GOVENDA

Best Practices for Implementing Board Oversight Frameworks

Keep your board up to date on risk oversight expectations

The phrases board oversight, governance, and board framework have been increasingly thrown around within the corporate sphere in the past few years. But what do these terms mean? And how can corporations ensure they are making meaningful decisions to improve their governance and oversight?

While there are no one-size-fits-all solutions to implementing a governance and oversight framework, there are best practices organizations can consider for their boards.

To lay the groundwork for these practices, it's essential to recognize that boards of directors are increasingly responsible not only for overseeing checks and balances within an organization, but also designing what those checks and balances are, and figuring out how to measure them for effectiveness. If they are to advise executive leaders on implementing policies and procedures throughout an organization, boards must define proper board governance and metrics for themselves and management personnel.

Ultimately, directors remain responsible for the results of those implemented processes, even if they are not actively enforcing them.

What is a Governance Framework?

The governance framework is the highest level of defining board governance. The framework should broadly outline the board and senior management roles and define the expectations of governance. These expectations may include risk management, performance, reporting procedures, and organizational culture.

Within that framework, governance infrastructure helps narrow down the framework and defines the day-to-day organizational roles and responsibilities of individuals and groups. The framework is put into practice with specific procedures and job responsibilities within the infrastructure, also called an operating model. The board of directors may actively participate in the infrastructure processes or solely oversee them.

The operating model should:

- Define the operational, financial, risk management, and reporting processes.
- Define each role's responsibilities and reporting processes.
- Help maintain board governance by outlining how the board and management can identify and adjust processes based on new regulations or market changes.

With that understanding, we can dive a little deeper into board oversight and board governance.

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What is Board Oversight?

Board oversight is how a board monitors policies, procedures, and plans to ensure they are compliant and effective in helping a corporation achieve its strategic and financial goals. Compliance can refer to policies, laws, regulations, and ethics.

When discussing board oversight, it's usually in relation to risk oversight. The board's ability to effectively execute oversight can either help a company thrive, or lead to a company's rapid decline. Risk oversight is a topic not to be taken lightly.

A board's duty for risk oversight entered the spotlight in 1996, when the Delaware Chancery Court ruled that a director may be liable for losses caused by a lack of adequate corporate information and reporting systems.

The court found that directors are, in fact, responsible for overseeing the processes in place to report timely, accurate information to the board.

The directors of Caremark International, Inc. reportedly breached their fiduciary duties by not having sufficient control systems in place, which led to the committing of criminal offenses by company employees. The Delaware ruling said that boards of directors had a duty of care to attempt, in good faith, to assure that the corporate information and reporting system exists and is adequate.

"...A director's obligation includes a duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists, and that failure to do so under some circumstances may, in theory at least, render a director liable for losses caused by non-compliance with applicable legal standards."

– JUSTIA US LAW

Since that case, additional court rulings have strengthened the need for board oversight of compliance.

Today, a board's fiduciary duties are:

- To ensure there is an effective corporate compliance program in place for management.
- Oversight of the program and monitoring compliance.
- To remain informed on the program's content and operation.

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What Does Board Oversight Look Like Today?

In the past, boards were told to remain out of the day-to-day risk management operations. Their risk oversight role was to put processes in place and depend on management to inform the board of risks.

Today, monitoring is more of a hands-on board responsibility. Board members must take a more active role in risk assessment. Boards should be more directly involved in leadership and strategy risks, since management cannot be expected to objectively assess their own performance and strategies.

Now, Board Risk Oversight means boards:

- Identify and assess corporate risk.
- Continuously review planning and outcomes of processes.
- Mitigate risks to the extent possible.
- Reevaluate policies.

Directors must be able to understand the risks that pose a threat. Unfortunately, risks cannot be entirely negated, but they should be balanced based on possible rewards. It's in the board's hands to maximize rewards and minimize negative consequences. This includes planning for possible risks that could impact future decisions when mapping out the vision and mission of a corporation.

Directors should also understand the company's appetite and capacity to take risks. Some boards are choosing to establish board-level risk committees to address risk, or even appoint a chief risk officer, but these steps are not necessary for all organizations.
Boards can also assess risks as an entity. If risk committees are established or a chief risk officer is appointed, the committee or officer responsibilities should be clearly defined.