

Board Committee Structure, Responsibilities, and Composition

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Panelists

- **Anne Ross – Moderator**
Foley & Lardner LLP
- **Dan Rashke**
TASC, Inc.
- **Ann Wenzel**
American Family Mutual Insurance Company

Overview

- Model Business Corporation Act
- Purposes of Establishing Committees
- Delegation of Board Authority
- Types of Committees
- Performance of Delegated Responsibilities

Model Business Corporation Act

Model Business Corporation Act

- Section 8.25 of the Model Business Corporation Act (the “Model Act”) allows a board of directors to create one or more committees and appoint one or more members of the board of directors to serve on such committees, unless such right is otherwise restricted by the Model Act or the corporation’s articles of incorporation or bylaws.

Model Business Corporation Act

- Any committee of the board of directors so created, may exercise the powers of the board of directors to the extent specified by the board of directors or in the corporation's articles of incorporation or bylaws, except that a committee may not:
 - authorize or approve distributions, except according to a formula or method, or within limits, prescribed by the board of directors;
 - approve or propose to shareholders action that the Model Act requires be approved by shareholders;
 - fill vacancies on the board of directors or, subject to subsection 8.25(g) of the Model Act, on any of its committees; or
 - adopt, amend, or repeal the corporation's bylaws.

Model Business Corporation Act

- Section 8.30 of the Model Act provides that members of board committees, like directors generally, shall discharge their duties with the care that a person in a like position would reasonably believe appropriate under similar circumstances.
- In addition, Section 8.30 of the Model Act provides that such members of committees have a duty to disclose, or cause to be disclosed, to the other committee members information not already known by them but known by the director to be material to the discharge of their decision-making or oversight functions, except where the director reasonably believes that such disclosure would violate a duty imposed under law, a legally enforceable obligation of confidentiality, or a professional ethics rule.

Purposes of Establishing Committees

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- To enhance the effectiveness of the board by:
 - Dividing up the workload:
 - Committees enable the board to be involved in a broad range of tasks without requiring every director to be involved in each aspect of the work.
 - Expediting board meetings:
 - Committees gather information, consult with staff and outside experts, and bring fully developed proposals to the board in the form of written reports and recommended board action.

Purposes of Establishing Committees

Cont'd.

- To enhance effectiveness of the board by:
 - Taking advantage of special talents/knowledge:
 - Many directors are well-suited to be chairs of or serve on specific committees due to their specialized talents and knowledge.
 - Appointment of directors to board committees enables corporations to take fuller advantage of the attributes directors bring to the table.

Delegation of Board Authority

Delegation of Board Authority

- Committee authority is advisory unless board powers are delegated by the board.

Committees with Board Powers

- Useful when:
 - Board does not have sufficient information to take final action that must be resolved before the next board meeting.
 - Large number of directors have a conflict of interest or cannot be included in the decision for the corporation.
 - Action must be taken more quickly than board can be convened.
- May exercise the board's power when it is not in session.
 - As discussed previously, the Model Act contains certain limited restrictions on the committee's exercise of board powers.
- Board is not relieved of its fiduciary responsibility for the operations of the corporation.

Should you delegate board powers?

- Factors to Consider:
 - General level of board activity, level of inconvenience involved in convening special meetings of the entire board, and level of comfort directors have with consolidating board power into the hands of a small number of directors.
 - Case law indicating that formation of a “special committee” will support fulfillment of board’s fiduciary duty.

Types of Committees

Types of Committees

- Two Basic Types:
 - Standing (i.e. permanent).
 - Ad hoc (i.e. for special purposes).

Executive Committee

- **Typical Composition:**
 - Chair, Chief Executive Officer and/or President, one or more Vice Presidents, Secretary, and Treasurer, lead outside director(s), and other officers who serve as directors.
 - Usually chaired by the Chair or, if none, the Chief Executive Officer or President.
- **Activities:**
 - Meets more frequently than the board.
 - Carries on the work of the board between meetings.

Executive Committee Cont'd.

- Risks of Relying on the Executive Committee:
 - One or a few individuals could essentially control the corporation, withhold information and usurp authority from the other board members.
- Avoid risk by placing specific restrictions on the executive committee's powers and include these restrictions in the company's bylaws.

Other Standing Committees

- Typical Composition:
 - Should reflect the corporation's essential activities
- Other Common Standing Committees:
 - Audit Committee
 - Compensation Committee
 - Nominating and Governance Committee

Audit Committee

- **Composition:**
 - Members should have certain financial expertise, at a minimum being “financially literate” (i.e. able to understand the financial reports of the corporation).
 - Sarbanes-Oxley Act: emphasizes that members should not be employed by the institution or have a conflict of interest.
 - Members of management should NOT serve on the audit committee.
 - CEO and CFO are key advisors to the audit committee.

Audit Committee Cont'd.

- Activities:
 - Reviews periodic financial statements and financial reports of operations, assets and liabilities.
 - Examines the corporation's internal control over financial reporting (usually with help of external, independent auditors).
 - Reviews work of the auditors, especially reports to management about internal controls, alternate reporting options, disagreements with management, and difficulties encountered in performing the audit.
 - Reviews the annual budget.

Audit Committee Cont'd.

- Impact of Sarbanes-Oxley Act (15 U.S.C §§ 7201-7266):
 - Created and expanded duties of audit committees for publicly held corporations.
 - Meet with auditors and obtain a specific report of problems and deficiencies.
 - Report weaknesses and problems contained in audit report to the board.
 - Limits services outside auditors may perform and requires auditor to be changed every 5 years for public corporations.

Compensation Committee

- Activities:
 - Implementing and monitoring the Company's overall compensation structure, including, among other things, base salaries, fringe benefits and employee plans, particularly the compensation of the corporation's executive officers.
 - Ensuring that compensation decisions are tied to the realization of predetermined performance goals and objectives.

Nominating and Governance Committee

- Activities:
 - Identify individuals qualified to become members of the board of directors and its committees.
 - Establish and implement core governance policies and principles.
 - Oversee the evaluation of the board of directors.

Performance of Delegated Responsibilities

Performance of Delegated Responsibilities—Generally

- Meet regularly.
- Proceed with work in an organized manner.

Performance of Delegated Responsibilities—Key Elements

- Committee Charter:
 - Draft and submit for board approval.
 - Format may be similar to a mission statement or a general statement of purpose.
 - Include strategic goals and operational goals or objectives.
 - Blueprint for committee's work and for corporation overall.
 - Board should revise as appropriate.

Performance of Delegated Responsibilities—Key Elements Cont'd.

- Staff Support:
 - May be essential to committee's work.
 - Duties may include drafting and sending meeting notices, attending meetings, keeping minutes, gathering information, making recommendations, engaging and supervising outside service providers, drafting committee reports and recommendations to the board.

Performance of Delegated Responsibilities—Key Elements Cont'd.

- Chair:
 - Overall responsibility for committee's work.
 - Should not single-handedly dictate and carry out the committee's agenda and recommendations.
 - Report to the board regularly, preferably in writing, regarding committee's accomplishments and progress.

Performance of Delegated Responsibilities—Key Elements Cont'd.

- Committee Members:
 - Where to find them?
 - Recruited from the board (and for nonprofit organizations, membership, and sometimes the general public).
 - Who are they?
 - Persons with expertise relating to the committee's purpose.
 - Size of committee?
 - Depends on the nature of the committee's tasks.
 - Find balance to ensure all perspectives and areas of expertise are represented, as well as each member feeling like he or she plays a vital role.

Performance of Delegated Responsibilities—Sarbanes-Oxley Act

- Only publicly held companies are required to comply.
- Practices are now viewed as best-practices for publicly held and privately held corporations, as well as non-profit organizations.

Performance of Delegated Responsibilities— Sarbanes-Oxley Act Cont'd.

- Best-practices:
 - Each board committee should have either a specific charter or a specific list of duties and responsibilities with a timetable to complete each duty/responsibility.
 - Specific guidelines for the audit committee discussed previously.
 - Create a written policy on document destruction.
 - Act criminalizes destruction of corporate records, especially those necessary for a legal investigation or proceeding.

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