

HOW NOT TO RUN A FOUNDATION

Lessons learned from:

The People of the State of New York

v.

Donald J. Trump, Donald J. Trump, Jr., Ivanka Trump and Erik F. Trump, and The Donald J. Trump Foundation

The logo for Lane Powell, featuring a large, thin white arc that starts above the text and curves around it to the right.

LANE POWELL

Our Panel

Jeff Bird

Shareholder and Business Transitions
Team Chair, Lane Powell



Jeff is a transactional business lawyer with more than 25 years of experience representing public and private businesses in complex business transactions and securities matters. He counsels businesses of all sizes in mergers and acquisitions, public and private securities offerings, tender offers, proxy contests, divestitures for public and private companies, corporate finance and governance, securities law and venture capital transactions. Jeff has extensive knowledge of SEC compliance matters and regularly advises public companies on corporate governance issues and SEC periodic reporting requirements under the Securities Exchange Act of 1934. He advises and works closely with boards of directors, board committees, special committees and management.

Our Panel

Janet Knauss Larsen, J.D.
Shareholder, Lane Powell

Janet Larsen represents businesses and individuals in all aspects of business and commercial litigation and dispute resolution, including matters in state and federal courts throughout the country, and in multi-district litigation matters. She also provides tailored business and risk mitigation advice to clients in multiple industries.

Janet's practice focuses on disputes involving: business torts/contract dispute; corporate governance issues/shareholder disputes; fiduciary liability of officers, directors, trustees and other professionals; construction litigation; insurance litigation; trusts and estate litigation; securities litigation; investment adviser liability in all types of proceedings; and real estate and land use disputes.

Janet received her J.D. from Lewis & Clark Law School and her B.A. from Whitman College. She is a former Chair and current Executive Committee Member of Oregon State Bar Association's Business Litigation Section. Janet also serves as a Board Member for the Federal Bar Association's Oregon Chapter.



Our Panel

Karen E. Hobson

Counsel to Lane Powell

Karen Hobson advises individuals and high net worth families in estate planning and administration, and assists clients with tax planning, business transactions and succession planning. She is experienced in the preparation of wills, trusts and other estate planning documents, and provides strategic tax and legal advice to help her clients reach their business goals. Karen regularly assists clients in the creation and development of estate plans through the assessment of assets and goals, and understands complex tax and entity planning including the use of grantor trusts and family limited liability companies. She also has experience advising on pre-formation planning, entity formation, corporate governance, mergers and acquisitions, contractual interpretation issues and business succession planning.



THE NEW YORK ATTORNEY GENERAL



- Very Aggressive Prosecutorial Office
- Past Victories and Actions
- Political Overtones
- Reasons for Attorney General bringing the action

- The Pleadings of the Case
 - Verified Petition of the Attorney General
 - Defendant's Motion to Dismiss
- Nature of our Presentation

WHAT IS THE DONALD J. TRUMP FOUNDATION ("FOUNDATION")?

- Founded by Mr. Trump in 1987.
- A private foundation under Section 509(a) of the Internal Revenue Code.
- Stated mission: "Receive and maintain a fund ... to [be] used exclusively for 'charitable, religious, scientific, literary or educational purposes.'"

THE “FOUNDATION” FACTS

- Mr. Trump served as President from the Foundation’s inception until January 23, 2017 (three days after the inauguration).
- Board of Directors: Mr. Trump, Ivanka Trump¹, Eric Trump, and Donald Trump Jr.
- The Foundation has no employees.
- The Foundation delegated authority over its operations to the accounting office of the Trump Corporation, Inc., a management company owned by Mr. Trump.
- As of December 31, 2016, the Foundation reported to the IRS assets of \$1 million.
- The Foundation’s funds have been scrutinized because donations come from Trump’s business partners rather than the Trump family.

¹Ivanka stepped down as a Board member as of January 23, 2017.

THE UNDERPINNINGS OF THE LAWSUIT

- On November 22, 2016, The Washington Post published an article titled, "Trump Foundation admits to violating ban on 'self-dealing,' new filing to IRS shows."
 - The article revealed a host of confirmed and potential legal violations involving the Foundation.
- Then-New York State Attorney General Eric T. Schneiderman investigated and then ordered the Foundation to cease soliciting donations in New York.
- On June 14, 2018, the New York State Office of the Attorney General issued a press release titled, "Attorney General Underwood Announces Lawsuit Against Donald J. Trump Foundation And Its Board Of Directors For Extensive And Persistent Violations Of State And Federal Law".

THE LAWSUIT ALLEGATIONS

- “Improper and extensive political activity”
 - The Foundation’s Board “knowingly permitted” it to be “co-opted by Mr. Trump’s presidential campaign.”
- “Repeated and willful self-dealing/related party transactions”
 - The Foundation ceded control over grants to the Trump campaign and the Trump campaign determined when and who would receive grants, and timed gifts to benefit campaign.
 - Mr. Trump and the Foundation are accused of a wide array of “self-dealing transactions,” and transactions designed to serve Mr. Trump rather than the Foundation.

THE LAWSUIT ALLEGATIONS (CONTINUED)

■ “Failure to follow basic fiduciary obligations”

- Mr. Trump and family failed to discharge duties as directors with the degree, skill, prudence, diligence, and undivided loyalty required of them.
- The suit accuses the Foundation of being “little more than an empty shell,” with Mr. Trump running the Foundation “according to his whim, rather than the law,” individually approving grants and disbursements with no oversight from Board members.
 - No employees.
 - No oversight of Trump Organization staff running Foundation.
 - No annual board meetings.
 - The Board has not met since 1999.

RELIEF SOUGHT IN THE LAWSUIT

- Seeks to bar Mr. Trump from serving on the leadership of any charitable organization operating in New York for 10 years.
- Seeks to bar Eric, Donald Jr., and Ivanka from serving on the leadership of any charitable organization operating in New York for one year.
- Seeks \$2.8 million in restitution and damages.
- Seeks an Order against Mr. Trump to repay the Foundation for up to double the amount of benefits he obtained after July 1, 2014—a sum of millions.
- Seeks to dissolve the Foundation and to cooperate with the Attorney General's office in disbursing remaining funds it possesses.
 - Mr. Trump had already announced his intention to dissolve the Foundation and he has already paid more than \$330,000 in reimbursements and penalty taxes since 2016.

RELEVANT OREGON STATUTES

- ORS 128.610-128.769, Charitable Trust and Corporation Act.
 - Applies to “all charitable organizations holding property for charitable purposes over which the state’s Attorney General has enforcement or supervisory powers.”
- ORS 130.000-130.910, Uniform Trust Code.
- ORS 65.001-65.990, Nonprofit corporations.

OREGON LAW CONTINUED – CHARITABLE PURPOSE

- “Charitable Purpose” broadly defined by statute:

Any purpose to promote the well-being of the public at large, or for the benefit of an indefinite number of persons, including but not limited to educational, literary, or scientific purposes, or for the prevention of cruelty to children or animals, or for the benefit of religion, rehabilitation services, public recreation, civic improvement, or services which lessen the burdens of government. ORS 128.630(1).

CHARITABLE PURPOSE EXPLAINED

- “The principal and distinctive characteristics of charitable institutions are that they ‘derive their funds mainly from private and public charity and hold them in trust for the object of the institution’.”
- In other words, the test of whether an enterprise is charitable is whether it exists to carry out a purpose recognized in law as charitable, or whether it is maintained for gain, profit, or private advantage.” *Hamilton v. Corvallis General Hospital Ass'n.*, 146 Or. 168, 185; 30 P.2d 9 (1934).

OREGON LAW CONTINUED – MANDATE COMPLIANCE WITH IRS RULES

- ORS 128.318 acknowledges the need to comply with duty of loyalty and to manage and invest an institutional fund and act in good faith and with the care of an ordinary prudent person in a like position under similar circumstances.
- ORS 128.085 expressly requires compliance with Internal Revenue Code provisions related to the administration of private charitable foundations, and the provisions prohibiting self-dealing set forth in IRC section 4941(d).

ENFORCEMENT PROVISIONS

- ORS 128.675 and ORS 128.866 allow the state's Attorney General to:
 - Investigate breaches of fiduciary duty;
 - Place conditions on or enjoin activities of charitable corporation/trust for breaches of fiduciary duties;
 - Seek penalties against the charitable corporation or its officers and directors; and,
 - Remove or hold the officers and directors responsible, among other things.
- ORS 128.735 provides the Court the authority to award attorneys' fees against a charitable organization or charitable fiduciary in *any suit or action* to enforce any fiduciary duty or other duty arising under statute or common law.

FIDUCIARY EXPLAINED

"[T]he heart of a [corporate] fiduciary's duty is an attitude, not a rule. 'The fiduciary best fulfills its duties if it approaches them with the attitude of seeking the beneficiary's interests rather than the personal interests of the fiduciary[.]'"

FIDUCIARY FURTHER EXPLAINED

"Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A [fiduciary] is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. * * * Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions * * *. Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd."

Meinhard v. Salmon, 249 N.Y. 458, 464, 164 N.E. 545 (1928), quoted in *Klinicki v. Lundgren*, supra, 298 Or. at 684, 695 P.2d 906. (Emphasis supplied.)

RELATIONSHIP DEFINES DUTY

- The nature of the relationship typically dictates the scope of the fiduciary's duty; but all fiduciaries must act in good faith, with loyalty, and with full, fair and frank disclosure.
 - *Lindland v. United Business Investments, Inc.*, 298 Or. 318, 322, 693 P. 2d 20 (1984)(real estate broker owes a duty of "full fair and frank disclosure.");
 - *United States Nat'l Bank v. Guiss*, 214 Or 563, 583, 331 P.2d 865 (1958) (trustee owes a duty of "utmost good faith" and "undivided loyalty.");
 - *Pereira v. Thompson*, 230 Or. App 640, 654-656, 217 P.3d 236 (2009) (distinguishing a fiduciary duty claim against a lawyer from the standard of care applicable to a negligence claim against a lawyer, confirming that an attorney owes a client a duty of loyalty, good faith, and fair dealing, which is the concern of a breach of fiduciary duty claim.);
 - *Chiles v. Robertson*, 94 Or. App 604, 619, 767 P.2d 903 (1984) (majority shareholders of a close corporation owe minority shareholders duties of "loyalty, good faith, fair dealing and full disclosure."); and,
 - *Klinicki v. Lundgren*, 298 Or. 662, 666, 695 P.2d 906 (1985); see also 12B Fletcher, Cyclopedia Corporations § 5811 (perm ed 1984); § 838 (rev ed 1986) (directors and senior executive officers of corporations owe fiduciary duties of loyalty, good faith, fair dealing and full disclosure.)

DUTIES OF A TRUSTEE

- The duties of a board of directors (or Trustees) of a charitable corporation are guided by the duties of a Trustee:
 - Trustees have a duty to administer the trust property “in good faith, in accordance with its terms and purposes” and solely in the “the interests of the beneficiaries.” ORS 130.650; 130.655.
 - A Trustee owes a duty to apply the assets and income of the trust to the particular objectives of the trust; it is a duty that cannot be delegated to others. *Restatement (Second) of Trusts* § 348 Comment, p. 211 (1959).
 - Trustees owe a duty to inform and report. ORS 130.710.
 - The duty of loyalty applies and prevents self-dealing and transactions that place the Trustee’s own interests over those of the beneficiaries.
 - Even if a trust instrument allows a Trustee to consider his/her own interest (i.e. includes an exculpatory clause), a Trustee must give consideration to the interest of the beneficiaries and determine whether the transaction is fair to them. *Mest v. Dugan*, 101 Or. App. 196, 790 P. 2d 38 (1990).
 - A Trustee that, as a result of lack of due care, disposes of an asset for less than could reasonably be obtained in the open market violates its duties. *Id*; *Hatcher v. U. S. Nat. Bank of Oregon*, 56 Or App 643, 643 P.2d 359 (1982).

STATUTORY DEFINITION OF CONFLICT OF INTEREST

- ORS 65.361, “Director conflict of interest”:
 - A transaction with the corporation in which a director of the corporation has a direct or indirect interest.
 - *See* ORS 65.364 and 65.367 for specific transactions expressly prohibited in non-profit corporation context related to loans or guarantees involving directors or officers and unlawful distributions.

CONFLICTS OF INTEREST/SELF-DEALING DEFINED

- Section 4941 of Internal Revenue Code: Self-dealing defined to embrace the following if interested or related parties involved:
 1. Sale, exchange, or leasing of property;
 2. Leases (but see Certain Leases, under Exceptions to Self-Dealing);
 3. Lending money or other extensions of credit;
 4. Providing goods, services, or facilities;
 5. Paying compensation or reimbursing expenses to a disqualified person;
 6. Transferring foundation income or assets to, or for the use or benefit of, a disqualified person; and,
 7. Certain agreements to make payments of money or property to government officials.

CONFLICTS OF INTEREST/SELF-DEALING EXPLAINED

“‘Conflict of interest’ encompasses situations in which the agent is acting entirely or substantially for the agent's own benefit and situations in which the agent is acting on behalf of a third party whose interest is adverse to that of the principal”.

BREACHES OF DUTY OF LOYALTY

"[C]onflict of interest or self-dealing is a breach of duty [of loyalty]." *Synectic Ventures I, LLC v. EVI Corp.*, 353 Or. 622; 94 P.3d 478 (2012); *see also* Restatement (Third) of Agency § 8.03 (2006) (duty of loyalty includes duty not to deal with principal either as adverse party or on behalf of adverse party).

CONFLICTS OF INTEREST/SELF-DEALING

- Common law of agency is a guide:
 - “In the agency context, the term ‘conflict of interest’ encompasses situations in which the agent is acting entirely or substantially for the agent's own benefit and situations in which the agent is acting on behalf of a third party whose interest is adverse to that of the principal.” *Synectic Ventures I, LLC v. EVI Corp.*, 353 Or. 62, 294 P. 3d 478 (2012); citing *Lindland v. United Business Investments*, *supra*, 298 Or. at 322.

CONFLICTS OF INTEREST/SELF-DEALING

■ What happens when a fiduciary “self-deals”:

- Authority is questioned because an agent ordinarily lacks authority to act on behalf of a principal in a transaction in which the agent has a conflict of interest. See *Fine v. Harney Co. National Bank*, 181 Or. 411, 447–48, 182 P.2d 379 (1947) (“It is an established principle of the law of agency that an agent cannot bind his principal in a matter in which his own interest conflicts with the duty he owes his principal.”).
- 1 Mechem on Agency (2d ed) 535, § 754: “It is often said that his endeavor to [engage in self-dealing] operates as an immediate revocation of his authority. That an agent undertakes to do so is therefore enough to put the other party on his guard.”
- If the charitable organization has officers or directors and runs like a corporate entity, the “business judgment rule” or insulation of liability that may otherwise apply will no longer insulate those officers or directors from liability.
- When self-dealing exists in the corporate context, the burden of proof shifts to the fiduciary to establish that the transaction is fair to the organization; did not result in harm to the organization or that, the fiduciary fully disclosed the conflict and obtained consent from the affected parties.
- In the trust context the fiduciary has the burden to show that the fiduciary considered the beneficiaries’ interest and that the transaction is fair.
- Statutory violations are likely to result, the character of the charitable organization may be questioned and substantial excise taxes could result from the self-dealing transactions.

ALLEGATIONS OF “WASTE” BY NEW YORK ATTORNEY GENERAL



- \$2.8M in charitable assets used for political activities
- \$100,000 in charitable assets used to settle Mar-A-Lago legal dispute
- \$158,000 in charitable assets used to settle legal dispute against a Trump Golf Club
- \$10,000 in charitable assets used to purchase Trump self-portrait

WASTE IN OREGON



- “Waste” not defined in Oregon statutes
- Typical Examples:
 - luxury travel
 - vacations
 - personal apartments
 - expensive meals
- Judicial Dissolution because of waste—ORS 65.661

WHY NONPROFITS ARE SUSCEPTIBLE TO MISUSE OF ASSETS



- Less stringent controls than for-profit counterparts
- More trusting of employees
- Do not have the personnel necessary to implement procedures
- Lower pay (expectations and responsibilities are high)
- Minimal training

NONPROFIT GOVERNANCE



- Fiduciary Duties
 - Duty of Care
 - Duty of Loyalty

- Statutory Requirements
 - Certificate of Incorporation
 - Annual Meeting and Reports

NONPROFIT GOVERNANCE (CONT'D)



- Board Composition
 - Independent Directors
 - Time for the Job
- Oversight Responsibilities – The Basics
 - Grant Approval
 - Investment Policy
 - Conflict of Interest Policy
 - Criteria for Making Grants

- Corporation Formalities
 - Meetings
 - Minutes
 - Approvals
 - Policies
 - Oversight Documentation

Lessons Learned

- Have a Functioning Board
- Exercise Oversight Responsibility
- Take Corporate Formalities Seriously
- Review and Understand Certificate of Incorporation Prohibitions



Nonprofit and Political Activities Generally Do Not Mix



INTERNAL CONTROLS AND BEST PRACTICES



- Segregation of duties
- Conflict of interest policy
- Strong policy against fraud
- Encourage whistleblowing
- Background checks

Considerations		
	Donor Advised Fund	Private Foundation
Start-up Time		
Start-up Cost		
Required Distributions		
Excise Taxes		
Privacy		
Administrative Responsibilities		



QUESTIONS?

TRUSTED
COUNSEL.
ADVOCATES.
ADVISORS.