A Guide to the Board's Compliance Oversight Duties

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One of the most crucial of all fiduciary duties of the hospital or health system board member is to exercise oversight over the effectiveness of the organization's corporate compliance activities. Healthcare is one of the most heavily regulated industries, on both a federal and state level.

THIS IS ESPECIALLY THE CASE given the dramatic anti-fraud changes implemented by the seismic Patient Protection and Affordable Care Act (PPACA). Violations of related law and regulations potentially expose not only the organization but also its key officers, executives, and (in the extreme) board members to a broad array of painful civil and criminal penalties and reputational harm. Exposure to such risks can be dramatically reduced through organizational commitment to an effective corporate compliance plan. Board members have explicit fiduciary and related obligations with respect to the implementation and operation of such plans. Board members' informed and attentive exercise of these duties can contribute materially to lowering the organization's compliance risk profile. In other words, compliance oversight is one area of governance responsibility where the board can make a real, positive contribution to the organization and its mission.

> Increased compliance education for the governing board is the "smart play"—both for the board, and for the organization.

The purpose of this special section is to brief board members on the essentials of their compliance oversight duty: what it provides, how it is practically implemented, how it can work to benefit the organization, the view of the enforcement agencies, new interpretive developments, and the risks associated with board oversight failures. Through the following discussion, we aim to better prepare board members to carry out this very important fiduciary obligation on behalf of their hospital or health system.

What's the Big Deal?

Surely, this isn't the first time you've heard about compliance! You've probably been subjected to countless discussions of compliance issues at board meetings. So why raise the issue now? Why devote special attention to the issue? Because compliance, as an element of the board's fiduciary duty, is again a *hot, hot, hot topic*.

Why? Because expectations of board conduct are dramatically increasing in a healthcare reform environment, where policy powers are working to bend the quality curve up and the cost curve down. The traditional healthcare financing model has been turned upside down by the concept of "accountable care." This new policy initiative is designed to restructure the means by which healthcare is paid for, and provided, in order to enhance cost efficiency, patient outcomes, and patient satisfaction.

With the emphasis on accountable care comes a corresponding decrease in regulatory tolerance for oversight lapses, particularly those that involve significant interference with patient freedom of choice or reduction in the quality of care provided to patients. New compliance plan-related requirements are being introduced on a consistent basis. The PPACA incorporates several significant new anti-fraud and abuse enforcement provisions with direct implications for hospitals and other healthcare providers. There is also a disquieting new emphasis by the government on individual accountability for compliance violations, particularly with respect to officers and key managers who, by virtue of their organizational title, may have been in a position to prevent the violation (but did not). In such an evolving environment, it is vitally important that board members remain attentive to their oversight duties, so that they can more effectively serve the organization. In other words, increased compliance education for the governing board is the "smart play"—both for the board, and for the organization.

The Regulators' Perception

Health industry regulators place great value on a vigorous board compliance function, in addition to an effective corporate compliance plan. To regulators, compliance plans demonstrate a hospital's commitment to "honest and responsible conduct."[1] Further, they represent a "good faith effort" to comply with relevant law and federal healthcare program requirements, and materially reduce the risk of illegal activity and corresponding sanctions.[2]

To the regulators, compliance plan effectiveness is dependent in large part on the good faith and meaningful support of the governing body. The stronger the compliance commitment of the board, the more likely the underlying compliance plan will be effective.[3] Evidence of such a commitment may include active board leadership on compliance matters; attentiveness to specific compliance issues coming to the board's attention; allocation of sufficient resources; and support for

1 HHS OIG Supplemental Compliance Program Guidance for Hospitals, 70 F.R. 4858 (January 31, 2005).
2 Ibid.
3 Ibid.

the authority, autonomy, and accountability of organizational compliance staff.[4]

Department of Health and Human Services (HHS) Inspector General Daniel Levinson has repeatedly expressed in public comment his appreciation for board attentiveness to compliance matters.[5] He describes the "best boards" as those that are active, questioning, and "don't shy away" from asking the tough questions. He has called for more board "engagement," which might fairly be interpreted as a call for more attentiveness (especially on compliance matters). Notably, Levinson suggests that there be greater governance involvement in quality-of-care compliance matters. He encourages boards to take a leadership stance on these matters, and not to be overly deferential to medical personnel simply because as board members they may lack a medical background. This is particularly the case with respect to evaluating data regarding mortality rates, hospital infections, or medical errors. An "outsider's view" may actually position board members to more clearly spot negative quality-of-care trends.[6] In this regard, the inspector general's emphasis is consistent with the increasing compliance implications of healthcare outcomes, as the federal government links Medicare and Medicaid reimbursement to patient quality matters, both in terms of monetary rewards and penalties. Hence, while Levinson clearly "wants boards to succeed," he may be signaling that the time is right for boards to reevaluate the vigor with which they exercise compliance-related oversight.

Of course, an effective plan focuses on *all* laws materially affecting the hospital's legal risk profile, not just those relating to fraud and abuse, Stark, reimbursement, and the like. Compliance with, for example, the antitrust laws, IRS regulations, licensing, document retention, and myriad other significant risk areas may appropriately be covered by an organization's compliance plan.

The Essentials of the Duty

The director's oversight obligation is centered in the core fiduciary duty of care. This duty refers to the obligation of the governing board to carry out its responsibilities in "good faith,"[7] with the level of care that an ordinarily prudent person would exercise in similar circumstances, and in a manner he/she reasonably believes is in the best interests of the hospital or health system.[8] Thus, the duty of care subsumes the traits of attentiveness and diligence. The duty of care has two fundamental elements:

- The *judgment element:* the application of duty of care principles to situations in which the board is called to exercise judgment (e.g., a vote, or similar action).
- The *oversight element:* the application of duty of care principles to the obligation of the board to exercise oversight of executive leadership—to ensure it is responsive to its management duties in a manner consistent with applicable law. In essence, it is the obligation to "keep a finger on the pulse of what's going on."

Board members' obligation for compliance plan oversight specifically arises under the oversight element. A series of leading Delaware court decisions describe the obligation as an attempt in good faith to ensure both a) the existence of a corporate information and reporting system (i.e., a compliance plan) that the board concludes is adequate, and b) that this system/plan is sufficient to ensure that appropriate information regarding organizational compliance with applicable laws will come to the board's attention in a timely manner and in the ordinary course.[9] In sum, this "Caremark" standard requires the board to ensure that an effective compliance plan both is in place and works to make sure compliance plan information gets to the board in enough time to allow it to take responsive action.[10]

The *Caremark* cases recognize that there is no "one-size-fits-all" information system/compliance plan (i.e., the level of detail that is adequate for such a system/plan is the board's "call" or a matter of its informed business judgment). Yet, most compliance plans follow the template standards for an "effective compliance and ethics program" as maintained by the United States Sentencing Commission in its Federal Sentencing Guidelines Manual.[11] The manual sets forth seven specific elements of what the Sentencing Commission describes as the elements of an effective compliance and ethics program. Most healthcare organizations also incorporate within their plans supplemental compliance program guidance promulgated in regulations issued through the HHS Office of the Inspector General (OIG).[12] The *Caremark* cases also generously recognize that no rationally designed information and reporting system could be expected to remove the possibility that the organization will violate applicable laws, or that officers and/or directors will be misled or fail to detect compliance problems.[13] In other words, the emphasis is more *process* oriented, rather than *results* oriented, focusing on the manner in which the board oversees the plan, rather than on the extent to which the plan actually succeeds in detecting or preventing compliance issues.

The *Caremark* and regulatory standards are supplemented by additional governance obligations incorporated within the Sentencing Guidelines. These are "tone at the top"-related: first, that the board will promote an organizational culture that encourages ethical conduct and compliance with law; and second, that the board will do its homework—be reasonably informed with respect to the compliance plan, and (like the judicial standard) help ensure

4 HHS OIG Supplemental Compliance Program Guidance for Hospitals (2005). See also, HHS OIG Original Compliance Program Guidance for Hospitals 63 FR 8987 (February 23, 1998).

5 See Daniel R. Levinson, "Trustee Engagement and Hospital Success," *Trustee,* July 2010.

6 Ibid.

7 Honesty of purpose; acting with a true faithfulness and devotion to the interests of the corporation and its constituents.

8 See e.g., Section 8.30, "General Standards for Directors," Revised Model Nonprofit Corporation Act (Prentice Hall Law & Business, 1987); Section 8.30, "Standards of Conduct for Directors," Model Nonprofit Corporation Act, Third Edition (Prentice Hall Law & Business, 2009).

9 *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996); *Stone v. Ritter*, 911 A.2d 362, (Del. 2006); *In re Citigroup, Inc. Shareholder Derivative Litigation*, 964 A.2d 106 (Del. Ch. 2009).

10 Ibid.

11 See Chapter 8 of the Sentencing Guidelines Manual, available at www.ussc.gov/guidelines/2010_guidelines/Manual_PDF/2010_Guidelines_Manual_Full.pdf.

12 The HHS Office of Inspector General (OIG) believes that every effective compliance program must begin with a formal commitment by the board to implement a compliance plan incorporating all seven elements.

13 *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996); *Stone v. Ritter*, 911 A.2d 362, (Del. 2006); *In re Citigroup, Inc. Shareholder Derivative Litigation*, 964 A.2d 106 (Del. Ch. 2009).

that the plan has been reasonably implemented.[14] So, it's really not enough for the board to know that the compliance plan exists—it also needs to be familiar with its content and exercise such oversight as may be necessary to make sure that the plan is working. That's a potential trip wire for many boards—how would the average director respond when asked to describe in general terms the plan's structure and operation? Could the average director identify by name the organization's chief compliance officer? *Inquiring (regulatory) minds may want to know.*

> "The 'best boards' are those that are active, questioning, and 'don't shy away' from asking the tough questions."
>
> —*Daniel Levinson*

How Does This Work?

The *Caremark* cases establish baseline guidance on how board members are expected to implement the compliance plan oversight obligation. Board members must exercise general supervision and control of corporate officers. Yet, they're not expected to exercise "proactive diligence" (i.e., to ferret out compliance problems in the absence of specific warning signs). Instead, board members are expected to act in circumstances when suspicions are aroused, or should be aroused[15]—the proverbial "red-flag-waving" situation. In other words, the board must make reasonable inquiry when confronted with extraordinary facts or circumstances of a material nature (e.g., suggestions of defalcation, self-dealing, fraud, or similar issues). This is when things must get "ratcheted up." In these circumstances, board members are expected to "keep pushing" unless and until their questions are resolved. Absent suspicious developments, it's "okay" for board members to rely on the executive leadership team (including the general counsel and the chief compliance officer) in the performance of their duties and in their oversight of the compliance program.

What the *Caremark* cases *don't do* is to provide basic, "nitty-gritty" guidance on how directors can satisfy their compliance oversight duty in a practical context. To fill that void, the HHS OIG and the American Health Lawyers Association jointly published, over the last eight years, a series of three monographs focusing on the oversight obligation.[16] These monographs were intended to provide non-exclusive nuts-and-bolts suggestions to healthcare boards on how they might effectively carry out their oversight duties. Each monograph was designed to address a specific component of the compliance oversight obligation and offer sample questions board members may wish to raise:

- ***Corporate Responsibility and Corporate Compliance*** (2003): This first monograph was designed to provide a specific methodology for satisfying the *Caremark* standards. A series of sample questions focus on enhancing the board's understanding of both the scope and structure of the compliance plan, and of the actual operations of the compliance plan.
- ***An Integrated Approach to Corporate Compliance*** (2004): This second monograph was designed to assist the board in reconciling various differing policy perspectives regarding the proper roles of the general counsel and the chief compliance officer in supporting the board's oversight responsibilities. The OIG in particular is concerned that appropriate "checks and balances" are maintained between these two important positions. A series of sample questions are offered to help the board understand the respective duties of the general counsel and the compliance officer as they relate to compliance plan implementation.
- ***Corporate Responsibility and Health Care Quality*** (2007): This third monograph introduces the board's increasingly important compliance-related responsibilities with respect to quality-of-care and patient safety issues. A particular value is the extent to which the monograph describes the basis for the government's enforcement focus (particularly under the False Claims Act) on quality-of-care issues. A series of sample questions are provided to help the board understand the scope and operation of the organization's quality and safety initiatives.

Members of both the full board, and particularly of the compliance committee, should be provided with copies of these monographs as resources on the exercise of their compliance oversight duties.

Structure, Staffing, and Reporting

The board should recognize several important nuances as it maintains the *administrative approach* to compliance oversight. Primary among these is the *organizational structure* through which it exercises oversight. As noted elsewhere in this special section, the *Caremark* obligation extends to each voting member of the board (i.e., to the board as a whole). However, the general industry practice is for the board to delegate direct compliance oversight responsibility to a standing committee of the board.[17] Whether that committee's sole focus is compliance (e.g., a standing compliance committee) or it has a shared focus (e.g., compliance subsumed within the duties of the audit committee) is a matter of the board's business judgment. However, that should be a highly informed decision, reflective of the size and complexity of the organization and its historical legal and compliance profile. Don't make compliance a "stepchild" of a larger committee (i.e., where compliance matters are marginalized within the larger activities of the committee). To do so could give both internal (e.g., employees and physicians) and external (e.g., regulators and other third parties)

14 *In re Caremark Int'l Inc. Derivative Litig.,* 698 A.2d 959 (Del. Ch. 1996); Stone v. Ritter, 911 A.2d 362, (Del. 2006); *In re Citigroup, Inc. Shareholder Derivative Litigation,* 964 A.2d 106 (Del. Ch. 2009).

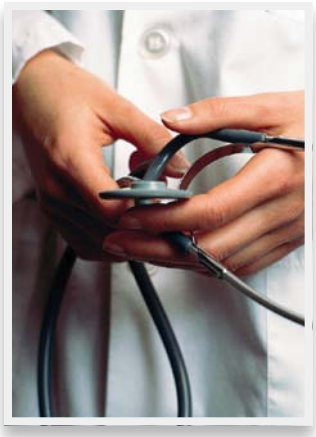
15 Ibid.

16 Available at www.governanceinstitute.com/LinkClick.aspx?fileticket=2ZMnzMdFBoI%3d&tabid=165. *Editor's Note:* Michael W. Peregrine was a coauthor of each of these white papers.

17 This board-level committee is not to be confused with any management-level compliance committee that serves to coordinate the day-to-day compliance management matters and reports to the board-level compliance committee.

audiences a highly negative impression of the organization's commitment to compliance.[18] Indeed, boards that initially delegated compliance oversight functions to an "audit" committee, or a similar existing committee, should periodically revisit the utility of that decision and whether compliance functions would be better served in a discrete board committee. Along the same lines, where compliance functions are assigned to a dual-purpose committee, the general counsel and compliance officer should ensure that both the substance of the charter and the time allocation of the actual meetings reflect the appropriate level of attention to compliance matters.

For multi-hospital organizations, the OIG encourages coordination with each operating hospital, through the use of a headquarters or parent-level senior compliance officer who communicates with parallel positions in each operating entity, provider, or division, as may be appropriate. Oftentimes the work of such a "system-level" compliance office is supported by a compliance committee at the parent organization level, which works to coordinate the compliance supervisory activities of the hospital/operating entity boards. While there is no "master template" for how multi-hospital system compliance plans work, the best practice is for the board of each operating entity in the system to maintain some basic responsibility for compliance oversight, even if its work is subordinate to the overall system compliance oversight activity at the parent board level.



The board should also ensure that the compliance committee is staffed with voting members who are both "independent" as defined by board governance policies, and possess the necessary expertise, background, and time commitment essential for effective compliance oversight purposes. The "independent" qualification is crucial; compliance committee members must not have, by fact or appearance, any financial, employment, or personal relationship with members of the executive management team, whose actions they may from time to time be called upon to evaluate for compliance purposes. Beyond designation of committee members as "independent," the committee should regularly apply the board's conflict-of-interest policy to address situations where potential bias of committee members may arise in the course of committee affairs. The background that observers generally feel is particularly valuable for compliance committee service includes experience in law, compliance, accounting/audit, finance, law enforcement, evaluative enterprises, and the judicial and regulatory branches of government.

From a staffing perspective, it is well established that the organization's compliance plan management activities should be assigned to a dedicated senior executive management position.[19] This position should be high enough within the executive hierarchy as to reflect an organizational commitment to compliance. Whether the role of chief compliance officer can be filled by the individual who simultaneously serves as the organization's general counsel has long been the subject of debate. Given the close relationship between legal and compliance matters, there is a natural suggestion of efficiencies to be achieved when the general counsel performs both functions. The HHS OIG has, however, historically preferred that the two positions be kept separate. According to this view, staffing by different persons helps ensure proper checks and balances (where the size and structure of the hospital/health system make this a feasible option). The OIG's position is that the roles of compliance officer and general counsel serve the hospital in fundamentally different ways. While the OIG recognizes that the roles have natural areas of overlap, in its view, "the lawyers tell you whether you can do something, and compliance tells you whether you should. We think upper management should hear both arguments."[20]

In addition, concerns will arise in larger, more operationally complex organizations that compliance is marginalized when the compliance position is combined with the duties of another officer.

It is also a recommended practice that the compliance committee, if not the full board, approve the selection, retention, and compensation of the organization's chief compliance officer. While such powers might meet with CEO pushback, they are a crucial part of the checks and balances provided through vigorous board oversight and reflect the dual CEO/board reporting relationship of the CCO (as described in more detail below). These powers help ensure not only that a competent compliance executive is hired for the chief position, but also that he/she is compensated in a manner commensurate with the scope of responsibilities. Notification (if not actual approval) of the termination of the CCO should be non-negotiable; such an event is a seminal development for the organization, and the compliance committee and the full board must be in an informed position in order to determine if there are any underlying plan problems or weaknesses.

Along the same lines, the compliance committee should coordinate with the human resources and executive compensation committees to help ensure that individual executive and management compensation arrangements contain appropriate incentives to comply with and support the compliance plan.

Similar corporate policy issues arise with respect to compliance *reporting relationships*. Accepted practice is for the CCO to have a dual reporting relationship to both the CEO and to the board. Indeed, recent amendments to the Federal Sentencing Guidelines include a direct, unrestricted CCO–board reporting

18 This is particularly an issue as non-lawyer consultants advise boards on ways to "streamline" the governance process and reduce members' time commitment. Reducing the number of standing committees by combining functions is a favored, if risky, tactic.

19 See e.g., Sentencing Guidelines Manual §8B2.1(b) (2)(C).

20 Amy Miller, "42.3bn Pfizer settlement strips legal team of compliance brief," legalweek.com, September 11, 2009; Erica Salmon-Byrne and Jodie Frederickson, "The Business Case for Creating a Standalone Chief Compliance Officer Position," May 25, 2010, *Ethisphere*, available at http://ethisphere.com/the-business- case-for-creating-a-standalone-chief-compliance-officer-position/.

relationship as a component part of its "effective compliance plan guidelines."[21]

> It's really not enough for the board to know that the compliance plan exists—it also needs to be familiar with its content and exercise such oversight as may be necessary to make sure that the plan is working.

Along the same lines, OIG has opposed internal reporting relationships that provide for the compliance officer to be subordinate to the general counsel, comptroller, or similar financial officer.[22] This is to protect the independence of the compliance officer and reduce the potential that the general counsel or financial executive can thwart or otherwise interfere with the compliance officer's exercise of judgment. However, the potential for overlap between the responsibilities of the two positions is significant, and the compliance committee must work to ensure a proper level of communication and cooperation between the two positions, and their coordination in terms of reporting to the committee and to the full board. The failure to achieve this communication, cooperation, and coordination can create significant gaps in the compliance process.

These are extremely important administrative concerns in which the board's compliance committee, and not just the CEO, should play a direct role because of the message that related decisions send about the organizational/board commitment to compliance.

Emerging "Hot Spots"

Permissive Exclusion
New pressure on the compliance committee is arising from increased OIG exercise of its extraordinary permissive exclusionary authority.[23] This allows the government to exclude from the federal healthcare programs officers and key employees of hospitals and health systems when they knew—or should have known—of prohibited conduct that led to hospital sanctions. It is the ultimate "find a new line of work" penalty and is applied without regard to actual intent or knowledge, and more according to the person's title and organizational authority. One of the few defenses to this "strict liability" penalty is where the individual exercised "extraordinary care" yet was powerless to prevent the violation. The adoption of a state-of-the-art compliance program, with all the "bells and whistles," is thought to be a possible means of demonstrating "extraordinary care." As the threat of permissive exclusion enforcement increases, compliance committees will be called upon by management to evaluate related plan improvements.

Quality of Care
It is very important that the board recognize the dramatic regulatory focus on quality of care and patient safety as key compliance concerns. The relationship between federal healthcare program reimbursement and quality of care has led to new criminal, civil, and administrative exposure to hospitals (e.g., failure of care creating False Claims Act violation). Furthermore, new federal authorities create additional quality-of-care-related exposure based on the integrity of provider data transparency and disclosures. As noted previously, the OIG is unwilling to accept "lack of a medical background" as an excuse for board members to defer to physicians to scrutiny of quality-of-care indicators. While important quality/patient safety issues such as mortality rates, hospital infections, medical errors, and so forth are the responsibility of the quality committee, we argue that they should also be in the scope of the compliance committee's jurisdiction.

New Collaborative Models
A wave of new corporate structural arrangements and, in particular, hospital–physician collaborative transactions are arising as part of a good faith attempt to respond to the changed financial model prompted by the PPACA. Each of the federal Stark laws, the Anti-kickback statute, and the Civil Monetary Penalties Law may be implicated by models intended to provide financial incentives to physicians to cross-refer, or to under- (or over-) utilize certain services of Medicaid providers. Thus, the shift toward accountable care is not without fraud and abuse risk. Some of the arrangements have little or no compliance risks, others raise risks that can easily be managed, while still others create uncertain or even aggressive levels of compliance risk that cannot be readily or comfortably managed or modified. The compliance committee must insist that these new arrangements are closely and appropriately vetted for legal risk.

> Don't make compliance a "stepchild" of a larger committee.

Keys to Effectiveness

Experience suggests that a series of practices, perspectives, and attitudes of the board and its compliance committee may serve to enhance the overall quality of oversight, and build a clear record of the board's satisfaction of its related fiduciary duties. This might include the following.

Education
It is simply crucial for the compliance committee to receive regular and reasonably detailed education on new developments, so that it may be more capable of exercising informed judgment on matters coming before the committee and the associated compliance risk. This is especially the case with the changes in compliance-related laws and regulations, and government enforcement activity, prompted by the PPACA. This does *not* mean that the committee can't rely on the advice and instruction provided by its compliance staff and legal counsel. Rather, it *does* mean that extra effort should be made by committee members to be

21 Available at www.ussc.gov/Guidelines/index.cfm.
22 Levinson, supra.
23 "Guidance for Implementing Permissive Exclusion Authority Under Section 1128(b)(15) of the Social Security Act" (October 20, 2010). Available at http://oig.hhs.gov/exclusions/files/permissive_excl_under_1128b15_10192010.pdf.

sufficiently familiar with the evolving environment so they may place the advice received in a proper perspective and make more informed decisions, especially those that involve risk evaluation. For example, the committee should be provided with anti-fraud recovery statistics annually trumpeted by the federal government;[24] another example is the impact of new case law and enforcement initiatives on particular hospital–physician arrangements.[25] These are the types of developments of which a compliance committee should be made aware. The key is to avoid a "*had I only known about that*" moment.

Awareness

The committee must be made aware of organizational activities that might create specific compliance issues. This is particularly important as the organization seeks to pursue new types of hospital–physician and similar arrangements in response to healthcare reform pressures. To the extent that the committee is generally familiar with organizational initiatives that have compliance implications—and that executive leadership is obligated to inform the committee of those initiatives—the more likely it is that the committee will be able to exercise an appropriate level of oversight. The key is to avoid a "*that never came before the committee*" moment.

Appropriate Reliance

It is totally appropriate for the board and the compliance committee to rely on the compliance-related advice of both executive management and outside advisors in connection with the exercise of oversight. The principal limitations to this general rule are a) where there is evidence that reliance may not be warranted in a specific circumstance (e.g., the executive officer has a conflict of interest, or the specific legal issue is outside the level of expertise of the compliance officer or legal counsel); and b) where the board/committee is excessively deferential to the executives or to the advisors, by reason of their experience, reputation, respect, or position in the organizational hierarchy. Where professional advisors would normally be involved in management's analysis, the committee is entitled to inquire as to the extent of the advice provided. What issues did they cover? What was their evaluation of risk? Did the organization hire the "A-Team" of professional advisors? Were the advisors constrained in the performance of their analysis by time/fee limitations imposed on them by overly cost-conscious financial managers?

The OIG is unwilling to accept "lack of a medical background" as an excuse for board members to defer to physicians to scrutiny of quality-of-care indicators.

Constructive Skepticism

Ask the tough questions. Don't be hesitant. If something doesn't look right, *ask*. What are the legal risks from a transaction? *Ask*. Has the transaction been vetted for conflicts of interest? *Ask*. Are there any qualifications to the expert's opinion? *Ask*. Why is the hospital doing this transaction—how does it achieve the mission? *Ask, ask, ask*. The compliance committee is no place for the shy or deferential.

"Foot Stomping"

Compliance committee members need the proverbial "titanium spine." They can't be afraid to take a tough disciplinary stance, or to make difficult and potentially expensive, invasive decisions with respect to internal reviews or investigations of compliance concerns. They must be free to pursue inquiry where the facts lead them. Similarly, they can't be afraid to reject a transaction or arrangement for compliance risk. We know the reasons to be tentative: maybe it will make the physicians mad; you like and trust the executive who is proposing the concept; the particular business opportunity may be lost if it is not approved; or the proposal has been so long in the works that the momentum is hard to stop. What's the right thing to do? Don't hesitate to stomp your feet or hold your breath until your face turns blue if you're not getting the answers you need to the

24 Department of Justice, Office of Public Affairs, News Release, "Department of Justice Recovers $3 Billion in False Claims Cases in Fiscal Year 2010; $2.5 Billion Health Care Fraud Recovery Largest in History—More Than $27 Billion Since 1986," Monday, November 22, 2010. Available at www.justice.gov/opa/pr/2010/November/10-civ-1335.html.

25 See e.g., the new anti-fraud and abuse, and Stark law decisions, *U.S. v. Borrasi*; No. 09-4088 (7th Cir. May 4, 2011); and *U.S. ex rel Singh v. Bradford Regional Medical Center* 2010 WL 4687739 (W.D.Pa. Nov. 10, 2010).

compliance questions you raise. The essence of oversight is applying informed, independent judgment, and sometimes that may involve just saying, "No, we're not going to do these kinds of deals anymore—they're just too risky."

Following Up

It is crucial for the committee to continually evaluate the effectiveness of plan components involving internal monitoring and auditing, discipline and incentives, and correction. These are highly critical elements of an effective compliance plan and the measure with which they are satisfied speak volumes (to third parties) as to the level of organizational compliance commitment. *Is the plan working? Are we sending the right signals? Are we responding appropriately when problems are identified? Have we, as an organization, learned our lesson? Have we changed our approach to reflect past problems?*

Reporting Up

The oversight onus is not on the committee alone. Every member of the board is subject to the *Caremark* oversight standard, and assumes some level of ultimate responsibility for the effectiveness of the organization's compliance program, regardless of whether specific oversight has been delegated to a committee. Thus, the frequency by which the committee reports to the full board on compliance matters and the extent of that reporting are important fiduciary concerns. To be sure, no one wants to reinvent the wheel. Board members have little interest in replicating compliance committee meetings. Yet, it is difficult to see how the full board can adequately address its overall responsibilities without having some basic understanding and awareness of the compliance environment and the organization's specific compliance profile. Indeed, the compliance reporting by the committee might ultimately impact the manner in which the board approaches an entirely separate issue. Full board attentiveness serves as an important compliance oversight "check and balance." It is very important that the full board monitor the effectiveness of the compliance committee, and step in when changes need to be made.

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When Things Go Wrong

Stuff happens. In the heavily regulated world of healthcare, compliance challenges are bound to arise, and the law does not hold compliance plans, nor those who oversee them, to a standard of perfection. Nevertheless, if the system appears to the outside world to have broken down, to the detriment of the organization and the patients it serves, the question will undoubtedly arise, "*Where was the board?*" And board members will, in turn, ask the logical question, *"Do I have exposure?*" The short answer for the individual director is, "No." The risk of personal liability for breaching the compliance oversight obligation has historically been pretty small. But times are changing, and you wouldn't want to "bet the farm" that no one will at least ask questions when compliance failures "hit the fan."

There's really no established case law in the non-profit sector that speaks to the standard of conduct expected of the non-profit director in the exercise of the oversight obligation (i.e., no statement of expectations or examples of how a board can "mess up" in the performance of these duties). The good news, however, is that the *Caremark* cases place an extremely high burden on attempts to hold board members personally liable for breach of the oversight obligation, calling it "possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment."[26]

These cases provide that for liability to arise, a plaintiff must show that the directors *knew* they were not discharging their fiduciary obligations or that by their actions they demonstrated a *conscious* disregard for their responsibilities (e.g., by failing to act in the face of a known duty to act). Examples of such conscious disregard could include either a) utterly failing to implement any reporting or information system of controls; or b) having implemented such a system of controls and consciously failing to monitor or oversee its obligations, thus disabling themselves from being informed of risks or problems requiring the board's attention.[27] C*an a board ask for better protection than that*?

Well, the real answer is that, for non-profit boards at least, it's not that simple. Depending upon the facts, one can't assume that a regulator or court reviewing the actions of a non-profit board in the context of a compliance failure would be as generous as the Delaware courts in *Caremark*. Unlike public companies, no "market remedy" exists in the non-profit context, where the state attorney general, rather than shareholders, is the principal agent of redress. In the non-profit model, the governing board is perceived as the "first line of defense" of charitable interests. Accordingly, regulators may be less willing than the Delaware courts to evaluate significant board oversight lapses under the *Caremark* standard of "conscious disregard." This is particularly the case if the facts show that plenty of compliance failure "red flags" had been flying but ignored by the board. In such cases, regulators may feel more compelled to point fingers at the board.

To date, the OIG has dealt with board oversight failures through new education, reporting, and oversight requirements mandated through corporate integrity agreements. State regulators may choose to take a more direct enforcement approach. Indeed, the New York State Medicaid Inspector General has expressed a clear willingness to hold board members accountable when oversight failures have contributed to organizational violations of applicable law.[28]

In Practice

In a "big picture" way, the suggestions presented in this special section are intended to help board members achieve the dual purpose of enhancing the effectiveness of the compliance plan while simultaneously reducing board member liability exposure.

The most direct course of action is for the board, through the compliance committee, to request the specific compliance program recommendations of both the CCO *and* the general counsel. Not only will this serve to demonstrate the board's good faith, but it will also invariably work to improve the effectiveness of the organization's compliance plan.

26 *In re Citigroup, Inc. Shareholder Derivative Litigation*, 964 A.2d 106 (Del. Ch. 2009).

27 *In re Citigroup, Inc. Shareholder Derivative Litigation* (2009).

28 New York State Medicaid Inspector General Work Plan FY 2011, *Corporate Responsibility and Health Care Quality.* Available at www.omig.ny.gov/data/images/stories/work_plan/omig_work_plan_2010_2011.pdf.

In the current environment, that's a valuable use of governance energy.

Action Items

Given the significant regulatory focus on corporate compliance in the healthcare sector, boards and their compliance committees are well advised to chart a specific agenda for future activity. Such an agenda might include, but would not be limited to, the following action items, which have a direct impact on the effectiveness of the board's oversight function and the process by which it is carried out:

1. Specifically address tangible measures by which the board and the compliance committee may demonstrate (individually and collectively) appropriate "tone at the top" conduct supportive of an organizational commitment to compliance.

2. Invite the general counsel and the chief compliance officer to periodically share with the committee their views on the extent to which the compliance plan satisfies the relevant standards for effectiveness, and recommendations on how the plan effectiveness can be enhanced.

3. Specifically evaluate the methodology of the compliance plan to monitor patient safety issues and the related compliance risks; consider ways the compliance committee and full board members can be educated on how best to monitor these issues without excessive reliance on organizational medical personnel.

4. Promote an intra-board review of the compliance risks arising from hospital–physician and other major transactions periodically under consideration by the organization. This might involve compliance coordination between the various board committees that evaluate significant transactions on behalf of the board. The goal of such a review would be to adopt a more uniform, board-level evaluation of the proper legal (and reputational) risk assessment applied in the transaction review process. Is there a level of risk in any transaction that the organization should be unwilling to accept?

5. Periodically evaluate the effectiveness of prior compliance committee-directed measures that were applied both a) in response to allegedly criminal conduct; and b) to prevent further similar allegedly criminal conduct, through modifications to the compliance plan. With the benefit of hindsight, how well did our responsive measures work?

6. When the positions of general counsel and CCO are separated and held by *different* persons, the board should ensure that the job descriptions of the two positions are complementary, not contradictory, and support (in an integrated and coordinated manner) the provision of compliance and legal risk information to the board.

7. When the positions of general counsel and CCO are held by the *same* person, ensure the imposition of a written procedure intended to resolve related actual or potential conflicts with respect to the conduct of internal investigations and in board reporting.

8. Ensure that the compliance plan has adopted the 2010 Federal Sentencing Guidelines Amendments, with particular focus on the express, personal, and regular reporting relationship of the "reasonable" compliance officer with the board or compliance committee. "Push back" if the initial answer is "we've done that"; the devil's in the details.

9. For organizations with a robust enterprise risk management function, ensure that corporate compliance activities are not marginalized or confused by the overall organizational commitment to ERM.

10. Where compliance oversight responsibility is delegated to a standing committee, ensure that a) compliance matters occupy an appropriate portion of the committee's agenda; b) committee members satisfy the board's "independence" definition; and c) the committee reports to the full board with an appropriate frequency.

11. When the positions of general counsel and CCO are separated and held by *different* persons, the board should ensure that they pursue an integrated and coordinated approach in guiding the organizational response to suspected compliance failures, especially when a) there is risk of civil, criminal, and/or administrative liability; and b) the compliance officer is not a lawyer.

12. When the positions of general counsel and CCO are separated and held by *different* persons, the board should ensure the implementation of protocols intended to identify and resolve disagreements between the general counsel and the CCO relating to organizational response to suspected compliance failures.

13. The board should be advised on the application and limitations of the attorney–client work product and other legal privileges and should seek assurance that the roles and responsibilities of the general counsel and CCO are structured to position the organization to satisfy the conditions for application of these privileges. This is particularly the case where the CCO is a licensed attorney.

14. The board should be assured that systems are in place to facilitate internal "up-the-ladder" reporting of actual or potential legal violations by the general counsel in satisfaction of his/her ethical responsibilities under state bar rules of professional responsibility and, where applicable, SEC rules.

15. When the positions of general counsel and CCO are separated and held by *different* persons, the board should ensure the implementation of communication protocols between the two positions (other than direct reporting relationships) that maximize coordination and integration and minimize the potential for conflict of interest.

The Governance Institute thanks Michael W. Peregrine, Esq., partner, of McDermott Will & Emery, LLP for contributing this special section. *He can be reached at mperegrine@mwe.com.*