AMERICAN UNIVERSITY
WASHINGTON, DC

December 1, 2005

The Honorable Charles E. Grassley
Chairman, Committee on Finance
United States Senate
219 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Max Baucus
United States Senate
511 Hart Senate Office Building
Washington, DC 20510

Dear Senator Grassley and Senator Baucus:

This letter accompanies the production of documents and information by American University ("AU" or the "University") in response to your October 27, 2005 letter.

We recognize that the Senate Finance Committee (the "Committee") is interested in understanding the circumstances relating to the termination of Dr. Benjamin Ladner as President of the University. This letter endeavors to provide you with our perspective on these matters, including areas in which we feel the Board of Trustees acted consistently with good governance practices and those in which certain of our practices at the time, and in hindsight, were deficient and which the Board is actively engaged in correcting.

Summary of Events Related to the Termination of Dr. Ladner as President of American University

In the view of the Board, Dr. Ladner was an effective leader of the University during his eleven-year tenure as its President. This view is certainly borne out by the achievements of the University during this period from 1994 to 2005 based on external measures of improved quality, enhanced reputation and increased financial strength. Perhaps, because of the University's success under his leadership and a concern that Dr. Ladner might be recruited to another university, the Board failed to follow sufficiently rigorous procedures for reviewing and approving the President's employment contract and compensation, as well as effectively auditing his expenses. The full Board, ourselves included, did not learn until early 2005 that in 1997 the then-Chair of the Board entered into an "evergreen" contract with Dr. Ladner, with no ending term, which had ambiguous terms that provided for the reimbursement of expenses over and above those allowed by University policies, and agreed to have Dr. Ladner serve as a highly paid tenured professor indefinitely following his Presidency.

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In 2002, the Board's Compensation Committee engaged outside compensation consultants to advise it on compensation matters. Under the chairmanship of a trustee with considerable professional background in personnel management, the Committee questioned some of the advice it was receiving and, in 2004, retained Mercer Consulting to advise it on the appropriateness of the compensation of the President and other senior officers of the University. The law firm of Arnold & Porter LLP was also retained in 2004 to advise the Board on legal issues implicated by these compensation matters.

Mercer reported to the Compensation Committee that, while the compensation of the University's vice presidents was reasonable in comparison with other comparable universities, Dr. Ladner's compensation was at the high end and could be subject to challenge as excessive. After considerable discussion, the Board, in April 2005, accepted the Compensation Committee's recommendation that the President's total annual compensation, including base salary, a performance-based incentive bonus to be awarded by the Board, and various forms of deferred compensation, be reduced from \$886,750 to a potential high of \$793,000. A majority of trustees continued to regard Dr. Ladner as a highly successful and effective leader of American University, but felt this downward adjustment of his compensation was a prudent exercise of their fiduciary responsibility to ensure that the President's compensation was in line with that paid by comparable universities. Other trustees believed that Dr. Ladner's leadership and contributions to the University fully justified the level of compensation he had been receiving.

The reduction in Dr. Ladner's compensation created considerable friction between him and the Board's leadership, including the chair of the Compensation Committee. It was during this period, in early 2005, that the full Board for the first time was made aware of the existence of the 1997 employment contract entered into between the then-Board chair and Dr. Ladner. Some trustees objected to this contract and felt that it should be either renegotiated or annulled.

In March 2005, the Executive Committee received an anonymous letter alleging improper spending of University funds by the President and his wife for personal purposes. The Executive Committee of the Board promptly authorized its Audit Committee to investigate these allegations and report back to the Board. The full Board was informed of these allegations at its regular May meeting, at which time the Board resolved that the investigation should continue as expeditiously as possible.

The Audit Committee retained forensic accountants (Protiviti, Inc.) and two outside law firms (Arnold & Porter LLP and Manatt, Phelps & Phillips LLP) to assist it in conducting a thorough and objective investigation. While it endeavored to conclude its investigation by the end of June, the Audit Committee was frustrated by what appeared to it to be a lack of understanding, if not a lack of cooperation, on the part of Dr. Ladner in providing access to needed information.

The Audit Committee completed its work in late August as the new school year was about to commence. The Audit Committee reported to the Executive Committee that the allegations were largely confirmed by its investigation. The Executive Committee acted on August 23, before the start of the fall semester, to suspend Dr. Ladner from his post as President until the Board could receive the Audit Committee's report and act on its recommendations. The

Executive Committee also decided to terminate a full-time chef employed by the Ladners at University expense, and to reassign a social secretary/assistant who assisted Mrs. Ladner in her role as the President's wife and in operating the President's official residence. These actions by the Executive Committee were taken before notification to the full Board.

The full Board met in a special meeting on September 10 to receive the just-completed report of the Audit Committee and to hear its recommendations. In order to give Dr. Ladner a fair hearing, he and his counsel attended a portion of the meeting and made a presentation to the Board. Dr. Ladner's lawyers maintained, in essence, that his expenses were either reasonable and justified University expenses and/or authorized by the provisions of his 1997 contract. At that meeting, the Board decided that further examination of certain expenses was appropriate and asked the Audit Committee to undertake that further review promptly.

The Audit Committee completed its work in early October. The full Board convened on October 10, again in special session. It accepted the Audit Committee's final recommendations to report to the Internal Revenue Service an additional $398,911 of imputed income for Dr. Ladner for the period of 2002 to April 30, 2005, and to demand reimbursement for $125,703, plus interest, in personal expenses paid for by the University. It also decided that Dr. Ladner would not be returned to the presidency, and authorized a committee of trustees to negotiate with Dr. Ladner regarding the termination of his presidency. The Board also established a committee to consider whether, when and how to commence a search for a new president, and another committee to consider and recommend changes in the Board's governance to guard against a recurrence of the circumstances that contributed to the controversy over Dr. Ladner's compensation and expenses.

As explained below, the Board was seeking a reasonable settlement with Dr. Ladner both to end his affiliation with the University and to resolve legal claims he would likely assert if he were unilaterally terminated by the Board. He and his lawyers asserted that the 1997 employment agreement was a valid contract and that there were no contractual or legal grounds to terminate his employment. While some trustees felt that the University would have strong grounds to defend against such claims, there was certainly no guarantee or assurance that the University would ultimately prevail. At least some trustees, the undersigned included, anticipated that the costs of a multi-year defense of any legal action by Dr. Ladner could easily exceed $1 million. Such legal action would likely be quite costly, regardless of whether it was eventually settled or tried, and also would likely be an ongoing drain on University resources and a distraction from its educational priorities.

On October 20, the full Board met again in special session. It received a report from its negotiating committee, which recommended that negotiations be brought to a conclusion promptly – whether or not successful – and that to do so Dr. Ladner be presented with a "final and best" proposal. The negotiators reported that there was a wide gulf between what they felt was a reasonable settlement and Dr. Ladner's demands. The Board approved such a proposal, under which Dr. Ladner would immediately relinquish his presidency and all claims under the disputed 1997 employment agreement, including any claim to continued employment as a member of the faculty, in return for being allowed to retain certain deferred compensation totaling $2.75 million previously awarded and set aside for him with respect to prior years of service (but which, arguably, had not yet fully vested), and a one-time settlement payment totaling $950,000 before taxes and other adjustments.

Dr. Ladner was given until October 25 to decide whether to accept the Board's final offer. If he refused it, the Board was prepared to terminate him for cause and defend against the legal action Dr. Ladner was expected to bring against the University, notwithstanding the cost, disruption and uncertain result of such litigation.

At its October 20 meeting, the Board unanimously elected a new Chair, Gary Abramson, who took office on November 11, at the time of the next regularly scheduled Board meeting. The Board also named the University's Provost, Dr. Cornelius Kerwin, the interim President of the University to serve until a new President is selected.

On October 25, Dr. Ladner accepted the Board's final offer, and his resignation was effective immediately.

With this overview in mind, we are pleased to provide you with more details concerning these matters, including the achievements of American University during the period of Dr. Ladner's presidency, the dispute over his compensation, and finally the investigation and substantiation of anonymous allegations that led to the termination of Dr. Ladner's presidency and other affiliations with the University. In all of these matters, we believe that the University's Board, comprised wholly of volunteers and acting without any compensation, endeavored individually and collectively to take actions and reach decisions that were in the best interests of the University and all the constituencies which comprise the AU community, including students, faculty, staff, alumni and donors. Notably, by reducing the compensation of a successful President when advised to do so by outside experts, and by conducting a thorough investigation of allegations of improper expenditures by the President which led to his suspension and eventual resignation, we believe that the Board acted with fidelity to its fiduciary obligations to the University.

I. <u>The Growing Strength and Reputation of American University.</u>

Founded in 1893, American University currently enrolls 11,500 students in programs offered by its six schools and colleges with nearly 600 full-time faculty, several hundred adjunct faculty, and more than 1,300 full-time staff. The strength of the deans and the faculty of AU, and the programs they have developed, is outstanding. The Middle States Commission on Higher Education, which accredits colleges and universities in this region, awarded AU unconditional accreditation in 2004, commended the University for its progress since its last evaluation in 1994, and noted that:

> American University faculty members are committed instructors both in and out of the classroom while they pursue impressive research and service agendas. Examples abound of faculty members who are exploring, with the support and encouragement of the University, the interconnections between teaching, research, and service/engagement.

Internal measures of the quality and effectiveness of the teaching which occurs at AU were recently confirmed by the National Survey of Student Engagement (supported by the Pew Charitable Trusts) which found that AU placed first among its peers on three of five dimensions of the undergraduate educational experience, such as faculty quality and intellectual rigor, and second on a fourth criterion.

Another recent study by U.S. News and World Report identified AU as among the universities whose overall ratings had improved most dramatically in recent years, and also placed programs in the University's Washington College of Law and School of Public Affairs in the top ten nationally. Similarly, the Kogod Business School, School of International Service, School of Communication, and College of Arts and Sciences have been recognized for the quality of their programs by specialized accrediting bodies or other external studies.

Over the past decade, American University has held its tuition increases, on average, below the norm for increases at both public and private institutions. The tuition charged for an AU undergraduate education is in the middle range of comparable institutions. AU is the only college or university in the Washington, D.C., area selected as a "best value" in the Fiske Review of Higher Education. To assure that students from all walks of life can attend it, AU dedicates about 30% of all tuition revenue to financial aid which is distributed on both merit and need.

Certainly, the attainments and good administration of the University cannot be laid to the credit of any one person, even its President. But, like the coach of a team or CEO of a corporation, the president of a university is ultimately responsible for success or failure of the institution. It has to be acknowledged that AU made remarkable progress during Dr. Ladner's eleven-year tenure, which began in 1994, following a period of unstable leadership at the University.

Under Dr. Ladner's leadership, the University developed and is implementing a comprehensive strategic plan designed to improve the quality of the education it offers, the service it provides locally, nationally and globally, and its financial strength. (AUSF 010423-010429.) Also during Dr. Ladner's tenure, faculty governance was improved and the Board itself established and periodically revised its own policies, including policies relating to conflicts of interest, engagement with campus representatives, trustee responsibilities and governance. (AUSF 009164-009177, 009185-009186, 009280-009283, 009392-009394, 009440-009516.) These policies set forth clear expectations for effective trusteeship on behalf of the University.

A comparison of the state of the University today with its status in 1994, Dr. Ladner's inaugural year, tells a tale of remarkable success for which the entire University community collectively deserves credit. In addition to the external rankings mentioned above, the number of applications received annually almost tripled from 4,830 to 13,560. Selectivity, as reflected in the University's acceptance rate of freshman applications, improved from 77% to 51%. The average high school grade point and SAT score for entering freshman increased, as did the freshman retention rate (from 84% to 89%).

As part of the University's Strategic Plan, there was also a greater emphasis on the global reach of the University. It helped to establish a new and thriving U.S. accredited university in

Sharjah in the United Arab Emerites, and has been commissioned to help found a new university in Nigeria, among several international educational affiliations and consultancies. In 1994, 400 AU students studied abroad. In 2005, that number had increased substantially.

Financial support for the University also grew dramatically under Dr. Ladner's leadership. The endowment which stood at $36 million in 1994 has grown over eightfold to $280 million today. The alumni giving rate has more than tripled, as have annual total cash contributions. During Dr. Ladner's tenure, the University received some of its largest individual gifts, including one of $15 million and another to name the new arts center. Grants awarded to faculty annually grew from $5 million to $14 million.

The scale of the University and its complexity also grew under Dr. Ladner. The budget in 1994 was $181 million. In 2005, it is $357 million. Sixteen percent of the campus was renovated or rebuilt during those eleven years. The University's total facilities grew by 40 percent during that period. Staff salaries started out below the regional mean, and now are above the mean. Faculty salaries have also improved relative to other institutions, and several key categories are now at AAUP Level 1.

More could be said about the growth and development of American University during the Ladner years, but the foregoing illustrates why we believe Dr. Ladner was held in very high regard by the trustees and certainly many friends of the University. We reiterate that these accomplishments cannot all be laid at his feet by any means, but they occurred on his watch, and they contributed to a sense on the Board and beyond that he had proven to be an exceptional university president and a strong leader.

II. <u>The Board's Review of Presidential Compensation.</u>

As discussed above, in 1994 the University engaged Dr. Ladner as President. A written contract, drafted by the then-General Counsel of the University, Anthony Morella, was signed by Dr. Ladner and, on behalf of the University, by the then-Chairman of the Board of Trustees, Edward Carr, and the Vice President of Finance of the University, Donald L. Myers, who had full contracting authority to bind the University. The 1994 contract (AUSF 000060-000067) had a three-year term and contained appropriate terms and protections for the University and compensation provisions comparable to standard practices in higher education. Although the contract was not made public, its terms were widely understood by the members of the Board and, of course, by the University's Office of Finance.

In 1997, Dr. Ladner signed what purported to be a new employment agreement (AUSF 000068-000072). He negotiated the terms of this contract with then-Chairman of the Board, William I. Jacobs, who has since left the Board. In contrast to the 1994 contract, the 1997 contract was not prepared by the University's lawyers. In further contrast to the 1994 contract, the 1997 employment agreement was an "evergreen" contract, with no fixed termination date. The 1997 contract was signed by only Dr. Ladner and Mr. Jacobs. It was not signed or reviewed by the Vice President of Finance, or any other individual at the University with contracting authority, and no one with such authority was provided a copy of the contract at that time.

There is no contemporaneous documentary evidence that the 1997 contract was presented to the Board for its approval despite the fact that the University's Bylaws provide that the President "shall receive such compensation as the Board may direct." Bylaws, Section 2, Article 10 (AUSF0009398-0009412). While it is unclear whether a few individual trustees were informed about the 1997 contract when it was executed, it was not until 2005 that the 1997 contract was made known to the full Board.

The 1997 contract, and lack of adequate internal controls over the President's expenses, created the potential for misunderstanding and abuse. In 1997, Dr. Ladner retained a University-paid chef to prepare food for receptions and meals at the President's residence, apparently based on the expectation that he would be engaged in frequent entertaining on the University's behalf at the residence, and, according to Dr. Ladner, also based on the contract's provision that the University would cover all costs of Dr. Ladner's dining. The 1997 contract repeated the provisions of the 1994 contract under which the President was given a lifetime faculty position, but the 1997 contract added a requirement that, after the end of his presidency, he be paid a salary at least 20% higher than the next highest paid professor. The 1997 contract, drafted without the participation of University counsel, contained a number of ambiguous provisions. For example, the 1997 employment agreement, unlike the 1994 contract, did not require Dr. Ladner to comply with the University's spending, travel and other policies, and instead provided for "first class" travel, a term Dr. Ladner construed quite broadly.

Between 1997 and 2002, Board officers led annual reviews of the President's compensation. However, the Board minutes do not reflect any mention or discussion of the 1997 contract at any meeting.

Without such knowledge, the Board in 1997 did approve a "split dollar" life insurance policy for Dr. Ladner to provide income for retirement and a deferred compensation plan in 1999/2000. The Board also approved a retention bonus of $400,000 funded by the University in 2000, but set to vest over time. Prior to the date it was to vest on its original schedule, Dr. Ladner deferred the vesting until 2010. The Board concluded that these deferred compensation payments were justified because Dr. Ladner was regarded as a very successful leader of the University, as reflected in virtually all relevant metrics and indicators, and the Board was concerned that another university might try to lure him away. There was also a recognition that Dr. Ladner, having come to the University late in his career, was legitimately concerned about his retirement security. The structure of his deferred compensation was viewed essentially as a tax issue to be determined by Dr. Ladner and his advisers.

Beginning in 1999, the full Board began a process of more actively reviewing and setting the President's compensation. Beginning in 2002, the Compensation Committee was chaired by a trustee with a distinguished professional background in personnel management. The Committee engaged outside experts, who advised it on the appropriateness of the President's total compensation. The Committee questioned the advice it was receiving from one consultant and eventually retained Mercer Consulting, as well as the law firm of Arnold & Porter LLP, to advise it. Based on the advice it received, the Compensation Committee concluded, and the full Board was advised, that Dr. Ladner's annual compensation was likely at the high end of what comparable university presidents reportedly earn, and might be subject to challenge under Internal Revenue Service regulations.

After much discussion and exploration of alternatives, the Board, in April 2005, reduced Dr. Ladner's total compensation by approximately 16%. His total annual compensation, including base salary, incentive bonus, insurance premiums, and deferred compensation, was capped at $793,000, reduced from a high of $886,750. This process reflected a significant oversight initiative, voluntarily undertaken by the Board, to ensure that the University did not pay excessive compensation, based on comparable data and expert opinions.

Dr. Ladner reacted to this downward "correction" in his compensation. Specifically, he asserted that the Board's action was inappropriate given its overall assessment that he was doing an outstanding job for the University. Relations between Dr. Ladner and certain members of the Board became quite strained in the latter part of 2004 and into 2005.

III. The Board's Prompt Action on Anonymous Allegations of Expense Abuse.

In March 2005, the Executive Committee received anonymous allegations of improper spending of University funds by the President for personal purposes, and the Board's Executive Committee immediately authorized an investigation in March 2005. (The decision to treat this anonymous complaint in a serious manner is fully consistent with the approach to long-term public policy concerns that this Senate Committee has advocated.) At its May, 2005 meeting, the full Board was informed of the allegations and authorized the continuation of the investigation. The Audit Committee, while frustrated and delayed by what it felt was a lack of understanding and cooperation from Dr. Ladner, pressed on with its work until it was completed in late August.

This investigation ultimately led to the Audit Committee finding that the University had paid, or Dr. Ladner had been reimbursed by the University improperly, for approximately $125,703 in personal expenses, and that Dr. Ladner had incurred approximately $398,911 of additional imputed taxable income, both occurring over the period 2002 to 2005.

The Board's consideration of the Audit Committee's recommendations was complicated by several factors. First, there was a legal question as to whether the 1997 employment agreement was a valid contract. Second, some of the terms of the 1997 agreement were ambiguous, leaving open questions about what expenses by the President were authorized to be paid by the University. Third, in an attempt to maintain confidentiality and protect Dr. Ladner's privacy, the initial investigation was conducted by the Audit Committee, which then reported and made recommendations to the Executive Committee on August 23. Consequently, a majority of the Board was not kept abreast of the information known to the Audit and Executive Committees as the investigation unfolded. Finally, Dr. Ladner himself was quite critical of the motivations of individual Board members, the qualifications of some of those conducting the investigation, and the fairness and adequacy of the investigative process. Nonetheless, based on the recommendations of the Audit Committee, the Executive Committee, on August 23, suspended Dr. Ladner from office as the 2005-06 academic year began. .

The Audit Committee submitted its report to the full Board on September 12. After hearing that report, the Board allowed Dr. Ladner and his counsel to make a rebuttal. The Board determined that Dr. Ladner had raised certain questions that should be considered further by the Committee, and the Board requested that the Audit Committee review certain of its conclusions. The Audit Committee conducted further review and made minor modifications to its initial findings and recommendations.

Subsequently, the full Board met and took action. On October 10, the Board adopted the Audit Committee's recommendations without modification, to report to the IRS additional imputed income for Dr. Ladner and to require Dr. Ladner to reimburse the University, with interest, for personal expenses paid for with University funds. In doing so, the Board rejected the legal and other arguments advanced by Dr. Ladner and his advisers to support most of his expenses.

The Board also decided at this meeting that Dr. Ladner would not be restored to active status as President and that the sole remaining issue was how Dr. Ladner's employment would be terminated – would he resign or would the Board terminate his employment with or without cause. The University prepared and filed with the IRS amended Forms W-2 and 990, reflecting the imputed income, and issued a demand for reimbursement to Dr. Ladner, both over the strenuous objections of Dr. Ladner and his counsel, including threats of lawsuits. In short, the Board made an appropriate – though very tough – set of governance decisions which balanced Dr. Ladner's rights and the need for decisive action in light of the Audit Committee's findings. In doing so, the Board demonstrated the seriousness with which it carried out its fiduciary duties with respect to the allegations of expense abuse by the President.

IV. The Settlement Terminating Dr. Ladner's Presidency and Eliminating Potential Major Litigation.

The Board further determined at its October 10 meeting that the remaining question of how Dr. Ladner would leave the University's employ should be resolved promptly, and authorized three Board members to negotiate this issue with Dr. Ladner.

On October 20, the Board received, and with some modification approved, the recommendation of its negotiating committee as to how to proceed. Essentially, the negotiators reported that they and Dr. Ladner were far apart in terms of reaching a settlement. They were concerned that negotiations might drag on for some time without any assurance of reaching a resolution. Consequently, they recommended that the Board authorize them to present a "final and best offer" on a "take it or leave it" basis to Dr. Ladner.

In approving this strategy, the Board was aware of the potential for major litigation by Dr. Ladner if he was simply dismissed from University employment. The validity of the 1997 contract was open to legal dispute. While it had not been ratified formally by the Board, the 1997 contract had been executed by the Board Chair, and Dr. Ladner would argue that the Board Chair had apparent authority to enter into such a contract. In weighing the risks of litigation, the Board was aware that its former Board Chair, a distinguished businessman, would likely appear as a witness supporting Dr. Ladner's position that the 1997 contract was valid. The record was mixed as to the extent that other trustees were aware of the contract's existence, and, as Dr. Ladner argued, the 1997 contract had been honored in fact since it was signed in 1997.

If the 1997 contract were held valid, the Board could terminate Dr. Ladner "for cause" only if he engaged in dishonesty or fraud. Dr. Ladner contended that the vast majority of the personal expenses questioned by the Board were for the University's benefit or were clearly authorized by his 1997 contract. At the very least, the ambiguous terms of the 1997 contract, and the fact that some University officials and perhaps some members of the Board were aware of many of the Ladners' spending practices, made proving dishonesty or fraud far from certain. Moreover, if the contract were held valid and cause for termination was not supported, Dr. Ladner would be entitled to damages based on contractual rights, including larger severance payments and lifetime employment as a fully tenured professor at a salary equal to 120% of the next-highest paid University professor.

In short, speaking at least for ourselves and, we believe, many trustees, litigation reasonably seemed inevitable in the absence of an agreed settlement. While the University would have strong legal arguments in its defense, and perhaps the better of the arguments, the Board had no assurance that the University would ultimately prevail. If his lawsuit eventually settled, as most legal disputes do, there would presumably be some monetary settlement with each side bearing its own legal costs. If the case were tried to judgment and went through appeals, there was a risk of loss which could not be ignored, and, even if the University ultimately prevailed, the legal cost could have exceeded $1 million, based on the likely discovery and motions practice which would have been pursued. Litigation would have kept the controversy over Dr. Ladner's contract and expenses alive, requiring University personnel and trustees to devote considerable attention to it, resulting in significant non-monetary costs of disruption and distraction from normal University functions.

Notwithstanding the risks to the University associated with litigation, the Board was not willing to pay whatever Dr. Ladner might demand to reach a prompt resolution. As noted, the negotiators had reported that Dr. Ladner and they were far apart on the terms of any settlement. The Board accepted the advice of its negotiators to decide on the "final and best" offer it felt appropriate to make to Dr. Ladner. If that offer was not accepted, the Board determined that it would end the negotiations, accept the attendant risks and costs of litigation, and terminate Dr. Ladner based on the Board's determination that the 1997 contract was not valid, and that he be dismissed for cause if the contract were deemed valid. Basically, the Board said to Dr. Ladner, "enough negotiation, your demands are unacceptable, here is the best offer the University will make, and, if it is unacceptable to you, you are hereby terminated."

The Board accepted the recommendation of their negotiators that, as part of its separation offer, it allow Dr. Ladner to retain approximately $2.75 million in deferred compensation previously awarded to Dr. Ladner, set aside for him in trusts and insurance products, and funded in prior years based on his performance and the University's achievements under his leadership. While the University contended that these amounts had not vested (a fact disputed by Dr. Ladner), the Board concluded that Dr. Ladner was due some consideration for the progress the University had made during his eleven year tenure and that allowing him to keep previously awarded and funded deferred compensation was both fair and appropriate.

The negotiators also recommended offering a one-time settlement payment to Dr. Ladner. The Board, after much discussion, settled on a payment of $950,000. It was recognized that income taxes not only on that amount, but on the additional imputed income, would be withheld, as would the reimbursement determined by the Board, based on the Audit Committee's investigation, to be due the University. As a consequence, Dr. Ladner would actually receive and retain a relatively small amount of this payment.

Apart from a modest allowance for actual moving expenses up to a maximum of $20,000 and one final payment ($103,000) due on his split dollar life insurance policy, no other consideration was offered to Dr. Ladner. In return, he was to resign all University appointments immediately and give up and release all claims he might have under the 1997 contract or otherwise against the University, including any claim to continued employment as a tenured professor. Dr. Ladner was responsible for his own substantial attorneys' fees.

On October 24, Dr. Ladner accepted the take-it-or-leave-it proposal presented to him by the Board, and submitted his resignation effective immediately. In paying him the amounts offered, the Board spared the University almost certain contentious, costly and uncertain litigation, and ended any prospect of Dr. Ladner's returning in any capacity to the University.

V. <u>Steps Toward Better Governance of the Office of President.</u>

In the wake of the public controversy surrounding the departure of Dr. Ladner, the Board, with input from the entire University community, has begun a comprehensive review of the University's governance processes, a review that will focus on greater transparency and accountability. (As an example of such transparency, we will post a copy of this letter on the University's website.) This intensive review will include consulting with outside experts and discussion with the University's many constituencies. The Board is committed to learning from, and responding to, the lessons of the Ladner episode, and to refocus the University on its educational mission.

To this end, the Board has undertaken to develop a new Board policy (AUSF 010462) to establish appropriate procedures for entering into contracts with future presidents. Any such contract must be reviewed and voted upon by the whole Board, and we believe should be subject to a process that ensures rigorous oversight, including review by lawyers, compensation experts and contracting professionals. We anticipate that this policy will be voted upon, with whatever amendments are deemed necessary, at the February 2006 Board meeting.

Similarly, the Board has also determined, through its Audit Committee, to have much more regular and robust processes relating to the review of expenses of University officers, including the President. The Audit Committee adopted these processes at its November 11 meeting.

Finally, the Board is also considering, and expects to adopt, an enhanced conflict of interest policy for itself and the University. A copy of the current draft of that policy is also being provided to the Committee, along with the previous version of the conflict of interest policy. (AUSF 009280-009283, 009286.)

These newly revised proposed policies and processes are among many steps that the University will likely consider in consultation with the University community to enhance greater transparency and inclusiveness in its governance practices.

Conclusion

This narrative response is intended to assist the Committee in any consideration it gives to these events at American University. We certainly recognize that the Board's past practices were deficient in the respects noted above, and we have acknowledged that to the University community. Certainly, the Board has recognized that it must improve its governance in these areas and is committed to doing so. While we greatly regret the negative publicity the Ladner situation has generated, and the distraction it has caused on and off campus from the University's educational mission, we believe that some good will follow, not only by reason of improved governance and controls at AU, but because our experience may prompt other university and college governing boards to assure themselves that they are exercising proper oversight over such matters as presidential compensation and expense reimbursement.

As the Committee's staff is aware, the University has retained Stephen M. Ryan, Esq., to assist it in responding to your inquiries. Mr. Ryan is coordinating the University's document production and responses to your letter. Any specific questions the staff may have regarding the University's position or production can be addressed to Mr. Ryan, who will respond promptly to such matters.

In closing, we observe that the foregoing narrative reflects our present understanding and impressions, and is based on information we have been provided by others in some instances. While we have no reason to doubt the accuracy of this information, not all of it is based on our personal knowledge. We should also point out that as you would expect with a volunteer board comprised of 23 individuals, our views and characterizations would not necessarily be shared in all instances by every trustee. We have provided you with our own impressions and understanding recognizing that some trustees might have perspectives which may differ to some degree from our own.

Sincerely,

Gary M. Abramson
Chairman
Board of Trustees

Thomas A. Gottschalk
Vice Chairman
Board of Trustees