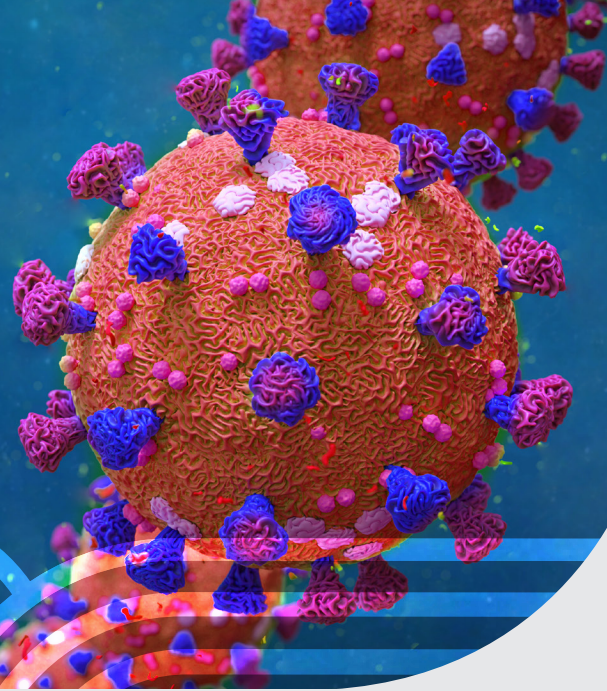


Corporate Governance: COVID-19 and the Board of Directors



COVID-19 and Crisis Management

The outbreak of the Coronavirus Disease 2019 (COVID-19) has evolved into a pandemic, with major implications for the world population's health and the economic order. Governments, the private sector and citizens are responding to this unprecedented scenario by taking measures to prevent the spread of COVID-19 while maintaining vital sectors of the economy active.

In these challenging times, private companies need capable leadership to navigate uncertain waters and take urgent action while con-

sidering multiple factors. Good governance in this scenario is key, as it translates into superior leadership and decision-making processes. The objective of this paper is to provide indicative guidance to Boards of Directors in identifying, prioritizing and implementing a governance framework to deal with the strategy and oversight challenges that COVID-19 may present, and to provide a list of questions that can be asked by investors and that the Boards of Directors should consider for building an effective response to the COVID-19 crisis.

Important Considerations

- This guidance is not a replacement for following national, regional or local mandates on COVID-19. All companies must keep abreast of, and follow any national, regional, and local mandates on COVID-19 in the jurisdiction where they operate.
- This document is intended to reflect non-binding, indicative guidance and recommendations. Each recipient should develop its response to the impact of COVID-19 on its business considering the particular circumstances of its business and all applicable laws and regulations, using its own independent judgment. IDB Invest makes this Guidance available to each recipient on a non-reliance basis and shall not be responsible in any manner for any use made of this Guidance by any person.
- This Guidance aligns with IDB Invest Corporate Governance Guidelines and the Corporate Governance Development Framework (CGDF) at www.cgdevelopmentframework.com
- The dynamic nature of the current COVID-19 pandemic requires that companies stay abreast of, and incorporate, new guidance on COVID-19 as it becomes available.

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Board's Role in the Crisis

Boards need to ensure that management has the ability to act quickly in a constantly evolving landscape and prioritize the safety and well-being of the company's employees, as well as of those who depend on the company for essential services.

The Board's role is one of strategy and oversight, as well as ensuring ensuring an adequate communication with shareholders and stakeholders, which is particularly important during a crisis. The Board, under the guidance and leadership of the chair, should set the tone in relation to the company's response to a crisis and act to protect the company's financial structure as well as its reputation.

COVID-19 impacts the business in different manners and on different levels. In order to create an environment for the company to be agile, the Board should assess if revisions to the governance structures are necessary (and appropriate within each relevant jurisdiction)

to ensure adequate performance for the current pandemic, as well as to fully understand the risks to the company and to its various stakeholders arising from the pandemic and from the consequent economic downturn, which may be of uncertain duration.

In addition to the impact on workforce health, remote work challenges, demand patterns and supply chain disruptions, the Board should carefully consider the balance between indebtedness and the need for immediate liquidity. This exercise will guide the Board in assessing its existing strategy and determining actions needed from a short and long-term perspective.

The Board of Directors can be a powerful liaison with shareholders and stakeholders, including government authorities, as such, conducting appropriate communication is particularly important in times of crisis.

Culture Matters

In the response strategy, it is important to emphasize that culture matters: having a people-first mindset, taking care of the workforce and stakeholders, communicating properly and building trust, is crucial to developing confidence and maintaining reputation.

To promote effective decision making during the COVID-19 pandemic and its aftermath, an environment of trust, respect and shared concern should prevail. The Board should send the message and adopt a "nose-in, fingers-out" approach, delegating authority and empowering teams to take decisions quickly especially in areas or sectors that are more affected, while increasing transparency for communication to flow seamlessly across the organization. For this, a crisis committee and a response plan can be very useful governance tools.

The current crisis presents directors and executives with the unique opportunity to test their business shrewdness, flex their innovation muscles, and demonstrate their commitment to the creation of value, both for the company and all its stakeholders. Lessons learned from this crisis can be used to build systems that are even more resilient to deal with future challenges.

It is always important to remember that the "business judgment rule" is an important standard by which directors are judged on their compliance with their fiduciary duties. This means that directors should act on an informed basis, in good faith, and in the honest belief that their decisions are in the company's best interests.

Immediate (non-exhaustive) Corporate Governance Actions

- 1** Set the “tone from the top” to demonstrate leadership and commitment to crisis management.
- 2** Establish frequent communication with the CEO, emergency Board meetings and communication processes between key management personnel and the Board for effective and ongoing information flow and reporting.
- 3** Consider creating a specific COVID-19 cross-functional crisis committee (members can include a Board member, senior management, finance, HR, IT, legal and compliance).
- 4** Revise and adapt delegation processes and reporting lines for expedited communication and decision-making processes.
- 5** Revise and/or adopt succession plans and emergency contingency plans for key personnel.
- 6** Consider revising the roles of audit committee, risk committee and other Board and management committees to include communication and oversight of the crisis.
- 7** Adopt virtual Board and committee meetings, increase interactions and exchange of documentation via virtual means; review meeting requirements (quorum, advance notice) to adapt to virtual reality.
- 8** Consider establishing a COVID-19 response plan (or activate a crisis management plan if already existing).
 - Establish a dedicated point person for the COVID-19 response plan: this person would communicate with the crisis committee and be responsible of managing the response and the need of corporate capacity to implement the strategy.
 - Develop crisis response playbook, with decision process flows and escalation protocols. Communicate clearly, so all participants know their roles and the critical approval processes that are in place.

Oversight and Strategy: Financial and Business Impact

- 1 Assess the risks, revise and adequate the corporate strategy and work with management on the design of a business continuity plan:
Workforce: key person succession planning, contingency planning, health and safety concerns, viability of work-from-home, impact on compensation, mission-critical personnel, unforeseen employee cash needs, potential of productivity reduction.
Customers: abnormal demand patterns for products and services, possible increase in customer complaints.
Supply chain: slowdown of the supply-chain; logistics challenges with several countries, macro-economic impact; difficulties in planning.
Financial liquidity: decline in revenue; reduction in working capital; need for financing, associated with rising risk profile and cost of capital.
Legal/Regulatory/Contractual: new laws and regulations imposed by local and foreign authorities; contractual obligations or regulatory requirements triggered by changes in business or financial position throughout the crisis.
IT Related Issues: ensuring connectivity, productivity, data privacy and confidentiality issues, cybersecurity breaches.

- 2 Assist management in designing a new organizational structure, creating *ad hoc* response teams as adequate.

- 3 Analyze the key control functions of the business: adequacy of internal controls policies and procedures, increase in immediate business risk taking and its long-term implications, increase in compliance requirements, the capacity of internal auditing system for continuing the work plan.

- 4 Consider the potential for corporate transactions which can be beneficial to create value or expand or consolidate a business.

Shareholder and Stakeholder Engagement

- 1 Assist management in communicating with shareholders/investors, holding virtual shareholders meetings to the extent permitted by law, and disclosing material information that may have a financial impact on the business or the decision to hold, purchase or sell securities.

- 2 Assist management in stakeholder engagement, mapping relevant stakeholders (which include customers, suppliers, employees, local communities, government authorities and regulators) and appropriately implementing communication and transparency measures. Appropriate messaging of the company's actions with respect of the crisis will help avoid confusion and thwart the speculation that can generate distrust among investors and the public. This will also allow the company to be better informed about the external perception of its response to the pandemic.

Questions to consider during COVID-19 crisis:

For investors¹

- 1** Does the Board recognise its role and accountability to provide oversight to the company's management of the COVID-19 crisis?
- 2** How is the Board structured to address the crisis? Is there a clarity of roles and responsibilities?
- 3** How does the Board get information about the crisis and demonstrate that it has an adequate and up-to-date understanding of the risk faced by the organisation?
- 4** Does the Board have access to internal or external subject matter experts on COVID-19 to support decision making?
- 5** If a crisis management committee exists, how does the Board allocate responsibilities to it and how does this committee interact with management and the Board as a whole?
- 6** Scoping the problem: what are the key financial risks and pressures and how resilient is the company to confront negative economic outcomes?
- 7** How is the Board addressing the crisis and its impact on employees, customers, supply chains and local communities?
- 8** What key financial and strategic decisions have to be made and in what timeframe?
- 9** How will the company balance the interests of shareholders, stakeholders and the overall sustainability of the company itself?
- 10** What are the plans for business continuity?
- 11** How are communications managed internally and externally?
- 12** How will the company communicate the economic impacts and threats to the company's financial sustainability and business model?

¹International Corporate Governance Network. (2020, March). Coronavirus as a new systemic risk: Implications for corporate governance and investor stewardship. Retrieved from icgn.org: <https://www.icgn.org/coronavirus-new-systemic-risk-implications-corporate-governance-and-investor-stewardship>

For Board of Directors^{2 3}

- 1 How prepared is the company to react with precision, speed and confidence?
- 2 What ongoing information does the Board need to have about the crisis?
- 3 What can we do to ensure the health and safety of our workforce?
- 4 What should the organization communicate to its stakeholders and the public about the crisis?
- 5 What are our customers telling us? What are our employees telling us? What are our investors and lenders telling us? What are our regulators telling us? What is our financial reporting telling us?
- 6 What is going on in the world that could affect us?
- 7 What is our CEO and/or key management succession plan?
- 8 What is the company's ability to cover near-term expenses?
- 9 How are we managing credit and liquidity risk, loan defaults and covenant breaches?
- 10 What tradeoffs do we have to make around payroll expenses?
- 11 Do we need to adjust our supply chains?
- 12 Are we prepared to work remotely for an extended period of time?
- 13 How do we keep our company culture alive?
- 14 How are we interacting with the financial markets?
- 15 How strong is our underlying business model?
- 16 Are we behaving as a socially responsible organization?
- 17 How effective is the Board being in this sudden crisis? How well is the CEO and management team responding?
- 18 How does the Board learn from this experience?



Illustration 1.
Aspects of Corporate
Governance

² Adapted from Enns, D., & Lindsay, H. (2020, March 18). 20 Questions Directors Should Ask About Crisis Management. Retrieved from <https://www.cpa.canada.ca>: <https://www.cpacanada.ca/en/business-and-accounting-resourcestrategy-risk-and-governance/strategy-development-and-implementation/publications/questions-for-directors-about-crisis-management>.

³ Adapted from Moyo, D. (2020, April 13). 10 Questions to Guide Boards Through the Pandemic. Retrieved from Harvard Business Review: <https://hbr.org/2020/04/10-questions-to-guide-boards-through-the-pandemic>

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