



METROPOLITAN WASHINGTON AIRPORTS AUTHORITY

EXECUTIVE AND GOVERNANCE COMMITTEE

**PROPOSED AMENDMENT TO BYLAWS
ESTABLISHING NEW INDEMNIFICATION POLICY
FOR
BOARD OF DIRECTORS**

March 2013



BACKGROUND

The Airports Authority's policy for the indemnification of members of the Board of Directors, set out in Article XI of the Bylaws, has been in effect for over twenty years.

Last fall, a Board working group was established to review the policy, consider "best practices," and propose a revised or new indemnification policy.

The working group, with assistance from staff and outside consultants, has proposed an amendment to the Bylaws that sets out a new indemnification policy for the Board.



DISCUSSION

Major features of the proposed new policy:

- Two areas of coverage: General Coverage and Removal Coverage
- Under General Coverage
 1. Base rule: if Director is made a party to a proceeding based on status as Board member or conduct undertaken as member, the Authority will provide legal representation and will indemnify for any personal liability . . . subject to two qualifications: Exclusions and Standard of Conduct
 2. Exclusions: (i) criminal conduct and (ii) fraudulent and related conduct – if applicable, legal representation and indemnification are unavailable, but with the “prevailing” exception



3. Standard of Conduct

- What is content: a good faith and reasonable belief that conduct within scope and consistent with interests of Airports Authority
- When applied and by whom: after proceeding . . . by Board or independent counsel
- Ever deemed to be satisfied: yes, if prevail “on merits” in proceeding
- What are consequences of not satisfying: reimburse for legal representation and no indemnification of personal liability



- Under Removal Coverage
 1. Applicability: Director removal from Board
 2. Process: for determining whether indemnification of legal costs should be provided
 3. Standard of Conduct: its satisfaction is a condition of indemnification . . . and is deemed satisfied if prevail in proceeding



CONCLUSION

It is recommended that the Committee forward the proposed amendment to the Bylaws to the Board of Directors with a recommendation that it be approved by the Board.

RECOMMENDATION PAPER TO THE
EXECUTIVE AND GOVERNANCE COMMITTEE

PROPOSED AMENDMENT TO BYLAWS PROVIDING A NEW
INDEMNIFICATION POLICY FOR MEMBERS OF THE BOARD OF DIRECTORS

MARCH 2013

RECOMMENDATION

That the Executive and Governance Committee review the attached amendment to the Bylaws, which proposes a new policy governing the Airports Authority's indemnification of members of the Board of Directors, and recommend its adoption by the Board.

BACKGROUND

The Airports Authority's policy for the indemnification of members of the Board of Directors, set out in Article XI of the Bylaws, has been in effect for over twenty years. Last fall, the Board recognized a need for the policy to be reviewed and for appropriate revisions to be recommended for its consideration.

Over the past few months, a Board working group, consisting of Chairman Curto and Directors Connor and Session, has been evaluating the current indemnification policy, reviewing "best practices," and considering potential revisions of the policy. The working group has undertaken this work with assistance from staff and outside consultants. The working group is now proposing a new indemnification policy for the Board and its officers. This proposed policy is set out in a new section 2 of Article XI of the Bylaws, which is attached as Attachment A. A detailed summary of the proposed policy is set out in Attachment B.

DISCUSSION

The proposed policy provides generally that the Airports Authority will supply *legal representation* to and will *indemnify* Directors from personal liability whenever they are made a party or a participant in a judicial, administrative or investigative proceeding based upon their status as a member of the Board or conduct they have undertaken as a Board member. In providing direct legal representation to Directors, the policy represents a significant shift from the current policy under which Directors may be *indemnified after* the conclusion of a proceeding for the legal representation costs they *actually incurred* during the proceeding.

The proposed policy imposes two conditions on the provision of legal representation and indemnification: the absence of any *Exclusions*, and the Director's satisfaction of a *Standard of Conduct*.

The *Exclusions* identify certain Director conduct for which neither legal representation nor indemnification will be provided. The Exclusions are twofold: (1) proceedings in which a Director, based on personal conduct, is charged with a criminal offense or is being investigated for having committed a criminal offense; and (2) proceedings in which the *sole* allegations against a Director consist of fraudulent or dishonest activities, intentional violation of a fiduciary or other duty owed to the Authority, or activities undertaken for personal gain.

The proposed policy does provide an exception to the application of these Exclusions. This occurs if and when a Director ultimately prevails in a proceeding involving conduct falling within an Exclusion. In that case, the Director will be *indemnified* for the reasonable legal costs he or she incurred in the course of the proceeding, subject to the Director's satisfaction of the Standard of Conduct.

The *Standard of Conduct* condition requires a determination that the Director, when engaging in the personal conduct that has been alleged in a proceeding, had both a good faith belief and a reasonable belief that the conduct was within the scope of the Director's duties and was consistent with the interests of the Authority. This determination is made after the conclusion of the proceeding, and it is made by the Board or independent counsel selected by the Board. However, the proposed policy provides that, when a Director prevails in a proceeding (other than a proceeding addressed in the prior paragraph), the Director will be deemed to have satisfied the Standard of Conduct in which case no Board or independent counsel determination will need to be made. When a Director does not prevail in the proceeding and does not satisfy the Standard of Conduct, two consequences occur: the Director will not be eligible for the indemnification of any personal liability imposed in the proceeding; and the Director will be obligated to reimburse the Authority for the cost it incurred in providing the Director with legal representation during the proceeding.

The proposed policy also addresses a different type of proceeding involving Directors—the removal of a Director from the Board of Directors. Here, the proposed policy defines a process to determine whether the Director may be indemnified by the Airports Authority for the legal costs the Director incurs in contesting the removal. The process is as follows:

1. A Director intending to initiate a proceeding to contest the removal may request that the Board authorize the indemnification of the legal costs the Director will incur during the proceeding.
2. Upon receipt of the request, the Board will select an outside independent counsel to review the request and will forward the request to that counsel.

3. The independent counsel, following whatever inquiry is deemed necessary, will determine whether approval of the Director's request is in the best interest of the Airports Authority, will state the reasons for the determination, and will recommend that the Airports Authority approve or deny the request.
4. The Chairman and Vice Chairman of the Board and the General Counsel will review the independent counsel's recommendation, and will decide to approve or disapprove the Director's request.
5. If the request is approved, the Authority will indemnify the Director for all reasonable legal costs incurred during the proceeding, subject to the Director's satisfaction of the Standard of Conduct at the conclusion of the proceeding.
6. If the Director prevails in the proceeding, the Standard of Conduct will be deemed to have been satisfied, and the Director will be indemnified for incurred costs; if the Director does not prevail, indemnification will occur only if the Director satisfies the Standard of Conduct.

CONCLUSION

It is recommended that the Executive and Governance Committee forward to the Board of Directors the attached proposed amendment to the Bylaws, which sets out a new indemnification policy for Directors, with a recommendation that it be approved by the Board.

Prepared by

Office of General Counsel
March 2013

Attachments

Proposed New Indemnification Policy for Board of Directors

BYLAWS

* * * * *

ARTICLE XI

Miscellaneous

* * * * *

Current Section 2 (Proposed to be deleted)

Section 2. Indemnity. The Authority shall indemnify each Director and Officer against all costs and expenses (including counsel fees) the Director actually incurs in connection with or resulting from any action, suit or proceeding, of whatever nature, to which the Director is or shall be made a party by reason of his being or having been a Director or Officer of the Authority, provided (1) that the Director or Officer conducted him- or herself in good faith and (2) reasonably believed that his or her conduct was in the best interest of the Authority. This indemnity shall not apply in actions when the Director or Officer is adjudged liable to the Authority.

Proposed New Section 2

Section 2. Representation and Indemnification. The Authority shall defend and indemnify each Director as follows. For purposes of subsections (a) through (e) of this section, the term Director includes Officers elected or appointed by the Board.

a. *Legal Representation.*

(i) A Director shall be provided legal representation by the Authority, at no cost to the Director, whenever the Director is made or required to become a participant in a Proceeding, as defined in subsection (f), whether as a defendant or respondent, a witness, a deponent, the recipient of a subpoena for physical materials, or otherwise, as the result of an action of another person *other*

than the Authority itself, and due to the Director's status as a member of the Board or to conduct in which the Director is alleged to have engaged while acting as a member of the Board; provided, that legal representation shall not be provided for a Director when a Legal Representation Exclusion, as defined in subsection (c), is applicable; and provided further, that the Director shall be required to reimburse the Authority for its actual cost of providing legal representation if, at the conclusion of the Proceeding, it is determined, pursuant to subsection (d), that the Director has not satisfied the Standard of Conduct.

(ii) A Director shall immediately notify the General Counsel of any Proceeding to which the Director has been made or is required to become a participant. The General Counsel, after determining that the Director is eligible for legal representation under paragraph (i), shall obtain legal counsel for the Director at the Authority's expense. Throughout the Proceeding, the General Counsel will maintain a financial oversight of the Director's legal representation to ensure that it is being provided in an efficient and cost effective manner. However, that oversight shall not interfere with or alter the duties of loyalty and representation that legal counsel owes to the Director.

(iii) In the event a Director elects not to accept legal representation provided by the Authority under paragraph (i) and to obtain his or her own counsel in the Proceeding, the Director shall be responsible for the entire cost of such representation, and none of the cost shall be eligible for indemnification by the Authority.

b. *Indemnification.* A Director shall be indemnified and held harmless by the Authority for any judgment or order entered in a Proceeding against and imposing a personal financial liability upon the Director, or for any settlement approved by the Board in a Proceeding that imposes such liability upon the Director, when the judgment or order, or settlement, arises from or is based upon the Director's status as a member of the Board or upon conduct in which the Director engaged while acting as a member of the Board; provided, that such indemnification shall not be provided for a Director in the event an Indemnification Exclusion, as defined in subparagraph (c), is applicable; it is determined, pursuant to subsection (d), that the Director has not satisfied the Standard of Conduct; or the Director refuses to assign to the Authority all claims that the Director has or may have against any person, including an insurer, that arise from or relate to the events or circumstances giving rise to the judgment or order, or settlement, for which the Director is being indemnified.

c. *Exclusions.*

(i) *Legal Representation Exclusions.* A Director shall be not be eligible for legal representation under subsection (a) in any of the following circumstances:

(1) The Proceeding is an Individual Criminal Action in which the Director is charged with a criminal offense based upon the Director's personal conduct, rather than his or her institutional conduct as a member of the Board;

(2) The Proceeding is an Investigative Matter in which a Director is being investigated for having engaged in personal conduct that, if true, would form the basis for an Individual Criminal Action against the Director; or

(3) The *sole* conduct in which the Director is alleged to have engaged and which is the subject of the Proceeding consists of fraudulent or dishonest activities, the intentional misuse of the Director's position as a member of the Board, the intentional violation of a fiduciary or other duty owed to the Authority, or activities undertaken for personal financial gain or the financial gain of members of the Director's immediate family or other relatives;

provided, however, that in the event a Director prevails "on the merits," as defined in subsection (d)(v), of a Proceeding described above in subparagraph (1), (2) or (3) and thereafter satisfies the Standard of Conduct, the Director shall be indemnified for the reasonable legal costs the Director actually incurred in the course of the Proceeding.

(ii) *Indemnification Exclusion.* A Director shall not be eligible for indemnification under subsection (b) for any of the following judgments or order:

(1) Any judgment or order in a Criminal Action; or

(2) Any judgment or order in a Civil Action that is based solely upon any of the conduct described in subparagraph (2) or (3) of paragraph (i).

d. *Standard of Conduct.* A Director shall be required to reimburse the Authority for its cost in providing the Director with legal representation during a Proceeding under subparagraph (a) and a Director shall not be eligible for any

financial indemnification under subsection (b) if the Director does not satisfy the Standard of Conduct when applicable to the Director and as applied in accordance with this subsection. Provisions describing the circumstances in which the Standard of Conduct is applicable, defining the Standard of Conduct, and explaining the manner in which the Standard of Conduct shall be applied are set out below in this subsection.

(i) *Applicability.* A Director shall be required to satisfy the Standard of Conduct whenever the Director's participation in a Proceeding is based, in whole or in part, upon personal conduct in which the Director is alleged to have participated as a member of the Board; the Standard of Conduct shall not be applicable when a Director's participation in a Proceeding is based solely upon other factors (e.g., his or her status as a member of the Board, participation in a vote or other action taken by the Board, or ability to contribute to the Proceeding's fact-finding process (e.g., as witness, deponent, producer of documents)).

(ii) *Standard.* A Director shall be deemed to have satisfied the Standard of Conduct when it is determined that, based upon the circumstances surrounding the Director's conduct that were known or reasonably should have been known by the Director, the Director was acting with both a good faith belief and a reasonable belief that the conduct was within the scope of the Director's duties and responsibilities as a member of the Board and was consistent with the interests of the Authority;

(iii) *Decision-maker.* The determination whether a Director has satisfied the Standard of Conduct shall be made by the Board based upon a majority vote of disinterested Directors or by an independent counsel selected by such members of the Board.

(iv) *Timing.* The determination whether a Director has satisfied the Standard of Conduct is to be made as soon as practicable after the conclusion of the Proceeding in question.

(v) *Effect of Proceeding Outcome.* Except as otherwise provided in this subparagraph, while the outcome of the Proceeding may be a factor in deciding whether a Director has satisfied the Standard of Conduct, it shall not be determinative on this question. Thus, the fact that a Proceeding concludes in a manner that is favorable to, or adverse to, a Director shall not conclusively determine whether the Director, when engaging in the personal conduct that was alleged in the Proceeding, satisfied the Standard of Conduct. However, when a

Director prevails on the merits of a Proceeding other than a Proceeding described above in subsection (c)(i), the Director shall be deemed to have satisfied the Standard of Conduct; prevailing “on the merits of a Proceeding” shall mean that the substance of the claims or allegations made in the Proceeding that were based upon the Director’s personal conduct were considered and were dismissed, denied or otherwise rejected by the Proceeding’s decision-maker and, for this reason, whether in whole or in part, the Proceeding was terminated, the Director was dismissed from the Proceeding, or the Director’s participation in the Proceeding otherwise was ended.

e. *Definitions.*

(i) *Proceeding* means any Civil Action, Criminal Action, Administrative Proceeding or Investigative Matter, as defined below in this subsection, but *excluding* any such action, proceeding or matter that has been filed by the Authority at the direction of the Board and names a Director as defendant or respondent or has been filed or initiated by a federal, state or local government agency at the request of, or as the result of a complaint filed or similar submission made by, the Authority at the direction of the Board, and any Removal Proceeding.

(ii) *Civil Action* means any civil lawsuit filed in a federal or state court that seeks monetary (including damages for bodily injury, personal injury or property damage, or civil penalties), injunctive or other form of relief against a Director or the Authority, and any appeal filed by the plaintiff or petitioner in such a lawsuit from a decision of a court of record; the term does not include an appeal filed by a Director in such a lawsuit (unless, in a particular matter, the Board determines that a Director’s appeal is to be considered a part of the Civil Action).

(iii) *Criminal Action* means any criminal action filed in a federal or state court in which a Director or the Authority is named as a defendant or respondent, and any appeal filed by the prosecuting entity in such a criminal action from a decision of a court of record; the term does not include an appeal filed by a Director in such an action (unless, in a particular matter, the Board determines that a Director’s appeal is to be considered a part of the Criminal Action).

(iv) *Institutional Criminal Action* means a Criminal Action that alleges a violation of criminal law that is based upon conduct of the Authority or of the Board, as a whole, rather than the conduct of one or more particular Directors.

(v) *Individual Criminal Action* means a Criminal Action that alleges a violation of criminal law that is based upon the conduct of one or more particular Directors.

(vi) *Administrative Proceeding* means a process that is initiated by a federal, state or local government agency as the result of a complaint, charge or similar submission filed with the agency by an individual or entity that makes allegations regarding, and that may seek a remedy against, a Director or the Authority, and provides for the agency to consider information presented by the filing party and the Director or Authority, to assist the parties in reaching a resolution of the matter complained about, or to enter a decision on the matter which may be advisory only.

(vii) *Investigative Matter* means any investigation initiated by a federal, state or local government agency that may result in the assessment by the agency or another government agency of a civil penalty, or in the filing by the agency or another government agency of a Civil Action or Criminal Action, against a Director or the Authority.

(viii) *Removal Proceeding* means a civil lawsuit in a federal or state court or any other form of proceeding filed or otherwise initiated by a Director that contests a decision by an appointing official to remove the Director from the Board or filed or otherwise initiated by an appointing official or another person or entity that seeks the removal of a Director from the Board.

f. *Director Removal.* This subsection addresses Removal Proceedings and the Authority's indemnification, if any, of the legal representation costs incurred by a Director in a Removal Proceeding. Removal Proceedings and the legal costs incurred by a Director in connection with a Removal Proceeding are addressed solely by this subsection and not otherwise in this Section 2.

(i) *Written Request.* A Director who wishes to initiate or is the subject of a Removal Proceeding may submit a written request to the Board that the Authority indemnify the Director for the reasonable costs of legal representation the Director will incur in the Removal Proceeding. This written request shall include the following: documents showing the reasons for the decision to remove the Director or the grounds on which the Director's removal is sought; a statement of the reasons for the Director's belief that the removal decision is legally invalid or that the grounds for the removal are legally insufficient; a statement of the reasons for the Director's belief that it is in the best

interest of the Authority for the removal decision to be contested or the request for removal to be opposed; and an identification of any other sources of indemnification, actual or potential, including insurers, that are or may be available to the Director in connection with the Removal Proceeding.

(ii) *Board Referral.* Upon receipt of a request made under paragraph (i), the Board, acting through its disinterested members, shall select an independent counsel and refer the Director's request to that counsel for action under paragraph (iii).

(iii) *Independent Counsel Review and Recommendation.* The independent counsel shall review the written request submitted by the Director to the Board and make such further inquiry as the counsel deems necessary. The independent counsel shall then determine whether approval of the request would be in the best interest of the Authority, shall state in writing the reasons for the determination and, based upon the determination, shall recommend that the Authority approve or disapprove the Director's request for indemnification.

(iv) *Decision.* The Chairman and Vice Chairman of the Board and the General Counsel shall review the determination, the reasons therefor and the recommendation of the Independent Counsel, and shall approve or disapprove the Director's request for indemnification. Any such approval shall be subject to the Director's eventual satisfaction of the Standard of Conduct in accordance with paragraph (vi) below. In the event the Director's request is not approved, the Director shall be responsible for the costs of the independent counsel; if the request is approved, the Authority shall be responsible for such costs.

(v) *Advancement of Costs.* Following a decision to approve the Director's request, the Chairman and Vice Chairman of the Board and the General Counsel, if requested by the Director, may authorize advance payments of legal representation costs to the Director while the Removal Proceeding is pending; provided, that no advance payments shall be made unless the Director enters a written agreement with the Authority in which the Director represents that, with respect to the Director's conduct that is given or alleged as the basis for his or her removal, the Director either did not engage in the conduct or did so in compliance with the Standard of Conduct, and agrees to repay all advance payments made by the Authority if it is later determined in accordance with paragraph (v) that, with respect to such conduct, the Director has not satisfied the Standard of Conduct.

(vi) *Application of Standard of Conduct.* In the event a Director prevails in a Removal Proceeding, the Director shall be deemed to have satisfied the Standard of Conduct, as defined in subsection (d)(ii) above. In the event a Director does not prevail in a Removal Proceeding, that outcome may be a factor in deciding whether the Director, with respect to the conduct that is the basis for the removal, has satisfied that Standard of Conduct, but shall not conclusively determine this question which shall be determined by the Board or an independent counsel selected by the Board.

* * * * *

Adopted: March 4, 1987

Amended: January 8, 1992; April 1, 1992; September 6, 2000; January 3, 2001; June 5, 2002; August 8, 2007; April 20, 2011; January 4, 2012; February 15, 2012; October 17, 2012; January 16, 2013; and March 20, 2013.