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Knowledge Resources for Governing Effectiveness

The Board's Fiduciary Responsibility: Putting the Community's Trust into Action

In any venue, fiduciary responsibilities have to do with issues of trust and confidence. In the realm of hospital governance, it is imperative that hospital governing boards understand their particular fiduciary role as it pertains to accountability, financial responsibility, confidentiality and integrity.

For hospital governing boards, fiduciary responsibilities and their related issues of accountability and trust are complex. Boards have a two-way responsibility: they must act in the best interests of both the hospital and the communities their hospital serves.

In today's economic environment, it is particularly important for governing boards to earn and keep the public trust. In the handling of finances, identifying of community needs and assessment of programs and services, governing boards can and must be held accountable to the people of the communities they serve. There can be no room for question of integrity or credibility of board members. ***Trust is an asset no board can do without.***

What are "Fiduciary Responsibilities?"

Legally, board members must take particular care to:

- Become thoroughly informed before making a business decision *(Duty of Care)*
- Put the needs of the organization first when taking responsibility for its operations *(Duty of Loyalty)*
- Abide by laws, regulations and standards of the organization's operations *(Duty of Obedience)*

These three main responsibilities are usually referred to as the Duty of Care, the Duty of Loyalty, and the Duty of Obedience. Each may be applied in a court of law to determine whether or not a board member has acted improperly. They are to be taken seriously by every person accepting a position on a board of directors.

Duty of Care. When engaging in organizational business, board members must use the same level of judgment they would use in their own personal business activities. The tenets are primarily common sense:

- Obtain necessary and adequate information before making any decisions
- Act in good faith
- Make decisions in the best interest of the organization
- Set aside personal interests in favor of those of the organization

Individual state courts often further define board members' fiduciary duties, as does the U.S. Internal Revenue Service (IRS). The IRS, in recommendations for board members, encourages putting policies and procedures in place to ensure that each board member is totally familiar with the organization's activities, that every activity promotes the mission of the organization and helps it achieve its goals, and that each board member should be fully informed about the organization's financial status.

Duty of Loyalty. The duty of loyalty bars board members from using their board positions to serve themselves or their businesses. When acting in their fiduciary capacity, the duty of loyalty requires that board members place the interest of the organization before all else. Board members must be:

- Objective and unbiased in their thinking and decision-making
- Free from external control and without ulterior motives
- Free of any conflict of interest when discussing issues and making decisions
- Able to observe total confidentiality when dealing with organizational matters

Carrying Out the Board's Fiduciary Duties

The Duty of Care is fulfilled by…

- Consistent attendance at board and committee meetings
- Attentive and introspective preparation for board meetings
- Obtaining and reviewing relevant data and information before voting to ensure evidence-based decisions
- Exercising independent judgment
- Periodic examination of the performance of the executives and board members who lead the organization
- Meaningful review of the organization's finances and policies

The Duty of Loyalty is carried out by…

- Full disclosure of potential conflicts of interest
- Compliance with the organization's conflict of interest policy
- Avoidance of the use of corporate opportunities for personal gain or benefit
- Maintaining confidentiality when required

The Duty of Obedience is carried out by…

- Strict adherence to the bylaws of the board and the mission of the organization
- Compliance with all regulatory and reporting requirements
- Understanding of all documents governing the board and its operation (bylaws, articles of incorporation, board and committee job descriptions, charters, etc.)
- Ensuring that decisions further the organization's mission and comply with the scope of its governing documents

To identify potential conflicts of interest, board members and staff should annually disclose, in writing, any known financial interest with any business entity that transacts business with the organization or its subsidiary businesses.

The IRS recommends creating written procedures for determining whether a relationship, financial interest or business affiliation results in a conflict of interest, and outlining a course of action in the event that a conflict of interest is identified.

Duty of Obedience. The duty of obedience requires board members to be faithful to the organization's mission, and to follow all state and national laws, corporate bylaws, rules and regulations when representing the interests of the organization.

Board members, in carrying out their duty of obedience, will protect the limited resources of the organization to ensure optimal services and benefit to the community. They will ensure legal compliance with all applicable laws and regulations.

The IRS recommends several board actions to promote good governance practices related to the board's duty of obedience:

- Develop both a code of ethics and whistleblower policies
- Adopt and monitor specific fundraising policies
- Carefully outline and determine compensation practices
- Develop and strictly adhere to document retention policies

Two Roadblocks to Fiduciary Effectiveness

Strong boards are independent-minded, curious, and able to focus on what matters most. Their members are willing to challenge status-quo thinking and stretch themselves intellectually.

Weak boards are the opposite—complacent and submissive. Their members do not ensure that all sides of issues are considered, or that "conventional wisdom" is challenged. Weak boards are not likely to successfully carry out their fiduciary responsibilities.

There are two true roadblocks to any board's ability to maintain fiduciary effectiveness: 1) a tendency toward "rubber stamping;" and 2) a tendency toward micromanagement. Both are most likely to occur when a majority of members lack interest, drive or the ability to speak from the shadow of one or more overbearing board members.

Rubber Stamping. Members of rubber-stamping boards fail to ask pertinent questions or engage in deliberative dialogue on solutions to challenges, and do not work successfully together to arrive at independent-minded decisions. They accept recommendations with little questioning or debate, and fail to explore alternatives and scenarios that may reveal the weaknesses of arguments or positions.

Rubber-stamping boards are often a result of overly dominant individuals and weak board chair leadership. A strong board chair will ensure that every board member is meaningfully engaged in constructive thinking and deliberation on the important issues that come before the board.

From a legal standpoint, individual members of a rubber-stamping board may be considered negligent and liable for their actions or inactions, and may be held personally liable for a lack of adequate oversight.

Micromanagement. It's often a challenge for board members to see the fine line between management and governance. Board members must understand that they are expected to be leaders and overseers, not managers and implementers. They should be concerned with the "what," not the "how." Micromanagement is a term generally applied to boards that pay too much attention to details, and not enough attention to the "big picture" strategic issues and implications.

It's up to everyone on the board to guard against micromanagement. The board chair should ensure that its members understand their roles, and consistently adhere to them. In addition, the CEO needs to be willing to candidly discuss problems of micromanagement with the board chair to work out board-driven solutions to this problem.

Maintaining the Public Trust

Whether a board member is serving for the first time or has been in the role for a number of years, it behooves every organization to have each board member review these fiduciary responsibilities. Demonstrated personal accountability and acceptance of responsibility are key. No board can afford to lose the public trust.

The bottom line is that board members must act in such a manner that protects both the organization's operations and the community's trust.

Sources and Additional Information

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