



YOUR DELAWARE ADVANTAGE

Healthcare Compliance Symposium: Compliance Responsibilities of Boards

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Disclaimer: This presentation is for informational purposes only and does not constitute legal advice. You should consult with your counsel to obtain advice with respect to any particular issue or problem.



Role of Boards

Role of Boards

- The proper role of the board is to manage, direct, and oversee the affairs of the corporation.
- The board functions as a decision-making body, and members ordinarily have no power to act on an individual basis on behalf of the board or the organization.
- Nonprofit board members sometimes take a more direct role in certain aspects of the day-to-day affairs of the corporation.
 - However, this direct involvement ordinarily does not occur in one's capacity as a board member, but more likely, in one's capacity as an officer, committee member, or volunteer.



Role of Boards

Typical Board Responsibilities

- Establish a mission and organizational values and ensure that these are upheld by the board, management, employees and volunteers.
- Approve significant policies and policy changes.
- Act as stewards of the corporation's human and financial resources.
- Ensure that the corporation's resources are appropriately invested and applied in fulfilling the mission, and promote development of new resources.
- Ensure compliance with the organizational documents of the corporation and the board's fiduciary duties.
- Establish long-range plans consistent with the mission and organizational values.
- Approve significant changes to organizational structure and technological utilization that affect the corporation's ability to fulfill the mission.
- Develop strategies and approve proposals for significant relationships.
- Hire, fire and supervise the chief executive officer / executive director



Role of Boards

Typical Board Responsibilities (cont'd)

- In addition to the foregoing responsibilities, boards also:
 - Approve an annual operating budget;
 - Oversee regulatory compliance and financial integrity;
 - Establish internal control procedures and review compliance with such procedures;
 - Select an independent auditor;
 - Review technology plans for the corporation;
 - Approve significant transactions and contracts;
 - Elect and remove officers of the corporation; and
 - Periodically review the certificate of incorporation, bylaws, committee charters, and organizational policies to ensure, among other things, conformity with the corporate mission, compliance with tax and other applicable laws and regulations, and compliance with corporate laws and governance best practices.



Duties of Board Members

Duties of Board Members: Fiduciary Duties

- Under Delaware law, board members are charged with the following fiduciary duties to the corporation and its members:
 - Duty of Care; *and*
 - Duty of Loyalty (including an obligation to act in Good Faith).
- In addition to traditional fiduciary duties, the members of the governing body of a nonprofit nonstock corporation also owe a special duty to advance the charitable goals of the corporation and protect its assets.
 - For-profit boards are focused on maximizing shareholder value
- The Delaware Supreme Court has emphasized that “fiduciary duty does not operate intermittently but is the constant compass by which all [board members] actions for the corporation ... must be guided.” *Malone v. Brincat*, 722 A.2d A.2d 5, 10 (Del. 1998).



Duties of Board Members: Fiduciary Duties

Duty of Care: General Standards

- Focuses on the process by which a decision is made.
- Requires board members to exercise the same degree of care and prudence in managing the business and affairs of the corporation as would be expected of them in the management of their own affairs.
- Board members must inform themselves of all reasonably available information that is material to their decision.
- Board members should take sufficient time to deliberate regarding their decisions, including time to consider the information before them, to ask appropriate questions of management and advisors, and to deliberate among themselves.
- Delaware law applies a “gross negligence” standard in determining whether a business decision reached by a board was sufficiently informed to satisfy the board members’ duty of care.



Duties of Board Members: Fiduciary Duties

Duty of Loyalty: General Standards

- The duty of loyalty requires board members to act in a manner that they reasonably believe to be in the best interests of the corporation.
- At its core, the duty of loyalty requires board members to place the interests of the organization ahead of their own interests.
- The duty of loyalty is implicated if the board member has a material conflict of interest or lacks independence from someone who has a conflict of interest with respect to the matter under consideration.
 - Conflicts of interest may arise, for example, if a board member (or a family member) is employed by or invested in an entity with which the corporation is dealing or if a board member is performing professional services for the corporation, such as an insurance agent, attorney, or real estate broker.
 - Boards should not assume that a conflict cannot exist for a board member who receives no direct monetary or other tangible benefit from a transaction with the corporation.
- Subsumed within the duty of loyalty is the requirement that board members act in good faith. Good faith requires members to act in the best interests of the corporation and act honestly and in a manner that is not knowingly unlawful.



Duties of Board Members: Fiduciary Duties

Oversight Obligations

- Board members' fiduciary duties give rise to oversight obligations requiring them to confirm that policies and procedures are in place to ensure that the corporation complies with applicable regulatory, legal, and financial requirements.
- Under Delaware law, board members may be liable for breach of their fiduciary oversight obligations if:
 - They utterly fail to implement any reporting or information systems or controls; *or*
 - Having implemented such a system or controls, they consciously fail to monitor or oversee the corporation's operations, such that they are disabled from being informed of risks or problems that require their attention. *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006).
- “Where [board members] fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith.” *Id.*



Duties of Board Members: Fiduciary Duties

Oversight: Practical Guidance

- Delaware courts expect boards to establish appropriate oversight and controls at the board level to ensure that the corporation complies with all applicable legal and regulatory requirements, and to be vigilant in monitoring the corporation's operations and ensuring the effectiveness of its audit and compliance functions.
 - The standard for liability for oversight claims is stringent, but implementing best practices rather than industry minimums should be the goal.
- The duty of oversight is particularly important for corporations in highly regulated areas, such as health care.
- Areas of concern / high risk for healthcare operations may include:
 - Billing and documentation requirements for Medicare and other payers;
 - Procedures for handling controlled substances;
 - Professional licensing for staff as well as entity level licensing;
 - Referral relationships; and
 - Compliance with HIPAA privacy and security regulations, and any other applicable data security requirements.
- Boards should monitor trends in industry enforcement actions and litigation.





Rights of Board Members

Rights of Board Members

- Board members are entitled to receive information necessary to fulfill their duties, including evaluating matters they are asked to approve and fulfilling their duty of oversight.
- Board members have a right to receive copies of all of the minutes of full board meetings as well as committees of the board.
- Board members have the right to inspect the books and records of the corporation.
 - For a proper purpose, which is one that is reasonably related to such member's position as a member.
- Board members are entitled to notice of meetings of the board.
 - Regular meetings of the board may be set pursuant to a resolution of the board and further notice is not required unless otherwise specified therein.
 - Notice of special meetings of the board is required.
 - If notice is not properly provided, members may, at the outset of a meeting, object to the holding of such meeting.
- Board members have a right to vote against matters put to a vote of the board and have their dissent noted in the minutes for the meeting.



Liability of Board Members

Liability of Board Members

- To whom may board members potentially be liable?
 - Board members may be liable to the corporation itself, its members, and the constituencies served by the corporation.
- Liability of the corporation
 - Even if board members are not liable, the corporation may still be liable for violations of law, such as, breach of contract, tort (e.g., harm caused through negligence), or failure to comply with tax regulations or employment laws.
 - The corporation may also be liable for damages based on negligent acts or omissions from a volunteer under the doctrine of respondeat superior.
 - Board members should be aware of the potential liabilities of the corporation and take steps to implement oversight procedures designed to limit such claims.





The Role of Boards in Compliance

The Role of Boards in Compliance

- Compliance promotes the prevention, detection, and resolution of actions that don't conform to legal, policy or business standards.
- Boards promote compliance by:
 - Forming a clear mission statement for the organization.
 - Carefully selecting and supervising outside advisors.
 - Observing corporate formalities.
 - Compliance with corporate formalities is just as important for nonprofit corporations as for for-profit corporations.
 - Commonly encountered problems with respect observation of corporate formalities include:
 - Failure to properly elect board members;
 - Formalities of acting at meetings of the board;
 - Formal record keeping;
 - Delegation of board functions to committees that include persons who are not board members; and
 - Failure to comply with corporate statutes and organizational documents.



The Role of Boards in Compliance

- Establishing formal lines for reporting potential compliance issues not only to superior officers but also directly to the board.
 - To have an effective compliance program, the organization should have a compliance officer, a culture of compliance, and oversight of the compliance program by the governing board.
- Adopting a plan that addresses how the board will stay up-to-date on ever-changing legal and regulatory requirements that impact the organization.
 - Periodic updates from informed staff during regular meetings
 - Presentations by outside advisors
 - Recruit knowledgeable board member(s)
 - Attend outside training programs
 - Goal: understand the business climate in which the organization operates and have enough understanding to ask the right questions of management to make the best decisions and identify risk areas



The Role of Boards in Compliance

- If an organization deals with federal health care programs, the government expects the organization's board to be well educated and involved in the compliance program.
 - Refer to OIG publication: *Practical Guidance for Health Care Governing Boards on Compliance Oversight* (2015).
- Organizations must provide training to board members to address the responsibilities of board members regarding corporate governance and review and oversight of the organization's compliance program.
 - Training should address the unique responsibilities of the healthcare board members, including the risks, oversight areas, and strategic approaches to conducting oversight of a healthcare entity.
 - Training should emphasize the role of the board in setting the tone for a culture that promotes integrity and ethical conduct based on the organization's values. Board members should understand that they are expected to “walk the walk” and serve as examples of compliant and ethical behavior. Board members should be visible to the organization.
- Boards should conduct self-assessments, including committees.



Compliance Hypothetical

Compliance Hypothetical

City Healthcare is a large urban healthcare system. It has extensive policies and procedures for HIPAA compliance, including a notice of privacy practices and security protocols, and it regularly trains staff on privacy and security requirements. In 2017, City engaged an IT consultant to perform a security risk assessment. The consultant found that City had implemented multiple measures and best practices to protect against unauthorized access to protected health information, including unique logins, strong passwords, system logs, dual factor authentication for remote access, and laptop encryption. Still, the consultant recommended that City take additional actions to protect against data breaches, including penetration testing, staff education on phishing scams, regular testing of system back-ups, and regular system log audits to detect possible data intrusions. Copies of the IT consultant's report and recommendations were provided to City's management team and the Audit Committee of City's board.

In November 2019, City was the victim of a ransomware attack that encrypted several critical systems, including electronic health records of 50,000 patients. System back-ups were unavailable. System logs reflected evidence of unusual activity dating back to August of 2018, but had not been reviewed. City paid the ransom to restore access to the critical files. Breach notifications followed.



Compliance Hypothetical

- Does City's board bear any responsibility for the ransomware attack and possible breach?
- What are the potential exposures?
 - Allegations in data breach cases have included breach of fiduciary duty, invasion of privacy, negligence, breach of implied contract, and violation of various state and federal statutes.
 - In the for-profit context, a shareholder derivative action could be brought against the corporation's directors and officers. In its 1996 *Caremark* decision, the Delaware Chancery Court declared that, in such actions, directors can be held personally liable for failing to "appropriately monitor and supervise the enterprise."
 - Directors and officers should be wary of demonstrating a "conscious disregard" for their duties or ignoring "red flags" – doing so can result in a director or officer being held personally liable for a corporation's losses.



Compliance Hypothetical

- Seeing these types of claims in large data breach incidents: Target, Yahoo, Experian
- Steps A Board Could Take to Protect The Organization
 - Hire a Chief Information Security Officer and engage outside technical experts to conduct regular risk assessments and to educate officers and board members on data security
 - Appoint a board committee that is focused on data security
 - Regularly address and deliberate when deciding issues of data security, and carefully document the deliberations to demonstrate appropriate care
 - Conduct training sessions to increase awareness of data security issues at all levels of the organization
 - Ensure that there are pathways for reporting issues and concerns directly to the board
 - Adopt a security plan that is tailored to the organization's specific risks and regularly review and assess those risks; adjust plan as necessary
 - Follow up to ensure that identified risks have been addressed



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