

Future Facing Disputes

Is climate change the ultimate hot potato for parent companies?

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 corporate group structures. As such an important structural shift in the English legal system may be underway. Multinational companies need to carefully consider if the relevant decisions are being made by the appropriate parties within their group structures.



UN climate targets and the difficulties with multilateralism

World greenhouse gases are set to rise 16% by 2030 compared with 2010 based on a recent United Nations analysis of existing climate pledges (NDC Synthesis report, 17 September 2021). This is the exact opposite of the cuts required to meet the 2015 Paris Agreement and limit warming to well below 2C and ideally 1.5C. Furthermore, references to temperatures have reportedly been removed from the UK/Australia trade deal (The Guardian, 11 September 2021). Trade deals involve politics, business and ultimately compromise. Kim Stanley Robinson's "The Ministry for the Future" near future novel refers to the significant overlap between the political and corporate world as climate targets are set. The book contends that of the total of 3,000 gigatons of fossil carbon that have already been located in the ground, 2,500 gigatons of fossil carbon will need to be left in the ground as stranded assets if the average global temperature warming limit of 2C is not to be exceeded. One of the ways climate change is tackled is by issuing a new form of currency, a carbon coin – a digital currency disbursed on proof of carbon sequestration, in return for leaving fossil carbon in the ground.

Securing compliance with international law is difficult. The League of Nations, the predecessor to the United Nations created after WWI, struggled and ultimately failed to impose international law and prevent WWII. Tom Burke the Chairman of E3G, a policy think tank, has compared climate change to WWII, observing that following Pearl Harbour, the US economy shifted from making cars to tanks in 12 months and the economy improved (E3G, 14 September 2021). Steve Baker, a Conservative MP and a member of the group of MPs dubbed the "Net Zero Scrutiny group", has stated that unless the UK's climate change plans are economically viable, they will not be politically viable (The Financial Times, 29 September 2021). Both these points of view are most likely correct, suggesting that a systemic change in the way we do business is necessary.

Unfortunately, current corporate structures are not designed with climate protection in mind. Paul Polman, the former CEO of Unilever and author of Net Positive, considers that multilateralism, or international diplomacy, is not working and that what happens between now and 2030 is going to be crucial. In his view, the majority of climate issues can be solved by 2030 if action is taken now and that companies should invest for the long term to protect themselves from climate change otherwise there isn't going to be a longer term (Financial Times, 1 October 2021). Tariq Fancy, author of The Secret Diary of a Sustainable Investor, considers that ESG investment is a deadly distraction that prevents reform, and that irresponsible behaviour needs to be penalised at a systemic level (Financial Times, 13 August 2021).



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

Okpabi v Royal Dutch Shell Plc and another [2021] UKSC 3 is a decision of the Supreme Court that represents a potentially profound change to the way the concept of corporate liability and responsibility is determined. In 2015, 40,000 Nigerian citizens initiated High Court proceedings against Royal Dutch Shell Plc ("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. However, in February 2021 Supreme Court overturned these earlier decisions, concluding that there was a real issue to be tried against RDS and its Nigerian subsidiary.

The claimants relied upon two internal documents, witness statements provided by former employees of the Shell group and expert evidence. They argued that RDS has deliberately structured the Shell Group in a way that enables RDS to direct, control and intervene in the management of subsidiaries' operations. Whilst legal entities were required to take formal binding decisions "organisational approval" as a general rule preceded corporate approval.

The judgment refers to the evidence given by Mr Briggs, one of the former Shell employees *"Nigeria was seen as a hot potato...Not only is there the financial scale of the Nigerian operation, it is also a delicate political and environmental operation and there is the huge reputational risk and significance of Nigeria means that it could be in the top one of two concerns of Shell's Committee of Managing Directors amongst all of Shell's global activities."* The judgement also referred to an expert report prepared for litigation in the United States that provided *"Control comes in the form of monitoring and approving business plans, allocating investment resources, choosing the management and overseeing how the subsidiary responds to public affairs issues"*.

The Chancellor of the Court of Appeal found that mandatory policies, standards and manuals were of a high level and that control rested with the subsidiary company which was responsible for its own operations. RDS did not enforce standards. Instead RDS said there should be a system of supervision and oversight but left it to the subsidiary to operate that system. Justice Sales dissented, noting that there were several indications in the papers that the Shell group was aware of particularly acute problems in Nigeria, and that it could be inferred that RDS would wish to exert direct central control if the subsidiary was perceived as being ineffective in managing the risk of oil spills.

The Supreme Court, agreeing with Justice Sales, found that there was a very real and far more than a speculative possibility that documents will emerge on disclosure which will provide substantial support for their case at trial. As such the Court of Appeal had materially erred in determining the arguability of the claim at an interlocutory stage as to its treatment of what constitutes an arguable case and its approach to contested factual issues and significance of future disclosure – proper disclosure was important and raised triable issues. The Supreme Court noted that the organisational structure worked in practice and the extent to which the delegated authority of RDS was involved was very much in dispute. It noted that it was significant that the Shell group was organised along business and functional lines rather than simply according to corporate status and that this vertical structure involves significant delegation.

It is not so much that the substantive law itself has changed but the way in which the Supreme Court was prepared to look at the evidence in a different way to the Court of Appeal and recognise that there was a triable issue as to what may constitute control by a parent company. This suggests that when deciding where decisions are actually taken within corporate structures, courts will now 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 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).

Climate change risk and how to effectively manage it is perhaps the ultimate hot potato. A parent company will want to ensure that a subsidiary's activities are being managed appropriately. It is easy to see how the issue of parent company control could arise in the context of a climate change dispute. Equally, it is difficult to see how a parent company can effectively insulate itself from the risk that supervising a subsidiary may subsequently be found to amount to control and thus create a potential climate change liability for the parent company.

Conclusion

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. Climate change risk, like other forms of environmental liability, is not easy to price in conventional monetary terms. Okpabi's fact-based caveat to the concept of corporate liability and the Ministry for the Future's carbon coin, offer glimpses of a solution to the tragedy of the commons. The difficulties of multilateralism mean that 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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