

## BOARD OVERSIGHT ROLE IN RISK MANAGEMENT

The rules recently adopted by the SEC require added disclosure in the 2010 proxy materials regarding the board's role in the oversight of risk management and the effect on the leadership structure of the company.

### **Risk Oversight**

The new requirement of added disclosure regarding board oversight of risk is intended to provide investors with a more complete understanding of how the board manages risk, whether by committee, the full board or both. The rules are designed to highlight how the company perceives the roles and relationship of management and the board in managing material risks. The SEC points out that risk oversight is considered a "key competence" of the board.

To be able to make the proper disclosures, the board will need to review and ensure its familiarity with the company's policies and processes relating to risk management. The board must understand the company's business strategy and the risks that may impact strategic decisions both in the short and long term such as credit risk, liquidity risk and operational risk, among others. If necessary, the board may determine that a committee devoted to the oversight of risk management should be established, or such duties should be assigned to an existing committee. Regardless of how the board determines to allocate the responsibility for risk oversight, the board must ensure that it is specific and appropriate to the needs of the company.

The board must be prepared to disclose the risk oversight process including such things as how risk reporting occurs. The SEC has indicated that, where appropriate, a company may want to disclose whether an individual responsible for daily risk management reports directly to the board or committee, or how the board or committee otherwise receives information from the company regarding risk.

The board should also be aware of the processes in place with respect to risks associated with board decision making, including compensation and governance decisions. Evaluating how matters are brought to the board, whether resources are available for decision making and ensuring that matters are treated objectively is a recommended part of this review.

The board needs to understand its role in the risk management process and the role of board committees. The board's actions will be judged under the business judgment rule, but with the benefit of hindsight. While the audit committee has generally thought to be principally responsible for risk oversight (a position reinforced by NYSE rules), the board must not depend entirely on this. It is the responsibility of the *full board* to oversee company risk and all members of the board should contribute their skills to this action.

#### *Recommended Actions:*

- *Continue to be educated with respect to the company's business and strategy*
- *Understand company risks as they relate to the company's business and strategy*

- *Identify vulnerabilities that may affect company performance and assess whether management has accounted for those risks as they affect company operations*
- *Review risk management policies specifically considering the company's appetite for risk*
- *Assess the current structures implemented to manage risks, including whether a risk committee is appropriate*

### **Board Leadership Structure**

As with the new rules regarding risk oversight, the added disclosure about the board's leadership structure and its appropriateness for the company is intended to provide investors with added transparency about the company's corporate governance. The company is required to disclose whether and why it has chosen to combine or separate the chairman and CEO positions and why this is appropriate for the company. In addition, companies that have a combined chairman/CEO position must also disclose whether and why it has a lead independent director and the specific role the lead independent director plays in the company's leadership.

#### *Recommended Action:*

- Be prepared to describe why the company has a separate chairman and CEO and why that is appropriate for the company

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