

Clarifying Fiduciary and Advisory Roles

By Pamela R. Knecht, President and CEO, **ACCORD LIMITED**

There is one issue that is predictably raised every time board members within a health system are asked what, if anything, concerns them about their board's effectiveness and efficiency. Board members will almost always say that they are not entirely clear on their board's role and/or decision-making authority. This is especially the case for those who serve on subsidiary boards.

This anecdotal observation is supported by data from The Governance Institute's 2017 Biennial Survey of Hospitals and Healthcare Systems.¹ Overall, only 61 percent of survey respondents stated that "assignment of responsibility and authority is *widely understood and accepted*." Interestingly, in 2015, 86 percent responded "yes" to that same question. In other words, there seems to have been a significant drop in clarity about responsibility and authority among boards in health systems. This article attempts to explain why some boards are confused about this issue, and how to obtain more clarity.

A Legal Explanation of Governance Structure

One of the key areas of role confusion is whether a subsidiary

¹ Kathryn Peisert and Kayla Wagner, *The Governance Evolution: Meeting New Industry Demands*, 2017 Biennial Survey of Hospitals and Healthcare Systems, The Governance Institute.

Key Board Takeaways

The following actions should be taken by systems that are committed to excellence in governance at all levels:

- Be honest and clear about the nature of the entity (fiduciary or advisory) at the beginning (e.g., when a subsidiary is considering joining the system and when an individual is being recruited for the board).
- Ensure the subsidiary's bylaws accurately describe the system's reserved powers and the responsibilities of the subsidiary board.
- Develop a detailed governance authority matrix, outlining the specific level of authority for each governance responsibility and entity (e.g., approve, recommend, provide input).
- Name the entity appropriately (e.g., Community Advisory Council, not ABC Hospital Board, if it is an advisory body).
- Select subsidiary board or council members who have the skills, competencies, and perspectives that match the entity's role (e.g., for an advisory council, recruit local social service agency executives, not financial experts).
- Provide robust initial orientation and assign mentors to new board members to help them understand their role.
- Convene an annual education session, clarifying the role, responsibility, and authority of subsidiary entities.

board is a fiduciary entity or an advisory entity. To help clarify the situation, it may be useful to start with an explanation of governance structure from a legal perspective.

At a very basic level, every organization that is a legal corporation must have a board. This concept applies to both for-profit and not-for-profit organizations. The organizing documents (e.g., articles of incorporation) and bylaws of the corporation include specific requirements regarding the board's legal, fiduciary responsibilities in overseeing the business of the organization.

The board of a stand-alone hospital (and the parent board of a system) are responsible for all the fiduciary duties and core governance responsibilities related to that organization. These responsibilities include oversight of mission and strategy, finance and investment, audit and compliance, quality and safety, executive performance, governance effectiveness, and community benefit (for not-for-profit healthcare organizations). In some organizations, the board may also be responsible for philanthropy. For each of these responsibilities, boards are to set direction and goals, approve policies, hire the

CEO, delegate work to the CEO, and hold the CEO accountable for the performance of the organization vis-à-vis the strategy, goals, and policies.

However, the board of a subsidiary within a system may not retain ultimate legal responsibility for *all* those responsibilities. The determining factor here is the “reserved powers” that the system board has over the subsidiary board, as articulated in the subsidiary’s bylaws. Every system board must retain some authority over its subsidiary boards to ensure the system has adequate control over the subsidiary. The system or parent board needs that control because it has (most likely) taken on responsibility for the legal, regulatory, financial, and other issues related to that subsidiary. This is certainly the case if the system is the sole corporate member of the subsidiary and they are both part of the same obligated group for financing purposes.²

Responsibilities of Fiduciary Boards vs. Advisory Bodies/Councils

Over the last decade or so, health systems have become more sophisticated, and the nature of their reserved powers has changed. In the past, a system may have allowed a significant amount of authority to remain at the subsidiary level. Over time, most systems have found that arrangement hindered “systemness” so they have narrowed the fiduciary duties of the subsidiary. For example, today, the system board and its committees may

handle the subsidiary’s fiduciary duties regarding the following responsibilities:

- Approving the subsidiary’s audit
- Approving the hiring, evaluation, and termination of the subsidiary’s CEO
- Approving the subsidiary’s executive compensation
- Approving the subsidiary’s capital and operating budgets above a threshold
- Approving the subsidiary’s strategic plan
- Approving the subsidiary’s board members

In this scenario, the subsidiary may still be a fiduciary board if it remains a separate, legal corporation with some fiduciary duties such as final approval of:

- Capital and operating budgets below a threshold
- Medical staff credentialing
- Subsidiary-specific quality, safety, and service goals
- Community benefit goals

These subsidiary boards would also provide advice to their senior management on the responsibilities

for which the system retained ultimate decision-making ability, such as input on strategic planning, input into their CEO’s hiring and evaluation, and recommendations regarding individuals to serve on their board. For those tasks, they would be “advisory.” This type of subsidiary board is actually a hybrid of fiduciary and advisory.

However, some systems have decided that the best way to ensure consistently high- quality, low-cost care for the population served is to convert their subsidiary corporation boards to advisory entities. (*Note:* State law varies regarding the ability to eliminate hospital corporations, so legal counsel should be sought on this issue.)

In this scenario, *all* the legal, fiduciary duties of the subsidiary board are retained by the system board and its committees. In most cases, though, the system would create advisory bodies in each geographic market to ensure understanding of and connections to the local market. (*Note:* Using the name “board” for an entity that

Affiliation Agreements Create Varying System–Subsidiary Relationships

Often the relationship between the parent or system board and its subsidiary boards differs based on the nature of the affiliation agreement(s) under which the subsidiary joined the system. Some subsidiary boards negotiated agreements that resulted in their retaining more authority than might be the case for other subsidiaries. For example, one subsidiary might retain some authority for selecting the subsidiary’s CEO and that CEO may have a dual reporting relationship to the subsidiary board and to the system CEO. Another subsidiary in the same system might have a different affiliation agreement under which their CEO is hired, evaluated, and if necessary, terminated by the system CEO, with input from the subsidiary board.

In the above example, the first subsidiary board described has a fiduciary responsibility regarding CEO selection, evaluation, and termination, whereas the second subsidiary board is serving in an advisory capacity regarding that specific responsibility.

² For more information, see Michael Peregrine, “[Understanding the Role of the Subsidiary Board](#),” *Subsidiary Focus*, The Governance Institute, September 2018.

is not a legal corporation is one of the key sources of role confusion, so it is best if the advisory body is named something like “Community Advisory Council.”)

Advisory councils often play a significant role as fiduciary boards. And, in many cases, individuals serving on those entities appreciate not being legally responsible for overseeing an organization in a highly complex industry in which they are not experts. They may also feel that they are more suited to providing advice in areas about which they are knowledgeable and/or passionate.

Advisory councils can provide much-needed advice to the system on their community or region, while allowing the healthcare experts (e.g., senior management) to handle running the organization. Such councils can play an essential role in assuring that needed care is delivered and coordinated in each community

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in an era of population health management. They often provide *advice and recommendations* to management on the following:

- Identifying their community’s health needs across the full continuum of care
- Clarifying gaps in creating a unified patient experience and providing excellent, safe care
- Suggesting services to address current gaps in healthcare within their community
- Managing the health of specific demographic and health-status populations (e.g., the elderly, children, and individuals with chronic health or behavioral health issues)

- Connecting with community leaders, organizations, and agencies to address social determinants of health (e.g., transportation, housing, and healthy food options)
- Supporting the system’s philanthropic efforts
- Being advocates for the system/hospital/clinic/nursing home in the community

Whether a board is fiduciary or advisory does not really matter. What is important is that the individuals serving (usually as volunteers) on boards, committees, and councils understand what is expected of them and feel that their contributions are meaningful.

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