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General Counsel As Persuasive Counselors

How A Law Firm Can Assist General Counsel In Their Enhanced Role

The Editor interviews ***Thomas Wardell****, Partner, McKenna Long & Aldridge LLP.*

Editor: Please tell our readers about your background.

Wardell: I attended Harvard Law School and began my career at Mayer Brown in Chicago. At that time the firm only had offices in Chicago and Paris. From there, I went to Sullivan & Worcester in Boston. I practiced there for many years. I had a stint as a CEO of a $250 million privately held company which served as a system's house. We sold that company and I moved to Atlanta where I wound up working for McKenna Long & Aldridge.

I have always been a corporate finance lawyer. That is why I went to law school. I was fascinated by the idea of working with all the components of a corporate transaction. My entire career has been spent working with in-house counsel and their clients, typically with larger public companies, but not always.

During the time I spent as a CEO, I had daily interaction with the general counsel and frequent interaction with our law firms. Because I came from a legal background, I had a greater involvement in selecting and working with lawyers than might be true of other CEOs.

Editor: Are you seeing situations among your clients where general counsel act as persuasive counselors?

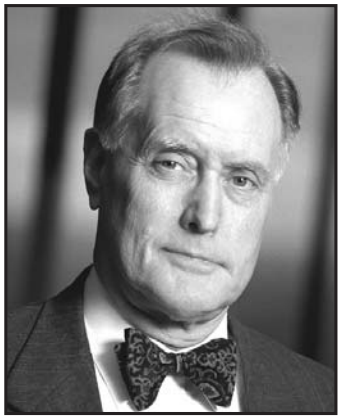
Wardell: Yes. It is an important function. The law has not changed in many ways. Some of the mandates for majority independent directors are new, not that they were not in some respects a best practice in the past. However, the history of the recent past has led directors to take their responsibilities to shareholders much more seriously.

What is different now is that globalization has made keeping the corporate machine smoothly moving in a compliance mode between the noncompliance ditches a much more difficult enterprise. Today, discharging the duties of a director is a very time consuming task. They need access to all the expertise that they can get and particularly that of the general counsel . This means that the role of the in-house lawyer is a bigger one with greater demands and expectations. The lawyers need to keep people apprised on a regular basis of the legal and governance exposures, which is no small task.

The various scandals, Sarbanes-Oxley and the various pronouncements coming out of Delaware have emphasized the need for diligence on the part of the independent directors.

The Tech Boom crash taught a painful lesson to directors who were not paying close attention to what was going on in the business. That lesson has been reinforced by the bitter experience of present day scandals. After the backdating scandals, people again are asking "Where were the lawyers?"

Editor: Does your firm include experts on questions relating to the conduct of board and board committee meetings, preparation of minutes and otherwise documenting the due diligence of the directors?



Thomas Wardell

Wardell: We find ourselves regularly invited by clients to attend board meetings. We are asked directly by directors or by the general counsel about best governance practices. We field such questions as "How complete should the treatment in the minutes of a particular agenda be? or "Should the discussion of a particular topic be carried over to another meeting?" Directors welcome our presence at board and board committee meetings and our help in finding ways to document their diligence. You become one of them, someone who is perceived as the outsider and independent person who is there to perfect and validate the processes they follow and to provide expert guidance.

With respect to the general counsel, while it is true that boards are more diligent now, it is not true that all of them are. It is sometimes necessary for the general counsel to say that there needs to be another meeting to thoroughly establish that the board has exercised the necessary care. That is not always something that people want to hear. The role of the outside counsel in that situation is to buttress the position of the general counsel.

Editor: Does your firm assist the general counsel in the indoctrination of directors and in answering questions of directors with respect to avoidance of personal liability and the adequacy of D&O insurance and indemnification?

Wardell: We do. It comes in a number of forms. There is a cluster of companies for which we do annual director education. I tailor to each company's needs a course that takes place in the middle of proxy season where I deal with the current and most important issues relevant to that company. I can include coverage of issues such as those you mentioned having to do with director liability at those sessions or in separate sessions, including sessions with individual directors. I recently provided training for a foreign company that just opened a large operation in this country. One of the issues it asked me to cover was how to insulate the parent and its U.S. subsidiary from the liabilities of the other. This reflects the concern that many foreign companies have about our litigation climate. Where companies invite us to attend their board meetings, we are frequently asked to address governance questions that come up in the course of the meetings.

Editor: Are boards expressing a high level of concern about personal liability growing out of securities class action litigation?

Wardell: Exposure to litigation is a constant concern. Most of the boards that I am working with are made up of very capable and mature people. They usually frame the question in a slightly different way. They ask whether they have exercised the time, care and diligence necessary to discharge their responsibilities. They are much more focused on their obligation to the shareholders than on their concern for their own liability.

Editor: Many companies have gotten into trouble because of accounting issues, such as those involved in the recent backdating scandals. Does your firm have lawyers who are well versed in law and accounting issues?

Wardell: The lawyers in our corporate area begin their training with financial statements and develop an understanding of what is involved in creating the footnotes and what the accounting standards are for such things as "materiality" and how they differ from the legal standards. Within the corporate finance group we begin with the premise that due diligence begins with the financial statements and that everything keys off of them. They provide a roadmap of what you should expect to find. If you start to find things that are not reflected in the financials, you need to know why. We do get called upon to challenge the auditors and push them on their explanation and sometimes to back them up vis-à-vis our clients.

Editor: Do you or your firm have the tax and other expertise required to analyze the effects of complex transactions?

Wardell: I used to be a tax lawyer so consequently I am always the facilitator and interpreter in those situations. Last week a question came up as to how to reflect a potential patent dispute in the footnotes to the financials. We have the expertise required to assure that the proper disclosure is made. It doesn't make economic sense for most corporate legal departments to hire in-house experts to provide such advice

Editor: Is your firm available to act for boards of directors, audit committees and special investigation committees of the board where there is a need for independent counsel? What is your relationship to the general counsel under such circumstances?

Wardell: The kinds of independent counsel relationships in which we become involved come in a number of forms.

One is the independent counsel relationship that relates to a particular transaction or circumstance and is designed to avoid any taint of any external influence in reaching a decision. For example, where one of the major stockholders of a company that is considering a going private transaction is a participant in the buyout group. Because there is an inherent conflict, the best practice is to appoint a special committee of independent directors that in turn appoints special counsel that is independent.

Another category of independent counsel relationship involves an ongoing representation by independent counsel of the audit or other board committee or even the independent directors. In one case, we serve as independent counsel to the independent directors. Typically, the audit committee or the independent directors may want to use a firm that one or more directors have reason to trust.

In other situations, an issue may involve too many people inside the company, including directors, wearing too many hats. Therefore independent counsel may be selected to serve a special committee that has been appointed to sort out the issue. This can come up in a corporate opportunity situation. Should the company pursue the opportunity or not?

Finally, there is another cluster of independent counsel relationships which center around investigations. If it is a situation where you have the government involved, it can have the added overlay of having the government's own standards with respect to fraud and abuse and disclosure come up. That shows up in the defense and health industries. We do that kind of investigation commonly. There are times when an internal investigation is one which must be conducted by a law firm that has always been independent of the company and will be for the future after the investigation is completed in order to provide absolute protection for everyone – the company, management, directors and shareholders – from any suggestion that all the facts were not gathered and then carefully and fully developed.

In-house counsel's role in selecting independent counsel really depends on their relationship to the problem. If you are talking about a situation in which a company is considering getting independent counsel for the work of a committee or the independent directors, then it is very likely that general counsel will be involved. If you are talking about a problem that will require an investigation and which either directly or remotely implicates a failure on the part of the general counsel's office, then our experience suggests that we will usually end up being selected by an independent director or a committee of independent directors. The general counsel may have some input into the roster of firms that directors may look at, but the selection process will be conducted by the directors themselves.