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# Socially Responsible Investing is Not Enough: Lawyers Ethical Duties as a Tool to Deliver on Paris Agreement Goals and Prevent Irreversible Climate Tipping Points

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Over half of global industrial emissions since human-induced climate change was officially recognized can be traced to just twenty-five corporate and state producing entities.[1] Since 1988, 71% of all global greenhouse gas ("GHG") emissions can be traced to just one hundred fossil fuel producers.[2] The same data also shows that 32% of these legacy emissions come from public investor-owned companies, highlighting the power of investors in the transition to a sustainable economy.[3] Moreover, it is in investors' best interests to prioritize such a transition. A study by the *Economist* found that by 2100, climate risks alone could jeopardize $4 trillion to $14 trillion in private sector assets and $43 trillion when public sector assets are included.[4]

Climate change is widely recognized as a systemic challenge, posing significant issues for legal structure and governance.[5] Indeed, climate change is highly "polycentric, dynamic, uncertain, and socio-politically sensitive, and so poses challenges to legal orders which seek certainty and stability."[6] When public governance fails to address important environmental threats, private governance by firms, not-for-profits, individuals, and households can produce

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[1] Dr. Paul Griffin, *Carbon Majors Report 2017*, July 2017, at 8, https://cdn.cdp.net/cdp-production/cms/reports/documents/000/002/327/original/Carbon-Majors-Report-2017.pdf?1501833772

[2] *Id.; see also* Joshua Axelrod, *Corporate Honesty and Climate Change: Time to Own up and Act*, Nat'l Res. Def. Council, Feb. 26, 2019, https://www.nrdc.org/experts/josh-axelrod/corporate-honesty-and-climate-change-time-own-and-act.

[3] Griffin, *infra* note 1 at 8. https://www.cdp.net/en/articles/media/new-report-shows-just-100-companies-are-source-of-over-70-of-emissions.

[4] Andy Green & Andrew Schwartz, *Corporate Long-Termism, Transparency, and the Public Interest*, Ctr. for Am. Progress, Oct. 8, 2018, https://www.americanprogress.org/article/corporate-long-termism-transparency-public-interest/ (examining the role that improved corporate disclosure could play in boosting long-termism, focused especially on ESG information); Brian Gardner, *The Cost of Inaction: Recognizing the Risk From Climate Change*, The Economist, 2015, https://www.americanprogress.org/article/corporate-long-termism-transparency-public-interest/

[5] Lisa Benjamin, *The Road to Paris runs Through Delaware: Climate Litigation and Directors' Duties*, 2020 UTLR 313, at 323 (2020).

[6] Elizabeth Fisher et al., *The Legally Disruptive Nature of Climate Change*, 80 MOD. L. REV. 173, 174 (2017).

significant reductions in greenhouse gas emissions ("GHGs").[7] In 2017, as the United States repudiated its previous commitments to fighting climate change, both internationally and domestically, more than 1,700 businesses and investors stepped forward to declare that they remained committed to cutting GHGs.[8] This announcement centered the potential for private organizations and investors to use their market power to perform activities traditionally associated with public governance and regulation— this is known as "private climate governance." Changes in supply chain management, for example, illustrate the effectiveness of a private governance approach. The not-for profit organization CDP (formerly the Carbon Disclosure Project) reports that pressure from large purchasing firms led their suppliers to reduce annual carbon dioxide emissions by more than 550 million metric tons in 2018.[9] Private environmental governance cannot substitute for public regulation, but it has the potential to make meaningful contributions to reducing GHGs.[10] Moreover, it is necessary for addressing climate change in light of recent abdication by political figures, such as former United States president Donald Trump.

The private and public sector alike are being forced to transition to new economic models and adapt new regulatory schemes as the risks of climate change become increasingly severe and certain. These actions are rooted in the need to deliver on the commitments made in the COP21 Paris Agreement signed in 2015. [11] In this monumental step in the world's response to climate

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[7] Jonathan Gilligan, *Carrots and Sticks in Private Climate Governance*, 6 Tex. A&M L. Rev. 179 (2018).
[8] *Id.*
[9] CDP, Closing the Gap: Scaling Up Sustainable Supply Chains 4, 6 (2018), available at https://6fefcbb86e61af1b2fc4-c70d8ead6ced550b4d987d7c03fcdd1 d.ssl.cf3.rackcdn.com/cms/reports/documents/000/003/014/original/CDP Supply Cha in Report 2018.pdf?1518084325 [https://perma.cc/Q35D-XWSM].
[10] Gilligan, *supra* note 10, at 182; Michael P. Vandenbergh & Jonathan M. Gilligan, *Beyond Politics: The Private Governance Response to Climate Change* 8-14 (2017).
[11] Climate Governance Initiative, *Primer on Climate Change: Directors' Duties and Disclosure Obligations*, June, 2021, at 2, https://www.tcfdhub.org/wp-

change, countries large and small have committed to collective action measures to slow global warming.[12] The Agreement set out a goal of achieving net-zero greenhouse gas emissions by 2050 or earlier, consistent with an average temperature rise above the pre-industrial age of no more than 1.5 degrees Celsius.[13] The Paris Agreement expressly calls for mobilizing private sector financing to support the enormous investments in green technologies and infrastructure that will be necessary to realize its carbon emissions goals.[14] This mobilization has already began. At the 2021 COP26 in Glasgow, the UN Special Envoy for Climate Action and Finance announced that $130 trillion in assets, spread across 450 financial institutions, were committed to reach net-zero emissions by 2050.[15]

While I believe all aspects of ESG must be incorporated into fiduciary responsibilities, this essay primarily focuses on why the "E" aspects must be prioritized to leverage the maximum potential to fight climate change. Part I of this essay provides a general overview of the sustainable finance movement and orients the discussion within the competing models of governance. Part II starts with a discussion of the changing role of the corporation, highlighting institutional investors' recent shift toward a sustainability-focused approach. This shift is then illustrated with a discussion of BlackRock, the world's largest institutional investor. Part III connects and analyzes Parts I and II and makes recommendations to maximize the potential of the sustainable finance movement to drive the transition to a net-zero future. Part IV begins by describing how ESG incorporation is consistent with the shareholder primacy fiduciary duty

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[12] Park, *infra* note 14, at 3.

[13] *See* Climate Governance Initiative, *supra* note 11.

[14] Stephen Park, *Investors as Regulators: Green Bonds and the Governance Challenges of the Sustainable Finance Revolution*, 54 Stan. J. Int'l L. 1, 4 (2018).

[15] Katherine Dunn, *Financial firms managing $130 trillion commit to net-zero goals, but no one can agree on what that really means*, Fortune Magazine, Nov. 3, 2021, available at https://fortune.com/2021/11/03/net-zero-finance-coalition-cop26-mark-carney/

model. Part IV then proposes that holding lawyers to their existing ethical duties can shift to a more inclusive stakeholder paradigm to meet the Paris Agreement goals.

## I. Background: Sustainable Finance Movement & its Connection to ESG

The sustainable finance movement refers to the incipient revolution in socially responsible approaches to finance.[16] This revolution is being led by the most unlikely of revolutionaries: the mutual funds, pension funds, and insurers that collectively hold the largest pool of capital in the United States.[17] These institutional investors increasingly use the global capital markets to promote sustainability and play a key role in corporate governance through their consolidated ownership of equity markets.[18] Recently, under the rubric of investment due diligence and stewardship, these entities have expanded their analyses to prioritize non-financial matters— namely environmental risks, social issues, and governance reforms.[19] This is known as environmental, social governance ("ESG"), an outgrowth of corporate social responsibility (CSR). ESG considerations are increasingly regarded as integral to investment decision-making and as new determinants in the framing of fiduciary duties.[20]

A lack of standardization in terminology has created confusion over how ESG investing and sustainable investing differentiate, and about which is the best approach for investors to take. Through ESG investing, market participants consider in their decision-making the ways in which environmental, social, and governance risks and opportunities can have material impacts on companies' performance. [21] Sustainable investing, sometimes known as socially responsible

[16] Park, *supra* note 14, at 4.
[17] *Id*. at 4-5.
[18] See *Id.*
[19] Kraik, *infra* note 58 at 494.
[20] *Id*. at 495.
[21] *What is the Difference Between ESG Investing and Socially Responsible Investing?*, S&P Global, Feb. 25, 2020, available at https://www.spglobal.com/en/research-insights/articles/what-is-the-difference-between-esg-investing-and-socially-responsible-investing

investing (SRI) or impact investing, puts a premium on positive social change by considering both financial returns and moral values in investments decisions.[22]

## A. Differentiating Sustainable Finance Approaches Through the Governance Dichotomy

The traditional governance model well established in U.S. corporate law is known as the shareholder primacy model[23] in which the primary fiduciary duty of corporate managers is that of profit maximization. The competing model of governance, known as the stakeholder model, broadens the scope of a managers' fiduciary duties to include all the stakeholders effected by a corporation's activity, including society at-large. It is important to distinguish the two approaches by different players in the sustainable finance space because while their ESG results may overlap, their intentions and fiduciary duties remain distinct. [24] For example, pure ESG investors, "impact investors," and "responsible" investment methods are dual method, in that they aim for both return and beneficial social and environmental impact. "Impact investing" is distinct from socially responsible investing ("SRI").[25] SRI, although advancing, at its roots describes a screening mechanism to avoid or pursue investments based on ecological, social, environmental, or other ethical criteria.[26] Impact investing takes things a step further by actively seeking to invest in companies that have the potential to create positive economic, social, and environmental outcomes.[27]

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[22] *Id.*
[23] *See* D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277, 278 (Dec. 31, 1998), https://digitalcommons.law.byu.edu/cgi/viewcontent.cgi?article=1027&context=faculty_scholarship
[24] *See id.* at 527.
[25] Karim Harj & Edward Jackson, *Accelerating Impact: Achievements, Challenges and What's Next in Building the Impact Investing Industry*, xi (Rockefeller Found., July 2012), available at https://www.rockefellerfoundation.org/wp-content/uploads/Accelerating-Impact-Full-Summary.pdf
[26] *Id.* at 49-50.
[27] *Id.* at 41, 43.

Conversely, large asset managers such as BlackRock hold fast to the shareholder-primacy model that places profit-maximization as the top priority and legal responsibility.[28] In fact, BlackRock has disclaimed CSR and SRI approaches, stating that its role is not to make social, ethical, or political judgments on behalf of its clients.[29] This approach, therefore, can be classified as a social risk approach to governance: it has an expectation that companies will operate with awareness of broader contexts and will plan for the effects from the societal impacts of their businesses.[30] Thus, ESG factors are integrated into BlackRock's quantitative return seeking, but these factors are not its priority or main end.[31]

## II. Shifting Attitudes in the Role of the Corporation, ESG, & Fiduciary Duties

The "green revolution" is transforming business and investment practices, standards, and even laws. Some have gone as far as claiming that an entirely new and distinct area of the law is emerging, known as sustainable business law.[32] Put simply, "[i]n light of the significant impact that firms can have on the environment. . . the law governing the corporation throughout its life-cycle— corporate law, securities regulation, antitrust law, and bankruptcy law — should be understood as a fundamental part of environmental law."[33] On a broader scale, companies who incorporate ESG factors rank higher in financial and overall performance. A Deutsche Bank meta-study found that companies with high ESG ratings outpaced their peers in terms of financial performance: 89% of studies showed market outperformance and 85% showed

[28] *See* BlackRock, *2019 Investment Stewardship Annual Report*, 3 (Aug. 2019), https://www.blackrock.com/corporate/literature/publication/blk-annual-stewardship-report-2019.pdf
[29] Larry Fink, *Larry Fink's 2020 Letter to CEOs: A Fundamental Reshaping of Finance* (2020), https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter
[30] Kraik, *infra* note 58, at 522.
[31] *Id.*
[32] *See generally*, Myers et al., *infra* note 41.
[33] Sarah E. Light, *The Law of the Corporation as Environmental Law*, 71 Stan. L. Rev. 137, 140 (2019).

accounting outperformance.[34] For funds employing these strategies, the results were either neutral, positive, or mixed between the two.[35] Further, ESG factors relate to a company's overall performance.[36]

Likewise, over the past few decades, commentators have identified a "new wave"[37] in the socially responsible investing movement whereby responsible investors integrate environmental, social, and governance (ESG) factors into their actions as shareholders, including whether to buy, hold, or sell shares in a company, and how to exercise voting rights.[38] Notably, these investors are not incorporating ESG considerations out of moral convictions, but based on the belief that these factors have a material effect on long-term investment returns and value.[39] Interestingly, this approach to investing is often summed up in the catchphrase "doing well by doing good."[40]

This green revolution is also affecting corporate and investor legal obligations. Historically, director and manager duties in for-profit corporations have been premised on profit maximization for shareholders.[41] A major turning-point in this debate came following the

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[34] *See generally* MARK FULTON ET AL., DEUTSCHE BANK, SUSTAINABLE INVESTING: ESTABLISHING LONG-TERM VALUE AND PERFORMANCE (2012) (reporting that firms with high ESG ratings generally outperformed the market).
[35] *Id.* at 8-9.
[36] Kraik, *infra* note 58, at 535; Gunnar Friede et al., *ESG and Financial Performance: Aggregated Evidence from More than 2000 Empirical Studies*, 5 J. SUSTAINABLE FIN. & INV. 210, 210 (2015) (summarizing that a meta study of over 2,200 studies that finds a positive effect between ESG factors and overall company performance).
[37] Gail Henderson, *Making Corporations Environmentally Sustainable: The Limits of Responsible Investing*, 13 German L. J. 1412, 1413 (2012).
[38] *Id.* at 1413;
[39] *Id.*; *see also* Preamble to the PRI, online: www.unpri.org/principles/ (last accessed: 2 December 2022) ("[W]e believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios. . . We also recognize that applying these Principles may better align investors with broader objectives of society.").
[40] Henderson, *supra* note 37, at 1414.
[41] Colin Myers & Jason Czarnwzki, *Sustainable Business Law? The Key Role of Corporate Governance and Finance*, 51 Envtl. L. 991, 1003 (2021); *see also* Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. Times Magazine, Sept. 13, 1970, at 32, 33, https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html (asserting that a corporate executive "has direct responsibility to his [shareholders]…. To make as much money as possible").

publication of the now famous "Statement" of the Business Roundtable in August 2019.[42] This Statement represents a sea-change in the role of the corporation beyond merely a vehicle for profit-maximization to the pursuit of broader societal stakeholder goals and interests.[43] In essence, the shareholder primacy paradigm is shifting to incorporate a broader swath of stakeholders, thereby recognizing the need to increase corporate responsibility.[44] To better understand this comprehensive shift towards the inclusion of environmental and social considerations in the business and finance realms, it is necessary to first discuss underlying governance paradigms. Further, it is important to ground this discussion in the role of institutional investors and fiduciary duties.

### A. Short-Termism vs Long-Termism: A Primer

The growth of environmental and social aspects in institutional activism is often viewed as a nuanced, progressive addition to the optimal strategy for long-term value creation.[45] To fully understand this shift, it is necessary to touch on the short-termism vs. long-termism paradigms. "Short-termism" has been defined as "a preference for actions in the near-term without due consideration of the long-term consequences."[46] The Business Roundtable describes it as "the excessive focus of some corporate leaders, investors, and analysts on short-term, quarterly earnings and a lack of attention to the strategy, fundamentals, and conventional approaches to long-term value creation."[47] Short-termism grew out of the transition from manager-owned companies to investor-owned companies.[48] The emergence of a professional management class

[42] Giovanni Strampelli, *Can BlackRock Save the Planet? The Institutional Investors' Role in Stakeholder Capitalism*, 11 Harv. Bus. L. Rev. 1, 2 (2021).
[43] *Id.*
[44] *See* Joseph Manning, *Myopic Madness: Breaking the Stranglehold of Shareholder Short-Termism to Address Climate Change and Build a Sustainable Economy*, 10 Ariz. J. Envtl. L. & Pol'y 425, at 438 (2020).
[45] *Id.*
[46] Emeka Duruigbo, *Tackling Shareholder Short-Termism and Managerial Myopia*, 100 KY. L.J. 531, 531 (2012).
[47] *Id.* at 536.
[48] Manning, *supra* note 44, at 428.

produced concerns that these managers would pursue their own interests at the expense of the interests of the owner-shareholders.[49] Consequently, the latter part of the Twentieth Century saw the rise of shareholder primacy.[50] The recognized problem with a shareholder-primacy model is that shareholders' interests do not always align with the long-term sustainability of the companies they hold. By extension, the drive for short-term financial gains results in sacrificing the long-term investment and planning that is essential to a sustainable economy.[51] Many investors, especially hedge fund money managers, receive compensation based on short-term stock performance.[52] Short-termism infiltrates corporate management practices as well.[53] Managers describe concerns that missing the quarterly earnings estimates developed by shareholders will result in a large-scale sell-off of shares, which will drive down stock prices, and ultimately cost these managers their jobs.[54]

### B. BlackRock & the Importance of Institutional Investors

Arguably one of the most important financial players in terms of their potential to drive the sustainable finance movement are institutional investors. Attention to ESG issues by these asset managers has expanded from a niche of socially responsible investment funds to encompass a broad variety of funds.[55] The term institutional investor is used to describe a legal entity that accumulates the funds of numerous investors to invest in various financial instruments— put simply, it is a largescale investor that invests on behalf of its members.[56]

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[49] *Id.*
[50] *Id.*; *see also* Steven A. Rosenblum, *Hedge Fund Activism, Short-Termism, and A New Paradigm of Corporate Governance*, 126 YALE L.J. F. 538, 538-39 (2017).
[51] Manning, *supra* note 44, at 428; David Millon, *Shareholder Social Responsibility*, 36 SEATTLE U. L. REV. 911, 917-19 (2013).
[52] Manning, *supra* note 44, at 428-29.
[53] *Id.*
[54] *Id.*
[55] Jonathan Gilligan, *Carrots and Sticks in Private Climate Governance*, 6 Tex. A&M L. Rev. 179, 180 (2018).
[56] CFI Team, *Institutional Investor*, Corp. Fin. Inst., March 16, 2023, https://corporatefinanceinstitute.com/resources/wealth-management/institutional-investor/

There are several types of institutional investors, including hedge funds, pension funds, mutual funds, venture capital funds, real estate investment trusts, and insurance companies.[57] Where retail investors once dominated capital markets, societal changes in equity investing, investor demographics, and decisions to privatize retirement savings have led to a sharp increase in institutional equity holdings.[58] In 1950, institutional shareholders held 6.1% of total outstanding U.S. equities.[59] By 2016, that number increased to 70%.[60] The largest of these asset managers—BlackRock, Vanguard, and State Street—each have greater than $1 trillion in assets under management (AUM), comprising 20% of the S&P 500.[61] The rapid growth and control of the market by institutional investors reflects their potential to force markets in particular directions. Recently, there has been a lot of attention given to institutional investor's concerted effort to incorporate ESG considerations into their investment strategies and decisions as investors have focused attention on the significance of the climate risk for investment activities. Moreover, research supports the contention that the influence of institutional investors is positively associated with climate change disclosure by large companies.[62]

BlackRock, specifically, provides a great case study to illustrate what some have termed the sustainability-centered "tectonic shift" in the asset manager sector. As the world's largest asset manager, BlackRock invests in thousands of companies internationally, and is the most

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[57] *Id.*
[58] Alexander Kraik, *Environmental, Social, and Governance Issues: An Altered Shareholder Activist Paradigm*, 44 Vt. L. Rev. 493, 500; *see also*, Giovanni Strampelli, *Can BlackRock Save the Planet? The Institutional Investors' Role in Stakeholder Capitalism*, 11 Harv. Bus. L. Rev. 1, 4 (2021) ("ownership of listed companies is becoming increasingly concentrated owing to the unstoppable growth of institutional investors").
[59] Paula Loop et al., *The Changing Face of Shareholder Activism*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 1, 2018), https://corpgov.law.harvard.edu/2018/02/01/the-changing-face-of-shareholder-activism/ (explaining that institutional investors have the most impact in driving corporate change and governance practices); Kraik *supra* note 15, at 500.
[60] Loop et al., *supra* note 15.
[61] Kraik, *supra* note 15, at 500.
[62] Julie Cotter & Muftah Najah, *Institutional Investor Influence on Global Climate Change Disclosure Practices*, 37 Aus. J. of Mgmt., 127, 185 (2012).

important shareholder for many of them.[63] For the first time, in his now famous annual letters, the CEO of BlackRock made waves in the world of asset management with a pointed and unprecedented message on climate change. In his 2018 annual letter to the CEOs of investee companies he asserted "[t]o prosper over time, every company must deliver financial performance, but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders, including shareholders, employees, customers, and the communities in which they operate."[64] In 2020, the annual letter's predominant message centered the importance of the climate risk as "a defining factor in companies' long-term prospects. . . with the impact of sustainability on investment returns increasing. . . sustainable investing is the strongest foundation for client portfolios going forward."[65] Consequently, Fink asserts that sustainability and climate-integrated portfolios will provide better risk adjusted returns to investors and will create the best long-term value.[66]

BlackRock's Global Executive Committee has set out how it plans to achieve these goals in its annual letters to its clients.[67] In the 2020 letter, the Committee listed the following initiatives: eliminating BlackRock's exposure to bonds or equities of companies operating in certain sectors with a high ESG risk; limiting investment in companies that produce thermal coal, with an intent to completely divest from companies that generate more than 25% of their revenues from the production of thermal coal from "active" portfolios within the first six months

[63] *See* https://www.businessinsider.com/what-to-know-about-blackrock-larry-fink-biden-cabinet-facts-2020-12
[64] Larry Fink, Larry Fink's 2018 Letter to CEOs: A Sense of Purpose (2018), http://assobenefit.message-asp.com/sites/assobenefit/files/lettera_black_rock_con_logo.pdf
[65] Larry Fink, *Larry Fink's 2020 Letter to CEOs: A Fundamental Reshaping of Finance* (2020), https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter; Strampelli, *supra* note 17, at 6.
[66] *See id.*
[67] *See* BlackRock's Global Executive Committee, *BlackRock's 2020 Letter to Clients: Sustainability as BlackRock's New Standard for Investing* (2020), https://www.blackrock.com/us/individual/blackrock-client-letter; BlackRock's Global Executive Committee, *BlackRock's 2021 Letter to Clients: Net Zero: A Fiduciary Approach* (2021), https://www.blackrock.com/corporate/investor-relations/blackrock-client-letter [hereinafter BlackRock's Global Executive Committee's 2021 Client Letter].

of 2020; and creating portfolios that aim to generate a return by picking companies that are selected due to their positive, measurable impact.[68] In the 2021 letter,[69] BlackRock further pledged to increase the number of meetings with listed companies and vote against any proposals that do not comply with ESG standards deemed to be adequate; increase transparency related to its own stewardship activities and high-profile votes; and requiring companies to disclose a plan for how their business model will be compatible with a net-zero economy.[70]

### C. Fiduciary Duties in the Context of ESG

Fiduciary duties not only require company directors to manage sustainability performance, but also fiduciary investors that manage other peoples' money must consider ESG risks in investment and portfolio construction.[71] The connection between institutional investors and the pursuit of long-term value is grounded in fiduciary law.[72] In 1963, the Supreme Court in *SEC v. Capital Gains Research Bureau* interpreted § 206 of the Investment Advisors Act as congressional recognition of the fiduciary nature of an investment-advisory relationship.[73] This holding stands for the legal conclusion that every investment institution is obligated to further and safeguard the interests of its investors.[74] Therefore, combining this with corporate law's prioritization of long-term shareholder value for managers, a firm's investment policies and activities must be aimed at delivering value over the long-term for its beneficiaries and clients.[75] ESG incorporation relates to an institution's fiduciary duties because it is interpreting the

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[68] *Id.*
[69] 2021 Letter, *supra* note 26.
[70] Larry Fink, *Larry Fink's 2021 Letter to CEOs* (2021), https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter [hereinafter *Fink's 2021 Letter to CEOs]*.
[71] Myers, *supra* note 41, at 1004.
[72] Kraik, *supra* note 58, at 532.
[73] *Sec. Exch. Comm'n v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 191 (1963).
[74] *Id.* at 187, 189, 191.
[75] Kraik, *supra* note 58, at 531.

emphasis and appraisal of non-financial factors and risks to be for the long-term benefit of its beneficiaries.[76]

This trend in interpretation has given way to an ongoing debate over how ESG factors into fiduciary duties. The U.N. Global Compact has addressed whether fiduciary duty is a barrier to ESG inclusion, asserting that there should not be fiduciary barriers to incorporating ESG issues into investment processes and that it should be a breach of fiduciary duty not to do so.[77] However, many believe this goes too far, arguing instead that ESG incorporation should be viewed as a furthering of fiduciary duties.[78] This is the interpretation that seems to be the standard applied by major institutional investor asset managers.[79]

Beyond investor duties are the fiduciary duties corporate directors owe to corporate shareholders.[80] In many ways, these duties also favor the shareholder-primacy, profit maximization paradigm. This is epitomized in the preeminent and controlling case of *Dodge v. Ford Motors*, which held that the Board's decision to forgo paying dividends to shareholders, in order to invest in the company's employees and operations, constituted a breach of the directors' fiduciary duty to the company's investors.[81] Although this has been the historic approach, directors do have sufficient flexibility while fulfilling their fiduciary duties to incorporate approaches with a longer-term perspective that consider the opportunities and benefits from energy transitions and sustainability metrics.[82] This view squares with the stakeholder-focused

[76] *Id.* at 523; OECD, INVESTMENT GOVERNANCE AND THE INTEGRATION OF ENVIRONMENTAL, SOCIAL, AND GOVERNANCE FACTORS 7-9 (2017), https://www.oecd.org/finance/Investment-Governance-Integration-ESG-Factors.pdf.
[77] RORY SULLIVAN ET AL., U.N. PRI, FIDUCIARY DUTY IN THE 21ST CENTURY (2015), at 9, https://www.unpri.org/download?ac=1378
[78] Kraik, *supra* note 58, at 534.
[79] *Id.*
[80] *See Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1280 (Del. 1989) ("[D]irectors owe fiduciary duties of care and loyalty to the corporation and its shareholders.").
[81] *Dodge v. Ford Motor Co*., 170 N.W. 668, 684 (Mich. 1919).
[82] Myers, *supra* note 41, at 1003.

approach endorsed by the Business Roundtable in 2019. In this way, directors must identify and assess climate risks and their financial implications.[83]

## III. Analysis & Conclusions

A recent study[84] published in the journal Nature showed that the world is potentially on track to meet the Paris Agreement goals, contingent upon countries meeting their promised targets.[85] Specifically, countries must fulfill their specific pledged national targets for curbing carbon emissions by 2030, but also come through on more distant promises of reaching net-zero carbon emissions by 2050.[86] The problem is this: governments are far from implementing their long-term targets. Clearly, leveraging the power of the financial sector to combat climate change requires a coordinated global mobilization of public and private financial resources.

While business leaders, such as the Business Roundtable, have acknowledged a sea-change in the role of the corporation beyond mere profit maximization, the genuineness of their intentions will be proven through their actions and urgency to make changes. There is evidence that the companies whose CEOs backed the BRT Statement have yet to act on their recommendations.[87] For example, over the 2014-2018 period, the EPA recorded a higher number of environmental protection violations by companies whose CEOs signed the BRT Statement.[88] Whether this Statement represents a true commitment by these companies to improve their sustainability policies or whether it was just a hollow attempt to appear virtuous remains to be seen. The influx of shareholder proposals encouraging actual compliance with the BRT

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[83] *Id*. at 1004.
[84] Meinshausen, Nature,
[85] Seth Borenstein, *Study Finds Nations Can Keep Global Warming to 2 Degrees if Pledges are Met*, PBS, April 13, 2022, https://www.pbs.org/newshour/world/study-finds-nations-can-keep-global-warming-to-2-degrees-if-pledges-are-met
[86] *Id.*
[87] Strampelli, *supra* note 42, at 2-3.
[88] *Id.*

Statement during the last few annual general meeting (AGM) seasons[89] provides hope that they will be held to their stated promises regardless. However, if shareholders afford priority to short-term objectives, the reality of the BRT objectives fades.[90] Still, critics have pointed out that dichotomizing the role of the corporation into the shareholder v. stakeholder paradigms oversimplifies the debate and doesn't properly account for shareholder influence since they play a central role in both models.[91]

However exciting, BlackRock and other leading institutional investors' resounding endorsement and adoption of sustainable investment policies may not be rooted in altruism.[92] In fact, BlackRock published a study in 2020 which found that the success of investment strategies that incorporate sustainability is largely due to the belief that they will achieve higher returns with less risk in the long run, and due to changes in preferences of investors.[93] Specifically, investor preference for ESG-focused funds will likely increase with demographic changes to the market, such as when the millennial generation ("millennials") gains more investment control.[94] In that view, even if BlackRock's current ESG support is still primarily premised on profit-maximization, who's to say this underlying premise won't become more altruistic as the younger generations become the leaders of these institutions. Indeed, the younger generations (millennials and "Gen Z") are increasingly aware of and concerned with addressing the systemic risks of climate change. BlackRock's increase in transparency around its stewardship and voting practices is a great step in the right direction. However, if their stewardship initiatives are to be

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[89] *Id.*
[90] *Id.* at 4.
[91] *See* John Gerard Ruggie, *Corporate Purpose in Play: The Role of ESG Investing* (Harvard Kennedy Sch. Faculty Rsch. Working Paper Series RWP19-034, 2019), https://ssrn.com/abstract=3483205.
[92] Strampelli, *supra* note 42, at 12.
[93] *Id.*
[94] *Id.* at 13; *see also* BLACKROCK, SUSTAINABILITY: THE TECTONIC SHIFT TRANSFORMING INVESTING 3, 5 (2020), https://www.blackrock.com/us/individual/insights/blackrock-investment-institute/sustainability-in-portfolio-construction.

effective, BlackRock should commit to contributing more resources to these efforts. With current portfolios of five-hundred companies each, invariably, their stewardship members are limited in how thorough of an analysis they can conduct.

Beyond institutional investors, the corporate norms driving managers' short-term focus must be addressed to keep in line with investors' long-term focus. For example, the practice of linking executive compensation to stock prices creates an incentive for management to focus on stock performance at the expense of other aspects of the business, such as their long-term sustainability, workers, and research and development.[95] Moreover, a bedrock principle of American corporate culture is the idea that shares of equal class deserve equal treatment.[96] The problem here is this norm does not reflect the reality that not all investors are equally valuable to a company.[97] Evidence suggests that for companies to successfully pursue long-term objectives, they require a core group of investors committed to holding the stock for the long-term.[98] However, achieving this is difficult in today's stock market where the average share is held for only six months.[99] Therefore, this trend heavily disincentivizes investors from holding stock long-term, which would in turn allow companies to prioritize long-term objectives, such as sustainability.

Shifting corporate norms towards long-term approaches, whether through private or public governance mechanisms, will go a long way in reframing corporate and investor fiduciary duties to include other stakeholders, such as the environment. The growing consensus that the corporation is undoubtedly responsible for much of the effects of climate change and thus must

[95] Manning, *supra* note 44, at 429.
[96] Emeka Duruigbo, *Tackling Shareholder Short-Termism and Managerial Myopia*, 100 KY. L.J. 531, 566 (2012)
[97] Manning, *supra* note 44, at 434.
[98] *Id*; John H. Matheson & Brent A. Olson, *Corporate Law and the Longterm Shareholder Model of Corporate Governance*, 76 MINN. L. REV. 1313, 1371-72 (1992).
[99] *Id*; *See* P. Alexander Quimby, *Addressing Corporate Short-Termism Through Loyalty Shares*, 40 FLA. ST. U. L. REV. 389, 395 (2013).

take on a larger role in mitigating and reversing these effects requires corporate directors to manage sustainability performance as an integral part of their fiduciary duties. Ideally, this obligation will propel the formation of more “benefit corporations” and other environmentally focused special-purpose entities. Further, the wide-spread adoption of the stakeholder paradigm informing fiduciary duties is necessary to be able to enforce corporate accountability.

As a driving force in capital management and allocation, institutional investors must continue to push ESG objectives as their ownership and control of global markets expand. Regardless of institutional investors motivations for riding the climate-centered “tectonic shift,” they must substantially increase their ESG and stewardship budgets in relation to the revenue their fees generate. Corporate norms, such as those favoring short-termism, must shift to allow directors to account for non-shareholder interests and long-term perspectives. Long-term oriented companies and capital markets will not solve the climate crisis singlehandedly, but they are necessary to achieving Paris Agreement goals.

## IV. ESG in the Context of Lawyer & Fiduciary Ethics

There is already a business case for ESG within current fiduciary duty paradigms. Empirical studies looking at large universes of companies over long periods of time indicate that companies with higher ESG ratings, meaning these companies were doing a better job of managing financially relevant ESG issues, in comparison to their industry peers with similar businesses, were more profitable, had higher valuations and were less likely to suffer major draw downs.[100] Moreover, there is a growing belief that incorporating ESG factors into investment strategies will lead to better risk-adjusted returns for clients by mitigating systemic risk at a

[100] *See e.g.*, *ESG now.: ESG is Becoming Polarized— It Doesn’t Need to Be*, MSCI ESG Research LLC (March 10, 2023) (downloaded using iTunes).

portfolio level.[101] In fact, indices based on ESG parameters appear to have done better during the financial downturn following the 2020 Coronavirus pandemic.[102] For many corporations, ESG-related issues are already financially material[103] and policy and regulatory frameworks are changing to require ESG information.[104] It's not a matter of if "E" factors will have a material effect on long-term investment returns and value, it's a matter of when.

While we have seen some progress in the shifting of corporate norms towards increased sustainability, these norms need to go farther, faster, to meet Paris goals. Lawyers, through our ethical mandate, can drive this charge. Arguably, the Professional Rules of Responsibility can be read to incorporate ESG into existing lawyer duties. Rule 1.13 states that a lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.[105] Comment 1 to the Rule defines organizational constituents as officers, directors, employees, and shareholders.[106] Thus, Attorneys' representative duty to an organization is ultimately a duty to the people components of the organization. This definition is compatible with the shift away from shareholder primacy to stakeholderism, endorsed by the Business Roundtable in 2019.

This is not the only ethical basis justifying attorney advocacy for ESG incorporation. Rule 2.1 states that lawyers shall exercise independent professional judgment and render candid

[101] *See* Paul Davies, *The UK Stewardship Code 2010-2020 From Saving the Company to Saving the Planet?* 8 (Eur. Corp. Governance Inst., L. Working Paper No. 506/2020, 2020), https://ecgi.global/sites/default/files/working_papers/documents/davies5062020final.pdf.
[102] *See* Gillian Tett, Billy Nauman, Patrick Temple-West & Andrew Edgecliffe-Johnson, *ESG shines in the crash; legal milestone for ratings*, FIN. TIMES (Mar. 13, 2020), https://www.ft.com/content/dd47aae8-ce25-43ea-8352-814ca44174e3.
[103] Myers, *supra* note 41, at 1004.
[104] *Id.*
[105] Model Rules of Prof'l Conduct r. 1.13.
[106] Model Rules of Prof'l Conduct r. 1.13 cmt. 1.

advice.[107] Importantly, the Rule drafters note the inclusion of unpleasant advice.[108] Candid advice includes a rendering of social and environmental realities, and the risks that these realities pose to a client organization's success. The Rule goes farther to say: "It is proper for a lawyer to refer to relevant moral and ethical considerations in giving advice. Although a lawyer is not a moral advisor as such, moral and ethical considerations impinge upon most legal questions and may decisively influence how the law will be applied."[109] This growing shift in attitude towards the expansion of fiduciary duties to other corporate stakeholders indicates an eventual commensurate shift in how current law is applied. Thus, attorneys must anticipate and take preemptive action on ESG matters.

The inevitability of climate change necessitates a broadening of the current interpretation of fiduciary duties beyond profit maximization. The fiduciary duties of loyalty and care, protected by the business judgment rule, should require the incorporation of ESG issues.[110]

Holding fast to the profit-maximization paradigm of fiduciary duties without considering other values and stakeholders is the approach that has landed us in our current position: desperate to avoid the consequences of irreversible environmental degradation. At the end of the day, the ultimate beneficiaries of investment decisions and corporate shareholders are people, who may benefit more from a clean environment, safe consumer products, and other social goods, than from increased returns.[111]

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[107] Model Rules of Prof'l Conduct r. 2.1.
[108] Model Rules of Prof'l Conduct r. 2.1. cmt. 1 ("Legal advice often involves unpleasant facts and alternatives that a client may be disinclined to confront.").
[109] *Id*. at cmt. 2.
[110] *See* Janet E. Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board's Decision to Engage in Social Entrepreneurship*, 29 CARDOZO L. REV. 623, 634 (2007).
[111] *See* Ann M. Lipton, *ESG Investing, or, If You Can't Beat 'Em, Join 'Em* 5 (Tulane Pub. L. Rsch. Paper No. 20-19, 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3715935