Trustee Insights

BOARD STRUCTURE

Subsidiary Boards: "e pluribus unum?"

How subsidiary boards can contribute to one, effective system

BY JAMIE ORLIKOFF

According to the 2024 AHA Hospital Statistics, at least 67% of all U.S. community hospitals are part of a system. Having multiple governing boards is a unique governance characteristic of most of these systems. As in any system or hospital with more than one governing board, there legally must be a governance hierarchy. If there are two boards in a system for example, one board is superior, and the other board is subsidiary or subordinate. The subsidiary board reports to and is overseen by the superior board which is often referred to as the system or parent board. One of the unique roles of a system or parent board in a system with multiple boards is to oversee and coordinate the subsidiary boards in the system. But what are the roles, functions, purposes and challenges of the subsidiary boards, the boards that report to another board?

Why have subsidiary boards?

Some health care systems are governed by a single board which performs all the required governance functions of the entire system. So, if this model can work, what is the rationale for having multiple boards, where all but the system or parent board are subsidiary boards? There are both practical and political answers to this question.

One practical answer is that having multiple boards allows the system to distribute disparate governance functions, thus reducing the heavy and markedly different workloads that would otherwise be placed upon a single board. In theory, this allows all of the boards to focus on governance work which is categorically consistent and focused on a common level of governance function. For example, a system with several hospitals that is governed by a single board faces a significant governance challenge. On the one hand it must perform high-level governance functions relating to the system as a whole and the environment in which the system functions. Such high-level system functions include system strategic planning, system CEO oversight, system financial oversight, enterprise risk management and generative governance regarding the future, to name only a few.

But on the other hand, this single system board is also the legal governing board of all the hospitals and other organizations in the system. As such, it has very granular governance functions it must perform and accountabilities it must fulfill per legal and regulatory mandates. Such detail-oriented, organizational-specific governance functions include oversight of medical staff credentialing in all of the hospitals (where the board actually is required to make the decision regarding the medical staff membership and privilege delineation for every individual physician at each separate hospital medical staff), oversight of regulatory compliance and accreditation, oversight of quality and patient safety and oversight of community health needs assessments.

Combining big picture system governance functions with much more detail-oriented organizational governance functions in a single board presents several challenges. It creates a constant struggle for the board to organize and balance very different governance responsibilities as it attempts to perform both high-level and detail-oriented tasks well. A very real risk is that the board will overemphasize one of these categories of governance function at the expense of the other, causing overall governance effectiveness to suffer.

Another challenge in attempting to effectively perform and reconcile the constant tension between these disparate governance functions is that the board will likely require significant or inordinate amounts of time from its members to do so. This can generate board member burnout and make recruitment of new board members more difficult. This tension often manifests in the issue of board meeting frequency. Strategic and generative governance (big picture system-oriented governance) often requires deep discussion and engagement which requires longer meetings, and system boards that focus exclusively on such high-level governance functions often prefer to meet less frequently, such as once a quarter, but for longer lengths of time (full day or two-day meetings). Conversely, boards that are responsible for the oversight of medical staff credentialing (detail oriented organizational-specific governance) find that they must meet more frequently, such as monthly, but for shorter meeting times (such as two-hour meetings) in order to make these time-sensitive, granular decisions necessary to keep the specific hospital functioning. So, what is the best meeting frequency and length for a board that combines these two very different functions? A monthly meeting that is relatively brief can facilitate the effective performance of the granular governance functions but gives short shrift to the bigger-picture, system-level governance functions, and vice versa.

Yet another challenge is presented in the composition of the single system board that combines all governance functions, as the skill sets required of board members to perform high-level system governance functions are different than the skill sets needed to effectively oversee medical staff credentialing, quality, safety, regulatory compliance and other detail-oriented governance functions. How does such a board balance the skills and experience of its members to assure that it has the necessary expertise to effectively oversee both categories of very different governance responsibilities? How does it ensure that all board members have a similar perspective and knowledge base about the very different levels of governance responsibility combined in the single system board? How does it create an effective governance culture by reconciling the varying board member interests regarding these wildly disparate governance functions?

Very often these practical challenges result in the conclusion that effectively governing a system, especially a large system with many organizations that are distributed across large geographic areas, might be best accomplished with multiple boards. The very different governance work can be divided among different boards and these boards can focus on a specific level of governance work making it easier for them to perform their governance tasks more effectively and efficiently. Further, by pushing the detail-oriented governance to the subsidiary boards, the system board is free to focus exclusively on high-level, system governance issues.

Many systems also choose to have multiple boards for political reasons: to create many board positions within the system to involve more community members and constituents in its governance, and more specifically, to avoid excluding stakeholders from governance. This approach tends to be a vestige of systems created through mergers, where composing the system board of the new company from the members of the two founding system boards. This means that to keep the new company system or parent board to a reasonable size not all members of the two founding organizations' parent boards will "survive" as members. Maintaining or creating multiple subsidiary boards serves the political purpose of ensuring that everyone who was involved in the governance of the two founding systems can remain involved in governance of the newly formed system. This political approach is further favored if either or both of the founding systems had multiple board models pre-merger.

Are subsidiary boards "real" boards?

A governance hierarchy can be a challenging concept to many subsidiary board members, as this type of multi-board governance model is unique to health care. It is very rare to have multiple boards in other types of large, for-profit corporations — other than small boards composed exclusively of executive management. A person with extensive experience serving on boards of non-health care corporations may not be familiar with this concept and thus have difficulty reconciling it. For such members of subsidiary boards in health care systems, this is often expressed as frustration with being on a "junior" or "baby" board or with not being where the "real power" or "action" is, i.e., on the system or parent board.

Subsidiary board members who feel this way often believe that to be a "real" board it must have specific authorities, such as CEO oversight, budget and finance, audit and strategic planning. To assuage these concerns, the governance culture of many systems will explicitly or implicitly minimize the necessary concept of the governance hierarchy in their use of language to describe the boards in their system. These systems tend not to use the terms subsidiary or subordinate to describe boards that report to the system board. Rather, they call them partner or affiliate boards. Likewise, they will not refer to the system board as the parent board to further the implication that there is no governance hierarchy and all the boards in the system are equal. But this approach both obscures the concept of a governance hierarchy and makes a complex governance model more confusing and therefore less functional. It is also inconsistent with the legal principles that require a governance hierarchy if there are multiple boards.

A key to making a multiple board model work is to understand that even though the ultimate governance authority rests with the system board, governance authority and responsibilities can be subdivided between all the boards in a system. It is also important for every member of every board in a system to understand that every governing (but not advisory) board in a system has fiduciary duties relative to their defined authority and responsibilities. In systems with multiple boards, fiduciary duty does not reside exclusively with the system or parent board. Subsidiary boards have fiduciary duties and authority, even though they do not have the ultimate governance authority or fiduciary duty for the system as a whole.

An example is the subsidiary board that has authority over the medical staff credentialing process and decisions for one or more hospitals in a system. This is a crucial governance responsibility which has a major impact on the quality and safety in the hospital, and also has significant liability exposure to the board if it does not perform this function effectively, consistently and fairly. A subsidiary board with the ultimate authority to make decisions regarding medical staff credentialing has the ultimate fiduciary duty for this function, even though it does not have the ultimate fiduciary duty for the system or for quality or safety across the system. Such a subsidiary board has fiduciary duty, authority and exposure to liability. So, yes, subsidiary boards are most definitely "real" boards.

A subsidiary board in a system that governs a hospital or hospitals, or other organizations or regions within the system, has crucial fiduciary duties in its defined areas of responsibility and authority. This board still has critical governance duties, responsibilities and liabilities even though it may have no responsibility to hire and fire a CEO or for audit, strategy or budget. While unique to health care and outside the experience of many board members, this governance hierarchy is a crucial concept of effective governance of systems with multiple boards. The understanding and execution of this concept is critical to the success of the multiple board model of system governance.

Avoiding "Governance Creep" on Subsidiary Boards

In systems that attempt to avoid clarity in their governance hierarchy by referring to subsidiary boards as partner or affiliate boards, or who allow members of the subsidiary boards to regard these boards as "junior" or "baby" boards, there is a tendency to allow the subsidiary boards to engage in activities which are inconsistent with their defined duties and responsibilities. This "governance creep" is marked by subsidiary boards demanding and receiving information, setting agendas and having board committees which bear no relationship to their defined function and authority. For example, a subsidiary board with no financial authority should not have a finance committee, nor should it devote routine time in its meetings to discussion of finance. Yet, many subsidiary boards do precisely that in attempts to subvert the concept and purpose of the governance hierarchy and to persuade the board members that they are indeed a "real" board. Subsidiary boards that do this implicitly reject not only the governance hierarchy, but also reject the critical importance of their defined roles and responsibilities, which means that these more granular — but crucially important — governance functions are not performed well as the board spends its time on issues for which it has no authority or responsibility. This defeats the purpose of having multiple boards.

Such governance creep subverts effective system governance by:

- Slowing down the governance metabolism of the system — where it takes too long to make decisions because too many boards are involved in the issue and there is lack of clarity regarding which board in the system has the authority to make a specific decision and which other boards in the system, if any, have any role in making the decision.
- Causing conflict between boards in the system where relative roles, responsibilities and authority are not clearly and commonly understood. An example of this is a foundation board that has the role of raising philanthropic funds for the system. The foundation board is subsidiary to the system board, but due to governance creep, the foundation board believes that its role includes participating in strategic decisions about how the philanthropic funds will be spent by the system board. The system board, not wishing to create conflict or impede fundraising, initially allows the foundation board to receive information and participate in decisions that are well outside its role. This further convinces the members of the foundation board that their role transcends fundraising for the system and includes system governance functions such as strategic planning, budget approval and use of capital. This can create conflict when the system board attempts to assert the governance boundaries of the foundation board. This is a common area of governance creep between boards in a system, and there have been instances where it resulted in lawsuits filed by foundation boards against system boards, which is certainly not an effective functional expression of a governance hierarchy.
- Obliging executive management to spend inordinate amounts of time "greasing the wheels" of the subsidiary boards to reduce tension or mediate conflict between boards and to make overall system governance marginally functional.

Clearly, avoiding governance creep is a necessary component of an effective governance hierarchy for making multiple boards in a system work. To avoid governance creep, the roles, responsibilities, authority and liability of every board in the system must be clearly defined and frequently communicated to all members of all the boards in the system. Typically, this is best accomplished through the use of a governance authority matrix which specifically defines how decision making is divided among different boards in a system (as well as between the system board and the CEO and even between boards and their committees).

This clear division of governance roles and authority specifies:

- Which board in a system has the ultimate accountability for making a specific decision.
- What other board or committee might have the ability to recommend a decision or course of action to a superior board.
- What subsidiary board, if any, must be consulted before a specific decision is made by a superior board — making clear whether the subsidiary board's approval is required for the superior board to make a particular decision, or if it is simply that the subsidiary board's input must be sought but does not have to be followed by the superior board in making the decision.
- What board must be informed of a decision after it has been made but before it is publicly announced.

For maximum clarity, effective system boards will specifically define key terms used in their governance authority matrix such as: approve, recommend, consult and inform. Then, they will list each different governance decision, issue or function and assign a specific authority or role to each board, board committee and relevant executive in the system.

Once the distinct roles and responsibilities of the different boards in a system are defined, the issue of the composition of each of these boards should be addressed.

Who should be a member of a subsidiary board?

Linking the composition of every board in a system to the specific role, function and authority of that individual board is key to avoid governance creep and to drive effective governance among all the boards in the system. In many systems, subsidiary boards are explicitly or implicitly regarded as feeder boards, or "farm teams," where the members of these boards expect to ascend to membership on the system/parent board. In some systems, membership on a subsidiary board is an actual prerequisite for consideration of membership on the system/parent board. The challenge with this approach is that it results in recruitment of board members at the subsidiary board level who have skills sets that are appropriate for the system/parent board, but not for the defined roles, functions and authorities of the subsidiary boards. This then exacerbates the tension of these members resisting or resenting being on board that is not the "real" board and further contributes to governance creep.

As the system/parent and subsidiary boards have different roles and responsibilities, they should have different board composition criteria. A subsidiary board that is responsible for the oversight of hospital functions like medical staff credentialing, safety and quality, regulatory compliance, and community health assessment should seek board members who have both interest and expertise in these issues. Yet, many subsidiary boards have members who not only lack such characteristics, but they have skill sets that are associated with a standalone board or a system/parent board. If a potential or current member of a subsidiary board does not regard the role and function of that board as important or believes that board to be a "junior" or "baby" board, or regards time spent on that board as a steppingstone to membership on the system, they should not be a member of the subsidiary board.

For any board to function effectively the members of the board must be selected based on skills and interests that are consistent with the roles, responsibilities and authority of the board on which they will serve. When there is a mismatch between the skills and interests of the board members and the role and function of the board, governance inefficiency is a predictable consequence. This does not mean that a member of a subsidiary board may not become a member of the system/parent board in the future, but it should not be an implicit guarantee or even an expectation. It should be the exception, not the rule.

Making the Governance Hierarchy Work

One of the unique governance characteristics of the vast majority of not-for-profit health systems is having multiple boards with a governance hierarchy. If each board understands its role, focuses its work on its role, and selects members based on expertise and interest in that role, the many boards in a system will contribute to the system functioning as an effective, single organization.

Jamie Orlikoff (j.orlikoff@att.net) is president of Orlikoff & Associates, a consulting firm specializing in health care governance and leadership. He is the national adviser on governance and leadership to the American Hospital Association. He is a member and past chair of the board of the St. Charles Health System in Bend, Ore.

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