President Trump, Potential Conflicts and Health System Boards

It is important to note that the rapid growth of health systems, the equally rapid diversification of their businesses and investment portfolios, and the expanding diversity of board members’ backgrounds in board membership significantly complicate the conflict-of-interest review process.

The “Trump Transition” conflicts checklist logically could include the following:

#1 – Intent.

The transition process has required incoming officials to confront and resolve actual and potential conflict-of-interest issues. Indeed, the president has made public statements expressing an intent to step away from his global business interests to address conflicts of interest. From a nonprofit law context, the intent factor is an important part of the process—namely, the inherent value of acknowledging the duty of loyalty, and the willingness to avoid business transactions and other arrangements that could give rise to an actual or apparent conflict. For the health system board, it is an acknowledgment that must be made both in the recruitment process and at least annually through the disclosure protocol.

#2 – Disclosure.

There has been much media coverage of Cabinet nominees’ business holdings, and of whether they have fully (and timely) disclosed those holdings as part of the Senate hearings process.

From a nonprofit law context, this underscores the importance of conflicts disclosure by director candidates, as well as by sitting directors. Both the director nomination process, and the board’s conflicts questionnaire, should be sufficiently detailed so as to prompt disclosure of all business and investment interests and fiduciary relationships that could reasonably cause episodic or disabling conflicts, as well as cause potential public perception issues. The disclosure questionnaire also should call for sufficient detail so that the materiality of those interests can be evaluated in the proper context. The spirit and intent of the conflicts disclosure process should incentivize directors and nominees to make the most timely and fulsome possible disclosure, which will help to anticipate actual or potential conflicts.

Michael W. Peregrine and Ralph E. DeJong

Political biases aside, the transition process for the new administration—both as to President Donald Trump and his Cabinet nominees and White House advisers—does a great service for nonprofit health systems by highlighting critical conflict-of-interest concerns. The last several weeks’ headlines provide health system general counsel with a rare opportunity to offer practical board education based on current events.

The president’s personal asset divestiture plan, announced on Jan. 11, along with the broader public scrutiny of key administration members’ business interests, present an important teaching moment on identifying, resolving and managing conflict-of-interest issues. And that’s a subject on which many health system boards could use continuing guidance, given the strictures of the duty of loyalty.

Neither the particulars of the administration’s potential conflict issues nor the details or adequacy of the president’s divestiture plan needs to be addressed here. Instead, the issues themselves provide something of a checklist that can help health system boards ensure their internal conflict-of-interest policies and processes are as fulsome as possible. Strong conflict-of-interest inquiries are critical to protect the reputation of the organization and its board members, and to sustain key business arrangements.

Michael W. Peregrine (mperegrine@mwe.com) and Ralph E. DeJong (rdejong@mwe.com) are partners in the Chicago office of McDermott Will & Emery LLP.
#3 – Adequate Time for Review.

Recent media articles have addressed the speed with which the Cabinet nominations are proceeding through the Senate confirmation process. Some observers are concerned the process’s speed is impacting ethics and Senate staffers’ ability to adequately review candidate disclosures.

In the nonprofit law context, a risk arises when the board doesn’t apply a vigorous and timely conflict review process. Indeed, the failure to adequately review disclosed interests and the conflicts that might occur as a result can create breach-of-duty exposure separate and distinct from that associated with a failure to make adequate disclosure. The health system board will want to assure there is a process, including review by independent directors and support by the general counsel, that allows close examination of all individual directors and director nominees’ disclosed interests for actual and potential conflicts.

#4 – Board Diversity.

Public concern has been expressed about the magnitude of Cabinet nominees’ financial holdings, specifically, that the Cabinet will be made up primarily of millionaires and billionaires and will lack perspective as a result. This concern relates to the very vital corporate governance debate about the breadth of diversity on a governing board.

One question typically addressed in the nomination process is whether there are certain qualifications or experiences that all board members should meet or whether board members should have a broader scope of qualifications or experiences. New governance best practices suggest companies benefit from a board composed of members of diverse backgrounds and perspectives, not only as to gender and race, but also as to experience, thought and perspective.

#5 – Nepotism.

Trump announced he has appointed his son-in-law, Jared Kushner, a New York businessman, as a senior White House advisor. There is no clear nonprofit analogy to such an arrangement.

Many health systems, however, prohibit or limit the employment of relatives of board members or senior executives, at least at levels where the board member or senior executive could exert influence over the employment arrangement. In addition, nonprofit governance best practices call for a significant percentage of the board to be comprised of independent directors. A director who has a family member employed by the nonprofit likely wouldn’t qualify as such. Nonprofit health systems should bear in mind that most situations involving employment of a family member of a current or recent officer, director, trustee or key employee must be disclosed on the annual tax Form 990, Return of Organization Exempt From Income Tax, and thus will be subject to additional scrutiny.

#6 – Conflict Management Plans.

The president has stated that he will address the potential for conflicts arising from his vast business interests not through divestiture, but rather by transferring all of his business operations to a trust controlled by his two oldest sons and a longtime associate. This form of financial interest restructuring invites comparison to the process by which nonprofits manage board-approved conflict-of-interest arrangements.

Many states provide a specific statutory rebuttable presumption for conflict-of-interest arrangements approved in advance by the board using specific factors. When satisfied, these factors shift the burden of proving an alleged conflict to the individual or entity bringing the challenge. The extent to which boards subsequently monitor approved conflict-of-interest arrangements often provides evidence supporting the board’s good faith in approving the arrangement, conflict notwithstanding. Yet, perhaps like the president’s proposal, even conflict management plans that meet the letter of a governing policy are rarely free from media or regulatory scrutiny or criticism.

#7 – Divestiture of Conflicting Interests.

Many of Trump’s Cabinet nominees have presented detailed plans to fully divest themselves of financial and other business interests to avoid the appearance of bias upon taking office. For the nonprofit health system, this implicates situations in which a valued director possesses an interest or relationship that creates a conflict that can’t be managed effectively or otherwise resolved in the organization’s best interests. Rather than assuming the risk of a conflict-of-interest transaction, or requiring that the director resign from office, the board and its governance committee may suggest divestiture of the offending interest or relationship. In extreme situations, where divestiture can’t be made without the director suffering unreasonable financial loss, some form of comprehensive blind trust or similar vehicle may be an alternative.

The comparison to Trump also serves an additional, conceptual purpose. Fairly or unfairly, some commentators have seemingly conflated the existence of the president’s vast business interests with ethical impropriety, as if the mere existence of those holdings represents a fundamental disqualification from public service, as opposed to holdings creating potential conflicts that must be addressed.

A similar distinction can be made as to nonprofit directors. Individuals who serve or may wish to serve as directors may have significant and complex business and personal interests, but the mere existence of those interests need not disqualify an individual from service as a nonprofit director nor expose the director to a potential breach of fiduciary duty. Rather, it is the failure to adequately disclose those interests, or the board’s failure to adequately review those interests and manage the resulting actual or potential conflicts, that creates the breach-of-duty risk. This distinction is an important one to keep in mind.

Conclusion.

The landscape that encompasses the totality of the president’s family business interests and those of his Cabinet appointees—and their relationship to the ethics of government—is many layered. It nevertheless offers certain valuable analogies for the health system board—for which the duty of loyalty is sacrosanct. It
isn’t all that great a leap to go from Trump’s transition issues to the conflict-of-interest policies of a nonprofit health system board. And it should be noted that the breadth of scrutiny of transition-related conflicts of interest likely hasn’t gone unnoticed by health-care industry regulators, including but not limited to state charity officials. Regulators may be far more likely than before to apply greater sensitivity to issues and relationships that may present conflict issues and their broader legal implications.