Investors are 'flying blind' to risk of climate lawsuits, researchers say

January 12 2024

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Polluting companies could be liable for trillions in damages from climate lawsuits. But few investors and regulators are taking these risks into account when evaluating companies' climate-related financial risks, according to new Oxford Sustainable Law program research published Jan. 11 in *Science*. The research calls for an overhaul in how climate litigation risks are assessed and provides a new framework for doing so.

"Financial risk is the dominant frame through which investors and regulators engage with climate change. But climate risk analysis fails to satisfactorily account for legal developments. Against a backdrop of increasingly impactful climate litigation and regulatory enforcement actions, which shift and amplify climate risks, we argue that current climate risk assessments misrepresent the distribution and scale of climate-related financial risks.

"That means investors end up investing in the wrong projects and run risks that neither they nor regulators understand, thereby further aggravating the financial risks climate change entails," explains Associate Professor Thom Wetzer, lead author and Director of the Oxford Sustainable Law Program.

In all 2,485 climate lawsuits have been filed globally to date, and their growing impact presents significant risks for some of the world's biggest carbon emitters. For example, U.S. oil and gas giant Chevron could be liable for up to $8.5 trillion alone, according to the authors' estimates. In 1990–2019, the company's profits were $291 billion. "It's possible that Chevron's business may in fact be net value destroying," says co-author, Dr. Rupert Stuart-Smith, Senior Research Associate at the Oxford Sustainable Law Program.

The research also highlights how organizations tasked with providing frameworks for assessing climate risks, such as the International Sustainability Standards Board and The Network for Greening the Financial System, lump in legal risks with "transition risks" and provide "little to no" detail on how to evaluate them.

"This suggests they see climate litigation as merely a peripheral risk, when recent events in the courts demonstrate that it is something far greater," says co-author, Dr. Arjuna Dibley, Head of Sustainable Finance Research at Melbourne Climate Futures.

Climate litigation presents direct threats to companies through successful lawsuits, but it can also hurt businesses in other ways, including by raising borrowing costs or by forcing policy changes such as subsidy reductions, emission reductions, or enhanced disclosure requirements, say the authors. "For these reasons, conventional assessments that do not meaningfully account for the effects of litigation misrepresent the true extent of companies' climate-related financial risk," adds Dr. Stuart-Smith.

Professor Wetzer and his team set out five ways that climate-related legal risks could be assessed by investors and regulators, including market-impact analysis; analysis using the social cost of carbon; attribution of climate change damages; estimating costs of accelerated climate mitigation, and qualitative analysis.

"Policymakers, investors, and companies have accepted the need to understand climate risk exposures. But doing so diligently means engaging with the law through research that combines legal reasoning with financial analysis and climate science. Else, they will continue to fly blind in their treatment of climate risk," concludes Professor Wetzer.

More information: Thom Wetzer et al, Climate risk assessments must engage with the law, *Science* (2024). DOI: 10.1126/science.adj0598

Provided by University of Oxford