To Our Clients and Friends:

Over the past few years, interest in corporate social responsibility ("CSR") has increased significantly. The spotlight on CSR has led companies to expand and strengthen their CSR efforts. Many companies in turn have published sustainability reports, posted materials on their websites and made other statements about their past CSR efforts and future CSR goals. Certain website CSR disclosures are also required by statutes such as the California Transparency in Supply Chains Act of 2010 and the U.K. Modern Slavery Act 2015. Some organizations are also encouraging companies to include more CSR statements in their filings with the Securities and Exchange Commission ("SEC").

While CSR statements may foster public goodwill and inform customers and investors about positive company initiatives, they can also create real litigation and liability risks. This alert discusses a recent wave of litigation taking aim at CSR statements and steps companies can take to minimize these risks.

Background

Over the last two years, a significant number of lawsuits were filed challenging companies' CSR-related statements as false and misleading under various state consumer protection laws. These include more than ten cases against major consumer products manufacturers and retailers alleging that the companies made misstatements and omissions regarding various aspects of their supply chains, including the use of forced and child labor, factory safety, and working conditions.

Several securities fraud lawsuits challenging CSR-related statements were also filed during the past few years, including a case against a leading restaurant company challenging CSR statements about supply chain food safety initiatives and audit processes, and a case against a leading oil and gas company challenging CSR statements about safety reform efforts and environmental cleanup capabilities. In addition, leading consumer products manufacturers have received "books and records" complaints demanding access to company records and seeking details about whether companies knew their CSR statements were false or misleading.

The majority of these cases were brought as class actions on behalf of consumers and shareholders. Most challenge disclosures on corporate websites, including statements in sustainability reports, human rights documents, employee codes of conduct, third-party supplier codes, statements of ethics and integrity, and audit protocol descriptions. They assert that consumers and investors relied on and were deceived by the statements and suffered damages by either paying an unwarranted price premium for a product or
security or making a purchase they otherwise would not have made. The plaintiffs in these cases have sought injunctive relief in the form of modifications to the challenged disclosures, damages (including punitive damages), restitution (including refunds for products) and attorneys' fees and costs.

To support assertions that the challenged statements are material to consumers and investors (a required element of many consumer protection and securities claims), a number of the suits point to studies by major consumer data collection and securities consulting firms purportedly reflecting that: (1) consumers may be willing to pay a premium for products provided by companies committed to sustainability efforts and positive environmental impact; (2) consumers may consider companies' social responsibility efforts when deciding whether to buy those companies' products; (3) CSR statements may impact purchase decisions when included on product labels or advertising; and (4) institutional investors may consider corporate sustainability efforts in their investment strategies.

Some examples of CSR statements challenged in recent cases include:

- Company and supplier workers "are treated with respect and in compliance with the law."
- The company "is committed to fair treatment of all employees wherever it operates."
- The company requires its suppliers and their employees to "demonstrate honesty, integrity, and fairness."
- The company "expects its suppliers to comply with all applicable laws and regulations."
- Suppliers "must under no circumstances use, or in any other way benefit, from forced labor."
- The company "has the right to audit third-party suppliers."
- The company follows a "rigorous quality assurance program to ensure . . . safety and the highest quality products for our customers."

Most of the suits claim the statements are false or misleading based on public reports regarding instances of: (1) mistreatment of employees; (2) forced labor in supply chains; (3) child labor in supply chains; (4) unsafe working conditions in supply chains; and (5) failures of audit protocols and practices to eradicate these and other problems in supply chains. Some of the suits also assert that CSR statements are rendered false or misleading by major industrial accidents, which the plaintiffs claim would have been avoided if the statements regarding CSR initiatives and efforts were truthful.

**Recent Decisions in CSR Statement Litigation**

Thus far, the majority of these claims have been unsuccessful and dismissed at the pleading stage. Most courts find that statements in employee codes of conduct, guidelines for third-party suppliers, and ethics and integrity statements are aspirational in nature and not guarantees that companies, and their employees and suppliers, will in all circumstances follow the codes' requirements.
• For example, one federal district court in California recently dismissed a suit against a leading food manufacturer with prejudice, holding that proof that some of the company's suppliers actually used forced or child labor did not render statements in the company's supplier code false, because the company's statements "were aspirational, and when read in context, were actually a nuanced and correct summary of its efforts to combat forced labor." The court noted that the company "asks" its suppliers and their sub-tier suppliers to comply with its requirements and that the standards of the Code set forth expectations for suppliers." It concluded that the statements would "not mislead" reasonable consumers "into thinking that [the company's] suppliers abide by those rules and meet those expectations in every instance."

• Similarly, in Ruiz v. Darigold, Inc./Northwest Dairy Association, another federal district court dismissed challenges to CSR statements, noting that "in order to construe the [company's] CSR [report] as a guarantee of perfection . . ., plaintiffs ignore[d] the vast majority of the report, its purpose, and its structure to focus on a handful of sentences or, in some cases, phrases. Such an interpretive practice is, itself, unreasonable." No. 14-cv-1283, 2014 WL 5599989, at *3 (W.D. Wash. Nov. 3, 2014). The court examined each of the challenged statements, and found that they were, when read in context, "aspirational statements," or were not shown to be "false in any material respect." Id. at *4.

• In Bondali v. Yum! Brands, Inc., a federal appellate court affirmed the dismissal of claims challenging CSR statements in a company's supplier code of conduct, noting that the plaintiffs failed to allege any facts suggesting the company did not require its suppliers to abide by its standards. 620 Fed. Appx. 483, 489 (6th Cir. 2015). The court said that the fact "that a few suppliers did not adhere to the standards does not mean [the company] did not have the standards in place, and it is not reasonable to interpret [the company's] statements as a guarantee that its suppliers would, in all instances, abide by the corporate standards and protocols." Id. The court held that "a code of conduct is not a guarantee that a corporation will adhere to everything set forth [therein]," but rather "a declaration of corporate aspirations." Id. at 490. It also stated that "to treat a code of conduct as a statement of what a corporation will do, rather than what it aspires to do, would turn the purpose of a code of conduct on its head." Id.

Courts have also rejected challenges to CSR statements where plaintiffs fail to allege that they viewed and relied on the challenged statements before making their purchase decisions. Most consumer protection and securities laws require plaintiffs to show reliance as an element of a misstatement claim.

• For example, in Sud v. Costco Wholesale Corporation, a federal district court recently dismissed claims challenging website statements in a "Disclosure Regarding Human Trafficking and Anti-Slavery" and supplier "Code of Conduct" regarding the prohibition of forced labor, based on purported violations by third-party suppliers in Thailand, Indonesia, Vietnam and Malaysia. No. 4:15-cv-03783, 2017 WL 3459994, at *5 (N.D. Cal. Jan. 24, 2017). The court held that the claims failed for lack of standing and reliance because the plaintiffs did not allege they read and relied on the website statements prior to purchasing the products at issue. Id.
A number of federal district courts have also rejected CSR claims based on alleged disclosure omissions, where plaintiffs asserted that companies had an affirmative duty to disclose the existence of problems like forced or child labor in their supply chains on their websites or product packaging.

• For example, in one case, the plaintiff sought additional disclosures regarding forced labor in a company's supply chain, but the court held that such disclosures would be inconsistent with California's Transparency in Supply Chains Act (the "California Act"). According to the court, this statute requires retailers doing business in California to make disclosures on their website about their efforts to eradicate slavery and human trafficking, but nothing more. The court held that the California Act's provisions created a safe harbor against the proposed additional disclosures.

• Another district court also held, with respect to challenged omissions pertaining to child labor in a company's supply chain, that while such disclosures are not protected by the California Act (it drew a distinction between child labor and slave labor), the company had no affirmative duty to disclose "situations . . . where information may persuade a consumer to make different purchasing decisions." Hodson v. Mars, Inc./Mars Chocolate North America, LLC, No. 15-cv-04450, 2016 WL 627383, at *6 (N.D. Cal. Feb. 17, 2016). It noted that while child labor was a terrible humanitarian tragedy and that consumers may very well care about the use of child labor in a manufacturer's supply chain, absent any false or misleading statements regarding child labor, there was no duty to disclose. Id. Other district courts have subsequently come to the same conclusion. See, e.g., Dana v. Hershey Co., No. 15-cv-04453, 2016 WL 1213915, at *9 (N.D. Cal. Mar. 29, 2016) ("the weight of authority limits a duty to disclose . . . to issues of product safety, unless disclosure is necessary to counter an affirmative representation."); Sud v. Costco, 2017 WL 345994, at *7-8 (same).

In a few instances, however, claims challenging CSR statements have survived motions to dismiss, where companies made more concrete and measurable factual statements or promises to meet CSR goals by dates certain.

• In one securities fraud case, for example, a federal district court found that a major oil and gas company's statements about its safety reform efforts and environmental protection measures, including statements in sustainability reports and sustainability reviews on its corporate website, were sufficiently concrete to form the basis of a misstatement claim. The court held that the safe harbor for forward-looking statements did not apply to a number of the statements because they were not predictions of future events or aspirations, but rather "statements of existing fact." The court also found that the plaintiffs adequately pled that the website statements were actionable because the plaintiffs alleged that the statements "were intended to reach shareholders and the investing public."

• Similarly, in a relatively recent books and records case, a Delaware Chancery court permitted a complaint to proceed past the motion to dismiss stage. It found that plaintiffs' allegations pointing to the company's public promises and stated goals over the past two decades to eradicate the problem of child labor in its supply chain by 2020, adequately supported an inference that the
company's board of directors knew of at least some instances of exploitation of child labor in its supply chain "that would have triggered a duty to inform." The court allowed discovery to proceed against the company and its directors regarding a number of topics, including: (1) procedures the company used to monitor child labor in its supply chain; (2) reports, investigations and documents presented to the board; (3) reports from the company's suppliers; (4) discussions regarding the public promises the company made; and (5) reporting or compliance requirements the company imposed on its suppliers.

**Minimizing Litigation and Liability Risks**

These cases highlight the importance of taking steps to minimize the risk that CSR statements will result in a lawsuit. While the majority of the recent civil suits challenging CSR statements and omissions have failed, many of those cases are now on appeal. Claims challenging CSR statements have also survived the pleading stage in at least a few instances, subjecting companies to costly discovery. CSR statement lawsuits are also increasing in popularity, and may start gaining traction given the increasing prevalence of CSR statements and the growing number of studies reflecting that CSR issues may be important to consumers and investors. Companies need to be aware that there are real litigation risks relating to CSR statements. There are, however, a number of steps companies can take to minimize litigation and liability risks.

1. **Add disclaimer language.** Generally, companies should consider having disclaimer language accompany CSR statements. The disclaimers should note that the standards are not guarantees or promises. It also may be appropriate to note that the standards of measurement and performance are developing or are based on assumptions. In addition, it is particularly important for companies to consider such disclaimers on the website postings of CSR statements if they include a cross-reference or link to the website in their proxy statement or other SEC filings.

2. **Check the facts.** As with other types of public statements, companies should confirm the accuracy of CSR statements before they are made public. This includes reviewing CSR statements for overstatements, misstatements, or concrete statements about initiatives that might be rendered misleading or untrue by an adverse supplier or other event. For example, companies that publish commitments to achieve specific CSR goals/targets by certain dates may face litigation alleging misrepresentations to consumers if the goals/targets are not met. Companies should also confirm they have adequate diligence procedures in place for information in sustainability and other reports about progress on CSR goals, and consider whether to involve internal or external auditors to help verify or attest to the concrete facts and numbers included in CSR documents.

3. **Use aspirational language and estimates.** Companies should also endeavor to keep CSR statements aspirational. For example, when discussing CSR initiatives or codes of conduct, companies should favor words like "should," "expect," or "strive," as opposed to making broad and generalized assertions that the company, its employees, or its suppliers "are" in compliance or "do" comply with applicable laws and standards. Companies can also minimize litigation risk when measuring progress on CSR goals by talking about "estimates" or "approximations"--as
opposed to stating concrete measurements. Companies should also consider process-based or soft goals, rather than setting objective targets.

4. **Location matters.** Detailed CSR statements in SEC filings or on product packaging may increase the risk of litigation, as courts may presume that the statements are material or that investors and consumers relied on them. Statements on websites can also present heightened risks, particularly if products are sold through websites, as courts might presume that consumers have seen the statements before making purchases. Statements suggesting that CSR initiatives and statements are material to the company, investors, or consumers also could be problematic in litigation.

5. **Educate internally on litigation trends.** Companies should educate employees responsible for updating and preparing CSR documents about the growing risk of lawsuits based on alleged misstatements. Employees should also understand that CSR statements need to be consistent with descriptions of the company's business and material trends and risks in SEC filings. Even if CSR materials are not required in SEC filings, companies may face pressure in the future to incorporate them.

6. **Consider internal and external processes carefully.** Companies should carefully consider who signs off on CSR statements, and what role directors and senior management have in their review, if any. Companies should also carefully evaluate the role of outside CSR consultants, understanding that communications with these consultants may not be privileged, and that consultants often benchmark against other companies' CSR reports and are not always sensitized to litigation risks.

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[1] The phrase "corporate social responsibility" often encompasses a broad variety of corporate goals and initiatives, including efforts regarding environmental sustainability (such as combatting climate change and resource scarcity), human rights (including protecting human health and labor rights), responsible sourcing and audit procedures, compliance with laws in places where companies do business, and ethics and integrity.


[3] For example, the Sustainability Accounting Standards Board (SASB) has developed a voluntary reporting approach for U.S. publicly traded companies that encourages companies to identify sustainability issues material to their business and discuss their performance on those issues in their SEC filings.
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Gibson Dunn’s lawyers are available to assist in addressing any questions you may have regarding these developments. If you have any questions or would like to discuss these issues further, please feel free to contact the Gibson Dunn lawyer with whom you usually work or one of our subject matter lawyers:

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