

**W**hen nonprofit hospitals, health maintenance organizations, insurers or other health organizations are converted to for-profit status, the full value of their charitable assets must continue to be used for the public benefit and for health purposes. Where substantial assets are involved, the most common solution is formation of a charitable foundation dedicated to the same or similar purposes as the nonprofit organization. These new health foundations also are created as the result of nonprofit mergers or acquisitions to preserve benefit for a particular community or purpose historically served by a nonprofit health institution. By the end of 1999, more than 120 new health foundations with assets totaling \$15B had been created as the result of health care organization conversions and consolidations.<sup>1</sup>

Decisions about the governing board are among the most important to be made regarding the new foundation: regarding who will sit on the initial governing board as well as how board members will be qualified and selected in the future. The planning process should be open to public participation and comment as these decisions will have great impact on how responsive the foundation is to community interests, how effective it is, and how accountable to the public.

### **Formation of a new board is critical.**

When the original purposes of the nonprofit health institution are preserved following a conversion, the assets are held in a different kind of organization, generally a foundation vehicle that operates primarily by awarding grants. The new foundation will require particular skills and expertise on its governing board. Planning should consider what knowledge and experience are needed, based on the foundation's mission. Criteria should be developed for individual board members, and for the board in aggregate. The carry-forward of boards of trustees in full from the hospital or health plan is not likely to result in the most appropriate and qualified governing board for the new health foundation.

### **The board should be diverse and reflective of the community served.**

This requirement flows from the fact that nonprofit assets are held in trust for public benefit and were created from a broad pattern of public support, voluntary contributions and the advantages of tax exemption over many years. Because the general public is the beneficiary of nonprofit assets and has participated in building their value,

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<sup>1</sup> Philanthropy's Newest Members: Findings from the 1999 Survey of Foundations Created by Health Care Conversions, Grantmakers in Health, 2000.

conversion foundations have a strongly public character. Beyond what is required of corporate, family or private foundations, they should have governing boards that are reflective of the community served.<sup>2</sup> Governing boards should include people with diverse backgrounds, people from different areas of the community served and people with a variety of philanthropic interests. It is important to seek representation from groups intended to benefit from the foundation's programs, including providers and advocates who have direct experience with target populations, and consumers. The variety of ethnic, cultural and linguistic groups represented in the community served should be reflected on the foundation's governing board. A commitment to achieving diverse and broadly representative participation on the board should be stated in the foundation's bylaws.

**The board should include the skills that will be needed for governance of a new philanthropic institution.**

The foundation planning process should include an inventory of expertise that should ideally be represented on the governing board. Together with goals for diversity and the inclusion of important constituencies, this analysis will help shape the search for board member prospects, the selection process and priorities for recruitment. Among the important categories to consider are understanding of community health needs, public health, health policy or systems expertise, financial and investment management, experience in philanthropy, nonprofit management, legal and board leadership skills. Other criteria may be articulated for all board members, such as a demonstrated commitment to community health or community improvement, and prior community service or leadership experience.

While the quality of the governing board is always important, the initial board will make critical formative decisions, including the hiring of executive staff. Constitution of the first board will greatly influence how well the foundation is able to meet the challenges involved in starting a new philanthropic institution.

**An independent governing board is essential.**

To deliver the maximum benefit to its community, the new health foundation must act impartially, and it must be viewed from the outset as making decisions fairly and without bias. It is essential that the foundation not carry obligations to provide or fund

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<sup>2</sup> This standard is included in model legislation on nonprofit health conversions adopted in 1998 by the National Association of Attorney's General, which suggests criteria for evaluation of resulting foundations, including " "

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services that should be delivered by the successor corporation. It must not favor (or disfavor) providers or other community partners on the basis of their alignment with, or competition with, the converting nonprofit or its successor. It is for these reasons - together with the need to assemble the right mix of skills and background - that the board of the converting nonprofit should not be carried forward to become the board of the new foundation.

Once the planning process has identified criteria and priorities for board recruitment, some members of the board of the converting nonprofit may be considered, together with other candidates, for board seats. However, they should not receive priority consideration, and no seat on the governing board, contract or staff role with the foundation should be committed in advance to an executive or board member of the nonprofit that is the source of the endowment. With regard to successor for-profit corporations, the need for complete separation from the foundation is even greater.

Foundations formed as the result of joint ventures present a particular challenge because the nonprofit and for-profit partners participate together in governance of the resulting health care organization on an ongoing basis.

Boards of conversion foundations should also not be controlled by state, county or municipal governments. They must not be subject to political or partisan influence. If they are to fully serve and add value for their communities, foundations cannot assume funding obligations of the public sector, or displace government grants and programs. Thus, while regulators or other government officials may play a role in selection of the first board, their ongoing participation in governance of the foundation should be avoided.

### **Selection of board members is a critical issue.**

A foundation planning committee may be formed to nominate members of the initial board. Regulators or other public officials often make the first appointments, or the board of the converting nonprofit may guide the process. Ideally, to address the goals of diversity of background and interest as well as community representation and openness, a broad outreach effort should be undertaken to fill board seats on new conversion foundations. Key elements of such a process include the publication of criteria for board membership, a widely publicized call for nominations, the opportunity for many people to respond with suggestions, and clear answers to how final selections are determined. Examples of open board recruitment processes from California and Colorado are attached to this paper.

Regardless of how its initial board members are selected, the foundation bylaws will include a provision for subsequent nominations or appointments to fill vacancies on the governing board. In reviewing the options, advocates should consider the goals of providing both for sufficient autonomy of the foundation and for responsiveness to the community.

A permanent community advisory committee to the foundation may be formed to reflect the public ownership stake in nonprofit assets. Vesting the responsibility for nominating members of the governing board in the community advisory committee can guard against insularity and ensure that the foundation is responsive to community concerns on an ongoing basis.<sup>3</sup> Another way to broaden participation in selecting the foundation board is to grant other institutions or officials the right to appoint or nominate members.

**Board size and terms should ensure that leadership is active and open to new participation.**

The boards of conversion foundations range considerably in size with the median being 12.<sup>4</sup> Boards that are larger generally assign significant authority to a more limited executive committee. The goal of providing opportunities for broad participation and the representation of communities and interest groups may be better served by forming advisory committees to the foundation rather than by creating a board of unwieldy size.

Limited terms of service and the requirement for rotation of new members onto the governing board are essential principals of sound nonprofit management and should be provided for in the bylaws. Advocates should be critical of any proposals for "life trustees." Reserving seats on the foundation governing board for physicians or other specific groups should also be questioned. It is generally preferable to frame requirements in terms of background, skills or expertise that should be represented on the board.

**Bylaws should establish a strong conflict of interest policy for the governing board.**

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<sup>3</sup> Please see also "Community Advisory Committees: An Important Structural Provision for Conversion Foundations" available from Consumers Union/Community Catalyst Community Health Assets Project

<sup>4</sup> Grantmakers in Health

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Foundation bylaws should include clear provisions for conflict of interest appropriate to the needs of a grantmaking institution. The goal is not to prevent individuals who provide leadership for important community constituents or health services from serving on the foundation board. Rather, it is to ensure that foundation decisions are not subject to conflicts of interest and that public confidence in the foundation is not weakened by the potential or appearance of conflicts of interest. Sound policies generally will require board members to declare their affiliations with other nonprofits (including employment, contracts, membership or service on governing boards) and those of close family members. A board member should be required to leave the room prior to a vote on any business involving an organization with which he/she has a relationship. The member should not participate in the board discussion about that organization unless specifically questioned by another member of the board.

### **Compensation policy should be appropriate for a public institution and should support the board's diversity goals.**

The practice of paying fees for service on public foundation boards such as community foundations is not widespread. Proposals to pay fees to members of the governing board of a new health foundation should be scrutinized carefully. However board members certainly should be compensated for the costs of travel and other expenses associated with their service on a foundation board. This may include the option to be reimbursed for loss of income or childcare expenses or to receive a modest stipend. Such a provision may be important to enable people with limited means to serve in this role.