

Investor Alert

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LITIGATION AS A TOOL FOR ACHIEVING ESG GOALS

Environmental, Social and Governance (“ESG”) investing has become more widely accepted, investors have increasingly used litigation to achieve ESG goals while enhancing shareholder value.

Broadly, ESG investors seek to encourage the companies in which they invest to further environmental, social, and corporate governance goals while minimizing their negative impact on the same.¹ For instance, an ESG investor might choose not to invest in companies which negatively impact the environment. Alternatively, an ESG investor who owns stock in a public company might use its rights as a stockholder to encourage a company to adopt environmentally responsible policies.

Indeed, ESG investing has exploded in popularity in recent years,² and ESG-oriented investors have scored major victories in their efforts to change corporate behavior. For instance, in 2021, Engine No. 1, a relatively small hedge fund, won three seats on ExxonMobil’s board of directors with the goal of addressing the company’s carbon emissions.³

ESG, however, has also drawn substantial criticism, including from politicians who have sought to forbid some investors from considering ESG factors in

investment decisions.⁴ In the face of such challenges, investors have employed a wide variety of tools to achieve their ESG goals. One of the most successful but underdiscussed of these tools is litigation.

Investors Have Successfully Used Litigation to Achieve ESG Goals

In numerous instances, investors have leveraged litigation to achieve ESG goals.

In fact, environmental activist group ClientEarth has designed an advocacy strategy around achieving ESG goals using investor litigation. Recently, ClientEarth brought a derivative lawsuit in its capacity as a shareholder against the board of Shell plc.⁵ In that case, ClientEarth is exercising its right as a shareholder to sue Shell plc’s board for breaching its legal duties by failing to manage the material and foreseeable risks posed to the company by climate change.⁶ ClientEarth is seeking an order requiring the board to adopt a strategy to manage climate risk in line with its legal responsibilities.⁷

In one successful example of investor litigation responding to irresponsible corporate policies, Labaton Sucharow represented the Commonwealth of Massachusetts Pension Reserves Investment Trust, a

¹ Investor Bulletin, [U.S. Securities and Exchange Commission, Environmental, Social and Governance \(ESG\) Funds](#) (Feb. 26, 2021),

² Joan Michelson, [ESG Investing Is ‘Soaring.’ What Does It Mean?](#), FORBES (Nov. 18, 2022), (according to a recent report, “ESG-oriented assets under management (AUM) will ‘more than double’ in the United States to \$10.5 trillion,” by 2026).

³ Jillian Ambrose, [‘This isn’t ideological’: reluctant ‘green hero’ behind Exxon coup](#), THE GUARDIAN (June 4, 2021).

⁴ See, e.g., David Morgan, [U.S. House Republicans target ESG investments in latest culture war salvo](#), REUTERS (February 28, 2023), (“Senate

Republican leader Mitch McConnell said the bill would ensure that plan managers consider only financial returns in making investments, and not ‘extraneous factors’ such as environmental pollution and employment policies.”); Adam Bluestein, [These states are trying to ban ESG investing](#), FAST COMPANY (October 26, 2022).

⁵ Press Release, ClientEarth, [ClientEarth files climate risk lawsuit against Shell’s Board with support from institutional investors](#) (Feb. 9, 2023)

⁶ *Id.*

⁷ *Id.*

pension fund serving a wide variety of public employees in the state of Massachusetts, in a case against Massey Energy Company, a large coal mining company, for violations of federal securities laws.⁸ In that case, Massey Energy Company's claims that it was investing heavily in worker safety were proven false when a massive coal dust explosion, caused by flagrant safety violations, led to the deaths of twenty-nine miners. The case resulted in a substantial \$265 million monetary settlement for shareholders and allowed investors to take action against the coal miner's reckless safety policies.⁹

Labaton Sucharow also represented the City of Monroe Employees' Retirement System, a relatively small pension fund serving public employees, in connection with a major settlement involving 21st Century Fox, Inc. which arose out of the sexual harassment scandals that plagued Fox News beginning in 2016. The lawsuit secured not only a favorable \$90 million cash settlement, but also a positive social outcome in the form of significant corporate governance reforms.¹⁰ As part of the settlement the company established the new Fox News Workplace Professionalism and Inclusion Council to directly address the company's culture of discrimination and harassment.¹¹

Investors have several options in addressing ESG goals through the courts.

Several Litigation Tools Help Investors Achieve ESG Goals

Under American law, investors have several litigation tools at their disposal to influence the behavior of companies in which they invest. Because a majority of large American corporations are incorporated in the state of Delaware, many of the litigation tools available to investors derive from Delaware state law, but there are also ways for investors to leverage federal investor protections.

For instance, many investors utilize Section 220 of the Delaware General Corporation Law, which allows stockholders of Delaware corporations to demand to inspect the books and records of corporations "for any proper purpose."¹² Initially, the stockholder sends a non-public letter directly to the corporation laying out the demand. If the corporation does not respond within five days, or the corporation refuses to permit the inspection, the stockholder may apply to Delaware's Court of Chancery for an order to compel the inspection.¹³

Delaware courts' definition of proper purpose under this statute generally includes investigating wrongdoing or mismanagement.¹⁴ The stockholder must also demonstrate a "credible basis" for the suspected wrongdoing.¹⁵ Stockholders can utilize Section 220 to gain access to formal board materials such as minutes and even, in certain situations, the personal emails of

⁸ *In re Massey Energy Co. Securities Litigation*, No. 10-cv-00689 (S.D.W. Va.).

⁹ *Id.*

¹⁰ *City of Monroe Employees' Retirement System v. Rupert Murdoch, et al.*, No. 2017-0833 (Del. Ch.).

¹¹ *Id.*

¹² Del. Code Ann. tit. 8, § 220 (West).

¹³ Del. Code Ann. tit. 8, § 220 (West).

¹⁴ Gail Weinstein et al., *Section 220 Decisions Amplify Stockholders' Rights to Inspect Books and Records*, HARVARD LAW SCHOOL FORUM ON CORPORATE GOVERNANCE (October 3, 2022).

¹⁵ *Id.*

board members and officers.¹⁶ Section 220 demands have become an invaluable “first step” for many investors pursuing ESG goals to get a fuller picture of actions being taken by corporate boards. With this visibility, investors can determine what tactics create the most viable path forward.

For instance, before investors in the Boeing Company brought a lawsuit to hold Boeing’s directors and officers liable for failing to provide oversight of the company’s safety protocols, leading to the 737 MAX crashes, the investors brought a books and records demand through which they received over 600,000 pages of documents.¹⁷ Investors in that case, represented by co-lead plaintiffs New York State Comptroller Thomas P. DiNapoli, as trustee of the New York State Common Retirement Fund, and the Fire and Police Pension Association of Colorado, secured a \$237.5 million cash settlement and substantial corporate governance reforms including ensuring that members of the Boeing Company’s board will have aerospace and safety expertise going forward.¹⁸

Derivative litigation is often a viable path forward for stockholders trying to influence the behavior of corporate boards and officers. A derivative action is a suit brought by a shareholder on behalf of a corporation against that corporation’s management or board to address misconduct such as breaches of

fiduciary duty.¹⁹ The Boeing Company and Fox News examples above were derivatives lawsuit brought under Delaware law.

Shareholders can also pursue ESG goals through class action litigation under the federal securities laws. For example, in a case brought against Bank of America by a group of pension funds including Stichting Pensioenfondszorg en Welzijn, represented by PGGM Vermogensbeheer B.V., Fjärde AP-Fonden, the State Teachers Retirement System of Ohio, the Ohio Public Employees Retirement System, and the Teacher Retirement System of Texas, alleging that defendants misled investors regarding Bank of America’s acquisition of Merrill Lynch, plaintiffs achieved both a large cash settlement and substantial governance reforms including changes to director elections.²⁰

In a case against video game developer Take-Two Interactive, Labaton Sucharow represented a group of pension funds which successfully secured both a substantial cash settlement and corporate governance reforms including a “clawback” provision providing for the recovery of bonus or incentive compensation paid to senior executives if such compensation was awarded based on erroneously reported financial results as an outcome of fraud or other known misconduct.²¹ Similarly, investors suing Strategic Realty Trust for violations of the federal securities laws were able to achieve both a favorable cash settlement

¹⁶ *Id.*

¹⁷ Stephen A. Radin and Joshua Glasser, *Well Gotshal Discusses Boeing Decision and Board Oversight of Product Safety Risks*, THE CLS BLUE SKY BLOG (September 20, 2021).

¹⁸ *In re the Boeing Company Derivative Litigation*, No. 2019-0907-MTZ

(Del. Ch.).

¹⁹ See Del. Ch. Ct. R. 23.1.

²⁰ *In re Bank of America Corp. Sec. Litig.*, No. 09 MDL 2058 (S.D.N.Y.).

²¹ *In re Take Two Interactive Sec. Litig.*, No. 06-cv-803 (S.D.N.Y.).

and governance reforms including changes to the company's procedures for removing directors and filling board seats.²²

Takeaways

Litigation is one of the most powerful tools at the disposal of investors seeking to influence a company's ESG policies. One major advantage is that, utilized correctly, lawsuits can bring corporate leaders to the negotiating table on a broad range of ESG topics which might otherwise be overlooked. As the challenges to ESG investing mount, investors should be sure to incorporate litigation into their overall strategy where appropriate.

Labaton Sucharow's lawyers are available to address any questions you may have regarding these developments. Please contact the Labaton Sucharow lawyer with whom you usually work or the contacts below.

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²² *Booth v. Strategic Realty Tr., Inc.*, No. 13-cv-04921 (N.D. Cal.).