

Corporate Governance in Time of Crisis

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Being Prepared



Crisis Principles

- **Proactive Crisis Planning:** Boards should develop and regularly update crisis management plans that address potential scenarios.
- **Adaptability and Flexibility:** Companies need to be agile in adapting their structures, processes, and roles to effectively respond to rapidly changing circumstances.
- **Maintaining Purpose and Values:** Even in times of crisis, the company's business purpose and values should remain at the center of decision-making.
- **Prioritizing Safety and Well-being:** Ensuring the health and safety of staff, clients, and board members must be a priority.
- **Effective Communication:** Clear, consistent, and transparent communication is critical in crisis management.
- **Board Engagement:** The board chair should be a key partner with the CEO, providing support and leadership.
- **Fiduciary Responsibilities:** Boards must continue to uphold their fiduciary duties.
- **Post-Crisis Evaluation:** After the crisis, the board should evaluate the company's response and its own performance.

Initial Triage

- Is this a crisis?
- Who is the client?
- Who are the stakeholders?
- Who do you discuss this with? How do you discuss it?
- Do you get outside counsel involved?
- Who on the Board needs to know? When and what do they need to know?
- Do they need counsel?
- How do you approach communications?

Scenario Example



Internal Players

- DMV Gaming – a corporation whose business purpose is to develop, publish, and release video games and video game consoles, promoting a great gaming experience for all.
 - Amy is the CEO
 - Bob is the CFO
 - Steffon is the Chief People Officer
 - Monique is the Chair of the Board
 - Elaine is the Board-elected President
 - Greg is the GC



The Problem



- Last night, a video began circulating online showing Amy romantically embracing a man who was not her husband at the Maroon 5 concert.
- It turns out the man Amy was embracing is DMV's Chief People Officer, Steffon, who is also married.
- The video went viral due to Amy's and Steffon's awkward reactions when they were shown on the concert Jumbotron.
- DMV Gaming is fearful that this incident will make the company a laughingstock and cause its stock price to drop.

Stage One - Internal

- Amy and Steffon fear their jobs may be at risk.
- Amy and Steffon are dodging calls from Board members and colleagues.
- Close review of the viral video shows that Elaine also attended the concert with Amy and Steffon.
- Investors are reaching out to the Board to understand how this negative press will impact the company.



Stage Two - External

- A Cable News Now reporter calls Bob and Monique asking for their comments on the company's culture and non fraternization policy/disclosure requirements.
- Unnamed DMV Gaming employees start leaking relationship information about Amy and Steffon, as well as other potentially problematic relationships between leadership and other employees at the company.
- Because DMV Gaming is vulnerable, it received an unsolicited cash offer from a competitor.



Stage Three - Legal



- Both Amy and Steffon's spouses retain divorce attorneys.
- Amy's spouse told Amy that he hired a "pitbull" divorce attorney who will make broad discovery requests, subpoena Amy's colleagues to testify, and "bring down the whole company."

Conclusion

- Be prepared
- Determine if there is a crisis
 - Who are the stakeholders?
 - Who is your client?
- Execute your plan
 - Have a law firm in place
 - Have a communications firm in place
- Be flexible as facts change

Appendix: Legal Considerations

Legal Considerations – Board Authority

- The Board authority:
 - The Board must have a quorum to act.
 - The Board may delegate authority to committees or individuals.
 - **Individual Board members lack authority to act on their own unless authorized by the Board.**
- Board members may expose themselves or the company to liability if they act outside of their scope of authority.
- **Where a board of directors fails to act on repeated incidences of directors exceeding the scope of their authority, the board may be deemed to have passively condoned such behavior and may be held liable.**

Officer Authority

- Officers have four main sources of authority (in order of precedence):
 - State law;
 - But – may also include restrictions, such as the ability to hold multiple officer roles at the same time.
- Articles of Incorporation;
 - The most common approach is for Articles be silent on officer authority, or else to specifically delegate such provisions to the Bylaws.
- Bylaws; and
- Authority granted by Board resolution.

Fiduciary Duties

- **Fiduciary Duties are responsibilities imposed on people trusted to act in good faith and honesty on behalf of a third party.**
- **Duty of Care**
 - Good business judgment at all times
 - Due diligence in decision making
- **Duty of Loyalty**
 - Act in the best interest of the company and membership
 - Avoid conflicts of interest



Duty of Care

- **Board members must act:**

- In good faith.
- With the care that a person in a like position would reasonably believe appropriate under similar circumstances.

- **Practical Application of Duty of Care:**

- Review all relevant information and take reasonable steps to become informed.
- Make informed decisions.
- Make reasonable inquiries where appropriate.
- Rely on experts, with appropriate oversight.



Conflicts of Interest

- Arise when a Board member or employee (or related person) has a financial or other interest in a matter such that it would reasonably be expected to exert an influence on the member's judgment.
- **Board Members and employees must:**
 - Avoid ***acting*** with a conflicts of interest.
 - Disclose conflicts of interest to the Board.
 - Abstain from participating in any discussion or voting regarding any matter in which such member (or related person) has a conflict of interest.



Test: *Is the interest such that it would reasonably influence a person's judgment?*

Duty of Loyalty

- Board members and employees must act in a manner they reasonably believe to be in the best interests of the company.
- **Best Practices:**
 - Do not use your position to gain secret profit or compete with the company.
 - Do not usurp the company's opportunities.
 - Beware of conflicts of interest.



Duty of Confidentiality

- Board members and employees have a duty to maintain confidentiality (i.e., not to use or disclose confidential, non-public information obtained in their capacity as Board member or employee, without authorization).



Acting Beyond Authority

- **Board members must act in the best interest of the overall company and keep their individual interests from affecting the role of the board.**
- **Apparent Authority**
 - Outside parties are entitled to rely on a title in assuming that an officer or director has the right to speak for a company and to legally bind it. This is called “apparent authority.”
 - Given that an individual’s words or actions can bind the company, even if board approval was not obtained before acting, it is crucial to educate all officers and directors about the precise limits of their authority.
 - Even if you do not have authority to enter into a contract, a third party may rely on your apparent authority.

Acting Beyond Authority (Cont.)

■ Risk to Insurance

- In some instances where a board of directors does not take action to prevent a director from acting beyond the scope of its authority, insurance policies may not cover liability.

■ Power Dynamics

- All boards need to be aware of power dynamics. When “directors” interact with third parties, it comes with a certain level of perceived influence/authority, **and as such, we should take extra care not to step on or interfere with company staff plans (i.e., “noninterference”)**.
- Third parties include: people in the industry, vendors, politicians, customers.

■ Where does it become tricky?

- Delineating personal capacity from association with the Board.
- Acting within **explicitly delegated** authority.



Business Judgment Rule

- Board members are generally not liable for mistakes in judgment if they act:
 - in good faith,
 - with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, and
 - in a manner the directors reasonably believe to be in the best interests of the company.



Special Considerations

- Mergers and Acquisitions
- Regulatory Changes
- Publicly Traded Companies
- Nonprofit Organizations

What Can You Do?

- Stay current.
- Be consistent.
- Review corporate documents.
- Have periodic training sessions for your Board and others.

