

# Non-Legal Advice: How Attorneys Counsel Clients on Investors' ESG Demands

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## INTRODUCTION

In 1970, Milton Friedman, an economist at the University of Chicago, published “A Friedman doctrine – The Social Responsibility of Business Is to Increase Its Profits” in the *New York Times*, in which he argued that companies should focus exclusively on providing financial benefits to their shareholders.<sup>1</sup> In August 2019, the Milton Friedman doctrine was forcefully rejected by the Business Roundtable (“BRT”) when they revised their Principles of Corporate Governance (“BRT Principles”) to redefine that the purpose of a corporation is to “deliver value to all” stakeholders, including customers, employees, suppliers, communities, and shareholders.<sup>2</sup> The CEOs from 181 publicly traded companies signed the BRT’s revised BRT Principles.<sup>3</sup> Companies switched their focus from “shareholders” to “all stakeholders,” and the updated BRT Principles advise corporations to “deliver value to customers, invest in employees, deal fairly and ethically with suppliers, support the communities in which they work, and generate long-term value for shareholders.”<sup>4</sup> Many, however, find the BRT Principles and other similar statements, such as social media posts promising to support racial justice, to have been more performative than substantive.<sup>5</sup>

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1. Milton Friedman, *A Friedman doctrine– The Social Responsibility of Business is to Increase Its Profits*, *N.Y. TIMES* (Sept. 13, 1970) § SM (Magazine), at 22, <https://timesmachine.nytimes.com/timesmachine/1970/09/13/issue.html> [<https://perma.cc/WE5J-BMJZ>].

2. *Business Roundtable Redefines the Purpose of a Corporation to Promote ‘An Economy That Serves All Americans’*, *BUSINESS ROUNDTABLE* (Aug. 2019). See generally STATEMENT ON THE PURPOSE OF A CORPORATION, *BUSINESS ROUNDTABLE* (DATE?), <https://opportunity.businessroundtable.org/ourcommitment/> [<https://perma.cc/5B9L-3PJ7>].

3. KKS Advisors & Test of Corporate Purpose, *COVID-19 and Inequality: A Test of Corporate Purpose*, 6 (Sept. 2020), [https://c6a26163-5098-4e74-89da-9f6c9cc2e20c.filesusr.com/ugd/f64551\\_67ddb692f7d476e971388737ecfbf77.pdf](https://c6a26163-5098-4e74-89da-9f6c9cc2e20c.filesusr.com/ugd/f64551_67ddb692f7d476e971388737ecfbf77.pdf) [<https://perma.cc/F39Y-Z2CA>].

4. *Id.* at 23.

5. See, e.g., Peter S. Goodman, *Stakeholder Capitalism Gets a Report Card. It’s Not Good.*, *N.Y. TIMES* (Sept. 22, 2020, updated Dec. 2, 2020) (finding that signatories to the BRT Principles have performed no better than other companies. Shareholders, during the COVID-19 pandemic, have “suffered initial plunges in asset values but then recovered; tens of millions of wage-earners remain jobless, massing at food banks”); Lucien Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholders Governance*, *HARV. L. SCH. F. ON CORP. GOVERNANCE* (2020) (asserting in a blog post summarizing their forthcoming Cornell Law Review article that the BRT Principles should “not be expected, and was largely not intended by its signatories, to bring about major changes in the treatment of stakeholders”); Letter from Senator Elizabeth Warren to Business

The relevance and importance of ESG is skyrocketing.<sup>6</sup> ESG stands for “environmental, social and corporate governance.” The “environmental” prong includes greenhouse gas emissions, energy efficiency, and waste management.<sup>7</sup> The “social” prong includes human rights, labor standards, and employee relations.<sup>8</sup> Finally, the “corporate governance” prong includes board diversity, executive pay, and bribery/corruption.<sup>9</sup> ESG investing considers these three criteria—environmental, social, and governance—when making investments while also considering financial returns.<sup>10</sup> ESG investing is premised on the assumption that ESG practices have positive effects, at least in the long-term, on the financial performance of a company.<sup>11</sup> Often it is considering these criteria in light of the fact that they can have long-term effects on the financials.<sup>12</sup> For example, as the world moves toward renewable energy, ESG considerations help investors understand that oil and gas may not be as profitable as it once was; solar or wind energy might be extremely profitable in a decade.<sup>13</sup>

Roundtable (Sept. 17, 2020) (urging BRT signatories to take more concrete efforts, especially record and publicly report the specific efforts they are taking to end their contributions to systematic racial inequality).

6. See, e.g., Rhea Rao, *How Shops Recruit for ESG Roles*, IGNITES (Nov. 16, 2020) (noting there is a “growing interest in sustainable investing” that has required asset managers to hire ESG-focused professionals).

7. *How has COVID-19 impacted ESG investing?*, UBS (2020), <https://www.ubs.com/global/en/asset-management/insights/panorama/mid-year/2020/covid-19-impacted-esg-investing.html> [<https://perma.cc/L2ZE-Q8UK>] [hereinafter UBS REPORT ON COVID-19 IMPACTS].

8. *Id.*

9. *Id.*

10. See Riccardo Boffo & Robert Patalano, *ESG Investing: Practices, Progress and Challenges*, OECD PARIS, 6 (2020), <https://www.oecd.org/finance/ESG-Investing-Practices-Progress-Challenges.pdf> [<https://perma.cc/KAR4-JSEA>].

11. See, e.g., *Crisis as Catalyst: Corporate Resiliency and the Future of ESG*, STATE STREET, 6 (2020) <https://www.statestreet.com/content/dam/statestreet/documents/Articles/Crisis-as-Catalyst-Corporate-Responsibility-and-ESG-George-Serafeim.pdf> [<https://perma.cc/MNZ8-2SJ8>] (acknowledging that quarterly earnings calls are short-term performance based, whereas ESG are inherently longer term); Edelman Trust Barometer 2020, *Special Report: Institutional Investors*, 15 EDELMAN? (2020), <https://perma.cc/Z3MR-VBBS> (88% of US investors agree that “companies that prioritize ESG initiatives represent better opportunities for long-term returns than companies that do not”).

12. See, e.g., UBS REPORT ON COVID-19 IMPACTS, *supra* note 7 (“ESG investing is based on the assumption that ESG factors have financial relevance.”).

13. See, e.g., Letter from Engine No. 1 GP LLC to Exxon Mobil Corp. (Dec. 7, 2020) (letter from Engine No. One, in coordination with one of Exxon’s largest investors, the California State Teachers’ Retirement System, to Board of Exxon Mobil Corporation illustrating their atrocious financial performance and urging Exxon to consider adding four new independent directors with energy industry experience to its Board); Clifford Krauss, *U.S. and European Oil Giants Go Different Ways on Climate Change*, N.Y. TIMES (Sept. 21, 2020, updated Dec. 11, 2020) (noting that while European-based energy companies are “selling off oil fields, planning a sharp reduction in emissions and investing billions in renewable energy,” American energy companies are “doubling down on oil and natural gas”); Anne Barnard, *New York’s \$226 Billion Pension Fund Is Dropping Fossil Fuel Stocks*, N.Y. TIMES (Dec. 9, 2020) (stating that New York State’s pension fund is dropping “many of its fossil fuel stocks in the next five years and [selling] its shares in other companies that contribute to global warming”).

While there is significant debate, extensive research, and ongoing inquiry into the financial impact of considering ESG when making investment decisions,<sup>14</sup> many scholars agree that ESG considerations can be beneficial on “bottom-line” financial returns for a plethora of reasons.<sup>15</sup> This Note, however, does not address these questions of financial performance, yet it relies on the assumption that, in general, ESG considerations are beneficial to most companies and their investors.

Instead, this Note argues that due to the increasing importance of ESG policies, practices, and investments, both in-house and external counsel to investment firms should more forcefully advise their clients to consider investors’ ESG demands when making investment decisions. Part I will discuss ESG and the debate over which entities should hold firms accountable, focusing on large institutional investors. Part II will briefly discuss the impact of the COVID-19 pandemic and how both the pandemic and racial justice movements have skyrocketed the support for ESG from many customers, consumers, and employees. Part III will discuss several instances in which Model Rule 2.1, which allows, but does not require, attorneys to offer non-legal advice, has been applied in the ESG context. Finally, Part IV will discuss how Model Rule 2.1 impacts attorneys advising investment firms on ESG considerations, and will urge attorneys to take a more forceful role in advising their clients to strongly consider, respond to, and implement investor demands for strong ESG practices and procedures.

## I. ESG - DEBATE OVER WHO SHOULD HOLD CORPORATIONS ACCOUNTABLE

ESG has, in recent years, but especially in 2020, become a priority for investors, employees, and customers alike.<sup>16</sup> Who should hold corporations accountable for broader consideration of ESG? Some of the most relevant actors in this debate include the government, employees and customers, and investors;<sup>17</sup> but, note that

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14. See, e.g., Jan-Carl Plagge & Douglas M. Grim, Vanguard, *Have Investors Paid a Performance Price? Examining the Behavior of ESG Equity Funds*, 46 J. PORTFOLIO MGMT. (2020) (finding that the majority of equity funds have not been found to produce statistically significant positive or negative alpha); Gunnar Friede, Timo Busch & Alexander Bassen, *ESG and financial performance: aggregated evidence from more than 2000 empirical studies*, 5 J. SUSTAINABLE FIN. & INV. 210, 211 (2015) (finding, when aggregating 2,000+ studies of the financial effects of considering ESG when making investments, that 90% of studies have found a “non-negative” ESG and corporate financial performance relation).

15. Chris Brummer & Leo E. Strine, *Duty and Diversity*, FACULTY SCHOLARSHIP PA. LAW. 2255. at 26 (Feb. 2021); see also Paul Sullivan, *Investing in Social Good Is Finally Becoming Profitable*, N.Y. TIMES (Aug. 28, 2020).

16. See Dan Clark, *Investors Are Noticing Social Justice Benchmarks More in Corporate ESG Efforts*, LAW.COM (Oct. 13, 2020) (paraphrasing Paul Davies, partner, Latham & Watkins LLP); see also Lisa Lee, *Carlyle Inks \$4.1 Billion Credit Line Linked to Board Diversity*, BLOOMBERG (Feb. 17, 2021) (noting that Carlyle’s credit line ties borrowing costs to specific milestones for the diversity of its portfolio companies’ boards).

17. See Kristen Sullivan, Amy Silverstein, & Leeann Galezio Arthur, *ESG and Corporate Purpose in a Disrupted World*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 10, 2020) (noting that, “[i]n the United States, much of the current focus on corporate purpose and ESG is likely to continue to be driven by investors rather than regulators or legislators in the near term”); Brummer & Strine, *supra* note 15 at 38, 49–50

there are some surprising players, including the Vatican<sup>18</sup> and stock exchanges.<sup>19</sup> While this push should, and does, come from many directions (many of which will be at least briefly discussed in this Note), the focus of this Note will be on pressure coming from investors, and more specifically, large institutional investors.

#### A. RECENT GOVERNMENT RULES AND THEIR IMPLICATIONS ON ESG

Both the Securities and Exchange Commission (“SEC”) and the Department of Labor (“DOL”) can impact ESG. Under the Trump administration, the SEC implemented a rule that increases shareholder resolution requirements.<sup>20</sup> This rule has two main implications. First, it increases both the monetary and time amount that investors must give before submitting a proposal.<sup>21</sup> This reduces the influence of smaller investors on promoting companies to advance ESG policies.<sup>22</sup> Second, it increases the “resubmission” threshold of a proposal to three years; proposals cannot be resubmitted for three years “if they fail to gain traction and don’t receive a certain threshold of support.”<sup>23</sup> An investigation by Bloomberg discovered that the driving force behind this proposed rule was a group of oil and gas interests, some of whom are signatories to the BRT Principles.<sup>24</sup> Such companies justify their decision as serving to “free up time for

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(discussing the impact of firm reputation on customers, employees, and investors, as well as the SEC’s board diversity disclosure rules).

18. *Council Commitment Index*, COUNCIL FOR INCLUSIVE CAPITALISM WITH VATICAN, [https://www.inclusivecapitalism.com/commitments/?campaign\\_id=4&emc=edit\\_dk\\_20201208&instance\\_id=24819&n=dealbook&regi\\_id=142186690&segment\\_id=46330&te=1&user\\_id=a135da1f2a395223cc144e313ce03778](https://www.inclusivecapitalism.com/commitments/?campaign_id=4&emc=edit_dk_20201208&instance_id=24819&n=dealbook&regi_id=142186690&segment_id=46330&te=1&user_id=a135da1f2a395223cc144e313ce03778) [https://perma.cc/VJW2-2TBS] (listing the commitments offered by certain firms to the Vatican to “advance inclusive capitalism”); Jim Yardley & Binyamin Appelbaum, *In Fiery Speeches, Francis Excoriates Global Capitalism*, N.Y. TIMES (July 11, 2015) (discussing the Pope’s calls to action against capitalism).

19. See generally Nasdaq, Proposal to SEC (Dec. 1, 2020) (“A proposal to advance board diversity and enhance transparency of diversity statistics through new proposed listing requirements.”); see also Phillip Bantz, *What In-House Leaders Should Know About Nasdaq’s Proposed Board Diversity Rules*, LAW.COM (Dec. 2, 2020); Susan Bokermann, *Analysis: New Long-Term Stock Exchange Could Boost PBCs and ESG*, BLOOMBERG (Sept. 15, 2020) (noting that companies on the LTSE are committed to long-term value and sustainable business).

20. Press Release, Securities and Exchange Comm., SEC Adopts Amendments to Modernize Shareholder Proposal Rule (Sept. 23, 2020); see also Douglas MacMillan, *Small investors have pushed companies toward social change. A New SEC rule will limit their influence.*, WASH. POST (Sept. 25, 2020). The rule was approved in a 3-2 vote. Chairman Jay Clayton supported the rule as “modernizing” policies that had not been revised in decades and said it reduces the risk that “shareholder-proponents would use the proposal process in a way that does not benefit the company or its other shareholders.” *Id.* Dissenting Commissioner Allison Herren Lee disagreed, claiming the new rule is detrimental to ESG efforts and disadvantages small investors. *Id.*

21. MacMillan, *supra* note 20 (explaining that the new rule, which previously required investors to hold only \$2,000 worth of stock for one year, now requires investors to hold \$25,000 worth of stock for one year, \$15,000 for two years, or \$2,000 for three years).

22. *Id.*

23. Rhea Rao, *SEC Rule May Stop New ESG Issues From Gaining Traction*, IGNITES (Nov. 30, 2020) (pointing out that this new rule would make 27% of ESG shareholder proposals voted on in 2020 ineligible from consideration if the rule was already in place).

24. KKS Advisors & Test of Corporate Purpose, *supra* note 3, at 12.

management teams and shareholders who are bogged down by these votes each year,” but many criticized the supposed contradiction between the BRT Principles’ support to protect the environment and these signatories advocacy for and support of the new SEC rule.<sup>25</sup>

The DOL, under the Trump administration, implemented a rule regarding ERISA plan fiduciary duties; the final rule states that investment professionals are fiduciaries and therefore must act in the retirement investors’ best interest.<sup>26</sup> Essentially, ERISA plan fiduciaries are unable to invest in ESG vehicles if the investment would reduce their risk-adjusted returns; however, in response to an aggressive notice and comment process, the rule no longer explicitly references ESG or ESG-themed funds, but rather restrains ERISA plan fiduciaries from making an investment for any reason that would reduce risk-adjusted returns.<sup>27</sup> Still, however, the DOL claims they only removed the language because there is no generally accepted definition of ESG.<sup>28</sup> The bill “raises the bar for considering ESG” when making investment decisions<sup>29</sup> by prohibiting ERISA plans from casting proxy votes in support of ESG initiatives unless the vote also benefits the bottom-line financials.<sup>30</sup>

There is, however, an expectation that the Biden administration will prioritize increasing and standardizing the required ESG disclosures.<sup>31</sup> Most in the industry back such changes of heightened disclosure.<sup>32</sup> It is also expected that both aforementioned bills—the SEC rule and the DOL rule—will be overturned.<sup>33</sup> There are intentions in Congress to prevent the implementation of the two new rules through legislation.<sup>34</sup> A bill proposed by several members of the House of Representatives requires asset managers, investment advisors, and retirement plan fiduciaries to “divulge how they incorporate environmental, social, and governance factors into investment decisions.”<sup>35</sup> These bills, if passed, would

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25. MacMillan, *supra* note 21.

26. 29 C.F.R. 2509, 72846–48 (Nov. 2020).

27. See Paul A. Davies, Nicola Higgs, Kristina S. Wyatt & Deric Behar, *Latham & Watkins Discusses Department of Labor Rule on ESG Investing*, CLS BLUE SKY BLOG (Nov. 2020).

28. Beagan Wilcox Volz, *DOL Finalizes ESG Rule, With Tweaks*, IGNITES (Nov. 2, 2020) (quoting an announcement from the DOL).

29. Rheaa Rao, *Dems Float Bills Requiring Shops, Plan Fiduciaries to Weigh ESG*, IGNITES (Dec. 16, 2020).

30. See, e.g., Emily Brill, *DOL Finalizes Ban on Socially Conscious ERISA Proxy Votes*, LAW360 (Dec. 11, 2020).

31. David Isenberg, *Biden’s SEC May Target ESG, Proxies, Reg BI: Lawyers*, IGNITES (Nov. 11, 2020) (stating that Biden, on his first day in office, is also expected to sign an executive order requiring “public companies to disclose climate-related financial risks” and “greenhouse gas emission data”).

32. Isenberg, *supra* note 31 (paraphrasing John Baker, of counsel, Stradley Ronon); see also Task Force on Climate-Related Financial Disclosures, <https://www.fsb-tcfd.org> [<https://perma.cc/VG4Y-QL79>].

33. David Isenberg, *Dem-Controlled Congress Could Unwind Trump-Era SEC, DOL Rules*, IGNITES (Jan. 7, 2021); Rheaa Rao, *Biden to Order Review of DOL’s ESG Rule*, IGNITES (Jan. 21, 2020).

34. Rao, *supra* note 29.

35. *Id.*

overrule the recently passed DOL rule.<sup>36</sup> Many believe that the Biden administration, combined with Democratic-controlled House and Senate will lead to a quick unwinding of both the DOL's fiduciary rule and SEC's proxy-voting thresholds.<sup>37</sup>

#### B. CUSTOMERS AND EMPLOYEES DEMAND COMPANIES TO HAVE VALUES AND ROBUST ESG POLICIES AND PRACTICES

Increasingly, customers and employees of firms play a large role in demanding robust ESG policies and practices.<sup>38</sup> Individual consumers of products can use their purchasing power to support certain corporations at the expense of others.<sup>39</sup> Customers will be loyal to particular firms that espouse particular values.<sup>40</sup> Especially with large companies, any charitable or philanthropic efforts can help "humanize" such companies; though, it is important that such companies actually act on their words.<sup>41</sup> Any scandals that occur, often with respect to diversity and racial issues, can have detrimental effects on a company's financials and overall success as customers take their money to competitors.<sup>42</sup>

Employees can similarly choose to provide labor for companies whose values align with their own.<sup>43</sup> In order for companies to attract and retain talented employees, companies must consider the preferences of such individuals.<sup>44</sup> A

36. See Kristina M. Zanotti, Karishma Shah Page, & Robert L. Sichel, *Trump Era DOL Rules – Will They Remain Under a Biden Administration?*, K&L GATES (Jan. 4, 2021), <https://www.klgates.com/Trump-Era-DOL-Rules-Will-They-Remain-Under-a-Biden-Administration-1-4-2021> [<https://perma.cc/6JZL-66XD>]; Isenberg, *supra* note 33 (arguing that now that Democrats have control of the Senate, "the door opens for them to undo unpopular rules that were finalized during the Trump administration").

37. Isenberg, *supra* note 33; see also Ben Edwards, Law Professor, Univ. Nev. Las Vegas, (@BenPEdwards), TWITTER (Jan. 6, 2021, 12:31 AM) ("[i]f the votes hold, this could unwind the DOL's fake-dutary rule."), <https://twitter.com/BenPEdwards/status/1346690739783127042> [<https://perma.cc/9JT9-C7AB>].

38. See, e.g., David Gelles, *Patagonia's Former C.E.O. Retreats to the Rainforest*, N.Y. TIMES (Feb. 18, 2021, updated Feb. 19, 2021) (quoting former Patagonia CEO Rose Marcario, "[s]ome amazing C.E.O. opportunities came to me, but they were in retail brands and other companies that I felt like were more contributing to our environmental problems and not solving them").

39. See, e.g., Brummer & Strine, *supra* note 15, at 40-41.

40. See, e.g., *BKI Brand Study: How Patagonia Builds Brand Loyalty*, BOUVIER KELLY (Jan. 4, 2019) (citing a study that, when choosing between two brands of equal quality and cost, 90% of consumers supported the brand that was aligned with a charitable cause); Clark, *supra* note 16 (paraphrasing Carol Ward, corporate governance leader, Corporate Governance Partners Inc.).

41. BOUVIER KELLY, *supra* note 40.

42. See, e.g., Chauncey Alcorn, *Papa John's is still haunted by its founder using the n-word*, CNN BUSINESS (Nov. 5, 2019). After Papa John's CEO criticizing NFL player Colin Kaepernick's anti-police brutality protests and using a racial slur during an internal diversity training meeting, sales slumped. In 2019, "an estimated 25-30% of franchisees failed to make a profit due to declining sales." *Id.*; see also Michael Barzuza, Quinn Curtin, & David H. Webber, *Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance*, 153 (October 2020) (noting that competitors capitalized on Papa John's public relations scandal by engaging in "Twitter wars").

43. Brummer & Strine, *supra* note 15, at 39-40.

44. Alan Kohll, *What Employees Really Want At Work*, FORBES (July 10, 2018) (citing a study finding that one of the most "underrated desire[s] of modern-day employees is the desire to work with purpose" because without a sense of purpose, "it's difficult for employees to connect with their work and their company").



diverse workforce is vital to attracting top talent.<sup>45</sup> In the face of scandals, employees can be instrumental in persuading a firm to change its policies or actions.<sup>46</sup> Many top employees have publicly left firms because the firm took actions that employees did not morally or ethically agree with.<sup>47</sup>

### C. INSTITUTIONAL INVESTORS RECENT TREND

The focus of this Note, however, is the pressure coming from investors. Institutional investor interest in ESG is at an all-time high.<sup>48</sup> Why? Societal pressure is certainly important, because investors are often compiled of large groups of retail investors that are increasingly cognizant and supportive of ESG.<sup>49</sup> Millennials and Gen Z, in particular, tend to prefer being customers, employees, and investors of companies whose values align with their own.<sup>50</sup> Many institutional investors also eventually need an exit opportunity from their investment, such as an IPO, in order to provide returns to their investors; by investing in companies with robust ESG practices, there will likely be more retail interest during the IPO process and therefore an easier and more lucrative exit process for the institutional investor.<sup>51</sup>

The trend toward investors focused on ESG was initially led by European public pension plans, specifically the pension plans of Nordic countries.<sup>52</sup> U.S. public pension plans were quick to follow, though not to nearly as drastic an extent, especially because of the different regulatory regimes in the United States versus

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45. See, e.g., *Over 86% of Job Seekers Say Workplace Diversity Is an Important Factor When Looking for a Job*, CISION PR NEWSWIRE (Nov. 25, 2019); Ruth Umoh, *75% of senior execs say they'd leave their company for one that values diversity*, CNBC (July 26, 2017).

46. Rakeen Mabud, *Two Lessons From The Wayfair Walkout*, FORBES (July 12, 2019) (using the Wayfair employee walk-out as an indicator that employees are “willing and able to use organizing for issues beyond those that directly affect them”).

47. See, e.g., Jessica Sidman, *The Entire Staff Quit Over This Coffee Shop's Racist and Covid-Denying Tweets. The Owner Claims They're Not His*, WASHINGTONIAN (June 16, 2020) (detailing why the entire staff at an Arlington, Virginia coffee shop quit after the owner allegedly liked and retweeted racist tweets about the BLM movement and George Floyd, as well as tweets denying the deadly COVID-19 pandemic).

48. See, e.g., MacMillan, *supra* note 21.

49. See, e.g., Clare Connellan, Maia Gez, Seth Kerschner, & Jacquelyn MacLennan, *ESG takes center stage amid economic crisis and social unrest*, WHITE & CASE LLP (Aug. 7, 2020); Larry Fink, *Larry Fink's 2021 Letter to CEOs* (2021), <https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter> [<https://perma.cc/43EW-VA8T>]. *But see* Barzuza, Curtin, & Webber, *supra* note 42, at 106 (acknowledging that index funds sometimes actually receive political backlash, not support, when they intervene with management decisions on ESG issues).

50. Barzuza, Curtin, & Webber *supra* note 42 at 140 (noting that while not indifferent to investment returns, millennials are “less focused on their investment returns than any generation”).

51. See, e.g., Betsy Atkins, *Strong ESG Practices Can Benefit Companies and Investors: Here's How*, NASDAQ (June 5, 2018) (discussing that “[s]trong ESG practices can increase stock liquidity” and “unlock competitive value”).

52. See, e.g., *Climate change higher on agenda of European pension investors*, CONSULTANCY.EU (Nov. 11, 2020) (discussing two new regulatory frameworks in Europe: The 2017 European Pensions Directive and the UK Department for Work and Pensions Investment Regulations, “both of which make ESG factors a mandatory consideration for pension fund investments”).

the European Union and United Kingdom.<sup>53</sup> More recently, educational endowments and sovereign wealth funds have also focused on ESG when making investments.<sup>54</sup> A report by Blackrock found that U.K. public pension schemes are also driving the shift.<sup>55</sup> Lastly, index funds are playing a powerful role; specifically, the so-called “Big Three”: BlackRock, Vanguard, and State Street.<sup>56</sup> One important caveat is that investors who receive carried interest, such as private equity and hedge funds, are less likely than index funds to cater to investor demands.<sup>57</sup> While index funds simply seek to match market performance and therefore are more concerned with the monetary amount of investments they receive,<sup>58</sup> carry-based funds typically receive 20% of the fund’s returns and therefore are much more financially dependent on fund performance.<sup>59</sup>

Common ownership of competitor companies by large institutional investors is incredibly impactful in pushing corporations toward ESG because, all else equal (price, quality, etc.), customers and employees will likely flock to the company who has “better” policies and practices.<sup>60</sup> Scholars generally focus on three types of investors: large index asset managers (Blackrock, State Street, and Vanguard), active institutional investors that are “quasi-index” (Fidelity, JPM, BNY Mellon, and Northern Trust), and large pension funds (Norges Bank Investment Management, AP, and New York Common Retirement Fund).<sup>61</sup> There is,

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53. Alastair March, *U.S. Falls Further Behind Europe in Fast-Growing ESG Market*, BLOOMBERG (Dec. 21, 2020) (noting that in sustainable funds, “inflows to European offerings were about five times larger than investments in the U.S.” in 2020).

54. See, e.g., Bhakti Mirchandani, *Sustainable Investing at Endowments and Foundations: What It Is And What it Takes*, FORBES (Sept. 4, 2019).

55. Thomas Fekete, *Sustainable Investing: enduring through COVID-19 and beyond*, BLACKROCK (Apr. 28, 2020), <https://www.blackrock.com/institutions/en-gb/our-clients/defined-contribution/esg-amid-covid-and-beyond> [https://perma.cc/D7AQ-4R2C]; see also Gwladys Fouche, *Exclusive: Norway wealth fund tells firms: put more women on your boards*, REUTERS (Feb. 15, 2021) (noting that “Norway’s \$1.3 trillion sovereign wealth fund, the world’s largest, wants the companies it invests in globally to boost the number of women on their boards and to consider setting targets if fewer than 30% of their directors are female”).

56. Barzuza, Curtin, & Webber, *supra* note 42 at 103; see also Fink, *supra* note 49; Amy Harder, *BlackRock unveils new way to assess climate investment risk*, AXIOS (Dec. 1, 2020) (claiming that the action by BlackRock is “one of the most concrete signs investors are getting more serious about acting on risks they’ve been saying for years they’re worried about”); Attracta Mooney, *BlackRock vows to back more shareholder votes on climate change*, FT (Dec. 10, 2020).

57. See, e.g., Barzuza, Curtin, & Webber *supra* note 42, at 111 (stating that carry-based fund managers “reap huge rewards when their funds have strong returns,” whereas index funds are “rewarded for managing large funds, but not directly for performance”); *What is carried interest, and how is it taxed?*, TAX POLICY CENTER (2020) (defining carried interest as a “contractual right that entitles the general partner of an investment fund to share in the fund’s profits,” and noting that private equity funds typically divide profits by allocating 20% to the general partner).

58. *Id.*

59. *Id.* at 114.

60. See George Serafeim, *Can Index Funds Be a Force for Sustainable Capitalism?*, HARV. BUS. REV. (Dec. 7, 2017).

61. *Id.* I would also add a fourth category of investment and private equity firms (Blackstone, Neuberger Berman, Apollo, The Carlyle Group, and KKR). Private equity firms have become increasingly focused on ESG-related issues, driven in part by pressure from public pension funds and other institutions that invest in



however, often a free-rider concern—why would a company choose the “good” path when it would be more costly, and their competitors could reap the benefits?<sup>62</sup> Further, why would one investor spend resources engaging with their portfolio companies on ESG, when the other investors of that company would also benefit from the long-term returns created by such ESG policies and practices?<sup>63</sup> The key to resolving this free-rider dilemma is collaboration amongst competitor corporations and their investors, who, again, tend to be a lot of the same players.<sup>64</sup>

## II. COVID-19’S EFFECTS ON ESG POLICIES

ESG considerations have become especially pronounced during the COVID-19 pandemic, as broad concerns about the employee health, the environment, equality, and access to health care are not only brought to the forefront of conversation but are also understood to have drastic impacts on the economy.<sup>65</sup> The speed at which the economy unraveled during the COVID-19 crisis demonstrated that ESG is “integral to corporate resiliency and the proper management and governance of an organization.”<sup>66</sup> Companies with robust ESG policies and practices were less drastically impacted by COVID-19 than companies who ignored or limited their ESG focus.<sup>67</sup> That being said those corporations who signed the BRT Principles fared no better than their peers who did not sign the BRT Principles.<sup>68</sup>

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them. See, e.g., Miriam Gottfried, *Blackstone Sets Goal to Reduce Carbon Emissions*, WALL ST. J. (Sept. 29, 2020); Jason M. Thomas & Megan Starr, *From Impact Investing to Investing for Impact*, CARLYLE GROUP (2020). For a more specific discussion on a particular ESG investment, see *2020 Impact Review, Sustainable Growth: Weiman Case Study*, CARLYLE GROUP (2020) (noting how Carlyle opted not to invest in a particularly ESG-focused company, but to increase ESG policies and accountability once they held ownership of Weiman. For example, within the first year of Carlyle’s ownership, Weiman increased from 0% of sales from green products to 27% of sales from green products).

62. Serafeim, *supra* note 60.

63. *Id.*

64. *Id.*

65. See generally KKS Advisors & Test of Corporate Purpose, *supra* note 3, at 6.

66. Serafeim, *supra* note 60, at 3.

67. Saijel Kishan & Emily Chasan, *Older ESG Funds Outperform Their Newer Rivals in Market Tumult*, BLOOMBERG (March 13, 2020) (finding that while the average ESG fund has fallen 12% from January-March 2020, the S&P 500 Index has fallen almost double that amount during the same 4-month period); see also Fekete, *supra* note 55; Edelman Trust Barometer 2020, *supra* note 11, at 11.

68. KKS Advisors & Test of Corporate Purpose, *supra* note 3, at 45. The factors that actually had an impact on a company’s successful COVID-19 response were prior track record with respect to other issues and the speed at which the company responded to the COVID-19 crisis. *Id.* The following characteristics were either all or mostly present in the most successful companies and all or mostly absent in the least successful companies: quantitative sustainability disclosures, quantifiable sustainability targets, board oversight of sustainability issues, materiality analysis highlighting crisis-relevant issues, examples of competitive advantage through ESG, sustainability audits, and engage with sustainability initiatives and principles (UNGC, OECD, PRI, etc.). *Id.*

This finding further supports the argument that signing the BRT Principles is more performative than substantive.<sup>69</sup>

Despite the aforementioned findings that companies with robust ESG policies and practices were less drastically impacted by COVID-19, the economic downfall caused by the COVID-19 pandemic also led to a de-prioritization of ESG initiatives, as investors and the companies in which they invest shifted their priorities to financial returns in order to minimize the effects of the economic crisis.<sup>70</sup> Likely, however, as economic recovery begins, ESG will be pushed back to the forefront,<sup>71</sup> potentially at even higher levels than pre-pandemic.

### III. SCHOLARLY APPLICATIONS OF MODEL RULE 2.1

Model Rule 2.1 states the following:

In representing a client, a lawyer shall exercise independent professional judgement and render candid advice. In rendering advice, a lawyer may refer not only to law but to other considerations such as moral, economic, social and political factors, that may be relevant to the client's situation.<sup>72</sup>

Model Rule 2.1 is the only Model Rule that considers the lawyer's role as an advisor rather than as an advocate.<sup>73</sup> The Model Rule has been applied in several, but not many, situations. This Note will discuss the impact of Model Rule 2.1 in three different applications: (1) tax; (2) a case study of Martha Stewart's insider trading scandal; and (3) the "grease payments" exception to the Foreign Corrupt Practices Act ("FCPA").

#### A. TAX ATTORNEYS SERVE AS ADVOCATE OR TRUSTEE, DEPENDING ON THE PARTICULAR SITUATION

Tax attorneys often provide nonlegal advice.<sup>74</sup> Tax attorneys instruct corporate clients on how to best structure their business, their business operations, and their

69. *Id.* at 46, 53–54. For example, Invesco Ltd., a US asset management company, was ranked as one of the most successful companies at responding to COVID-19 and they did not sign the BRT Principles. Wells Fargo, a US commercial bank, was ranked as one of the least successful companies at responding to COVID-19 and they did sign the BRT Principles. Blackrock both signed and was quick to respond to the COVID-19 crisis; as noted, BlackRock has long been committed to ESG and has demonstrated this commitment through concrete action. *Id.*

70. Edelman Trust Barometer 2020, *supra* note 11, at 8 (finding that 79% of US investors say their firm is currently deprioritizing ESG as an investment criteria and 77% of US investors say the companies they invest have deprioritized ESG initiatives); Elise Hansen, *Pandemic Response, ESG to Drive 2021 Shareholder Activism*, LAW360 (Jan. 3, 2021) (noting a report by Schultz, Roth & Zabel LLP and Activist Insight that there was a "14% downturn globally in public demands in the first three quarters of 2020" as compared to 2019).

71. Edelman Trust Barometer 2020, *supra* note 11, at 12 (finding that 96% of investors expect their firm to increase prioritization of ESG as we recover and 93% of investors expect the companies they invest in to increase prioritization of ESG as we recover).

72. MODEL RULES OF PROF'L CONDUCT R. 2.1 (2018) [hereinafter MODEL RULES]

73. MODEL RULES R. 2.1.

74. Milton C. Regan, Jr., *Tax Advisors and Conflicted Citizens*, 16 LEGAL ETHICS 322, 322 (2013).

other particular activities in order to reduce their tax liability.<sup>75</sup> An ongoing debate discusses whether tax attorneys should serve their clients as advocates or as trustees.<sup>76</sup> The advocate engages in creative compliance; that is, complying with the literal terms of the law while strategically acting in the best interest of the client.<sup>77</sup> The advocate does not impose her own views so long as her client's actions are in compliance with the literal terms of law.<sup>78</sup> The advocate theory has a pitfall: exploitation of gaps or anomalies in law can frustrate the law's purpose and threaten the integrity of law by undermining citizens' respect and confidence.<sup>79</sup> The trustee, on the other hand, protects the integrity of the law by advising on the spirit, not just the letter, of the law.<sup>80</sup> The trustee must "prompt the client to adopt a view of the law as possessing intrinsic normative weight," meaning that law is more than simply words and often has an "underlying purpose" or expected outcome.<sup>81</sup> The attorney should exercise her practical judgement in determining whether to act as an advocate or as a trustee.<sup>82</sup>

One argument is that the decision to be either an advocate or a trustee is not dichotomous, and such decision turns on the specific context of the circumstances.<sup>83</sup> Certain advisory settings may require the attorney to serve as an advocate and other situations may require the attorney to serve as a trustee.<sup>84</sup> The factors to be considered include:

individual and societal interests that are at stake in the area of practice, the extent to which the law is seen as expressing important moral convictions, characteristics of the enforcement regime, factors that affect the likely degree of voluntary compliance, the market for legal services in the field in question, and the role that the lawyer plays in the regulatory regime.<sup>85</sup>

In applying these factors to tax law, an attorney should serve as an advocate in several situations, most importantly in tolerance of avoidance of tax liability.<sup>86</sup> The "complexity and opacity" of the tax code makes considering purpose almost impossible, suggesting that complying with its literal terms is better.<sup>87</sup> A number of other circumstances in the tax realm, however, require the attorney to serve as

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75. *Id.* at 324.

76. *Id.* at 323.

77. *Id.* at 322–23.

78. *Id.*

79. *Id.* at 327.

80. *Id.* at 323.

81. *Id.* at 323, 328.

82. *Id.* at 329.

83. *Id.* at 323.

84. *Id.* at 329.

85. *Id.*

86. *Id.* at 333 ("Certain features of the tax system provide a potentially strong basis for the claim that a practitioner advising a client on tax obligations should assume the role of advocate.").

87. *Id.*

a trustee rather than as an advocate.<sup>88</sup> The successful functioning of government relies on tax revenue; if attorneys only serve as advocates, they “risk causing damage to tax morale that can trigger a self-reinforcing cycle of distrust and tax evasion.”<sup>89</sup> If taxpayers believe that other citizens are also paying their fair share of taxes, they will feel more obligated to similarly pay their fair share.<sup>90</sup>

Analogous to the role played by tax attorneys, investment funds’ attorneys should choose when to act as an advocate and when to act as a trustee. Situations such as ESG policies and practices are best handled by an attorney serving as a trustee because it protects the integrity of the law; therefore, attorneys should consider the factors listed above, particularly the societal interests in the area.

#### B. MARTHA STEWART’S COUNSEL HAD AN OBLIGATION TO WARN HER OF THE IMPLICATIONS OF MAKING A DECISION

Could have and should have Martha Stewart’s pretrial counsel, John Savarese, attempted to stop Stewart from lying about her role in insider trading?<sup>91</sup> When questioned by the SEC, Stewart lied, claiming she always intended to sell her shares if the stock price fell below a specific monetary threshold.<sup>92</sup> Before her interview with the SEC, Savarese should have warned Stewart about the implications of lying.<sup>93</sup>

Savarese should have warned her of the implications, and, if she did not heed his warning, he should have withdrawn from the case.<sup>94</sup> Several people knew about Stewart’s cover-up, so common sense would have dictated she be honest.<sup>95</sup> Similarly, the cover-up was almost immediately following the Enron scandal, so Savarese should have known that the government would take Stewart’s case very seriously; therefore, he should have discussed the business and moral consequences of lying prior to Stewart’s interview with the SEC.<sup>96</sup> If he had elected to do so, it is likely that Stewart would have faced significantly less penalty.<sup>97</sup>

Similar to the role Savarese should have taken in advising Stewart, investment funds’ attorneys should discuss the business and moral consequences associated

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88. *Id.* at 342 (“Certain features of the tax system support the claim that a tax advisor should serve as a trustee of the system who encourages clients to comply with the spirit as well as the letter of the tax code.”).

89. *Id.*

90. *Id.*

91. Drew Hoffman, *Martha Stewart’s Insider Trading Case: A Practical Application of Rule 2.1*, 20 GEO. J. LEGAL ETHICS 707, 707 (2007). As brief background, Stewart, who at the time was worth \$750 million, sold her shares in a friend’s biotech company after the friend’s assistant tipped her off that the company’s application for a cancer drug was going to be denied. She avoided \$45,673 of losses by selling her 3,982 shares of the business, an amount equivalent to 0.006% of her net worth. *Id.*

92. *Id.* at 709.

93. *Id.* Stewart’s jail time and other significant monetary and punitive penalties only arose because of her attempt to cover up her insider trading; she received a fine of a mere \$195,081 for the insider trading itself. *Id.*

94. *Id.* at 716.

95. *Id.* at 714.

96. *Id.* at 714–15.

97. *Id.* at 716.

with robust ESG policies and practices with their clients. Not only would such discussion have beneficial impacts on broader society but would also benefit the investment firm and their portfolio companies by enhancing their reputation with customers and employees and likely increasing their long-term financial success.

### C. THE VAGUE NATURE OF THE FCPA REQUIRES ATTORNEYS TO CONSIDER NON-LEGAL FACTORS

The FCPA prohibits American companies from bribing foreign officials for business advantages.<sup>98</sup> The “grease payments” exception to the FCPA enables American companies to make expenditures in order to facilitate routine government action, so long as the payments are not made to influence a decision to create new business or continue business with the paying company.<sup>99</sup> The ambiguous and vague nature of the exception suggests that attorneys need to play an advisory role and consider any “moral, social, economic and political factors” when determining whether a payment falls under the exception.<sup>100</sup>

With respect to moral considerations, attorneys must consider how grease payments are viewed in light of the corporation’s own ethical policies, as well as the cultural opinion of bribery within the foreign country.<sup>101</sup> Similarly, once corporations begin grease payments, foreign officials may begin to expect them.<sup>102</sup> Potential consequences include a weak and unstable civil society, economic inequality, and violence and extortion.<sup>103</sup> Attorneys have a moral duty to consider the “company’s size and influence in the foreign nation, the country’s current degree of low-level bribery, the direct effects on individuals and more diffuse effects on society as a whole, and how frequently such bribes are requested.”<sup>104</sup>

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98. 15 U.S.C. § 78dd-1 (1977).

99. *Id.* at (b).

Routine government action encompasses those actions which ordinarily and commonly are performed by a foreign official in: (a) obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country; (b) processing governmental papers, such as visas and work orders; (c) providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country; (d) providing telephone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or (e) actions of a similar nature. Routine governmental action does not include, among other actions, any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a company, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to, or to continue business with, a company.

*Investor Bulletin: The Foreign Corrupt Practices Act – Prohibition of the Payment of Bribes to Foreign Officials*, SEC OFFICE OF INVESTOR EDUCATION AND ADVOCACY, 2 (Oct. 2011).

100. Amanda Boote & Anne H. Dechter, *Slipped Up: Model Rule 2.1 and Counseling Clients on the Grease Payments Exception to the Foreign Corrupt Practices Act*, 23 GEO. J. LEGAL ETHICS 471, 471–72 (2010).

101. See Philip M. Nichols, *Are Facilitating Payments Legal?*, 54 VA. J. INT’L L., 127, 141–42, 153 (2013).

102. Boote & Dechter, *supra* note 100, at 478.

103. *Id.* at 479.

104. *Id.* at 480.

With respect to social considerations, lawyers should pay particularly close attention to the customs and norms of the foreign country, and, importantly, lawyers should consider the laws of that country, international law, and the foreign country's process of privatization.<sup>105</sup>

With respect to economic considerations, there are significant economic consequences to the foreign country if attorneys do not advise their clients to take mitigating action. The most corrupt countries are often the least developed; corruption leads to inefficiency as officials purposefully increase bureaucratic interference in order to incentivize American companies to provide further payments.<sup>106</sup> There are several actions an attorney can advise a company to take to limit this possibility of corruption. First, firms should implement a robust internal regulatory scheme,<sup>107</sup> allowing companies an "our-hands-are-tied" excuse.<sup>108</sup> Second, attorneys can encourage companies to take measures such as agreeing anti-bribery pacts with their peers and competitors stating that none of the companies will engage in grease payments.<sup>109</sup>

Finally, with respect to political considerations, attorneys can opine on political issues,<sup>110</sup> including how the public will view the actions of the company and how changing norms will alter these perceptions.<sup>111</sup> In more recent years, many foreign states adopted the Organization for Economic Cooperation and Development ("OECD") and its anti-bribery convention.<sup>112</sup> Attorneys should advise corporations of these continuing developments, as corruption becomes

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105. *Id.* at 481.

106. See Beverley Earle, *The United States' Foreign Corrupt Practices Act and the OECD Anti-Bribery Recommendation: When Moral Suasion Won't Work, Try the Money Argument*, 14 DICKINSON J. INT'L L. 207, 222 (1996) (noting that corruption shifts the choice from the "best" and most helpful or necessary project to the project that is providing the most bribes).

107. Kevin Davis, *Self-Interest and Altruism in the Deterrence of Transnational Bribery*, 4 AM. L. & ECON. REV. 314, 334 (arguing that law enforcement can be enacted through the implementation of a "corporate compliance program" that is well-publicized and effective).

108. Boote & Dechter, *supra* note 100, at 483; Earle, *supra* note 106, at 230 (arguing that each company should implement their own internal guidelines or policies which would be "useful from a public relations perspective").

109. See Stuart Marc Weiser, *Dealing with corruption: Effectiveness of existing regimes on doing business*, 91 AM. SOC'Y INT'L L. PROC. 99, 102 (2007) (noting that when the business community wanted to "show again that it stood firm in its condemnation of bribery," it established an ICC Ad Hoc Committee on Extortion and Bribery in International Business Transactions with goals to: "make recommendations to governments; coordinate ICC Participation in intergovernmental and nongovernmental discussion on extortion and bribery issues; and educate the international community about the long-standing commitment by international business to eradicate corruption").

110. Walter Sterling Surrey, *Foreign Corrupt Practices Act: Let the Punishment Fit the Crime*, 20 HARV. INT'L L. J. 293, 293-94 (1979). The FCPA was passed after, in conducting the Watergate investigations, the committee also discovered many prominent American companies were engaging in foreign corruption. *Id.*

111. Alexandros Zervos, *Amending the Foreign Corrupt Practices Act: Repealing the Exemption for "Routine Government Action" Payments*, 25 PENN. ST. INT'L L. REV. 251, 280 ("Firms that develop reputations for not bribing often find that they are less pressured to make corrupt payments than would otherwise be the case.").

112. Earle, *supra* note 106, at 225.



increasingly frowned upon across the globe, which could damage the company's reputation amongst its customers.<sup>113</sup>

Similarly to attorneys who advise on the FCPA exception, investment funds' attorneys should consider the moral, social, economic, and political factors associated with robust ESG policies and practices with their clients. Moral considerations should include the policies, such as commitments to sustainability and diversity, whether in social media, press releases, public filings, or elsewhere, of the investment fund and its portfolio companies. Social considerations should include current norms and customs of Americans, which, as noted, increasingly view ESG in a positive light. Economic considerations, while less conclusive, generally support the hypothesis that robust ESG policies and practices have beneficial financial impacts on a company. Finally, political factors should include the reputation of the investment firm and its portfolio companies and changing societal norms, which, again, are supportive of robust and actionable ESG considerations.

#### IV. COMBINING OF ESG AND MODEL RULE 2.1

As noted above, many scholars have discussed the recent growth in ESG considerations, yet only a few scholars have addressed Model Rule 2.1.<sup>114</sup> No one has yet to consider how Model Rule 2.1 effects the behavior of attorneys with respect to investor demands about ESG considerations. Importantly, Comment 5 to Model Rule 2.1 suggests that, while generally a lawyer "is not expected to give advice until asked by the client," it is permissible, and arguably recommended, to "initiate advice to a client when doing so appears to be in the client's interest."<sup>115</sup> Attorneys might not have a duty to their clients to recommend assenting to the ESG-related demands of investors', but perhaps, considering the wealth of data and studies demonstrating the positive effects of ESG policies on customers, employees, and investors,<sup>116</sup> lawyers should more forcefully advise clients to at least consider, and preferably implement, such demands.

Legal departments within firms are increasingly taking on two new ESG-related roles. First, they are stewards of fostering trust; "[i]n-house lawyers . . . understand that trust is critical, and they are increasingly asked to play key roles to build trust from the inside and contribute to cultivating the company's relationship with investors, shareholders, employees and clients alike."<sup>117</sup> The focus is often on whether increasing gender and racial diversity builds trust, and which

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113. *See, e.g., id.* at 230–31 (discussing how Levi Strauss implemented a policy prohibiting the use of child labor for its products after being public embarrassed for having poor working conditions in its suppliers' factories).

114. *See, e.g.,* Connellan, Gez, Kerschner, & MacLennan., *supra* note 49.

115. MODEL RULES R. 2.1, cmt. 5.

116. *See, e.g.,* Brummer & Strine, *supra* note 15, at 39.

117. Phillip Bantz, *Chief Legal Officers, Investors Differ on How to Build Trust in a Company*, LAW.COM (Sept. 28, 2020) (quoting Association of Corporate Counsel president and CEO Veta Richardson).

approach best builds trust.<sup>118</sup> Key to developing trust is maintaining a healthy corporate culture,<sup>119</sup> which, especially due to the priorities of millennials and Gen Z, relies on robust and actionable ESG policies and practices.<sup>120</sup>

Second, legal departments are often spearheading their firms' own internal ESG efforts.<sup>121</sup> For example, there has been a recent trend to put the firm's general counsel or legal department "in charge of [ESG] efforts."<sup>122</sup> Both of these new roles demonstrate that legal departments are best situated to work with investors on ESG demands.<sup>123</sup> Some practitioners argue that the company's most senior legal employee is best situated to handle ESG issues, stating that ESG is about "risk management, reputation, the intersection of new regulations, litigation and compliance efforts."<sup>124</sup> External counsel is similarly ramping up ESG work; their clients are focusing on ESG more because their investors are pushing for such efforts.<sup>125</sup>

Of course, supplemental to these two new responsibilities of in-house counsel, is the potential for a more robust regulatory scheme; many believe the U.S. will increase regulation and reporting requirements under the Biden administration.<sup>126</sup> With an increased focus on public reporting comes an increase in attorneys' responsibility,<sup>127</sup> both in-house and external counsel. For example, some argue that the entire industry could benefit from moving away from quarterly and monthly reporting, thereby emphasizing the long-term rather than short-term.<sup>128</sup>

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118. *Id.*

119. Edelman Trust Barometer 2020, *supra* note 11, at 28.

120. Barzuza, *supra* note 42, at 140.

121. *See* Clark, *supra* note 16.

122. *Id.* (paraphrasing Laura Ann Smith, assistant general counsel, Tailored Brands Inc.); *see also* Dan Clark, *Directors, GCs Need to Examine Board Diversity, ESG Issues in 2021, Says Akin Gump Report*, LAW.COM (Feb. 10, 2021) (restating a report by Akin Gump Strauss Hauser & Feld LLP that concluded "diversity and inclusion, environmental, social and governance (ESG) efforts . . . are among the topics that boards of directors and their general counsel should be concerned about in 2021") [hereinafter *Akin Gump Report*].

123. *See, e.g.,* *Akin Gump Report*, *supra* note 122.

124. Dan Clark, *Investors Are Watching ESG – in 2021, They Look to Measure It*, LAW.COM (Jan. 4, 2021) (quoting Veta Richardson, president and CEO of Association of Corporate Counsel, who also noted that in 2020, "93% of chief legal officers and general counsel either lead or play a helping role in leading their companies' ESG initiatives").

125. *Id.* (paraphrasing David Curran, Paul, Weiss Rifkind, Wharton & Garrison LLP, clients are looking for "legal to take the lead").

126. Emily Glazer, *Companies Brace Themselves for New ESG Regulations Under Biden*, WSJ (Jan. 18, 2021) (noting that one area that could impact many industries is new requirements surrounding "diversity, carbon emissions, and other types of sustainability metrics").

127. Clark, *supra* note 124.

128. *See, e.g.,* Jamie Dimon & Warren E. Buffett, *Short-Termism Is Harming the Economy*, WSJ OPINION (June 6, 2018) (arguing that "quarterly guidance often leads to an unhealthy focus on short-term profits at the expense of long-term strategy, growth and sustainability"). *But see* Shivaram Rajgopal, *What Would Happen if the U.S. Stopped Requiring Quarterly Earnings Reports?* HARV. BUS. REV. (Sept. 6, 2018) (finding that "frequent reporting doesn't lead to less investment" and "frequent reporting increases analysts' accuracy"). ESG investing tends to perform better financially in the long-run because there may be up-front costs associated with increased reporting or other commitments to ESG, such as reducing emissions or hiring diverse Board members.

There are differing opinions about whether considering ESG violates fiduciary duties.<sup>129</sup> The Supreme Court has held that ERISA law requires pension trustees to act “solely” in the financial interest of the participants and for the “exclusive purpose” of providing them financial benefits.<sup>130</sup> This discussion is outside the scope of this Note.

The focus of this Note is instead Model Rule 2.1. This Note shares the results of a series of interviews with attorneys and businesspeople, conducted between September and November 2020.<sup>131</sup> The general consensus was that attorneys should give nonlegal advice in addition to legal advice, but that ESG has not yet risen to the level where a firm *must* consider it.<sup>132</sup> Generally, those interviewed agreed that the corporate sphere is moving in the direction of increasing ESG considerations, especially in the current COVID-19 and social justice era.<sup>133</sup> The role of the attorney is often to advise on the types of investor demands that are “off-market,” as well as which demands are most practical and reasonable.<sup>134</sup>

There are three main legal provisions—excuse rights, reporting requirements, and investment limitations—included in the fund governing documents that relate to ESG, all of which have become more common recently.<sup>135</sup> First, excuse rights

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129. See Max M. Schanzenbach & Robert H. Sitkoff, *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee*, 72 STAN. L. REV. 381, 386 (2020) (arguing that ESG investment is permissible under trust fiduciary duty “if . . . (1) the trustee reasonably concludes that ESG investing will benefit the beneficiary directly by improving risk-adjusted return; and (2) the trustee’s exclusive motive for ESG investing is to obtain this direct benefit”). *But see* United Nations Principles for Responsible Investment, *What are the Principles for Responsible Investment*, <https://www.unpri.org/pri/what-are-the-principles-for-responsible-investment> [https://perma.cc/3GQU-F3ZH] (arguing that the fiduciary principles require a trustee to use ESG factors). The six principles of the PRI are:

- (1) We will incorporate ESG issues into investment analysis and decision-making processes,
- (2) We will be active owners and incorporate ESG issues into our ownership policies and practices,
- (3) We will seek appropriate disclosure on ESG issues by the entities in which we invest,
- (4) We will promote acceptance and implementation of the Principles within the investment industry,
- (5) We will work together to enhance our effectiveness in implementing the Principles, and
- (6) We will each report on our activities and progress towards implementing the Principles.

The PRI has also called on companies to ensure their financial reports and accounts are prepared consistently with the Paris Agreement on climate change. See United Nations Principles for Responsible Investment, *Investor groups call on companies to reflect climate-related risks in financial reporting*, <https://www.unpri.org/accounting-for-climate-change/investor-groups-call-on-companies-to-reflect-climate-related-risks-in-financial-reporting/6432.article> [https://perma.cc/8F2F-T6T6] (Sept. 16, 2020).

130. See, e.g., *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. 409, 415 (2014).

131. Interviewees consisted of two entrepreneurs, two in-house counsel (one at a private equity firm and one at an index fund), five partners at four big law firms, one investment professional, one associate at a private equity team working on portfolio value creation, and one venture capital partner focused on portfolio company operations [hereinafter: Interviews].

132. *Id.*

133. *Id.*

134. *Id.*

135. *Incorporating Responsible Investment Requirements into Private Equity Fund Terms* (July 2017), <https://www.unpri.org/private-equity/options-for-esg-provisions-in-private-equity-fund-terms/121.article> [https://perma.cc/9Q96-5AAW] [hereinafter: ESG Options]; Kristen M. Rylko & Mark C. Dempsey, *Beginner’s Glossary to Fund Finance*, MAYER BROWN, 4–5 (Feb. 17, 2016).

are investor-specific, meaning investors will ask that their capital contributions are not used for certain investments.<sup>136</sup> Excuse rights are often complicated because certain investors have strict internal policies about what they can or cannot invest in.<sup>137</sup> Second, reporting requirements are sometimes fund-specific and sometimes investor-specific.<sup>138</sup> They vary in substance but generally provide investors with specifics on portfolio companies current ESG policies and practices and steps, if any, the sponsor is embarking on to expand its ESG policies and practices.<sup>139</sup> Finally, there are investment limitations, which are binding on the fund in its entirety, rather than a specific investor.<sup>140</sup> Examples of investment limitations include limiting the percentage of the overall fund contributions that can be invested in a certain company, a certain part of the world, or a certain industry.<sup>141</sup>

An attorney should not pretend to know everything.<sup>142</sup> Lawyers should speak their minds, regardless of upsetting their client.<sup>143</sup> That being said, a lawyer's advisory role should not be pushed so far as to withdraw from the attorney-client relationship, per Model Rule 1.16(b)(4).<sup>144</sup>

Investors have the power to “put their money where their mouth is” and invest in sustainable investment opportunities.<sup>145</sup> By choosing managers who invest within certain ESG guidelines, investors can ultimately decide which asset managers are successful and which are not.<sup>146</sup> An asset manager that does not follow the guidelines or ESG policies will lose key investors and either fail or, hopefully, change their decision-making process and begin to consider ESG, even if only to ensure that they continue to fundraise and be successful managers.<sup>147</sup> Many asset

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136. ESG Options, *supra* note 135.

137. *Id.* at 16. Some investors, for example, may have policies prohibiting certain types of investments in companies engaged in certain activities (e.g., cluster munitions) or companies associated with certain countries. *Id.*

138. *Id.* at 18.

139. *Id.*

140. *Id.* at 16.

141. Interviews, *supra* note 131.

142. See Hoffman, *supra* note 88, at 713.

143. See *id.* at 716.

144. MODEL RULES R. 1.16(b)(4) (“[A] lawyer may withdraw from representing a client if . . . the client insists upon taking action that the lawyer considers repugnant or with which the lawyer has a fundamental disagreement”). There is, however, not a lot of color on what type of situations exist in which a lawyer might withdraw using this rule, though it has been argued that the language is broad. See Joel S. Newman, *If Shylock Had a Lawyer*, 7 WAKE FOREST J.L. & POL’Y S.S. 21, 27 FN 35 (2017). But see Suzanne Lever, *Breaking Up Is Hard To Do*, NC STATE BAR (2017) (concluding that while an attorney may ask to withdraw her representation, the court has discretion to deny such a request).

145. See KKS Advisors & Test of Corporate Purpose, *supra* note 3, at 59.

146. See *id.*

147. See *id.*

managers are supporting efforts to be more transparent, including by sharing their government-required diversity data with the larger public.<sup>148</sup>

Many attorneys are calling on each other to participate in efforts to increase diversity, whether that be ensuring a broad range of pro bono opportunities, expanding internships for law students of all backgrounds, or serving as mentors to students or junior lawyers.<sup>149</sup> A letter from the General Counsels at twelve global financial institutions published a letter advocating for such efforts, stating that “our culture and what we value and promote in our departments must recognize and account for the full breadth of talent, styles and perspectives, including those who are racially and ethnically diverse. Our profession will be better and stronger for our having done so.”<sup>150</sup> Such influential attorneys, however, should take a stronger and more explicit stance; lawyers should not only play a role in increasing diversity within their own organizations, but also in increasing diversity in their clients’ organizations and investment opportunities.

### CONCLUSION

ESG policies and practices have broad implications on the success of companies, a trend that is likely to be accelerated not only by COVID-19, but also by the Biden administration and the emerging investing coalition of Millennials and Gen Z. There is evidence that companies with robust and actionable ESG policies and procedures are more attractive to customers, employees, and investors, particularly institutional investors. Attorneys to investment firms should understand this new trend and urge their clients to strongly consider any reasonable demands from investors, including excuse rights, reporting requirements, and investment limitations that are ESG-related. In doing so, attorneys are not only advising their client to make smart business decisions, but are also promoting a world in which corporations commit to bettering society and the world we live in.

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148. See Jena McGregor, *Urged to back up pledges for racial justice, 34 major firms commit to disclose government workforce data*, WASH. POST (Sept. 29, 2020) (noting that the firms who have committed to sharing their diversity data publicly includes BlackRock).

149. Dan Clark, *12 Global Financial Services General Counsel Call for Greater Diversity & Inclusion in Legal Profession*, LAW.COM (Sept. 30, 2020).

150. *Id.*