CHAPTER 1

Governing

OBJECTIVES

After completing this chapter, you will understand:

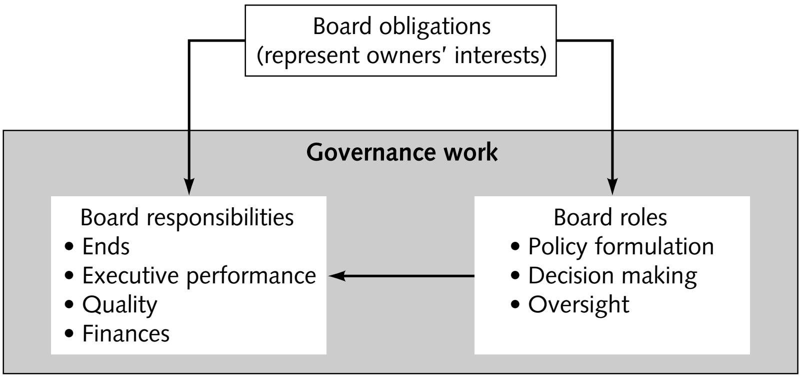
- Your board's obligation to stakeholders
- The nature of governance work (responsibilities and roles)
- Factors that most affect your board's performance and contributions

gov•ern [gûv' `ern], verb; syn. guide, direct, control
Exercise ultimate authority and accountability
Represent the interests of an organization's owners as an agent or trustee
What boards do

Health system boards, hospital boards, medical group boards, home health agency boards, health plan boards, health maintenance organization (HMO) boards, professional association boards . . . there are approximately thirty thousand boards in the health care industry, and about 330,000 people serve on them. They govern nonprofit organizations, commercial corporations, and government agencies ranging from small, local institutions to multibillion dollar enterprises national in scope.

Health care organization boards are a diverse lot. But beyond some superficial differences, they are identical in terms of their obligations, responsibilities, and roles (see Exhibit 1.1).

Exhibit 1.1. The Dimensions of Governance



OBLIGATIONS

Every board exists to represent the interest of an organization's owners: stockholders in commercial corporations, stakeholders in nonprofits, constituents in government agencies. The overarching obligation of a board is to ensure an organization's resources and capacities are deployed in ways that benefit its owners.

Organizations are collections of resources: money, people, facilities, equipment, supplies, capabilities. They are *means.* Their *end* is benefiting those who own them. Boards make sure this is the case; this is the *why* aspect of governance. For nonprofit health care organization boards, the essence of the verb "governing" is advancing and protecting the interests of stakeholders, serving as their agent, and deciding and acting on their behalf.

The owners of commercial corporations are easily identified (everyone who owns stock); additionally, they have roughly similar objectives (wealth enhancement). Things are not so simple in nonprofits. Stakeholders are often vaguely defined (such as "the community") and they typically want different things, some of which can be in conflict with one another. To represent stakeholders, boards must specifically identify the key ones and then understand their needs, demands, and expectations. Governing begins here.

The Board's Fiduciary Duty of Loyalty

All state incorporation laws require boards and directors to discharge a fiduciary duty of loyalty. Loyalty holds that directors, in performing their roles, owe allegiance to the organization and its stakeholders, acting in their best interest rather than for personal gain or the benefit of other organizations, groups, and individuals. All dealings, actions, and decisions of directors in their official capacity must meet two requirements. First, they must have *good faith* intentions, manifesting honesty and a genuine desire to discharge their obligation. Second, they must behave in ways that demonstrate *reasonable belief* their decisions and actions are in the best interest of the organization and its stakeholders.

Health care organization directors breach their duty of loyalty when, for example, a material conflict of interest influences a decision; they disclose confidential information that could have a detrimental effect on the organization; they seize a business opportunity for themselves or other parties that legitimately belongs to the organization; or, in nonprofit, they vote for an unlawful distribution of the organization's assets that subverts its charitable purpose or results in private inurement.

RESPONSIBILITIES

Peter Drucker succinctly defines effectiveness as "doing the right things." To govern effectively, a health care organization board must fulfill four responsibilities and sets of associated duties; this is the *what* aspect of governance.

Responsibility	Duties
Organizational ends	• Formulating a vision; a precise, explicit, "fine-grained," and empowering notion of what the organization should become (on behalf of stakeholders) at its very best, in the future

Organizational ends *(continued)*	• Specifying key goals; the organization's most important specific "accomplishables"; what must be achieved to fulfill the vision • Making sure management strategies are aligned with (and lead to achieving) key goals and the vision
Executive performance	• Selecting the chief executive officer (CEO) • Specifying expectations of the CEO • Assessing the CEO's performance and contributions • Adjusting the CEO's compensation • Terminating the CEO's employment, should the need arise
Quality of care	• Appointing, reappointing, and determining privileges of medical staff members • Ensuring that necessary quality, utilization, and risk management systems are in place and functioning effectively • Monitoring and assessing the quality of care provided and, if problems are detected, expecting corrective action
Organizational financial health	• This responsibility is the focus of Chapter Two

A board must fulfill these four responsibilities, which are legally mandated and functionally necessary. There are many other things that a board and its directors can, and might choose, to do: make personal contributions or solicit funds for the organization, serve as an organizational advocate and spokesperson, and offer advice and counsel to the CEO. Though adding great value if done well, they are optional. Suggestions for performing these tasks are given in the sidebar "Other Board Tasks."

Other Board Tasks

Directors have the right, and may be encouraged, to make personal financial contributions to the organization. However, such contributions should never be the only (or even an important) prerequisite for being nominated to, or continuing to serve on, the board.

Directors often have access to potential donors. Because of their commitment to, investment in, and knowledge of the organization, they can be very helpful soliciting contributions. However, fundraising should be viewed as a supplemental (even a peripheral) activity of the board; it should never overwhelm, displace, or jeopardize fulfilling core governing responsibilities. Fundraising is a distinctive organizational function that is often most effectively conducted by a separate foundation with its own board.

Serving as an advocate for the organization is something expected of every director. However, they should be careful speaking on behalf of the organization; too many people doing so in an uncoordinated way can send confusing and conflicting messages that could do more harm than good. When it is necessary for someone to talk with key external constituents about important issues, consider having the board chair, accompanied by the CEO, make the presentation.

CEOs often, and appropriately, seek counsel from the board chair and individual directors on substantive issues related to the performance of their managerial roles. Because of their familiarity with the organization (in addition to standing outside of it), directors can be quite helpful. But the key here is that when offering such counsel, a director is not acting in a governance capacity and the advice can be accepted or rejected.

ROLES

To fulfill its responsibilities, a board must perform three roles: formulating policies, making decisions, and engaging in oversight. These are the *how* aspects of governance.

Formulating Policies

It is by formulating policies that a board influences an organization, ensuring that it benefits stakeholders and advances their interests. Board policies are declarative statements that direct and constrain subsequent decisions and actions. They are mechanisms for performing two absolutely essential governance functions: first, expressing board expectations of management and the medical staff, conveying what it wants done (acceptable methods) and accomplished (desired results); and second, setting policies that specify delegated authorities and tasks.

Decision Making

Ask what the most important thing a board does, and the answer is typically to make decisions. But board decisions must be grounded on, and flow from, policies (absent this, they risk being idiosyncratic and disjointed) and deal only with the most important organizational issues requiring governance-level involvement. A board has four decision-making options:

1. Retain authority and make a decision itself
2. Request proposals and recommendations (from management and the medical staff) and then decide
3. Delegate decision-making authority with constraints; a decision is handed off to management or the medical staff, but with limitations
4. Delegate decision making by exception; management and the medical staff are authorized to make all decisions in a given area, with the exception of those that have been expressly prohibited or reserved by the board

Examples of Decisions Boards Make

- Are the strategies proposed by management appropriately aligned with key organizational goals and the vision? Should they be approved? (This is a decision regarding *ends.*)
- Did the CEO meet board-specified performance objectives last year? How much of a bonus should he or she be awarded? (This is a decision regarding *executive performance.*)
- Should Dr. __________ be reappointed to the medical staff? Which diseases should she be allowed to treat, and which procedures should she be authorized to perform? (This is a decision regarding *quality.*)
- Should a new audit firm be retained? (This is a decision regarding *finances.*)

Board Policy

There are four different types of policies (see Exhibit 1.2). The board can convey its expectations and directives by being prescriptive (stating "thou shalts") or by being prohibitive (stating "thou shalt nots"). Additionally, policies can focus on either methods or results.

Exhibit 1.2. Types of Board Policies

	Methods	Results
Prescriptions	Policies that prescribe certain methods	Policies that prescribe certain results
Prohibitions	Policies that prohibit certain methods	Policies that prohibit certain results

The most effective policies *prescribe results* and *prohibit methods.* Results are what a board wants accomplished. The best way of conveying them is simply saying "achieve this." As a general rule, a board should avoid specifying methods; there are an infinite number of them, and getting involved in determining the way results are to be achieved bogs a board down in detail. Also, prescribing one method eliminates all others. Doing so takes a board dangerously near, if not across, the line that separates governing from managing. Therefore, if a board must express expectations regarding methods, we recommend formulating policies that restrict, limit, and prohibit—clearly denoting those that are unacceptable.

Engaging in Oversight

The dashboard of your car doesn't give a lot of information. But try driving without it—no gas gauge, speedometer, odometer, battery indicator, oil pressure light, or engine thermometer. In performing the oversight role, a board monitors and assesses key organizational processes and outcomes, answering four questions:

1. Is the organization performing in a manner that protects and advances stakeholder interests?
2. Are the board's expectations, as conveyed in its policies, being met?
3. Are board decisions having the desired impact?
4. Are board directives and constraints being respected as management and the medical staff perform delegated tasks?

GOVERNANCE WORK

A board's job is to formulate policies; make decisions; and oversee ends, executive performance, quality, and finances.

As depicted in Exhibit 1.3, governance work is a three-by-four matrix. To govern effectively, a health care organization board must fill all twelve cells.

The work of a board, when contrasted with the work of management and clinicians, is distinctive for several reasons. First, governance is the ul-

Exhibit 1.3. Governance Work

Responsibilities	Roles: Policy formulation	Roles: Decision making	Roles: Oversight
Ends			
Executive performance			
Quality			
Finances			

timate team sport. A board decides and acts only as a group. Individual directors have no authority or power. Second, it is part-time work. Other key leadership groups have a continuous presence in the organization, but boards do not; they come and go. Third, governance work is fragmented. A board convenes, does its work, and then adjourns. Weeks or months pass before the directors meet again. As a consequence, thrust, follow-through, and follow-up can be difficult to sustain.

GOVERNANCE "ENABLERS"

The work of governing is influenced by a board's structure, composition, and infrastructure.

Structure is the way governance work is subdivided and coordinated, including: board size; number and type of board committees; and, in a system, the number of governing layers and boards. *Composition* is the characteristics of directors in addition to their knowledge, skills, and experience. *Infrastructure* comprises resources such as budget, staff, and information systems.

IN THE BOARDROOM

- ➢ Get a copy of your board's bylaws and review them.
- ➢ Ask for a briefing on your organization's directors and officers (D and O) indemnification policy and liability insurance coverage. It's prudent to have your personal attorney review these documents. In making this suggestion, the intent is not to scare you. Health care organization boards and directors are rarely successfully sued. But keep in mind that there are potential liabilities associated with board service.
- ➢ If you have not had an orientation to the organization (its facilities, programs and services, management team, market and competitors), ask for one.
- ➢ Review your organization's vision and mission statement(s) and key goals.
- ➢ Has your board done a stakeholder analysis? That is, have you mapped key organizational stakeholders and their most important needs and expectations? It's impossible for your board to effectively represent the interest of stakeholders if it hasn't identified them.
- ➢ Does your board have a precise, coherent, and shared fix on its obligation, responsibilities, and roles? Your board will not be effective if directors have differing definitions of the why, what, and how aspects of governance.