Lowenstein Sandler's In the Know Series

Video 4 –
ESG Regulatory Scrutiny and Tips for Robust D&O Insurance

By Eric Jesse
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Eric Jesse: Hi, I'm Eric Jesse, partner in Lowenstein Sandler's Insurance Recovery Group. Welcome to "In the Know." Today, we're going to talk about an issue that is at the forefront of conversations happening in many boardrooms across the country, and that is the ESG movement. In particular, we're going to share some tips on how companies can navigate the D&O insurance underwriting process with respect to these ESG issues.

For those unfamiliar with the term, "ESG" stands for environmental, social, and governance issues. "Environmental" typically refers to a company's climate change initiatives; "Social" and "Governance" initiatives are broad and can encompass things like diversity, inclusion, employee welfare—it can be broad enough to capture even cyber security, for example.

Aside from doing the right thing and considering the impact that their operations have on the communities around them, companies can also receive a financial benefit as a result of their ESG efforts. For example, banks and investors are intentionally deploying their capital to ESG-friendly companies who share their vision of corporate responsibility. But these financial benefits can also create incentives for companies to exaggerate the extent of their ESG efforts. This practice is known as "greenwashing."

Regulators, like the SEC, are making ESG a top priority, and they're cracking down on greenwashing. Companies should also expect that regulators, and inevitably the plaintiffs' bar, as they hone in on ESG matters, are going to try to develop broad theories of liability to hold companies and their directors and officers responsible for ESG-related failures and misrepresentations. And that's where insurance can come in, because directors and officers in companies can seek protection for these types of claims through a robust D&O insurance policy.

Insurers are also attuned to these potential risks, and they are going to take a keen interest in a company's ESG efforts during the underwriting and policy renewal process. Companies should expect D&O insurers to really probe their ESG efforts, and insurers are also going to want to understand how companies intend to comply with regulations that govern ESG-related disclosures. And as claims come in, insurers may even try to avoid coverage for these ESG-related lawsuits by claiming that companies made misrepresentations during the underwriting process or on their application with respect to ESG.

To help prepare for what is likely to be a more intensive underwriting process on the ESG front, here are a few tips to consider:

- First, companies should be prepared to answer not only questions about their ESG efforts, but they should be prepared to substantiate them. The executive team can send clear messages that they take ESG seriously, but they should be prepared to explain how they do so in concrete ways. Doing this will make the company a more attractive risk.
- Second, because their competitors are also investing in ESG, companies need to figure out ways to differentiate themselves. Some insurance brokers are offering a tool where companies can submit to an examination and receive a score on their ESG efforts. Companies should embrace tools like these because they can help add credibility to their ESG representations.
- And third, companies should recognize the importance of diversity on their corporate board, not only in terms of race, gender, and ethnicity, but also with respect to different skill sets and industry experience. Companies that embrace a diverse board show that they take ESG seriously, which in turn has the benefit of making the company become an attractive insured.

Thank you for joining us, and we look forward to seeing you next month on “In the Know.”