Updates
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Board Oversight Is Critical in Crisis Management

The coronavirus (COVID-19) outbreak and its possible impacts on corporations highlight the importance of the board of directors' oversight function in times of crisis.

Faced with a crisis, a board must consider both the near-term and long-term risks, and in some cases the opportunities, that the crisis presents to the company. The following outlines the board's duties and role in a crisis such as the COVID-19 outbreak, and some practical ways the board may address its duty of oversight and manage risk in that context.

Fulfill Oversight Duties

Under state law, it is the responsibility of the board to oversee the management of the company. Delaware courts have demonstrated their willingness to examine whether a board discharged its oversight role by adequately addressing risks of which the directors were aware. Focus on board risk management is also a top governance priority for institutional investors.

Oversight entails knowledge of and familiarity with the company's business, its strategic plan, and its unique tolerance for risk, together with diligence in gathering the information relevant to address specific situations. Against this background, in an event such as the COVID-19 outbreak, the board must consider the multitude of possible impacts on the company's operations and prospects: safeguarding its employees, reviewing key relationships and contracts, assessing the company's financial position, liquidity, and access to capital, reviewing the near- and longer-term impact on its revenues, and maintaining its relationships with key regulators. The board should consider long-term effects and possible forward-looking strategies, as well as short-term responses to the crisis. Primarily, the board must be certain that management is fully informed of all aspects of the impacts of the crisis and is adequately addressing those impacts.

Actively Communicate With Management

As the board's primary source of information is the senior management team on the front line of the crisis, the board should establish a communication plan with management. Management will need to spend considerable time dealing with the crisis, so agreeing on a regular schedule and appropriate methods of communication will help the board fulfill its duties while also minimizing management distraction. The social distancing required in response to the COVID-19 threat will necessarily require heavy reliance on technology, such as conference calls, emails, and board portals. Whatever the methods selected, the board should have the opportunity for meaningful and thorough engagement with management.

Utilize Board Committees

Although the full board will wish to participate in information-gathering and decision-making, in the interests of speed and efficiency, certain matters may more effectively be addressed in relevant board committees.

Audit committee should review public financial disclosures and address internal controls and accounting issues. The COVID-19 outbreak has created significant economic dislocations that will place stress upon the company's financial disclosure process, at the same time that it has created unprecedented obstacles to internal and external communications. Oversight of the company's disclosure controls, procedures, and communications will fall most heavily on the audit committee, which has specific responsibility for overseeing such issues. The audit committee should be fully apprised of all the financial impacts of the crisis, approve any updates to guidance or other necessary market communications, and sign off on any SEC filings. The audit committee should be in communication with the company's auditors with respect to issues such as changes to internal controls and procedures that may be necessary to adapt to changed means of communications, any changes in critical accounting assumptions, the need for a subsequent event note due to material impacts on operations, and similar considerations.

Compensation committee should address issues with equity-based compensation. A crisis such as the COVID-19 outbreak also raises compensation issues for the board, which should be addressed first in the compensation committee. Drastic reductions in stock price may play havoc with equity-based compensation plans and require reconsideration of performance goals, both in plans and in individual contracts and grants. Compensation plan adjustments will raise separate disclosure issues and will need to be carefully considered. The compensation committee must balance the company's need to retain critical employees against institutional shareholder and shareholder advisory firm reactions, which may be negative. Accordingly, the committee and board may wish to focus on immediate retention issues and defer consideration of any long-term incentive adjustments until the company's financial picture is clearer.

Special committees can support effective and efficient oversight. In some cases, the board may want to establish one or more special committees to deal with certain aspects of the crisis. For example, a finance committee could focus on liquidity concerns, identify sources of available capital, and suggest options, such as deferring or cancelling dividends or stock buyback programs, for conserving cash.

Focus on Capital Plans and Liquidity

In a crisis such as the COVID-19 outbreak, the company's plans for capital expenditures, strategic initiatives, and other uses of capital become critical issues that require the attention of the full board. The board must understand the company's existing sources of liquidity, including any public debt, its major bank lines of credit, and any key covenants that may be affected by the impact of the crisis on the company's financial results. The board should request analyses of the implications of any material capital decisions and carefully manage the communication of any such decisions. That analysis should also take into account opportunities that the crisis may create for the company to acquire assets that might not otherwise have become available.

Rely on Experts

In a crisis, as in less challenging times, the board and its committees are entitled to rely on, and should avail themselves of, the input of experts in the matters they are considering. In the case of COVID 19 issues, in addition to the advice of its accountants, the board may seek input from legal advisors, financial advisors such as investment bankers, insurance advisors, and other experts, in order to assess the impact on their business. Directors need to consider any such expert input carefully, in light of their own knowledge of the company's business and their individual business experience.

Review Readiness to Respond to Activist Attack or Acquisition Overture

In the current market conditions of depressed stock prices, as in other crises, activist investors with liquidity may take positions in companies that they view as vulnerable and agitate now or in the future for board seats or for a sale or reorganization of the company that may not be in the best long-term interests of the company's stakeholders. Similarly, strategic or financial acquirors may see an opportunity to acquire the company at a bargain price.

The most important way that a company can prepare for activist or acquisition overtures is to ensure that there is robust discussion and consensus in the boardroom on the company's long-term strategic plan, as well as on its short-term response to the current crisis. Directors should be in agreement that the CEO, or in some cases, the chairperson, is the designated spokesperson for the company and board, and that any inquiries should be directed to that spokesperson to ensure the company is speaking with one voice. The board should also maintain its communications with the company's large shareholders and share with them (subject to the constraints of Regulation FD) the company's views regarding current uncertainties, the company's short-term response, and its long-term strategy.

The COVID-19 crisis, as well as other challenges that a company may face, will place greater oversight demands on its board of directors. But as long as directors meet their responsibilities by reviewing all reasonably available information, actively participating in board and committee meetings, working co-operatively with management, utilizing experts where necessary, and acting in good faith in the best interests of the company's shareholders and other stakeholders, they will be protected from judicial second-guessing of the difficult decisions with which they are faced.

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