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Simone van Ommeren-Akelman

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INTRODUCTION

On March 12, 2019, Operation Varsity Blues and the corresponding charges were made public.[2] The investigation, spearheaded by United States federal prosecutors, revealed the largest-ever college admissions bribery scheme.[3] The investigation drew public attention not only because the scandal included several celebrities, but also because it shined a light on money and the influence it has on college admissions.[4]

In brief, the scandal involved manipulating the college admissions process to improve admission chances for weaker students with a lot of parental resources. Central to the scheme was Rick Singer, the mastermind behind the operation.[5] One favored strategy was to rig admissions tests, where Singer would either coerce the proctor into allowing students more time on the SAT or ACT, or even specially place proctors in the exam room that would interfere with exam results.[6] Another was to bribe athletic

1. Simone van Ommeren-Akelman, Juris Doctor, University of California, Hastings College of the Law, 2020; B.A. in Political Science with an Emphasis in American Politics and a Minor in English, University of California, Davis, 2017. To my mom and dad, who taught me the definition of tenacity through their own actions and instilled in me the value of education. To Kylee Cecchini and Athena Kautsch, who have served as life-long role models in their advocacy for justice and their promotion of youth voices. To Malwine van Ommeren, who has made a lifetime of sacrifices to afford me the opportunity of pursuing my dreams. And finally, to Rory Houghton-Berry, who has never wavered in his belief in me and inspires me simply by the nature of his being. *Fiat Lux*. *Fiat Justitia*.

2. Graham Kates, *Lori Loughlin and Felicity Huffman among dozens charged in college bribery scheme*, CBS NEWS (Mar. 12, 2019, 8:35 PM), https://www.cbsnews.com/news/college-admissions-scandal-bribery-cheating-today-felicity-huffman-arrested-fbi-2019-03-12/ [https://perma.cc/N8H7-646L].

3. Maria Puente & Joey Garrison, *Felicity Huffman released on bail after allegedly bribing to get kid into college as part of sweeping admissions scandal*, USA TODAY (Mar. 12, 2019, 10:57 AM), https://www.usatoday.com/story/life/2019/03/12/felicity-huffman-lori-loughlin-indicted-admissions-bribery-case-reports/3139204002/ [https://perma.cc/43U2-7PJB].

4. *Id.*

5. *Id*.

6. *Id.*

coaches. Singer would doctor photos and create athletic profiles for students who were by no means athletes, and thereby used the "side-door" of athletic recruiting.[7] An essential component of Rick Singer's scheme was complicit administrative members of the United States' top universities. There is clearly room for significant oversight in the admissions process, but these schools currently benefit too much from wealthy parents to enforce such oversight from their own initiative.

If a scandal such as Varsity Blues were to happen in a corporate environment, alarm bells would sound. Shareholders would file derivative suits, attempting to pierce the corporate veil. The news would be reporting on the violations of fiduciary duties and inherent corruption. When Elon Musk tweeted misleading information about taking Tesla private, the media immediately jumped on the opportunity to hold Musk accountable for his actions within the company.[8] The same standards of responsibility are not replicated in Varsity Blues—both because there is a gap in the application of fiduciary duties to non-profit organizations, and because there is arguably too much latitude in the college admissions process.

It is only recently that public corporations have been expected by law to maintain oversight over their companies. In a 1996 opinion, the Supreme Court ruled that directors are potentially liable for a breach of duty to exercise appropriate attention if they knew or should have known that employees were violating the law, declined to make a good faith effort to prevent the violation, and the lack of action was the proximate cause of damages.[9] The *Caremark* precedent, however, only applies to public corporations and their respective boards of trustees. The universities in Varsity Blues have benefitted from the law not yet broadening the fiduciary net to encompass non-profits as well. Otherwise, court precedent would point to the various Boards of Trustees having violated fiduciary duties by turning a blind eye to the practice of bribing for college admission. Thus, there seems to be a drastic need to address the lack of fiduciary duties in both non-profit governance and by extension, as well as university governance.

With this background, the present article analyzes the potential extension of *Caremark* to non-profits, with a special focus on the university organizational form that was at issue in the Varsity Blues scandal. While Varsity Blues has returned this issue to prominence, scholars and lawyers have long been concerned with non-profit governance. This Note will use that research to examine whether the *Caremark* duty of oversight can be

7. *Id.*

8. Alan Ohnsman, *Elon Musks' Bombshell Tweets About Taking Tesla Private Trigger SEC Review*, FORBES (Aug. 8, 2018, 5:22 PM), https://www.forbes.com/sites/alanohnsman/2018/08/08/elon-musks-bombshell-tweets-about-taking-tesla-private-said-to-trigger-sec-review/#61e344c0c37b [https://perma.cc/P3TE-Y54E].

9. *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967 (1996).

extended to boards of trustees, and if so, how responsibility can be imposed on directors to exercise their fiduciary duties. Part I examines the structure of the corporate university and the variety in the structure of boards. Part II analyzes the current fiduciary duties of Boards of Trustees as well as the overlay of the business judgment rule and standing of potential claimants. Part III presents an overview of the application of law as applied to the Varsity Blues scandal and provides a possible resolution for the lack of oversight through the imposition of liability or through the incentivization of ethical gatekeepers, while offering countering views as to why such strategies have yet to be applied. Part V concludes.

THE STRUCTURE OF THE CORPORATE UNIVERSITY

The Creation of the Parallel Worlds of Corporate Evolution and University Evolution

While there are many differences between corporations and universities, the similarities between the two allow universities to be considered under the umbrella of corporate law. The foundation of American corporate law was incidentally decided in a lawsuit where a private college prevailed in protecting its corporate charter from state control.[10] In 1819, New Hampshire wanted to take control of a private college–Dartmouth–and felt justified in doing so because they supported Dartmouth through chartering and support.[11] The Supreme Court held that the New Hampshire state legislature's efforts to seize Dartmouth College were illegal, thereby rendering the charter imposed by King George valid.[12] In essence, upholding the original charter meant that the court recognized it as a contract. In the case, Chief Justice Marshall recognized that a corporation is "an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creation of law, it poses only those properties which the charter of its creation confers upon it, either expressly, or as incidental to its very existence."[13] Through his opinion, Chief Justice Marshall reaffirmed the importance of contracts under the US Constitution as "it … play[ed] a key role in the rise of the American business corporation."[14] Thus, through the limitation of state control of private institutions, the deference to the university charter was born.

Accordingly, private universities were able to create their own methods of governance through their charters. The organization of

10. Trs. of Dartmouth Coll. v. Woodward, 17 U.S. 518, 524 (1819).
11. *Id.*
12. *Id.* at 636.
13. *Id.*
14. R. Kent Newmyer, *John Marshall as a Transitional Jurist: Dartmouth College v. Woodward and the Limits of Omniscient Judging*, 32 CON. L. REV. 1665, 1666 (2000).

universities is typically described rather simply: a board of trustees receives a charter from the state, selects a president, and approves a faculty to teach and to select the students.[15] However, this simplicity is a façade.[16] "Organizationally the university is . . . one of the most complex structures in modern society; it is also increasingly archaic. It is complex because its formal structure does not describe either actual power or responsibilities; it is archaic because the functions it must perform are not and cannot be discharged through the formal structure provided in its charter."[17]

The Lack of Formalized Rules and Standards for the Behavior of Trustees

In addition to the lack of formalized structure, the duties of a trustee have never been standardized and enforced. Louis Heilbron, the first chair of the Board of Trustees of the California State Colleges (now universities), tried to capture the essence of the duty of a trustee when he said, "The key part of the trustee's title is (or should be) the word *trust*. He holds something valuable in trust – the classrooms, the libraries . . . the institution itself – for high purposes and benefits, not for himself, but for others."[18] The precise discernment of duties, however, is still a substantially gray area. "Unlike the for-profit corporate boards, whose main objective is to increase shareholder value, the mission-based nonprofit universities must satisfy different sets of constituencies, including students, employees, alumni, donors, public officials, and society at large."[19]

With a universal objective not clearly codified, the role of the trustee is open ended, rendering liability for improper acts virtually impossible. The following duties, at a minimum, have been identified but not codified:

Protecting the welfare of the individual institution and its missions;[20]

Protecting the institution autonomy from external economic and political forces;[21]

Protecting the academic freedom of the institution's members;[22]

15. JAMES A. PERKINS, THE UNIVERSITY AS AN ORGANIZATION 3 (1973).

16. *Id.*

17. *Id.*

18. LOUIS HEILBRON, THE COLLEGE AND UNIVERSITY TRUSTEE: A VIEW FROM THE BOARD ROOM 3 (1973).

19. Salar Ghahramani, *Fiduciary Duty and the Ex Officio Conundrum in Corporate Governance: The Troublesome Murkiness of the Gubernatorial Trustee's Obligations*, 10 HASTINGS BUS. L.J. 1, 8 (2014).

20. CLARK KERR & MARION GRADE, THE GUARDIANS: BOARDS OF TRUSTEES OF AMERICAN COLLEGES AND UNIVERSITIES 12 (1989).

21. *Id.*

22. *Id.*

Ensuring adequate resources;[23] and
Considering the public welfare.[24]

These points are not exhaustive; they merely encapsulate what is the bare minimum norm of an existing Board of Trustees. Each university has their own objectives, and are tasked with the endeavor of confronting, defining, and tackling each problem. "For instance, should the board's performance be based on evaluating teaching effectiveness? Enrollments? Enhanced educational quality? Reputation? Revenue? Research and innovation? Accessibility? Societal impact? The fact that these criteria may at times be competing objectives can complicate the evaluation of the board's performance."[25]

THE REGULATION OF BOARDS OF TRUSTEES

While university trustees are now considered fiduciaries, that hasn't always been the case. This section will examine the origins and extension of fiduciary duties, and how they came to be applied to university boards of trustees.

Overview

A fiduciary is one who "often [is] in a position of authority who obligates himself or herself to act on behalf of another (as in managing money or property) and assumes a duty to act in good faith and with care, candor, and loyalty in fulfilling the obligation."[26] The need for a fiduciary relationship between members directing any type of organization has been well recognized, even before the creation of the United States Constitution.[27] As such, the responsibilities of a fiduciary are well established in the law.

One of the cornerstones of fiduciary law within the United States was created in *Meinhard v. Salmon*.[28] The court held, in application to a joint real estate venture where one partner took advantage of the financial benefits of the partnership, that the co-venturers had a fiduciary duty to each other.[29] Judge Cardozo wrote, "Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those

23. RICHARD T. INGRAM, GOVERNING PUBLIC COLLEGES AND UNIVERSITIES: A HANDBOOK FOR TRUSTEES, CHIEF EXECUTIVES, AND OTHER CAMPUS LEADERS 93, 102 (Richard T. Ingram ed., 1993).
24. Kerr & Grade, *supra* note 20.
25. Ghahramani, *supra* note 19, at 9.
26. *Fiduciary*, MERRIAM-WEBSTER LEGAL DICTIONARY (11th ed. 2019).
27. Evan J. Criddle, *Fiduciary Foundations of Administrative Law*, 54 UCLA L. REV. 117, 123-24 (2006).
28. Meinhard v. Salmon, 164 N.E. 545, 546 (1928).
29. *Id*.

bound by fiduciary ties. A trustee is held to something stricter than the morals of the marketplace. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate . . ."[30]

Fiduciary relationships have expanded in application, and now even include relationships between "a trustee and beneficiary, a guardian and ward, an agent and principal, a lawyer and client, a member of the clergy and a parishioner, a director and a corporation, a partner and other partners, an employer and an employee, and a broker and client."[31] As a result, the fiduciary duties have multiplied and grown in murkiness, as they now apply to a sea of relationships.[32]

While rooted in concepts such as good faith, trust, and confidence, the duties that courts have categorized under the rubric of fiduciary duty are many and varied, and are often described in very lofty terms. These duties include the duty not to commit fraud, not to engage in self-dealing, to be loyal, obedient, diligent, and exercise good faith, to disclose material information and to exercise care and prudence, among others.[33]

Fiduciary Obligations of Non-Profit Organizations and Universities

Historically, however, courts have struggled to articulate the fiduciary expectations of directors and officers of non-profit organizations.[34] The roots of nonprofit corporate law began at the intersection of trust law and corporate law,[35] but through the counsel of the American Bar Association and the American Law Institute, as well as state imposed regulation, charitable corporate law and charitable trusts began to take two separate paths.[36]

The final separation of corporate law and trust law occurred in *Oberly v. Kirby*, where the court recognized both parallels and distinguishing factors between for-profit corporations and non-profit corporations. In this case, the Supreme Court of Delaware found that the fiduciary duty of a

30. *Id*.

31. Brett G. Scharfs & John W. Welch, *An Analytic Framework for Understanding and Evaluating the Fiduciary Duties of Educators*, 2005 BYU EDUC. & L.J. 159, 163 (2005).

32. Scharfs & Welch, *supra* note 31, at 162.

33. *Id*.

34. Nina J. Crimm, *A Case Study of a Private Foundation's Governance and Self-Interested Fiduciaries Calls for Further Regulation*, 50 EMORY L.J. 1093, 1133-40 (2001).

35. Susan N. Gary, *Regulating the Management of Charities: Trust Law, Corporate Law, and Tax Law*, 21 U. HAW. L. REV. 593, 597 (1999).

36. *See, e.g.*, MODEL NONPROFIT CORP. ACT (Am. Bar Ass'n 1952); MODEL NONPROFIT CORP. ACT (Am. Bar Ass'n 1964); MODEL NONPROFIT CORP. ACT (Am. Bar Ass'n 2008); PRINCIPLES OF THE LAW OF NONPROFIT ORGS (Am. Bar Ass'n 2005 and 2007);. Rev. MODEL NONPROFIT CORP. ACT (Am. Bar Ass'n 1987).

non-profit board member is "measured under standards developed in the jurisprudence of for-profit corporations."[37] In finding this, they recognized the need for deference in decision-making for strategic purposes, and that the business judgment rule applied to the directors of a non-profit corporation.[38] However, they noted that non-profit corporations are generally for limited charitable purposes, whereas for-profit corporations are for larger and more inclusive purposes.[39] Reflecting on that, the court found that the fiduciary duty of a non-profit is determined by tailoring the duty to the nonprofit corporation's purpose.[40] "The *Oberly* decision, therefore, indicates that principles of corporate law will govern the activities of the governing body, but the fiduciaries have a 'special duty' to advance the goals and purposes of the nonprofit corporation."[41]

The Duty of Loyalty

Fiduciary duties are broken into two independent duties: the duty of loyalty and the duty of care. This section will analyze in detail the duty of loyalty. The duty of care will be addressed in the subsequent section.

The duty of loyalty and duty of care significantly overlapped until *Guth v. Loft* clarified the definition of the duty of loyalty.[42] In a 1939 ruling, the Delaware court defined the duty of loyalty as affirmatively protecting the interests of the corporation as well as refraining from engaging in anything that might bring injury to the corporation.[43] In addition, the case said that directors must not divide loyalties between the corporation and other entities.[44]

The duty of loyalty also requires acting in good faith and "maintain[ing] . . . unequivocal allegiance to the corporate mission."[45] The duty of loyalty is largely centered around acting in the best interest of the company by avoiding conflicts of interest.[46] Traditionally, we distinguish

37. Oberly v. Kirby, 592 A.2d 445, 461 (Del. 1991).
38. *Id.* at 466.
39. *Id*. at 462.
40. *Id*.
41. Mary A. Jacobson, *Commentary to Recent Developments in Delaware Corporate Law: Nonprofit Corporations: Conversion to For-Profit Corporate Status & Nonprofit Corporation Members' Rights – Farahpour V. DCX, Inc.*, 20 DEL. J. CORP. L. 635 (1995).
42. Carter G. Bishop, *The Deontological Significance of Nonprofit Corporate Governance Standards: A Fiduciary Duty of Care Without a Remedy*, 57 CATH. U.L. REV. 701, 738 (2001).
43. Guth v. Loft, 5 A.2d 503, 510 (Del. 1939).
44. *Id.*
45. Michael W. Peregrine, *Legal Concerns in Specific Health Care Deliver Settings: Nonprofit Corporate Governance*, 3 HEALTH L. PRAC. GUIDE 43, §22 (2010).
46. Thomas Lee Hazen & Lisa Love Hazen, *Punctilios and Noprofit Corporate Governance – A Comprehensive Look at Nonprofit Directors' Fiduciary Duties*, 14 U. PA. J. BUS. L. 347, 381 (2012).

the duty of loyalty from the duty of care by recognizing that "disloyal acts are generally intentional, although indifference to protect the organization or abdication and dereliction of duties are sufficient to establish breach of duty of loyalty."[47]

The Duty of Care

The duty of care requires directors to exercise good faith and diligence,[48] which is applied to nonprofit corporations and for-profit corporations alike.[49] The duty of care usually has the flavor of self-dealing, while the duty of loyalty has the flavor of wearing two hats at the same time.

The duty of care, as applied to nonprofit corporations, was later codified in the Model Nonprofit Corporate Act, which asserts: A director shall discharge his or her duties as a director, including his or her duties as a member of a committee:

> In good faith;
> With the care an ordinarily prudent person in a like position would exercise under similar circumstances; and
> In a manner the director reasonably believes to be in the best interests of the corporation.[50]

One caveat to the duty of care is that the business judgment rule protects decisions that are made with the belief that the decision is in the best interest of the corporation.[51] Courts have repeatedly maintained a strict standard of non-interference, unless "it be made to appear that . . . acts were fraudulent or collusive, and destructive of the rights of the stockholders. Mere errors of judgment are not sufficient as grounds for equity interference, for the powers entrusted with corporate management are largely discretionary."[52] As such, liability may not be imposed on directors if there is no claim of gross negligence.[53]

47. Ghahramani, *supra* note 19, at 16.
48. James J. Fishman, *Improving Charitable Accountability*, 62 MD. L. REV. 218, 232 (2003).
49. *See* Bishop, *supra* note 42, at 703-04.
50. REV. MODEL NONPROFIT CORP. ACT § 8.30 cmt. 3 (1987).
51. *See* Bishop, *supra* note 42, at 730.
52. Leslie v. Lorillard, 110 N.Y. 519, 532 (1888).
53. *In re* Lemington Home for the Aged, 777 F.3d 620, 634 (3d. Cir. 2015).

Effects of the Business Judgment Rule on the Fiduciary Duties of Care and Loyalty

While the duty of loyalty and duty of care place broad responsibilities on directors' shoulders, the business judgment rule was created to free directors to make business decisions that they rationally believed was in the best interest of the corporation.[54] The only qualification for the business judgment rule to remove liability for an error is that the decision was made with due care and in good faith.[55] In *Aronson v. Lewis,* the Delaware Supreme Court found that the determination of compliance with the duty of care cannot be made in reference to the content of the loss without consideration of rationality or good faith.[56] Egregious mistakes are still protected by the business judgment rule so long as they were made in good faith or with a rational belief that the decision was in the best interest of the corporation.[57] The underlying idea behind this is to give directors wide decision-making latitude in taking steps to benefit a corporation, which incentivizes "corporate innovation and rational risk-taking"[58] whilst limiting judicial intrusiveness."[59] In fact, this rule has been not only been applied to for-profit corporations but non-profit entities as well.

The Build-Up of *In re Caremark* and the Expansion of the Duty of Care

The law began to place requirements on the conduct of directors of for-profit corporations in *Barnes v. Andrews*, where the court held that a director has fiduciary duties to remain informed of business-related problems.[60] The suit focused around a passive director defendant, who the shareholders elected on to the board and on whom they placed the burden of guilt for the business not being successful.[61] In a famous opinion, Judge Learned Hand noted that it would be unfair to hold a director liable for an unsuccessful business, as directors are "not specialists like lawyers or doctors . . . they are general advisors of the business."[62]

In addition, Judge Learned Hand notes the importance of shareholders attention in selection of corporate directors. If a corporate director is chosen who is not well-suited for the position, shareholders cannot be particularly

54. *See* American law Institution, Principle of Corporate Governance §5.01(c).
55. *See* Park McGinty, *The Twilight of Fiduciary Duties: On the Need for Shareholder Self-Help in an Age of Formalistic Proceduralism*, 46 EMORY L.J. 163, 194 (1997).
56. *Id.*
57. McGinty, *supra* note 55.
58. Ghahramani, *supra* note 19, at 19.
59. *Id*.
60. Barnes v. Andrews, 298 F. 614, 614 (1924).
61. *Id.* at 618.
62. *Id.*

surprised when he doesn't execute his job as well as they had hoped.[63] The case is largely an embodiment of the Business Judgment Rule in that it centers around good faith efforts, and it starts to bring in inklings of the duty of oversight because it begs the question of whether good faith encompasses a duty to be informed as a component of exercising judgment.[64]

This question raised by the penumbras of *Barnes v. Andrews* gave fodder to a new component of the duty of care through *In re Caremark Intern. Inc. Derivative Litigation*, where the court found a duty of oversight.[65] In *Caremark*, two officers employed by Caremark were indicted because they participated in a kickback program with a physician.[66] Caremark had paid $1.1 million to a Minneapolis based physician to encourage him to prescribe and distribute Protropin, a human growth hormone made by Genentech and marketed by Caremark.[67] The payments started in 1986 and continued through 1993, and were hidden in cloaks of grant funds or consulting agreements.[68] Following the indictments, the Board was subsequently informed and denied any claim of wrongdoing. After the news broke about the first indictment, a slew of other kickback agreements came to light.[69] While Caremark worked to settle the claims, the shareholders were unhappy with the management of the company, and filed a derivative action to both judge the fairness of the settlement and simultaneously hold the directors responsible for not monitoring the inner workings of the company.[70] For the purpose of this paper, the discussion of *Caremark* will focus on the latter part of the aforementioned judgment.

The basis of the shareholders claims regarding directorial responsibility rested in the duty of care.[71] Specifically, the shareholders claimed that the "directors allowed a situation to develop and continue which exposed the corporation to enormous legal liability and in so doing they violated a duty to actively monitor corporate performance."[72] Liability for breach of the duty to exercise appropriate attention arises in two distinct situations:

> When a board decision causes a loss because the decision was ill advised or "negligent"

63. *Id.*
64. *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967 (1996).
65. *Id.*
66. *Id.* at 964.
67. *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d at 964.
68. *Id.*
69. *Id.*
70. *Id.* at 965.
71. *Id.* at 967.
72. *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d at 964.

> When an unconsidered failure of the board to act in circumstances in which due attention would have prevented.[73]
>
> In addressing the second question, the court proposed an extension of the duty of care when they posed the question, "what is the board's responsibility with respect to the organization and monitoring of the enterprise to assure that the corporation functions within the law to achieve its purposes?"[74]

The court deviated from an earlier holding in *Graham v. Allis-Chalmers* that "absent cause for suspicion there is no duty upon the directors to install and operate a corporate system of espionage to ferret out wrongdoing which they have no reason to suspect exists."[75] In *Caremark*, the court held that the board of directors' have a duty to be "reasonably informed concerning the corporation," which requires that the board ensure "that information and reporting systems exist in the organization that are reasonably designed to provide . . . timely, accurate information sufficient to allow . . . the board . . . to reach informed judgments concerning both the corporation's compliance with law and its business performance."[76]

Chancellor Allen justified the "refinement" of *Allis-Chalmers* in a three-part rationale. First, he outlined the over-arching shift in the importance of the board of directors, both in guiding the company as well as protecting shareholder interests. Second, he cited Delaware Corporation Law Section 141, which requires relevant and timely information to satisfy the board's duty to monitor. Lastly, he noted the impact of the federal sentencing guidelines on corporations. "Any rational person attempting in good faith to meet an organizational governance responsibility would be bound to take into account this development and the enhanced penalties and the opportunities for reduced sanctions that it offers."[77]

Since the *Caremark* decision, the court has only continued to strengthen the opinion that corporations have a duty to monitor the innerworkings of the company, regardless of company size or how far removed the board of directors are. In 2006, the court identified specific non-exhaustive examples of a violation of oversight liability, which includes things such as, "where the fiduciary intentionally fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties." A full enunciation of a *Caremark* claim was detailed in an unpublished opinion in 2016, when the Delaware Chancery Court wrote that plaintiffs need to show either:

73. *Id.*
74. *Id.* at 969.
75. Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (1963).
76. *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d at 970.
77. Paul E. Fiorelli, *Why Comply? Directors face heightened personal liability after Caremark*, 41 BUSINESS HORIZONS 49 (July/Aug. 1998).

(1) That the directors knew, or (2) should have known that violations of law were occurring and, in either event, (3) that the directors took no steps in a good faith effort to prevent or remedy that situation, and (4) that such failure approximately resulted in the losses complained of.[78]

Further strengthening *Caremark* were the Federal Sentencing Guidelines passed by Congress in 1984,[79] which Chancellor Allen recognized the importance of in his three-part refinement.[80] In his *Caremark* analysis, Chancellor Allen indicated that through the implementation of guidelines, companies will move towards federal compliance. "[T]he Guidelines offer powerful incentives for corporations today to have in place compliance programs to detect violations of law, promptly report violations to the appropriate public officials when discovered, and take prompt, voluntary remedial efforts."[81] The guidelines were amended in 1991 and 2004 to include organizational offenders, in addition to individuals.[82] To comply with the sentencing guidelines that the United States Sentencing Commission established, a corporation must:

> Establish adequate compliance standards and procedures to reduce the prospect of criminal conduct;
>
> Assign high-level personnel to oversee the compliance program, such as an ethics officer, ombudsman, or compliance officer;
>
> Use due care not to delegate substantial responsibility to a person with a propensity to engage in illegal activities;
>
> Communicate compliance procedures through publications (code of ethics, standards of conduct) or training;
>
> Audit its compliance programs and maintain a violation reporting system;
>
> Consistently enforce its compliance programs and not favor star employees; and
>
> Respond reasonably to an offense and modify the program to prevent future offenses.[83]

In addition to these guidelines, the United States Sentencing Commission also defined "organization" in order to determine who these guidelines applied to. They defined organization as, "a person other than an individual . . . [which] includes corporations, partnerships, associations,

78. Reiter v. Fairbank, No. 11693-CB, 2016 WL 6081823, at 7, (Del. Ch. Oct. 18, 2016).
79. *See* Sentencing Reform Act (SRA) of 1984, 18 U.S.C.A §3551 (1984).
80. Fiorelli, *supra* note 77.
81. *In re* Caremark Derivative Action, 698 A.2d at 969.
82. Sentencing Reform Act, *supra* note 79.
83. Fiorelli, *supra* note 77.

joint-stock companies, unions, trusts, pension funds, unincorporated organizations, governments and political subdivisions thereof, and non-profit organizations."[84]

EXTENSION OF FIDUCIARY OBLIGATIONS TO THE NONPROFIT SECTOR

The enforcement of fiduciary duties within nonprofits (both charitable trusts and nonprofit corporations) is through public enforcement by state attorney generals,[85] through the special interest doctrine,[86] or through a derivative suit.

State attorney generals are empowered by statutory law to supervise nonprofits and enforce fiduciary duties to protect the public interest.[87] Much of the actual supervision is limited, however, due to "lack of funds and resources."[88] "[State attorney generals] have neither the person-power, nor sometimes the will, to monitor nonprofits effectively."[89]

As such, the special interest doctrine is used to empower the private individual.[90] If a person has a "special interest" in the organization, they will be allowed standing to sue.[91] According to a 1993 study, special interest status is granted by considering the five following factors:

> The extraordinary nature of the acts complained of and the remedy sought by the plaintiff;
>
> the presence of fraud or misconduct on the part of the charity or its directors;
>
> the state attorney general's availability or effectiveness;
>
> the nature of the benefitted class and its relationship to the charity;
>
> subjective and case-specific factual circumstances and social desirability.[92]
>
> If a special interest plaintiff is granted standing to sue, they must seek relief in the form of a "benefit to the charity itself and not money damages for the plaintiffs."[93]

84. Federal Sentencing Guidelines Manual § 8A1.1 (2018).

85. MARION R. FREMONT-SMITH, GOVERNING NONPROFIT ORGANIZATIONS: FEDERAL AND STATE LAW AND REGULATION 43-48 (Harvard University Press, 2008).

86. *See* RESTATEMENT (SECOND) OF TRUST § 391 (1959).

87. *See* Gary, *supra* note 35, at 622.

88. Ghahramani, *supra* note 19, at 21.

89. Fishman, *supra,* note 48, at 268.

90. *See* Gary, *supra* note 35, at 627.

91. *Id.*

92. Mary Grace Blasko, et al., *Standing to Sue in the Charitable Sector*, 28 U.S.F. L. REV. 37, 61 (1993).

93. *See* Gary, *supra* note 35, at 627.

Suits Against Boards of Trustees

Automatic standing is only granted to state attorney generals.[94] Standing is otherwise permitted on a case-by-case basis, depending on whether or not the individual qualifies as having a "special interest."[95] Justice Marshall's note in *Dartmouth* that "the students are fluctuating, and no individual among our youth has a vested interest in the institution, which can be asserted in a court of justice"[96] has been the arm that has allowed the court to deny students who claim a "special interest" to gain standing.[97] Derivative actions are also unavailable to students, as they are not a membership-based entity.[98]

The Case against Wilson College's Board of Trustees

There is, however, precedent available for holding directors accountable for neglecting their duties. Wilson's College was a private college chartered by the Pennsylvania legislature.[99] The Board of Trustees voted to close the university due to financial constraints and to change the corporate name to "Wilson College Foundation," which would receive the university's corporate assets to invest them to "continue to work toward the aims of Wilson College . . . [the purpose for which], as stated by its founders . . . [was] to provide for women the opportunity for broad and thorough education of the highest quality."[100] The decision was rooted in a declining number of prospective students seeking admission.[101]

A coalition was formed to challenge the decision by seeking court interference through injunctive relief.[102] A dissenting trustee, alumnae, faculty, enrolled students, and not yet matriculated students not only sought injunctive relief, but also asked that Wilson College be made a co-petitioner.[103] The judge gave standing to everyone except the current and prospective students.[104]

The petitioners argued that "the very act of voting to close the College and then without Court approval proceeding to implement that decision . . .

94. Ghahramani, *supra* note 19, at 22.
95. *See* Gary, *supra* note 35, at 627.
96. Ghahramani, *supra* note 19, at 23.
97. Miller v. Alderhold, 184 S.E.2d 172, 175 (Ga. 1971).
98. Sarah R. Kusiak, *The Case for A.U. (Accountable Universities): Enforcing University Administrator Fiduciary Duties Through Student Derivative Suits*, 56 AM. U. L. REV. 129, 156 (2006).
99. Zehner v. Alexander, 3 Franklin County Legal J. 27, 29 (Pa. Orphans' Ct. 1979).
100. *Id.* at 70-71.
101. Fred M. Hechinger, *Wilson College, A 'Lost Cause,' Looks Lively*, N.Y. TIMES, Nov. 11, 1980, at C1.
102. Zehner v. Alexander, 3 Franklin County Legal J. at 28, 30-34, 37.
103. *Id.*
104. *Id.* at 84.

was totally detrimental to the charter purpose of Wilson College and grounds for judicial removal"[105] and that the evidence showed "established a history of mismanagement."[106] As a result, the petitioners wanted the trustees to "show cause [as to] why they should not be removed immediately as trustees"[107] and why they should not be "permanently enjoined from implementing the closing of the college."[108]

Through the cy-près doctrine, the court acknowledged the petitioners need for the court to issue approval for any "fundamental change to a nature of a nonprofit corporation, which the respondents had not sought."[109] In their opinion, the court wrote:

"By implementing the decision to close Wilson College the Trustees attempted to essentially deprive the Court of its power to review the recommendation of the Board and to approve or disapprove the proposed diversion of college assets from a teaching institution to some other charitable use. In addition, the implementation of the decision to close Wilson College without prior approval of the Court attempted to deprive the public, represented by the Attorney General as *parens patriae*, of an opportunity to comment upon or protest the decision."[110]

The court didn't dismiss the entire board as they didn't find evidence of dealing in bad faith (evidence of "fraudulent conduct or dishonest acts").[111] The college president, though, was found to have acted with "gross abuse of authority and discretion," which resulted in her permanent removal from the board.[112] Another member was found to have conflicting interests through their presidency at Bryn Mawr College, which presented "proper cause" for their removal as well.[113] Wilson College was enjoined from closing without court approval, and Wilson College was forbidden from paying respondents' court fees.[114]

THE 2019 COLLEGE ADMISSIONS SCANDAL AND THE LACK OFMONITORING

As this analysis has shown, fiduciary law requires a duty of care from all trustees, requiring trustees to conduct directorial functions that an ordinarily prudent person would exercise in a like position and under

105. *Id.* at 83.
106. *Id.*
107. Zehner v. Alexander, 3 Franklin County Legal J. at 28.
108. *Id.*
109. Ghahramani, *supra* note 19, at 25.
110. Zehner v. Alexander, 3 Franklin County Legal J. at 82.
111. *Id.* at 83-84.
112. *Id.* at 83.
113. *Id*.
114. *Id.* at 86.

similar circumstances.[115] Encompassed in this duty is responsibility of oversight, requiring all directors to know of the inner functions of their corporation, regardless of how far removed from operations they are.

With respect to Operation Varsity Blues, it is clear that a majority of universities involved breached their duty of oversight by failing to supervise their admissions process. Athletic departments were not overseen by any sort of regulatory figure within the university, allowing for a side-door to be utilized by prospective students and their parents. While a director may be far removed from the processes of athletic recruitment, there still should have been enough oversight by the admissions department to not only vet the prospective students to the same degree as other students, but also to validate their credentials for admission.

An additional layer of oversight could simply be transparency in money donated to specific athletic departments. A pivotal move in the side-door scheme was donating a large sum of money to specific athletic divisions of the university, which the coach or head of the department accepted and utilized to his or her own benefit. The universities should have maintained their duty of oversight by requiring financial reports from each department to inform them of any illegal or fraudulent activity within their colleges. In the case of Georgetown University and Gordon Ernst, the college found out about Ernst's conduct in 2017 and remedied the issue by removing him from his position.[116] But no further action was taken to fix the lack of oversight.[117] With no active oversight, Rick Singer was able to keep his charade going for far too long.

Furthermore, the boards of trustees also conjunctively violated their duties of loyalty. The duty of loyalty requires trustees to pursue what is in the best interest of the corporation they serve and not act in self-dealing. If the directors knew (or implicitly knew) of the corrupt practice of utilizing Singer's "side-door" for admissions, they breached their duty of loyalty. The best interests of a university are maintained by promoting a certain level of integrity in their admissions process and taking bribes on the side in no way mirrors that.

RECOMMENDED ACTION

It is apparent that boards have taken little initiative to incorporate transparency into the university admissions process, and as such, there should be a policy shift in order to encourage universities to move into this

115. *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 959 (1996).

116. Alex Lewontin & Nick Gavio, *Nationwide Admissions Scandal Implicates Former Georgetown Tennis Coach, Parents*, THE GEORGETOWN VOICE, Mar. 12, 2019, https://georgetownvoice.com/2019/03/12/nationwide-college-admissions-scandal-implicates-former-tennis-coach-parents/ [https://perma.cc/VJ84-ZMXV].

117. *Id.*

important realm of honesty. It was once thought that the biggest incentive for boards of trustees was image, as serving on college and university boards signals wealth and status to one's peers.[118] In the face of public controversies, board reputations suffer.[119] This observation, however, addresses the aftermath of the problem rather than preventing the wrongdoing in the first place. As a result, university presidents and boards of trustees need to be encouraged to make an ethical admission process an important agenda topic.

To make this a priority in their university governance agenda, the next three sections suggest three methods of encouraging university admissions transparency. The first two recommendations are through extensions of the Sarbanes-Oxley Act, which would impose liability on specific board members or university presidents for not maintaining accurate reporting or codes of conduct. The last proposal is a compensation incentive for the president, encouraging voluntary action. The first two actions work as a metaphorical stick, while the other works as a carrot.

The Sarbanes-Oxley Act and Section 302

In the late 1990s, the burst of the stock market bubble uncovered a widespread problem of financial fraud within public companies. Through the Sarbanes-Oxley Act of 2002, Congress imposed new standards of accountability for boards of directors as well as corporate officers.[120] The new law encompassed requirements for corporate ethics and civil and criminal penalties for non-compliance.[121] The purpose of the law is simply put: "An Act to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes."[122] While the purpose of the act is simple, the composition is not. For the purposes of this note, the analysis will focus on the two components of the law that are best suited to impose a duty of oversight through statutory means: corporate responsibility for financial reports and codes of conduct.

Corporate Responsibility for Financial Reports

The second component of Sarbanes-Oxley establishes corporate responsibility for financial reports by requiring an individual within the company to vouch for the accuracy of the internal audits and reports. This

118. ROBERT E. MARTIN, THE COLLEGE COST DISEASE: HIGHER COST AND LOWER QUALITY, 102-103 (2011).
119. *Id.*
120. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745.
121. *Id.*
122. *Id.*

is imposed on two roles: "the principal executive officer or offices and the principal financial officer or officers, or person performing similar functions."[123] Thus, following the completion of reports, the CEO and CFO are required to sign a statement saying that "to the best of the signer's knowledge, the report does not contain any untrue statement that is material, or neglect to include any fact that would help to make any statement in the report 'not misleading.'"[124] If invalid for any reason, the CEO and CFO are required to give back any bonus or equity they received, as well as all profit made on their sale of company stock within the twelve months prior to the date of certification.[125] This does not include any consequences imposed by the corporation itself.[126]

If this component of Sarbanes-Oxley were expanded to universities, it would require accuracy and transparency in the admissions process. By not including details of monetary contributions geared towards a side-door admission via athletic programs, the university would be making untrue statements about the financial integrity of the university as well as the level playing field for the admissions process. In addition, they would not be including facts that would make the statements in the report not misleading.

The fourth component of Sarbanes-Oxley requires that "two officials have design[ed] and implement[ed] the 'internal controls' that they believe are necessary to ensure that all material information . . . [has] been provided to them and included in the reports, and have tested those controls to see if they are working.'"[127] While most corporations are able to satisfy this element through an internal structure that is then submitted to an audit by an accounting firm, the same is not required to be mirrored in non-profit entities.[128] Furthermore, the meaning of "internal controls" is largely subjective and up to the corporations discretion on how to create and maintain them. "Like the speck of dust held by Horton, the simple words 'internal controls' contain a universe."[129]

To satisfy part of the fourth requirement, a university could engage an external auditor to review and verify financial statements. More importantly, and integral to the admissions scandal, however, would be employing internal auditors, who not only would ensure financial information accuracy, but also that all parts of the organization are complying with laws, regulations, policies, and procedures. If the internal

123. Sarbanes-Oxley Act § 302(a) (codified at 15 U.S.C.A. § 7241(1998 & West Supp. 2004)).

124. *Id.*

125. Sarbanes-Oxley Act § 302(a) (codified at 15 U.S.C.A. § 7241(1998 & West Supp. 2004)).

126. Carl Oxholm III, Sarbanes-Oxley in Higher Education: *Bringing Corporate America's "Best Practices" to Academia*, 31 J.C. & U.L. 351, 358 (2005).

127. *Id.*

128. *Id.* at 359.

129. *Id.*

auditors were unable to validate the internal levers and controls of the university, the board would be alerted.

To expand the Sarbanes-Oxley Act to universities, the requirement for a signatory to validate a form as a hook for liability could be added to a Form 990, which is an informational tax form that tax-exempt entities are required to file annually.[130] Not only would the signatory create liability, but it would resolve the issue of standing by encouraging state attorney generals to impose civil and criminal penalties like they do on for-profit institutions.

If the compliance initiative proposed by Section 302 of the Sarbanes-Oxley Act were broadened to both encompass non-profit corporations as well as universities, signatories who either failed to implement a thorough internal audit system or signed off on reports that were inaccurate or misleading would be subject to severe penalties, both through civil and criminal penalties as well as penalties imposed by the university itself. In turn, the university would both be incentivized to choose leaders who were highly ethical as repeated mistakes by university leaders (and subsequent penalties) are fodder for the media and could hurt admissions.

Moreover, society would not only see a shift in the ethics of the admissions processes but also in the proactivity of both boards of trustees as well as university presidents or chancellors. ". . . A prudent president will assess the institution's financial systems to identify the areas in which it is most at risk for holes and 'disloyal' conduct." Through the imposition of Sarbanes-Oxley, there would be no room for a claim of a violation of the duty of oversight. University leaders would be conscious of the inner workings of each department because of the thorough process they would carefully create and deploy.

University Presidents as Compensated Gatekeepers

While the aforementioned resolutions are a form of ensuring transparency every step of the way, incentivizing the president to act as a gatekeeper could also produce this result. While university presidents are not technically a part of the board of trustees, they are selected by unanimous agreement of the trustees.[131] The board usually gives the president governing guidelines, but the president has the authority to make decisions using their own discretion.[132] Their role largely mirrors the role

130. Barbara Weltman, *The Purpose of IRS Form 990*, INVESTOPEDIA (Oct. 29, 2019, 9:12 PM), https://www.investopedia.com/articles/personal-finance/083115/purpose-irs-form-990.asp [https://perma.cc/VC29-QZYJ].

131. Nick Price, *The Roles and Responsibilities of a Board of Directors for a College or University*, BOARD EFFECT (Feb. 2, 2018), https://www.boardeffect.com/blog/roles-responsibilities-board-directors-college-university/ [https://perma.cc/5SER-N5QC].

132. *Id.*

of a CEO.[133] As an arm of the board, one such proposal could take the form of a president gatekeeper, who would be enabled and incentivized to prioritize transparency in the admissions process by increased compensation. A "president gatekeeper" would be empowered to work independently to ensure that the admissions process is done ethically and with integrity. The logic behind this parallels executive pay-for-performance incentives.[134]

One of the biggest differences between boards of directors and university presidents, however, is equity-based compensation.[135] Equity based compensation allows directors and executives to root themselves in the long-term success of the business, thereby incentivizing them to work diligently, responsibly, and reach high levels of success. This form of compensation is absent in universities; presidents have salaries and cash-based performance bonuses.

Cash-based incentives aren't effective at promoting ethical management for two reasons. Firstly, the size of existing compensation packages mean that any additional incentives are just drops in the bucket. Secondly, university presidents should already be incentivized to promote ethical behavior in admissions because of their base salary being presumably tied to a code of ethics. An illustration of this is the former President of the University of Southern California. The University of Southern California has a Code of Ethics, which commits university employees to discharging obligations in a "fair and honest manner" as well as "respecting the rights and dignity of all persons."[136] As such, the university president would likely be bound to these obligations. In 2017, prior to Operation Varsity Blues' publicity, the President of the University of Southern California made a base salary of $1,467,330 and earned a bonus of $239,612, resulting in total compensation of $2,404,232.[137] Presumably since the President was bound to terms of ethics, the idea of fostering morality in the admissions process would have been within the scope of his employment. Creating an incentive program for a university president to encourage the idea of an ethical admissions process would throw money at presidents to just do the job they were hired to do.

The idea of establishing the university president as a compensated gatekeeper, therefore, appears hard to execute effectively, given the

133. *Id.*

134. Michael C. Jensen & Kevin J. Murphy, *CEO Incentives – It's Not How Much You Pay, But How*, HARV. BUS. J. (last visited Feb 8. 2020), https://hbr.org/1990/05/ceo-incentives-its-not-how-much-you-pay-but-how?fbclid=IwAR2FL_2N87LSyG3vKD DoxhNWHdpQuYXJ2eKi4JDn-xUvY2p2mVYdFzrcHps [https://perma.cc/Q4EF-JAXR].

135. Dan Bauman, et al., *Executive Compensation at Public and Private Colleges*, THE CHRONICLE OF HIGHER EDUCATION (last visited Feb. 9, 2020), https://www.chronicle.com/interactives/executive-compensation#id=table_private_2017 [https://perma.cc/HSS8-7QWL].

136. USC Code of Ethics, https://policy.usc.edu/ethics/ (last visited Feb. 9, 2020).

137. Bauman, et al., *supra* note 135.

existing compensation these figures receive. As a result, we are left with the strongest method for incentivizing more comprehensive oversight being the extension of *Sarbanes-Oxley*.

CONCLUSION

Daniel Golden and Doris Burke wrote about Operation Varsity Blues in the Washington Post, asserting a need for universities to take responsibility for their role in the matter.[138]

Such allegedly criminal tactics represent the logical, if extreme, outgrowth of practices that have been prevalent under the surface of college admissions, and that undermine the American credos of upward mobility and equal opportunity. Although top college administrators and admissions officials were apparently unaware of the deception, their institutions do bear some responsibility for developing and perpetuating the system that made it possible.[139]

This paper functions off of a similar premise—that the university and its board of trustees are there to safeguard the interests, integrity, and reputation of the university. Those boards involved in the scandal did not safeguard the interests of their universities, but rather violated their duty of care.

As of today, a couple of student initiated court decisions are pending in court and the only repercussions for those involved are criminal penalties for Rick Singer and parents who utilized Singer's service.[140] While the universities themselves aren't being held accountable for their role in the ordeal, other universities are beginning to engage in proactive measures. Southern Methodist University began independently investigating students with ties to Rick Singer and his college-counseling firm.[141]

This paper, however, functions on the premise that an internal review of students' associations with Rick Singer is not enough to satisfy a duty of oversight. A duty of oversight encourages directors to serve for the benefit of the university, as well as to have a keen eye for its internal health. This obligation is imposed by the extension of fiduciary duties to nonprofit entities and overcoming an issue with lack of standing through a similar extension of the Sarbanes-Oxley Act of 2002 that directly implicates a trustee who hasn't satisfied their fiduciary duties. If anything has become evident through

138. Daniel Golden, *He investigated how rich buy their way into elite colleges. Some took his book as a how to guide*, WASH. POST (Oct. 29, 2019, 4:12 PM), https://www.washingtonpost.com/education/2019/03/13/he-investigated-how-rich-buy-their-way-into-elite-colleges-some-took-his-book-how-guide/ [https://perma.cc/R5NY-CMMN].

139. *Id.*

140. Tamboura v. Singer, Docket No. 5:19-cv-03411 (N.D. Cal. 2019).

141. Connor Pitman, *National college admissions scandal leads to letter from R. Gerald Turner*, SMU DAILY CAMPUS (Oct. 29, 2019, 5:32 PM), https://www.smudailycampus.com/news/national-college-admissions-scandal-leads-to-letter-from-r-gerald-turner [https://perma.cc/8XSQ-T39F].

Operation Varsity Blues, it's that action is required to ensure a fair playing field for university applicants. With little incentive for trustees to correct their own errors and avoid an Operation Varsity Blues II, it is up to the state to pursue a way to hold boards of trustees to a higher standard.