

## Insights

### Three Minute Update - Day in the Life of a Business: Who Gets Invited to Board of Directors' Meetings?

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Recent guidance indicates that some confusion may be running rampant in Board rooms about who gets invited to their meetings. This question surfaces when advising clients on governance issues associated with new entities, transforming entities, and merging entities, regardless of the form of organization and, more specifically, often in the urgency of a meeting with a surprise visitor knocking on the door.

Answers can be found to some degree in the statutory frameworks for the entities involved. Often, however, statutory frameworks will not address all scenarios or will defer to modifications to the norm that might be found in bylaws of a corporation or an operating agreement of an LLC.

If you are working with an existing entity, whether on a stand-alone basis or as part of some transformation or combination, the constituent documents for that entity should be reviewed. The answer about who gets invited may be resolved by the guidance or directives found there. However, even if guidance is included in the constituent documents, you will want to consider whether those provisions establish the desired framework or help in the situation at hand. If not, changes should be implemented. This will be particularly true when considering scenarios in which combining entities with their own histories, policies and philosophies will take different approaches that need to be reconciled.

We offer some "thinking points" to consider when laying out a best practices approach to this issue.

#### ***Why Be Concerned?***

With many current policies favoring transparency and collegiality, some may wonder why it is important to consider rights and limitations early in the structuring of an entity or in the process of combining entities. The umbrella rationale focuses on the mandate of the Board to act in the best interest of the entity.

Some may argue that full participation will enhance the decision-making process of the Board, resulting in better, more informed decisions with Boards having a higher level of certainty that their decisions will promote the best interest of the entity. However, the entity could be disadvantaged by careless sharing and dissemination of confidential and proprietary information that comes from over participation in a Board meeting.

Group dynamics could also play a role in inhibiting candid conversations among the decision makers. Many of us have a propensity to avoid confrontation and may temper comments in many circumstances in order to avoid creating disharmony. Consider the willingness of members of the Board to be fully candid about the performance of the management team if those members of management are participating in the meeting. Additionally, some participants invited to the meeting may have interests that are not fully aligned with those of the entity, such as an investor with multiple initiatives in the same industry in which the entity operates.

Another consideration ties to assuring the preservation of privileged communications, such as attorney-client privilege and community of interests or joint defense arrangements. If participants in the meeting include those who are outside of the privileged group, the discussions may not be protected. Over-participation increases the risk that the privileges will be lost.

Finally, Board members owe fiduciary duties to the entity and its shareholders, which include a duty of loyalty and a duty of care. Pursuant to Board members' duties of loyalty and care, members of the Board must protect confidential entity and Board information and those duties may restrict disclosure of certain information to non-Board members unless authorized to do so.

### ***Can Members of the Board Be Excluded?***

Recent guidance confirms that, in some circumstances, a person serving on the Board can be limited in the access that person has to the entity's information. For example, in conflict situations, the conflicted Board member should recuse himself or herself from participating in the discussions on that conflicted transaction. If the person does not do so, then the Board may want to utilize an executive session or establish a special independent committee for the issue that would not permit participation by the conflicted Board member.

Another scenario could arise where the relationship with the Board member has become adversarial and the Board needs to discuss and perhaps receive legal advice about the issues of concern related to that adverse Board member. The Board should be able to make clear that the Board's counsel does not represent the adverse Board member and to limit such Board member's participation in the group's discussions and the receipt of advice provided to the Board generally.

### ***What About Management?***

Certainly, for the Board to do its job and fulfill its responsibilities to be informed about the decisions it is making, input from management will be essential. In fact, many statutory schemes inherently assume that management will participate in Board meetings because Board members are expected to receive and are entitled to rely upon information and advice received from appropriate management personnel.

Different positions about management participation can be taken depending upon the strata of management that an invitee serves in that entity. The senior executive officer, if not already a member of the Board, may better serve the other Board members by full participation in a meeting, while a subject matter specialist will not have the same need or value to the Board to support full participation.

While management participation in Board meetings usually brings value to the process, many best practice advisors indicate that including an executive session (in which only the members of the Board are present) as a standard agenda item for Board meetings is appropriate and encouraged. Including executive sessions as a standard serves multiple positive purposes, including ensuring confidentiality and minimizing management anxieties if an executive session is suddenly scheduled when it has not historically occurred.

### ***Can Shareholders Be Excluded?***

Statutory schemes applicable to non-public companies generally provide very limited informational rights to shareholders, such as limiting them to receipt of annual financial statements and providing for exclusion of certain financial information and other classes of identified documents. (We note that the regimen applicable to public companies addresses disclosure obligations, but these are not part of this alert.) Accordingly, shareholders should not be considered to have an inherent right to attend Board meetings. In fact, full participation by all shareholders could be used in a “piercing the veil” action as an indicator that the entity and its shareholders did not honor the corporate formalities.

However, in some circumstances, investors will have negotiated rights to participate in Board meetings either as an observer or as an elected member of the Board. The variables to consider for these scenarios present too many complexities for this alert, but these positions are negotiated by the parties and will reflect the respective negotiating positions and the mutual and separate interests being served. Some investors may require that their representatives hold a majority of the Board positions, while others prefer to avoid having any voting authority for their own risk management considerations.

### ***Other Considerations***

Even if the decision to open the door to a Board meeting is made, whether broadly or to a specifically limited group of management, shareholders, or other advisors, certain limitations on such attendees may be imposed. To maintain order and expectations during the meeting, the agenda distributed in connection with any notice of the Board meeting should be followed, and the chair or other person leading the Board meeting may consider limiting discussions during any particular portion of the Board meeting to the current agenda item. Time limitations on any individual speaker may also be imposed if necessary, and the Board may determine whether it will respond to any such comments during the meeting or take them under advisement. The Board can also establish the rules of the meeting that limit or ban the right of those with only observer status to also participate in the meeting unless called on.

### ***Takeaways***

- Be aware of the requirements found in the applicable statutory scheme and governance documents.
- Act proactively to include provisions in the governance documents that clearly establish attendance rights and limitations.

- Maintain awareness and sensitivity to circumstances where participation by others could risk privileged communications or dissemination of confidential information.
- Build in structures that allow attendance and participation to be controlled during the course of a meeting, such as executive sessions that exclude management, investors who have only observer rights, limitations on attendance for Board members with conflicted positions or adversarial claims against the entity and controls on participation by those who are not Board members.
- Establish special committees to better support segmentation of information rights among Board members who are on or off such committees.

Readers are advised to contact legal counsel to determine how these concepts may apply to their specific situations. If you have any further questions, comments or concerns, please feel free to contact **Robert A. Greising**, **Sarah E. Jones**, or a member of our **Business, Acquisitions & Securities** team.

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