

C L I F F O R D
C H A N C E

**COMMERCIAL DISPUTE RESOLUTION: ESG ANTE PORTAS?
ASA CONFERENCE – ESG AND DISPUTES: FLASH IN THE PAN OR GAME CHANGER?**

DR. MORITZ KELLER
3 FEBRUARY 2023

CLIMATE CHANGE IN THE SPOTLIGHT



RECORD-SEARING HEAT		
HOTTEST DAY IN U.K. HISTORY		
LOCATION	TEMP (°F)	TEMP (°C)
▶ Coningsby	104.5°	40.3°
▶ St. James Park	104.4°	40.2°
▶ Heathrow	104.5°	40.2°
▶ Gringley On The Hill	104.1°	40.1°
▶ Kew Gardens	104.1°	40.1°
▶ Northolt	104.0°	40.0°

*AT LEAST 34 LOCATIONS EXCEEDED THE U.K.'S PREVIOUS NATIONAL RECORD HIGH 102°F (38.7° C)

UN – Heat trend until 2060 not reversible

Forest fires in Europe

Floods in Australia

Heat record in the UK



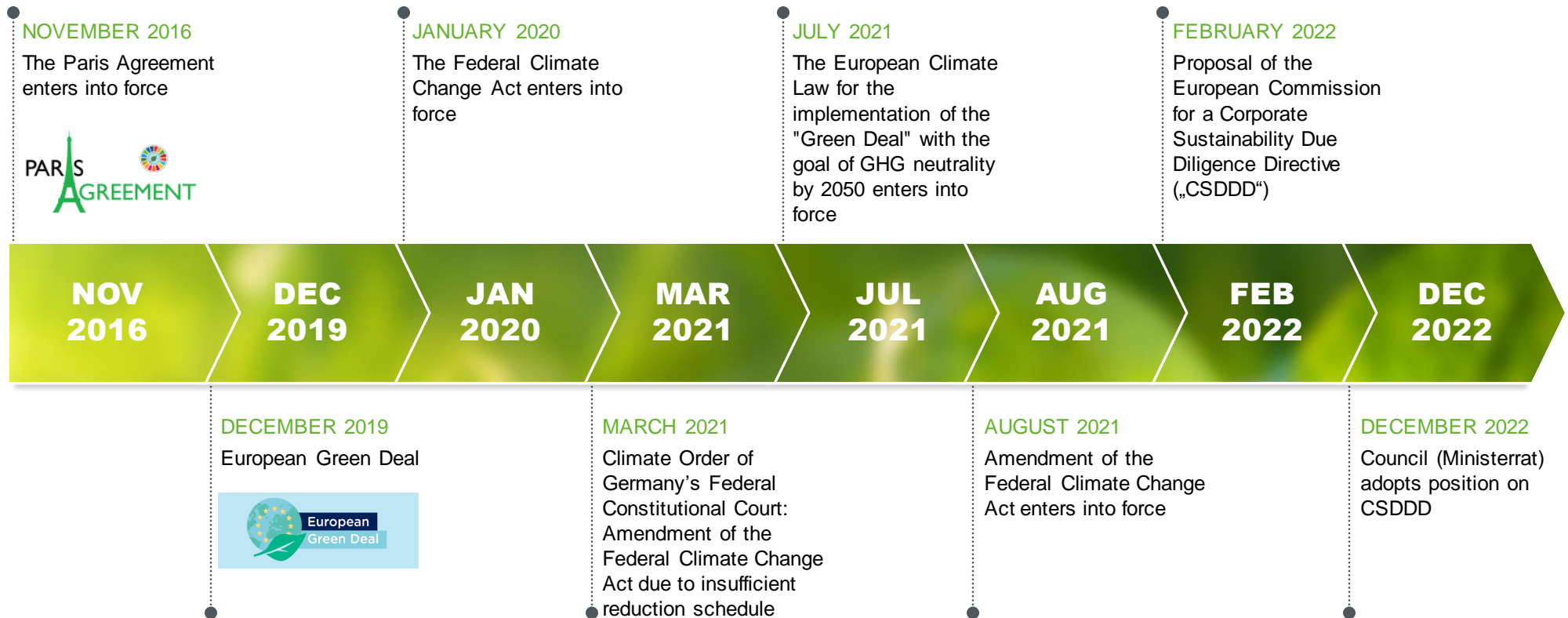
Paris Agreement: limit global warming well below 2 degrees Celsius

European Green Deal: accelerate clean energy transition

Climate Verdict BVerfG: net zero roadmap violates intergenerational justice

COP27: loss & damage funding for countries hit by climate disasters

NEW OBJECTIVES AND LEGISLATION IN LIGHT OF THE ESG DEBATE

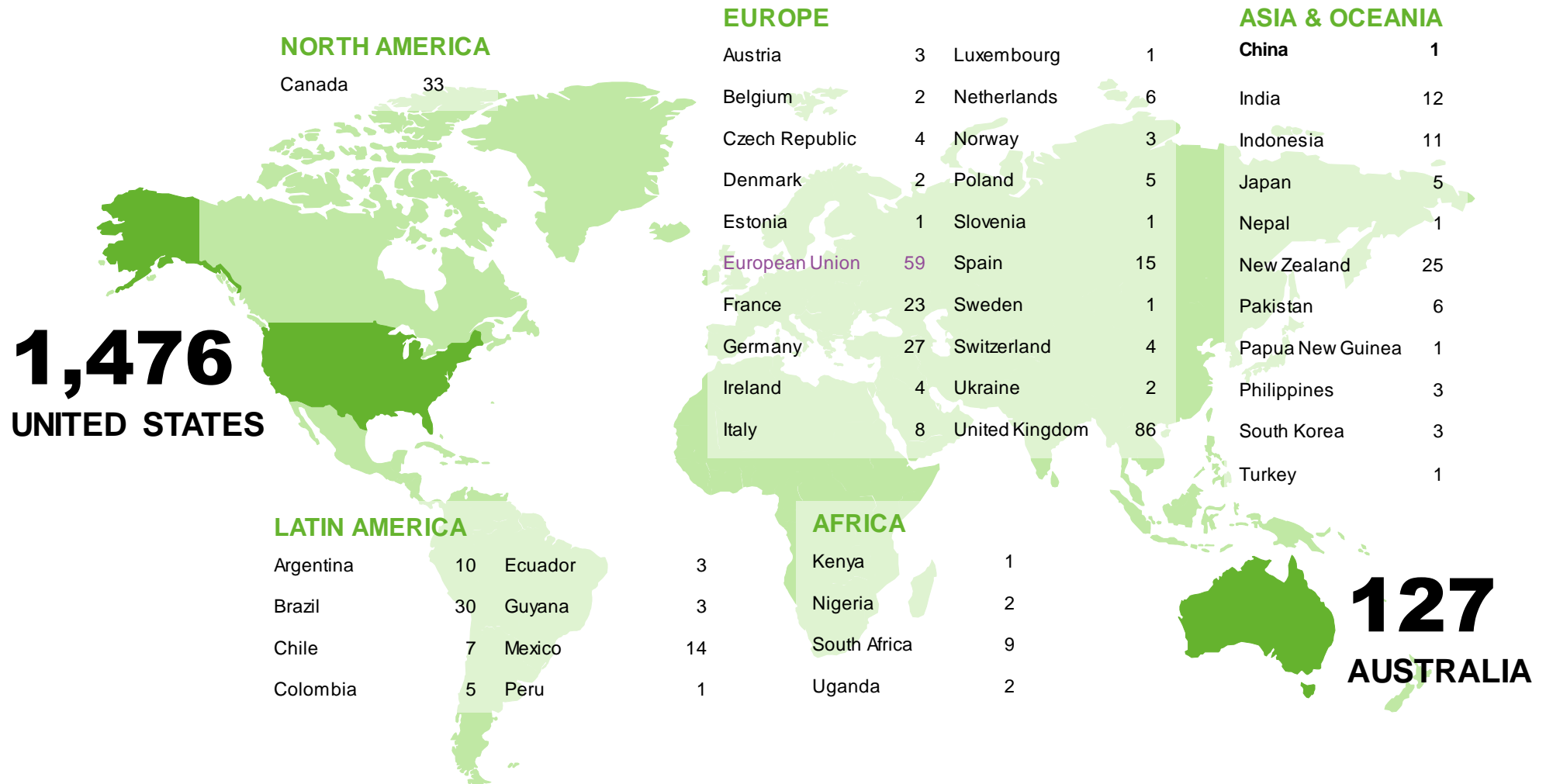


“ART. 20A OF THE GERMAN CONSTITUTION ENCOMPASSES THE NECESSITY TO TREAT THE NATURAL FOUNDATIONS OF LIFE WITH SUCH CARE AND TO LEAVE THEM IN SUCH CONDITION THAT FUTURE GENERATIONS WHO WISH TO CARRY ON PRESERVING THESE FOUNDATIONS ARE NOT FORCED TO ENGAGE IN RADICAL ABSTINENCE.”



BVERFG | CLIMATE VERDICT DATED 24 MARCH 2021 – HEADNOTE 4

OVERVIEW OF GLOBAL LAWSUITS RELATED TO CLIMATE CHANGE



CLIMATE CHANGE RELATED LAWSUITS AGAINST STATES



URGENDA FOUNDATION ./. NIEDERLANDE (2015)

The Dutch state is obliged to reduce GHG emissions by 25% by 2020 compared to 1990. The state must reduce GHG emissions in order to prevent the devastating consequences of climate change. This obligation follows, among others, from Art. 21 of the Dutch Constitution (habitability of the country and environmental protection), the European Convention on Human Rights (ECHR) and EU targets for GHG reduction.



FRIENDS OF THE IRISH ENVIRONMENT ./. THE GOVERNMENT OF IRELAND (2017)

Supreme Court overrules High Court decision and government's National Mitigation Plan. It is not clear how Ireland intends to achieve its 2050 targets.



BVERFG CLIMATE VERDICT (2020)

BVerfG rejects violation of fundamental rights due to breach of duty to protect, but criticizes insufficient roadmap (only until 2030) on the way to the targeted GHG neutrality by 2050. Legislature should define a roadmap for GHG neutrality until 2050. Article 20a of the German Constitution is justiciable and protects against a unilateral shift of the GHG reduction burden to future generations.



DEUTSCHE UMWELTHILFE ./. FEDERAL REPUBLIC OF GERMANY (2020-2022) (PENDING)

DUH files several complaints against the Federal Republic of Germany, inter alia a complaint in 11/2022 to establish a climate protection program that complies with the climate targets in the land use and forestry sector (LULUCF).

HUMAN RIGHTS RELATED LAWSUITS



YOUNG PEOPLE FROM PORTUGAL ./. 33 STAATES – ECHR (2020), CASE NO. 39371/20

Assertion of various human rights violations, including Art. 2 ECHR (life); Art. 8 ECHR (private and family life) by respondents (Germany, Great Britain, Norway, etc.). They are obliged to take sufficient measures to achieve Paris climate goals.



KLIMASENIORINNEN V. SWITZERLAND – ECHR (2020), APPLICATION NO. 53600/20

“Klimaseniorinnen” allege that Switzerland has failed to reduce its GHG emissions by 20% by 2020 and to establish measures to comply with the 1.5 degree target provided for in the Paris Agreement. Swiss national courts dismissed the case, following which Klimaseniorinnen called upon the ECHR.

Public hearing due on 29 March 2023!

Bundesregierung soll mehr für das Klima tun Erstmals deutsche "Klimaklage" vor dem EGMR eingereicht

18.10.2022



ENGEL ET AL. V. FEDERAL REPUBLIC OF GERMANY – ECHR (2022), CASE NO. 46906/22

Follow-up case to Germany's Federal Constitutional Court's judgment regarding the Climate Protection Act, where the Court had ordered the legislator to amend the act to comply with the environmental targets. The applicants complain that the Climate Protection Act amendments are insufficient to meet the targets agreed upon in the Paris Agreement.

ESG RELATED LAWSUITS AGAINST COMPANIES (1)



LLIUYA V. RWE (GER, 2015)

- **Objective:**

A Peruvian farmer, Raul Lluyia, seeks compensation for protective measures he is required to take to a glacier melt near his village. Mr. Lluyia alleges that RWE is responsible for a glacier melt due to its GHG emissions, for which it has to pay pro-rata compensation.

- **Judgment (District Court Essen):**

Action dismissed essentially due to lack of causation. The court held that no causal link can be established between RWE's GHG emissions as such and climate change. Climate change with its adverse effects would persist even if RWE's emissions were to be ignored.

- **Status of the Proceedings (Higher Regional Court Hamm):**

The Appellate Court assumes that the claim is conclusive. It therefore took evidence and held an on-site hearing in Peru. The outcome depends to a large extent on the results of the expert opinions on two topics:

- Is there a serious threat of harm to the claimant's premises from flooding and/or a mudslide as a result of the increase in the spread and volume of water in the lagoon?
- Does the defendant contribute to the compression of greenhouse gas molecules and thus to global warming? Is the volume of water in the lagoon also increasing as a result of the rising average temperature? Is the defendant's contribution to the cause measurable and calculable?

Peruvian farmer sues German energy giant for contributing to climate change

Saul Luciano Lluyia wants damages from RWE to protect hometown of Huaraz from a swollen glacier lake at risk of overflowing from melting snow and ice



ESG RELATED LAWSUITS AGAINST COMPANIES (2)



FOUR ISLANDERS OF PARI /J. HOLCIM (CH, 2022)

- **Claimants:**

Four residents of the Indonesian island Pari, supported by the NGOs HEKS/EPER, the European Centre for Constitutional and Human Rights and WALHI.

- **Objective:**

Assertion of an obligation of Holcim to pay pro rata compensation for climate change-related damages on Pari Island, to make financial contributions to protective measures against flooding and to reduce greenhouse gas emissions.

- **Argumentation:**

Procedural documents are not accessible. From the press releases of the NGOs, however, it can be inferred that the core of the argument will be that Holcim, as a major emitter, bears significant responsibility for climate change and its consequences on Pari. The claimants seek compensation for anti-flood measures. Similar questions are likely to arise as in the *Lliuya v. RWE* case.

- **Status of the Proceedings:**

A request for conciliation has currently been submitted to the so-called justice of the peace (Friedensrichter). This procedure precedes the actual legal proceedings.



ESG RELATED LAWSUITS AGAINST COMPANIES (3)



NGOS /. ROYAL DUTCH SHELL PLC (NL, 2019)

- **Objective:**

Milieudefensie/Friends of the Earth Netherlands and other NGOs as well as a large number of Dutch citizen seek conviction of Shell on GHG reductions.

- **Judgment (The Hague District Court):**

Shell is ordered to reduce the greenhouse gas emissions caused by itself and its customers (!) by 45% by 2030 compared to 2019. Shell had an unwritten duty of care within the meaning of the relevant general tort clause of the Dutch Civil Code. The court took into account, inter alia:

emissions from Shell and consequences of climate change for the Netherlands;

Rights guaranteed in the ECHR such as Art. 2 ECHR (life) and Art. 8 ECHR (private and family life);

The UN Guiding Principles (UNGP) as “soft law”;

- Shell's control over emissions (Scope 1 to 3);
- Paris Climate Change Agreement as an expression of broad consensus on what is needed to prevent dangerous climate change;
- IPCC report SR15 on possible reduction pathways;
- Compensatory effect of the EU Emissions Trading System (ETS);
- Proportionality considerations.

- **Status of the Proceedings:**

Royal Dutch Shell PLC has appealed against the judgment.



ESG RELATED LAWSUITS AGAINST COMPANIES (4)



DUH, GREENPEACE /I. WINTERSHALL DEA, BMW, MERCEDES, VOLKSWAGEN (GER, 2021)

- **Claimants:**

Managing Directors of DUH (against BMW, Mercedes, Wintershall); Managing Directors of Greenpeace and individuals (against VW); in each case financially and ideologically supported by DUH and Greenpeace.

- **Objective:**

Defendant companies to cease natural gas/oil production and the sale of vehicles with combustion engines by 10/2030. This is to compensate for alleged regulatory failure and accelerate the phase-out of fossil energy.

- **Argumentation:**

BVerfG recognised the CO2 budget approach in the climate order. Businesses should cease emissions-relevant activities in order to achieve the 1.5 degree target regulated in the Paris Agreement. Otherwise, legislators would take measures to reduce CO2 and impair the claimants' general right of personality (*allgemeines Persönlichkeitsrecht*).

- **Judgment of the District Court of Stuttgart in the Daimler-Proceedings from 13th September 2022: :**

Action dismissed; no evidence that the claimants' general right of personality is affected; unclear whether and how legislator will become active; matter must be regulated by legislator in a generally valid manner.



INTERIM CONCLUSIONS



- The cases referred to are “direct ESG disputes”. Such disputes are brought before national courts due to lack of an arbitration agreement between the parties.
- In direct ESG disputes claimant accuses defendant of directly contributing to climate change and causing adverse impact on claimant’s rights and interests (cf. Lluïya v. RWE, Islanders v. Holcim).
- Claimants often pursue strategic goals (so-called “strategic litigation”), e.g.
 - (1) raise public attention to ESG issues, inter alia through media coverage of proceedings,
 - (2) push for changes in the way legislators and society deal with ESG-related issues
- Disputes at state courts are better suited for achieving these goals as the proceedings, particularly the oral hearings, are public.
- In contrast, indirect ESG disputes usually concern contractual disputes which to some extent or indirectly relate to ESG. These disputes may become relevant in the context of arbitration.

ESG DISPUTES IN ARBITRATION – OVERVIEW



According to the ICC Report on “Resolving Climate Change Related Disputes through Arbitration and ADR”, published in November 2019, the following categories of ESG disputes in the context of arbitration can be identified:

- **Energy transition-driven disputes**
 - **Category I:** Specific transition, adaption or mitigation contracts
 - **Category II:** Contracts not specifically related to transition, adaption or mitigation
- **Submission Agreements for direct liability claims**
- **Human rights and the supply chain**
- **Shareholder claims**
- **Knock-on effects of the anti-ESG movement**



ESG DISPUTES IN ARBITRATION – ENERGY TRANSITION-DRIVEN DISPUTES

CATEGORY I: SPECIFIC TRANSITION, ADAPTION OR MITIGATION CONTRACTS

Scope:

Low-emission (mitigation) and climate-resilient (adaptation) projects and programs for contributing to countries' climate change priorities according to the Paris Agreement are on the rise. Accordingly, contracts – with arbitration clauses – are being concluded for adapting to a warming climate and reducing greenhouse gas emissions, e.g.

- funding, insuring and licensing of renewable energy,
- decommissioning of non-renewable power plants,
- adaptation of existing buildings and infrastructure, etc. including with reference to the UNFCCC framework.



Hypothetical case no. 1:

The bank has financed a wind farm project and is in dispute with the project company about the release of tranches because construction is not progressing according to the plan agreed upon in the loan agreement.



Hypothetical case no. 2:

The building owner seeks compensation because the renovation carried out by the contractor is not sufficient to insulate the building and to save the amount of energy stipulated by the law or the authorities.



ESG DISPUTES IN ARBITRATION – ENERGY TRANSITION-DRIVEN DISPUTES

CATEGORY II: CONTRACTS NOT SPECIFICALLY RELATED TO TRANSITION, ADAPTION OR MITIGATION

Scope:

Commercial contracts – with arbitration clauses – that have no specific climate change-related purpose or subject-matter and may even pre-date the Paris Agreement, but nevertheless may be impacted by the contracting parties' responses to

- changes in national laws;
- regulation to meet the country's commitments under the Paris Agreement;
- voluntary industry commitments; (4) environmental impacts of climate change.



Hypothetical case no. 1:

A coffee farmer is required to change the production methods due to amendments in the agricultural law. He seeks price adjustment to pass on the increased costs to the buyer, a global coffee retailer.



Hypothetical case no. 2:

The car manufacturer has committed to establish a life cycle for the supplied materials. On the basis of an ESG clause in the supply contract, the car manufacturer now demands from his suppliers to collect and recycle the surplus material. The supplier in turn seeks contract adaptation due to increased costs.



ESG DISPUTES IN ARBITRATION – DIRECT LIABILITY CLAIMS (1)

Scope:

Arbitration agreements entered into after a ESG related dispute has arisen, e.g., the Bangladesh Factory Accord

- The “Accord on Fire and Building Safety in Bangladesh” signed on 15 May 2013 is an agreement between global brands and IndustriALL Global Union and UNI Global Union. The Accord expired on 31 Dec 2018 and was extended by a second agreement until 31 May 2021.
- The Accord was concluded in the aftermath of the Rana Plaza building collapse which killed over 1,100 garment workers and injured more than 2,000.
- The Accord aims at establishing a fire and building safety program for workers in Bangladesh. It covers 2.5 million workers in Bangladesh’s ready-made garment industry.



bangladeshaccord.org

ACCORD
on Fire and Building Safety in Bangladesh

UPDATES FACTORIES SIGNATORIES WORKERS RESOURCES ABOUT EN LOGIN

Download the Accord agreements:

2018
Accord on Fire and Building Safety in Bangladesh

2013
Accord on Fire and Building Safety in Bangladesh

> 190 brands

> 1600 factories

> 2 Million workers

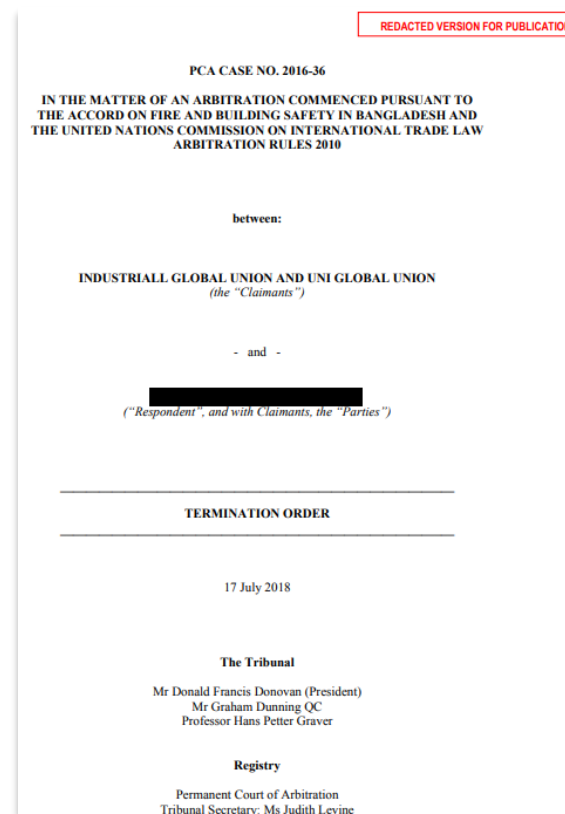


ESG DISPUTES IN ARBITRATION – DIRECT LIABILITY CLAIMS (2)

- Arbitration Clause in Art. 5 of the 2013 Accord:

*"[...] Any dispute between the parties to, and arising under, the terms of this Agreement shall first be presented to and decided by the SC, which shall decide the dispute by majority vote of the SC within a maximum of 21 days of a petition being filed by one of the parties. **Upon request of either party, the decision of the SC may be appealed to a final and binding arbitration process.** Any arbitration award shall be enforceable in a court of law of the domicile of the signatory against whom enforcement is sought and shall be subject to The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (The New York Convention), where applicable. [...]" [emphasis added]*

- IndustriALL Global Union and UNI Global Union (Claimants) commenced arbitrations under the Accord and the UNCITRAL Rules of Arbitration 2010 against a global fashion brand (Respondent in PCA Case No. 2016-36) on 8 July 2016, and against another global fashion brand (Respondent in PCA Case No. 2016-37) on 11 October 2016.
- On 17 July 2018, the Tribunal constituted in the two arbitrations issued termination orders following the settlement by the Parties of both sets of claims. The brands paid USD 2.3 million towards remediating unsafe conditions in Bangladesh ready-made garment factories.
- The cases were administered by the Permanent Court of Arbitration (PCA).



ESG DISPUTES IN ARBITRATION – HUMAN RIGHTS AND THE SUPPLY CHAIN (1)

GERMAN ACT ON CORPORATE DUE DILIGENCE OBLIGATION IN SUPPLY CHAINS
FROM 16 JULY 2021



- **Scope:** Companies with seat in Germany and at least 3,000 employees in Germany (from 1 Jan 2024: reduction of threshold to 1,000 employees, cf. Art. 1).
- **Subject matter:** Companies are obliged to conduct human rights and environment-related due diligence in their supply chains, i.e. by establishing a risk management system and allocating responsibility within the company (sec. 4), performing regular risk analyses (sec. 5), issuing policy statement and establishing preventive measures vis-à-vis suppliers (sec. 6), taking remedial action (sec. 7), establishing complaints procedure (sec. 8), documenting and reporting (sec. 10).
- **Civil liability:** A violation of the obligation under the Act does not give rise to any liability under civil law. BUT: Any liability under general civil law arising independently of the Act remains unaffected (sec. 3 para. 3).
- **Standing in civil proceedings (*Prozessstandschaft*):** Any person claiming to have been violated in a legal position pursuant to sec. 2(1) may authorize a domestic trade union or NGO to initiate proceedings to enforce his/her rights (sec. 11(2)).
- **Relevance for arbitration:** Sec. 11(2) lowers the hurdles for bringing a civil law complaint against the company due to ESG or human rights violations in the supply chain. Should the company be held liable, it could take recourse against the supplier who is supposed to have caused the violation.

ESG DISPUTES IN ARBITRATION – HUMAN RIGHTS AND THE SUPPLY CHAIN (2)

PROPOSAL OF THE EU COMMISSION FOR A CORPORATE SUSTAINABILITY DUE DILIGENCE DIRECTIVE (“CSDDD”) FROM 23 FEBRUARY 2022



Art. 22(1) CSDDD:

Member States shall ensure that companies are liable for damages if:

- a) they failed to comply with the obligations laid down in Articles 7 and 8 and;
 - b) as a result of this failure an adverse impact that should have been identified, prevented, mitigated, brought to an end or its extent minimised through the appropriate measures laid down in Articles 7 and 8 occurred and led to damage.
- Art. 22 CSDDD provides for direct civil liability of the company for non-compliance along the supply chain.
 - Should the company be directly held liable for violations in the supply chain, it will in turn seek indemnification from the respective business partner.
 - Contracts with suppliers will increasingly include human-rights or sustainability compliance provisions which will encourage companies to initiate proceedings against the supplier who is supposed to have committed the violation.
 - Such disputes will likely often be resolved by arbitration.

ESG DISPUTES IN ARBITRATION – SHAREHOLDER CLAIMS



ESG-related disputes **between shareholders** are conceivable at all levels.

- For example, there may be a dispute over a change to the Articles of Association, if a part of the shareholder intends to establish the 1.5 degree target from the Paris Agreement in the Articles of Association.
- Another example could be a dispute on further investments related to renewable energy or the reduction of the company's carbon footprint.

Likewise, disputes **between the shareholders and the company** could also be subject to arbitration, for example if the shareholders demand disclosure of the company's carbon footprint or the company's lobbying against stricter laws against climate change.

KLIMASCHUTZ

VW-Aktionäre wollen Autobauer zu mehr Transparenz bei Lobbyarbeit zwingen

Mehrere Pensionsfonds haben den Konzern in Verdacht,
durch Lobbyaktivitäten seine Klimaziele zu hintertreiben.
Nun soll die Justiz nachhelfen.



ESG DISPUTES IN ARBITRATION – KNOCK-ON EFFECTS OF THE “ANTI-ESG MOVEMENT”

- The **anti ESG-movement** is currently pulling back investments from the ESG sector.
- On 23 August 2022, Governor Ron DeSantis along with the Board of Administration passed a resolution "directing the state of Florida's fund managers to invest state funds in a manner that prioritizes the highest return on investment for Florida's taxpayers and retirees without considering the ideological agenda of the environmental, social, and corporate governance (ESG) movement".
-
- On 1 December 2022, the State of Florida announced that it would pull USD 2 billion worth of its assets due to BlackRock's ESG policy.
- If companies are pressured by politics to act against ESG, this will inevitably cause disputes with pro-ESG stakeholders, e.g., investors, shareholders, contractors, etc.



ESG DISPUTES IN ARBITRATION – CONCLUSIONS



1. Increase of ESG representations and warranties in contracts (with arbitration clauses), specifically due to the EU supply chain regulation. Disputes will arise if the contractual representations and warranties turn out to be untrue.
2. Energy transition and changes of ESG/climate regulation could impact existing contracts (with arbitration clauses) and lead to disputes, e.g. due to contract adaptation, non-performance, etc.
3. Increasing demand of ESG considerations by (institutional) investors could potentially lead to disputes with companies.
4. Anti-ESG movement could inflict disputes with ESG-oriented investors if companies are forced to ignore/neglect ESG factors.

QUESTIONS?





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MANY THANKS!

A hand holding a small globe of the Earth against a background of green leaves.

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