



# AMERICAN UNIVERSITY

W A S H I N G T O N , D C

May 31, 2006

The Honorable Charles E. Grassley  
Chairman  
Senate Committee on Finance  
SD-219 Dirksen Senate Office Building  
Washington, D.C. 20510

**Re: American University**

Dear Chairman Grassley:

Thank you for your letter of May 17<sup>th</sup> regarding American University and for giving us the opportunity to respond to the concerns and questions you posed. We appreciate the interest you and your staff have in the future of American University ("AU"), as well as the fidelity which boards and managements of not-for-profit institutions generally have for their fiduciary duties.

You indicate that you are aware that the Board of American University has been considering a number of governance changes intended to ensure that there will be greater openness and transparency at AU. We are pleased to report that, in fact, such proposals were developed with considerable input from the various constituencies which comprise the AU community and were unanimously adopted by the AU Board at its recent meeting on May 19<sup>th</sup>. Bylaw amendments are being drafted to implement those reforms where appropriate and we expect their adoption at a special board meeting called for that purpose on June 9<sup>th</sup>. We will be happy to provide you with those bylaw amendments as well after their adoption.

**Major Governance Changes**

You asked to be informed about the details about the governance changes we have adopted. Consequently, we are providing you with this letter and a copy of the report agreed to during the Board of Trustees meeting on May 19<sup>th</sup>. While you will have the benefit of the full thirty page report for your review, we would like to highlight some of the key changes which we think address in particular your concerns about greater transparency and accountability in the governance processes, and relatedly assuring that faculty and students will have a meaningful voice in those processes.

Faculty/Student Trustees. A key recommendation approved by the Board is the addition of three new non-voting Trustees -- two faculty members and a current student. In addition, the Board directed its Trusteeship Committee to include on the Board a recent graduate of American University selected in consultation with student government and alumni representatives. The

OFFICE OF THE PRESIDENT

4400 MASSACHUSETTS AVENUE, NW WASHINGTON, DC 20016-8060 202-885-2121 FAX: 202-885-3265

Board recognized that 85% of independent colleges and universities do not have faculty and student trustees. However, the Board endorsed the recommendation that such participation be allowed to assure that the perspectives of faculty and students will be known to the full Board on all matters coming to it, while alleviating concerns that faculty and students might be conflicted in some ways by providing that they have non-voting status. Importantly, the Board also adopted the principle that the President of the University, who is also “affiliated” or “non-independent,” would be a non-voting Trustee as well.

Trusteeship Responsibilities. The Board adopted a detailed twelve point statement of the responsibilities of, and expectations for, service by each AU Trustee. The Board mandated administration of a Trustee orientation program to ensure that Trustees are adequately acquainted with the institution and their duties. It required periodic assessment of the performance of the Board itself, as well as the service provided by individual Trustees. While an assessment of Trustees’ performance will be conducted annually by the Board, another comprehensive review of University governance is mandated within five years from this month to assure that periodic attention is given to maintaining a strong, responsible and responsive system of governance for AU in the future.

Presidential Performance Review. The Board further specified that there shall be comprehensive periodic assessments of the President's performance. To foster enhanced connection between the Board and University constituents, in addition to a number of other substantial steps -- such as the addition of faculty and student trustees, and involvement of constituents in Board meetings -- Trustees will periodically meet with constituents at discussion forums open to all. This greater connectedness between the Board members and representatives from the University community will help ensure the Board stays current and informed about how others view the President’s performance.

Role of the President. To safeguard against the possibility of dominance or undue influence by the President of the University, the Board also agreed that the President would not be a member of the Executive Committee and Trusteeship Committee. Obviously, as the CEO of the University, the President will be expected to meet with the Executive Committee regularly. However, it is anticipated that some portion of every Board meeting and every Executive Committee meeting will be held among the “independent” or non-affiliated” Trustees without the President in attendance.

Board Committee Transparency. The reforms also address the array and functioning of Board committees. University constituents will be encouraged to participate extensively in Board committee work. Further, each committee is directed to revise or develop a committee charter, identifying committee duties, functions and membership, for review and approval by the full Board later this year. The responsibilities of the Compensation Subcommittee are fully described. The Executive Committee's authority is specified extensively in a manner that ensures that the Executive Committee, while serving its necessary role, will not take actions that properly fall within the province of the full Board.

Board Diversity. The governance reforms also address the key objective of fostering diversity among AU Trustees, including, among other diversity-enhancing characteristics, experience in higher education and not-for-profit governance.

Increased Board Meetings. The reforms increase to four the number of regular meetings of the Board annually, and also authorize special meetings of the Board, as well as emergency meetings on as little as 24 hours notice.

Conflict of Interest/Whistleblower Policies. The reforms require the Board to adopt updated, best-practices policies on Trustee conflicts of interest, and on the proficient, sensitive, institution-wide handling of whistleblower complaints. These policies are also being presented to the Board for adoption at its June 9 meeting.

Board Support. The Board also committed to augment the staffing of the Board itself, to ensure that the Board's administrative needs, for oversight and otherwise, will be robustly supported.

The reforms identified above only illustrate the range of governance reform steps the Board has taken. Although the governance needs of various universities will differ, we believe that the steps we have taken to date reflect the rigor, seriousness, and responsiveness with which our Board is addressing its governance responsibilities as a fiduciary for American University.

### **Process for Recommending Reforms**

These actions, and others described in the report of the Board Governance Committee, signal a significant transition for the AU Board, which, after the events of autumn, 2005, committed to a thorough review of its governance in furtherance of its fiduciary duties. In addition to the creation of the Special Committee on Governance that resulted in adoption of the reform package, the Board and its members embarked on a program of dedicated openness and accessibility; greater campus representation in Board and committee discussions; and improved communications with, and presence on, campus. For instance, the Board authorized the creation of a governance website so that AU constituents and the public were able to track the governance progress over the past six months. The website will be used in the future to promote accountability and transparency in the Board's work.

The governance reforms the Board adopted on May 19th resulted from extended consultations with all AU constituent groups over a period of months, and also from study of best governance practices of leading well-governed universities throughout the United States. The Board's Governance Committee met 18 times over a six-month period to review these matters in depth. It benefited throughout from the advice of two nationally-regarded authorities on university board governance, Mr. Martin Michaelson, a partner in Hogan & Hartson and former counsel to Harvard University, and Mr. Richard T. Ingram, who recently retired from a career in which he led the Association of Governing Boards of Universities and Colleges.

### **Support From Campus Communities for Reform Measures**

The report of the Governance Committee was shared with representatives of the AU faculty and student body, as well as the deans. We are pleased to report that the reform measures adopted by the Board have earned wide support from these campus constituencies, as well as from alumni representatives. There is a prevailing sense on the AU campus that with the

adoption of these measures, the Board has embarked on a new era of transparency, inclusiveness, and accountability that will make American an even stronger university in the future.

The deans issued a statement strongly supporting the work of the Board's Governance Committee: "The deans are pleased that the five core principles and eighteen recommendations contained in our December 5, 2005, *Preliminary Proposal on Governance Reform* are so clearly reflected in the report. The final document supports the core principles of integrity, transparency, accountability, engagement, and legitimacy. While there are differences between our recommendations and the final proposals, we are satisfied that the Special Committee's report reflects serious and thoughtful consideration of the issues. It is our view that the proposals themselves, which will be reviewed within five years, will foster meaningful reform and include substantive voice for the various constituencies of the university community."

Faculty leaders also applauded the package: "The Board's actions bring increases in oversight, transparency, accountability, and faculty voice. The consultative approach that has marked Board reform has strengthened American University. We urge the Board to continue with this approach to governance." In particular, we note that leaders from the Faculty Senate had produced a report containing their suggestions for governance improvement including the provision for appointment of faculty Trustees with non-voting status.

While student leaders indicated they would prefer more than one student trustee, they expressed overall pleasure with the majority of the reforms adopted by the Board, and in particular appreciated the Board's commitment to appoint a very recent graduate as a voting Trustee in consultation with student government groups and alumni representatives.

### **New Trustees Provide New Leadership**

After a rigorous selection process which utilized the knowledge and standing of the deans and faculty, the University added seven distinguished new Trustees at its May 19<sup>th</sup> meeting. These talented individuals bring the Board back to a level of 25 Trustees. Two of them are former college presidents; one is a former director of the Peace Corps; one is a former AU student government president; and four are AU alumni. Selection of the new Trustees resulted from an inclusive campus-wide process that produced some 85 recommendations and reflects a stated commitment by the AU Board to bring an enhanced diversity of experience and breadth of knowledge to Board service. The Trustees were vetted by the Board's Trusteeship Committee and were approved by the Board of Higher Education and Ministry of the United Methodist Church. A short biography of each of the seven new members is appended to this letter.

### **Removal Of A Trustee Is Permitted By The Current Bylaws**

You asked us to evaluate the adequacy of current legal authority for the Board to remove a Trustee. Article III, Section 7 of the current bylaws permits the removal of a Trustee at any regular meeting if two-thirds of the Trustees present agree "adequate cause" to remove a Trustee exists. For example, if 15 members of the Board are present, a vote of 10 or more to remove a member is sufficient. "Adequate cause" has been defined in case law, Morgan v. American University, 534 A. 2d 323, 329 (D.C. Court of Appeals 1987) (upholding dismissal of a professor for misrepresentations made in the course of obtaining employment at AU). In the governance

reforms just adopted, this particular bylaw provision will be extended to permit removal of a Trustee at a “special” meeting of the Board. Article XVI of the current bylaws permit the AU Board to make such changes.

We have further agreed that all Trustees who seek reappointment will be subject to a careful review of their past performance on this Board, their participation in Board meetings and committees, and their contributions to AU more generally. This is effective immediately and applies to all current Trustees, as well as future Trustees.

Our analysis of AU’s charter, and our recent actions in adding new Trustees and assuring meaningful review of trusteeship service before reappointment, persuade us that the charter under which American University operates provides the Board with the full measure of authority needed to assure that AU has at all times a dedicated and responsible diverse group of Trustees who must demonstrate their qualifications for service by their experience and stewardship. We do not request or recommend any charter amendments, and respectfully suggest that none are necessary under these circumstances.

### **Whistleblower Protection Is A Core AU Value**

With respect to the issue of “whistleblower” protection, AU and its Board of Trustees recognize your long-term leadership in the area of protecting whistleblowers against retaliation. We also fully share your concern. The University has maintained a series of policies to protect whistleblowers for more than 12 years. The current policies are posted on the University’s website. As a result of the experiences last year, we are consolidating these policies and updating them, and the Board will vote on this revision on June 9th.

In this respect, the entire investigation which led to the resignation of American University’s former President was triggered by AU’s affirmative response to a whistleblower complaint. No particular effort was made to identify the whistleblower. (One former employee has publicly claimed to be the author of the two whistleblower letters. We cannot verify that claim. But, it is reassuring that AU’s outside counsel did interview the former employee prior to his claim that he authored the letters, and presented his information, along with many others, to the Board.) Other AU personnel who knowingly cooperated with our internal investigation were promised protection from retaliation. In fact, one particularly courageous employee who came forward was given a written commendation in the employee’s personnel file. These employees were also provided legal counsel if they desired representation. By its words and actions, both during and after the internal Ladner investigation, we believe the AU Board has indicated its respect for the function of whistleblowers to alert the institution to suspected illegality or malfeasance on the part of its leaders.

Your letter refers to an email written by an individual Trustee. As we read his e-mail, and as the author has confirmed to us (and we believe to your staff) that email was not directed at “whistleblowers”, but at individuals who may have compromised their fiduciary duties to the University by leaking confidential information to the media. It is a fact that Trustees were upset during this period over leaks to the media of confidential information. The source of these leaks was never determined. What we can say definitively is that this particular email had no impact on how the internal investigation was conducted, and all “whistleblowers” and

cooperating witnesses were protected by the Board from any form of search for their identity or retaliation against them.

### **Minority Votes On The Ladner Issues**

Your letter summarizes specific concerns regarding how individual Board members voted on some of the issues regarding Dr. Ladner's contract and severance agreement. We addressed this overall issue in detail to you in our letter of December 1, 2005. We acknowledged in that letter that mistakes had been made by the AU Board and gave you and the American University community our assurance that our governance reforms would include actions to address them.

In each of the four votes taken by the Board which your letter addresses, the majority votes resulted in definitive Board actions to end not only the Ladner presidency, but cut his remaining ties to the University and end the threat of continued controversy, distraction, and expense through litigation over his termination. That said, it does not imply that those voting in the minority were any less conscious of, or faithful to, their sense of fiduciary responsibility to the University. We believe that the differences reflected in particular votes reflected differences regarding the means best suited to protect the University, and not over the duty and desire to protect the University.

Your letter asks for our comment on four specific votes taken by the Board. The first issue concerns unsuccessful efforts to amend or reject the Audit Committee's report. We think those failed motions stemmed from good faith disagreements over what the Board's prior understandings and accepted courses of dealing with Dr. Ladner permitted, primarily with respect to discrete categories of expense. Second, you asked about those Trustees who voted against the declaration of Dr. Ladner's contract as unauthorized and unenforceable. Again, we believe they were voting their conscience based, in part, on the recognition by AU's counsel that the issue was not totally one-sided in the University's favor, and/or the countervailing arguments which had been put forward by Dr. Ladner's counsel. Third, while it is true that some Board members voted not to terminate Dr. Ladner for cause, all the Trustees had agreed that his presidency must end and this vote reflected as much a difference over the means to that end, rather than a disagreement over the termination of his presidency. Finally, you raised the issue of a Trustee who unsuccessfully urged that a settlement package be offered to Dr. Ladner that would extend payments out over an eight year period. As we understood it, that proposal was a repackaging of the consideration the Board was considering as part of a settlement to extinguish the threat of litigation and not in addition to the settlement the Board ultimately authorized. In summary, whether these minority views were right or wrong, we believe these Trustees – indeed, all the Trustees – were motivated by their good faith judgment as to what was best for the University in a very difficult and contentious crisis period for the University.

### **Board Respect for Legal Requirements**

Your letter also references a document which apparently left the impression that at least one Trustee did not take seriously certain legal requirements related to AU's non-profit status, possibly because the financial penalties for noncompliance were not considered severe. With respect to the issue of the President's compensation, the Board actually had sought and received expert advice from compensation consultants as to the propriety of Dr. Ladner's compensation.

When the Board's leadership became wary of certain advice and changed consultants, the Board was advised for the first time that it might be vulnerable to a claim of excess compensation triggering intermediate sanction penalties. In response to that advice, and corresponding legal advice, the Board acted to reduce Dr Ladner's compensation. Thus, the specter of intermediate sanctions penalties was actually a factor which prompted the Board to be sure that his compensation was set at reasonable levels. There were some on the Board who believed that his compensation was appropriate and justifiable at the higher levels based on the progress the University had made during his tenure. Importantly, their view was that the compensation should not have been considered excessive, and hence no sanctions were appropriate, rather than reflecting a dismissive attitude or indifference toward the possibility of financial penalties. Whatever the likely risk of sanctions in terms of financial penalties to Dr. Ladner or the Trustees, the desire not to run the risk of incurring sanctions, or even criticism, prompted the Board to follow its consultants' advice and lower Dr. Ladner's compensation significantly.

Moreover, the University and, certainly, the Board have no disagreement with you over the imperative for not-for-profit institutions to obey the law and, going beyond the minimum legal requirements, to reflect a pervasive regard for ethical and honest behavior. The University spent over \$1 million dollars in its internal investigation to ensure it was complying with federal non-profit tax law, among other requirements. We recognize having non-profit status is a benefit of public policy decisions, and that American University has profound fiduciary obligations as a result. We as a Board are recommitted, in word and deed, to these principles. As your letter noted, AU may be one of the only situations where the consultant hired by a university recommended a lower salary for a university president. We went ahead and followed that recommendation and lowered Dr. Ladner's salary consistent with expert advice. We intend to continue to seek advice from experts and follow it whenever it is appropriate to do so.

### **Addressing Document Issues**

With respect to the University's document production to the Senate, to-date AU has produced approximately 10,000 pages of materials to the Committee. It is obvious to us that you and your staff have carefully reviewed these materials. Most importantly, AU has attempted at all points to cooperate with the Committee's requests.

As you know, internal and external AU lawyers were heavily involved in investigating the whistleblower complaint and the resulting audit and investigation. There is one on-going litigation matter still occurring related to this issue. We are advised that the Committee has not questioned the legitimacy of the attorney-client privilege and attorney work product doctrine claims the University has made. While we appreciate the Committee's desire to have the University share all this privileged information with the public, as a result of the on-going litigation we are advised by counsel that given the continued potential for litigation, it is not in the University's interest to waive the attorney client privilege. This recommendation comes from outside counsel, as well as the University's general counsel. As indicated, we feel obliged to follow the advice of counsel in such matters, and therefore the University will continue to assert its legitimate privilege and work product claims on a limited number of documents.

We note that the American Bar Association and other professional organizations have taken the position that the invocation of attorney/client privilege should not be taken as an



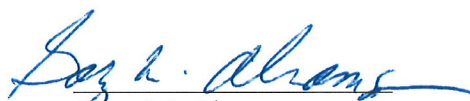
indication of a lack of cooperation. In light of our sharing of vast documentation with the Committee staff and efforts to respond fully to your and their questions, we hope that you will recognize that we have been as forthcoming and cooperative as possible up to the point where a waiver of attorney/client privilege might be adverse to the University's interests in other contexts.

We are particularly grateful and appreciative to you and your staff for working with AU's lawyers to ensure that any document made public has been the subject of careful analysis to ensure it will not contain proprietary, personal, or privileged information.

### Conclusion

We recognize that it was our actions as the Board of American University that prompted you, as Chairman of the Senate Finance Committee, to give serious attention to what had transpired and serious consideration as to the adequacy of remedial measures needed to be taken to safeguard against repetitions of such episodes at AU or other respected institutions of higher education. During the past several months of inquiry and scrutiny, the AU Board has tried to respond fully to the concerns raised not only by you but by the AU community itself. The fact that we have now openly arrived at a set of reform measures which have won the endorsement of the many elements of that community should reassure you as Chairman and the Members of your committee that your concerns have been heard and meaningfully addressed by the AU Board. While it would not be any institution's choice to be in the spotlight of inquiry by a Senate committee, we fully understand why that attention was trained on us. We hope that the improvements we have made will not only measure up to the goals expressed in your letter of greater openness and transparency for American University, but will serve to refocus institutions of higher education generally on assuring that they are following best governance practices themselves.

Sincerely,



Gary M. Abramson  
Chairman  
Board of Trustees



Thomas A. Gottschalk  
Vice Chairman  
Board of Trustees