MEMORANDUM

PRIVILEGED AND CONFIDENTIAL
ATTORNEY-CLIENT COMMUNICATION

TO: Board of Trustees

FROM: Gita P. Bolt
General Counsel

DATE: April 8, 2013

RE: Directors and Officers (D&O) Liability Insurance Arrangements

At its most basic, D&O insurance protects directors and officers from liability arising from actions connected to their corporate positions. This memorandum seeks to provide a brief summary of the University’s D&O coverage as applicable to the Board of Trustees.

Indemnification and The Bylaws

Indemnification means a legally enforceable assurance that one person (in this instance the University) promises to protect another (a member of the Board) against liability arising out of the legal consequences of the trustee’s failure to act.

The Bylaws provide that the University shall indemnify and hold harmless any person who was or is a party or is threatened to make a party to any action, suit or proceeding,... by reason of the fact that he is or was a trustee... against expenses (including attorneys’ fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the Corporation... and with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful...Bylaws Article XIV.

However, there are preconditions. You are indemnified only if:

1) Action brought against you by reason of the fact that you are a trustee, i.e., your actions taken in your capacity as a trustee.

2) You acted in good faith and in a manner you reasonably believed was consistent with the best interest of the University.

3) In criminal proceedings, you had no reason to believe your conduct was unlawful.

4) You did not receive an improper personal benefit from your actions.

Insurance

Consistent with the Bylaws, the University has D&O insurance with United Educators Insurance, a Reciprocal Risk Retention Group (“UE”). The policy defines “individual insureds” as “past, present and future trustees, directors or officers..., while acting within the
scope of their duties or obligations.” In addition, “the spouses or domestic partners of directors or trustees (but only to the extent they are involved in claims solely because of their status as spouses or domestic partners of directors or trustees)” and “their estates, heirs, legal representatives or assigns” are considered “insureds.”

Some examples of UE insurance policy coverage are the following:

- Complaints filed with the Equal Employment Opportunity Commission or state civil rights agencies
- Emotional distress arising out of wrongful employment practices
- Mental injury or emotional distress coverage for non-insured third parties arising out of sexual harassment or unlawful discrimination
- Attorneys’ fees awarded pursuant to state statute
- Prejudgment and post-judgment interest

Under the policy covered claims are subject to a $25 million limit per claim, subject to a pre-claim deductible of $150,000, and $25 million annual aggregate. For claims of wrongful employment practices, the University has a $150,000 self-insured retention, and $1,000 self-insured deductible for Governing Board Directors, Trustees or Officers, who cannot be lawfully indemnified-per claim.

Notice
UE requires that as a condition precedent, the University provide written notice of any claim as soon as reasonably practicable and promptly and with such information as may be required.

Exclusions
Coverage is not provided for prior and/or pending litigation; cases where there was intent to harm or injure; bodily injury or death of any person; mental injury or emotional distress; assault or battery; pollution; insured versus insured; failure to perform professional services; breach of contract outside directorship liability; punitive damages awards; violations of federal security or perjury laws; and claims under the Fair Labor Standards Act.

Liability of Board Members
All corporate trustees are afforded standard protection against liability under the “business judgment rule.” The business judgment rule limits court review of board member’s actions. In making a business decision, trustees are presumed to act on an informed basis, in good faith, and in the honest belief that the actions taken are in the best interest of the University. The business judgment rule protects board members against liability for honest mistakes in judgment, but not for breaches of fiduciary duty occasioned by fraud, gross negligence, or illegal conduct.

There is a Fifth Circuit case that confirms a finding of no liability by board members. However, there are specific circumstances where a board member of a non-profit could be
liable and the Louisiana Supreme Court established a cause of action under the statute in RS 12:226 and RS 12:219.

In 1988, the Fifth Circuit established the standard of care expected by corporate officers and directors, which expressly states that directors/board members are not liable for mere errors of judgment on their part where they act in good faith. They are only required to exercise reasonable care and diligence and act in good faith. They are liable for willful neglect of duty, gross negligence or their fraudulent breach of trust. *Louisiana World Exposition v. Federal Ins. Co.*, 858 F.2d 233, 237-38 (1988).

The Louisiana Supreme Court further examines the issue and creates a cause of action in *Mary v. Lupin Foundation*, 609 So.2d 184, 190 La., 1992. It establishes that RS 12:219 imposes a liability for breach of duty. However, board members may only be held directly liable for receipt of unlawful distributions when the distributions resulted from formal corporate action by the members. *Id.* In order to impose liability, these five elements of RS 12:226 must be established: (1) an “unlawful distribution, payment or return;” (2) of “assets;” (3) to the “members;” (4) resulting from a “vote” in favor thereof by the directors; (5) which vote was done “without the exercise of reasonable care and inquiry.” *Id.* at 189.

In 2006, a magistrate judge in the W.D.La. approved a 12(b)(6) dismissal motion of a non-profit corporation in *Hammond v. St. Francis Medical Ctr.*, making this statement: “The statutes and jurisprudence are clear that shareholders or members in either profit or non-profit corporations are not responsible for the debts of the corporation.” This was not reported in F.Supp.2d, 2006 WL 1675407 but is a 12(b)(6) dismissal motion and made public by *Financial Acquisition Partners, L.P. v. Blackwell*, 440 F.3d 278, 286 (5th Cir.2006). This decision was positively cited in 2007 and 2009 decisions.

If I may be of further assistance, please feel free to contact me.