The general counsel’s relationship with an institution’s governing board(s) is one of the most important and complex parts of the job. University attorneys are usually hired by the administration and typically report on a day-to-day basis to the President, Chancellor, or some other senior executive officer of an institution (or as part of a system office if that is the applicable structure). Board members are sometimes (but not always) involved in the process of selecting a general counsel, and are sometimes (but not always) also involved in performance and compensation reviews for the general counsel. Given that the actual client is the institution (and not any particular individual or officer within the institution), the general counsel must balance internal administrative relationships with the need to be responsive to a governing board and its fiduciary duties for overall governance. The general counsel’s ability to accomplish this task can be helped or hindered by the culture of the institution, the relationship of the board to the President or Chancellor, and the relationship of the board to other members of the administration.

We will share some general thoughts below from our perspectives as the general counsel of a large public research university with two governing boards, and as the general counsel of a private research university with a single governing board.

The public board experience. Reflecting its unusual history as a private colonial college that eventually became the state’s comprehensive public research university, Rutgers, The State University of New Jersey has both a Board of Governors and a Board of Trustees (the historic board that oversaw the institution when it was private). The Board of Governors has overall authority to determine policies for the organization, administration and development of the University, whereas the Board of Trustees acts in an overall advisory capacity and has specific authority over properties, funds and trusts that were held by the University as of August 31, 1956 (the date of the legislation by which Rutgers became the State University of New Jersey). See N.J.S.A. 18A:65 (the “Rutgers Law” of 1956). The general counsel works with both of these governing boards. They hold separate meetings and have a variety of joint committees.

Public institution governing boards vary widely in terms of their size, composition, scope of authority, and selection processes. As state actors, public institutions must be cognizant of their particular responsibilities under constitutional and state law. Board members who are accustomed to working with private sector corporations or other non-public governing boards
need to be apprised of the special legal responsibilities associated with a public college or university. The Association of Governing Boards of Colleges and Universities (“AGB,” www.agb.org) is a wonderful resource on higher education governance and leadership issues for academic governing boards.

The private board experience. Though its origins date back to 1838, Duke University as it is now known was founded in 1924 after the James B. Duke family created an endowment for its operation. It since has grown to be a national and international university, governed by a 37-member board of trustees. Duke University also oversees the Duke University Health System, Inc. which has its own board of directors, as well as numerous separately-incorporated support corporations which conduct certain activities in support of Duke and its health system. The general counsel’s office oversees legal services to these entities.

Private educational governing boards, like public boards, vary among institutions and states. Most are subject to many federal laws attendant to receiving federal funds, and some state laws, but the exercise of their responsibilities generally is not subject to constitutional law, and they do not have the constraints of state open meeting and records laws. Private universities do not have sovereign immunity which results in a steady diet of litigation for legal counsel. Private universities must pay close attention to taxation issues, including filing tax information returns on an annual basis. These activities can engage the trustees’ interest and thus the general counsel’s attention.

**Board Orientation and Education**

Many institutions have some sort of orientation for new governing board members. The general counsel may or may not have a role at orientation. If not, the general counsel should seek the opportunity to be included in the orientation. One way to do so is through a written memorandum like the attached appendix, but ideally “face time” is preferable. As important as imparting information to board members is the general counsel’s goal of establishing credibility with the board.

In conjunction with the office that functions as the secretary to the governing board(s), possible topics to include in legal counsel’s orientation might be the following:

- The institution’s legal/statutory structure and foundation and relationship to the state (for public institutions)
- The institution’s status under federal tax law (e.g., is it a 501(c)(3) tax-exempt organization)
- The relationship with the institution’s foundation/development function (e.g., whether the foundation is separately incorporated and subject to separate governance), and with any other held corporations that support the institution.
- Open public meetings act requirements (for public institutions), such as
  - What constitutes a quorum?
  - How and when can board meetings be called?
  - What can be discussed in “closed” sessions?
  - What is the role of committees and committee meetings?
  - How and when must the board allow for public comments?
• Board bylaws and other governance documents
• The fiduciary responsibilities of board members (as set forth in statutes and more generally)
• Conflict of interest rules that apply to board members; financial disclosures; recusal policies and processes; etc. (e.g., the Rutgers statute includes a rule that prohibits board members from being compensated by the institution for other forms of service such as teaching)
• Personal liability of board members; indemnification policies; applicable insurance
• How the institution issues bonds/debt
• The sources of institutional policy (e.g., Rutgers has an online and searchable “University Policy Library” that compiles policies on a wide range of academic and administrative issues; Duke’s policies are not so centrally kept)
• How to treat confidential information (note any applicable statutory obligations)
• Whether the institution’s documents in the hands of trustees should be saved for document retention purposes
• What types of decisions must be reviewed and/or approved at the board level (e.g., certain contracts, employment arrangements, etc.)
• Open meetings and public records acts (for public institutions) and their impact on the communications of board members (e.g., will their e-mails be considered “public records” subject to possible disclosure)
• Communications/attorney-client privilege (when it does and does not apply)
• How and when outside counsel are hired

Communications with Board Members

The general counsel may need to communicate with board members frequently between meetings to provide updates on legal matters and cases. At some institutions, the president or chancellor lays down rules about communications with board members—thus it is important for the general counsel to know the rules and expectations before contacting a board member. The board secretary should also be kept apprised of contacts with board members (see below). Given their fiduciary responsibilities, board members should be apprised of important legal matters and aware of what they should or should not say publicly about such matters. At Rutgers, for instance, our general practice is not to comment publicly on pending litigation. Board members are aware that requests for comments on legal matters should be referred to the General Counsel’s office.

Given all the demands on the time of board members and their meeting agendas, it may be challenging to provide board members with updates on all the legal matters of which you would like them to be aware. Some legal offices prepare confidential written reports for the governing board (which may not be confidential under certain state public records laws). Others have special committees that discuss legal issues so that a subset of board members (often but not always
consisting of lawyers themselves) can help to oversee and comment on legal matters. The committee may then identify particular matters that need to be brought to the attention of the full board. At Rutgers, we have a Legal Affairs Subcommittee that receives bi-annual written reports covering the full range of legal issues affecting the University (highlighting high-profile cases and issues, trends in outside counsel use and spending, etc.). This group is also convened by conference call, and receives separate notifications on time-sensitive matters on an as-needed basis.

Board members who are lawyers must understand the difference between their role as a board member and the role of an attorney for the institution. Lawyer-trustees also can become an ally to the general counsel, however, so these relationships are important. Legal advice and services should be coordinated centrally through the general counsel’s office to avoid confusion.

Board members should also be apprised of how and when their own communications related to the institution will be treated legally. Given their fiduciary responsibilities, board members have special obligations when speaking in their capacity as board members. The rules should be clear about who speaks on behalf of the institution for various topics and matters. In general, individual board members should not speak on behalf of the institution without explicit authorization. Given their visibility, board members may sometimes be approached by government agencies, the press, or other outside entities that are aware of the board member’s role at an institution. In such instances, board members should report the outside contact and seek guidance before responding (often such contacts should be referred to the board chair or administration for response). In conjunction with the secretary’s office, the counsel’s office can serve as a resource for board members who receive such contacts to ensure that such communications are handled appropriately (especially when the contact relates to legal issues).

New forms of technology may be helpful in managing confidential communications. For example, Rutgers and Duke both have secure portals that are password-protected on which board members and administrators can review documents, share comments, etc.

Whether the general counsel is or must be the exclusive “lawyer” to the governing board may depend on your laws and governing documents (for example, some systems have separate legal counsel for the system governing board), and on the particular matter. There may be times when the general counsel is better served by the governing board having its own lawyer, such as when negotiating the president’s employment agreement or termination.

**Relationship with the Board Secretary**

The general counsel should have a close, collaborative relationship with the board secretary (indeed, at some institutions the general counsel or a designee in that office serves in this role). As noted above, the general counsel will want to keep the board secretary in the loop with regard to any communications with board members (the same may be true for the president or chancellor, depending on that individual’s preferences and ground rules). The board secretary can be an important ally in ensuring that appropriate policies and procedures are followed in board decision-making, and can also provide an early warning system to counsel about upcoming board issues or matters that raise possible legal concerns. The board secretary can also be a valuable resource in understanding board politics and personalities. Calls or questions from the
secretary’s office need to be given high priority, as they are often trying to respond to board members and to ensure that board members have confidence in the institution’s administration.

**Conflicts of Interest/Recusals**

The general counsel may be called upon (working with the secretary’s office and possibly others such as the internal auditor) to monitor possible conflicts of interest of board members. This work requires familiarity with the agendas of board and committee meetings as well as with the employment and other relationships of board members. Institutions may have formal recusal policies and procedures, and it is helpful if any possible conflicts can be identified well in advance of meetings so that board members know that they should not participate in certain discussions or matters. Board leadership should also be apprised of such conflicts if and when they are identified.

**Board Decision-Making Processes**

As a general rule, the general counsel should be aware of the agendas for all board and committee meetings and of any action items/resolutions coming before the governing board. When possible, resolutions may need to be drafted in ways that provide some flexibility for the administration to carry out its responsibilities between meetings without going back to the full board (e.g., in negotiating details of a particular contract or transaction).

General counsels should also be involved in reviewing the minutes of board and committee meetings. This is especially important at public institutions, where such records may be official public records and subject to possible public disclosure.

**Compliance**

Governing boards are increasingly interested in compliance issues in higher education. At Rutgers University, the General Counsel is also currently designated as the Chief Compliance Officer for the University. In that capacity, the General Counsel reports annually to the Audit Committee on compliance initiatives and issues. This role requires coordination with all of the academic and administrative units with compliance responsibilities (e.g., athletics, health and safety, environmental, research, privacy, etc.). Some institutions have separate compliance offices that play this role. As compliance concerns become increasingly prominent, there is an opportunity for the general counsel to demonstrate proactive leadership by discussing (in conjunction with other university leaders) areas of evolving risk where policies and procedures may need to be developed to respond to new legal and regulatory requirements. These conversations can also shed light on where resources may be needed for the future to ensure that compliance responsibilities can be met.

Like compliance, institutional-wide risk management is now becoming more important to many boards of trustees. At Duke, the chief audit executive takes the lead role in enterprise risk management and compliance, but other offices share in the compliance responsibilities such as the health system’s chief compliance officer. The general counsel is closely involved in both tasks, particularly in helping to identify institutional risks, staying abreast of new laws and regulations,
and when possible ensuring written audit and risk assessment reports are appropriately worded. The general counsel at Duke also reviews all draft internal audit reports before they are issued.

**Issues Involving the President/Chancellor**

The general counsel’s role with the governing board(s) is particularly sensitive when dealing with issues involving the institution’s chief executive officer (to whom the general counsel often reports). The general counsel may be called upon by the board(s) to assist with employment contracts, discussions regarding benefits, and development and assessment of accountability goals and metrics. The general counsel may also be involved if the board has performance concerns. These situations are among the hardest to navigate. As a general rule, however, the general counsel can encourage clear communication between a governing board and chief executive officer to ensure that expectations are set and expressed clearly. Regular performance evaluations based on clearly articulated sets of goals and expectations can go a long way in alleviating potential misunderstandings and surprises.

**The Higher Education Legal Context and Academic Values**

Board members with backgrounds outside of higher education may have different governance models in mind (e.g., Sarbanes-Oxley Act requirements that apply to corporations) with regard to how institutional decisions are made, how compliance is handled, etc. The general counsel can be helpful in pointing out the differences in how institutions of higher education are governed and in the law that applies to them.

Academic values and norms can also be confusing to individuals whose primary areas of expertise are outside higher education. Thus, it may be helpful to provide board members with an overview on issues such as academic freedom, shared governance, tenure, and due process. It can also be helpful to provide board members with presentations about evolving trends and best practices on other legal and policy issues in higher education so that they have a sense of context when making decisions.
To: Members, University Board of Trustees of XXX Private University
From: University Counsel
Subject: The Legal Duties and Obligations of University Trustees
Date: XXX

This memorandum is designed to acquaint you with your formal duties and obligations as members of the Board of Trustees and to describe some of the legal protections that safeguard trustees against personal financial exposure arising from your service on the board. A concluding section briefly describes good governance practices of nonprofit corporation boards.

I. SOURCES OF LAW DEFINING THE DUTIES AND OBLIGATIONS OF TRUSTEES

The legal obligations of X trustees are described in several places: (1) the Nonprofit Corporation Act, which generally governs the activities of nonprofit corporations in the state of X; (2) the Articles of Incorporation of X University; and (3) the Bylaws of X.

The X Nonprofit Corporation Act. The X contains rules relating to the structure and governance of all nonprofit corporations that operate in X. For example, the general powers the board may exercise, procedures for the appointment of trustees and the election of board officers, quorum rules, and a requirement for the preparation of annual reports. All the requirements of the law apply to X University and its Board of

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1 The full text is available online at www.xxxxx.
Trustees—both of which, to the best of my knowledge, are in compliance with them all.

*The Articles of Incorporation.* X University’s articles of incorporation is the organizational document which formed X University as a corporation. The articles describe among other things the powers and duties of the Board. The articles can be amended by the Board, upon filing any amendments with the State Secretary of State.

*The Bylaws.* Bylaws are defined in the Nonprofit Corporation Act as the rules for the oversight, regulation or management of the affairs of the corporation. They will provide more a detailed description of the Board’s structure and managerial responsibilities, and they can be amended, revised, or repealed by the Board at any time in accordance with the procedures specified in the Bylaws. *All trustees should read the Bylaws and understand what they mean.* An up-to-date copy of the Bylaws is attached to this memorandum as Appendix A. The University Secretary will have a copy of the Bylaws for any trustee who wishes to review them during the course of a meeting.

**II. THE POWERS OF THE BOARD**

The powers of the Board of Trustees are spelled out in a single broadly worded paragraph in the Articles of Incorporation:

[The Board] shall have power to make such rules, regulations and bylaws and to take such other action … as may be necessary or appropriate for the governance of the corporation and its operations and management of its property and funds, and to exercise all powers granted to non-profit corporations under the laws of the State of X.

The Bylaws vests “[a]ll powers of the University” in the Board of Trustees, a grant of authority broad enough to encompass all powers traditionally exercised by the governing boards of America’s private colleges and universities. These powers include:

- Appointing the President and the fixing of the President’s compensation.
- Approving degrees and honorary degrees.
- Authorizing changes in tuition and fees.
- Acting on the University’s operating and capital budgets.
- Approving the sale, purchase, construction or renovation of land and buildings.
- Promoting major fund-raising efforts.

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2 The full is available online at www.xxxxx.
3 The full text is available online at www.xxxx.
• Incurring and securing debts.

• Approving institutional policies on faculty appointment, promotion, tenure, sabbaticals and leaves.

• Periodically reviewing the University’s mission and the Board’s performance.

In keeping with the practice at most institutions of higher education in the Bylaws allow certain Board committees—in particular the Executive Committee—to act for the Board in prescribed areas of institutional governance. For example, the X Committee—rather than the Board as a whole—exercises certain powers over XXXXX.

III. YOUR LEGAL DUTIES AS A TRUSTEE

A trustee is required to discharge his or her duties in good faith, with due care and in the best interests of the nonprofit corporation. The duty to act in good faith and in the best interests of the corporation also is known as “fiduciary duty.”

The duty to act with due care means in practical terms that you should be generally familiar with the Bylaws (an obligation satisfied by reading and understanding the Bylaws); and be prepared for, attend, and participate in scheduled meetings of the Board and the committees to which you are assigned.

The most important duty you have as a member of the Board of Trustees is your duty as a corporate fiduciary. Under the law of X, a member of a corporate board owes an enforceable legal duty to the corporation to manage its fiscal affairs prudently. A board member who breaches that duty can be held personally liable for any consequent damages the corporation suffers. The following are some examples of breach of fiduciary duty:

• **Conflicts of interest or self-dealing:** A trustee violates his or her fiduciary duty by knowingly allowing the corporation to enter into a business transaction with an entity (corporation, partnership, etc.) in which he or she has a substantial interest without disclosing that fact to other board members.

• **Failure to exercise independence of judgment:** Establishing an executive committee that routinely accepts the recommendations of the president without discussion or debate, establishing a finance committee that does not meet regularly, and generally ceding to the president important financial decision-making authority vested under the bylaws in the board all constitute breaches of a trustee’s fiduciary duties.

The University’s conflict-of-interest policy for trustees is designed to ensure that

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4 [cite statute here]
trustees recognize potential conflicts of interest, disclose them as appropriate, and protect themselves and the institution against the potential adverse consequences of conflicts.

IV. PROTECTION AGAINST LIABILITY

You are protected in three different ways against personal liability for actions you undertake in your capacity as a member of the Board of Trustees. First, you enjoy the standard protection afforded to all corporate trustees under the “business judgment rule.” Second, under the Bylaws, you enjoy indemnification against claims and law suits that may be filed against you. And third, the University has purchased comprehensive Directors and Officers (“D & O”) liability insurance and you are an insured under X D & O policy.

The Business Judgment Rule. The business judgment rule limits court review of Trustees’ actions. In making a business decision, you are presumed to act on an informed basis, in good faith, and in the honest belief that the actions you take are in the best interest of the University. The business judgment rule protects trustees against liability for honest mistakes in judgment, but not for breaches of fiduciary duty occasioned by fraud, gross negligence, or illegal conduct.

Indemnification. Indemnification means a legally enforceable assurance under which one person (in this instance, the University) promises to protect another (a member of the Board of Trustees) against liability arising out of the legal consequences of the trustee’s failure to act. The Bylaws provide substantial protection against lawsuits and other claims filed against trustees. Under the Bylaws, trustees are indemnified against claims to the maximum extent permitted by law. This would include claims asserted in any kind of action (civil, criminal, administrative, actual, threatened, pending, or completed) and for money payments in virtually any form (judgments, fines, settlement awards, and attorneys’ fees).

There are preconditions, however. You are indemnified only if:

1. The action is brought against you by reason of the fact that you are a trustee. In other words, the University will indemnify you only with respect to actions you take in your capacity as a trustee, not for actions relating to your business or your personal life.

2. You acted in good faith and in a manner you reasonably believed was consistent with the University’s best interests.

3. In a criminal proceeding, you had no reason to believe your conduct was unlawful.

4. You did not receive an improper personal benefit from your actions.
Insurance. The University has purchased commercial insurance policies that provide insulation from potential liability for board members. The policies are “Directors and Officers” (“D & O”) liability policies. The policies cover the University as an entity, the President and trustees, and all salaried employees (including faculty members) for their wrongful acts, including errors and omissions. Coverage, therefore, is provided for all individual trustees.

The policies provide X million of liability coverage, subject to a per-claim deductible of X. They provide comprehensive protection against judgments, settlements, and defense costs, including attorneys’ fees. Like most policies, the policies contain standard exclusions. It affords no protection against punitive damage awards; liability assumed under contract; liability for tortuous bodily injury; liability for willful or intentional torts; or liability for violations of federal securities or pension laws, among others.

All institutional insurance policies are reviewed regularly by the Director of the Office of XXXX to determine whether the current level of insurance protection for the Board and its members is sufficient.

V. CORPORATE GOVERNANCE

The Sarbanes-Oxley Act of 2002 was one of the governmental reforms enacted to address perceived weaknesses in financial reporting and corporate accountability practices among the nation’s publicly-traded, stock-issuing, for-profit corporations. Most colleges and universities in this country are not directly affected by Sarbanes-Oxley or other reforms. Universities so far have successfully avoided Congressional application to their activities by voluntarily adopting many of Sarbanes-Oxley’s requirements as “best practices.”

Audit committee requirements. Sarbanes-Oxley requires public corporations to create audit committees “directly responsible” for retaining and supervising outside auditors. Audit committee members must be independent, meaning that senior management personnel cannot be members. As part of this “independence” standard, audit committee members cannot be paid for consulting or other services provided to the corporation outside of their service as trustees. The Audit Committee of University X and its composition comport with these requirements.

Financial certification requirements. Sarbanes-Oxley requires “that the principal executive officer ... and the principal financial officer ... certify in each annual ... report” as to the following: that they have reviewed the report; that the report “does not contain any untrue statement of a material fact” or a material omission; that the financials fairly present the financial condition of the corporation; that the certifying individuals have designed and evaluated systems of internal controls to make sure that they are aware of material information concerning the corporation’s operations; and that the signers have disclosed to the company’s auditors and audit committee deficiencies in controls as well as any fraud involving management or other key employees. This is done at X. There
also are Internal Revenue Service requirements for trustees regarding the review of a university’s information return (Form 990), with which this institution complies.

*Restrictions on senior executive compensation.* Internal Revenue Service regulations prohibit unreasonable excessive compensation to employees of nonprofit institutions. The University must comply with the requirements of the Internal Revenue Code regarding executive compensation for officers, key management, as well as others whose position or salary level requires review by the Board for reasonableness. A brief summary of the process for reviewing executive compensation is attached as Appendix B.

*Required code of financial ethics.* Sarbanes-Oxley directs the Securities and Exchange Commission to promulgate rules effectively requiring corporations to adopt “a code of ethics for senior financial officers”. Other laws applicable to the university also require conflict of interest policies for certain officers, trustees and employees. University X has already adopted conflict-of-interest policies and those covering trustees are attached as Appendix C.

VI. CONCLUSION

By accepting service as a member of the Board of Trustees, you assume the responsibility to be diligent in that service. If you have any questions about these issues, please let me know.
THE GENERAL COUNSEL AND THE GOVERNING BOARD:
MANAGING AN IMPORTANT RELATIONSHIP AT THE INSTITUTION’S PINNACLE

THE BOARD AND ITS COUNSEL—BASIC ETHICAL PRECEPTS

January 28–29, 2011

Lawrence White
University of Delaware
Newark, Delaware

“Well, so far I’m managing to stay above the fray.”

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[This is an updated and revised version of a paper originally delivered at NACUA’s 2001 Annual Conference by former University of California System General Counsel James E. Holst and Lawrence White.]
I. SOME ETHICS BASICS

A. The ethical duality of serving as counsel to the board. Governing boards (indeed, whole institutions of higher education) are populated by individual human beings, including one to whom the board’s attorney may report directly; yet that attorney’s client is not an individual – the chair of the board, the president, or anybody else – but the organization as a disembodied whole. Discerning the identity of a lawyer’s client when the lawyer represents an institution is the subject of Rule 1.13 (“Organization as Client”) of the American Bar Association’s Model Rules of Professional Conduct, which establish ethical standards for lawyers in most jurisdictions. Rule 1.13(a) declares the general rule that “[a] lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.” (www.abanet.org/cpr/mrpc/rule_1_13.html.) The ironic and somewhat counterintuitive implication, as one commentator observed, is that “all of corporate counsel’s communications are necessarily with individuals whom the attorney does not directly represent” – an odd state of affairs, when one thinks about it. Alan L. Silverstein, Ethical Issues Facing Corporate Counsel, 13 ANTITRUST (ABA) 18, 19 (1998).

The duality of the role – representing an inchoate entity known as the organization that manifests its will only through the collective decisions of flesh-and-blood board members, not all of whom are necessarily in sync with what the board decides – can put counsel in an uncomfortable position. Consider these recurring problems.

(1) What happens if counsel gets conflicting instructions from different board members, or from a board member and the president? What if, heaven forbid, the chair of the board confides that the board wants to remove the president and asks counsel for information on the president’s rights under his or her employment agreement, and simultaneously the president (who is also a board member), fearing removal, asks counsel for advice on his or her rights if the board moves to terminate the appointment?

Rule 1.13(f) of the Model Rules of Professional Responsibility provides a partial and not entirely helpful answer: “In dealing with an organization’s directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer knows or reasonably should know that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing.” If one constituent ranks higher in the institutional hierarchy than another – as, arguably, the chair of the board does in this example – then counsel probably should explain to the president that, under the circumstances, the interests of the client represented by counsel are adverse to those of the president, meaning that counsel cannot advise the president.

(And if the president then retaliates against counsel or fires counsel? Then you have the ultimate ethical and practical morass. See Lawrence White, Clients Behaving Badly: Ethical Considerations, a paper prepared for the 2008 NACUA Annual Conference.)
What happens if counsel knows or suspects that a board member is doing something illegal, something improper, or something that jeopardizes the institution’s legal well-being? What if the president seeks to limit counsel’s communication with the board on issues that are coming, or could come, to the board for consideration? The ethical rules in such situations are complicated. First, the comment to ABA Model Rule 1.13 draws a distinction between “policy and operations” matters on the one hand, and matters involving legal judgment on the other – although the comment stops considerably short of offering useful guidance:

Decisions concerning policy and operations, including ones entailing serious risk, are not as such in the lawyer's province. … [But] when the lawyer knows that the organization is likely to be substantially injured by action of an officer or other constituent that violates a legal obligation to the organization or is in violation of law that might be imputed to the organization, the lawyer must proceed as is reasonably necessary in the best interest of the organization.

This suggests that, under appropriate circumstances, the lawyer would be warranted in presenting the matter to the full board – a step, obviously, that no lawyer would take casually or without being absolutely sure of the facts and circumstances.

B. Changes to Model Rule 1.13. In 2002, prompted in part by the highly publicized role of lawyers in the Tyco and Rite-Aid scandals and in part by the SEC’s consideration of rules governing the ethical obligations of attorneys practicing before that agency, the American Bar Association established a Task Force on Corporate Responsibility to examine “the mechanisms of public corporation governance in the United States, with particular emphasis on the role of lawyers,” and to consider changes in the Model Rules of Professional Conduct designed to enhance the lawyer’s freedom “to disclose to third parties information concerning criminal or fraudulent conduct by the client.” ABA Task Force Report 3, 34. The result in 2003 was the adoption of revised versions of Rule 1.13 with significant changes to the accompanying Commentary for the Model Rule.

It behooves all of us who represent institutional clients for a living to understand Rule 1.13 – the most important ethical precept shaping our practice.

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| (b) If a lawyer for an organization knows that an officer, employee or other person associated with the organization is engaged in action, intends to act or refuses to act in a matter related to the representation that is a violation of a legal obligation to the organization, or a violation of law which reasonably might be imputed to the organization, and is likely to result in substantial injury to the organization, the lawyer shall proceed as is reasonably necessary in the best interest of the organization. **In determining how to proceed, the lawyer shall give due consideration to the seriousness of the violation and its consequences, the scope and nature of the lawyer’s representation, the responsibility in the organization and the apparent motivation of the person involved, the policies of the organization concerning such matters and any other relevant considerations. Any measures taken shall be designed to minimize disruption of the organization and the risk of revealing information relating to the representation to persons outside the organization. Such measures may include among others:**

1. **(1) asking for reconsideration of the matter;**

2. **(2) advising that a separate legal opinion on the matter be sought for presentation to appropriate authority in the organization; and**

3. **(3) referring** the matter to higher authority in the organization, including, if warranted by the **circumstances** to the highest authority that can act on behalf of the organization as determined by applicable law. |

| (c) **Except as provided in paragraph (d), if**

1. **(1) despite the lawyer’s efforts in accordance with paragraph (b), the highest authority that can act on behalf of the organization insists upon action, or a refusal to act, that is clearly a violation of law [and is likely to result in substantial injury to the organization], the lawyer may [resign in accordance with Rule 1.16].** |

| **(d) If, despite the lawyer’s efforts in accordance with paragraph (b), the highest authority that can act on behalf of the organization insists upon action, or a refusal to act, that is clearly a violation of law [and is likely to result in substantial injury to the organization], the lawyer may [resign in accordance with Rule 1.16].** |

| **(e) The lawyer reasonably believes that the violation is reasonably certain to result in substantial injury to the organization, then** the lawyer may **reveal information relating to the representation whether or not Rule 1.6 permits such disclosure, but only if and to the extent the lawyer reasonably believes necessary to prevent substantial injury to the organization.** |

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**Substantially revised.** The text in italics has been eliminated; the bold-faced and underlined text has been added.
(d) Paragraph (c) shall not apply with respect to information relating to a lawyer’s representation of an organization to investigate an alleged violation of law, or to defend the organization or an officer, employee or other constituent associated with the organization against a claim arising out of an alleged violation of law.

(e) A lawyer who reasonably believes that he or she has been discharged because of the lawyer’s actions taken pursuant to paragraphs (b) or (c), or who withdraws under circumstances that require or permit the lawyer to take action under either of those paragraphs, shall proceed as the lawyer reasonably believes necessary to assure that the organization’s highest authority is informed of the lawyer’s discharge or withdrawal.

(d) In dealing with an organization’s directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer knows or reasonably should know that the organization’s interests are adverse to those of the constituents with whom the lawyer is dealing.

(f) In dealing with an organization’s directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer knows or reasonably should know that the organization’s interests are adverse to those of the constituents with whom the lawyer is dealing.

(e) A lawyer representing an organization may also represent any of its directors, officers, employees, members, shareholders or other constituents, subject to the provisions of Rule 1.7. If the organization’s consent to the dual representation is required by Rule 1.7, the consent shall be given by an appropriate official of the organization other than the individual who is to be represented, or by the shareholders.

(g) A lawyer representing an organization may also represent any of its directors, officers, employees, members, shareholders or other constituents, subject to the provisions of Rule 1.7. If the organization’s consent to the dual representation is required by Rule 1.7, the consent shall be given by an appropriate official of the organization other than the individual who is to be represented, or by the shareholders.

(1) The 2003 revision to Model Rule 1.13 made essentially three changes of substance.

(a) First, the shortened text of Rule 1.13(b) gives the attorney who “knows” of corporate malfeasance\(^1\) more discretion in determining whether to report

\(^1\) The “knowledge” standard is fairly restrictive and was the subject of spirited discussion as the proposed amendments to Rule 1.13 made their way through the ABA process. In the initial phases of its deliberations, the Task Force considered a broader standard: an attorney would have been required to take action whenever he or she knew or “reasonably should [have] know[n]” about corporate malfeasance. That standard was perceived to be too broad and too ill defined, and eventually the “actual knowledge” standard was kept. See Lawrence Hamermesh, *The
the problem “up the ladder.” Under the former version, the attorney was required to apply specific factors in reaching that determination. The new version leaves it to the attorney to decide what factors to apply and how to weigh them. (But note: the specific factors listed in the former version of the Rule—“the seriousness of the violation and its consequences, the scope and nature of the lawyer's representation, the responsibility in the organization and the apparent motivation of the person involved, the policies of the organization concerning such matters and any other relevant considerations”—haven’t disappeared entirely; they have been moved from the text of the Rule itself into a new “Comment” following the Rule. See ABA Task Force Report 86.

(b) Second and most important, a new provision—Rule 1.13(c)(2)—explicitly allows an attorney, if going “up the ladder” to the attorney’s superiors proves insufficient, to divulge hitherto confidential client information outside the walls of the corporation when, in the lawyer’s judgment, disclosure is “necessary to prevent substantial injury to the organization.”

(c) Third, although stopping short of a comprehensive safety net for whistleblowers, the new Rule 1.13(e) provides a measure of protection by allowing an attorney who suffers disciplinary consequences for disclosing corporate malfeasance to inform “the organization’s highest authority” of the reasons why he or she suffered adverse consequences.

III. SUBSIDIARY EXPECTATIONS OF BOARD COUNSEL

A. Insulating trustees from potential liability. One of the general counsel’s critical responsibilities is to ensure that trustees are discharging the duties of their office in a manner consistent with their fiduciary duties and their duties of loyalty and diligence— in other words, in a manner that does not raise the specter of potential liability for trustees or the institution.


(1) The duty of “honesty” is self-explanatory: a trustee cannot insist on being recorded as present at a meeting if in fact absent, or engage in any other misrepresentations of fact in connection with his or her duties as a trustee.

(2) The duty to act in “good faith,” also known as “fiduciary duty,” is discussed in detail below.

(3) The duty to act “with a reasonable amount of diligence and care” means in practical terms that a trustee should:

• Be generally familiar with the bylaws (an obligation satisfied by reading the bylaws and having them available at meetings); and

• Prepare for, attend, and participate in scheduled meetings of the board and the committees to which the trustee is assigned.

These duties are described more generally in a useful essay titled “Statement of Individual Board Member's Responsibilities,” originally published in the National Center for Nonprofit Boards’ TEN BASIC RESPONSIBILITIES OF NONPROFIT BOARDS.

(4) The most important duty a trustee has is the duty to act as a corporate fiduciary. A member of a board owes an enforceable legal duty to the organization to manage its fiscal affairs prudently. A board member who breaches that duty can be held personally liable for any consequent damages the corporation suffers. The Sibley Hospital case provides some examples of breach of fiduciary duty:

• Conflicts of interest or self-dealing: A board member violates his or her fiduciary duty by knowingly allowing the corporation to enter into a business transaction with an entity (corporation, partnership, etc.) in which he or she has a substantial interest without disclosing that fact to other board members. In Sibley Hospital, two hospital board members who were also members of the board of a local bank steered the hospital's accounts to that bank, and arranged to have unusually large amounts of cash held on deposit at that bank, without disclosing their interest to their fellow hospital trustees.

• Failure to exercise independence of judgment: In Sibley Hospital, the court found that trustees acted negligently by establishing an executive committee that routinely accepted the recommendations of the president without debate, establishing a finance committee that did not meet a single time in eleven years, and generally ceding to the president important financial decisionmaking authority vested under the bylaws in the board.

A measure of insulation is provided by the business judgment rule. “The business judgment rule insulates corporate directors from legal liability arising from decisions
they make in their capacity as directors. The rule is based on the notion that directors, in the course of performing duties on behalf of a corporation, take risks and make mistakes for which they should not be held legally accountable. This protection is lost only when a [claimant] proves that the director's decision was the result of serious wrongdoing or corruption rather than the result of an error in judgment.” Mary A. Lopatto, *Note: Hasan v. Clevertrust Realty Investors: The Business Judgment Rule and Procedural Review of the Special Litigation Committee*, 34 Cath. U. L. Rev. 791, 791-92 (1985) (footnotes omitted). As a practical matter, the business judgment rule insulates trustees from liability for decisions undertaken in good faith, as long as they (1) believe that they are acting in the best interests of the institution, and (2) exercise the degree of care that an ordinarily prudent person in a like position would exercise under similar circumstances. *Oliver v. Boston University*, 2000 Del Ch. LEXIS 104.

B. *The intermediate sanctions law.* This law poses special issues for lawyers who represent governing boards at private institutions.2

(1) In 1996, following a well-publicized scandal involving the financial practices of the chief executive officer at the United Way of America, Congress enacted a new section of the Internal Revenue Code designed to make nonprofit organizations more scrupulous about compensation and money management. The law is commonly referred to as the “intermediate sanctions” law, because it gives the IRS new enforcement tools for dealing with financial irregularities at tax-exempt, nonprofit organizations. Until 1996, the only sanction the IRS could levy against a nonprofit organization was to take away its tax exemption – a sanction likened by one IRS official to an “atom bomb” in that it was so destructive that, for all intents and purposes, it could never be used.


(2) Under the 1996 intermediate sanctions legislation, the IRS is empowered to levy excise taxes on nonprofits (and, in some cases, on the organization’s trustees and high-ranking executive officers) who are found to have engaged in so-called “excess benefit transactions” such as the authorization of excessively lavish salaries for employees or less-than-arm’s length business transactions with trustees or other senior officials.

(3) *The Key Concept: “Excess Benefit Transaction.”* In a nutshell, the intermediate sanctions law subjects trustees to potential personal financial

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2 The intermediate sanctions law does not apply to institutions that are part of state or local government or a state instrumentality and thus not subject to taxation under Section 115 of the Internal Revenue Code.
liability if they engage in or approve an “excess benefit transaction.” The statute defines an excess benefit transaction as

... any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person, and the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received for providing such benefit.

Internal Revenue Code § 4958(c)(1). In plain English, the law prohibits trustees from engaging in, approving, or profiting from any transaction with a “disqualified person” (more on that term in a moment) that cannot be justified on an arm’s-length-negotiating basis. If a trustee is deemed by the IRS to have engaged in, approved, or profited from an excess benefit transaction, then that trustee is subject to a personal excise tax that can range as high as 200 percent of the “excess benefit” represented by the transaction.

(4) The university violates the intermediate sanctions laws only if an excess benefit transaction is entered into with a “disqualified person.” That odd term is defined at length in the temporary regulations. For our purposes it includes:

- Each trustee who serves as a voting member of the board;
- The president;
- All officers and employees who report directly to the president;
- All employees who earn $85,000 or more in salary annually; and
- Certain other categories of people who “control or determine” a substantial portion of the capital or operating budget or who determine compensation for employees.

Putting all these definitions and terms together: A trustee cannot engage in, profit from, or approve an “excess benefit transaction” that unreasonably enriches another trustee, the president, the president’s direct hires, or certain other categories of “disqualified persons” who work at or are affiliated with the institution. Business relationships between a trustee and the university must be arm’s-length. Compensation arrangements involving the president or the people who report directly to the president must be market-based – in line with what similarly qualified people performing similar jobs at other colleges are paid.

And it is the general counsel’s job to see that these standards are observed.

(5) The Regulatory “Safe Harbor” Provision for Compensation Arrangements. The real significance of the intermediate sanctions law, insofar as the general counsel is concerned, lies in the “safe harbor” provision that protects trustees from potential exposure for excise-tax liability.
The regulations provide a procedure that enables the board to establish a rebuttable presumption that a particular compensation arrangement is reasonable and therefore raises no potential difficulty as an excess benefit transaction. Under this procedure, a compensation arrangement is presumed to be reasonable if three conditions are satisfied:

- First, the compensation arrangement is approved in advance by the board of trustees as a whole or a committee of the board specifically authorized to consider and approve compensation arrangements.

- Second, in reaching its decision, the board (or authorized committee) relies on appropriate data establishing market comparability. This could include information on compensation paid by other colleges to comparably qualified persons performing the duties in question; compensation surveys compiled by independent firms (such as the National Association of College and University Business Officers); or evidence (in writing) that the person whom the institution seeks to employ has received a comparable offer from another institution.

- Third, the board (or committee) adequately documents the basis for its determination at the time the decision is made.

To take advantage of the “safe harbor” in the regulations, compensation decisions involving the president and other senior staff should be made by the board (or by a board committee) only after “comparability” data are collected and analyzed. The decision should be memorialized in written minutes that describe the comparability analysis and support the board’s conclusion that compensation is reasonable. The president should prepare and (if necessary) revise, on an annual basis, a list of “disqualified individuals” as that term is used in the law and temporary regulations. And in general, counsel should be alert to intermediate-sanctions issues that could arise if trustees (or companies operated or controlled by trustees) engage in business transactions with the university.

V. SOME WORDS OF ADVICE, CAUTION AND PRUDENCE FOR LAWYERS CONFRONTING ETHICAL ISSUES ARISING FROM BOARD REPRESENTATION: HOW TO DODGE BULLETS AND AVOID PERSONAL EXPOSURE

A. Nothing—nothing—poses more of a challenge for a lawyer representing an institutional client than coping with the suspicion (or something greater than a suspicion) that a trustee is engaged in some form of self-dealing or misconduct. Needless to say, the challenge is particularly acute when the official suspected of misconduct is the official to whom the lawyer reports.

It goes without saying that somewhere near the top of the lawyer’s priority list is careful scrutiny of the ethical obligations to which the lawyer is bound, focusing specifically on the complicated up-the-ladder reporting obligation in the state-bar equivalent of Rule 1.13(b) and (c).
Are there other practical steps a lawyer would be well advised to take? Recognizing that ethical conundrums take an infinite variety of forms, that generalizations can be dangerous, and that nothing substitutes for experience, here are a few items for any lawyer’s checklist.

(1) **Seek advice from an ethics rabbi or other qualified advisor.** If you work with a law firm of any size, that firm probably has what one state bar journal referred to as an “‘ethics rabbi’ to give ethical and behavior advice to lawyers and conduct in-house MCLE programs in ethics, professionalism, and civility ….” Peter M. Appleton, *Is Winning Everything?: ‘Professionalism’ Doesn’t Have To Mean ‘Doormat’,* 62 Ore. St. Bar. Bull. 21 (2002). If you don’t have access to a partner or colleague who is professionally responsible for advising you, consider (if the situation is dicey enough) digging into your pocket and engaging someone to provide advice. It provides insulation a mile thick to double-check with someone and get considered advice you can rely on. And you may possibly have insurance or indemnification to defray some of the cost—see the next paragraph.

Some interesting sub-questions: If you go to your outside law firm’s ethics guru and seek advice about an ethical dilemma confronting you in dealing with a troublesome client, *who does that lawyer represent* when answering your question? Is that lawyer your lawyer—or the institution’s lawyer? What if there is a conflict between the two? Is it your obligation—or the institution’s—to pay whatever legal bill is generated by your ethics consultation? (Note: Model Rule 1.6(b)(4) explicitly allows you to share information that would otherwise be confidential client information if necessary “to secure legal advice about [your] compliance with these Rules ….”)

(2) **Check to see whether you are covered by an institutional indemnification provision or liability insurance policy.** Typically (at least if you are a salaried employee) your institution’s bylaws provide substantial protection against lawsuits and other claims filed against you. Senior administrative officers are usually indemnified against claims asserted against them in any kind of action (civil, criminal, administrative, actual, threatened, pending, or completed); and for money payments in virtually any form (judgments, fines, settlement awards, and attorneys’ fees). However, there are preconditions. You are indemnified only if you acted in good faith and in a manner you reasonably believed was consistent with the institution’s best interests, and only if you accept the appointment of counsel selected by the institution and agree to defer to the institution with respect to the settlement of claims against you. It is also typical for institutions to purchase a commercial “errors and omissions” or “professional legal liability” policy that provides insulation from potential liability. You may have additional insurance protection through commercial or state-sponsored legal malpractice policies.
(3) Once you get even a whiff of a potential legal or ethical problem, *make absolutely sure your client understands your obligations*—including your reporting and withdrawal obligations—as a lawyer subject to the state code of professional conduct. That, of course, can be easier said than done; but for whatever cold comfort it gives, remember that under Model Rule 1.13(e) you are entitled to go over the head of the person to whom you report if you suspect that you are the subject of adverse action on account of your adherence to governing ethical rules.

B. It’s too early at this point to tell how broadly the ABA’s new Model Rules will be adopted at the state level. The revised version of Rule 1.13 is controversial in some circles and have been criticized in harsh language. The American College of Trial Lawyers, for example, predicted that the revised Rule would “destroy[ ] the trust, loyalty, and confidentiality that our legal system requires and assumes” and strip away “the most basic protections of the attorney-client privilege.” REPORT OF THE LEGAL ETHICS COMMITTEE ON DUTIES OF CONFIDENTIALITY 23 (March, 2001), available online at a ridiculously long URL:


Other critics decried the prospect of expanded lawyer liability and fretted about the damage that would be done to the attorney-client privilege if lawyers were forced in effect to give *Miranda* warnings before speaking with their corporate clients. Lawrence Hamermesh, *The ABA Task Force on Corporate Responsibility and the 2003 Changes to the Model Rules of Professional Conduct*, 17 GEO. J. LEGAL ETHICS 35, 50-51 (2003). The proposed changes may not been adopted yet by the state supreme court in your jurisdiction, and they may be modified before they are.

C. Notwithstanding the foregoing, it’s certainly not too early to begin thinking about new kinds of ethical constraints that may operate on campus lawyers who learn, by virtue of their relationships with institutional higher-ups, about problematic behavior that threatens substantial injury to the college or university. If something akin to revised Rule 1.13(b) were enacted in the state in which you’re licensed to practice law, you could find yourself at some point *ethically obligated* to disclose a president’s or trustee’s transgression to members of your board—not an easy situation for any lawyer to confront.

D. Some commentators have perceptively noted that the real significance of the lawyer-related governance reforms of the last few years lies not in the liberalized disclosure rules—which after all are triggered only in the most extreme of cases—but, rather, in a series of other SEC and ABA recommendations designed to *regularize lines of communication between lawyers and the members of corporate boards*. From Jill E. Fisch & Kenneth M. Rosen, *Lessons From Enron: How Did Corporate and Securities Law Fail? Is There a Role for Lawyers in Preventing Future Enrons?*, 48 VILLANOVA L. REV. 1097, 1135-36 (2003):
Systems through which lawyers are regularly required to provide information on risks, liabilities and other potential problems relieve the lawyer of the responsibility for coming forward with information about potential misconduct. Structures in which lawyers regularly report directly to the board or a key corporate official allow lawyers to bypass managers without creating the risk of retaliation that might result from sporadic reporting up. Moreover, reporting structures signal to outside lawyers the corporation's receptiveness to such information and reduce the perceived risk of client displeasure. If corporations were required to institute such reporting systems as part of their system of internal controls, information flow would be both increased and regularized. In addition, because they would be responsible both for instituting the systems and ensuring that they were reliable, corporate decisionmakers would have an incentive to reward lawyers for high quality reporting.

“Would everyone check to see they have an attorney? I seem to have ended up with two.”

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