BOARD LEADERSHIP

POLICY GOVERNANCE IN ACTION

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How are board members' legal obligations met in a Policy Governance framework?

The Legal and Fiduciary Duties of Directors

by Jim Hyatt and Bill Charney

Board members generally recognize that they have "legal duties" but rarely have even the most basic knowledge of what these responsibilities are. In today's competitive environment, such a lack of understanding involves enormous risk. Unprecedented headlines about boardroom debacles, shareholder lawsuits being heard in jurisdictions previously considered favorable to corporate interests, and the passage of the Sarbanes-Oxley Act and widespread anticipation of similar legislation affecting the nonprofit sector have raised many new questions about Policy Governance and how it might help boards and board members fulfill their legal duties. In this article, Jim Hyatt and Bill Charney provide a primer on these basic responsibilities.

If, as John Carver asserts in his article in this issue, "proper leadership requires a board to accept and even accentuate its accountability for organizational performance, circumstances, activities, and status," how does a board weigh payoffs in organizational performance against potential liability? What standards will apply to board actions and decisions should they turn out poorly? Where does the board look for guidance as it navigates among the myriad issues confronting any modern enterprise?

As servant-leaders on behalf of the ownership, boards should not overlook common sense. If the decision the board is contemplating would cause embarrassment when viewed in a public spotlight or on the pages of the local newspaper, the board probably shouldn't adopt it. Consultation with legal counsel is another obvious place to turn, if these advisers are competent in the particular field of law relevant to the decision at hand.

But what principles underlie the legal questions pertaining to the litany of decisions a board is called on to make?

All boards, be they for profit or nonprofit, are subject to several underlying

(continued on page 2)

ALSO IN THIS ISSUE

LEGAL CONCERNS WITH POLICY GOVERNANCE 4

THE CONTRAST BETWEEN ACCOUNTABILITY AND LIABILITY..... 5

ON A PERSONAL NOTE

POLICY GOVERNANCE AND THE LAW

by John Carver

This issue of *Board Leadership* and the next focus on legal aspects and implications of the Policy Governance model. Although *Board Leadership* must disclaim any pretension to giving legal advice, the opinions of the lawyers and others in these issues may nonetheless be useful as boards consider their legal obligations.

It is obviously wise for board members to check the legality of their governance practices carefully, in terms of both what they do and what they fail to do. Consequently, it is unusual for a board *not* to ask whether governance behavior built on Policy Governance is unlawful or unnecessarily exposes it to liability. Boards also sometimes worry about the public's or other observers' opinions about their practices. Because that is a political matter rather than a legal one, it is not covered in these special issues.

We have found it useful to divide boards' legal concerns into two parts,

(continued on page 3)

Fiduciary Duties

(continued from front page)

principles that have evolved over time into a series of related duties. Many directors are generally familiar with concepts such as the duty of care and the duty of loyalty and have a rough idea as to their meaning. In both the Canadian and American systems of jurisprudence, these duties derive primarily from our heritage of English common law, though these concepts find similar expression in many other systems of law around the world. These duties seem very broad and general in scope at first reading, much like a "global" policy statement in any of the four Policy Governance categories. Their application, however, finds more specific expression in the particular facts and circumstances of a case as the judge or jury assesses whether the board's course of decisions and actions was appropriate. In doing so, these "triers of fact" look to prior cases to see what other courts had to say under similar circumstances.

As the legal principles evolve, bear in mind that *standards of appropriate behavior also change over time.* For example, prior to the rash of corporate scandals involving Enron, WorldCom, Tyco, and their ilk, board audit committees conducted more cursory reviews of financials, and meetings with independent auditors were much shorter in length and narrower in scope than they are today. Since the passage of the Sarbanes-Oxley Act in 2002, billions of dollars have been spent across the United States implementing the systems and controls now required by law. Audit meetings that formerly ran for a few hours now extend all day or into the next as directors scrutinize corporate statements and question both management and auditors closely. (Bear in mind that before or after Sarbanes-Oxley, this scrutiny has been and generally continues to be conducted in the absence of *any* prestated criteria.) What has transpired in the world of public companies as a result of Sarbanes-Oxley is now finding its way into the "best practices" of private and nonprofit organizations as well.

This is but one obvious example of how the duty of care has found a more explicit expression in today's boardrooms, but there are others. In fact, the line is moving all the time as cases wend their way through the court systems and government increasingly prescribes appropriate conduct. The overriding issue of concern to Policy Governance practitioners is that these efforts also acknowledge and incorporate principles of sound governance. Boards that apply Policy Governance principles find that they can not only meet but actually exceed today's legal standards. Policy Governance boards can have their cake and eat it too!

With this in mind, let us examine the general principles of board conduct, these fiduciary duties, in more detail. The first question to ask is, why are they "duties"? Why not simply call them "principles"? The answer lies in the law of negligence.

In a legal action against a director or directors for negligence, a plaintiff must show that the director owed the plaintiff a duty, that the director breached that duty, and that the plaintiff has suffered some foreseeable loss as a result of this breach. Absent the existence of a duty, the claim will not be heard. A potential plaintiff claiming that the board "wasted corporate assets," for example, must first describe the duty or duties the board owed before proceeding to the facts of the case. Here's where a plaintiff will begin.

The Duty of Care

State and provincial statutes in the United States and Canada have codified the duty of care. The language may vary slightly, but the elements are the same: a director's duties shall be discharged in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner that the director reasonably believes to be in the best interests of the corporation (its shareholders, owners, or other stakeholders).

Exercise of the duty of care takes several forms, depending on the particular circumstances.

1. *Active participation.* A director must actively participate in the governance of the organization. Policy Governance systematizes such functions as linking with ownership, setting appropriate policies, effective delegation, and monitoring and evaluation of performance against criteria.
2. *Committees.* A board may delegate some of its authority to committees to support its work, but the board remains responsible for all committee activity. To the extent that one or more committees help the board perform its governing tasks more effectively, the board as a whole is more able to meet its duty of care.
3. *Board actions.* When present at a meeting, a director is presumed to have agreed to actions taken by the board unless (a) the director objects to the lawfulness of the meeting itself (it was improperly called or convened) *and doesn't participate* or (b) the director either votes against the action or is prohibited from voting due to a conflict of interest.
4. *Minutes of meetings.* Written minutes should be taken at every board meeting. The minutes should accurately reflect actions taken by the board.
5. *Books and records.* A director should have general knowledge of the books and records of the organization, including its financial statements, as well as its operations. The organization's articles, bylaws, accounting records, voting agreements (if any), and minutes must be made available to members and directors who wish to inspect them for a proper purpose.
6. *Accurate record keeping.* A director should ensure that the organization's records and accounts are accurate. This may include regular audits by an independent auditor but should at least require a system of proper internal controls.
7. *Trust property.* A director has the duty to protect, preserve, invest, and manage the corporation's property and to do so in a manner consistent with donor restrictions and legal requirements. Directors of charitable trusts are held to a higher standard of care than those of other organizations.
8. *Resources.* A nonprofit corporation director must ensure that the organization has adequate resources to enable it to further its charitable

(continued on page 6)

Personal Note

(continued from front page)

one with more immediate utility and one with longer-range implications. The former considers the practice of Policy Governance under existing legal requirements. The latter considers the evolution of the legal requirements themselves—easily overshadowed by the immediacy of the former. (For the purposes of these discussions, we will consider regulations to be "legal requirements" if they are promulgated by an authority with proper jurisdiction.) Let us look, then, at these two aspects of boards' concerns about lawfulness and law.

The Effect of Law on Boards

Requirements vary from one jurisdiction to another, but a board's *relationship* to the law is virtually the same everywhere. Board members look to the law to define the legal obligations of governance—as they should—but make the mistake of relying on the law for guidance on governance theory and practice. They fail to recognize that legislators are not necessarily the most advanced thinkers on governance.

The board's obligation is to govern well on behalf of its ownership *and* to obey the law. Carrying out the first part of that duty does not ensure discharge of the second. But just as certainly, satisfying the second part does not ensure fulfilling the first. Although it might seem counter-intuitive, achieving both objectives is best attained by considering the exigencies of governance first and the requirements of the law second. Accordingly, we have long counseled our clients to first design the most responsible governance they can and only then employ legal counsel to check for adjustments needed to ensure lawfulness. It seems prudent to recognize that a law degree does not guarantee governance expertise; it guarantees *legal* expertise. For that reason, even competent legal counsel can be problematic if the lawyer does not understand the Policy Governance model.

To witness the clash of law and sensible governance, one need go only as far as the nearest public school board. Nearly all school boards are required to take the ridiculous action of approving all or almost all hirings, even in large systems. Policy Governance does not call on boards to violate the law, but it obliges them to recognize unintelligent law for what it is. With this insight, steps can then be added to the streamlined Policy Governance process that enable fulfilling the law without sacrificing superior governance. This best-compromise outcome is less likely if the board begins with legal requirements and then tries to tweak them into good governance; hence the one-two sequence that we recommend.

So the question before a board setting out to govern with excellence is, first, what is the best way to fulfill our obligation to the owners and, second, what adjustments must we make to achieve and maintain lawfulness? Legal counsel is indispensable for the latter part of this two-part obligation.

The Effect of Boards on Law

In the long run, there is little excuse for lamentable conditions to be tolerated. Laws are written by people and can be changed by people. In fact, in a fast-changing world, the law—which tends to change slowly—is doomed to being antiquated at least some of the time.

The law has valid authority over our actions not because it is right but because our social contract demands it. That means that while boards should strive to obey the law, they need not accept the law either as immutable or as conceptually authoritative. Because of an obligation to their ownerships, boards have a duty to strive for changes in law that are more conducive to responsible and effective governance. Boards should be thought leaders, not passive recipients of legislative action.

When the law does change, it frequently does so in piecemeal jerks as legislators react to popular unrest, crises, or opportunistic advantage. U.S. Senator Olympia Snowe (R-Maine) said, "It always takes the immediacy of the problem to get any reaction here in this institution [the Senate]. We're not exactly visionary, if you hadn't noticed." Theory-informed

(continued on back page)

The Policy Governance Model

Board leadership requires, above all, that the board provide vision. To do so, the board must first have an adequate vision of its own job. That role is best conceived neither as volunteer-helper nor as watchdog but as trustee-owner. Policy Governance is an approach to the job of governing that emphasizes values, vision, empowerment of both board and staff, and the strategic ability to lead leaders.

Observing the principles of the Policy Governance model, a board crafts its values into policies of the four types below. Policies written this way enable the board to focus its wisdom into one central, brief document.

Ends

The board defines which human needs are to be met, for whom, and at what cost. Written with a long-term perspective, these mission-related policies embody most of the board's part of long-range planning.

Executive Limitations

The board establishes the boundaries of acceptability within which staff methods and activities can responsibly be left to staff. These limiting policies, therefore, apply to staff means rather than to ends.

Board-Executive Linkage

The board clarifies the manner in which it delegates authority to staff as well as how it evaluates staff performance on provisions of the Ends and Executive Limitations policies.

Governance Process

The board determines its philosophy, its accountability, and specifics of its own job.

What kinds of policies arouse questions from legal counsel, and why?

Legal Concerns with Policy Governance

by Jim Hyatt and Bill Charney

WHENEVER WE HELP a board develop governing policies, we recommend that the resulting document be reviewed by the board's legal counsel to ensure compliance with applicable statutes prior to its formal adoption. Over the years, many attorneys in numerous jurisdictions have vetted policies developed pursuant to Policy Governance principles with little or no comment. But some attorneys do raise objections. Ours is a litigious society, and attorneys are ever on the lookout for potential sources of exposure to liability. So every now and then, we do encounter policies that some attorneys consider problematic. These may have arisen out of a specific case in a particular jurisdiction or a novel theory of liability on the part of a plaintiff's attorney that prompts legal counsel to seek to protect clients from a perceived threat. In any case, when attorneys' comments or opinions are provided, we have noticed, certain policies receive more attention than others.

Treatment of Staff

The "Treatment of Staff" policy language commonly used and embraced by many boards (and their attorneys) raises perhaps the most consternation with other lawyers. Some fear that a broad written policy precluding "unfair treatment" of staff creates "rights" for employees that could be the basis for employee lawsuits. Some even advise against informing staff of the policy, and the CEO's interpretations of it, for fear that doing so implies a promise that invites legal action if an employee feels that the promise has been broken. They maintain that the policy should be a private matter between the CEO and the board. Consider the implications of this approach.

A job applicant asks the interviewer what the company culture is like. Are employees treated fairly, with dignity? What is the interviewer to say? If she says yes, the applicant may have a basis for a lawsuit at some point when he believes he has not been treated fairly. If the interviewer says no, the applicant goes elsewhere. So she says nothing and refers the applicant to the company's personnel manual.

The board faces a choice: be proactive or defensive. If it accepts legal counsel's advice to avoid making a statement about staff treatment, the board retreats into its shell, doing and saying only what an attorney recommends in order to minimize possible exposure. Counsel's job, after all, is to protect the organization from potential claimants. But can a board *lead* the organization from such a defensive stance?

Policy Governance provides the means for boards to lead proactively, clearly stating their values. An employee might use the board's own words to claim the right to expect fair treatment. We ask, under what circumstances should an employee not be treated fairly and with dignity? Or is there value in a board's articulating a commitment to and the expectation of a culture of fairness and dignity among employees that compensates for the potential risk that is perceived by some attorneys?

Accountability of the CEO

Attorneys occasionally express concern that a policy stating that a board will view CEO performance as "mirroring" that of the organization gives a terminated CEO additional legal claims. The policy language in question typically states, "The board will view CEO performance as identical to organizational performance, so that organizational accomplishment of board stated Ends and compliance with Management Limitations will be deemed successful CEO performance."

Policy Governance significantly mitigates the "politics of personality" that guide many decisions to terminate or retain a CEO. Many organizations not using Policy Governance have no clear standards for assessing CEO performance, leaving both the CEO and the board in a state of confusion. Others compile a series of management goals that we know to be entirely means issues. Proactive ends statements describing what good is to be accomplished, for whom, and at what relative worth are often missing altogether. In the absence of well-defined ends and management limitations, boards often retain a CEO from year to year simply because they like the person or the person "works hard." Or they terminate a CEO for equally subjective reasons. Dick Grasso was not terminated because he was doing a poor job at the New York Stock Exchange. His compensation package had become an embarrassment to the board that approved it.

By tying CEO performance to clear articulations of ends to be accomplished and management limitations to be complied with, Policy Governance boards strengthen both their own position and that of the CEO. Both are clear and certain about what they are accountable for and to whom. To deny a CEO this clarity of purpose for fear of creating an additional claim in the event of termination runs counter to common sense. On what other basis *should* a CEO be terminated?

When a board sets down clear policy statements for its CEO, it demonstrates a good faith effort to fulfill its duty of oversight and duty of care. Rigorous oversight does not merely mean monitoring what the CEO does after the fact. Monitoring reaches its full potential only in the context of *previously stated* expectations.

Global Executive Constraint

Attorneys have also questioned whether the global executive constraint against "unlawful, unethical, or imprudent"

actions or circumstances exposes the board to more potential liability than it might otherwise have. They contend that by *not* stating this constraint explicitly, the board could distance itself from illegal or actionable CEO behavior and so absolve itself of liability. In effect, the board would be saying, "We didn't do our job well when we monitored our CEO's performance, but we shouldn't be held accountable or liable for it."

Another aspect of this policy that has garnered much attention is the breadth of the proscription against "imprudent" actions or decisions. Certainly, this is for many the most open to interpretation of the three most common concerns addressed in the global executive constraint. In fact, further definition of "imprudence" is what boards address by narrowing the range of interpretation through nearly all other language in the management limitations policy category. And it should be, as we would hope boards don't find it necessary to put a lot of time and effort into describing unlawful or unethical actions for fear that the CEO they hired would otherwise be inclined to engage in such actions!

The reality, and the irony, is that the "prudent person test" is a basic precept of many legal systems, including English common law and other systems of law around the world. The law recognizes that while certain actions are forbidden, there are others in which the judgment of legality is based on the facts and circumstances: "Did the defendant do what a prudent person would have done in similar circumstances?"

Balancing Risk Management and Leadership

By this point, a clear pattern should be apparent. Boards seeking to lead and be accountable for their organization's performance should recognize these legal considerations but cannot allow themselves to be hamstrung by them. The considerations are valid and should not be ignored. Boards

(continued on page 7)

The ownership does not define the law, and the law does not define the wishes of the ownership

The Contrast Between Accountability and Liability

by John Carver

INCORPORATED AND STATUTE-BASED organizations and their boards are creatures of law and as such owe an allegiance to the law. To be sure, the fidelity of any given organization should be primarily to its ownership—whether a legal ownership, as in the case of an equity corporation's shareholders, or a "moral" ownership, as in the case of a community hospital's community or a public school system's public. But just as my personal property is mine alone, it can only be used within the limits of public policy or law. So it is that a governing board of a school system or of an auto manufacturer must avoid unlawfulness while serving the wishes of its ownership. The ownership does not define the law, and the law does not define the wishes of the ownership.

Legal counsel is an invaluable resource to a governing board, both to help it avoid unlawfulness and to advise it concerning liability. Except in rare cases of intentional civil disobedience, it is generally assumed that law is not to be violated. But it is not similarly to be assumed that liability is to be avoided. In fact, liability is necessarily risked in the conduct of any enterprise. To avoid liability is to cease to operate. Ceasing to operate would, in most cases, be failing in accountability to the ownership.

It is the responsibility of legal counsel to detect sources of liability and to argue for minimal liability. It is the board's job to understand legal counsel's opinion, thereby reaping the benefit of professional knowledge. But it is not the board's job to accept legal counsel's opinion of how much liability is too much liability, how much risk is too much risk, or how much organizational achievement it should sacrifice to avoid various types and levels of risk. The board is accountable to the ownership for achieving its purpose for existence, not for minimizing its liability. This is not to say liability is no concern at all but that it must be prudently assumed. Legal counsel is and should be an advocate for reduced risk, but the board has a larger charge than counsel. The primary concern of a responsible board must be its accountability, not its liability.

Proper leadership requires that the board accept and even accentuate its accountability for organizational performance, circumstances, activities, and status. To cloud that clarity in the name of reducing liability is to cheat the ownership. Does it increase liability to instruct a school system to produce better results for children or a municipal government to create a level of safety for citizens? If so, does that then mean that the governing body should avoid stating boldly and clearly what it expects its subordinates to achieve? In that case, why have the board?

Liability is necessarily risked in the conduct of any enterprise. To avoid liability is to cease to operate.

Whereas assuming liabilities that promise no payoff in performance is clearly imprudent, it is simply irresponsible to shrink from liability in the course of pursuing potential gains. It is wise for the board to learn the nature of its risks, but it is its moral obligation to maximize the performance of its organization. ❑

Fiduciary Duties

(continued from page 2)

mission. Boards may choose to delegate all or part of its responsibility for this or to make fundraising an extension of their governance role.

9. *Investigations.* A director has a duty to investigate warnings or reports of officer or employee theft or mismanagement and in some situations to report misconduct to the appropriate authorities.

Policy Governance and the Duty of Care

Policy Governance *systematizes* the principles and accountabilities that lead to fulfillment of the duty of care. While directors have these responsibilities as individuals and as a group, Policy Governance clarifies that no authority is vested in individual directors unless explicitly authorized by the board, and it ensures that a board clearly explains its manner of delegation to officers, committees, employees, and others.

The Duty of Oversight

An aspect of the duty of care is the duty of oversight. Breach of the duty of oversight can cause liability if the board fails to act in circumstances in which due attention would have prevented corporate misconduct, violation of the law, or a corporate loss. To prevail on a lack-of-oversight claim, a plaintiff must show that the directors knew or should have known that violations of law or improper conduct were occurring, that the directors took no steps to prevent or remedy the misconduct, and that their failure proximately caused the losses.

Breaches of the duty of oversight typically occur in the following situations:

- When directors abdicate their fundamental functions, as when directors fail to supervise and monitor management and fail to be informed of the corporation's business, affairs, and activities
- When directors are informed of employee wrongdoing or of potential violations of law and fail to make an inquiry into and response to the situation
- When directors delegate corporate managerial responsibility to an untrustworthy officer or employee and fail to monitor such officer or employee.

Policy Governance and the Duty of Oversight

The principles of addressing policies at the broadest levels first and proscribing operational means to address unacceptable actions make it possible for boards to have comprehensive organizational oversight, addressing *all* aspects of corporate performance. Policy Governance boards delegate specific authority, such as the chief governance officer's authority to ensure the integrity of the board's performance and the chief executive officer's authority over operations. With the board maintaining authority to "monitor any policy at any time," fulfillment of the duty of oversight is simply a matter of exercising authority as explicitly set forth in board policies.

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The Duty of Loyalty

Traditionally, directors have an absolute duty of complete, undivided loyalty to the organization. This means that directors should avoid using their position or the organization's assets in a way that would result in pecuniary or monetary gain for themselves or for any member of their family. A director should put the good of the organization first and avoid engaging in transactions with the organization from which the director will benefit.

The board should have a written policy on conflicts of interest, precluding conflicting transactions, diversion of corporate opportunity for personal gain, and loans to directors or their families or businesses.

Policy Governance and the Duty of Loyalty

Policy Governance boards, by defining "ownership," make explicit the population they represent and on whose behalf they serve. This enables board members to clarify to whom their loyalty does and does not lawfully lie. Conflict-of-interest policies are set forth, to varying degrees of explicitness, in the code of conduct and governance process sections of a Policy Governance board's policy manual.

The Business Judgment Rule

The business judgment rule provides that the decisions of a corporation's board of directors will not be second-guessed unless a decision is self-interested (a violation of the duty of loyalty) or the board acted in an imprudent manner (a violation of the duty of care). Said another way, courts will not second-guess directors' business decisions if the directors act on an informed basis and in good faith.

The Business Judgment Rule Versus Inaction Under the Duty of Oversight

The law draws a distinction between two scenarios: deciding there is no problem and ignoring a problem. In the first case, when a board considers a situation and makes a decision that results in a loss, the business judgment rule will protect a board's decision if the board acted in good faith and properly informed itself in the process. The protection of the rule is not determined by the results of the decision but by the quality of the process employed. For example, when a board conducts a proper internal investigation into a matter and either takes action or consciously decides that action is not necessary, that decision, even if wrong,

will be protected by the business judgment rule.

By contrast, when a loss originates from the board's failure to consider a problem, there has been no process, there is no decision to protect, and there is no recourse to the business judgment rule. Instead, directors may face liability for breach of the duty of oversight. Thus when directors are made aware, or should have been aware, of material improper conduct, violations of law, or other actions that could result in material harm to the organization, the duty of oversight demands that they investigate the matter and decide whether or not corrective action is needed.

The board may not take action in either case, but the results in the two cases are dramatically different. Therefore, the duty of oversight creates an incentive for boards to respond to potential indications of wrongdoing in order to gain the benefit of the business judgment rule.

Policy Governance and the Business Judgment Rule

Boards adhering to Policy Governance principles, such as those addressing loyalty to ownership and conflicts of interest, are unlikely to be judged as not acting in good faith. Further, the Policy Governance approach to board decision making (starting with the broadest level of all decision categories, adding specificity until willing to accept *any reasonable interpretation*, and employing a rigorous monitoring system) are unlikely to be judged as imprudent or grossly negligent. Therefore, the fulfillment of the duties of care and loyalty provides for protection under the business judgment rule.

The Duty of Obedience

Directors have a duty to follow the organization's governing documents (articles of incorporation, bylaws, and board-established governing policies), to ensure that the organization's purpose is carried out, and to ensure that funds are used for lawful purposes. Directors must also comply with state and federal laws that relate to the organization and the way in which it conducts its business. Examples would include the Internal Revenue Code, tax and financial filing requirements, withholding obligations, and applicable state and federal registration requirements.

Policy Governance and the Duty of Obedience

Governance commitment and governing style policies typically set forth a board's commitment to informed decision making. Explicit delegation of responsibility for governmental reporting and filing requirements is set forth, typically under the heading of financial condition and activities. A board fulfilling its commitment to orientation for new board members and continual board education will typically be seen as having systematically fulfilled its duty of obedience.

Acting in Good Faith

Standards of good faith may also often be found in governmental codifications. This example, from the Arizona Revised Statutes, Section 10-3830, Subsection B, is typical:

> **General Standards for Directors**
>
> In discharging duties, a director is entitled to rely on information, opinions, reports or statements, including financial statements and other financial data, if prepared or presented by any of the following:
>
> 1. One or more officers or employees of the corporation whom the director reasonably believes are reliable and competent in the matters presented.
> 2. Legal counsel, public accountants or other person as to matters the director reasonably believes are within the person's professional or expert competence.
> 3. A committee of or appointed by the board of directors of which the director is not a member if the director reasonably believes the committee merits confidence.
>
> A director is not acting in good faith if the director has knowledge concerning the matter in question that makes reliance otherwise permitted by subsection B unwarranted.

(continued on back page)

Legal Concerns

(continued from page 5)

should govern with full awareness of the potential consequences of their policies. But they should not sacrifice the opportunities and benefits of effective governance just for the sake of reducing potential exposure to liability. Leading, by its very nature, involves risk. Leading well reduces but will never eliminate risk. And leading by means of risk avoidance is not to lead at all. ❑

Jim Hyatt is an attorney, a Policy Governance Academy graduate, and a consulting associate with Charney Associates. Bill Charney, also an Academy graduate, is a consultant and speaker on board governance and leadership. He cowrote, with Miriam Carver, The Board Member's Playbook *(Jossey-Bass, 2004). They may be contacted at jim@bcharney.com or bill@bcharney.com, respectively; through their Web site at www.bcharney.com; or by telephone at (303) 321-3190.*

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All offerings are conducted by John and Miriam Carver.

Fiduciary Duties

(continued from page 7)

A director who is found not to have acted in good faith may not be entitled to indemnification under the organization's bylaws and may also be denied coverage under its directors and officers liability policy. Both documents should be checked in this regard.

However, many statutes, particularly for nonprofit corporations, protect directors by *presuming* that they fulfilled their duty of care, including acting in good faith. This places the burden on the plaintiff to overcome this presumption with clear and convincing evidence.

Conclusion

This brief outline of the fiduciary duties of directors is, by necessity, a very general introduction to a very complex subject. Boards should always consult with their counsel for a fuller examination of these duties and their application in their particular jurisdictions. ❑

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Personal Note

(continued from page 3)

changes in the law, developed in a contemplative fashion, offer some escape from such disjointed progress. Absent the emergency atmosphere of crises, laws affecting governance might conceivably be grounded in conceptually coherent fundamentals rather than representing today's quick solution to concrete but ephemeral predicaments. The United States' Sarbanes-Oxley Act comes to mind, but other examples abound. Why are boards—those to whom governance is most dear—not leading the charge?

Consider, once again, public school boards. Taken together, the boards in a state or province have enormous political power with which to influence legislatures. That the law prescribes ridiculous practices, then, can be laid at the feet of school boards as well as legislators and regulators. Put simply, there is no excuse for the law to impede or even fail to encourage the best possible governance. That it does so is an indictment not only of lawmakers and regulators but also of associations of boards that do not see to it that corrections are made.

Policy Governance was not designed as a method to govern as responsibly as the law allows. It was designed to govern as responsibly as human possibility allows. Where there is conflict between the law and the demands of good governance, the law should change, not the governance. Before the law changes, however, boards are obliged to observe it. But if boards' governance commitment stops passively at the boardroom door, they fail in their duty to maximize owner accountability.

This Issue

We focus in this issue on the first of the challenges noted above, for boards must feel confident about the first before they can be powerful with the second. How are boards to deal with conflicts that either exist or are feared to exist between practicing Policy Governance and complying with laws and regulations? To address this question, Miriam Carver and I, along with our editor Ocean Howell, have accepted the help of Jim Hyatt and Bill Charney of Charney Associates in assembling and producing what we hope are helpful articles. We are very grateful for the able assistance provided by these two colleagues. This issue leads with Hyatt and Charney's extended piece outlining the legal and fiduciary responsibilities of board members. In a brief article, Hyatt and Charney consider what types of Policy Governance policies have tended to generate legal concerns. In another piece, I argue that a board must endeavor to avoid liability but must always remember that its first priority is to represent its ownership. ❑

BOARD LEADERSHIP

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