



The Governance Institute's E-Briefings



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Welcome to The Governance Institute's E-Briefings!

This newsletter is designed to inform you about new research and expert opinions in the area of hospital and health system governance, as well as to update you on services and events at The Governance Institute. Please note that you are receiving this newsletter because you are a Governance Institute member or expressed interest at one of our conferences.

News, Articles, and Updates

The "Value Added" of the Governance Committee

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This article is the sixth in a series on efficient board committee practices (refer to previous issues of E-Briefings to read about the strategic alignment committee, executive compensation committee, audit committee, compliance committee, and executive committee).

The governance committee is increasingly becoming one of the most active and vital of all board-delegated functions. Its focus on guiding the commitment to effective governance practices places it in a key board leadership position. This is especially the case with organizationally sophisticated hospitals, health systems, and similar organizations with large board, committee, and advisory support structures. Such a committee supports the non-profit mission by helping ensure that board members possess the necessary qualifications and competencies, and that the board's governance processes mirror recognized best practices.

Committee Purpose

The principal purpose of a governance or similar type of committee is to concentrate within one standing board committee the core responsibilities associated with board development matters. This portfolio typically subsumes the development of standards relating to the nomination, education, self-evaluation, independence, and fiduciary conduct of board and committee members. The most progressive of non-profit boards concentrate these responsibilities within a dedicated governance committee. Many other boards continue to allocate component parts of the overall portfolio within multiple different committees (e.g., executive, nominating, conflicts of interest, etc.).

Substance is often more important than form, and the key is that the board ensure that the full range of governance standards and issues are being addressed by its committee structure. Nevertheless, the increasing legislative, regulatory, and public policy focus on enhanced governance standards and principles in the non-profit sector argues strongly for a single committee to address these types of issues, with committee members specifically focused on matters of corporate governance and accountability. The single committee format allows for a concentrated and coordinated approach to board development matters.

Committee Profile

The specific portfolio of the governance committee may vary, depending upon the size, sophistication, and core mission of the non-profit organization and the complexities of its governance structure. A "menu" of possible duties and responsibilities could include the following (in no particular order):

- **Director recruitment:** preparation of a governance matrix identifying the fiduciary recruitment needs of the organization; identification and due diligence review of director and committee member nominees; monitoring of the election process and orientation of newly elected/appointed directors/committee members.

- **Director independence:** establishment and maintenance of independence standards for board and committee members, considering applicable state and IRS requirements and recognized corporate best practices.
- **Education:** development of a formal board education process by which members receive education on matters of relevance to their board responsibilities.
- **Fiduciary conduct:** adoption of policies and procedures (e.g., “principles of governance conduct”) designed to assist board and committee members in conducting their activities in a manner consistent with established legal standards. This may include the retention of legal counsel for advice on specific issues relating to fiduciary principles and the application of governance best practices.
- **Term limits:** addressing board policies with respect to terms, and possible term and age limitations on board and committee service.
- **Governing documents:** working with corporate counsel to periodically review the appropriateness and effectiveness of the articles of incorporation and bylaws of the organization and recommending changes when appropriate and in the organization/board’s best interest to do so. This includes monitoring, with the assistance of counsel, changes in applicable laws and regulations as they may relate to board conduct and governance practices.
- **Committee structure/meetings:** with the assistance of board leadership, providing guidance on the identification, formation, charter, membership, operation, and processes to be applied by the various standing and special committees of the board. This may also include recommendations on the participation of members of the senior leadership team (e.g., general counsel, chief financial officer, chief information officer) as staff to individual committees.
- **Conflicts of interest:** establishment of policies and procedures relating to the identification and disclosure of potential and actual conflicts of interest and other related party transactions, including the actual review and resolution of disclosed potential conflicts and the identification, where appropriate, of conflicts management plans.
- **Self-evaluation:** the adoption and management of processes intended to assist the board in the performance evaluation of board and committee members.

- **Director removal:** leadership of the process by which the removal of a board or committee member is considered. This may also include the adoption of policies intended to ensure the ongoing “fitness to serve” of individual board and committee members.

By no means is this intended to be an all-inclusive list of the specific duties and responsibilities of a governance committee; there is no “one-size-fits-all” approach or specific “best practice” in the area. Depending on the circumstances and needs of particular organizations, some of the above topics might be the primary responsibility of a separate standing committee (e.g., conflicts of interest, director orientation, and education). Other organizations may choose to add duties and responsibilities to the above portfolio (e.g., CEO succession planning), depending upon the perspectives and traditions of the board. The governance committee should work closely with the general counsel in the conduct of committee affairs, as virtually all of the responsibilities of the committee have clear legal implications.

Committee Composition

The three principal considerations relating to the composition of the governance committee are size, independence, and expertise. The size of the committee should be in direct correlation to the scope of committee tasks (i.e., the more extensive the committee tasks, the larger the size of the committee). For example, should the committee charter include responsibility for oversight of the board conflict-of-interest review and management process in addition to the other traditional duties, it may well mandate a committee of slightly larger than normal size to make sure that such responsibility can be adequately staffed. Especially where its charter includes nomination responsibilities, the composition of the committee should be limited to individuals determined to be “independent” under applicable state corporate law standards or best practices. Particular care should be given to satisfaction of specific IRS “disinterested director” standards in the (hopefully unlikely) event that executive compensation is added to the committee portfolio. As with the audit, finance, executive compensation, and other traditional standing board committees, it is vitally important that the composition of the governance committee include individuals well versed in principles of corporate responsibility, ethics, accountability, and director recruitment.

Emerging Duties

The importance of the governance committee is heightened by the continued evolution of statutes, regulations, governance principles, and best practices that directly or indirectly impact the composition, process, and conduct of the non-profit board. Working in consultation with corporate counsel, the governance committee serves as the portal through which the full board is kept advised on relevant developments in corporate governance, including those applicable primarily to public companies but which can be expected to “spill over” in some form to the non-profit sector. Examples of developments that a governance committee could be expected to review on behalf of the board include, but are not limited to: a) new legal developments, such as the efforts of the Massachusetts Attorney General Martha Coakley to prohibit compensation of non-profit directors; b) the governing board provisions of new federal legislation and rulemaking like Dodd-Frank (which are likely to have some impact on the non-profit sector); and c) the implications of emerging “best practices” compilations such as the new report, “Bridging Board Gaps.”¹ This report is designed to improve board performance and effectiveness by offering a series of recommendations in critical areas of governance. The report calls for a renewed commitment to the purpose of corporate boards, and suggests guidelines to improve board practices and standards along seven core dimensions: purpose, culture, leadership, information, advice, debate, and self-renewal. While geared primarily to public company governance, it has important relevance to organizationally sophisticated non-profit organizations.

Governance committees that include conflicts-of-interest management within their portfolio will be

¹ “Bridging Board Gaps,” Columbia Business School and the Weinberg Center for Corporate Governance, University of Delaware, 2011.

increasingly pressured to more closely monitor the effectiveness of such processes, including the review and evaluation of conflicts disclosures, given the increasing personal and organizational risks associated with conflicts-of-interest transactions. The recent scandals involving the Fiesta Bowl and Lifespan offer noteworthy lessons to governance committees in this regard.

Recommendations

In the current “corporate responsibility” environment, it is crucial that non-profit boards—either directly or through a standing committee—assume responsibility for the development of standards relating to the nomination, education, self-evaluation, independence/conflicts, and fiduciary conduct of board and committee members. Boards that do not have an established governance or similar committee should give strong consideration to adopting such a body to address this need. Boards that have essentially allocated board development responsibilities amongst several existing committees should give strong consideration to consolidating those responsibilities within a dedicated governance committee. Boards that do utilize a standing governance committee should review the sufficiency of the committee’s charter to ensure that it incorporates the duties and responsibilities most appropriate for the organization and its board. There is no one-size-fits-all approach to how the board addresses these responsibilities, with often differing approaches as to committee use and scope of assigned duties. That notwithstanding, there is little debate that the effective board will embrace the pursuit of these duties and responsibilities. The view here is that the dedicated governance committee is a particularly efficient way to achieve the ultimate board development goals, and will be responsive to the liability and standard of conduct interests of individual directors.

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