

# Exxon wins first climate change disclosure securities fraud case

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## In this Update

- On December 10, the New York Supreme Court released its decision in the ExxonMobil securities fraud case.
- The New York Attorney General had alleged that Exxon misrepresented the cost of future climate change regulations to investors.
- In emphatic terms, the New York Supreme Court dismissed the suit against Exxon.

## Introduction

The New York Attorney General's (NYAG) headline-grabbing climate change suit against ExxonMobil (Exxon) was dismissed, in emphatic terms, by the New York State Supreme Court last week. The securities fraud case alleged Exxon misrepresented the cost of future climate change regulations to investors. Justice Ostrager, referring to the NYAG's claims as "hyperbolic," found that Exxon's climate change disclosure had not misled investors.

## The allegations

Since the mid-2000s, Exxon has forecasted the impact of increased GHG regulations on the demand for oil and gas and how increased GHG regulations might affect the feasibility of future Exxon projects.

The alleged misrepresentations were contained in Exxon reports published in 2014 that were titled *Energy and Carbon – Managing the Risks* and *Energy & Climate* as well as in an annual publication titled *Outlook for Energy*. These publications outlined that Exxon used proxy costs for carbon emissions to account for anticipated increased GHG regulations when assessing oil and gas demand and when evaluating potential projects. The proxy costs outlined in the publications were estimates for 2030 and 2040.

The NYAG claimed three misrepresentations: (1) that Exxon's internal undisclosed guidance authorized applying a lower proxy cost than represented to the public; (2) Exxon did not apply proxy costs to projects in developing countries; and (3) Exxon applied lower proxy costs than it represented or no proxy costs at all in some parts of its business in developed countries, including the Alberta oil sands, and instead applied a proxy cost based on then-current regulations.

The claims against Exxon were brought pursuant to the *Martin Act* (NY Gen Bus Law, Art 23-A). The *Martin Act* requires that the NYAG show a "misrepresentation of material facts" based on a preponderance of the evidence. While reliance on the misrepresentation need not be

shown, a material fact is one that would have “actual significance in the deliberations of the reasonable shareholder.”

## The decision

Ultimately, the NYAG’s claim failed. The Supreme Court made it clear at the outset that this was not a platform for the NYAG to address climate change, writing that “this is a securities fraud case, not a climate change case.” From the judge’s perspective, the question wasn’t whether climate change is happening or who is responsible, it was whether there were material misrepresentations that could have misled investors.

The Supreme Court was not persuaded that proxy costs representing GHG regulations in 2030 and 2040 could have materially affected investor decisions in the 2013-2016 period. The proxy costs were at best an educated guess as to the economic effect of regulations in the distant future. The witnesses put forward to support the assertion that the alleged misrepresentations were material — an investment analyst who covered Exxon and an economics professor who presented an event study — were in the words of the Supreme Court “eviscerated” on cross-examination and by the Exxon expert witnesses. Further, the NYAG did not produce testimony from an investor who claimed to be misled by Exxon (despite previously representing that it would call such individuals at trial).

The Supreme Court found that the proxy cost was one of the factors that Exxon considered in forecasting future demand and, by extension, future oil and gas prices. Accordingly, since future energy prices are used to assess the economic viability of all projects, Exxon did take the proxy costs into account when assessing potential projects. Further, the Supreme Court, citing Alberta as a specific example, accepted that it was reasonable for Exxon to deviate from using the proxy cost where it had better information regarding anticipated future costs of GHG regulations for specific projects or geographies.

The allegation that proxy costs of future GHG regulations must be used uniformly by Exxon throughout its business was revealed to be in tension with SEC regulations concerning the estimation of reserves. The SEC requires that “existing economic conditions, operating methods, and government regulations [be used] in reporting proved reserves.” The Supreme Court observed that the SEC had investigated Exxon’s formal securities filings and found no impropriety. The Supreme Court further noted that the NYAG had not asserted that any of the disclosure in Exxon’s Form 10-Ks was false or misleading.

## Conclusion and implications

This decision will likely serve to dissuade regulators from advancing tenuous claims against GHG emitters relating to climate change disclosure. With that said, the NYAG investigation and claim against Exxon, together with a similar investigation in Massachusetts, reflect the prevalence of climate change suits and the risk they pose to companies in the oil and gas, energy and power industries.

Regardless of success or failure, climate change litigation can create significant expense for companies and complicate an already evolving regulatory and operating landscape. These developments reinforce the need for companies to be diligent in identifying potential climate change litigation risk.

For further information about climate change litigation and risk mitigation strategies, please contact [Colin Feasby](#) or [Matthew Huys](#).

