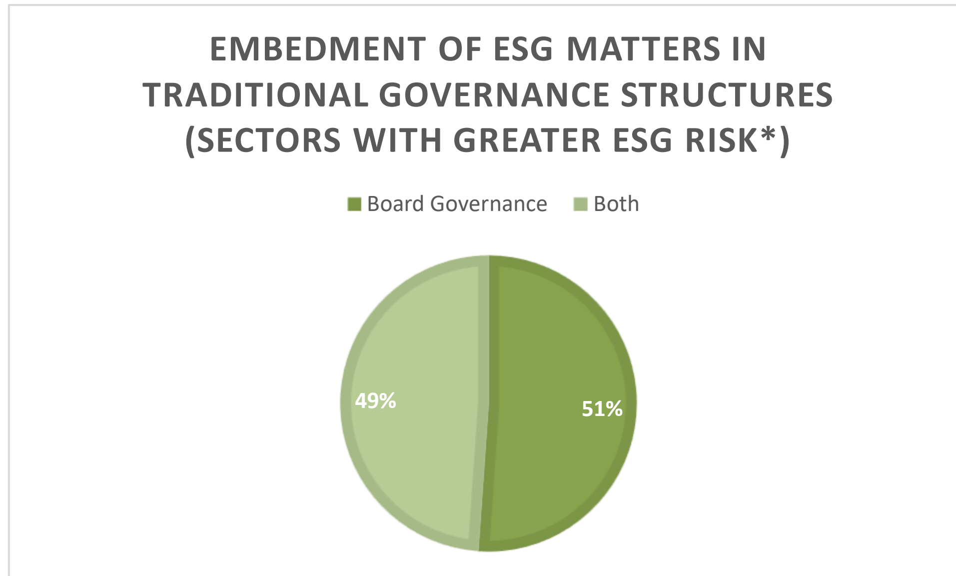

*Figure 2. Embedment of ESG Matters in (x) traditional board governance or (y) both board and executive governance structures by S&P100 companies from the consumer staples, health care, industrials, materials, energy, and real estate sectors (45 companies). *Please refer to figure 4 below.*

The data above displays two important facts. First, embedding ESG matters in traditional board structures (e.g., corporate governance and nominating committee) is commonplace for S&P100 companies. Second, companies with more ESG risk tend to embed environmental and social matters in both executive and board governance structures. This is interesting to see, as directors are traditionally more exposed to Caremark claims. Only recently have Delaware courts expressly held that officers owe to shareholders similar duties as directors.[157]

To confirm the tendency above, we analyzed how S&P100 companies operating in sensitive industries embedded ESG issues in traditional governance structures.[158] The results are displayed below:

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[157] *In re* McDonald's Corporation Derivative Litig., C.A. No. 2021-0324-JTL, at 22-24 (Del. Ch., Jan. 23, 2023).

[158] For this Article's definition of sensitive industries, *see infra* text accompanying note 165.

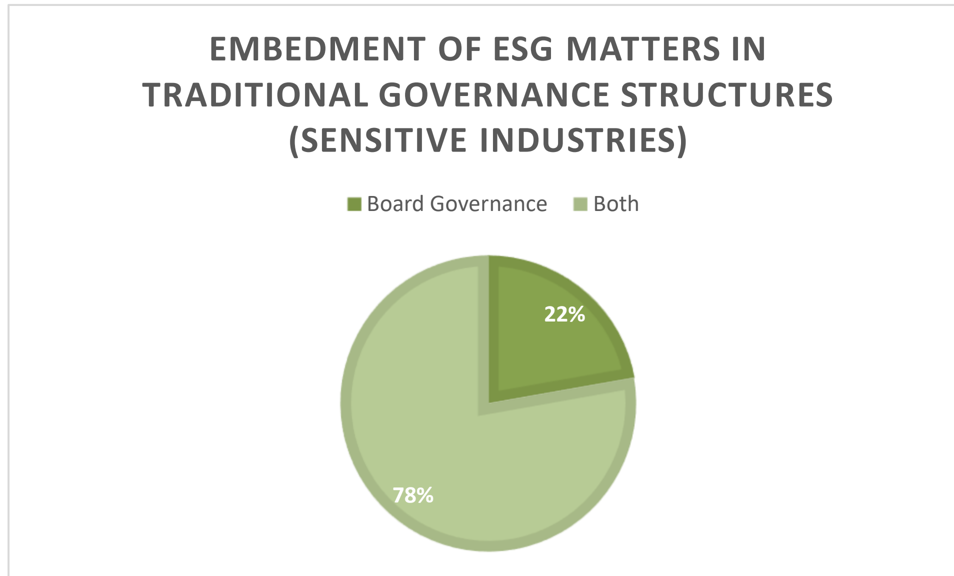

Figure 3. Embedment of ESG Matters in (x) traditional board governance or (y) both board and executive governance structures by S&P100 companies from sensitive industries (9 companies).

Therefore, the data confirm the thesis that the greater the relevant ESG risk is, the more likely a S&P100 company is to embed ESG matters in both board governance and executive governance structures.

2. Corporate Governance Structures Specifically Designed to Oversee ESG Issues

In addition to embedding ESG matters in traditional structures, S&P100 companies also tend to create a specific governance structure designed to oversee ESG issues. Out of the 100 surveyed companies, 88 had specific governance structures for ESG matters, 5 with only specific board governance structures, 60 with only specific executive governance structures, and 23 had both board and executive governance structures.

Our research also found that 29 companies of the entire set surveyed had ESG Steering Groups, ESG Committees, or ESG Councils: 2 from the communication sector, 1 from the consumer discretionary sector, 4 from the consumer staples sector, 7 from the financial sector, 5 from the health care sector, 2 from the industrials sector, 5 from the information technology sector, 1 from the material sector, and 1 from the utility sector (*see* Table 1 below).[159]

[159] For this Article's definition of sensitive industries, *see infra* text accompanying note 165.

COMPANY	SECTOR	NAME
UNITEDHEALTH GROUP INC	Health Care	ESG Steering Committee
MASTERCARD INC	Financials	ESG Executive Steering Committee
BROADCOM INC	Information Technology	ESG Steering Committee
WALMART INC	Consumer Staples	ESG Steering Committee
THERMO FISHER SCIENTIFIC INC	Health Care	Company Leadership Team Steering Committee
PFIZER INC	Health Care	Sustainability Steering Committee
ACCENTURE PLC	Information Technology	ESG Executive Committee and Steering Committee
ADVANCED MICRO DEVICES INC	Information Technology	ESG Executive Steering Committee
NEXTERA ENERGY INC	Utilities	Sustainability Executive Steering Committee
RAYTHEON TECHNOLOGIES CORP	Industrials	ESG Steering Committee
INTEL CORPORATION CORP	Information Technology	ESG Executive Steering Committee
UNION PACIFIC CORP	Industrials	Sustainability Steering Committee
AMGEN INC	Health Care	ESG Council Initiative Steering Committees
MEDTRONIC PLC	Health Care	Sustainability Steering Committee
INTERNATIONAL BUSINESS MACHINES CO	Information Technology	ESG Steering Committee
GOLDMAN SACHS GROUP INC	Financials	Firmwide Climate Steering Group
MORGAN STANLEY	Financials	Global Sustainable Business Steering Committee Global Capital Markets and Investment Banking ESG Steering Committee Corporate Services Global Sustainability Steering Committee
BOOKING HOLDINGS INC	Consumer Discretionary	Sustainability Steering Committee Diversity & Inclusion Steering Committee
MONDELEZ INTERNATIONAL INC	Consumer Staples	Sustainability Steering Committee
AMERICAN EXPRESS	Financials	ESG Steering Committee

CITIGROUP INC	Financials	Climate Risk Steering Committee
T MOBILE US INC	Communication	Sustainability Steering Committee
PAYPAL HOLDINGS INC	Financials	ESG Steering Committee & Working Group
COLGATE-PALMOLIVE	Consumer Staples	Sustainability Steering Committee
FEDEX CORP	Industrials	DEI Steering Committee
DOW INC	Materials	ESG Steering Team Climate Steering Team
CHARTER COMMUNICATIONS INC	Communication	ESG Operating Steering Committee (OSC) Executive Steering Committee (ESC)
KRAFT HEINZ	Consumer Staples	ESG Steering Committee ESG Steering Subcommittees
BANK OF NEW YORK MELLON CORP	Financials	Enterprise ESG Steering Council

Table 1. S&P100 companies with ESG Steering Committee(s).

Moreover, when we dive further into the companies' sector, it is possible to confirm several cross-industry differences deserving in-depth analysis. A total of 12 companies were found not adopting any type of specific governance to ESG matters.

NAME	**SECTOR**	**SPECIFIC GOVERNANCE STRUCTURES FOR ESG MATTERS? (Y/N)**
AMAZON COM INC	Consumer Discretionary	No
NVIDIA CORP	Information Technology	No
ALPHABET INC	Communication	No
BERKSHIRE HATHAWAY INC	Financials	No
META PLATFORMS INC	Communication	No
SALESFORCE INC	Information Technology	No
NETFLIX INC	Communication	No
ORACLE CORP	Information Technology	No
TEXAS INSTRUMENT INC	Information Technology	No
STARBUCKS CORP	Consumer Discretionary	No
BLACKROCK INC	Financials	No
EXELON CORP	Utilities	No

Table 2. S&P100 companies with no specific governance structures for ESG matters.

If we were to concentrate on the criteria adopted for the sectors' classification above, it would not be possible to perfectly capture the trend that companies linked to the technology industry presented a bias of having fewer specific ESG governance structures. But the connection of companies like Alphabet, Meta, and Netflix to the tech industry is indisputable. If we were to add these 3 companies to the group including Nvidia Corp., Salesforce Inc., Oracle Corp., and Texas Instrument Inc., the conclusion would be that technology companies are the majority of those not having a specific ESG governance structure.

Of course, this is not to say companies comprising this group do not have governance strategies to deal with ESG issues and risks. All 14 information technology companies classified in the database surveyed have traditional governance structures designated to oversee ESG matters. The same goes for Alphabet, Meta, and Netflix.[160] However, the results presented in Table 2 above appear to corroborate that: (1) ESG strategies do vary significantly across industries, and (2) the tech industry particularly may be more inclined to embed ESG matters in traditional governance structures compared to other industries.[161]

Moving forward with the analysis of differences by sector, of the 88 companies having specific ESG governance structures, we can break down the data by economic sector and verify variations in percentage terms:

[160] Data from authors' research.

[161] These results are also in line with Nabil Tamimi & Rose Sebastianelli study which found out that the information technology industry had computed the lowest median ESG scores amongst the surveyed industries. *See* Tamimi & Sebastianelli, *supra* note 149.

S&P100 companies with specific ESG governance structures
(*% per sector*)

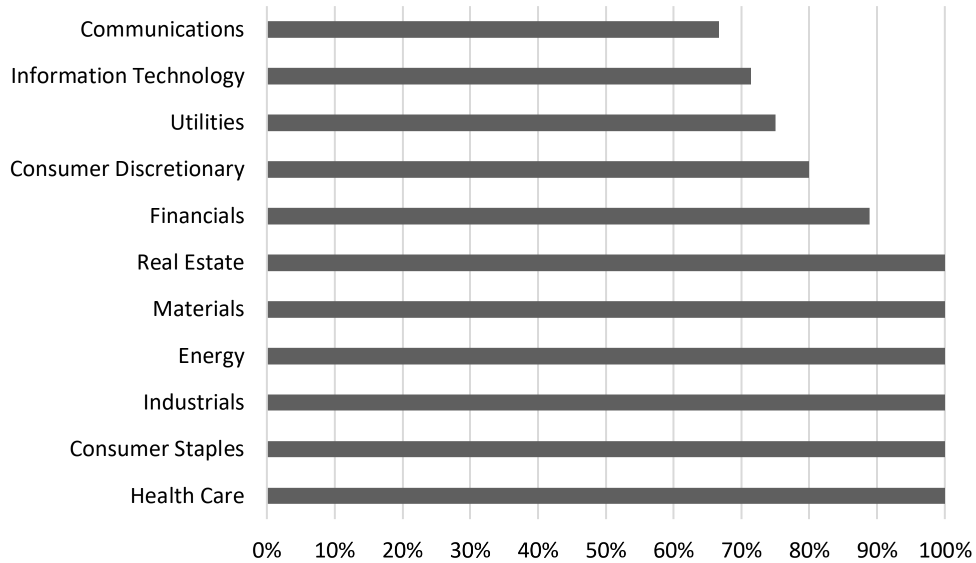

Figure 4. S&P100 companies with specific ESG governance structures

By adding Alphabet, Meta, and Netflix to the information technology sector (for data analysis purposes), it gets easier to understand that technology companies had ESG governance structures at a significantly lower percentage than overall S&P100 companies' average.

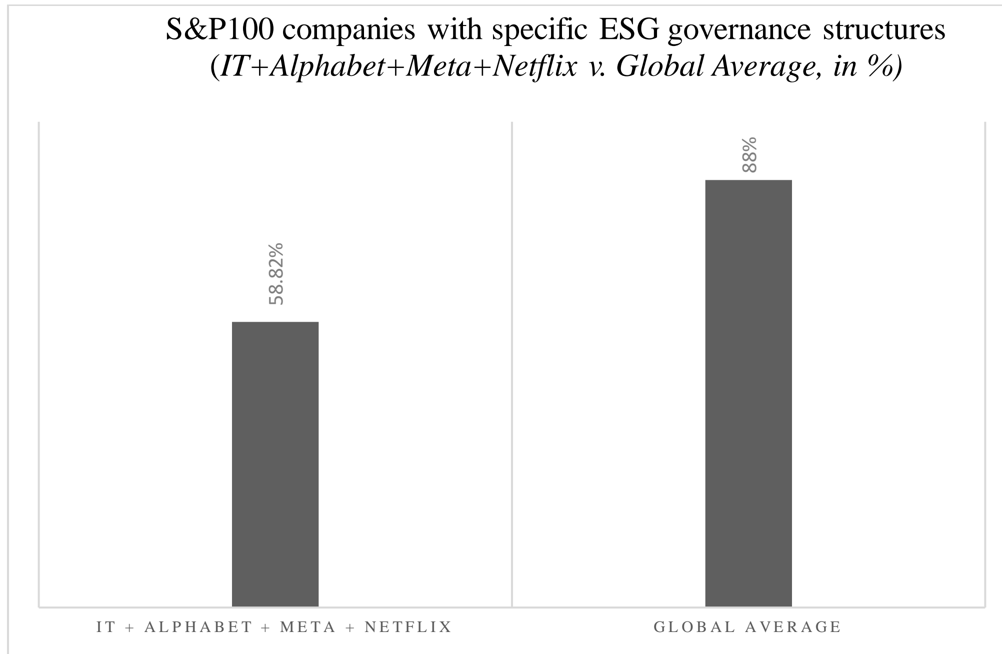

Figure 5. S&P100 companies with specific ESG governance structures

To investigate ESG governance variations across sectors to a further extent, we have also separated SP&100 companies into two categories: (1) sensitive industries, and (2) non-sensitive industries.

The following Table contains possibly the most relevant data of this Section, as it shows sensitive industries adopt specific governance structures for ESG matters. Grounded on the previous chapter's literature review, this Article considers as part of the "sensitive industries" the oil and gas industry, fast food industry, tobacco industry, and energy industry (if the company operated with "dirty energies," as the expression is commonly used). Considering these criteria, we selected a list of 9 companies.[162]

Table 3 below shows that all of them adopted specific governance structures for ESG matters (100%). This contrasts with the percentage of 86.81% of the companies in the non-sensitive industries group adopting specific ESG governance structures (79 of 91).

[162] *See* Figure 3 above and Table 3 below.

COMPANY	SECTOR	SPECIFIC GOVERNANCE STRUCTURES FOR ESG MATTERS? (Y/N)	STRUCTURES PART OF THE BOARD GOVERNANCE, EXECUTIVE GOVERNANCE, OR BOTH?
EXXON MOBIL CORP	Energy	Yes	Executive Governance
CHEVRON CORP	Energy	Yes	Both
MCDONALDS CORP	Consumer Discretionary	Yes	Board Governance
PHILIP MORRIS INTERNATIONAL INC	Consumer Staples	Yes	Executive Governance
CONOCOPHILLIPS	Energy	Yes	Both
CATERPILLAR INC	Industrials	Yes	Both
ALTRIA GROUP INC	Consumer Staples	Yes	Executive Governance
SOUTHERN	Utilities	Yes	Board Governance
DUKE ENERGY CORP	Utilities	Yes	Both

Table 3. Specific governance structures for ESG matters in S&P100 companies operating in sensitive industries.

These results are consistent with the part of the literature which states that the economic sectors in which companies operate are a factor affecting ESG strategy. They also coincide with (1) the greater environmental or social risk faced by these companies, and (2) previous research pointing out that companies operating in polluting industries such as oil, gas, and consumer goods are under more pressure from stakeholders regarding environmental and social impacts.[163]

V. CONCLUSIONS

This Article has demonstrated several reasons why companies' legal ESG risk is on the rise over the past few years. First, stakeholderism has been gaining ground in its long dispute with shareholder primacy. On the federal regulation front, the SEC has been discussing adaptations to its disclosure rules. If approved, this will greatly impact market participants.[164] The new rules will likely increase

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[163] Garcia, Mendes Da Silva, & Orsato, *supra* note 137. *See also* PwC, *supra* note 16.

[164] Apart from the cost of producing disclosures (that is significant), it seems reasonable to infer that companies will have to rebuild corporate governance solutions to reduce litigation risks. About

compliance costs and the risk of litigation. Officers and directors will have to be more alert to obligations to inform the market and shareholders on any relevant ESG matters. At the state level, there is plenty of political disagreement over how to address ESG matters. States with heavy participation in the national GDP such as California and New York are about to adopt legislation with ESG disclosure and reporting rules, perhaps even before federal regulation takes effect. But some others disagree and adopt anti-ESG rules. This lack of cohesion is yet another factor to increase ESG risk and must be taken into consideration by companies.

The literature review further demonstrated that companies, directors, and officers are subject to several litigation risks. This Article examines the two most relevant of them with regard to ESG corporate governance, *i.e.*, derivative actions and securities class actions. This Article pointed to the existence of board committees with proper documentation as a good defense in *Caremark* claims. From this, we can infer that not adopting a governance structure designating ESG responsibilities for a board committee can be an unsafe course of action from a legal standpoint.

This Article then contributes to the discussion with a detailed empirical analysis, focused on the companies composing the S&P100. After juxtaposing the results with relevant literature, the research found that increasing ESG litigation risks will probably push companies to create corporate governance structures specifically designed to oversee ESG issues, as it already occurs with all S&P100 companies operating in sensitive industries.[165]

Moreover, results revealed some important variations across industries. For instance, S&P100 companies in the technology industry tended to adopt less specific governance structures for ESG matters (58.82%), preferring more than other sectors embedding ESG tasks into traditional structures.[166] It could be inferred that this also has to do with the ESG risk level faced by tech companies being inferior to the average risk faced by other industries. That would reasonably explain why tech companies tend to embed oversight of ESG matters in traditional governance structures (*e.g.*, nominating & governance committee, audit committee) but are less keen to create specific board-level or executive C-level structures to deal with these matters. It is important to consider that traditional board governance structures may be sufficient for averting *Caremark* claims, as we

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the costs of producing disclaimers. *See*, *e.g.*, Andrew K. Jennings, *Disclosure Procedure*, 82 MD. L. REV. 920, 975 (2023).

[165] *See* Fairfax, *supra* note 90, at 404 ("[M]any boards have begun to incorporate ESG oversight into their committee charters.").

[166] This is consistent with the materials we have collected about technology companies and ESG. *See supra* notes 135, 152.

have seen in *City of Detroit Policy and Retirement Sys. v. Hamrock* case, for instance.[167]

[167] *See City of Detroit Police & Fire Ret. Sys. v. Hamrock*, C. A. 2021-0370-KSJM at 26 (Del. Ch. Jun. 30, 2022).