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An Open Systems Approach to Law, Strategy, and Sustainability: The Role of the In-House Counsel in the Anthropocene Era

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Introduction

In an embarrassing rebuke, referred to by some as "the vote heard round the world" (Le Berre, 2021), the board of directors of oil and gas giant ExxonMobil lost a proxy contest in May 2021 mounted by a group of institutional investors who faulted the company for not adequately taking into account the effects of climate change and the likely ensuing global regulation of greenhouse emissions on the firm's strategy and operations (National News, 2021). The insurgents forced the company to replace three members of its twelve-member board with the former chief executive of the oil and gas refinery Andeavor; a former Neste executive involved with Neste's expansion into renewable fuels; and a strategist at Alphabet's X innovation lab who is also a former U.S. assistant energy secretary (National News, 2021). The institutional investors voting for the insurgent slate included BlackRock, Vanguard, and State Street (Phillips, 2021). Clearly environmental concerns had moved from being a niche concern of "tree huggers" to major hard-core financial players concerned with ensuring a robust return for their clients, who include life insurance beneficiaries and pension holders who might not collect benefits until decades in the future. One must ask whether the general counsel of ExxonMobil could have done anything differently to have avoided this result.

We are living in what scientists call the Anthropocene Era (Bagley, Sulkowski, Nelson, Waddock, & Shrivastava, 2020: 548). It is "characterized by a new and dangerous climate state brought about through the dominance of a single species (*Homo sapiens*) breaking through the photosynthetic energy barrier, the human-directed evolution of other species, and the increasing interaction of the biosphere with technology" (Gasparin et al., 2020: 385-386, quoted in Bagley et al., 2020). As Rachel Kyte, dean of the Fletcher School at Tufts University, put it, "We are at the point where climate change means systems change—and almost every system will change" (quoted in Worland, 2021).

Human-made law and associated institutions are a critical aspect of the business, institutional, and planetary "ecosystems" within which firms operate (Capra & Mattei, 2015). There is accordingly "an inherently interactive and symbiotic relationship between the private business organization and the larger society that constitutes its host environment" (Preston & Post, 2012: 12). As a result, an organization's survival over time often depends on its "conforming to normative expectations rather than simply operating with greater efficiency" (Fiss & Zajac, 2006: 1173).

This paper applies the open systems approach to integrating law, strategy, and sustainability first introduced in the *Academy of Management Learning & Education* article entitled "A Path to Developing More Insightful Business School Graduates: A Systems-Based, Experiential Approach to Integrating Law, Strategy, and Sustainability" (Bagley et al., 2020) to the evolving role of the in-house counsel at a time when investors and other stakeholders are increasingly calling on corporate leaders to focus on "ESG"—matters associated with environmental, social, and governance issues.

Environmental issues include climate change, reducing carbon emissions, pollution, and deforestation; *social* issues include diversity, inclusion, and equity; privacy; data hygiene and security; immigration and refugee status; community relations; and product safety and customer success; and *governance* issues focus on board composition and executive compensation; ethics and firm culture; compliance; political contributions and lobbying; and hiring and retention best practices (Diligent Insights, 2021).

Companies are realizing that "societal impact" and other legal issues must be incorporated into their business strategy from the outset, and not tacked onto the end after the strategy has already been set based on a review of purely financial considerations (Bagley, 2005). Today's investors, employees, and other stakeholders are demanding more than a singular focus on maximizing profits for shareholders. ESG provides a "more holistic approach by considering the entirety of a business's impact on society" (Womble Bond Dickinson, 2021), especially when embedded within an open systems view (von Bertalanffy, 1968) of businesses' place within planetary ecosystems (Bagley et al., 2020).

The paper proceeds as follows. The first part begins with a discussion of the purpose of the firm and compares shareholder primacy with stakeholder theory. The second part continues the discussion of environmental issues (the "E" in "ESG"). The third part discusses social issues (the "S"). The fourth part outlines governance matters (the "G"), including the board of directors' obligation to have adequate policies and procedures in place to ensure compliance with the law. It also discusses the need for legally astute managers advised by strategically astute counsel. The last part embeds all of the foregoing in a graphic depiction of the open systems model of law, strategy, and sustainability (first described in Bagley et al., 2020, and depicted in graphic form in Bagley, 2021).

Purpose of the Firm: Shareholder Primacy Versus Stakeholder Theory

As the threats associated with climate change have become indisputable, the role humans have played in the degradation of planetary ecosystems has become undeniable, and economic inequalities (both within countries and among them) have become gaping, both experts and average citizens have increasingly questioned whether basing economies on capitalist systems largely run by firms operating on the premise that their purpose is just to earn profits for the shareholders is fair, just, equitable, and ultimately sustainable. Dominic Barton, the global managing director of the consultancy McKinsey & Company, put it this way: "business leaders face a stark choice: Either they reform capitalism, 'the greatest engine of prosperity ever devised,' or stand by and watch as government takes control" (quoted in Bagley, 2021). Although scholars had questioned shareholder primacy in earlier years (see, e.g., Bagley & Page, 1999), the volume and tenor of the criticism of a singular focus on shareholder returns has become both louder and more insistent.

In a recent Deloitte survey, 63% more millennial workers surveyed thought that the primary purpose of businesses should be "improving society" instead of "generating profit" (cited in Fink, 2019). As Larry Fink, CEO of BlackRock, the largest institutional investor in the world, pointed out in his 2019 letter to CEOs, "[i]n the years to come, the sentiments of these generations will drive not only their decisions as employees but also as investors". This demographic change means that "environmental, social, and governance issues will be increasingly material to corporate valuations" (Fink, 2019). This is true not only for companies and investors based in the United States but globally.

Economic Sciences Nobel Memorial laureate Milton Friedman famously asserted that "the one and only obligation of business is to maximize its profits while engaging in open and free competition without deception or fraud" (Friedman, 1962: 133). But faced with unsustainable environmental degradation, continued and widespread corporate wrongdoing, and massive civil unrest, more and more experts are pushing back. Professors Henry Mintzberg, Robert Simons, and Kunal Basu characterized the assertion that corporations exist solely to maximize shareholder value as a "half-truth" that contributed significantly to the "syndrome of selfishness" that took hold of corporations and society in the late twentieth and early twenty-first century (Mintzberg, Simons, & Basu, 2002: 67). They argued that focusing on shareholder value without taking account of other stakeholders' interests "reflects a fallacious separation of the economic and social consequences of decision making" (Mintzberg et al., 2002). As corporate governance expert Lynn Stout put it, managers "can choose to maximize profits; but they can also choose to pursue any other objective that is not unlawful, including taking care of employees and suppliers, pleasing customers, benefiting the community and the broader society, and preserving and protecting the corporate entity itself" (Stout, 2013).

The U.S. shareholder primacy model of capitalism is particularly brutal for workers, prompting Stanford Business School Professor Jeffrey Pfeffer to describe the adverse effect U.S. employment practices have on the mental and physical health of U.S. workers in a book of the same name *Dying for a Paycheck* (Pfeffer, 2018). In the United States, employees are generally hired at-will with few guaranteed benefits so they can be terminated by the employer for no reason without severance pay or continued benefits. As a matter of public law, Germany gives the employees of large corporations the right of codetermination whereby workers and work councils have representation on the supervisory board. Japan has historically also been more protective of employees though this has changed a bit more recently. (For an excellent international comparison of various laws governing employment relationships, see Friedman, 2021.)

China is a harder case given the role of the Communist Party in dictating the rules governing business enterprises and their founders, especially ones that seek capital on the foreign equity markets. The purpose of Chinese firms, especially as of late, might be best described as serving the people as represented by the Party.

R. Edward Freeman, the pioneer of stakeholder theory, posits that "profits are not the purpose of business", any more than making red blood cells is the purpose of life (Freeman, 2017: 456). Although humans need red blood cells to live, purpose is "the idea that we stand for something greater than ourselves and our self-interest" (Freeman, 2017: 456).

After the Enron and WorldCom debacles, even leading shareholder primacy-proponent Michael C. Jensen acknowledged the importance of focusing on long-term, not short-term, shareholder value: "Short-term profit maximization at the expense of long-term value creation is a sure way to destroy value" (Jensen, 2001: 8, 16). He cautioned that "we cannot maximize the long-term market value of an organization if we ignore or mistreat any important constituency" (Jensen, 2001: 8, 9).

The importance of taking both the economic and noneconomic interests of all stakeholders into account entered the mainstream of corporate America when the Business Roundtable, an elite group of corporate CEOs, issued a new *Business Roundtable Statement on the Purpose of a Corporation* on August 19, 2019. The 181 CEO-signatories abandoned the shareholder primacy model and replaced it with a stakeholder approach predicated on the belief that sustainable value creation and success over the long-term requires "meeting the needs of all stakeholders" (Business Roundtable Press Release, 2019). They committed to:

- *Delivering value to our customers.* We will further the tradition of American companies leading the way in meeting or exceeding customer expectations.
- *Investing in our employees.* This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect.

- *Dealing fairly and ethically with our suppliers*. We are dedicated to serving as good partners to the other companies, large and small, that help us meet our missions.
- *Supporting the communities in which we work*. We respect the people in our communities and protect the environment by embracing sustainable practices across our businesses.
- *Generating long-term value for shareholders*, who provide the capital that allows companies to invest, grow and innovate. We are committed to transparency and effective engagement with shareholders.

  Each of our stakeholders is essential. We commit to deliver value to all of them, for the future success of our companies, our communities and our country (Business Roundtable Press Release, 2019) (italics added).

Bill McNabb, former CEO of Vanguard, one of the world's largest institutional investors, praised the Business Roundtable's call for more business leadership: "By taking a broader, more complete view of corporate purpose, boards can focus on creating long-term value, better serving everyone – investors, employees, communities, suppliers and customers" (quoted in Business Roundtable Press Release, 2019).

Environmental: The "E" in "ESG"

Larry Fink's 2021 letter to CEOs noted that "[n]o issue ranks higher than climate change on our clients' list of priorities" (Fink, 2021). Climate change is already a "brutal reality in many geographical regions" (Gasparin et al., 2020: 386), and the scientific evidence of the dangers of "catastrophic changes in the Earth's climate" if dramatic reductions in greenhouse emissions and other mitigation measures are not taken are undisputed (UN Environment Programme, 2021).

In May 2021, the same month that ExxonMobil's shareholders replaced three incumbent directors with nominees dedicated to improving the oil and gas company's environmental performance, the District Court in The Hague, where Royal Dutch Shell is headquartered, held that Shell, Europe's largest oil company, was "obligated" to reduce the carbon dioxide emissions resulting from its activities by 45% by the end of 2030 compared with 2019 levels (Reed & Moses, 2021). A spokesperson for the court stated: "Severe climate change has consequences for human rights, including the right to life. And the court thinks that companies, among them Shell, have to respect those human rights" (quoted in Reed & Moses, 2021). The court acknowledged that respecting the reduction obligation "will have far-reaching consequences" for companies and "could curb the potential growth of the Shell group. However, the interest served with the reduction obligation outweighs the Shell group's commercial interests" (quoted in Williams, Eccles, & Mulholland, 2021).

To meet the "aspirational goal of the Paris Agreement", reached in 2015, to maintain global warming in the 21st century at 1.5°C above pre-industrial levels, annual greenhouse gas emissions will have to be cut in half by 2030 (UN Environment Programme, 2021; Masood & Tollefson, 2021). The president of COP26, a meeting in November 2021 in Glasgow, Scotland, of representatives from the 197 countries that are signatories to the United Nations (UN) Framework Convention on Climate Change, stated that the commitments made in Paris had "fallen short" and that steps must be taken now: "We have kept 1.5 degrees alive. But its pulse is weak, and it will only survive if we keep our promises and translate commitments into rapid action" (quoted in Masood & Tollefson, 2021). Maintaining global warming at 1.5°C above pre-industrial levels will require ratification of the Glasgow Climate Pact by the signatory nations, then the reduction of carbon dioxide emissions by 45% from the levels in 2010 by the year 2030 (Masood & Tollefson, 2021).

In 2018, the Committee for the Prize in Economic Sciences in Memory of Alfred Nobel cited *The Stern Report* for the proposition that climate change is "a result of the greatest market failure this world has seen" (Committee for the Prize in Economic Sciences in Memory of Alfred Nobel, 2018). Research by the recipients of the Economic award in 2018—William Nordhaus and Paul Romer—showed that governments and private firms must work together to address the existential threats posed to the Earth and her inhabitants, including humans, by climate change (Committee for the Prize in Economic Sciences in Memory of Alfred Nobel, 2018).

Notwithstanding urgent and repeated calls for action, "business as usual" often remains unchallenged, and "[b]usiness and management education continues to teach and promote human-centered economic models that are profoundly insensitive to the complex interdependencies between human action and the irreversible environmental changes that constitute the currently, and rapidly unfolding, reality of climate change" (Gasparin et al., 2020: 386). Yet, as Larry Fink of BlackRock cautioned, "[t]here is no company whose business model won't be profoundly affected by the transition to a net zero economy" (Fink, 2021). Climate risk is investment risk, but "climate transition [also] presents a historic investment opportunity" (Fink, 2021). The COVID-19 coronavirus pandemic "has [also] intensified discussions about the interconnectedness of sustainability and the financial system" (CFA Institute, 2021). As more investors opt to invest in sustainability-focused companies, "every management team and board" must be proactive and prepare for this lest their stakeholders lose confidence, causing company valuations to suffer (Fink, 2021).

Strategically astute counsel can help management and the board avoid this myopic focus on what the law requires today and help the firm convert seeming constraints into opportunities. Cummins Engine attained a competitive advantage when its lawyers and government affairs representatives lobbied for stricter controls on diesel emissions then, after the firm invested in the R&D necessary to attain those goals, persuaded the regulators to hold firm on the new standards, thereby precluding its competitors from selling their noncompliant dirtier engines (Bagley, 2010).

Diversity, Equity, Inclusion, and Other Social Issues: The "S" in "ESG"

The spread and mutation of the COVID-19 coronavirus is just the latest evidence of the importance of taking into account the relationships among different organisms, inequalities among human populations, and the need for holistic global responses designed to mitigate the negative social, health, economic, and political impacts of the "'Great Acceleration' of population, industrialization, and globalization that started in the mid-20th century . . . ." (Gasparin et al., 2020: 387). In a recent survey of 500 CEOs in eleven markets in the Americas, Asia, and Europe, 96% of respondents indicated that "their response to the pandemic has shifted their focus to the social component of ESG", an increase from 63% in mid-2020 (Lawrie, 2021).

South Africa reported its identification of a new and potentially more transmissible and virulent variant of COVID-19 to the World Health Organization ("WHO") on November 24, 2021. WHO classified it as a variant of concern two days later and dubbed it the "omicron" variant. Within days, the leading world equity markets dropped more than 2.5% and countries began to close their borders. Critics blamed the unwillingness of the richer nations to provide adequate access to and distribution of free vaccines to the poorer countries for the new variants and continued spread of the disease.

Other social factors included within the ESG movement are diversity, equity, and inclusion (DEI); privacy, data collection (including "Big Data"), and artificial intelligence; "Fake News" and other forms of information disorder (Aspen Institute Commission on Information Disorder, 2021); voter manipulation and voting access; customer satisfaction; gender, racial, religious, and LGBTQ+ rights and discrimination; immigration and refugee resettlement; employee health and engagement; community relations; human rights; and labor standards (see, e.g., CFA Institute, 2021).

Employees are now often "demand[ing] that their employers show that they care" (Logan, 2021). During the COVID-19 pandemic, multitudes of workers reconsidered their priorities and moved on to new jobs that have a "more meaningful mission" or offer more flexible working arrangements, including the option to work from home (Logan, 2021; Morgan, 2021). Many have left the workforce entirely in the "Great Resignation".

Fink (2021) noted that we are at a "historic crossroads on the path to racial justice". Resolution will require not just the enforcement of existing laws but also corporate leadership. A firm that does not avail itself of the "full spectrum of human talent" will probably not have the best talent or reflect the needs of its customers and communities, and thus will be less likely to outperform its competitors (Fink, 2021). Yet individuals in multiple countries remain deeply divided over immigration and the acceptance of refugees from countries with different dominant religions or ethnic backgrounds.

Political and other social issues Many executives have tried to avoid speaking out on highly charged political and social issues, such as the U.S. social movement Black Lives Matter (BLM) and its critics (who include white supremicists, sometimes bearing Nazi insignia); voting restrictions making it harder for non-Whites to vote; and anti-refugee settlement movements in Europe. But it is becoming more difficult for business leaders to stay silent.

After Donald Trump claimed to have lost the 2020 U.S. presidential election due to alleged voter fraud, Georgia, Florida, Texas, and other states passed legislation making it harder for Blacks to have their votes counted. Various organizations urged companies to fight voting restrictions by, for example, issuing joint statements condemning restrictive voting proposals, testifying in front of legislators, and withdrawing financial support from legislators who supported such restrictions (Bagley, 2021). Activists also called on companies headquartered in states with restrictive voting laws to vote with their feet by moving events from such states in protest. Rob Manfred, the Commissioner of Major League Baseball, did just that when he decided in April 2021 to relocate the All-Star Game from Georgia.

Former American Express CEO and Chair Ken Chenault (the third Black to serve as the CEO of a Fortune 500 company) has been particularly effective rallying other business leaders to speak up against restrictive voting laws, stating: "[c]orporations have to stand up. There is no middle ground. This is all about Americans having the right to vote, but we need to recognize the special history of the denial of the right to vote for Black Americans, and we will not be silent" (Stankiewicz, 2021).

Harvey Golub, also a former American Express CEO and chair, who happens to be White, disagreed. He "argue[d] that it is not the role of companies to speak on political issues" unrelated to the business (Fox News, 2021). Senate minority leader Mitch McConnell (R-Kentucky) agrees with him, though he sees no problem with corporate campaign contributions and lobbying (Goodkind, 2021).

Hubert Joly, the former CEO of Best Buy, an electronics chain headquartered in Minneapolis, Minnesota, where a White police officer was convicted of murdering George Floyd, a Black man arrested for allegedly using a counterfeit $20 bill at a convenience store, took more of a systems approach to social issues. When addressing the civil unrest in Minneapolis that occurred after Floyd's murder as advocates for BLM clashed with police and opponents of the BLM movement, Joly stated: "When the city is on fire, you cannot run a business. If the planet is on fire, you cannot run a business" (quoted in Joly & Fleming, 2021). One thing does appear certain: It is likely to be increasingly difficult for business leaders to avoid politics and charged social issues or at least explaining why their firm has decided not to take a stance.

Campaign spending and lobbying Countries vary in their rules regarding corporate campaign contributions and where to draw the line between corruption and ensuring access to government officials so politicians and administrative officers understand the legitimate concerns of business entities. In the United States, "The Supreme Court's decision in Citizens United v. FEC greenlit a whole new ability for corporations to spend on politics" (Torres-Spelliscy, 2021; see also Citizens United v. Federal Election Commission, 2010). Corporations in the United States spent more than $100 million in the 2020 federal elections, with at least $33 million coming from publicly traded companies (Torres-Spelliscy, 2021).

Even if a country does not permit corporations to donate money to candidates or parties, lobbying is generally permitted. A survey of Swedish in-house counsel revealed that 54% of the responding firms engaged in lobbying, with 7% hiring outside counsel with political lobbying experience; but 31% did no lobbying at all (Bagley, Roellig, & Massameno, 2016: 496).

A 2017 article in the *Harvard Business Review* provides a framework to help boards make decisions about whether their company should engage in corporate spending and other political activities. At a minimum, such decisions should be informed; comply with applicable law; be consistent with the company's strategies, policies, and values; and mitigate risks as much as possible (Bagley, Freed, & Sandstrom, 2015). "Dark money spending", where corporate money can be "hidden when it is spent using [certain] opaque nonprofits", can be particularly risky (Torres-Spelliscy, 2021). Increasingly, investors are demanding transparency so they know how their money is being spent (see, e.g., Carroll, Freed, Sandstrom, Holguin, & Hardin, 2021).

Governance: The "G" in "ESG"

Governance includes the purpose of the firm and the top management team's and board's relationship with the firm's stakeholders (discussed earlier), integrity and compliance with law, the processes by which the board exercises informed judgment when making decisions, and executive compensation.

Corporate boards are the "ultimate guardian of the firm's financial, human, and reputational capital" (Bagley, Cova, & Augsburger, 2017). "'[I]ssues surrounding social impact and responsibility'" are "'core business decisions'" that are "'inextricably linked to the value of a company"' (Womble Bond Dickinson, 2021) (internal citation omitted). As such, they should be part of the regular board agenda (Womble Bond Dickinson, 2021) and the basis for ongoing communications with in-house legal counsel. Counsel must ensure that the hard questions are asked even if it means putting the CEO or other officers on the spot. Of course, every effort should be made to avoid blindsiding the CEO by raising tough issues with the CEO first but, if the chief legal officer is not satisfied with the answers provided, the lawyer should escalate the issue to the board.

Compliance with law According to the Organisation for Economic Co-operation and Development (OECD), "the first obligation of enterprises" is to obey domestic law (OECD, 2011: 17). In an essay published in 2021, Economic Nobel Memorial laureate Nordhaus stated that he would damn firms ranging from Volkswagen (which used "cheat" software to falsify pollution control tests) to Purdue Pharma (which misled physicians and patients about the addictive nature of the opioid oxycontin) to Philip Morris (the cigarette maker that lied about the addictive nature of cigarettes then added more nicotine to make them more addictive) to Dante's Ninth Circle of Hell for their irresponsible conduct (Nordhaus, 2021: 68, 69). Other candidates include Parmalat, Deutsch Bank, Barclays, General Motors, and Toyota.

Independence of counsel and reporting up It is unclear what the general counsel at Volkswagen knew about the cheat software used to fraudulently and falsely certify the emissions of its diesel engines, but the company's chief compliance officer was convicted of knowingly violating the U.S. Clean Air Act. The CEO was also forced to resign. Similarly, BP was fined billions for the Deepwater Horizon oil spill, which was just one in a series of mishaps that many attributed to a firm culture that did not put a premium on safety. The general counsel of General Motors claimed to have been unaware of the potentially deadly ignition-switch defects that were kept hidden for more than a decade by in-house lawyers working under him who had used confidentiality agreements to settle cases in secret. At a minimum, the general counsel "had failed to create a culture in which his in-house counsel and external attorneys knew they were expected to report up to him any material legal or safety issues" (Bagley et al., 2016: 444).

In-house counsel need to work as strategic partners with their clients but never lose sight of their obligations as fiduciaries of the corporation and as officers of the court (Auerbach, 1984). Instead of "kowtow[ing] to the prerogatives of senior management" and "'defer[ring] to management's judgments about legal risk'" (Bagley et al., 2016: 438, quoting Nelson & Nielsen, 2000: 457) and giving undue "priority to business objectives rather than legal [imperatives]" (Nelson & Nielsen, 2000), counsel must jealously guard their "'cognitive independence'" so "unethical legal risks are [not] irrationally assumed" (Langevoort, 2012: 496) (internal citation omitted). Indeed, "one of the most challenging roles of general counsel is to have the courage and foresight to respond to the assertion, 'Everyone else is doing it this way,' with 'But we don't,' then move the dialogue to a discussion of how the firm might otherwise accomplish the business objective with less risk" (Bagley & Roellig, 2014).

Directors should have direct access to independent outside counsel (paid for by the company) if a contentious issue arises or there is even the appearance of a conflict of interest with a transaction or issue handled by the in-house counsel (Bagley et al., 2016: 459). For example, if in-house counsel has handled an internal employee complaint of sexual harassment by the CEO or another officer and the employee has threatened to sue, independent directors advised by independent counsel who do not normally represent the company should promptly evaluate the complaint and determine what action is necessary and appropriate. The "#MeToo" movement has underscored the reputational risks associated with neglecting to take such complaints seriously and failing to deal with them in an impartial, timely, fair and just manner.

While General Counsel and Executive Vice President of MassMutual Financial, Mark Roellig annually sent a letter to every outside lawyer making it clear that they were expected to report to general counsel any issue they saw where they believed the company's lawyers or other employees were violating the law (Bagley et al., 2016: 440). If the CEO or general counsel were involved, the letter instructed outside counsel to report any such activity to the CEO and ultimately report it to the board (Bagley et al., 2016: 440).

Importance of having legally astute managers Unfortunately, many business schools have dropped legal studies and business law from the core curriculum (Bagley et al., 2016). As a result, their graduates are often not legally literate and may lack the ability to engage with their counsel in a nuanced analysis of corporate governance, fiduciary duty, contracts, securities regulation, environmental law, employment law and discrimination, and other areas of law critical to running their business. A study of Swedish in-house counsel revealed that only 35% of responding counsel strongly agreed with the statement the "CEO of my company understands the laws and regulations most important to our business" (Bagley et al., 2016: 501). Thirty percent of the respondents either strongly agreed or agreed that their CEO would make an important decision without first consulting with counsel (Bagley et al., 2016: 499). It is hard to know when to call a lawyer when you do not even know what laws are involved. Only 69% of the respondents agreed or highly agreed that "[i]n my company, the board of directors expects the head of the legal department to alert it to highly risky choices by management"; 25% disagreed; and 6% were neutral (Bagley et al., 2016).

Effective management in today's dynamic and challenging environment requires legally astute managers advised by strategically astute counsel. Legal astuteness requires (1) a set of value-laden attitudes about the importance of law and ethical behavior to firm success, (2) a proactive approach to regulation and risk, (3) the ability to exercise informed judgment when managing the legal and business aspects of the firm, (4) context-specific knowledge of the law and the appropriate use of legal tools, and (5) strategically astute counsel (Bagley et al., 2016: 449) (internal citations omitted). Indeed, legal astuteness may be a valuable dynamic capability (Teece, 2007) and source of competitive advantage (Bagley, 2010, 2016).

Strategically astute counsel understand business fundamentals (including accounting, finance, management, and strategy), the applicable law, and the appropriate use of both managerial and legal tools (Bagley et al., 2016: 453). They know how the company makes money and are not afraid to ask questions when they do not understand something. Strategically astute counsel exercise informed judgment to determine "what is ethically and societally right and wrong, what is acceptable and what is not" (Bagley et al., 2016: 453). They "deliberate, for and with their clients, about the wisdom of their clients' ends, as opposed simply to supplying them with the legal means for realizing their desires" (Kronman, 1993: 133). They also understand that every legal dispute is a business problem requiring a business solution (which may include litigation) and work hand-in-hand with their clients to craft such solutions.

Strategically astute in-house counsel seek a place at the table from the outset, understanding that a "lawyer whose only responsibility is to prepare the way for ends that others have already set can never be anything but a deferential servant" (Kronman, 1993: 458). To promote better communication, build trust and enhance psychological safety (see, e.g., Edmondson & Mortensen, 2021), and make sure the in-house counsel is kept in the loop, counsel should avail themselves of opportunities to be physically close to the CEO and other business leaders (such as by having an office nearby even if it is smaller than one farther away), attend management meetings and forums, and engage in informal personal and business meetings and gatherings. For example, when the general counsel of USG Corporation was working to resolve the company's asbestos liability, his physical proximity to the CEO's office and their daily interactions were key to the blended legal-financial-political-business strategy that ultimately led to a resolution investor Warren Buffett called "the most impressive performance in bankruptcy I have ever seen" (Bagley, 2007).

Duty of directors to have appropriate compliance processes in place Boards are required to ensure that there are appropriate processes and procedures in place to ensure compliance with law. In November 2021, the directors of Boeing, the world's largest aerospace company and a leading manufacturer of commercial jetliners, settled a case for alleged breach of that duty for $237.5 million; they also agreed to implement various safety and oversight protocols and other corporate governance measures, all subject to court approval (LaCroix, 2021). The case (*In re* Boeing Derivative Litigation, 2021) involved two fatal crashes of the Boeing 737 MAX aircraft, the first in October 2018 and the second five months later, killing a total of 346 people.

Shareholders brought a derivative action against the directors in 2019, alleging that they were liable because they failed to exercise proper oversight over a "mission-critical aspect" of Boeing's business (Banks & Sweeny, 2021). To prevail under the relevant standard set forth in *In re* Caremark International Inc. Derivative Litigation (*In re* Caremark

International Inc., 1996; Michaeli & Philp, 2021), the plaintiffs had to prove that either the directors "completely failed to implement any reporting or information system or controls"; or that "[h]aving implemented such a system or controls, [they] consciously failed to monitor or oversee its operations, thus disabling themselves from being informed of risks or problems requiring their attention" (Banks & Sweeny, 2021).

It is unclear what, if any, specific advice Boeing's in-house or outside counsel gave the board regarding its obligations to review the company's safety protocols before or after the first and second crashes. Because courts rarely find that plaintiffs have pleaded adequate facts to satisfy the tough *Caremark* requirements for legal liability (Strine, Smith, & Steel, 2021: 1897), it must have been a shock to the Boeing directors and their lawyers when the court denied the defendants' motion to dismiss. Instead, the court found that the plaintiffs had shown that the board's failure to act after the first fatal crash "amounted to a conscious failure to oversee operations despite their awareness of a safety concern"; the directors completely failed to implement a safety reporting system; they did not have a committee that focused on airplane safety; they did not provide for regular reviews of airplane safety risks; and they never created a board-level reporting mechanism for safety concerns from management (Banks & Sweeny, 2021). "After the first crash, the board did not request any information about the safety of the 737 Max and passively accepted management's assertions that the plane was safe, ignoring safety red flags suggesting that it was not" (Banks & Sweeney, 2021). Even after the second crash, when the board was on notice that its existing safety precautions were not effective, the board did not establish a board safety committee. Instead, it continued to passively rely on management to diagnose and fix the problems.

A recent study of forty-eight corporate directors who sit on the boards of one hundred and forty diverse companies found "conclusively" that the directors viewed their jobs "as primarily supporting managers, not monitoring them" (Boivie, 2021). Most of the respondents said it was not possible to effectively monitor the work of the CEO or other executives because those individuals know more about the company than the directors. The authors of the study concluded that while investors, regulators, employees, and other stakeholders often blame the board of directors for company misbehaviour, their expectations of directors needed to be "reconcile[d]" with the "realities of the boardroom" (Boivie, 2021).

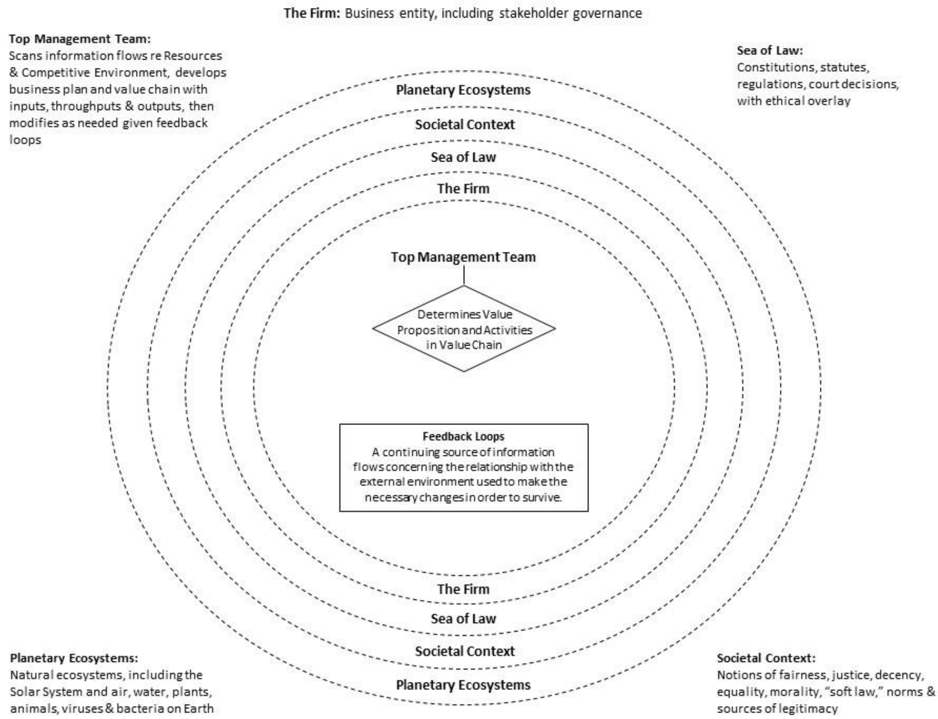
Bruno Cova, the former General Counsel of Fiat who oversaw the legal aspects of the Parmalat securities fraud investigation, Lee Augsburger, who was chief compliance officer at MassMutual Financial, and I disagree. In a *Harvard Business Review* article, we argued that legally astute directors and their strategically astute counsel can and will "set their bar higher, and replace reactive approaches to misbehavior with a proactive approach to winning with integrity. Instead of assuming everything is fine unless they hear otherwise, directors need to be more probing" (Bagley et al., 2017). We then set forth a ten-step program of strategic compliance management aimed at helping firms reduce the risks of illegal behaviour, reinforce ethical conduct as a core value, and enhance the company's reputation as a good corporate citizen, as viewed by both regulators and stakeholders (Bagley et al., 2017).

The Open Systems Approach to Law, Strategy, and Sustainability

Managers and business leaders often lack the nuanced transdisciplinary insights necessary for them to be able to tackle the "grand challenges of the present [which] cut across multiple dimensions of human life—material, economic, environmental, social, cultural, technical, political, medical, aesthetic, and moral" (National Academies of Sciences, Engineering and Medicine, 2018:12). Counsel and ethics and compliance officers can help by providing interactive, engaging, and tailored materials and by offering master classes taught by outside experts to help fill these gaps (Bagley et al., 2017).

Figure 1, the open systems approach to law, strategy, and sustainability, provides a graphic guide for coordinated deliberation among business leaders and their counsel. It places the top management team within the open systems that comprise our world and shows the importance of information flows and feedback loops. (Figure 1 is based on the textual analysis and cited works in Bagley et al., 2020, and on Figure 3 in Bagley et al., 2016: 473. Katz and Kahn (1966) are commonly credited with applying the open systems approach to the business organization (Bagley et al., 2020: 550, citing Mele, Pels, & Polese, 2010).

FIGURE 1: Open Systems Approach to Law, Strategy, and Sustainability



> At the center . . . is the firm's leadership: "one of the most critical resources for a successful corporate strategy" (Bagley et al., 2020: 550, quoting Shanley & Peteraf, 2004: 293). "The firm's strategic decisions and courses of action are informed by the education and other characteristics of the firm's top management team . . . as well as the team's dynamic capabilities, including its legal astuteness" (Bagley et al., 2020: 550). "The leadership scans available information flows to identify resources, opportunities, and threats. Leaders use heuristics to craft a value proposition and to define, orchestrate, perform, and modify the activities in the value chain" (Bagley et al., 2020: 550) (internal citations omitted).

The firm takes inputs from the environment and, with its human capital and other intangible resources, such as intellectual property and its dynamic capabilities, then transforms them into products and services. To stay competitive, the leadership of a firm needs to keep track of information flows, so it can alter the firm's value proposition and activities in the value chain in response to shifting customer demand, changes in the competitive environment, the continued availability and cost of resources, evolving societal expectations, and new and amended laws and regulations, including the forced internalization of externalities.

Firms operate in a "sea of law" (Edelman & Suchman, 1997) and are both constrained and enabled by it. Competition law limits the ability of a firm to abuse its dominant position to the detriment of customers and competitors. The EU fined Google $5 billion (€4.34 billion) in 2018 for anti-competitive behaviour, alleging the company had "imposed 'illegal restrictions'" on devices operated with its own Android system to "cement its dominant position in the market" (Euronews, 2021). Google is appealing the decision. Privacy protections limit what information a firm may collect from its customers and share with third parties. The U.S. Federal Trade Commission fined Facebook $5 billion in 2019 for privacy violations (U.S. Federal Trade Commission, 2019), and further investigations in various countries are underway. Multiple jurisdictions are considering whether firms like Google and Facebook have gotten just too big and powerful and should be broken up. They are also subjecting newly proposed mergers and acquisitions to heightened scrutiny.

Through lobbying and other political activities, firms can create opportunities for new business models, as Federal Express did when it persuaded the U.S. federal aviation regulators to permit hub-and-spoke distribution systems. Uber was initially not successful in Germany when it very heavy-handedly tried to bully its way into certain towns (Scott, 2016). More recently it has decided to "play[] nice" and is currently operating in a number of German cities (Moore, 2021). Its ultimate success there is, however, still "far from guaranteed" (Moore, 2021).

Patents can create barriers to entry and prevent the introduction of substitutes but, as seen with HIV drugs and the COVID-19 vaccines, patents can create a societal backlash from poorer nations against the pharmaceutical companies holding the patents. This feedback loop may force the firms or the governments that granted the patents to provide the drugs at a discount or for free.

Purdue Pharma drowned in the sea of law after its fraudulent representations about the addictiveness of OxyContin drove the firm into bankruptcy, dragged down by the weight of criminal and civil fines and forfeitures in excess of $8 billion (U.S. Department of Justice, 2020). Like a cybernetic governor (von Bertalanffy, 1968: 21), society will demand stricter regulation or deregulate certain activities, such as the sale of cannabis in parts of the United States or prostitution in Amsterdam, as conditions and societal mores shift over time. Finally, and most dramatically, firms affect planetary ecosystems and planetary ecosystems affect firms and the humans who work in them, buy and sell their products, supply various inputs, partner with them, compete with them, and are forced to deal with the messes they make.

Conclusion

Establishing the firm's strategy and modifying it in response to information flows and feedback loops is a key responsibility of the board of directors and the top management team, ideally acting with informed counsel from strategically astute legal advisors. The concepts behind the business policy courses first developed at Harvard Business School (HBS) were the precursors of the field of strategic management (Nag, Hambrick, & Chen, 2007: 935). There were four pillars:

1) appraisal of present and foreseeable *opportunity* in the company's *environment*;
2) assessment of the firm's unique combination of present and potential corporate *resources* or *competencies*;
3) determination of the *noneconomic personal and organizational preferences* to be satisfied; and
4) identification and acceptance of the *social responsibilities of the firm*.

(Christensen, Andrews, & Bower, 1973: 584) (italics added).

They remain as relevant today as when they were first taught to MBA students in the 1960s (see, e.g., Learned, Christensen, Andrews, & Guth, 1969). From the outset, the HBS business policy curriculum taught future managers that they must consider not only what they *could* do, but also what they *should* do. As a result, addressing the moral aspects of strategic choice required navigating "the tangle of ethics" (Bagley et al., 2020: 543, quoting Christensen et al., 1973: 578). As Economic Nobel Memorial laureate William Nordhaus explained, far too many business leaders have forgotten that admonition and engaged in patently unethical and illegal conduct to the detriment of not only planetary ecosystems and other stakeholders but also their own shareholders.

Similarly, former Yale Law School Dean Anthony Kronman cautioned that corporate lawyers were losing their "soul" and called on them to act less like commercial agents and more like lawyer-statesmen (Kronman, 1993: xiv). Decades earlier, U.S. Supreme Court Justice Louis D. Brandeis had warned that "lawyers have, to a large extent, allowed themselves to become adjuncts of great corporations and have neglected the obligation to use their powers for the protection of the people" (Brandeis, 1914: 337, quoted in Altman, 2003: 2406).

Human and corporate survival, and dare we hope flourishing, in the Anthropocene Era requires scrupulous attention to the morality and sustainability of personal and organizational behaviour. It requires integrity and radical acceptance of the limits imposed by the open systems within which we live and the organizations through which we do business. It also requires the humility to acknowledge how little control humans actually have over their world and how much we have to learn from others, including Indigenous Peoples, our elders, and non-human species.

Like a toddler trampling through an herb garden nurtured and tended for generations by wiser elders, too many industrialists, technocrats, entrepreneurs, and financiers and their counsel have literally taken a scorched earth approach to our island home in space, what astronomer Carl Sagan called the "pale blue dot" (Sagan, 1994). But one thing is clear: governments cannot solve these existential challenges alone. Nor can individuals acting alone. Businesses must step up even when the short-term profit of doing so is uncertain. But will their leaders and their counsel have the moral courage, will, creativity, and skills to make a difference? Taking a dialectic view and framing today's choices as both challenges and opportunities embedded within complex open systems strikes this author as a good place to start.

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Bagley Strategic Advisors LLC (BSA) is a boutique consultancy based in Connecticut, USA. BSA offers customized strategic counsel and advice, master classes, workshops, and other high level and specialized training for executives and entrepreneurs, including in-house counsel, outside law firms, board members, and venture capitalists in multiple countries, including the United States, Italy, Russia, and Guatemala. As CEO of BSA or in her individual capacity, Professor Bagley has extensive experience teaching and preparing materials for in-house counsel and managers, both in master classes for clients such as MassMutual Financial, Microsoft, CVS Health, Prudential Financial, and the Medical Companies of Colson Associates, and at the Practicing Law Institute's Corporate Counsel Institute and Stanford Law School's Directors College. She works closely with BSA's distinguished Advisory Board, which includes Jeffrey Pfeffer, Professor of Organisational Behaviour at the Stanford Graduate School of Business; Elizabeth P. Smith, formerly Vice President-Investor Relations and Shareholder Services and Corporate Compliance and Ethics Officer at Texaco, Inc., and Chair of the Board of Finance, Town of Darien, Connecticut; Nihal De Lanerolle, Professor of Neurosurgery and of Neurobiology Emeritus at the Yale School of Medicine; Paul T. Dacier, Executive Vice President and General Counsel of EMC Corporation prior to its merger with Dell Technologies; and Angela T. McConnell, Executive Director of the Montalvo Arts Center. Professor Bagley has coauthored multiple book chapters and articles with Mark Roellig, currently Senior Client Advisor at Perkins Coie, and formerly General Counsel and Executive Vice President, and Chief Technology and Administrative Officer, of MassMutual Financial where she worked closely with him and his team developing and delivering multiple master classes.

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