



Waiter, There's a Lawyer in My Soup!

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Charlie Deitch

Feature Story

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by Charlie Deitch

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When *Corporate Board Member* asked more than two dozen directors to tell us what bothers them about lawyers, common themes quickly emerged. Among those was a deep concern about the true independence of independent counsel, but leading the list was...

Excuse me, but I think there's a problem with my bill.

The high fees of outside law firms are one of the oldest and most widely leveled complaints directors have about the legal profession. And the increased need for lawyers in the Sarbanes-Oxley era of corporate America has sent costs even higher.

"There is a lot of work out there for lawyers, and a lot of it is time-consuming," says W. Ronald Dietz, 63, CEO of the office-management and leasing-services company W.M. Putnam Co. in Bloomington, Illinois, and a director of Capital One Financial. "But I think a lot of law firms are behind the curve in addressing issues like document-management problems and how to manage the increase in legal activity."

To try to keep costs down, Dietz says, law firms must examine alternatives like outsourcing more routine legal tasks and setting up more efficient systems to pass documents back and forth between lawyer and client. And client companies need to be more demanding with their lawyers, pressing to make sure that costs and billable hours are kept at reasonable levels, he says: "We have to become more aggressive in dealing with these issues to provide a more efficient product."

Nelson A. Diaz, 59, a partner in the Philadelphia law office of Blank Rome who also serves on the board of Exelon, a Chicago utility holding company, says that "developing a competitive environment of cost control has to be a priority for general counsel now and in the future. I think it's appropriate for major law firms to make discounts and cutbacks available to companies based on the nature of their relationship. It's going to

take a concerted effort by companies to force these kinds of changes. You have some Fortune 1,000 companies that have thought about it, but few have made inroads.”

Winston R. Hindle Jr., 75, former senior vice president at Digital Equipment Corp. and a director of Boston-based business-services outfit Keane Inc. and of Mestek Inc., which makes heating and air-conditioning equipment in Westfield, Massachusetts, says the problem starts with overregulation: “Generally, I think firms are getting rich on the fact that Sarbanes-Oxley is with us and that the SEC has stepped up surveillance. The fact is, public corporations have been loaded with too many regulations, and it’s a real burden on us.” But Arthur K. Lund, 73, an attorney himself and a director of Greater Bay Bancorp in East Palo Alto, California, argues that part of the blame for high legal costs must be placed on a litigious society. “I think the worst thing that has happened to the legal profession is the general attitude of people who want something for nothing,” he says. “Somebody trips, gets hurt, and wants money. Unfortunately, there are lawyers who are more than willing to try and get it for them, and that drives up the cost of legal services for everyone.”

Sometimes I feel like a lawyerless child.

Directors understand, of course, that in-house counsel works for the company, not for them individually. But as the organization’s overseers, they want legal advice in which the good of the company, not the interests of top executives, is paramount. “Whether it’s outside counsel called in by the board on certain matters or in-house counsel, the advice they give has to be relied upon based on legal issues and not on what management wants the advice to be,” says James L. Martineau, 65, a private investor and a director of Minneapolis glassmaker Apogee Enterprises and casino operator Pinnacle Entertainment in Las Vegas. “It’s difficult for lawyers and accountants not to side with management, but it has to happen.”

“I’m not saying that general counsel aren’t competent—they are,” says Guy Adams, 55, managing director of GWA Capital Partners in Pasadena, California. “But so many checks are signed by management that there is no upside to going against their wishes.”

Adams is a dissenting director who usually goes on boards where he’s not wanted. He waged a proxy fight in 2001 that enabled him to join the Lone Star Steakhouse board and help revamp that company’s operations and profitability, and in 2003, after threatening another proxy fight, he was put on the board of pulp and paper producer Mercer International, where he still serves. Last year a proxy fight got him on the board of Exar Corp., a Fremont, California, manufacturer of various communications equipment. Given his outsider status, Adams says that as a director he has frequently paid for independent legal advice out of his own pocket. On those occasions, he adds, he has often discovered that directors were told only half of what they should have known.

“Management opposes independent counsel for directors because it would be someone else in the room holding management to a higher standard,” says Adams. “How much would it cost—\$50,000, \$100,000 a year? I think that’s a pretty modest price to make sure the right decisions are being made.”

We don't always need middlemen.

Yes, management and the general counsel usually hire the outside counsel, but once again directors cite their role as overseers and say they should have their own access. ING Funds chairman Jock Patton, 60, a director of JDA Software Group in Scottsdale, Arizona, and Phoenix-based trucking company Swift Transportation, is one of many who insist, "There needs to be a direct line of communication between the board and outside counsel."

John E. Beard, 73, a retired attorney who sits on the board of BTU International, which manufactures thermal processing systems in North Billerica, Massachusetts, and until last year was a director of footwear maker Timberland in Stratham, New Hampshire, says he has heard of instances at other companies in which keeping directors away from outside counsel may have been a management strategy. "I think something has been lost by the practice of inside counsel keeping outside counsel away from the board," he says. "This commonly happens at the initiative of inside counsel, and the CEO often cheers because he or she doesn't have to be concerned with communications outside the boardroom between counsel and board members. Timberland has a strong relationship between inside counsel and outside counsel, and is to a great extent an exception to the usual guarded and grudging portal through which communication between outside counsel and the board occurs."

I can't talk now, my lawyer's in the room.

E. P. "Lou" Marinos, 64, chairman of Arrhythmia Research Technology in Fitchburg, Massachusetts, says that having one of a company's lawyers on the board is probably not in the best interest of the company. And indeed, it is happening less these days (see "Barring Lawyers From the Board" on page 31).

"The person sitting next to you is probably a good corporate lawyer, a good director, and a good businessman," says Marinos. "But the problem I have is that the advice you get when you ask this person as a director is not the same advice you might get if he were your outside counsel. If I want legal advice as a director, I want it to be at arm's length and completely independent."

Back off, guys!

Craig G. Matthews, 63, retired vice chairman and COO of KeySpan Corp. in New York City and a director of Amerada Hess and National Fuel Gas Co., says that for more than a hundred years KeySpan, a northeastern U.S. utility, had a policy of employing no in-house lawyers. The understanding was that the company would make the business decisions, and when legal advice was needed it would be sought.

During a merger, however, "the other company had a sizable internal legal staff," says Matthews, and "we decided to keep a reasonable staff of internal counsel. However, we set limits on the type of work we would handle and agreed to outsource all specialty litigation or other specialized legal work. Outside counsel who are specialists in certain areas will render opinions that may not be totally aligned with those of the general counsel. A good mix is healthy. Just as we wouldn't want all engineers to run a company

because the tendency would be to overbuild, or we wouldn't want all salespeople to run the company because we would overmarket, we can be overinfluenced by lawyers. The issue is one of balance."

Matthews adds, "We need lawyers to appropriately identify legal issues and corporate risks and protect our interests, but we need to be careful that they don't become too conservative in their advice. We need to keep their input in perspective and then make the appropriate business decision. Without being totally harsh to my lawyer friends, I think there is a reason that few CEOs are lawyers."

David A. Rosow, 63, is chairman and CEO of the Southport, Connecticut, private investment firm Rosow & Co. and a director of TD Banknorth Inc. in Portland, Maine. He says, "The principal concern I have is that the legal profession is running everything. They have become, by default, the last word on too many subjects. Business sense and business judgment is the responsibility of the board, and that power cannot simply be relegated to the opinion of legal counsel. In too many cases, the judgment of the board is clouded by the judgment of an attorney."

Objection sustained.