

Chemical Industry Update - November 2019

by Troy M. Keller, Dave Townsend, and T. Augustine Lo

Stand in the Place Where you Live

In the late 1980s, almost no antitrust enforcement cases were brought in jurisdictions outside the United States, even though active enforcement had been ongoing there for nearly 100 years. In the thirty years since, practically every developed nation has adopted an antitrust statutory regime and begun enforcing it. That timeframe may seem glacially slow, but in the regulatory world, this is in fact a relatively rapid global roll-out.

Given this reality, that law and policy developments take time, often years, REM's classic advice—to stand where you live and control what you can—has some value as a legal strategy. Consider Brexit. While the UK's exit from the European Union has threatened to upend value chains with the break-up of the European market, companies that did not panic in 2016 have now had several years to cycle through long-term agreements and mitigate foreign exchange risk, update governing law provisions, clarify force majeure clauses and broaden compliance requirements in anticipation of an additional UK layer of regulation and disrupted supply chains. The overall situation remains uncertain, and risks abound, but paying attention to the little things can pay off over time.

We believe this approach is effective with respect to most law and policy trends. Through watchful monitoring, businesses can make informed decisions about how best to position their unique product lines and be effective in their engagement with customers, suppliers, regulators and policymakers. In this issue we visit (and revisit) some legal trends that continue to be the most significant for the chemical industry. As always, don't hesitate to reach out should you have follow-up questions.

Toxic Tort Litigation Trends

There may be more behind the proliferation of product liability cases involving substances like glyphosate, PFAS, and talcum powder than one-off, product-related concerns. [This Law360 article](#) walks through some key trends influencing toxic tort litigation in the chemical industry. The article notes as a key factor that chemical

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manufacturers appear to be attractive targets in part because the universe of manufacturers is far smaller than that of all the potential sources of injury, such as the downstream players using the chemicals who are in fact more proximate to the place of injury. The article also cites a belief by some that delays in action by regulators like the Environmental Protection Agency (EPA) have led to a vacuum that courts and juries have tried to fill. The argument goes that instead of having clearly defined standards enforced by an active agency, there is now room for plaintiffs to bring claims and argue what the standards should be.

Another important trend results from more regulatory agencies (like California's Office of Environmental Health Hazard Assessment under Proposition 65) taking public health positions on particular chemicals, which affords plaintiffs persuasive authority to prove liability. Notwithstanding the fact that these health assessments should arguably be excluded as not relevant to the question of specific causation, judges have been loath to exclude them. This has put manufacturers at a severe disadvantage and emboldened plaintiffs.

We are also seeing an impact from states eliminating or loosening traditional bars to these types of claims. This New York law, adopted last week, is a real-time example. By increasing the statute of limitations period, the pool of available plaintiffs is likely to expand. Unfortunately, with these and other trends seem to be creating an environment that promotes product liability claims against the industry.

For more information, contact Jon Williams.

Global Trade Update

Attention from the business community will focus this month on the expected announcement of "Phase One" of a U.S.-China agreement to begin reducing trade frictions between the countries, which have led to reciprocal tariffs, reduced Chinese purchases of American exports, and other forms of retaliation during the past two years. Expected to be signed in November or December 2019, neither side has disclosed the full details of the agreement. According to recent statements from U.S. officials, Phase One potentially involves an agreement to remove some of the "Section 301" tariffs on imports into the United States of Chinese origin goods in exchange for Chinese commitments to purchase U.S. agricultural goods. However, the White House has equivocated on the extent of the tariff relief, if any. Phase One is intended to set the stage for Phase Two, which the Trump administration hopes will result in broader Chinese commitments related to protection of U.S. intellectual property rights and elimination of subsidies for Chinese businesses. As of today, nearly all goods between the two countries are subject to Section 301 tariffs, with a final tranche scheduled for December 15 that will impact a wide range of household goods purchased in the United States as well as a number of chemical products.

Several other significant international trade developments occurred in October that could affect the chemical industry.

- China gained World Trade Organization (WTO) approval to retaliate against \$3.5 billion worth of U.S. goods because of the continued use of “zeroing” in U.S. antidumping proceedings, which leads to the calculation of higher antidumping duty rates on Chinese goods. Now that China has won this WTO approval, China may impose tariffs on U.S. goods, possibly tariffs far in excess of tariffs already imposed as a result of the U.S.-China trade dispute (see above). China’s authority to impose these tariffs, consistent with WTO rules, would remain even after the United States and China reach an agreement to resolve the ongoing U.S.-China trade dispute, unless the two countries specifically resolve this separate WTO dispute as part of the agreement.
- A WTO panel found that India’s export subsidies, including those that benefit Indian producers of chemicals, are illegal under the WTO Agreement on Subsidies and Countervailing Measures. India can appeal the panel’s decision to the WTO Appellate Body. According to USTR, the value of subsidies provided to Indian businesses is \$7 billion annually, and include those to Indian chemical producers. The specific Indian programs at issue are: the Merchandise Exports from India Scheme (MEIS); Export Oriented Units Scheme and related sector specific schemes (EOU); Special Economic Zones (SEZ); Export Promotion Capital Goods Scheme (EPCG); and a duty free imports for exporters program (DFIS). Detailed information about the dispute can be found at the WTO’s website, [here](#).
- The U.S. Trade Representative (USTR) revoked Thailand’s benefits under the Generalized System of Preferences (GSP) for \$1.3 billion in annual imports into the United States from Thailand. A list of goods impacted is available [here](#). USTR’s decision resulted from a petition from the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) alleging violations of workers and human rights in Thailand. Thailand is one of the largest GSP beneficiary, with \$4.4 billion in annual trade from Thailand benefiting from GSP. USTR also announced new GSP reviews of South Africa and Azerbaijan, which could result in changes to their status under the GSP. Details from USTR can be found [here](#).

For more information, contact [Dave Townsend](#) and [Augustine Lo](#).

Retail Regulation Trends

Continuing the retail regulation trend, Staples recently announced a [detailed chemicals policy](#). Among the chemicals listed as priority items and targeted for elimination in its products are PFAS, BPA, nonylphenol and nonylphenol ethoxylates, all organohalogen, halogenated and organophosphate flame retardants, a number of biocides, phthalates, solvents and other chemicals.

The Staples announcement is the latest among major retailers no longer deferring to or waiting for governmental regulators. Target and Walmart adopted chemicals policies in 2017, and Amazon and Walgreens adopted theirs in 2018. A long list of retailers have followed suit in the ensuing months. This trend is the new reality for the industry and adds to the complexities of managing a modern-day chemical company, with the constant need to reformulate and find solutions that work within a layered regime of governmental regulation, retail policies and NGO advocacy.

For more information, contact [Troy Keller](#).

Tech Policy

While typically not the targets of these policies, chemical companies nonetheless bear the burden of dealing with new regulations in areas like data privacy, data ownership, content monitoring and competition law. These policies can have an outsized effect on the chemical industry due to its global nature, with products constantly moving back and forth across borders at various steps in the value chain.

This recent article in Politico EU argues that in the battle over tech leadership, the EU is considering more aggressive and potentially protectionist tech policies. A more idealistic but still interesting read was this article from the WSJ. The EU's success with GDPR may accelerate trends into areas like antitrust and data localization, a particularly scary one. Like any global industry, the chemical industry manages personal data of employees and contractors around the world. Add on top of that a high volume of cross-border commercial transactions involving highly regulated materials, and the personal and commercial data flow is tremendous. Digitalization, frequently pointed to as a future source of cost savings and efficiency for the industry, could be upended or at least delayed by higher compliance costs and limited operational flexibility as a result of aggressive tech policies.

For more information, contact Troy Keller.

In Case You Missed It

Updated Proxy Rules. The SEC continues to shake up the U.S. proxy process. In their hearing this week, the Commission proposed rules requiring disclosures of conflicts of interest, revising the share ownership thresholds for making a proposal and the approval thresholds for making repeat proposals. Shareholder proposals will remain a popular tool of shareholder activism, but these changes could certainly reduce some of the leverage proponents and proxy advisors have been accumulating over the years.

CCPA Rulemaking. California is in the process of adopting additional rules to clarify aspects of the California Consumer Protection Act of 2018. These rules will help in some respects but fall far short of what is needed.

PRC Trademark Law Updates. China recently announced revisions to its trademark laws to clamp down on bad faith applications. The changes also increase the maximum amount for statutory damages for trademark infringement from RMB 3 million (~US\$425K) to RMB 5 million (~USD710K), and the maximum punitive multiplier is increased from three to five (Article 63).

China Opens up Investment Opportunities. Via a collection of changes to previous rules restricting foreign access to certain end markets and trade zone opportunities, China has made moves to invite foreign investment in ways it has not before.

CFIUS Rules Released. Long-awaited rules implementing the Foreign Investment Risk Review Modernization Act of 2018 were released in October. The rules expand both the

scope and nature of review of foreign investments into the U.S.

CORPORATE LAW

M&A and the Evaluation of Corporate Compliance Programs

Acquisitions of chemical companies, especially target companies with international operations, require buyers to carefully scrutinize the target's compliance programs, including the target's compliance with the U.S. Foreign Corrupt Practices Act and other anti-bribery and anti-corruption laws. Doing so enables the buyer to more accurately assess the target's value and risk profile, negotiate for the costs of any misconduct to be borne by the sellers and evaluate whether remedial steps are needed.

When designing and executing a pre-M&A due diligence process on compliance-related matters and evaluating how to mitigate potential post-closing liabilities, buyers should consider the U.S. Department of Justice's updated guidance on the evaluation of corporate compliance programs, which was released in April 2019. The DOJ guidance document is aimed at prosecutors making decisions as to whether, and to what extent, a corporation's compliance program is adequate and effective. Under the DOJ's principles for the prosecution of business organizations, the adequacy and effectiveness of a corporation's compliance program is one of the factors that prosecutors should consider when conducting a corporate investigation, making charging decisions and determining the appropriate form of any monetary penalties or other enforcement action.

The guidance clearly indicates that the DOJ expects a buyer to conduct comprehensive due diligence of any acquisition targets. It provides, "flawed or incomplete due diligence can allow misconduct to continue at the target company, causing resulting harm to a business's profitability and reputation and risking civil and criminal liability." Among the questions prosecutors will consider when evaluating whether a buyer subjected an acquired business to appropriate scrutiny are the following:

- **"Due Diligence Process** – Was the misconduct or the risk of misconduct identified during due diligence? Who conducted the risk review for the acquired/merged entities and how was it done? What is the M&A due diligence process generally?
- **Integration in the M&A Process** – How has the compliance function been integrated into the merger, acquisition, and integration process?
- **Process Connecting Due Diligence to Implementation** – What has been the company's process for tracking and remediating misconduct or misconduct risks identified during the due diligence process? What has been the company's process for implementing compliance policies and procedures at new entities?"

The DOJ's guidance provides a reminder of the importance of assembling the right team of subject matter experts and prioritizing the analysis of compliance risks when planning and conducting pre-M&A due diligence. Buyers should also consider whether, based on the target's business and the regulatory environment in which it operates, enhanced due diligence is appropriate in certain jurisdictions or regarding particular compliance risks. Prospective sellers should anticipate greater scrutiny and earlier buyer inquiries in these areas, and ensure that remedial actions are taken to address any deficiencies.

For more information, contact [Edward Davis](#).

Exxon's Climate Change Trial

The trial in the case brought by the New York Attorney General's office over whether Exxon misled investors with respect to the potential impact of climate change on its business has had some dramatic twists and turns. The state trial court judge, Justice Barry Ostrager, expressed skepticism with one of the State's experts and at one point threatened to cut the AG's case off if it didn't manage the timing of its witnesses better. During closing arguments, the AG's office said they were dropping their claims for common law fraud and equitable fraud, resulting in outrage from Exxon's counsel that the AG's office is at this late stage "not pressing the two claims that have cost in many respects the most severe reputational harm to the company."

A decision is expected in about a month. However the trial turns out, the genie is to some extent out of the bottle. The Massachusetts Attorney General's office filed a case in October similar to the New York case, though expanded to include consumer claims. Several cases have been brought by private litigants in other states based on securities law claims and one as a derivative suit. Whether these types of claims turn into a broader trend beyond Exxon, however, may depend on how the New York case turns out.

Disclosure trends in the chemical industry could also be affected. One ground-breaking aspect of this case has been the baseline question of whether climate change disclosures can create liability under securities laws. For years, companies have been creating sustainability reports discussing the impact of their operations on the environment, but this case asks whether a company could face liability for failing to accurately assess and disclose the effects of climate change and related environmental policies *on the company's financial prospects*.

Such disclosure is a tall order. Many companies in the chemical industry already include high level risk factor disclosure regarding climate change, but getting more specific would require data that is not readily available and perhaps a new accounting framework in which to report it. Under Chairman Clayton, the SEC has declined to look seriously at adopting such specific requirements. The idea could gain momentum if plaintiffs start to make headway.

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