

CONVERSATIONS ON BOARD EFFECTIVENESS & THE LAW'S EXPECTATIONS

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GOALS AND OBJECTIVES

- To confirm the focus of director fiduciary obligations
- To provide an overview on current expectations of fiduciary oversight
- To describe the accepted range of director “effectiveness” standards
- To provide examples on how effectiveness can be favorably applied
- To describe the law’s expectation of “constructive curiosity”
- To take your questions

“IN A NUTSHELL”

Corporate governance generally, and board/management relationships in particular, are enhanced when board members adhere their conduct to one or more established indicia of “effectiveness”.

Board efforts to implement effectiveness indicia will usually be considered as evidence of “good faith”, which is a critical element of fiduciary responsibility.

“IN A NUTSHELL” (CONT’D)

Effectiveness is grounded in the core board/management “bargain”: the board must be sufficiently effective in order to be a resource to management, and management must be sufficiently respectful of the board’s governance duties.

THE OVERARCHING THEME:

“The all-volunteer governance model that dominates not-for-profit health systems and hospitals is losing adherents as the role of board directors becomes more complex and demanding.” Source:
Healthcare Financial Management

THE OVERARCHING THEME: (CONT'D)

One of the most subtle, yet important new Governance developments has been the increasing focus on the extent of director engagement in board affairs.

Are individual directors devoting sufficient time and energy to the performance of their duties?

WHO CARES ABOUT DIRECTOR PERFORMANCE?

- State and federal charity regulators
- DOJ, FTC, SEC
- Media
- Creditors, ratings agencies
- Disgruntled directors, donors

PART I:

GLOBAL OVERVIEW OF “BOARD EFFECTIVENESS”

WHAT IT MEANS

The concept of director effectiveness is applied to describe that set of practices and perspectives that are generally considered to contribute to superior corporate board performance; e.g. effective performance of fiduciary duties, positive and productive board/management dynamic and continued satisfaction of corporate mission and purposes.

Its meaning and concept overlaps to some degree with those of “best practices”.

WHY “EFFECTIVENESS” IS RECEIVING SO MUCH ATTENTION

The concept of director effectiveness has assumed greater prominence in governance dialogue given the interest of officers, directors and others to identify an accepted pathway to appropriate board conduct.

This, within an overall context of increasing judicial, regulatory, legislative and third party focus on the role of the board and the performance of the board as a unit, and individual directors.

THE VALUE OF EFFECTIVENESS

The extent to which a board can demonstrate a good faith attempt to adopt recognized governance effectiveness measures will help enhance the reputation of both the company and its mission and the strength of its governance function. It will also serve as a meaningful prophylactic against director liability and reputational harm.

CORE ELEMENT OF EFFECTIVENESS

The fiduciary duties of directors of non-profit healthcare companies are to be exercised in support of the corporate mission and purposes; i.e. to assure high quality, cost efficient, affordable and accessible health care for patients and the community at large.

WHEN A CLIMATE OF EFFECTIVENESS FLOURISHES

- a) boardroom clarity on the separate roles of governance and management;
- b) the board's working partnership as a resource for executive leadership; and
- c) a governance philosophy that board service is a privilege not an entitlement.

PART II:

HOW DIRECTOR EFFECTIVENESS IS APPLIED BY HIGH PERFORMING BOARDS: EXAMPLES RANGING THROUGH THE LIFE CYCLE OF THE GOVERNANCE PROCESS

EXAMPLE ONE: THE BOARD/MANAGEMENT DYNAMIC

High performing boards share with executive management a clear understanding of their respective duties and obligations (and where they can merge); appropriate lines of authority, and the circumstances in which boards are called upon by the law to assume greater duties.

EXAMPLE TWO: THOUGHTFUL BOARD COMPOSITION, SIZE PRACTICES

High performing boards have specific expectations for desired director experience and background, meaningful diversity goals and the most appropriate size of the board and its key committees.

These boards implement meaningful turnover/refreshment techniques in order to assure that they are appropriately diverse and are periodically infused with “new blood”.

EXAMPLE THREE: ONBOARDING AND DIRECTOR EDUCATION

High performing boards (particularly those serving companies in complex, regulated industries) require comprehensive director onboarding and ongoing director education programming. The twin goals are to assure effective transition to board service and to assure continued awareness of industry and environmental developments.

EXAMPLE FOUR: MONITORING OF DIRECTOR CONDUCT

High performing boards support the adoption and implementation of policies intended to govern the ethical conduct and performance of officers and directors. These include conflicts of interest policies, ethical standards, rules regarding harassment and bullying, and individual and full board evaluation processes.

EXAMPLE FIVE: LEVEL OF ENGAGEMENT

High performing boards appreciate the heightened standard of conduct to which they are held in the performance of their duties; the expanded scope of their oversight tasks, and expectations of commitment to the position. These boards often agree to limitations on outside board service and on other potential distractions.

EXAMPLE SIX: ATMOSPHERE OF COLLEGIALLY

High performing boards commit to maintaining collegial relationships between board members, and especially between the board and management, in order to support full and frank discussion of issues before the board.

EXAMPLE SEVEN: “TONE AT THE TOP”

High performing boards not only provide strong support to corporate legal and compliance functions, but also embrace a corporate culture that prioritizes ethical standards and integrity in the establishment and implementation of goals, and as a reflection on the corporation’s purposes.

EXAMPLE EIGHT: MEETINGS AND AGENDA

High performing boards direct management to work with board leadership in the preparation of board and key committee meeting agendas; to assure board focus on strategic rather than tactical matters, and that meetings schedules and agenda are sufficient to address key board issues.

EXAMPLE NINE: INFORMATION SUPPORT

High performing boards work with management to assure that they are provided with all relevant information from which they may make reasonable decisions and effect prudent oversight on issues coming before the board; e.g. performance, strategy, compensation, risks; financial stability and ESG related issues.

EXAMPLE TEN: EVALUATION OF STRUCTURE

High performing boards periodically consider examples of optimal board and committee composition and structure, as well as corporate structure, and compare against existing practices for purposes of possible enhancement. This, in order to assure the continued ability of the corporation and its board to fulfill their respective roles as effectively as possible.

PART III:

HOW BOARDS EFFECTIVELY EXERCISE CONSTRUCTIVE CURIOSITY WITH MANAGEMENT

EXERCISE OF CONSTRUCTIVE CURIOSITY

One of the enduring messages of the Sarbanes-Oxley Act, and the resulting emphasis on corporate responsibility, is that directors should abandon the passive role they may have been satisfied in playing, and instead adopt a new governance culture emphasizing the exercise of “constructive curiosity” and an active, independent oversight role.

DEFINITION OF CONSTRUCTIVE CURIOSITY

Directors exercise “constructive curiosity” through a boardroom culture that encourages directors to ask incisive, probing questions regarding key decision-making and oversight issues, and requires accurate, forthright answers to those questions.

DEFINITION OF CONSTRUCTIVE CURIOSITY (CONT'D)

Constructive curiosity should be viewed as different than acting as a “devil’s advocate”. It does not require board members to adopt an adversarial relationship with senior management.

Rather, it expects the board to maintain a collegial, working collaboration with the senior leadership team and act as a resource to that team in the performance of their duties.

DEFINITION OF CONSTRUCTIVE CURIOSITY (CONT'D)

Constructive curiosity rejects a culture of passivity and excessive deference to management.

It encompasses the director leveraging his/her diversity of experience and common sense, and raising to management, as appropriate, relevant, well-formed questions-all in a respectful, positive and collegial manner.

CONCLUSION

The adoption of various elements of board effectiveness offers corporate governance an accepted opportunity to demonstrate its good faith and to enhance the effectiveness of its service to the organization. Board effectiveness elements are well known, broadly established and in most circumstances do not require substantial cultural change to adopt.

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