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Best Practices in Corporate Governance When Lawyers Serve on Boards

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Introduction

At one point, it was not uncommon for lawyers to serve on boards of directors – especially on the boards of corporate clients of their law firms. Over time, however, the legal profession has frowned upon lawyers serving as directors. Opponents of lawyer-directors strongly feel that the potential conflicts and pitfalls outweigh the benefits of having a lawyer serve on a board. While the potential conflicts are serious and should be carefully considered and analyzed, a blanket prohibition on lawyers serving on boards has not yet been adopted.

Some studies have suggested that companies are hiring an increasing number of lawyers to serve on their boards. A Cornell Law School research study published on January 1, 2014[2], finds that, although lawyers still do not regularly serve on boards, the number of lawyer-directors serving on boards has nearly doubled from 2000 to 2009.[3] Along with various other material benefits, the study credits lawyer-directors with having a positive impact on litigation management, the alignment of executive compensation with shareholder interests, and the reduction of incentives on excessive risk taking.[4]

Despite some of the potential benefits of having lawyer-directors, companies, boards, lawyers, and law firms should exercise caution when considering having a lawyer serve on a board. There are a number of ethical concerns that a lawyer wearing both the "lawyer hat" and "director hat" should consider. A few of these potential concerns include the applicability of the attorney-client privilege, conflicts of interest, and the lawyer's potential lack of financial acumen and industry experience.

Although commentators have argued for a blanket prohibition of lawyers serving on the board of directors of a corporation that his or her firm represents as counsel, the American Bar Association's Model Rules of Professional Conduct contains no such prohibition. Rather, the Model Rules of Professional Conduct provide the following guidance in Paragraph 35 of the Comments to Rule 1.7:

> "A lawyer for a corporation or other organization who is also a member of its board of directors should determine whether the responsibilities of the two roles may conflict. The lawyer may be called on to advise the corporation in matters involving actions of the

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[1] Submitted by Neel Lemon, Baker Botts LLP, Dallas, Texas, and Steven M. Haas, Hunton Andrews Kurth LLP, Richmond, Virginia. Grateful appreciation to Sumair Sangha, Baker Botts LLP, Dallas, Texas, for his outstanding assistance in the preparation of these materials.

[2] Litov, Lubomir P.; Sepe, Simone M.; and Whitehead, Charles K., "Lawyers and Fools: Lawyer-Directors in Public Corporations" (2014). *Cornell Law Faculty Publications*. Paper 673.

[3] *Id.*

[4] *Id.*

directors. Consideration should be given to the frequency with which such situations may arise, the potential intensity of the conflict, the effect of the lawyer's resignation from the board and the possibility of the corporation's obtaining legal advice from another lawyer in such situations. If there is material risk that the dual role will compromise the lawyer's independence of professional judgment, the lawyer should not serve as a director or should cease to act as the corporation's lawyer when conflicts of interest arise. The lawyer should advise the other members of the board that in some circumstances matters discussed at board meetings while the lawyer is present in the capacity of director might not be protected by the attorney-client privilege and that conflict of interest considerations might require the lawyer's recusal as a director or might require the lawyer and the lawyer's firm to decline representation of the corporation in a matter."[5]

This paper begins with a discussion of the various benefits associated with having a lawyer serve on a company's board. Thereafter, this paper will discuss some of the potential challenges lawyers will face in that dual role. Finally, this paper will summarize the potential ways lawyers can mitigate the risk of board service and some "best practices" for lawyers to follow when they are considering taking on this dual role.

Benefits of Lawyer-Directors

There are many perceived benefits to having a lawyer-director serve on a company's board. Experienced lawyers can bring years of training and experience that otherwise may be missing from a company's board. Lawyer-directors can provide a different perspective to the board room which can enhance the board's deliberations and improve the quality of the decision-making process. Within any decision-making body, a diverse set of opinions and perspectives can be helpful to reaching an informed decision. Where boards comprised solely of like-minded "business" people may be well suited to making purely business decisions for a company, adding a lawyer to the board of directors can fill the gap that otherwise exists for risk management and attention to detail. A lawyer-director will often bring with him or her an emphasis on doing things "by the book."[6] This adherence to process and attention to detail can be a valuable addition to any company's board.

A lawyer-director can use his or her experience and judgment to implement procedures that can enhance the board's monitoring function. An important function of a company's board of directors is to monitor CEO performance and set executive compensation levels. Many companies have turned to incentive-based compensation schemes for top executives in an attempt to better align the interests of managers with shareholders. These financial incentives often reward managers for taking on additional risk and can motivate executives to focus on short-term gains rather than creating long-term value for shareholders. Having a lawyer-director present can assist the board in monitoring executive performance and creating executive compensation plans that align management and shareholder interests and promote long-term growth for a company's shareholders. The Cornell research study finds that the "presence of a lawyer-director is associated

[5] American Bar Association, Model Rules of Professional Conduct, Comment 35 on Rule 1.7.
[6] *See* supra note 2.

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