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Future Facing Disputes

Will ESG related concerns result in courts adopting a more purposive approach to corporate liability?

Given the increasing prominence of ESG issues, the decision of the Supreme Court in *Okpabi and others v Royal Dutch Shell Plc and another [2021] UKSC 3* has potentially profound implications for group structures and external supply chains. A fact-based caveat to the concept of corporate liability offers a glimpse of a solution to the tragedy of the commons. As such an important structural shift in the English legal system may be underway. Multinational companies now need to carefully consider if relevant decisions are being made by the appropriate parties within their group structures.

ESG and corporate liability

Corporate liability is the legal responsibility that a corporation has in relation to the actions of its employees as well as its agents, such as subsidiary companies, that hold themselves out as acting on its behalf. Traditionally, the courts have adopted a relatively strict default position where a parent company was rarely held responsible for the actions of its subsidiaries. This meant that a parent company could shield itself behind the 'corporate veil' and effectively separate itself from the actions of its subsidiaries. By setting the boundaries of what party may be legally responsible for the actions of another, the concept of corporate liability facilitates risk management and economic growth. Indeed, it is arguably one of the most important concepts in English private law, and perhaps most other legal systems:

> *'It's not laughter or the ability to use language that distinguishes man from the animals, but his capacity for incompetence. Each spider's web may be unique but, taken as a whole, perfection makes them uniform. The spider does not aspire to excellence, the gibbon swinging in the tree does not deliberate on error. Certainly they make mistakes but the result is starvation for one, a broken body for the other. Limitations for a spider or a gibbon are not something they have to learn to live with. Man alone has the opportunity to accept failure and it is this alone that allows him to lord it over creation. Our most important discovery was not fire, or that language could be written down, or the atom split, but the concept of limited liability.' (The Wisdom of Crocodiles, Paul Hoffman)*

Classical economists such as Adam Smith and Karl Marx held different perspectives on man's economic endeavours. However, they shared a common view that the environment formed a continuous and infinite backdrop to these efforts. Corporate liability forms an integral part of a legal and economic system that defines assets and upholds private law rights. It allowed man, for a time at least, to believe that he could lord it over creation. The recent rise in environmental, social and governance ('ESG') issues is, in part, due to the relatively recent recognition that resources are finite and that liabilities are not always easy to price in conventional monetary terms. This creates a difficult tension with the concept of corporate liability as externalities, such as pollution, were and are inherently more difficult and problematic to define and then fairly attribute to a specific individual entity or individual than the assets of a company.

Okpabi and others v Royal Dutch Shell Plc and another [2021] UKSC 3

The recent UK Supreme Court judgment in Okpabi suggests that UK based parent companies may be potentially liable as a result of their subsidiaries' overseas operations. It is indicative of a judicial trend whereby English courts appear to be prepared to expand the principles of duty of care and thus erode the concept of corporate liability.

In 2015, 40,000 Nigerian citizens initiated High Court proceedings against Royal Dutch Shell ('RDS'), the London based parent company of the multinational Shell group of companies. They alleged that RDS owed them a duty of care as it exercised significant control over material aspects of the operations and activities of its Nigerian subsidiary and was thus liable in negligence for various oil spills in the Niger Delta. In January 2017 the High Court held that it was not reasonably arguable that there was any such duty of care and in February 2018 the Court of Appeal upheld this decision.

This year the UK Supreme Court overturned these earlier decisions. It concluded that there was a real issue to be tried against RDS and its Nigerian subsidiary and held:

- Each case will be fact specific. Liability will turn on the conduct of the parent company. The key issue is the extent to which the parent did take over, or share the management of, the relevant activity with the subsidiary.
- The Court of Appeal had erred in law in terms of the procedure for determining the arguability of the claim at an interlocutory stage, wrongly dismissing the relevance of future disclosure and whether there were reasonable grounds for believing that a fuller investigation of the facts may add to, or alter, the evidence relevant to the issue, particularly the disclosure of internal corporate documents.
- The law relating to the liability of parent companies in relation to the activities of their subsidiaries is not a distinct category of liability in common law negligence. It gives rise to no new issues of law and must be determined on ordinary general principles of the law of tort regarding the imposition of a duty of care.

What does Okpabi mean for the future of corporate liability?

In Okpabi, the Supreme Court noted that the Shell group is organised along business and functional lines, as opposed to corporate status. This line of reasoning suggests that when allocating where liability lies within corporate structures and supply chains, courts will be more prepared to adopt a more flexible and fact-based approach that reflects the reality of what is occurring on the ground (as opposed to the more traditional approach to corporate separation). In this respect perhaps an analogy can be drawn with employment law and the purposive approach to determining employment status where it has been held that terms in the parties' written contracts could be disregarded when seeking to determine a claimant's employment status (*Autoclenz Ltd v Belcher and Others [2011] UKSC 41*).

The Okpabi decision is therefore an example of how an English domiciled parent company may be liable before the English courts for claims brought by overseas claimants in circumstances where the parent company can be shown to owe a duty of care towards the claimants for the acts of its subsidiary.

To this end, this greater responsibility could also extend to the directors of parent companies. Attempts may be made to hold the directors of UK based parent companies responsible for sub-standard ESG compliance in subsidiary companies. This could manifest through directors being held liable for breach of directors' duties, in particular Section 172 (d) of the Companies Act 2006 which requires a director of the company to have regard to 'the impact of the company's operations on the community and the environment'.

Moving forwards, can corporate liability risks be limited?

In light of the decision in Okpabi, multinational companies should take time to review the operations of their overseas subsidiaries and conduct audits specifically focussing on local ESG policies and reporting procedures to ensure compliance with all necessary responsibilities and that the relevant decisions are being made by appropriate parties.

With regard to the upcoming Glasgow COP, corporations should also bear in mind that if politicians do fail to deliver national climate pledges, NGOs, and other third parties, will be increasingly prepared to target the parent companies of multinationals and engage in strategic litigation to achieve their goals.

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