

The following developments from the past month offer guidance on corporate law and governance law as they may be applied to nonprofit health care organizations:

1. STATE AG JURISDICTION

A [newly released outline](#) offers general counsel useful, basic guidance on the role and authority of the state attorney general. Prepared under the direction of the prestigious National Attorneys General Program at Columbia Law School, the outline addresses such important topics as the common law powers of the state attorney general, the issuance of opinions, its control of litigation and its areas of functional responsibility (e.g., charitable trusts, criminal law, Medicaid Fraud). While not specifically focused on either health care or nonprofit organizations, it may nevertheless be a useful resource for the general counsel given the AG's broad authority over nonprofit health care organizations. Indeed, the outline was used by Columbia Law to brief newly elected state attorney generals on the duties and responsibilities of the office of state attorney general.

2. COMMITTEE PRACTICE

A new [whitepaper from Stanford University](#) provides useful guidance on trends in standing committee formation, composition and structure. In particular, the report highlights the importance attributed to the distribution of knowledge and workload across board committees. Key findings were that the audit and compensation committees had the heaviest workload of all board committees, and that knowledge-sharing benefit arises from board structures featuring overlap amongst the composition of key committees. The importance of monitoring individual director "busyness" was also identified. The use of a "committee as a whole" practice remains at low levels and is more common among small companies. The whitepaper suggests that greater board attention be given to policies on committee assignment, rotation and workload. This report might be shared with the board's governance committee.

3. DONOR DISCONTENT

According to a recent [The Wall Street Journal report](#), charities are witnessing an increase in the number of donor requests for refunds of charitable gifts. This, despite the traditional interpretation of a charitable donation as a "contract" between the donor and donee. The "refund" movement is attributed to greater attentiveness by donors to application of their gifts, and to concerns with misuse or mismanagement by the charity/donee. While such a refund request may be less disruptive than donor-(or AG) instituted litigation, it speaks to the need for a "meeting of the minds" as to donor intent. It also underscores the need for the general counsel to work directly with the development office in the structuring and monitoring of written gift agreements. Applicable state law should also be considered as it relates to a donor's standing to enforce the terms of his/her gift.

4. RISK OVERSIGHT PRACTICES

A new [survey from the National Association of Corporate Directors](#) concludes that many board members seek refinements in the allocation of risk oversight responsibility. A particular concern is that risk oversight has not been assigned to the proper board group, or that there is unnecessary duplication of effort on risk oversight amongst board committees. An additional concern is that the level of cyber and IT risk related information provided by management to the board may be inadequate. A third concern is with agenda allocation; a perceived discrepancy between the issues considered most important by directors, and those issues on which the directors spend the most time. Collectively, these concerns reflect the obligation of the board to adopt effective risk management oversight practices.

5. "DIRECTOR REFRESHMENT"

The ongoing [debate on director terms](#) was highlighted in a recent article in [The Wall Street Journal](#). The article reports that many boards are experiencing increased pressure on older and long serving directors to retire. While this movement

recognizes the value of deeply experienced directors, that value may be offset by a decreasing ability to stay current with industry changes. While some boards are responding with specific tenure limitations, resignation on “change in status” and mandatory retirement policies, others are using the need for new competencies to achieve board refreshment.

6. DIRECTORS' DUTIES TO CREDITORS

A recent [Delaware Chancery Court decision](#) clarifies the duties of directors of insolvent companies, especially as they may relate to creditors. In particular, the decision confirmed that Delaware law no longer recognizes a shift in directors' duties to creditors once a company moves into the “zone of insolvency”. Vice Chancellor Laster concluded that while insolvency may mark a shift in Delaware law, it does not refer to an actual shift of directors' duties to creditors. Rather, it refers to a shift in the ability of creditors to bring derivative actions for breach of fiduciary duty—which is not a special right. In other words, directors owe no special duties to creditors (e.g., preservation of capital and resources) once the company is in, or approaching, insolvency. This decision should greatly reduce concerns with the scope of fiduciary duties owed by health system directors as their system approaches financial distress.

7. CORPORATE CODE OF CONDUCT

The importance of an [effective code of corporate conduct](#) as a disciplinary device has been demonstrated in two separate controversies involving senior executives of large corporations. In one instance, an apparel company revised its code to clarify expectations of officer and director conduct following the termination of the CEO for misconduct and violations of company policy. In another instance, the compensation of the CEO of a major manufacturing company was reduced after he was determined to have violated company policy by an inappropriate personal relationship with a consultant to the company. These incidents are consistent with an increasing unwillingness of boards to tolerate what they perceive as flawed leadership traits of senior executives. The audit committee (in consultation with the general counsel) may thus wish to increase its focus on how a properly enforced code of conduct can incentivize appropriate behavior.

8. JOINT OPERATING COMPANIES

General counsel advising their system clients on the efficacy of joint operating companies will want to review the [recent decision of the U.S. District Court](#) (Southern District of Ohio) in *Medical Center at Elizabeth Place, LLC v. Premier Health Partners*. The case had been filed by “MCEP”, a small adult care facility, alleging that the defendants’ “joint operating agreement” violated certain antitrust laws (e.g., the Sherman Act). In ruling for the defendants, the District Court’s opinion provides generally helpful guidance on the antitrust treatment of bona fide joint operating companies. A key fact the court found nearly dispositive was that the participants in the JOA shared the risk of loss as well as the opportunity for profit by financially integrating their operations – a core provision of most JOAs. The decision provides additional antitrust-related comfort for health systems considering the joint operating company model to achieve a corporate alliance.

9. SEARCH COMMITTEES

A recent [report published by Challenger, Gray & Christmas](#) concludes that the healthcare industry was the leader across all industries in the extent of CEO turnover this year to date. According to the report, resignation was the most common basis for CEO departure, followed by retirement and “stepping down”. The Challenger, Gray report underscores the value of sophisticated board level executive evaluation, talent development and search and succession practices. The report is also consistent with broader industry trends reflecting high CEO turnover rates. The report speaks, indirectly, to the value of an ongoing relationship with a competent executive search advisor.

10. FINAL “501(r)” REGULATIONS

The board’s compliance committee should be briefed by the general counsel on the newly issued [final regulations](#) governing hospital charitable status, as initially provided for in the Affordable Care Act. While the final regulations don’t contain any huge surprises (positive or negative), they do identify several provisions that must be included in a charitable hospital’s financial assistance and related policies. They also provide helpful clarification on requirements relating to community health needs assessment, financial assistance policies, limitations on charges and certain collection practices. Failure to comply with the final regulations is grounds for significant penalty excise taxes or even loss of exemption. More significantly, the regulators’ issuance in final form suggests the beginning of more focused IRS enforcement. The general counsel can “team” with the corporate compliance officer with respect to the preparation and subsequent monitoring of “501(r)” policies and procedures.

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