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# **The NEW Revolving Door of Legal Advisors** **: Evidence from Environmental Enforcement**

by

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# Motivation

## ❑ Revolving door



From Financial Times, May 30 2013, (Pancho)

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# Motivation

## ❑ Benefits and risks of revolving door

### ▪ Benefit:

- ✓ Expertise
- ✓ External governance on regulatory agencies
- ✓ Human capital

### ▪ Risks:

#### ✓ Rent seeking

➤ Entry model

➤ Exit model

#### ✓ Public-private connection



From Financial Times, May 30 2013, (Pancho)

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# Motivation

- ❑ Public-private connection
  - **Former officials may leak proprietary information (Jerke, 2010)**



From Financial Times, May 30 2013, (Pancho)

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## **Motivation**

- ❑ Information leakage from public sector is not uncommon

*The New York Times*

### ***Ex-Goldman Banker and Fed Employee Will Plead Guilty in Document Leak***

By Ben Protess and Peter Eavis

Oct. 26, 2015

- The banker at Goldman Sachs (former employee at the New York Fed for seven years) was assigned to advise one of the banks in New York he previously regulated. The banker has received government information about the bank from his former colleague still working at the NY fed

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## Motivation

- ❑ Post public employment in legal sector

### FINANCIAL TIMES

## European Commission cracks down on revolving door of law firm jobs

Brussels staffers seeking to go on unpaid leave told they can no longer work for private companies

**Javier Espinoza** and **Sam Fleming** in Brussels SEPTEMBER 26 2022

- Substantial number of former government officials transition into the legal industry!!!

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## **Research questions**

- ❑ 1. Do firms gain advantages from affiliating with law firms that employ former government officials?**
  
- ❑ 2. Is the influence derived from expertise or potential information leakage?**
  
- ❑ 3. Evidence on potential information leakage**

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## **Preview of the findings**

- ❑ **1. Do firms gain advantages from affiliating with law firms that employ former government officials?**
  - Companies associated with law firms employing former EPA employees experience notably reduced enforcement actions
  
- ❑ **2. Is the influence derived from expertise or potential information leakage?**
  - Companies associated with law firms employing former EPA employees exhibit a temporary decrease in toxic chemical releases during periods of heightened investigation risk.



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## **Preview of the findings**

### **❑ 3. Evidence on potential information leakage**

- Corporate insiders realize significant profits from insider trading
  - ✓ Leading up to the final court ruling dates of EPA enforcement actions
  - ✓ Leading up to major changes to toxic chemical releases reporting scheme (EPA's TRI reporting program)

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## **Contribution**

- ❑ **Literature focusing on pre-private employment of public officials**
    - Lucca, Seru, Trebbik, 2014; Ed dehaan, Kedia, Koh, Rajgopal, 2015; Tabakovic and Wollmann, 2018; Kalmenovitz, Vij, Xiao, working
  
  - ❑ **Literature focusing on post-public employment of public officials and impact on corporate policies**
    - Correia, 2014; Lambert, 2019; Heese, 2022, Hendricks, Landsman, Pena-Romera, 2022
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## **Contribution**

- ❑ **Literature on public-private connections and insider trading**
  - Reeb, Zhang, Zhao, 2014; Jagolinzer, Larcker, Ormazabal, Taylor, 2020
  
- ❑ **Literature on the relationship between law firms (legal advisors) and corporations**
  - Krishnan, Masulis, 2013

# Focusing on revolving door legal advisors from the Environmental Protection Agency (EPA)

## ❑ Federal Agency Revolvers

White House	806	13.55%
US House of Representatives	737	12.39%
Dept of State	376	6.32%
Dept of Defense	348	5.85%
Dept of Commerce	320	5.38%
Dept of the Treasury	314	5.28%
Dept of Health & Human Services	275	4.62%
Presidential Transition Team	269	4.52%
Dept of Energy	256	4.30%
Dept of Justice	252	4.23%
Environmental Protection Agency	218	3.66%

From Opensecret.org

# Focusing on revolving door legal advisors from the Environmental Protection Agency (EPA)

## ❑ Top employers of the revolving door officials

Top Employers (Lobbying firms)			
Organization	Former	Current	
Akin, Gump et al	117	123	
Patton Boggs LLP	150	41	
Covington & Burling	62	97	
K&L Gates	79	77	
Cassidy & Assoc	93	62	
Holland & Knight	54	74	
Van Scoyoc Assoc	67	54	
DLA Piper	50	60	
Hogan & Hartson	70	36	
Venable LLP	46	57	

Top Employers (Companies and private org)			
Organization	Former	Current	
US Chamber of Commerce	105	61	
Pharmaceutical Research & Manufacturers of America	54	24	
National Assn of Manufacturers	36	38	
Lockheed Martin	36	30	
Boeing Co	43	23	
Georgetown University	54	10	
Heritage Foundation	57	6	
Brookings Institution	27	33	
Center for American Progress	43	17	
American Enterprise Institute	35	23	

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# Focusing on revolving door legal advisors from the Environmental Protection Agency (EPA)

## ❑ Revolving door legal advisors from EPA

### ▪ Data sources

- ✓ Opensecret
- ✓ EPA
- ✓ Boardex
- ✓ LinkedIn

\* We only keep within 10 years of job history post EPA

- 93 former employees from EPA (administrators, general counsels, chief of staffs, etc.)
  - ✓ 124 post EPA employment records

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# Empirical design

## □ Empirical setting

- Estimate the treatment effect of former EPA officials joining legal advisors on the EPA enforcement actions against client firms using a stacked difference-in-differences (DiD) regression framework (Gormley and Matsa, 2011)
  - Treatment
    - ✓ Event: ex-EPA officials joining a legal advisor firm
    - ✓ Treatment group: looking back 5 years , treated if the firm has employed the legal advisor in any of the business activities including M&A, debt or equity issuance, loan financing, lobbying / has undergone an IPO with the legal advisor firm
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# **Empirical design**

## **□ Empirical setting**

### **▪ Identifying cohorts**

- ✓ We focus on the sample of firms in industries (three digit-SIC) that are at high risk of EPA enforcement actions (5 years lookback window)
  - ✓ We pick the controls
    - That are in the same industry (three-digit SIC) as the treated firms
    - That are relying on external legal advisors in business activities (5 years lookback window)
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## **Data**

- ❑ EPA enforcement actions from EPA's Integrated Compliance Information System (ICIS) data
  - ❑ Toxic releases under the Toxics Release Inventory (TRI) program provided by EPA
  - ❑ M&A, new issuances, IPO information from SDC platinum
  - ❑ Loan information from Thomson Reuters Loan Pricing Corporation Dealscan database (DealScan)
  - ❑ Lobbying information from Opensecret data
  - ❑ Insider trading information from Thomson Reuters Insider Filings (Form 4) database
  - ❑ Accounting information from COMPUSTAT
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# Result 1

## □ 1. Do firms gain advantages from affiliating with law firms that employ former government officials?

	<i>Number of enforcements (Log)</i>	<i>Number of enforcements (Log)</i>	<i>Number of enforcements (Log)</i>	<i>Number of enforcements (Log)</i>
<i>Number of connections with the revolving door legal advisors (Log) × Post</i>	-0.03*** (2.85)	-0.02*** (2.71)		
<i>Revolving door legal advisor (Y/N) × Post</i>			-0.02*** (3.03)	-0.02*** (2.89)
Control variables	No	Yes	No	Yes
Event × Firm FE	Yes	Yes	Yes	Yes
Event × Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	211,914	211,914	211,914	211,914
Adjusted R <sup>2</sup>	0.6358	0.6360	0.6359	0.6360

# Result 2

## □ Dynamic difference-in-differences regression framework

	<i>Number of enforcements (Log)</i>	<i>Number of enforcements (Log)</i>	<i>Number of enforcements (Log)</i>	<i>Number of enforcements (Log)</i>
	<i>(i) = Number of connections with the revolving door legal advisors (Log)</i>		<i>(i) = Revolving door legal advisor (Y/N)</i>	
(i) × T-3	0.002 (0.19)	0.002 (0.21)	0.001 (0.17)	0.001 (0.19)
(i) × T-2	-0.01 (0.73)	-0.01 (0.71)	-0.01 (0.88)	-0.01 (0.85)
(i) × T-1	-0.01 (0.78)	-0.01 (0.74)	-0.01 (1.01)	-0.01 (0.96)
(i) × T+0	-0.01 (1.36)	-0.01 (1.28)	-0.01* (1.66)	-0.01 (1.56)
(i) × T+1	-0.02 (1.41)	-0.02 (1.32)	-0.02* (1.67)	-0.02 (1.58)
(i) × T+2	-0.03** (2.47)	-0.03** (2.34)	-0.02*** (2.70)	-0.02** (2.56)
(i) × T+3	-0.03** (2.19)	-0.03** (2.07)	-0.03** (2.34)	-0.03** (2.22)
(i) × T+4	-0.04*** (2.68)	-0.04** (2.55)	-0.04*** (2.90)	-0.03*** (2.78)
Control variables	No	Yes	No	Yes
Event × Firm FE	Yes	Yes	Yes	Yes
Event × Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	241,818	241,818	241,818	241,818
Adjusted R <sup>2</sup>	0.6350	0.6351	0.6351	0.6352

# Result 3

## □ 1. Do firms gain advantages from affiliating with law firms that employ former government officials?

	<i>Penalty amount (Log)</i>	<i>Penalty amount (Log)</i>	<i>Penalty amount (Log)</i>	<i>Penalty amount (Log)</i>
<i>Number of connections with the revolving door legal advisors (Log) × Post</i>	-0.19** (1.98)	-0.18* (1.91)		
<i>Revolving door legal advisor (Y/N) × Post</i>			-0.15** (1.99)	-0.14* (1.91)
Control variables	No	Yes	No	Yes
Event × Firm FE	Yes	Yes	Yes	Yes
Event × Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	211,914	211,914	211,914	211,914
Adjusted R <sup>2</sup>	0.5282	0.5284	0.5282	0.5284

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## **Result 4**

### **□ 2. Is the influence derived from expertise or potential information leakage?**

- Analyze toxic releases from the plants in proximate regions (based on zip code, within 100 miles) that have been subject to EPA enforcements 4 years around the beginning year of the enforcement actions
  - We include only those firms in the same industry (three-digit SIC) as the enforced firms
  - Exclude facilities that are subject to the EPA enforcement
  - Exclude facilities of the firms that are subject to other enforcement cases during the sample period
-

# Result 4

## □ Dynamic difference-

### in-differences

### regression framework

	<i>Toxic releases</i> (Log)	<i>Toxic releases</i> (Log)	<i>Toxic releases</i> (Log)	<i>Toxic releases</i> (Log)
	(i) = <i>Number of revolving door legal advisors</i> (Log)		(i) = <i>Revolving door legal advisor</i> (Y/N)	
(i)× T-3	-0.06 (0.27)	-0.12 (0.61)	0.04 (0.18)	-0.03 (0.13)
(i)× T-2	-0.33 (1.29)	-0.35 (1.33)	-0.18 (0.57)	-0.14 (0.44)
(i)× T-1	-0.13 (0.67)	-0.15 (0.77)	-0.18 (0.77)	-0.14 (0.59)
(i)× T+0	-0.69** (2.08)	-0.72* (1.90)	-0.72** (2.21)	-0.69* (1.93)
(i)× T+1	-0.43 (1.63)	-0.45 (1.36)	-0.37 (1.32)	-0.34 (1.03)
(i)× T+2	-0.56* (1.87)	-0.56 (1.64)	-0.42 (1.29)	-0.38 (1.05)
(i)× T+3	-0.34 (0.87)	-0.41 (0.91)	-0.16 (0.37)	-0.19 (0.38)
(i)× T+4	-0.21 (0.47)	-0.28 (0.54)	0.02 (0.04)	-0.02 (0.04)
Control variables	No	Yes	No	Yes
Event × Facility FE	Yes	Yes	Yes	Yes
Event × Year FE	Yes	Yes	Yes	Yes
Observations	4,604	4,604	4,604	4,604
Adjusted R <sup>2</sup>	0.8593	0.8611	0.8593	0.8609

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## ❑ 3. Evidence on potential information leakage

The New York Times

### *When 'Political Intelligence' Meets Insider Trading*

By Peter J. Henning

May 29, 2017

THE WALL STREET JOURNAL.

### **U.K. Investigates Leaks in Insider Trading Probe**

Britain's top law-enforcement body examining allegations that translator was paid to tip off target of investigation

By [Bradley Hope](#) [Follow](#)

Dec. 27, 2018 1:03 pm ET



### **End in sight for U.S. insider trading case over healthcare leaks**

By Jonathan Stempel

August 2, 2023 3:52 AM GMT+10 · Updated 9 months ago

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### ❑ 3. Evidence on potential information leakage

- According to Jerke (2010)
    - ✓ “The practice of gathering and selling political information prior to its public release is nothing new... One Washington insider predicts that **lobbying shops collectively generate \$30 to \$40 million in fees from their political-intelligence practices annually**”
    - ✓ “A number of Washington firms have advertised their political intelligence practices directly or have spoken with the media... including Patton Boggs LLP, Sonnenschein Nath & Rosenthal LLP, Washington Analysis, PodestaMattoon, Cormac Group, Mehlman Vogel Castagnetti Inc., Bryan Cave Strategies LLC, DLA Piper, Williams & Jensen, and Akin Gump Strauss Hauer & Feld LLP”
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## **Results 5-6**

### **□ 3.1 Evidence on potential information leakage (EPA court decisions)**

- Analyzing insider trading around (-90, +90 trading days) final court decision for EPA enforcement actions
  - ✓ Trading profit for insider trades
    - Average risk-adjusted return for each transaction made by the insiders calculated over 180 trading days following the transaction (related to FF and Carhart four factor models)
      - \*Mirroring Jagolinzer et al (2011), Kim and Oh (2023)
  - ✓ Net selling [(net sales – net purchases)/shares outstanding]
    - \*Mirroring Blackburne et al (2021), Arif et al (2022)

# Result 5

## □ 3. Evidence on potential information leakage (EPA court decision dates)

	<i>Trading profit</i>	<i>Trading profit</i>	<i>Trading profit</i>	<i>Trading profit</i>
<i>Number of revolving door legal advisors (Log) × Day [-30, 0]</i>	0.01** (2.54)	0.01** (2.47)		
<i>Revolving door legal advisor (Y/N) × Day [-30, 0]</i>			0.02** (2.51)	0.02** (2.43)
<i>Day [-30, 0]</i>	-0.02*** (2.86)	-0.02*** (2.78)	-0.02*** (2.96)	-0.02** (2.89)
Control variables	No	Yes	No	Yes
Event × Firm FE	Yes	Yes	Yes	Yes
Transaction date FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	102,580	102,580	102,580	102,580
Adjusted R <sup>2</sup>	0.8935	0.8955	0.8935	0.8955

# Result 6

## □ 3. Evidence on potential information leakage (EPA court decision dates)

	<i>Net sell</i>	<i>Net sell</i>	<i>Net sell</i>	<i>Net sell</i>
<i>Number of revolving door legal advisors (Log) × Day [-30, 0]</i>	0.001* (1.73)	0.001* (1.81)		
<i>Revolving door legal advisor (Y/N) × Day [-30, 0]</i>			0.007** (2.37)	0.007** (2.32)
<i>Day [-30, 0]</i>	-0.001 (0.62)	-0.001 (0.69)	-0.005 (1.65)	-0.005 (1.63)
Control variables	No	Yes	No	Yes
Event × Firm FE	Yes	Yes	Yes	Yes
Transaction date FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	20,269	20,269	20,269	20,269
Adjusted R <sup>2</sup>	0.5159	0.5175	0.5161	0.5177

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## **Results 7-8**

- ❑ **3.2 Evidence on potential information leakage (announcement regarding the addition of TRI chemicals)**
    - Analyzing insider trading around (-90, +90 trading days) the announcement regarding the addition of Toxic Release Inventory (TRI) chemicals
    - TRI is a tracking program for certain toxic chemicals released by facilities operating in United States
    - There were new substances added to the required chemical list in 2007, 2010, 2011, 2013, 2014, 2015, 2016, 2018, 2020, 2021, and 2022
-

# Result 7

## □ 3.2 Evidence on potential information leakage (announcement regarding the addition of TRI chemicals)

	<i>Trading profit</i>	<i>Trading profit</i>	<i>Trading profit</i>	<i>Trading profit</i>
<i>Number of revolving door legal advisors (Log) × Day [-30, 0]</i>	0.04*** (3.00)	0.04*** (2.87)		
<i>Revolving door legal advisor (Y/N) × Day [-30, 0]</i>			0.03 (1.54)	0.02 (0.98)
Control variables	No	Yes	No	Yes
Event × Firm FE	Yes	Yes	Yes	Yes
Transaction date FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	9,001	9,001	9,001	9,001
Adjusted R <sup>2</sup>	0.8370	0.8458	0.8363	0.8451

# Result 8

## □ 3.2 Evidence on potential information leakage (announcement regarding the addition of TRI chemicals)

	<i>Net sell</i>	<i>Net sell</i>	<i>Net sell</i>	<i>Net sell</i>
<i>Number of revolving door legal advisors (Log) × Day [-30, 0]</i>	0.01* (1.86)	0.01 (1.35)		
<i>Revolving door legal advisor (Y/N) × Day [-30, 0]</i>			0.02* (1.71)	0.02 (1.45)
Control variables	No	Yes	No	Yes
Event × Firm FE	Yes	Yes	Yes	Yes
Transaction date FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	2,578	2,578	2,578	2,578
Adjusted R <sup>2</sup>	0.3511	0.3692	0.3519	0.3700

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## **Conclusion**

- ❑ **We are the first to provide evidence that revolving door officials' post public employment at legal advising firms can influence the enforcement actions against client corporations**
  - Evidence from EPA enforcement actions
  
- ❑ **We provide evidence that the impact can potentially be from political intelligence**
  - Investigations
  - Court decisions
  - Regulation changes

- End