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Legal Pitfalls and Pratfalls in OVERSEAS VENTURES

BY MARTIN MICHAELSON

"THE FISH," A PROVERB SAYS, "IS THE LAST TO see the water." Universities in this country are hardly novices in international initiatives, yet overseas projects today, although enticing, often seem novel to them, long experience notwithstanding.

TAKEAWAYS

1 Several motivations, including visions of major revenue enhancement, are driving increased attention to proposed overseas teaching, research, and service ventures by American universities.

2 The increased urgency with which universities' overseas initiatives are being pursued is not always matched by rigorous attention to potential pitfalls, even at institutions with previous international experience.

3 Proper research, effective risk-management, and establishing a workable governance mechanism can help ensure the success of universities' overseas ventures.

The early U.S. colleges and universities, offspring of English, Scottish, and German institutions, promptly reached back across the ocean. Four members of Harvard's first graduating class took advanced degrees overseas, at Padua, Leyden, Oxford, and Dublin. Some 19th-century American scholars conducted sponsored research around the world. By 1958, a survey found, 184 U.S. universities were conducting 382 programs overseas. Higher-education institutions with the word "American" in their name long have functioned, often in concert with U.S. institutions and U.S. faculty members, in such places as Thessaloniki, Bulgaria, Cairo, Beirut, and Paris. For many years nearly every university in this country has had extensive links abroad.

Lately, though, attention to proposed international teaching, research, and service ventures, some of them very large-scale, has taken on new urgency at American universities. Prevailing interest in such efforts among university leaders can be ranked on a continuum from animated curiosity to seemingly heedless frenzy. University presidents and boards fear being left behind in the rush they perceive toward global expansion.

A number of motivators drive the new zeal to go overseas. Among these are a resolve to stay competitive in this era of heightened inter-institutional competition; visions of major revenue enhancement, intensified by the recent shocking drop in endowments and a year-long recession; a desire to enhance the institution's "brand value"; and rapidly increasing transnational intellectual exchanges and collaborations in many disciplines, spurred by, among other factors, the Internet, the trend toward free trade, the rise of service economies, and the mounting complexity and cost of science research.

Such prods as those are amplified by pressure from students and faculty members to visit, learn from, teach, and help a world many believe has ceased being spherical and has become flat. These days, only the most confident university fiduciaries have sufficient fortitude to risk being left behind in international outreach.

Today for many universities the Middle East beckons, sometimes seductively. Europe, including Eastern Europe, appears programmatically attractive and relatively safe. The door to China's vast population, 300 million of whom are presently studying English, looks more open. And opportunities await in parts of South Asia, South America, and even, such as for biological-sciences research, Africa.

As a partner in the higher-education practice of a law firm with 27 offices around the globe, who with colleagues from Washington to London to Beijing has worked on a great many international transactions for university clients, I can testify that the world of university transnational initiatives, far from being flat, is bumpy and resembles no conventional shape. Colleagues and I have seen at close hand why even universities with long experience in international research, teaching, and service often find the terrain so unfamiliar and dangerous, and why the institutions are sometimes prone to err.

Although apparently no comprehensive study has shown the ratio of successful to failed international ventures of universities, and although most of the ventures seem neither big successes nor complete failures, disappointing outcomes have been numerous. Many universities seem to tolerate suboptimal outcomes in this area, perhaps because the institutions hesitate to acknowledge that they've not done well, and perhaps because they willingly pay a heavy price for the prestige and the "learning experience" even sub-standard performance in the international field is thought to bring.

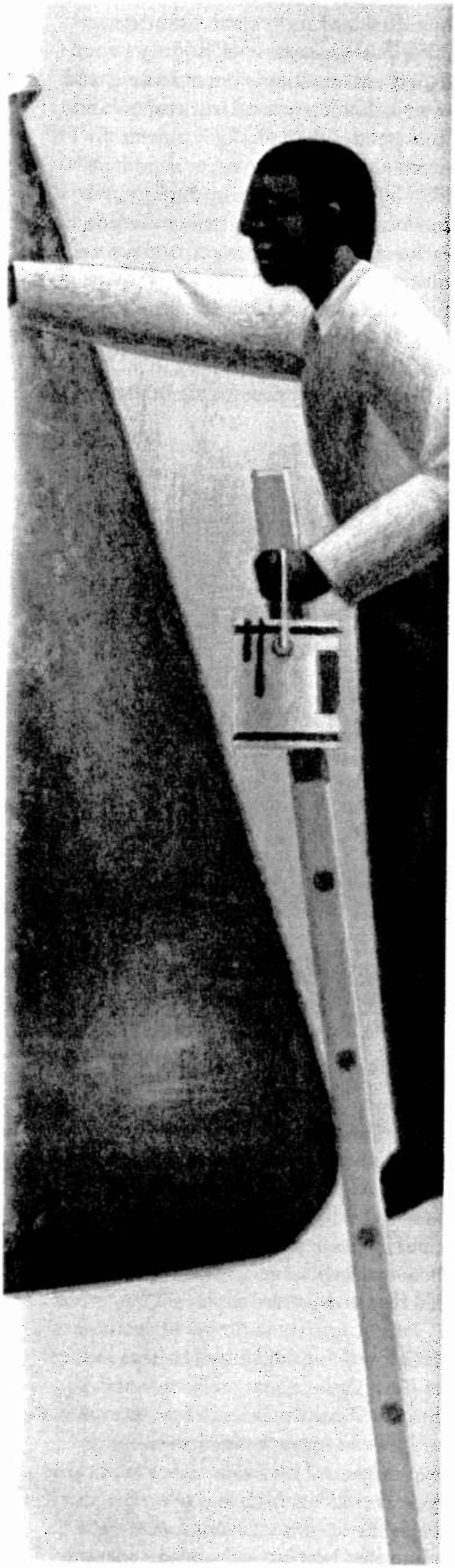
Outcomes of university overseas initiatives can and should be much better in many cases. Attention by fiduciaries to issues such as those flagged here—especially as the go/no-go point approaches on proposed ventures and at the formative stage of new ventures—can be exceptionally valuable.

Set out below are some key examples, from a lawyer's perspective, of costly mistakes universities should do their best to avoid in pursuit of new international activities. The list is merely illustrative. Not every point applies to all types of international activities. From these examples, though, perhaps presidents and trustees can draw useful inferences on such issues as how development and management of these activities should and should not be staffed. Mistakes to avoid:

Failure to appraise rigorously potential partners. Bad outcomes of universities' international academic transactions frequently can be traced to what hindsight clearly shows to have been unsuitability of the foreign partner. Institutions too often plunge into advanced exploration, planning, and consummation of overseas ventures before they've conducted careful due diligence on the parties with whom they are proposing to deal or are already dealing, whether those parties are foreign institutions, foreign individuals or companies, or middlemen.

This lack of appraisal seems especially to figure where a senior official of the institution, such as the president, has met and been initially impressed by the foreign entity or foreign persons involved. Subordinate administrators hesitate to second-guess what they see as a judgment of suitability made, or implicitly made, by an official high in their chain of command, even when that apparent judgment is based on scant, if any, confirmed facts.

Productive and, considering the scope of the transactions, inexpensive resources are available to institutions for vetting early in the exercise the persons and entities with whom they propose to deal. These resources include, for instance, thorough checking of publicly available, and often Internet-searchable, data and evidence of pertinent experience. Usually consideration should be given to engaging one of the specialized investigative firms experienced in digging privately and deeply into the backgrounds of foreign parties, including their record of fomenting and resolving lawsuits and other disputes; their pertinent business experience and reputation; and their finances. Properly instructed, the inves-



tigative firms can minimize the potential for awkward "blowback" to the parties under review.

Conventional reference checking is not feasible in some international transactions but should be considered and pursued when it may yield useful information. Too, there is often a greater hesitancy to ask basic questions of foreign entities and persons than of U.S. entities, due to a generally unwarranted belief that application of ordinary business norms will be construed as discourtesy or arrogance, or will betray an embarrassing extent of ignorance.

retrenchment on many campuses. International initiatives are an unrelenting drain on administrative capacity in the implementation, not merely the formative, phase. Although some universities, notably some of the best financed, have senior administrators whose only or main job is to identify, form, and manage international relationships, that model is not common; and even at those institutions, assigned administrators are usually burdened already. Presidents and boards should ask themselves whether the diversion of administrative attention from existing priorities to a contemplated

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Failure to gauge whether the U.S. institution's domestic operations are sufficiently under control that it is capable of launching proficiently the international venture. University administrations are spread thin. Administrators, under chronic stress to repair and maintain existing programs and services, are hard-pressed to find time for new ones—especially during this period of budget-cutting and overseas project can be justified and what the likely consequences are of the redirection of administrative time. Other considerations in this vein may figure as well. For instance, are faculty-administration relations sufficiently healthy to ensure that faculty members' involvement in the initiative will be well navigated or will the initiative probably entail painful and costly collisions with the faculty?

Failure to determine in advance that the institution has commitment and means to see the initiative to fruition. This shortfall, related to the prior point, is far from rare. A university may thoughtfully address the effort that starting a venture will entail, and yet not account for the often greater and more intense effort that will be required to run it for five or 10 years. Some universities have discovered, for example, that recruitment of faculty members can be easier at the beginning of an overseas venture than years into it. The fresh and exciting can in time appear to university personnel as old, laborious, and a headache. These considerations underscore the need to negotiate at the outset satisfactory rights to terminate overseas programs.

Failure to supervise adequately principal investigators and senior administrators responsible for the overseas operation. Some recent scandals in human-subjects research overseas by U.S. universities exemplify one kind of deficient institutional oversight. Other examples involve situations in which university managers posted abroad—some of them foreign nationals, others from the U.S.—run programs there in a virtual administrative vacuum and are effectively unaccountable. Tied to that pattern is the following mistake.

Failure to apply robust internal controls and academic, as well as administrative, supervision to the international operation. Management of disasters large and small at distant outposts has been a bane of multinational organizations since at least ancient Roman times. Universities already have plenty of trouble keeping a watchful eye on the local campus. To superintend a clinical trial conducted thousands of miles away, a contract to reform a foreign government's central banking system, or an instructional program for students on another continent is trying and fraught with risk. Universities too often enter international arrangements without thoroughly identifying the "what if" issues and without designing and staffing effective risk-management.

Failure to assure a workable governance mechanism for the venture. Foreign initiatives involving multiple operational parties that have never before worked together tend to be tricky to manage. Contract terms that lay out a management structure are of little benefit if the governance terms are ambiguous, overly complex, or impracticable. Ambiguous governance structures tend to result from ill-conceived compromise in deal negotiations. Too, a governance construct is only as good as the people who run it; the university that cedes to its foreign partner authority over appointment of management personnel is begging for trouble. Grief is minimized when the governance arrangement marries, rather than divorces, authority and responsibility.

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Failure to take local law into painstaking account in planning the venture. Amazingly, some universities enter substantial transactions for operations in foreign countries before they address the laws that apply there. Trouble usually follows. Although some local legal issues can be identified by attorneys in the U.S., retention of counsel in the foreign country involved is a sensible and basic step. Local counsel should be checked in depth to ensure their fitness for the role. For instance, many otherwise qualified lawyers in some countries are notoriously incapable of holding a confidence, exasperatingly unresponsive, and more beholden to local institutions and local politics than to a U.S. university. Attention should be paid to an array of local legal issues, from immigration to intellectual property to real estate, educational licensure, taxation, and, by no means least, employment law. Institutions have been surprised to learn belatedly, for instance, that in some nations and circumstances termination of personnel is very costly and entails protracted reviews. Universities that don't see in advance the local legal landscape expose themselves, among other risks, to loss of their exclusive rights to use their trademarks in a foreign country and can be needlessly subjected to uninsured liability to overseas employees.

Failure to prepare for application of U.S. law. A host of United States laws and regulations bear on foreign activities of U.S. universities. A few examples are laws on corrupt practices overseas, export-control laws sometimes applicable to academic research and to exported equipment, laws on foreign politically motivated boycotts, economic-sanctions laws against various countries, and, to the extent applicable overseas, U.S. anti-discrimination laws. Because inattention to strictures of this type can stop a foreign initiative in its tracks and result in messy investigations by the U.S. government, these rules-of-the-road should be considered before, not after, a deal is struck. Further, protective compliance-with-law provisions, which in some contexts must be delicately negotiated, should be included in contracts.

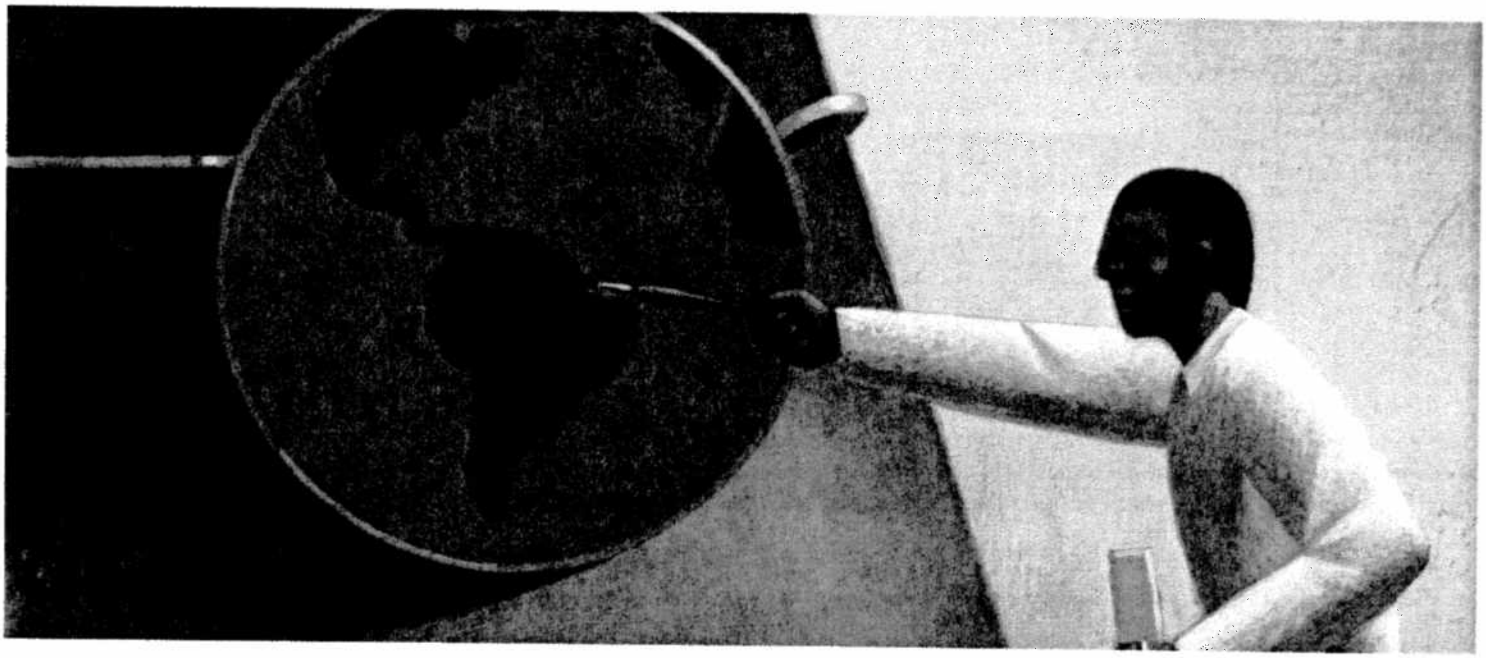
Failure to plan effectively for disputes. Although dispute-resolution terms are regularly included in universities' foreign-venture agreements, institutions need to be comfortable that when frictions arise, the provisions will actually work. Counsel can advise on a range of possible ways dispute resolution can be addressed, but the institution should examine whether these arrangements make sense from a conduct-of-business standpoint and are not just rights to declare war when all else has failed.

Failure to stay ahead on cash flow. Experience shows that the leverage a foreign partner has if favorable cash-flow arrangements are not in effect is likely to harm the university sooner or later.

Failure to resolve satisfactorily currency-conversion and foreign-currency payment terms. This issue, which has afflicted a number of universities' foreign projects, manifests in various ways. For instance, laws of some countries impede or forbid expatriation of revenues generated in-country. Counsel or an accounting firm often can advise on strategies to address that problem. Another issue likely to be consequential in the period ahead, in which currency fluctuations will probably be especially volatile, is how to reduce risk incident to major change in the value of the dollar relative to local currency. Banks today tend to charge outlandish premiums to hedge against swings in currency valuations. Here, too, a risk-reduction strategy should be identified early in consideration of the transaction.

Failure to gauge in advance whether, to what extent, and in what circumstances the institution's lead personnel overseas are reliable. A highly experienced colleague, when asked to identify key risks for universities in overseas ventures, offered this: "1. Deferring to the judgment of university representatives on the ground in the foreign country.
2. Not deferring to their judgment.
3. Not being able to tell whether you are making mistake #1 or mistake #2." Persons sent overseas by universities should be known quantities to the institution's senior officials. If the institution cannot confidently rely on judgments of its ambassadors, who are time zones away and who usually lack extensive staffs to consult on weighty matters, administrative Russian roulette is a foreseeable result.

In sum: Risk management entails multiplication of the probability of an adverse event times the magnitude of the event. Universities' overseas initiatives call for rigorous risk management, the more so because proponents of these ventures accentuate the positive, while those who review the ventures may be insufficiently alert to some of the major risks. ■



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T'SHIP LINKS: Richard A. Skinner, "It IS a Small World After All: Globalization of Higher Education." March/April 2008.