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Detailed rules, transparency should define health system CEOs' outside directorships

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When Evolent Health was just a fledgling technology firm, MedStar Health swooped in to be its first customer. Even today, the not-for-profit health system relies on Evolent's population health management system and health plan management services.

Meanwhile, MedStar's CEO, Kenneth Samet, has served as a director for Evolent since 2015. Last year, the gig paid him total compensation worth $177,500. He also owns more than 12,000 shares in the company.

The CEOs of not-for-profit health systems routinely serve as directors for outside companies, including publicly traded ones, and their latest Securities and Exchange Commission proxy filings show they're well compensated for doing so. It's also not uncommon for those health systems to simultaneously do business with those companies. Opinions on the practice run the gamut, but governance experts say such relationships can be managed by having detailed policies on conflicts of interest that are regularly reviewed.

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“It's not that there are not conflicts of interest,” said David McMillan, managing principal of strategy and integration with the healthcare consulting firm PYA. “It's that we manage the conflicts of interest."

But not everyone thinks that's possible. Northwell Health has a goal of not doing business with companies it has relationships with, said Greg Radinsky, Northwell's chief compliance officer. The SEC filings show Northwell CEO Michael Dowling was compensated $134,410 serving as a director for BankUnited. He also owns 5,000 shares of the company's stock.

Northwell does not do business with BankUnited.

"There's lots of shades of gray to look at, and we tend to take a conservative approach overall," Radinsky said.

Some take that even further. Jeffrey Romoff, CEO of UPMC, has had a long-standing practice of not serving on outside boards to avoid even the appearance of conflicts of interest, a spokesman wrote in an email. Romoff did not comment for this article.

In MedStar's case, a spokeswoman said Samet does not participate in business decisions pertaining to Evolent. The health system has conflicts of interest and ethics policies that determine how all of its associates, including Samet, interact with outside companies.

Drug giant Merck & Co. effectively paid Mayo Clinic $234,167 for CEO Dr. John Noseworthy's work serving on its board. Even though Mayo buys Merck's products and receives research funding from the company, Mayo's chief legal officer shrugged off any notion that the relationship influences purchasing or research decisions.

"The reality at Mayo Clinic is our researchers, pharmacists, physicians and businesspeople are making decisions based on what they think is best for our patients and for Mayo Clinic," said Josh Murphy, "and what relationships our CEO has with other external entities is not factoring into that analysis."

Health system executives' outside roles have taken the spotlight since September, when Memorial Sloan Kettering Cancer Center's chief medical officer resigned following reports that he failed to disclose several millions of dollars in payments he received from drug and healthcare companies in dozens of his research articles. In early October, Sloan Kettering's CEO resigned from the boards of Merck and Charles River Laboratories, from which he received roughly $600,000 in cash and stock compensation last year. The research institute also launched a new conflict-of-interest task force.

Governance experts interviewed for this article agreed there aren't hard and fast rules around health system CEOs serving as directors for outside companies—nor should there be. What's more important is that such relationships are entered into with clear expectations, the organization has written conflicts policies that are revisited regularly and there is transparency throughout.

Pam Knecht, CEO of Chicago-based governance consulting firm Accord Limited, said oftentimes the conflict disclosure forms board members must fill out are too general and don't call out the need to report all types of relationships that could pose potential conflicts.

“One answer to doing the right thing here is to make sure the conflict-of-interest policies and disclosure forms are detailed, and they ask specific questions,” she said. “Do you have an ownership interest in any companies with which the health system does business? What is your percentage ownership interest?”

Several CEOs of health systems who use and hold ownership stakes in the group purchasing organization Premier also sit on its board of directors. That includes the heads of Adventist Health, Adventist Health System, Banner Health, McLaren Health, Rochester Regional Health System and Texas Health Resources. And the GPO pays well for the work. Banner's Peter Fine, for example, was compensated a total of $221,000. Adventist Health's Scott Reiner received total compensation of $191,750 for serving on the board.

Serving on a vendor's board puts health system CEOs in the challenging position of having to balance their responsibility to their own organization, for whom supply costs might be the second- or third-largest expense, with their fiduciary responsibility as a board member for the GPO, said PYA's McMillan.

“That's where the conflict becomes a little bit difficult and boards have to pay particular attention to it, because what's good for Premier may or may not be good for me and the health system,” he said.

But Blair Childs, a Premier spokesman, said Premier is unique from other companies in that its hospital directors represent its owners. Premier is majority owned by about 200 health systems, and the CEOs who serve as directors do so at their health systems' behest, he said.

“We have a very different business model,” Childs added. “This is an alignment of interests, not a conflict of interests. That is really the key.”

CEOs in other industries have long served on outside boards that are part of their economic food chain, McMillan said. Healthcare, by contrast, is entering its first phase of managing those conflicts of interest as opposed to prohibiting them outright. Banning such relationships is no longer an option, considering the vertical integration that's caused sectors that were once siloed to do business with one another.

One example of that evolution would be a health system partnering with a third-party insurance company, McMillan said. Say that health system also owns a pharmacy, and their insurance company partner also buys a pharmacy with operations in the health system's service area. Now there is a potential conflict between the health system's pharmacy and the payer's pharmacy. That can be magnified if the payer-owned pharmacy has significant market share in the service area.

“This vertical integration you're seeing in the industry is creating a brand new dynamic,” McMillan said. “You have roles that were traditionally very segregated that are now overlapping. That has to be managed from a fiduciary standpoint. There's a lot more of these types of situations that are going to come up.”

Health systems can also benefit from the expertise their CEOs gain from serving on boards of outside companies, several experts said. While they of course can't divulge proprietary information shared by pharmaceutical companies, insurers, tech companies or others, they do bring back an understanding of how other industries do business.

“Wouldn't you love to have your CEO on the board of an organization that's been effective in business disruption? You would. But the responsibility is on the board to recognize and identify the limitations on that,” said Michael Peregrine, a partner at the law firm McDermott Will & Emery.

In Mayo's case, the relationship is mutually beneficial, Murphy said. CEO Noseworthy has brought back insight into how Merck approaches key topics like talent development, brand positioning and capital planning.

Noseworthy has also gotten an insider's view into how Merck approaches the challenge of applying scientific research to patient care, Murphy said.

In return, Noseworthy has shared with Merck what his physicians believe are their patients' greatest unmet needs.

“That's an important perspective that comes from our patients and physicians to this healthcare ecosystem,” said Murphy, who also noted that although Noseworthy keeps his compensation from Merck, Mayo adjusts his salary to subtract for that amount.

Knecht, of Accord Limited, said there are other ways for boards to get specific expertise without using people who have conflicts of interest. If they want a physician's perspective, perhaps they could look for a retired physician who lives in a different community.

“Think more creatively about this,” she said. “If what you're really trying to do is get the perspective and expertise, then try to do so without bringing onto your board someone who has potential conflicts of interest or even a real conflict of interest.”

Knecht also cautioned against companies building their boards based on the organizations they want to form relationships with. The primary concern should be adding people who have the right expertise and can abide by their fiduciary duties.

In some cases, health system CEOs serve on the boards of fast-food chains. Sharp HealthCare's Michael Murphy, for example, was compensated nearly $264,000 serving as a director for Jack In The Box. Sharp declined to comment for this article. Dignity Health's Lloyd Dean earned compensation of $280,800 serving on the board of McDonald's Corp. A Dignity spokeswoman referred Modern Healthcare to McDonald's for comment. McDonald's did not respond.

It might look bad if health system CEOs serve on the boards of companies generally deemed to contribute to poor health, McMillan said. On the other hand, health systems might argue their CEO is educating that company about healthier food options, he said. If they're going to do that, though, they'd better have evidence, such as if the fast-food company were to offer a smaller portion size as a direct result of evidence that director presented.

“Now you've created a positive comment to the market about your ability to reach across industries and affect healthcare," he said.

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